



**2016 – 2017
Pennsylvania General Assembly
Appropriations Hearing Materials**

Table of Contents

Mission Statement	2
Department Statement	2
Program Narrative	3
Program Performance and Goals	4
Program Challenges	6
Summary Financial Data	9
Complement Information	9
Detail by Major Object	10
Explanation of Changes	11
Cost Assumptions	12
Cash Receipts and Disbursements	13

Appropriation

General Government

Page Numbers of Governor's Executive Budget

E9-1, E9-2, E9-3, E9-4, E9-5, E9-6, H9, I3

Mission Statement

The Pennsylvania Department of Banking and Securities regulates financial services and works to ensure consumers and businesses are well-informed about the marketplace.

Department Statement

The Pennsylvania Department of Banking and Securities charters, licenses, registers, regulates, supervises, and/or examines state-chartered banks, bank and trust companies, trust companies, bank holding companies, savings banks, credit unions, consumer discount companies, sales finance companies, installment sellers, money transmitters, collector-repossessors, pawnbrokers, check cashers, debt management companies, debt settlement companies, mortgage bankers, mortgage brokers, loan originators, loan correspondents, securities agents, broker-dealers, investment advisers and notice filers, and investment adviser representatives.

The Department of Banking and Securities derives its authority from the:

- Banking Code of 1965
- Check Cashers Licensing Act
- Consumer Credit Code - Motor Vehicle Sales Finance (Chapter 63)
- Consumer Discount Company Act
- Credit Services Act
- Credit Union Code
- Debt Management Services Act
- Debt Settlement Services Act
- Department of Banking and Securities Code
- Licensing Business of Transmitting Money or Credit Act
- Loan Interest and Protection Law
- Chapter 5 of the Mortgage Bankers and Brokers and Consumer Equity Protection Act
- Mortgage Licensing Act
- Pawnbrokers License Act
- Investment Company Act
- Pennsylvania Securities Act of 1972
- Takeover Disclosure Law

Aside from the work and personnel engaged in enforcing the Pennsylvania Securities Act of 1972; Takeover Disclosure Law; and Investment Company Act, which are funded via industry assessment fees approximately three-quarters of which are paid into the General Fund, the work and personnel engaged in enforcing the authority outlined above are funded through the Banking Fund. All monies of the Banking Fund are derived from licensing fees and assessments on regulated entities.

Program Narrative

The Pennsylvania Department of Banking and Securities preserves and protects the integrity of the financial services marketplace and promotes public confidence in the commonwealth's financial services through:

- Conducting examinations to ensure the safety and soundness of Pennsylvania's state-chartered depository institutions;
- Conducting examinations to ensure that non-depository financial service providers are operating in accordance with applicable state and federal laws and regulations;
- Conducting examinations to ensure that securities registrants and firms are operating in accordance with applicable securities laws;
- Reviewing proposed securities offerings to ensure that such offerings made to Pennsylvania investors comply with all applicable securities laws;
- Working to protect Pennsylvania consumers and investors from unlawful and usurious financial products and offerings; and
- Assisting consumers and investors with financial matters that fall under the purview of the Department.

As of June 30, 2015, the Department supervised 212 financial institutions including 55 credit unions, 51 commercial banks, 48 savings banks, 41 bank and trust companies, 16 non-depository trust companies, and 1 private bank.

As of June 30, 2015, the Department licensed and regulated 20,375 non-depository financial service providers including 12,330 mortgage loan originators; 2,941 installment sellers; 1,751 mortgage lenders; 831 check cashers; 984 sales finance companies; 443 mortgage brokers; 213 debt management services; and 163 mortgage discount companies. The remaining 719 license categories include money transmitters, loan correspondents, collector-repossessors, pawnbrokers, debt settlement services and consumer discount companies.

As of June 30, 2015, the Department registered 192,162 securities agents; 19,244 investment adviser representatives; 3,121 investment advisers and notice filers; and 2,116 broker-dealers.

Consumers and investors can contact the Department to ask questions about financial transactions or to file complaints using a toll-free telephone number (1-800-PA-BANKS) or by submitting a form via the Department's website (www.dobs.pa.gov).

Consumers and investors can learn more about investing through PA Investor Education on Facebook: www.facebook.com/PAInvestorEducation.

Businesses and consumers can learn about the work of the Department and its initiatives through social media, including Facebook and Twitter.

Program Performance and Goals

Pennsylvania regulators understand local markets and the uniqueness of Pennsylvania business models. In comparison to federal regulatory entities, the Department of Banking and Securities provides: quicker examination turnaround; enhanced customer service on a more personal level; quicker transaction response times; greater accessibility to agency senior management; and a more cost effective regulatory option. Currently, approximately 77% of banks, banks and trusts, and savings banks headquartered in Pennsylvania are state-chartered.

In FY2014-15, the Department of Banking and Securities converted one federally chartered depository institution to the Pennsylvania state charter:

- First Community Bank of Mercersburg, Franklin County, converted from a national bank to a state-chartered bank

In FY2014-15, the Non-Depository Compliance Office and Bureau of Non-Depository Examination:

- Completed 1,274 examinations of licensed and unlicensed entities, which identified 1,839 compliance violations;
- Issued 139 enforcement actions, which included 35 public enforcement actions; and
- Levied total fines in the amount of \$2,080,425.

In FY2014-15, the Corporation Finance Office:

- Cleared for sale in Pennsylvania 71 registrations and 16 offerings that qualified as exempt from Pennsylvania's registration requirements;
- Received and docketed 4,072 mutual fund filings; and
- Received and docketed 2,686 Form D (non-public offerings pursuant to Federal Rule 506) filings.

In FY2014-15, the Bureau of Securities Licensing, Compliance, and Examinations:

- Conducted 35 examinations;
- Reached 17 settlements totaling \$242,220 ordered in administrative assessments and legal costs;
- Issued four orders to show cause resulting from complaints against registrants and non-registrants; and
- Issued two final orders totaling \$52,215 in administrative assessments and legal costs.

In FY2014-15, the Consumer Services Office fielded and resolved 5,875 inquiries and complaints from consumers and investors.

In FY2014-15, \$22,462,847 was deposited into the Banking Fund.

In FY2014-15, \$26,728,436 of Securities Operations revenue was deposited into the General Fund and \$9,432,687 was deposited into the Securities Operations fund.

In addition, a restricted account, the Securities Regulation Account, was created in FY2014-15 within the General Fund in accordance with Section 703.1 of Act 52 of 2014. An initial amount of \$8.66 million was deposited into the account in August 2014; these funds were received as part of a multi-state securities settlement. In order to bring the fund to its cap of \$12.5 million, an additional \$3.84 million was requested in FY2015-16 and is being requested in FY2016-17 to be transferred into this account. In accordance with Section 703.1, these funds will be used for administrative and operating costs associated with special initiatives or strategic regulatory needs, investor and entrepreneurial education and outreach programs, and unanticipated or adverse industry circumstances that require enhanced investor protection activities.

Legislative Initiatives:

Update and Modernization of the Money Transmitters Act

Representative Ryan Mackenzie has introduced HB-850, P.N. 1029, which would update and modernize the Money Transmitters Act (the Act). This Act has not seen significant amendment since 1977 when the business of money transmission involved simply sending money through a money order. Because of the phrase "or method for payment of money or transmittal of credit" in the Act and technological advances, the scope of the Act has grown over the years to encompass electronic payments and stored value cards. The proposed amendments in HB-850 will modernize the licensing and regulatory language in the Act to make it consistent with the Department's other non-depository licensing statutes, provide enhanced consumer protections including increasing the required bond amount which protects damaged consumers, require the companies to operate in a safe and sound manner and require agent registration. The amendments also narrow the scope of the Act by appropriately exempting business-to-business transactions. Additionally, Representative Mackenzie is considering amendments to the legislation that would include virtual currency (e.g., Bitcoin) under the provisions of the Act, requiring licensure and regulation of the relatively new digital based activity.

Licensing and Regulation of Non-Bank Mortgage Servicers

The Department will be requesting introduction and seeking enactment of amendments to the Mortgage Licensing Act that would require licensure and regulation of the non-bank mortgage servicing industry with the intent of providing better protection for borrowers, investors and other stakeholders. The enactment of state and federal statutes and regulations in 2008 - 2009 significantly strengthened oversight of the mortgage industry and ended lending practices that left homeowners vulnerable to foreclosure. However, the licensing and regulation of the non-bank

mortgage servicing industry was not addressed in these enactments and regulations. Since the mortgage servicing business is shifting from the large national bank servicers to non-bank servicers and the industry is growing in size and complexity, the Department believes that licensing and regulatory standards for non-bank mortgage servicers will protect consumers, provide a well-defined regulatory structure for the industry and a safe and sound mortgage servicing industry.

Program Challenges

The Department continues to face significant challenges in critical program operations resulting from both internal and external pressure. The financial services marketplace is an ever-evolving landscape, but the pace and nature of change has been so rapid within the past few years that financial services may be radically different in several years. The Department has been actively planning for this changing landscape and faces the following challenges in both the short and long-term:

Department Staffing

Recruiting staff with the skill set needed to fulfill the Department's program is a focus of the Department's strategic plan. The Department has experienced a loss in examination and management staff to industry and federal regulators over the past several years due to large pay differentials. Furthermore, recruiting staff with advanced industry skills in areas such as cybersecurity, IT examinations, and securities has been difficult given the limitations and inflexibility associated with state civil service requirements and process. Accelerating staff retirements have also posed a challenge to our program.

The Department continues to recruit additional examiner personnel and support the highest level of certification. For FY2015-16, the Secretary has implemented the 'RRRev UP' initiative to focus on recruitment, retention and recognition of employees to maintain a high level of qualified and certified staff for the programs and meet industry and regulatory needs. As an outgrowth of RRRev UP and our new strategic plan, a Recruitment Task Force has been established and is exploring new initiatives such as electronic postings, and intern and alumni employment involvement, among others, in attracting new talent to the department. It is the Department's goal to minimize the regulatory risks associated with losing experienced and talented staff through these programs.

Mortgage Servicing

The regulation and oversight of the mortgage industry has become significantly more effective at the federal and state level since the 2008 housing crisis. Pennsylvania is currently in the minority of states with regard to regulating non-bank mortgage servicing. The state banking departments in 35 states currently have regulatory authority over mortgage servings; Pennsylvania is one of only 15 states without this authority. The Department oversees that mortgage brokering and lending conducted in the commonwealth is done in accordance with all applicable federal and state laws; however, the state's Mortgage Licensing Act does not grant authority to the Department to regulate the non-bank mortgage servicing industry. This means that

the Department oversees the brokering and closing of the loan on the front-end of the process and ensures that the loans are properly closed out upon payoff of the loan at the tail-end of the process. Mortgage servicing is among the top issues for which Pennsylvania consumers contact the Department for assistance, but the Department is limited in how it can assist consumers with these issues given its lack of regulatory authority. Regulating mortgage servicing is a "best practice" promulgated by the Conference of State Bank Supervisors (CSBS) as part of its mortgage accreditation program for state banking departments. The Department is one of only 14 states in the nation to have its mortgage licensing and examination program accredited by CSBS.

Investment Adviser Oversight

The regulatory transfer of more than 2100 investment advisers (IAs) from federal to state oversight, commonly known as the "IA Switch," stemmed from Section 410 of the Dodd-Frank Act which raised the assets-under-management ceiling for state regulation of investment advisers from \$25 million to \$100 million. Prior to this change, regulation of investment advisers overseeing assets in excess of \$25 million was a responsibility of the Securities and Exchange Commission (SEC). Advisers now register with the Department and are subject to a robust review of their employment background, nature of their business, and regulatory record. Thereafter, the Department monitors on-going compliance with securities laws and regulations and conducts examinations of the firms. The Department assumed 138 IAs during the time of the transfer (March 2011 to December 2012), 92 of which were physically located in Pennsylvania. There are now in excess of 860 IA firms registered in PA. These firms are often more likely to utilize alternative investment strategies and products, and examiners are continuing to undertake desk audits and examination visits, necessitating the need for additional training of current examiners and the recruitment and hiring of new examiners.

Cybersecurity

As threats continuously evolve, cybersecurity is of paramount importance to the Department on two fronts: protection of financial data at financial institutions and licensees, and protection of the Department's systems. As part of any state-chartered financial institution's safety and soundness examination, the Department conducts an Information Technology (IT) examination. The Department examines for cybersecurity preparedness to assess the policies, procedures, and controls in place to ensure financial institution compliance with the Gramm-Leach-Bliley Act. In FY15-16, the Secretary launched an internal cybersecurity task force that provided informational resources on best practices to all Department financial institutions and licensees. The goals and objectives of the task force are twofold: to educate and inform our regulated entities and individuals about information security with a focus on cybersecurity issues and challenges; and to develop, coordinate and share information and resources concerning cybersecurity and information security practices and issues Department-wide.

Non-Traditional Financial Instruments

Emerging financial products and entities providing such products are posing operational challenges. An increasing number of non-bank entities are offering products that do not strictly adhere to definitions and activities outlined in the Department's authority. Often traditional financial products are offered by non-traditionally structured entities, or vice-versa. The Department is routinely required to review new financial offerings and industries to ensure that they are operating in compliance with all applicable laws and regulations if operating in Pennsylvania. Often, this category of financial products and entities is referred to as 'FinTech' (Financial Technology). Examples include peer-to-peer lending, virtual currency, and crowdfunding. The proliferation of non-traditional financial products and entities has required that the Department be increasingly vigilant to protect consumers from unlicensed, illegal, and usurious activities and entities. In FY15-16, the Department has placed an increased emphasis on evaluating FinTech by bolstering its research activities and educating Department management on the nature of financial products and entities. The research has also aided the Department's consumer education and outreach efforts.

Summary Financial Data

	2014-15 Actual	2015-16 Available	2016-17 Budget
BANKING FUND:			
General Government:			
General Government Operations	21,330	23,178	23,235
Transfer to Restricted Inst. Resolution Account	<u>3,000</u>	<u>2,000</u>	<u>2,000</u>
Total - General Government	<u>24,330</u>	<u>25,178</u>	<u>25,235</u>
BANKING FUND TOTAL	<u>24,330</u>	<u>25,178</u>	<u>25,235</u>
GENERAL FUND:			
General Government:			
Securities Operations (Restricted)	<u>7,916</u>	<u>8,005</u>	<u>8,500</u>
DEPARTMENT TOTAL - ALL FUNDS			
Special Funds	24,330	25,178	25,235
Restricted	<u>7,916</u>	<u>8,005</u>	<u>8,500</u>
TOTAL ALL FUNDS	<u>32,246</u>	<u>33,183</u>	<u>33,735</u>

Complement Information

	2014-15 12/26/2014 Actual	2015-16 12/25/2015 Available	2016-17 7/1/2016 Budget
State Funds			
Authorized	181	180	180
Filled	160	159	N/A
Other Funds			
Authorized	53	53	53
Filled	<u>44</u>	<u>46</u>	<u>N/A</u>
Totals			
Authorized	234	233	233
Filled	<u>204</u>	<u>205</u>	<u>N/A</u>

Detail by Major Object

	2014-15 Actual	2015-16 Available	2016-17 Budget	Change Budgeted vs. Available	Percentage Change
Personnel					
Banking Fund-GGO	16,843	17,738	18,644	906	5.11%
Securities Operations	<u>6,322</u>	<u>6,505</u>	<u>6,760</u>	<u>255</u>	3.92%
Total Personnel	23,165	24,243	25,404	1,161	4.79%
Operating					
Banking Fund	4,487	4,940	4,591	(349)	-7.06%
Securities Operations	<u>1,594</u>	<u>1,500</u>	<u>1,740</u>	<u>240</u>	16.00%
Total Operating	6,081	6,440	6,331	(109)	-1.69%
Restricted Institution Resolution Account					
Banking Fund	3,000	2,000	2,000	-	0.00%
Securities Operations	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	0.00%
Total Rest. Inst. Res. Acct.	3,000	2,000	2,000	-	
Budgetary Reserve					
Banking Fund	-	500	-	(500)	
Securities Operations	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	
Total Budgetary Reserve	-	500	-	(500)	
Total Funds	<u>32,246</u>	<u>33,183</u>	<u>33,735</u>	<u>552</u>	1.66%

Explanation of Changes

	2015-16	2016-17	Increase (Decrease)	% Change
Personnel				
Banking Fund	17,738	18,644	906	5.11%
Securities Operations	6,505	6,760	255	3.92%

FY2016-17 budget request contains funding for salaries and benefits for a complement of 233 positions.

Operating

Banking Fund	4,940	4,591	(349)	-7.06%
Securities Operations	1,500	1,740	240	16.00%

FY2016-17 budget request contains funding to continue cost-to-carry operations. The related agency operating expenses have been properly split between the funds. In addition, the decrease in the Banking Fund is consistent with our downward trend in operational spending over the past several years and achieved through numerous cost-savings initiatives that are being identified and implemented on an ongoing basis. The increase in the Securities Operations fund are expenses related to travel in order to support the increase in number of exams being conducted and as required upon the assumption of investment advisor oversight of jurisdiction from the Securities and Exchange Commission.

Restricted Institution Resolution Account

Banking Fund	2,000	2,000	-	0.00%
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This account is funded through transfers from the Banking Fund. The act authorizes the Secretary of the Department of Banking and Securities to determine the amount to be transferred from the Banking Fund each fiscal year based upon economic and regulatory conditions.

Budgetary Reserve

Banking Fund	500	-	(500)	
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FY2015-16 reflects the savings from the elimination of one position due to consolidations of administrative functions with other agencies and changes that are being implemented in order to better align the agency's resources with its strategic plan.

Cost Assumptions

Personnel

The Department's budget request includes total personnel funding (salaries and benefits) of \$25,404,000.

Operating

The Department's budget request consists of total operational funding of \$6,331,000.

Non-Recurring

There are no program revision requests or new initiatives considered in this year's budget request.

Lapsed Funds

The Department does not anticipate a lapse in the current fiscal year.

Litigation

The Department is not engaged in any litigation that meets materiality thresholds.

Total

For FY2016-17, the Department's overall budget request is \$31,735,000.

Banking Fund

The Banking Fund is a special revenue fund composed of monies received from fees, assessments, charges and penalties collected or recovered from persons, firms, corporations or associations under the supervision of the Department of Banking and Securities. It provides for the administration of the Department of Banking and Securities and regulation of the financial services industry. Per Act 86 of 2012, the Institution Resolution Account was established within the Banking Fund to be used at the discretion of the Secretary of Banking and Securities in the event of a seizure or liquidation of a financial institution.

Statement of Cash Receipts and Disbursements

(Dollar Amounts in Thousands)

	2014-15 Actual	2015-16 Available	2016-17 Estimated
Cash Balance, Beginning	\$ 17,435	\$ 20,823	\$ 18,774
Receipts:			
Licenses and Fees	\$ 21,687	\$ 21,700	\$ 24,317
Fines and Penalties	487	400	400
Interest	288	236	236
Other	^d 600	400	0
Total Receipts	<u>23,062</u>	<u>22,736</u>	<u>24,953</u>
Total Funds Available	\$ 40,497	\$ 43,559	\$ 43,727
Disbursements:			
Banking and Securities	\$ 19,674	\$ 24,785	\$ 23,235
Total Disbursements	<u>-19,674</u>	<u>--24,785</u>	<u>-23,235</u>
Cash Balance, Ending.....	\$ 20,823 ^a	\$ 18,774 ^b	\$ 20,492 ^c

^a 2014-15 Actual includes a balance of \$5,500,000 in the Institution Resolution Restricted Account.

^b 2015-16 Available includes a balance of \$7,500,000 in the Institution Resolution Restricted Account.

^c 2016-17 Estimated includes a balance of \$9,500,000 in the Institution Resolution Restricted Account.

^d Monies received for Consumer refunds