

The Arkansas Securities Department

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(DRAFT)

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Mission Statement

Promote an environment in which the securities and financial markets within the department's jurisdiction function efficiently and without unnecessary regulatory impediments and in which the Department protects the financial well-being of Arkansas citizens through effective consumer protection and education.

Jurisdiction

Arkansas Securities Act

- Ark. Code Ann. §§ 23-42-201 through 23-42-509

Fair Mortgage Lending Act

- Ark. Code Ann. §§ 23-39-501 through 23-39-518

Uniform Money Services Act

- Ark. Code Ann. §§ 23-55-101 through 23-55-1005

*Each Act accompanied by a separate set of administrative rules

Jurisdiction

Savings and Loan Institutions

- Ark. Code Ann. §§ 23-37-101 through 23-37-812

Credit Unions

- Ark. Code Ann. §§ 23-35-101 through 23-35-805

*There are no state-chartered savings and loan institutions or state-chartered credit unions in Arkansas at this time.

Background – Executive and Legal Staff

Arkansas Securities Commissioner

- Ark. Code Ann. § 23-42-201 – executive office appointed by the Governor

Deputy Securities Commissioner

General Counsel

Legal Staff - 7 Attorneys

- General Counsel
- Associate General Counsel

*Legal Staff is responsible for rendering policy and compliance advice to the various sections within the Department, as well as for enforcement of any violations of the Acts that the Department administers. Staff attorneys are also responsible for heading the Department's legislative and rule-making efforts.

Background – Registrants

Arkansas Securities Act

- Investment Adviser Firms
- Investment Adviser Representatives
- Broker-Dealer Firms
- Broker-Dealer Agents

- Securities

Background – Number of Registrants

Fair Mortgage Lending Act

- Mortgage Bankers
- Mortgage Servicers
- Mortgage Brokers
- Mortgage Loan Officers

Uniform Money Services Act

- Money Transmitters
- Currency Exchangers
- Money Services Delegates – 7,484 (current)

Background - Synopsis

Total Number of Registrants (Entities and Individuals) – 2019 Renewals

- 126,470

Total Number of Securities Filings – 2018

- 2,013

Total Number of Employees - Current

- 35

Fiscal Year 2019 Revenues

- \$19,033,264.23 (increase of 17.95% from Fiscal Year 2014)

Fiscal Year 2019 Budget Appropriation

- \$3,309,737.50

Arkansas Securities Act

*Name of Presenter

Jurisdiction – Key Areas

Offers and Sales of Securities

- Ark. Code Ann. § 23-42-501

Investment Advisers and Investment Adviser Representatives

- Ark. Code Ann. § 23-42-301(c)

Broker-Dealers and Broker-Dealer Agents

- Ark. Code Ann. § 23-42-301(a)

Non-Registrants

Jurisdiction – Potential “Overlaps”

United States Securities and Exchange Commission (SEC)

Financial Industry Regulatory Authority (FINRA)

Stock Exchanges

Arkansas Insurance Department

Arkansas Attorney General

Arkansas Department of Human Services

Jurisdiction – Important Federal Law

- Securities Act of 1933
- Securities Exchange Act of 1934
- Investment Company Act of 1940
- Investment Advisers Act of 1940
- National Securities Markets Improvement Act of 1996
- Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010
- Jumpstart Our Business Startups Act (2012)
- SEC and FINRA Rules and Regulations

Jurisdiction - NASAA

- The North American Securities Administrators Association (NASAA), founded in Kansas in 1919, is the world's oldest international investor protection organization.
- NASAA is an association of state securities administrators who are charged with the responsibility to protect consumers who purchase securities or investment advice
- NASAA's membership consists of 67 administrators from the territories, districts, and states of the United States, from Mexico, and from the provinces of Canada

Securities Registration

Securities Registration Section

- Examiner Supervisor, 2 Examiners

Ark. Code Ann. § 23-42-501 – it is unlawful for any “person” to offer or sell any security unless it is registered, exempt, or a covered security.

Securities Registration

Registration Methods

Registration by Notification – Ark. Code Ann. § 23-42-401

Registration by Coordination – Ark. Code Ann. § 23-42-402

Registration by Qualification – Ark. Code Ann. § 23-42-403

*Stop Orders – Ark. Code Ann. § 23-42-405 – deny, revoke, or suspend registration statement

No-Action/Interpretive Opinion Requests

Securities Registration

Exempt Securities

- Ark. Code Ann. § 23-42-503 – exempted securities and requirements
- Rule 503 of the Rules of the Arkansas Securities Commissioner

Exempt Transactions

- Ark. Code Ann. § 23-42-504 – exempted transactions and requirements
- Rule 504 of the Arkansas Securities Commissioner

*Certain exemptions require a filing with the Department prior to sale

*Burden of proof of an exemption rests with the claimant

Securities Registration

Covered Securities

- Section 18(b) of Securities and Exchange Act of 1933
 - Regulation A (Reg A) and Regulation (Reg D)

*Covered Securities not exempt from state anti-fraud provisions

- Notice Filings
- “Bad Boy” Reviews

BD/IA Section

Investment Adviser/Broker-Dealer Section

- Chief Examiner, Examiner Supervisor, 3 Examiners

Central Registration Depository (CRD) – central licensing and registration system used by the U.S. securities industry and regulators

Processes registration applications, reviews registrant disclosures, and examines registrants on a continuing basis

BD/IA Section – Registration Requirements

Broker-Dealers and Agents

- Rule 302.01 of the Arkansas Securities Commissioner
- Agent Examination Requirements – Rule 302.01(c)

Investment Advisers and Representatives

- Rule 302.02 of the Arkansas Securities Commissioner
- Representative Examination Requirements – Rule 302.02(f)

BD/IA Section – IAs and Reps

Investment Adviser – Ark. Code Ann. § 23-42-102(9) – any “person” who *for compensation* engages in the business of advising others as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or issues analyses or reports concerning securities

- The definition includes a financial planner or other entity that provides or holds itself out as providing investment advice to others for compensation

Representative – Ark. Code Ann. § 23-42-102(14) – any “person” employed by an investment adviser who *for compensation* makes recommendations or renders advice regarding securities, manages accounts or portfolios of clients, determines which recommendation or advice regarding securities should be given, or supervises employees who perform any of the foregoing.

BD/IA Section - BDs and Agents

Broker-Dealer – Ark. Code Ann. § 23-42-102(3)(A) – any “person” engaged in the business of effecting transactions in securities for the account of others or for his or her own account

Agent – 23-42-102(1)(A) – an individual, other than a broker-dealer, who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales of securities; or supervises individuals who effect or attempt to effect purchases or sales of securities for a broker-dealer

BD/IA Section –BDs vs. IAs

Two Key Differences

Standard Methods of Compensation Different

- Assets Under Management – common arrangement for IAs
- Commissions for BDs

Legal Standard of Care Different

- Fiduciary Duty for IAs
- Suitability Standard for BDs (But Reg BI!)

BD/IA Section - Examination Program

Routine Exams

- Arkansas-based firms undergo routine examinations on a continuing and regular schedule

For-Cause Exams

- May initiate exams for-cause, particularly following complaint or other notification of suspected misconduct

Enforcement

Enforcement Section

- Chief Examiner, 3 Examiners

Primary Ways Enforcement Section Receives Cases

- Complaints from Public (Phone Calls, Complaint Form on Website)
- Exam Referrals (Routine and For-Cause Exams)
- CRD Disclosures
- Referrals from Other Regulatory Agencies (AG, States, FINRA, SEC, DOL)

Enforcement – NASAA Statistics

2017 Enforcement Statistics at a Glance	
Investigations	4,790
Enforcement Actions (administrative, civil, and criminal)	2,105
Investor Restitution Ordered	\$486 million
Fines, Penalties, and Costs Assessed	\$93.8 million
Criminal Relief (incarceration, probation, deferred prosecution)	1,985 years
Licenses Withdrawn, Denied, Revoked, Suspended, or Conditioned	3,578

Enforcement – Arkansas Statistics

2018 Enforcement Statistics at a Glance	
Inquiries and Investigations	499
Enforcement Actions	29
Fines and Penalties Assessed	\$591,500.00
Licenses Withdrawn, Denied, Revoked, Suspended, or Conditioned	341

Enforcement – Primary Civil Remedies

Injunction (Circuit Court)

- TRO – Asset Freeze
- Receivership
- Disgorgement (“ill-gotten gains”)
- Restitution
- Fine (not more than total amount received for violations)

Administrative

- Cease and Desist Orders
- Fines (\$10,000.00 per violation or amount received; 2x for 65 and older)
- Denial/Suspension/Revocation of Registration

Enforcement - Registrants

Ark. Code Ann. § 23-42-308 sets out various grounds for which the Commissioner may deny, revoke, suspend, or condition a registration.

Additional Codes of Conduct

Broker-Dealers and Agents

- Rule 308.02 of the Arkansas Securities Commissioner – (a) through (y)

Investment Advisers and Representatives

- Rule 308.02 of the Arkansas Securities Commissioner – (a) through (y)

Enforcement - Registrants

Some Primary Enforcement Issues

- Fraud
- Violation of Fiduciary Duty
- Suitability
- Churning (BDs)
- Failure to Supervise (firms)
- Books and Records
 - Failure to Disclose Liens

Enforcement – Non-Registrants

- **Unregistered Persons/Entities** selling **Unregistered Securities** by means of **Securities Fraud** (“Flim Flam Artists”)
- Definition of a Security is Broad – Ark. Code Ann. §23-42-102(17)(A)
- Investment Contract (Catch-All Category) – defined by case law
 - Look For: investment in a common enterprise where expectation of profits is derived solely from the efforts of the promoter or a third-party

Enforcement - Fraud

Ark. Code Ann. § 23-42-507 – prohibits fraud or deceit in connection with offer, sale, or purchase of securities

It is unlawful for any “person” in connection with the offer, sale or purchase of any security, directly or indirectly:

- (1) To employ any device, scheme, or artifice to defraud;
- (2) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading; or
- (3) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

Enforcement – Fraud

Primary Investigative Techniques

- Subpoenas
 - Bank Records and Documents
 - Witnesses
- Bank Record Analysis
 - “People lie, but bank records never lie.”
 - “Follow the money.”
- Witness Interviews (under oath)

Enforcement – Fraud

Top Investor Threats

- Unregistered Products/Unregistered Salespersons
- Promissory Notes (business in trending areas)
- Oil/Gas Investments
- Affinity Fraud (Churches, Charities, Schools, Social Organizations)
- Ponzi Schemes/Pyramid Schemes
- Prime Bank Schemes
- Real Estate-related Investments
- Unsuitable Insurance Products

Enforcement - Fraud

NASAA - Emerging Investor Threats

- Marijuana Industry Investments (IPOs, MRBs)
- Digital Currency (initial coin offerings)
- Cybersecurity Risks (identity theft)

Enforcement - Fraud

Investment Red Flags

- **Guaranteed High Returns** – far better than index average!
- **No Risk!** – you've got nothing to lose!
- **High Pressure Tactics** – limited time/amount, get in before it's too late!
- **Exclusive Access/Opportunities** – available only to certain investors!
- **Inside Information** – only the promoter has the secret!
- **Offshore Investment** – tax free!
- **Credentials and Extensive Experience** – but not registered with ASD!

Enforcement – Criminal Referrals

A Sampling of Successful Criminal Referrals

- In the Matter of Dragonfly Industries International, LLC, et al.
 - 2018 – 2019 - One guilty plea, two indictments
- In the Matter of Thomas James, et al.
 - 2016 – 108 months in federal prison and \$524,203.46 in restitution
- Arkansas Securities Commissioner vs. Rodney Callaway, et al.
 - 2013 – 71 months in federal prison and \$300,000.00 in restitution
- In the Matter of Jeff Rand, et al.
 - 2012 – 57 months in federal prison and \$7.9 million in restitution

Investor Education Program

In 1998, the Department implemented the Investor Education Program, a public education initiative to inform Arkansas citizens regarding investing and securities.

- Town Halls - Civic and Senior Groups
- Middle and Secondary Schools
- Governor Hutchinson's Initiative – Prisons

Investor Education Fund

- Ark. Code Ann. § 23-42-213 – fines up to \$150,000 deposited into fund

2018

- 61 investor education programs
- 2,492 attendees in programs

Uniform Money Services Act

Presenter

Jurisdiction - Key Areas

- Money Transmission – receiving money or monetary value for transmission, selling or issuing payment instruments, or selling or issuing stored value.
- Currency Exchange – the receipt of revenues from the exchange of money of one government for money of another government.

Jurisdiction – Key Areas Continued

- A person may not engage in the business of money transmission or advertise, solicit, or hold itself out as providing money transmission unless the person is licensed or excluded from the Act. Ark. Code Ann. § 23-55-201
- A person may not engage in currency exchange or advertise, solicit, or hold itself out as providing currency exchange for which the person receives revenues equal or greater than five percent of total revenues unless the person is licensed. Ark. Code Ann. § 23-55-401

Jurisdiction – Potential “Overlap”

- Consumer Financial Protection Bureau (CFPB)
- Financial Crimes Enforcement Network (FinCEN)
- Department of the Treasury’s Office of Foreign Assets Control (OFAC)
- Arkansas Attorney General

Jurisdiction – Important Federal Law

- Bank Secrecy Act of 1970
 - AML/KYC Rule
 - SARs Reporting
- MSB Registration Rule

Jurisdiction - MTRA and CSBS

- Money Transmitters Regulatory Association (MTRA) founded in 1989, MTRA supports state regulators in the efficient and effective regulation of the money transmission industry in the United States. Currently MTRA consists of 49 member states.
- Conference of State Bank Supervisors (CSBS) was organized in 1902 to support state regulators in advancing the system of state financial supervision by ensuring safety, soundness and consumer protection; promoting economic growth; and fostering innovative, responsive supervision.

MSB Licensing

- Review and approve license and renewal applications for each of the money services business or currency exchanger.
- On-site compliance examinations are conducted at the main Arkansas offices.
- For-Cause examinations
- Utilizing data and analytics.

Industry Trends

- Moving from an agent based model to technology based model.
- Unbanked or underbanked
- Digital payments
 - How payments are received
 - Currency shifting to mobile options

MSB Agents - Nationwide

Number of Agents in NMLS	Companies
10,000 or more	9
5,000 – 9,999	4
1,000 – 4,999	17
500 – 999	11
100 – 499	24
50 – 99	23
10 – 49	55
Less than 10	61
0 (No Agents Used by Principal)	216

- 2018 MSB Fact Sheet as of 12-31-2018 prepared by CSBS

International Money Transmission Activity

- Global remittances reached \$689 billion in 2018 up from \$633 billion in 2017.
 - Mexico
 - China
 - India*
 - Philippines
 - Vietnam
- 33.48 billion was sent to Mexico last year, a 10.5% increase over 2017, which caused remittances to be the second largest foreign currency earner after auto exports.

Arkansas MSB Activity – Q1 2019

Heading	Line Item	Filing Quar...	2019Q1
Money Transmission	TA10 Total # of transactions from U.S. states and territories to U....		1,072,246,813
	TA20 Total \$ amount received for transmission from U.S. states ...		\$233,357,287,115
	TA30 Total # of transactions from U.S. states and territories to fo...		172,300,204
	TA40 Total \$ amount received for transmission from U.S. states ...		\$46,572,624,957
	TA50 Total # of All Money Transmission Transactions		1,244,547,017
	TA60 Total \$ Amount of All Money Transmission Transactions		\$279,929,912,072
Payment Instruments	TA70 Total # of payment instruments issued/sold		87,612,856
	TA80 Total \$ amount of payment instruments issued/sold		\$43,866,467,454
Stored Value	TA90 Total # of stored value transactions		1,282,717,591
	TA100 Total \$ amount of stored value transactions		\$91,467,826,069
Check Cashing	TA110 # of checks cashed		1,173,917,221
	TA120 \$ amount of checks cashed		\$2,632,387,028
	TA130 \$ amount of fees collected		\$31,309,347
	TA140 Maximum percentage charged for check		669.73
FIAT Currency Exchange	TA150 # of currency exchange transactions completed		822,414
	TA160 \$ amount of currency exchange transactions completed		\$1,038,567,918
	TA170 \$ amount of fees collected		\$5,105,825
Virtual Currency	TA180 Total # of Virtual Currency to Virtual Currency Transactions		682,959
	TA190 Total \$ amount of Virtual Currency to Virtual Currency Tra...		\$944,702,280
	TA200 Total # of Virtual Currency to U.S. Dollar Transactions		1,278,701
	TA210 Total \$ amount of Virtual Currency to U.S. Dollar Transact...		\$325,149,428
	TA220 Total # of U.S. Dollar to Virtual Currency Transactions		5,714,893
	TA230 Total \$ amount of U.S. Dollar to Virtual Currency Transact...		\$1,530,377,038
	TA240 Total # of Virtual Currency Exchange Transactions		25,330,210
	TA250 Total \$ amount of Virtual Currency Exchange Transactions		\$8,091,862,108
	TA260 Total # of Virtual Currency Transactions		33,006,763
TA270 Total \$ Amount of Virtual Currency Transactions (in U.S. ...		\$10,892,090,854	

Fair Mortgage Lending Act

Presenter

Jurisdiction – Key Areas

- Mortgage Broker – a person who accepts, solicits, negotiates, or issues mortgage loan commitments or interest rate guarantee agreements to borrowers.
- Mortgage Banker – a person who engages in the business of making mortgage loans by closing a mortgage loan, advancing funds, offering to advance funds, or making a commitment to advance funds to a borrower.
- Mortgage Servicer – a person that receives or has the right to receive from or on behalf of a borrower the funds or credits in payment for a mortgage loan or the taxes and insurance associated with a mortgage loan.
- Loan Officer – a person who accepts, solicits, negotiates, or issues mortgage loan commitments or interest rate guarantee agreements to borrowers on behalf of a mortgage broker or mortgage banker.

Jurisdiction – Key Areas continued

- It is unlawful for any person located in Arkansas other than an exempt person to act or attempt to act, directly or indirectly, as a mortgage broker, mortgage banker, loan officer, or mortgage servicer without first obtaining a license from the Securities Commissioner under this subchapter. Ark. Code Ann. § 23-39-503(a)
- It is unlawful for any person other than an exempt person to act or attempt to act, directly or indirectly, as a mortgage broker, mortgage banker, loan officer, or mortgage servicer with any person located in Arkansas without first obtaining a license from the commissioner under this subchapter. Ark. Code Ann. § 23-39-503(b)

Jurisdiction – Potential “Overlap”

- Consumer Financial Protection Bureau (CFPB)
- Financial Crimes Network (FinCEN)
- Office of the Comptroller of the Currency (OCC)
- Federal Housing Administration (FHA)
- U.S. Department of Housing and Urban Development (HUD)
- Government National Mortgage Association (Ginnie Mae)
- Arkansas Attorney General

Jurisdiction – Important Federal Law

- Equal Credit Opportunity Act of 1974
- Home Mortgage Disclosure of 1975
- Fair Debt Collection Practices Act of 1977
- Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010
- S.A.F.E. Mortgage Licensing Act of 2008
- Truth in Lending Act of 1968
- Real Estate Settlement Procedures Act of 1974
- Bank Secrecy Act of 1970
- Unfair and Deceptive Acts and Practices
- CFPB Rules

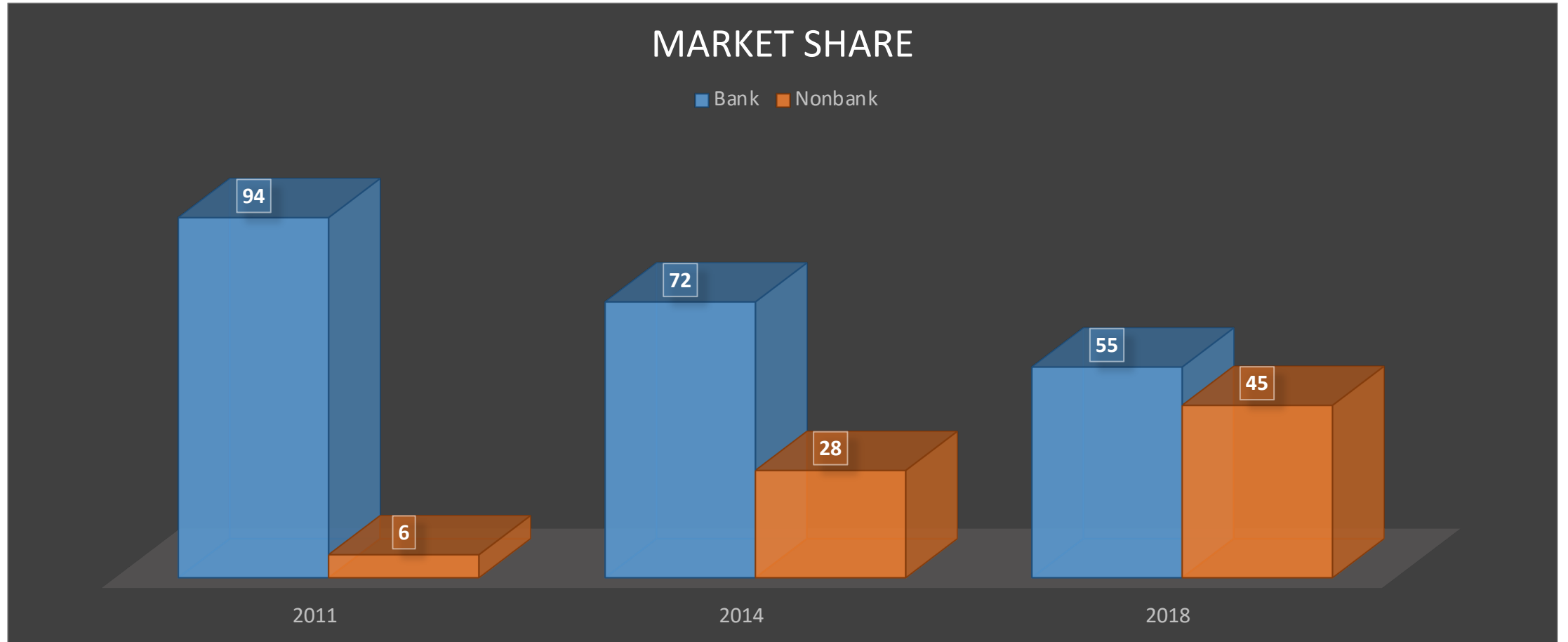
Jurisdiction – CSBS and AARMR

- The Conference of State Bank Supervisors (CSBS) - organized in 1902 to support state regulators in advancing the system of state financial supervision by ensuring safety, soundness and consumer protection; promoting economic growth; and fostering innovative, responsive supervision.
- The American Association of Residential Mortgage Regulators (AARMR) – organized to promote the exchange of information and education concerning the licensing, supervision and regulation of the residential mortgage industry, to ensure the ability of state mortgage regulators to provide effective mortgage supervision for a safe and sound industry meeting the needs of the local financial markets and to protect the rights of consumer

Licensing and Examination

- Review and approve license and renewal applications for each of the mortgage companies and their loan officers.
- On-site compliance examinations are conducted at the main Arkansas offices and branches.
- For-Cause examinations.
- Utilizing data and analytics.

Market Share Bank vs Nonbank



Industry Trends

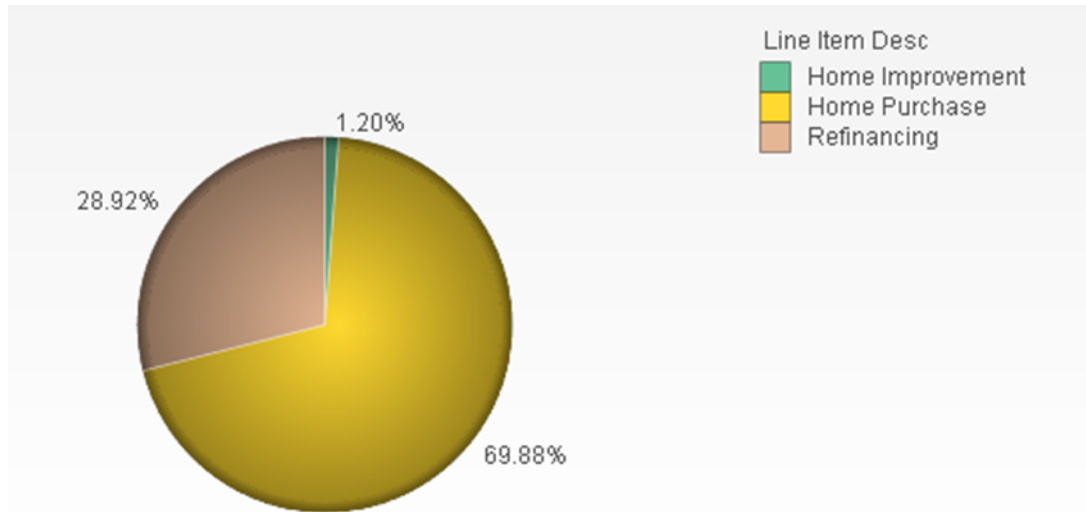
Mortgage Loan Originators Operating at Nonbanks and Depositories

Year	MLO Individuals (nonbank)	Companies (nonbank)	MLO Individuals (depository)	Companies (depository)
2018	165,240	17,572	415,517	9,196
2017	158,200	17,000	421,700	9,500
2016	145,200	16,300	422,600	9,800
2015	135,000	16,000	407,200	10,200
2014	131,700	16,000	398,700	10,500
2013	130,300	16,100	404,200	10,800
2012	105,600	15,900	399,300	11,000

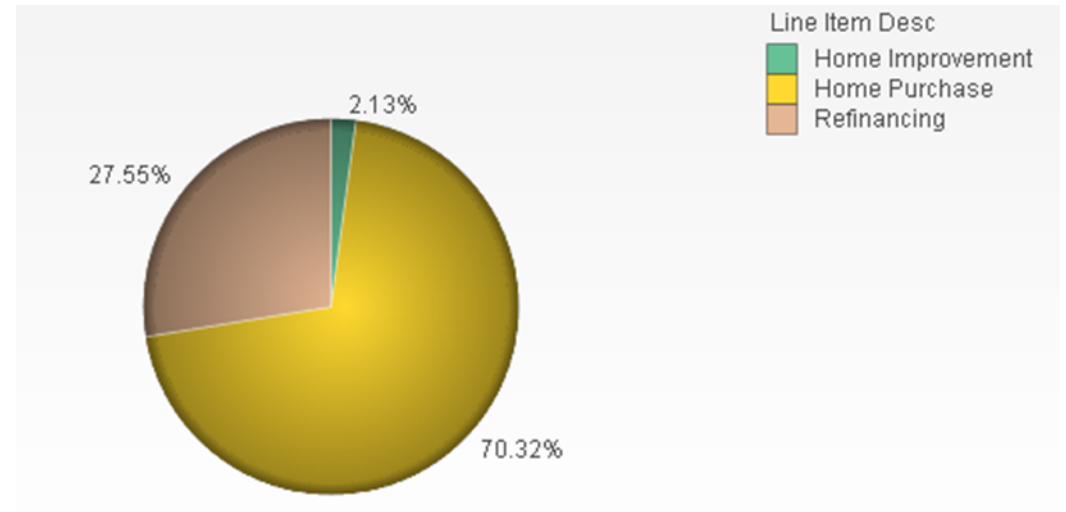
- 2018 Mortgage Industry Report prepared by CSBS

Arkansas Data

- 2018 Arkansas totals



- 2018 Nationwide totals



Industry Trends

- Acceleration of automation and digitization of the mortgage process.
- Cybersecurity.
- Continued trend towards nonbank origination and servicing.

Top Threats

- MSB
 - Cryptocurrency
 - Cyber Crimes
 - AML/BSA
- Mortgage
 - The economy
 - Antiquated systems
 - Cybersecurity

The Future of the Nonbank Industry

- Increase in automation, financial technology (fintech) or regulatory technology (regtech).
- A more harmonized market across state lines and internationally.
- The acquisition or closing of smaller companies as larger companies expand into more states.
- Artificial Intelligence.
- Blockchain.

Closing Remarks

Questions?

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