

STATE OF NEVADA

Performance Audit

Department of Business and Industry
Division of Financial Institutions

2018



Legislative Auditor
Carson City, Nevada

Audit Highlights



Highlights of performance audit report on the Division of Financial Institutions issued on May 2, 2018. Legislative Auditor report # LA18-18.

Background

The Division of Financial Institutions (Division), created in 1983, is an agency in the Department of Business and Industry. Its mission is to maintain a financial institutions system for the citizens of Nevada that is safe and sound, protects consumers, and defends the overall public interest. The Division also promotes economic development through the efficient, effective, and equitable licensing, examination, and supervision of depository, fiduciary, and non-depository financial institutions.

The Division's primary responsibilities include reviewing applications for licensing, issuing new and renewal licenses, examining licensees on an annual basis, processing written complaints, and conducting investigations of violations. As of June 1, 2017, the Division had 2,666 licensees.

The Division is self-funded with revenues consisting primarily of assessments on depository and non-depository licensees, and license and examination fees, which amounted to over \$3.3 million in fiscal year 2017. As of June 30, 2017, the Division had 30 filled positions in its Carson City, Reno, and Las Vegas offices.

Purpose of Audit

The purpose of this audit was to determine whether the Division's oversight of non-depository financial institutions effectively ensures regulatory compliance. Our audit focused on the Division's regulatory and financial activities for fiscal year 2017. We also included information in certain areas from prior years.

Audit Recommendations

This audit report contains five recommendations to enhance the Division's regulatory processes. The Division accepted the five recommendations.

Recommendation Status

The Division's 60-day plan for corrective action is due on July 27, 2018. In addition, the six-month report on the status of audit recommendations is due on January 27, 2019.

Division of Financial Institutions

Department of Business and Industry

Summary

The Division's oversight of non-depository financial institutions effectively ensured regulatory compliance; although, enhancements can be made to strengthen certain processes. The Division adequately administered annual examinations, fees, reports, violations, and complaints. However, inconsistencies in the examination process can be reduced by maintaining better documentation, improving the accuracy of reporting, and enhancing underlying policies and procedures. Additionally, the follow-up process on licensees with less-than-satisfactory examinations needs to be formalized in policies and procedures. The Division can also improve visibility into its ability to accomplish its mission by reporting an outcome-based performance measure detailing the results of examinations. Furthermore, the Division would benefit from a centralized tracking system for payday loans. These enhancements will help protect consumers and promote public interest in non-depository institutions.

Key Findings

The Division has adequately administered state laws and regulations concerning non-depository licensees. The Division completed required annual examinations, ensured licensees submit required fees and reports timely, and took prompt action regarding examination violations and consumer complaints. (page 6)

The Division could improve its documentation of the work performed during an examination. Documentation generally lacked a statement showing the population and sample selection methodology for licensee loans and check cashing transactions reviewed. Additionally, examination periods varied and often did not cover the entire period since the licensee's last examination, as management indicated is a Division practice. (page 9)

Examination reports did not always accurately reflect the scope of work performed. Our testing found instances where the standard language in the Division's report template was not revised to reflect the actual work performed. In addition, 19% of the examination reports reviewed, which stated the loan population and sample size, were inaccurate and did not agree with the reviewed loans documented in the examination workpapers. (page 11)

The Division needs to enhance its written policies and procedures over its examination process. Clearly defined policies and procedures provide a framework for conducting consistent and efficient work, while communicating approved processes and expectations to examination staff. (page 11)

The Division needs to formalize in policies and procedures the follow-up process for licensees receiving a less-than-satisfactory examination. The Division considers licensees' violation response letters and other factors when deciding whether its staff will conduct a follow-up examination to verify corrective actions were properly implemented. Considering approximately 33% of licensed payday lenders received a less-than-satisfactory examination rating annually over the last 5 years, performing adequate follow-up on licensees with noted violations of state laws and regulations is important for ensuring consumers are adequately protected against unfair or unlawful financial practices. Furthermore, documenting this process is important because licensees receiving less-than-satisfactory examinations should receive close regulatory supervision due to their increased risk of non-compliance. (page 13)

The Division can improve its performance measures by reporting an outcome-based measure detailing the results of examinations to the Legislature. Over the last 5 years, on average only 67% of licensees providing loan and check cashing services were in satisfactory compliance with state laws and regulations based on the Division's examinations. Current performance measures provide examination output and workload statistics, but do not show the impact examinations are having on licensees' overall compliance with state laws and regulations. (page 15)

A centralized tracking system for payday loans can be of significant value to the Division, its licensees, and Legislators. A database would assist licensees with managing loans and determining loan eligibility. It would also help licensees comply with state payday lending laws and help consumers avoid becoming overloaded with debt. Additionally, it would help the Division identify irregular lender activity and serve as an information system for staff preparing for an examination. A centralized tracking system would provide regulatory oversight and collect statistical information on licensees providing loan services. (page 17)

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This report contains the findings, conclusions, and recommendations from our performance audit of the Division of Financial Institutions. This audit was conducted pursuant to the ongoing program of the Legislative Auditor as authorized by the Legislative Commission. The purpose of legislative audits is to improve state government by providing the Legislature, state officials, and Nevada citizens with independent and reliable information about the operations of state agencies, programs, activities, and functions.

This report includes five recommendations to enhance the Division's regulatory processes. We are available to discuss these recommendations or any other items in the report with any legislative committees, individual legislators, or other state officials.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Rocky Cooper".

Rocky Cooper, CPA
Legislative Auditor

April 10, 2018
Carson City, Nevada

Division of Financial Institutions

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Introduction

Background

The Division of Financial Institutions (Division), created in 1983, is an agency in the Department of Business and Industry. Its mission is to maintain a financial institutions system for the citizens of Nevada that is safe and sound, protects consumers, and defends the overall public interest. The Division also promotes economic development through the efficient, effective, and equitable licensing, examination, and supervision of depository, fiduciary, and non-depository financial institutions.

The Division's primary responsibilities include:

- ❖ Reviewing applications for licensing;
- ❖ Issuing new and renewal licenses;
- ❖ Examining licensees on an annual basis;
- ❖ Processing written complaints; and
- ❖ Conducting investigations of violations.

As of June 1, 2017, the Division had 2,666 licensees. Exhibit 1 shows the number of licensees by type.

**Number of Licensees by Type
As of June 1, 2017**

Exhibit 1

Depository Institutions	
Banks ⁽¹⁾	26
Credit Unions ⁽¹⁾	58
Foreign Credit Unions ⁽¹⁾	7
Thrift Companies ⁽¹⁾	24
Total Depository Institutions	115
Fiduciary Institutions	
Family Trust Companies	27
Retail Trust Companies ⁽¹⁾	22
Total Fiduciary Institutions	49
Non-Depository Institutions	
Check Cashing/Deferred Deposit, High-Interest, and Title Loan Services ⁽¹⁾	524
Collection Agencies	445
Debt Management Services	29
Foreign Collection Agencies	252
Installment Loan Services	38
Money Transmitting Services	85
Total Non-Depository Institutions	1,373
Total Collection Agency Managers	1,119
Total Private Professional Guardians	10
Total Number of Licensees	2,666

Source: Division of Financial Institutions.

⁽¹⁾ Includes branch locations.

The Division's licensees include depository, fiduciary, and non-depository financial institutions. Depository institutions include banks, savings and loan associations, savings banks, thrift companies, and credit unions. These institutions hold or receive deposits, savings, or share accounts; issue certificates of deposit; or provide its customers other depository accounts which are subject to withdrawal. Fiduciary institutions include trust companies which receive on-deposit money or property from a public administrator or other fiduciary. However, a majority of the Division's licensees are non-depository institutions. The Division regulates the following non-depository institutions:

- Check Cashing Service – any person engaged in the business of cashing checks for a fee, service charge, or other consideration.

-
- Collection Agency – all persons engaging, directly or indirectly, and as a primary or secondary object, business or pursuit, in the collection of or in soliciting, or obtaining in any manner the payment of a claim owed or due or asserted to be owed or due to another.
 - Debt Management Service – an intermediary between an individual and one or more creditors of the individual for the purpose of obtaining concessions and includes credit counseling, the development and implementation of debt-management plans, and debt settlement services.
 - Deferred Deposit Loan Service – any person engaged in the business of making deferred deposit loans for a fee, service charge, or other consideration.
 - Foreign Collection Agency – any person meeting the qualifications to do business as a collection agency in this State, but located outside of the State, collecting claims from residents of the State on behalf of residents of another state.
 - High-Interest Loan Service – any person engaged in the business of providing high-interest loans for a fee, service charge, or other consideration.
 - Installment Loan Service – any person engaged in the business of lending, except for deferred deposit, high-interest, and title loans, for a fee, service charge, or other consideration.
 - Money Transmitting Service – any person engaged in the business of selling or issuing checks, receiving for transmission or transmitting money or credits, or both.
 - Title Loan Service – any person engaged in the business of providing title loans for a fee, service charge, or other consideration.

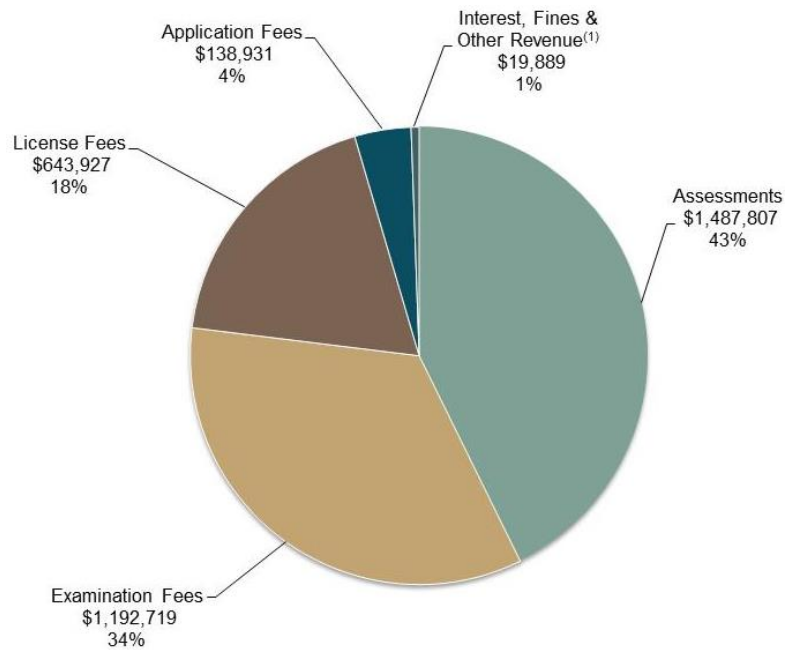
The Division also tests and certifies collection agency managers, and licenses private professional guardians who receive compensation for services as a guardian to three or more wards who are not related to the guardian by blood or marriage.

The Division has three office locations. The Commissioner, Certified Public Accountant, and southern Nevada examiners are located in Las Vegas, with northern Nevada examiners located in Reno. The agency's licensing and fiscal staff are located in Carson City with these duties performed by the Director's Office of the Department of Business and Industry. As of June 30, 2017, the Division had 30 filled positions.

The Division is self-funded with revenues consisting primarily of assessments on depository and non-depository licensees, and license and examination fees. Division expenditures are primarily salaries and operating expenses. Exhibit 2 shows assessments, fees, and other revenues during fiscal year 2017.

**Assessments, Fees, and Other Revenues
Fiscal Year 2017**

Exhibit 2



Source: State accounting system.

Note: The Division has reserves of \$4.1 million not included in the chart above.

⁽¹⁾ Other revenue includes a \$100 General Fund appropriation.

Scope and Objective

The scope of our audit focused on the Division's regulatory and financial activities for fiscal year 2017. We also included information in certain areas from prior years. Our audit objective was to:

- Determine whether the Division's oversight of non-depository financial institutions effectively ensures regulatory compliance.

This audit is part of the ongoing program of the Legislative Auditor as authorized by the Legislative Commission, and was made pursuant to the provisions of NRS 218G.010 to 218G.350. The Legislative Auditor conducts audits as part of the Legislature's oversight responsibility for public programs. The purpose of legislative audits is to improve state government by providing the Legislature, state officials, and Nevada citizens with independent and reliable information about the operations of state agencies, programs, activities, and functions.

Enhancements Can Improve the Division's Regulatory Processes

The Division's oversight of non-depository financial institutions effectively ensured regulatory compliance; although, enhancements can be made to strengthen certain processes. The Division adequately administered annual examinations, fees, reports, violations, and complaints. However, inconsistencies in the examination process can be reduced by maintaining better documentation, improving the accuracy of reporting, and enhancing underlying policies and procedures. Additionally, the follow-up process on licensees with less-than-satisfactory examinations needs to be formalized in policies and procedures. The Division can also improve visibility into its ability to accomplish its mission by reporting an outcome-based performance measure detailing the results of examinations. Furthermore, the Division would benefit from a centralized tracking system for payday loans. These enhancements will help protect consumers and promote public interest in non-depository institutions.

Administration of Annual Examinations, Fees, Reports, Violations, and Complaints Is Adequate

The Division has adequately administered state laws and regulations concerning non-depository licensees. The Division completed required annual examinations, ensured licensees submit required fees and reports timely, and took prompt action regarding examination violations and consumer complaints.

Annual Statutorily Required Examinations Performed

We found that the Division is performing annual examinations of non-depository licensees. Various state laws require annual examinations of non-depository institutions. During fiscal year 2017, the Division performed 1,447 non-depository licensee examinations.

Our testing of 75 non-depository licensees indicated all institutions were examined in fiscal year 2017. This is a significant improvement from our last audit. Annual examinations help ensure licensees are in compliance with the various state laws and regulations in place to protect citizens from unscrupulous lending practices.

Effective Collection of Examination Fees

The Division has an effective process for the collection of examination fees. Various state laws and regulations authorize the Division to charge and collect from each licensee an hourly examination fee. Hourly fees range from \$30 to \$100 depending on the type of licensee. During fiscal year 2017, non-depository institutions paid about \$1.2 million in examination fees.

Our testing of 75 non-depository licensees revealed examinations were promptly billed, billings were mathematically accurate, and hourly examination fees agreed with state law. Licensees also paid within 30 days or paid statutorily-defined late fees. Timely and accurate examination billings are critical to the Division's operations as it is primarily self-funded.

Licensees Submitted Reports When Required

The Division's monitoring ensured licensees submitted annual reports when required. State law requires licensees to submit an annual report of operations with financial statements. The Division's Certified Public Accountant reviews these reports as part of the institution's annual license renewal process. During fiscal year 2017, non-depository institutions paid over \$550,000 in licensing fees.

We tested 75 non-depository licensees and found most annual reports were submitted on time. The Division promptly followed up with late submittals and collected the proper late fees. Annual reports provide the Division insight into its licensees' business activities and financial health. Timely submittal allows for the Division's prompt review and analysis to confirm the licensee is viable and should continue being licensed.

Examination Violations Promptly Addressed

Our review of examinations performed on 75 non-depository licensees revealed that the institutions promptly addressed violations with the submittal of a 30-day violation response letter. Division management also reviewed all violations resulting in a less-than-satisfactory examination rating and considered disciplinary action when deemed necessary. In fiscal year 2017, the Division cited 2,156 violations of state laws and regulations. Appendix A on page 20 shows the most common non-depository licensee violations cited over the last 5 years.

The Division requires licensees with violations resulting in a less-than-satisfactory examination rating to respond in writing within 30 days outlining the actions that will be taken to correct all deficiencies and violations noted in the examination report. Enforcing licensees' prompt response to examination violations ensures issues are being detected and corrected in a timely manner.

Licensees' Timely Response to Consumer Complaints

The Division ensures licensees adhere to state law by responding to consumer complaints in a timely manner. Licensees are statutorily required to respond to written complaints filed with the Division within 10 or 20 days, based on license type. Without a timely response, the licensee is deemed to have admitted to the allegations contained in the complaint.

In fiscal year 2017, the Division received 172 written consumer complaints against non-depository licensees. Our testing of 75 non-depository licensees revealed 27% had consumer complaints filed against them during the year. We found that the Division monitored the licensees' response to each complaint ensuring they were addressed within the statutorily-defined timeframe. Licensees' prompt response to consumer complaints ensures concerns are being addressed, thereby protecting consumers against unethical business practices.

Improvements Needed in Examination Process

The Division's examination process can be improved with better documentation and reporting. Examination files generally did not state the licensee's total population and the Division's sample selection methodology for licensee loans and check cashing transactions reviewed. Examination reports also did not always accurately reflect the examiners' scope of work. Enhanced policies and procedures would help reduce the occurrence of these issues.

Examinations Could Be Better Documented

The Division could improve its documentation of the work performed during an examination. Documentation generally lacked a statement showing the population and sample selection methodology for licensee loans and check cashing transactions reviewed. Additionally, examination periods varied and often did not cover the entire period since the licensee's last examination, as management indicated is a Division practice.

For non-depository institutions providing loan and check cashing services, the examiner obtains from the licensee a comprehensive inventory of their loans and check cashing logs. The loan listings should be inclusive of active, delinquent, closed, and declined loans for the examination period. Using these listings, the examiner selects a sample of loans and check cashing transactions to review for compliance with applicable state laws and regulations.

The following documentation issues were identified in our testing of examination loan and check cashing reviews:

- Undocumented Loan Populations – Our testing of 75 non-depository licensees revealed 26% of examinations requiring a loan review lacked a record of the total number of licensee loans. The total number of loans per type (active, delinquent, closed, and declined) is needed to ensure an adequate sample of each loan type is reviewed. Although examiners documented the number of loans reviewed, the total loan population by type was not recorded for 27 of 39 examinations we tested making it difficult to determine if an adequate sample was selected.

- Various Review Periods – Examination review periods varied for the examinations we tested. Of the 39 non-depository licensee examinations we tested that required a loan review, 16 examinations conducted a review for a period of 3 to 6 months, 7 examinations reviewed loans since the prior examination, and 16 examinations did not document the loan period reviewed. The period for check cashing reviews also varied from 1 day to 4 months.

Division management indicated that examinations did not always include the total number of licensee loans because of the length and availability of certain licensee loan inventory listings. However, total loan and check cashing populations should be stated in examination documentation to ensure an adequate sample of loans and check cashing transactions are reviewed.

Our testing also found all 53 of the 75 non-depository licensees requiring a loan and/or check cashing review lacked documentation of the methodology used by the examiner to choose their sample. Division management indicated examiners are trained on how to select their review sample. Factors used in selecting a loan sample include consumers with multiple loans or complaints. An examiner's judgment is then relied upon and the reasoning behind this judgment is not documented in the examination workpapers.

Insufficient policies and procedures led to the documentation issues noted. Adequate documentation should provide support for the work performed and to assist management with their review in ensuring examinations are being completed adequately and consistently. Requiring examiners to document their sample selection methodology also enables management to effectively review and ensure examiners are identifying appropriate loans and check cashing transactions, which may lead to potential violations.

Furthermore, comparing licensee provided loan and check cashing listings to originating documents would enable the Division to verify the accuracy and completeness of loan lists provided by its licensees. Although not currently being performed,

this would ensure licensees are accurately reporting all loans and check cashing transactions to the Division and could help ensure licensees are not giving incomplete or altered lists to the examiners from which to select their samples.

Examination Reports Can Be More Accurate

Examination reports did not always accurately reflect the scope of work performed. Upon completion of an examination, staff use a report template to assist with the writing of the report. Our testing found instances where the standard language in the Division's report template was not revised to reflect the actual work performed. For example, a couple reports stated check cashing transactions were reviewed by the examiner; however, documentation indicated check cashing transactions were not reviewed.

In addition, the Division states in each examination report the total number of licensee loans by type and the number of loans reviewed, if applicable. Our testing revealed 19% of the examination reports which stated the loan population and sample size reviewed were inaccurate and did not agree with the reviewed loans documented in the examination workpapers. When we discussed these differences with Division management, they agreed and stated the differences were most likely typographical errors.

These inaccuracies indicate examination reports lacked a thorough review. Report templates should be revised to reflect the actual scope and results of work performed, and a thorough review of examination workpapers and reports will help ensure the accuracy of the information reported.

Examination Policies and Procedures Need Enhancing

The Division needs to enhance its written policies and procedures over its examination process. Clearly defined policies and procedures provide a framework for conducting consistent and efficient work, while communicating approved processes and expectations to examination staff.

Current procedures could be enhanced to provide additional guidance to assist staff with performing examinations. Examples

of Division practices not addressed in existing policies and procedures include:

- Documenting loan and check cashing population and sample selection methodology;
- Documenting the judgment used to determine examination rating based on the number and type of violations cited;
- Follow-up process for 30-day violation response letters on less-than-satisfactory examinations;
- Timeframe for new licensees' initial examination and existing licensees' follow-up examinations;
- Process for selecting unsatisfactory examinations for review by the Division's Disciplinary Committee;
- Process for assessing administrative fines, and cease and desist orders; and
- Process for granting annual report late fee waivers.

NRS 353A.020 requires each agency to develop written procedures to carry out a system of internal accounting and administrative control. This includes a system of practices to be followed in the performance of the duties and the functions of the agency. Undocumented processes lead to different interpretations of Division practices. For example, management stated in response to the previous audit that new licensees receive an initial examination within 6 months; however, at the beginning of the audit management indicated the initial examination is performed within 12 months.

Division management stated that the breadth of examinations and the multiple variables that go into each examination make it difficult to establish comprehensive written policies and procedures. While we recognize each examination may have unique circumstances requiring staff judgment, a standard set of guidelines should be documented and used as a reference so that new and existing staff know the minimum requirements and when

Examination Follow-Up Process Needs To Be Documented

supervisory assistance is needed. When situations arise requiring deviations or exceptions to the policies, these conditions should be documented. Comprehensive, standardized policies enable the Division to ensure examinations are being done consistently, while efficiently regulating licensees to ensure statutory compliance.

The Division needs to formalize in policies and procedures the follow-up process for licensees receiving a less-than-satisfactory examination. The Division considers licensees' violation response letters and other factors when deciding whether its staff will conduct a follow-up examination to verify corrective actions were properly implemented. Considering approximately 33% of licensed payday lenders received a less-than-satisfactory examination rating annually over the last 5 years, performing adequate follow-up on licensees with noted violations of state laws and regulations is important for ensuring consumers are adequately protected against unfair or unlawful financial practices. Furthermore, documenting this process is important because licensees receiving less-than-satisfactory examinations should receive close regulatory supervision due to their increased risk of non-compliance.

State law requires an annual examination of licensed non-depository institutions. Division policy defines the examination ratings. Upon completion of an examination, the examiner rates the licensee on a scale of satisfactory, needs improvement, or unsatisfactory as follows:

- A rating of "Satisfactory" indicates that the licensee and the management of the licensee have demonstrated substantial compliance with applicable laws and regulations and that any deficiencies noted in the report can be corrected by the licensee with a minimum of regulatory supervision.
- A rating of "Needs Improvement" indicates that the licensee and the management of the licensee have demonstrated less-than-satisfactory compliance, or instances and situations involving a lack of compliance with applicable

state and federal laws and regulations and that regulatory supervision is required.

- A rating of “Unsatisfactory” indicates that the licensee and the management of the licensee have demonstrated substantial lack of compliance with applicable laws and regulations, and that immediate remedial action is required for the correction of the violations and deficiencies noted in the report.

In our prior audit of the Division, we recommended revising the examination scheduling process to ensure higher risk licensees, especially those with unsatisfactory ratings and new licensees, receive an examination prior to lower-risk licensees. When asked to describe the current status of this recommendation at the start of this audit, management indicated the examination scheduling process ensures higher-risk licensees and new licensees receive an examination prior to lower-risk licensees by scheduling:

- A follow-up examination in 3 months for licensees that receive an unsatisfactory examination rating;
- A follow-up examination in 6 months for licensees that receive a needs improvement examination rating; and
- An examination in 12 months for licensees that receive a satisfactory examination rating.

During our audit, we found the Division does not follow the process described for follow-up examinations. Our testing found 13 licensees received a less-than-satisfactory examination rating in 2016. A follow-up examination was conducted for 2 of the 13 licensees in 2017. For eight licensees, management indicated it relied upon various factors including licensees’ corrective action responses to verify corrective actions were taken. For the last three licensees, the Division indicated pending litigation prevented them from conducting a follow-up examination.

According to management, the practice to conduct follow-up examinations of less-than-satisfactory licensees is not statutorily

required. The Division relies upon several miscellaneous factors, including licensees' examination violation responses, to determine whether a follow-up examination will be conducted. Although, this process is not documented in policies and procedures.

The frequency of less-than-satisfactory follow-up examinations was previously documented in Division policies and procedures. However, current procedures do not adequately describe the follow-up process on examinations with a less-than-satisfactory rating. Procedures also do not address the practice of relying on factors such as the violation response letter to supplant the follow-up examination.

**Licensee
Compliance
Performance
Measure
Would Be
Beneficial**

The Division can improve its performance measures by reporting an outcome-based measure detailing the results of examinations to the Legislature. Over the last 5 years, on average only 67% of licensees providing loan and check cashing services were in satisfactory compliance with state laws and regulations based on the Division's examinations. Current performance measures provide examination output and workload statistics, but do not show the impact examinations are having on licensees' overall compliance with state laws and regulations.

In the 2017-2019 Executive Budget, the Division reported the following two performance measures relating to licensee examinations: (1) percentage of financial institutions examined per statute, and (2) licensees requiring examination. While this information may be useful, a measure showing the percentage of licensee examinations receiving a satisfactory rating would help the Division monitor its performance in ensuring statutory compliance, provide insight to decision makers on how well the agency is doing in achieving its overall mission, and gauge overall compliance of the industry with state laws and regulations.

Division records indicate non-depository licensees received on average an 81% satisfactory rating on examinations conducted over the last 5 years. However, licensees providing check cashing, deferred deposit, and loan services only averaged a 67% satisfactory examination rating. Exhibit 3 shows the percentage of satisfactory examinations by license type.

**Percentage of Satisfactory Examinations by License Type
Fiscal Years 2013 to 2017**

Exhibit 3

Type of Licensee	2013	2014	2015	2016	2017	5 Year Averages
Check Cashing/Deferred Deposit, High-Interest, and Title Loan Services	75%	61%	64%	66%	70%	67%
Collection Agencies	84%	87%	93%	95%	93%	90%
Debt Management Services	94%	88%	94%	90%	87%	91%
Foreign Collection Agencies	95%	92%	95%	97%	95%	95%
Installment Loan Services	91%	90%	100%	91%	79%	90%
Money Transmitting Services	98%	79%	78%	87%	78%	84%

Source: Division of Financial Institutions' Non-Depository Statistics reports.

The Division maintains examination rating information internally for statistical purposes. In fiscal year 2017, Division records indicate that 30% of licensees providing check cashing, deferred deposit, and loan services received a less-than-satisfactory examination rating. While this number may seem high, some of these licensees may have received a less-than-satisfactory rating for violations identified at other company locations. Although each location operates under the same company name, each location is individually licensed and receives separate examinations. The Division applies the same examination rating to all company locations if systemic issues are identified. For example, our review of examination reports found violations noted at several, but not all, company locations. These violations were deemed a systemic issue by Division management; therefore, applied to all locations and ultimately affected the location's examination rating. The Division uses this approach to ensure systemic issues are corrected at the company level rather than at each location.

The Budget Division of the Governor's Finance Office emphasizes the importance of outcome measures in the state's budget instructions. Outcome measures provide the results or impact of an agency's efforts. Being that the Division's primary responsibilities include examining licensees for compliance with financial institution and consumer laws, monitoring and reporting overall compliance rates would help provide the Division and other state officials important information regarding the Division's regulation of non-depository licensees.

Benefits of a Centralized Loan Database

A centralized tracking system for payday loans can be of significant value to the Division, its licensees, and Legislators. A database would assist licensees with managing loans and determining loan eligibility. It would also help licensees comply with state payday lending laws and help consumers avoid becoming overloaded with debt. Additionally, it would help the Division identify irregular lender activity and serve as an information system for staff preparing for an examination. A centralized tracking system would provide regulatory oversight and collect statistical information on licensees providing loan services.

During the 2017 Legislative Session, a payday loan database was considered through various bills; however, none of the proposed legislation passed. Although the Division was neutral in its position on all three bills, management indicated that the database would be useful for obtaining licensee loan information and expediting the examination process. Appendix B on page 21 shows a summary of the legislative bills relating to a payday loan database.

Some of the issues described in this report can be addressed with better information provided to the Division through a centralized database. For example, examinations could be improved with real-time availability of licensee data, including loan inventories and check cashing logs. This would also assist the Division with planning and identifying potential violations prior to performing the on-site examination, which would allow for more efficient and targeted examinations.

A payday loan database has many benefits relating to regulatory compliance and statistical information. Examples of some of these benefits include:

Regulatory Benefits

- Ability to incorporate requirements in state law into the database – This can alert lenders that a borrower has exceeded borrowing limits. Nevada statutory limitations that could be monitored include loan amounts to monthly

income, rollover loans, interest rates, loan durations, and repayment plans.

- Real-time notification of borrower's loan history – This can alert lenders of a borrower's probability to default on a new loan; thereby, reducing lenders default rate and associated costs. Borrower's history could include loans obtained from multiple lenders.

Informational Benefits

- Loan statistics – Provide information regarding a licensee's loan volume, loan amounts, default rates, and fees charged.
- Demographical information – Provide geographical information on areas with the greater number of payday loan lenders, including lenders with the largest volume and dollar value of loans. Borrower information could also be provided, including age and monthly income.

Out of 36 states that offer payday loans, 14 states are using a centralized database tracking system. We surveyed these 14 states and received 8 responses regarding the benefits and uses a database provides. Appendix C, beginning on page 22, shows the states' individual responses to our survey.

A common benefit indicated by the states that responded to our survey included statistical information used for preparing internal and external reports. Internal reports include various reports on loan data which are used by the state regulatory agency to identify compliance violations. External reports to the public and state governmental entities provide various statistical information on payday lenders and their borrowers. Appendix D, beginning on page 24, contains excerpts of an external report prepared by the Washington State Department of Financial Institutions.

Of the 14 states that use a payday loan database, all rely on an outside vendor to manage the system. While the same vendor is used by all 14 states, each state has its own system tailored to their own needs and regulations. Typically, a licensee will enter

the borrower's information into the system during the loan application process. If state regulatory laws are built into the system, the system will assist in identifying whether the borrower is eligible for the loan in accordance with state payday lending laws. Otherwise, the borrower's information is maintained in the system for inquiry purposes. The cost of operating a database system is typically a fee for each approved loan, covered by the lender, the borrower, or both. Our survey revealed fees ranging from \$0.49 to \$1.24 per approved loan.

With this tool, the Division may be able to lengthen its examination cycle or perform desk examinations on lower risk licensees, which would reduce Division overhead costs. Additionally, the Division would be able to obtain more accurate and complete licensee loan information, which would help with the loan documentation issues noted previously in this report.

Recommendations

1. Establish controls to ensure examinations are performed consistently within established sample selection guidelines, and licensee loan and check cashing reviews are adequately documented, including the population, time period reviewed, and verification of loan listings.
2. Enhance supervisory oversight to ensure examination workpapers and reports adequately and accurately reflect the work performed.
3. Update licensee examination procedures to be inclusive of key aspects of the examination process.
4. Develop policies and procedures to formalize the process and time period for follow-up examinations.
5. Report to the Legislature an outcome-based performance measure for monitoring non-depository licensee examination results.

Appendix A

Common Non-Depository Licensee Violations Fiscal Years 2013 to 2017

State Law or Regulation	Description	Number of Examination Violations					5 Year Totals
		2013	2014	2015	2016	2017	
NRS 604A.450	Title loans cannot exceed the fair market value of the vehicle securing the title loan.	181	156	158	211	137	843
NRS 604A.425	Deferred deposit loans cannot exceed 25 percent of the expected gross monthly income of the customer when the loan is made.	116	119	143	156	107	641
NAC 604A.180	Licensees must maintain written documentation to establish that deferred deposit loans made have not exceeded 25 percent of the customer's expected gross monthly income.	91	125	99	125	88	528
NAC 604A.200	Maintenance of original books and records by licensees for at least 3 years.	76	126	90	101	106	499
NRS 649.375	Several prohibited business practices relating to the collection of debt from customers.	156	101	64	32	40	393
NRS 649.355	Each licensee shall maintain a separate account in a bank or credit union, located within the State, in which all money collected must be deposited.	114	103	73	43	40	373
NAC 649.280	All machine-derived form letters must receive written approval from the Commissioner before they can be used by a licensee.	85	92	53	61	69	360
NRS 604A.405	Required notices and disclosures must be posted by licensees in a conspicuous place in every location at which the licensee conducts business.	42	161	7	32	104	346
NRS 649.370	Adherence to the Federal Fair Debt Collection Practices Act.	147	86	45	29	18	325
NRS 649.059	Any printed form of agreements, listing sheets, acknowledgments, communications, or other documents used in business must be submitted to the Commissioner for approval or disapproval.	77	84	43	57	63	324
Other	All other NRS and NAC violations noted by the Division.	1,856	1,869	1,290	1,303	1,384	7,702
Totals		2,941	3,022	2,065	2,150	2,156	12,334

Source: Division of Financial Institutions' Count of Violation by License Type reports.

Appendix B

2017 Legislative Session Payday Loan Database Bills

Senate/Assembly Bill	Description
S.B. 17	AN ACT relating to financial services; prohibiting a person who is licensed to operate certain loan services from making certain short-term loans to a customer under certain circumstances; requiring the Commissioner of Financial Institutions to develop, implement and maintain a database storing certain information relating to short-term loans made to customers in this State; providing that information in such a database is confidential ; revising requirements for the contents of written loan agreements between licensees and customers; revising various provisions governing short-term loans; and providing other matters properly relating thereto.
A.B. 222	AN ACT relating to financial services; prohibiting a person who is licensed to operate certain loan services from making certain short-term loans to a customer under certain circumstances; requiring a person who is licensed to operate certain loan services to verify a customer's ability to repay the loan before making certain short-term loans to the customer; prohibiting a person who is licensed to operate certain loan services from making certain short term loans to a customer with an annual percentage rate greater than 36 percent; requiring the Commissioner of Financial Institutions to develop, implement and maintain a database storing certain information relating to short term loans made to customers in this State; providing that information in such a database is confidential ; revising requirements for the contents of written loan agreements between licensees and customers; revising various provisions governing short-term loans; and providing other matters properly relating thereto.
A.B. 515	AN ACT relating to financial services; requiring the Commissioner of Financial Institutions to develop, implement and maintain a database storing certain information relating to deferred deposit loans, title loans and high-interest loans made to customers in this State; providing that information in such a database is confidential under certain circumstances ; and providing other matters properly relating thereto.

Source: Nevada's legislative website.

Appendix C

Survey of States With Centralized Loan Databases

State ⁽¹⁾	Does Your State Use a Centralized Payday Loan Database?	Is Lender Participation in the Database Required?	What Is the Fee Associated with the Database?	What Information Is Recorded in the Database?	Does Your State Use the Database for Statistical Information, Regulatory Compliance, or Both?
Kentucky	Yes	Yes	Per Transaction Fee, \$1	Multiple, including name, SSN, address, DOB, driver's license number, and loan terms	Both
Michigan	Yes	Yes	Per Transaction Fee, \$0.49	Did Not Answer	Did Not Answer
New Mexico	Yes	Yes	Per Transaction Fee, \$0.50	Multiple, including name, address, SSN, monthly income, driver's license number, and loan terms	Both
North Dakota	Yes	Yes	Per Transaction Fee, \$0.74	Multiple, including name, SSN, and loan terms	Both
South Carolina	Yes	Yes	Per Transaction Fee, Less than \$1	Multiple, including name, SSN, address, driver's license number, and loan terms	Statistical Information
Virginia	Yes	Yes	Per Transaction Fee, \$1.24	Multiple, including name, last four digits of driver's license number, address, DOB, and licensee information	Regulatory Compliance
Washington	Yes	Yes	Per Transaction Fee, amount not stated	Multiple, including name, SSN, income, and loan terms	Both
Wisconsin	Yes	Yes	Per Transaction Fee, \$1	Multiple, including name, address, SSN, DOB, driver's license number, and loan terms	Both

Appendix C

Survey of States with Centralized Loan Databases (continued)

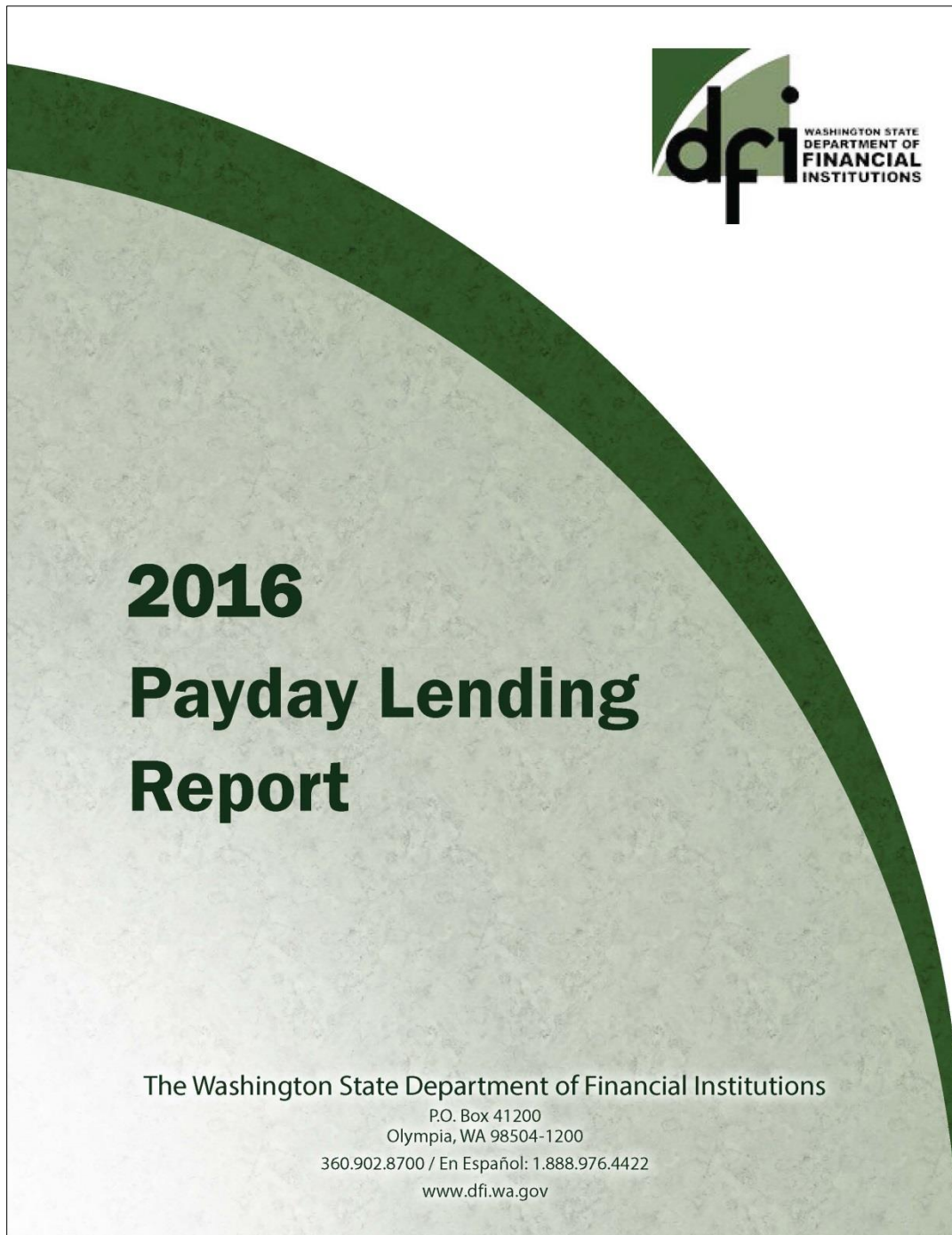
State ⁽¹⁾	What Type of Reports Are Utilized and Published from the Database?	What Statistical Information Is Gathered by the Database?	Does the Database Verify Compliance With Laws and Regulations?	Are Violations of State Laws and Regulations Flagged or Prohibited by the Database?	Does Your State Perform Periodic Exams of Payday Lenders?
Kentucky	Multiple statistical and regulatory reports	Multiple, including transaction volume, transaction amounts and fees, and number of active licensees	Yes	Yes	Yes, annually
Michigan	Did Not Answer	Did Not Answer	Did Not Answer	Did Not Answer	Yes, once every 3-5 years
New Mexico	Annual report to the legislature, and multiple statistical and regulatory reports	Multiple, including transaction volume and average transaction amounts	Yes	Yes	Yes, annually
North Dakota	Annual report to the legislature and transaction reports	Monthly and year-end data	Yes	Yes	Yes, once every 3 years
South Carolina	Annual report to the legislature, and multiple statistical and regulatory reports	Multiple, including transaction amounts and fees, number of borrowers, unpaid loan balances, and compliance statistics	Yes	Partially, the system will not allow more than one open transaction at a time, pursuant to state law	Yes, annually
Virginia	Multiple statistical and regulatory reports	Multiple, including transaction amounts and fees, interest rates, and average applicant pay cycle	Yes	No	Yes, once every 3 years
Washington	Multiple statistical and regulatory reports	Multiple, including transaction volume, transaction amounts, licensee statistics, and some demographic information	Yes	Yes	Yes, based on risk analysis and complaints rather than time
Wisconsin	Annual report to the legislature, and multiple statistical and regulatory reports	Multiple, including transaction volume, transaction amounts and fees, average percentage rate, and default information	Yes	Yes	Yes, no set frequency but averaging every 2-3 years

Source: Auditor compiled from June 2017 state survey responses.

⁽¹⁾ Survey was sent to 14 states using a shared payday loan database. No response was received from Alabama, Delaware, Florida, Illinois, Indiana, or Oklahoma.

Appendix D

Excerpts of a Washington State Payday Lending Report



Note: Selected pages of this report are presented for information purposes to show examples of information that could be available if a centralized loan database was utilized.

Appendix D

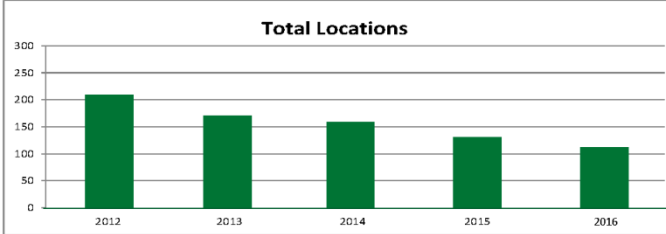
Excerpts of a Washington State Payday Lending Report (continued)

The Washington State Payday Lending Industry
2016 PAYDAY LENDING REPORT | LENDING INDUSTRY

NUMBER OF LICENSED PAYDAY LENDERS

The number of payday lending locations decreased 18.7% from year-end 2015 to year-end 2016. Overall, the number of payday lending locations has decreased 84.8% since its height in 2006.

	2012	2013	2014	2015	2016
Companies	52	46	39	29	26
Branches	151	128	121	110	87
Total Locations	203	174	160	139	113

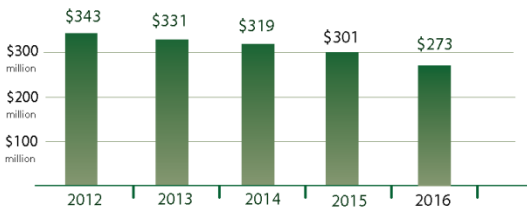


PAYDAY LOAN HISTORICAL DATA

Year	Small Loans Made	Total Amount of Small Loans
2012	909,570	\$342,989,751
2013	871,801	\$331,430,078
2014	819,755	\$319,290,707
2015	776,824	\$300,903,558
2016	710,163	\$273,746,893

TOTAL PAYDAY LOANS MADE (MEASURED IN MILLIONS OF DOLLARS)

The dollar volume of payday loans made decreased 9% from 2015 to 2016. Overall, the annual dollar volume of payday loans in Washington has decreased 80% from its peak in 2005.



Payday lending is a \$273.7 million industry in Washington.

PAGE 5

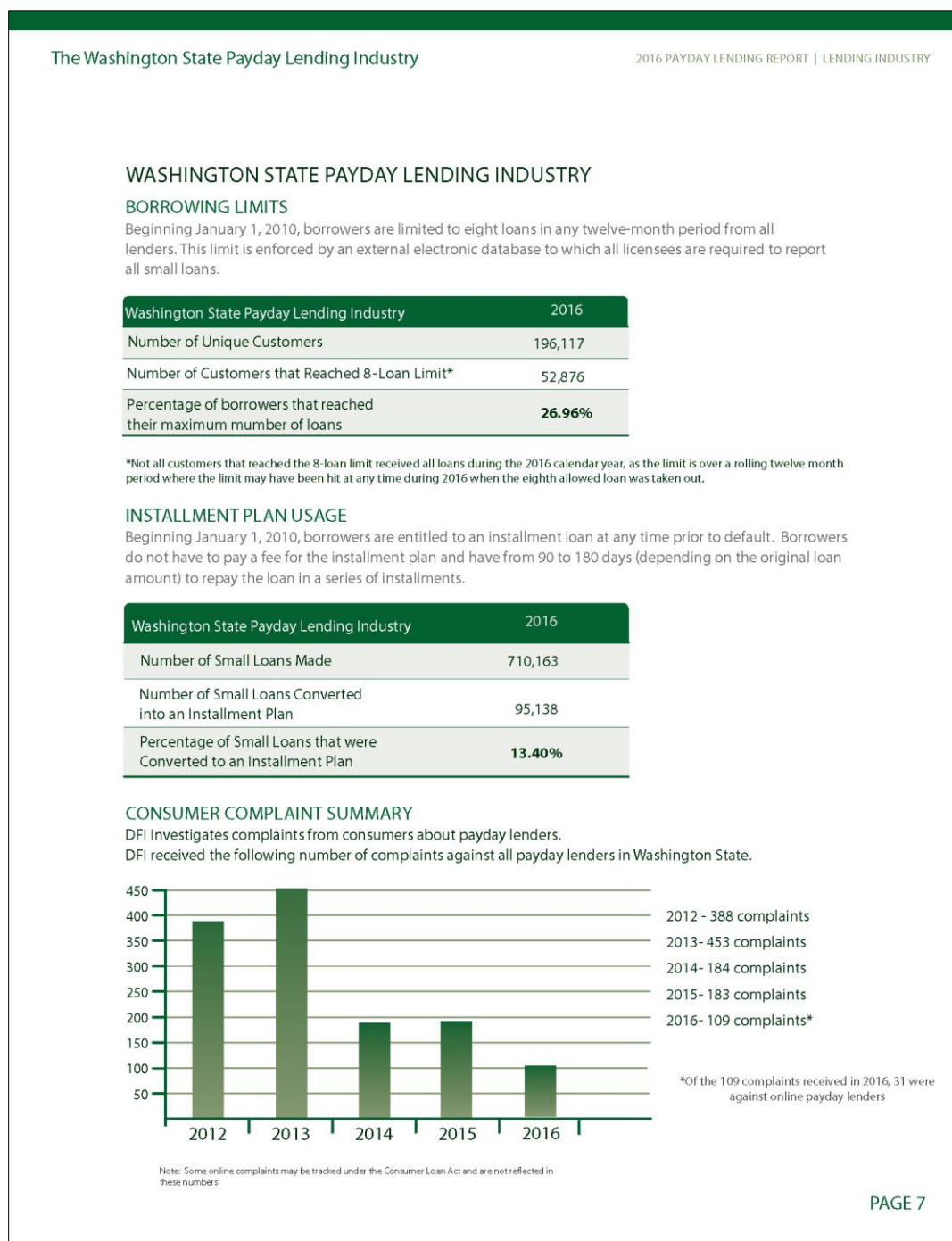
Appendix D

Excerpts of a Washington State Payday Lending Report (continued)

The Washington State Payday Lending Industry		2016 PAYDAY LENDING REPORT LENDING INDUSTRY
PAYDAY LOAN ANALYSIS		
Washington State Payday Lending Industry		2016
Volume of Payday Loans	\$273,746,893	The average payday loan in 2016 was \$385, compared to \$387 in 2015.
Number of Payday Loans	710,163	
Average Payday Loan Amount	\$385.47	
PAYDAY LOAN FEE ANALYSIS		
Washington State Payday Lending Industry		2016
Total Payday Loan Fees	\$39,017,108	The average payday loan fee in 2016 was \$54.94, compared to \$55.42 in 2015.
Number of Payday Loans	710,163	
Average Payday Loan Fee	\$54.94	
PAYDAY LOAN TERM ANALYSIS		
Washington State Payday Lending Industry		Average Term
Average Payday Loan Term for 2016- Agreement date to initial due date		22.3 Days
Average Payday Loan Term for 2016- Agreement date to final close date (including loans which went into installment plans)		38.9 Days
BORROWER INCOME		
Washington State Payday Lending Industry		Average Monthly Income*
Average Customer Income for 2016	\$3,121.80	The average monthly income in 2016 was \$3,122, compared to \$3,046 in 2015.
*Monthly income for customers is based on the most recent update to customer income in the Veritec database during 2016 and does not necessarily reflect monthly income at the time transactions were opened.		
BORROWER AGES		
Age Category	% of Customers	% of Transactions
18-24	11.0%	9.6%
25-34	26.1%	24.3%
35-44	21.7%	21.4%
45-54	18.9%	19.8%
55-64	14.4%	15.9%
65 or over	7.8%	9.1%
Total	100%	100%
		The average age of customers conducting transactions during the period was 42 years.

Appendix D

Excerpts of a Washington State Payday Lending Report (continued)



Appendix D

Excerpts of a Washington State Payday Lending Report (continued)

2016 PAYDAY LENDING REPORT | LENDING INDUSTRY

The tables on this page capture loan frequency data as the number of loans each individual borrowed during the calendar year 2016.

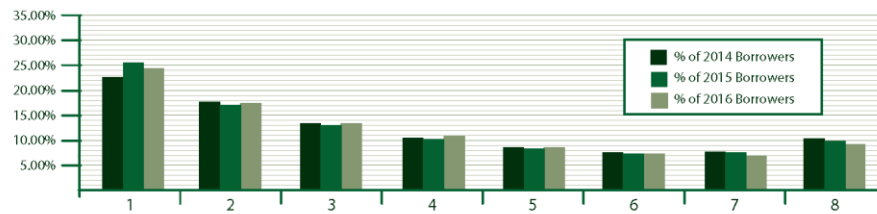
BORROWER LOAN FREQUENCY

Annual Loan Frequency	Total Borrowers	% Total Borrowers	Total Number of Loans	% of Total Loans
1 Loan	48,074	24.51%	48,074	6.58%
2 Loans	34,710	17.70%	69,420	9.50%
3 Loans	26,605	13.57%	79,815	10.93%
4 Loans	21,060	10.74%	84,240	11.53%
5 Loans	17,438	8.89%	87,190	11.93%
6 Loans	15,054	7.68%	90,324	12.36%
7 Loans	14,311	7.30%	100,177	13.71%
8 Loans*	18,865	9.62%	171,325	23.45%
TOTAL	196,117	100.00%	730,565	100.00%

*Note, this data is limited solely to loans taken out during the 2016 calendar year, which differs from the 52,876 borrowers reported on page 7 that took out an eighth loan over a rolling twelve month basis at some point during 2016.

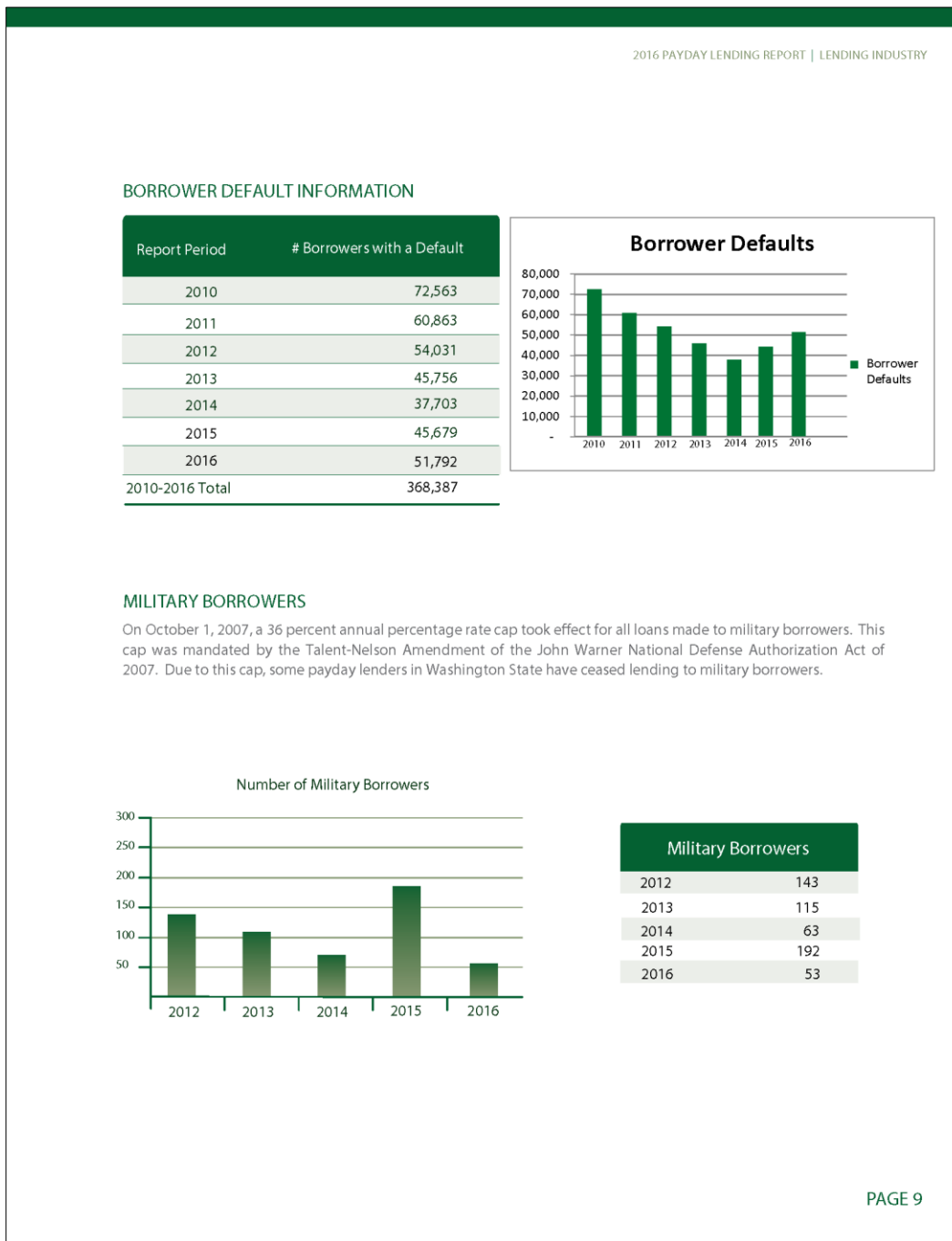
BORROWING FREQUENCY COMPARISON

No. of Loans:	1	2	3	4	5	6	7	8
2014 Percent of Total Borrowers	22.85%	17.79%	13.85%	10.60%	8.93%	7.85%	7.90%	10.22%
2015 Percent of Total Borrowers	22.56%	17.27%	13.01%	10.18%	8.61%	7.69%	7.69%	10.00%
2016 Percent of Total Borrowers	24.51%	17.70%	13.57%	10.74%	8.89%	7.68%	7.30%	9.62%



Appendix D

Excerpts of a Washington State Payday Lending Report (continued)



Source: Washington State Department of Financial Institutions' website.

Appendix E

Audit Methodology

To gain an understanding of the Division of Financial Institutions (Division), we interviewed staff and reviewed statutes, regulations, and policies and procedures significant to its operations. We also reviewed financial information, prior audit reports, budgets, legislative committee minutes, and other information describing the Division's activities. Furthermore, we documented and assessed internal controls over the Division's regulatory oversight duties, which include conducting licensee examinations, monitoring consumer complaints, and reviewing licensee annual reports of operations.

To obtain a better understanding of the Division's examination process, we discussed with management the key areas throughout the process and the existence of written guidance covering these areas. We then obtained a listing of the 1,373 non-depository institutions licensed as of June 1, 2017. From this listing, we judgmentally selected 75 licensees to perform our audit testing. The 75 licensees included 50 check cashing and high-interest loan institutions and 5 from each of the other types of non-depository institutions listed on pages 2-3 of this report. A higher concentration of check cashing and high-interest loan institutions were selected due to the greater number of less-than-satisfactory examinations over the last 5 years. The licensees were then randomly selected within each license type.

To determine if the Division performed timely examinations of non-depository institutions in accordance with state law, we reviewed the most recent fiscal year 2017 examination and prior examination for each selected licensee. We calculated the length of time between examinations and determined whether it met the annual statutory requirements. For licensees receiving a less-than-satisfactory rating on their prior examination, we also determined the timeliness of the follow-up examination in

accordance with Division guidelines. Additionally, Division records were reviewed and analyzed for the number of days it took to complete examinations. The Division maintains a majority of its licensee records in a VERSA database system. To ensure the reliability of examination data obtained from VERSA, we traced key examination data to and from the licensee's Report of Examination (ROE) to verify the accuracy and completeness of the data provided to us.

To determine if loan and check cashing reviews performed during licensee examinations were adequate and adhered to Division guidelines, we reviewed and analyzed population and sample selection data for the selected licensees' fiscal year 2017 examination. We identified the four types of licensee loans (active, delinquent, closed, and declined) listed on the ROE and compared populations stated and sample sizes chosen to supporting documents included in the examination workpapers. For licensees providing check-cashing services, we also reviewed licensee check cashing logs included in the examination workpapers and compared population and sample selection data to corresponding information stated in the ROE.

To determine if examination violations were promptly acted upon by licensees in accordance with Division guidelines, we obtained the selected licensees' fiscal year 2017 ROE. We reviewed Division records to verify violations stated in the ROE received appropriate supervisory review and were submitted to the Division's Disciplinary Committee, if warranted. We also identified examinations with repeat violations and reviewed licensees' violation response letters. We verified response letters were received within the Division's 30-day requirement, and if not, appropriate follow-up was performed. We also surveyed 14 other states for best practices in assessing examination violations.

To determine if licensee examinations were billed timely and accurately, we used the selected licensees' fiscal year 2017 ROE and compared billable hours stated on the ROE to hours stated on examiners' time records and licensee invoice. We verified the total billable hours were consistent throughout the three sources, and that the hourly rate charged complied with state law. We also

verified the mathematical accuracy of invoices, and that licensees paid invoices timely or were assessed a late fee in accordance with state law. To ensure the reliability of billing data obtained from VERSA, we traced key billing data to and from licensee invoices and payments to verify the accuracy and completeness of the data provided to us.

To determine if licensees addressed consumer complaints in accordance with state regulations and Division guidelines, we identified complaints stated in the selected licensees' fiscal year 2017 ROE and compared to complaints tracked in VERSA and Division internal tracking spreadsheets. We calculated the licensee response time to each consumer complaint and determined whether it met the 10- or 20-day response requirement. If the licensee did not respond timely, we reviewed Division records to ensure adequate follow-up was performed. To ensure the reliability of electronically stored complaint data, we traced key complaint information to and from complaint letters physically stored at the Division.

To determine if annual reports were submitted in accordance with state law, we reviewed Division records to ensure all selected licensees submitted a fiscal year 2017 annual report. We compared submission dates to statutorily defined due dates (or approved extension dates) to identify late submissions. For licensees submitting late, we verified the appropriate amount of late fees were assessed and collected in accordance with state laws and regulations. To ensure the reliability of annual report data obtained from VERSA, we traced annual report dates and late fees to and from annual reports, invoices, and payments to verify the accuracy and completeness of the data provided to us.

To obtain a more in-depth understanding of a centralized tracking system for payday loans, we reviewed legislative committee minutes from the 2017 Legislative Session relating to a shared payday loan database. We discussed with Division management and a payday loan database vendor, other states with similar payday lending laws and benefits they have received from implementing a payday loan database. We also surveyed 14 states utilizing this type of database to further our understanding

of the benefits and uses a database provides the regulatory agency, licensees, and state officials.

For our sample design, we used nonstatistical audit sampling, which was the most appropriate method for concluding on our audit objective. Based on our professional judgment, review of authoritative sampling guidance, and careful consideration of underlying statistical concepts, we believe that nonstatistical sampling provides sufficient, appropriate audit evidence to support the conclusions in our report. Since our audit sampling included judgmental selection, we did not project our results to the population.

Our audit work was conducted from January to August 2017. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

In accordance with NRS 218G.230, we furnished a copy of our preliminary report to the Commissioner of the Division of Financial Institutions. On March 27, 2018, we met with agency officials to discuss the results of the audit and requested a written response to the preliminary report. That response is contained in Appendix F, which begins on page 34.

Contributors to this report included:

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Appendix F

Response From the Division of Financial Institutions

STATE OF NEVADA



BRIAN SANDOVAL
Governor

DEPARTMENT OF BUSINESS AND INDUSTRY
FINANCIAL INSTITUTIONS DIVISION

CJ MANTHE
Director
GEORGE E. BURNS
Commissioner

April 6, 2018

Rocky Cooper, CPA – Legislative Auditor
Legislative Counsel Bureau
401 S. Carson Street
Carson City, Nevada 89701-4747

Mr. Cooper:

As requested, the following is the Financial Institutions Division (FID) response to the recently completed Legislative Counsel Bureau (LCB) audit report. I want to extend our appreciation for the efforts of your staff in assisting the Division in identifying its operational strengths and weaknesses in order for us to capitalize on the strengths and correct the weaknesses. This audit provided valuable information regarding FID operations since the last LCB audit that was conducted before my appointment as Commissioner in 2007.

The Division appreciates that this audit confirms that since the 2007 audit, the Division has come a very long way. The FID has:

- Established a functional organizational structure with specialization in each of the major areas that the Division is the regulator;
- Researched, developed and implemented all required administrative internal control policies and procedures for its operations;
- Computerized licensing, examination, complaint and enforcement operations that can provide the information used in this detailed audit;
- And, subsequently, the Division has come from conducting less than half of the statutorily mandated number of non-depository examinations, to meeting 100% of required exams with implementation of a follow-up examination program that has resulted in the Division taking more enforcement actions, that have led to more court litigation (some of which

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CARSON CITY
Licensing Office
1830 College Parkway, Suite 100
Carson City, NV 89706
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have gone all the way to the Nevada Supreme Court), than were taken in the 25 years of the FID's existence prior to 2007.

The Division does all that it can with the statutory tools, legal representation, and resources that it is given. Improvements that can be made in the FID's operations as indicated in the LCB audit recommendations are, in part, commensurate with improvements to these factors.

The Financial Institutions Division accepts each of the recommendations made in the audit report as indicated by the attached "Division of Financial Institutions Response to Audit Recommendations" page. Our initial responses to the Key Findings of the audit report are as follows, including clarifications and proposed plans to address each:

- 1. The Division could improve its documentation of the work performed during an examination. Documentation generally lacked a statement showing the population and sample selection methodology for licensee loans and check cashing transactions reviewed. Additionally, examination periods varied and often did not cover the entire period since the licensee's last examination, as management indicated is a Division practice. (Page 9)***

The FID accepts this recommendation, noting that the FID conducts approximately 1430 examinations per year with limited resources. 17 non-depository examiner staff are conducting over 85 exams each per year, which equates to 1.6 exams per week. The examination volumes and limited examiner resources necessitates practical examination protocols, methodologies and review processes.

Examiners will document the total population every time the licensee can provide such information. Some licensees cannot provide the total loan population since the last examination for various reasons, such as manual records systems or unsophisticated computer systems, making it a burdensome task for a licensee to manually count its loan portfolio and provide the total loan population to FID. The licensees referenced in the audit report were unable to provide the total population size to FID. Therefore, the examiner did not have an accurate population size to include in the report of examination. As the examination sampling methodology is not population size driven, total loan population is not essential to conducting the exam.

Examiners review an entire licensee loan listing and randomly select a minimum of five of each loan type necessary to conduct the examination (active, delinquent, paid and declined) as the sampling methodology. The sampling may increase if determined necessary by the examiner, team leads and/or supervisory examiner.

FID will improve its review processes to ensure examination reports consistently include a statement of the examination periods. The scope of an examination extends from examination-to-examination; however, not all loan types in the sampling can extend back to the last examination. For example, deferred deposit loans are short-term loans, typically underwritten for a term of 7, 14, 21, 30 or 35 days. Therefore, these short-term loans will no longer be part of the active loan listing and cannot be sampled as an active loan from the examination-to-examination period.

- 2. Examination reports did not always accurately reflect the scope of work performed. Our testing found instances where the standard language in the Division's report template was not revised to reflect the actual work performed. In addition, 19% of the examination reports reviewed, which stated the loan population and sample size, were inaccurate and did not agree with the reviewed loans documented in the examination workpapers. (Page 11)**

The FID agrees there is room for improvement in examination review processes. The audit report stated there were ten samples with a finding that the report of examination did not accurately reflect the examiner's scope of work. Two of the samples referenced were a multi-location licensee, at the time of the examination 30 locations were examined. The examiner mis-stated on 2 of the 30 report of examinations that check cashing activity was reviewed when it was not; those two locations did not provide check cashing services. The other eight instances were mis-labeled workpapers or workpapers attached to a different location for the same licensee.

These findings were due to a lack of time and attention to detail by the examiner, and the lead examiner, or supervisor during the review process. FID will seek to allocate additional time to the review processes to enhance the function and reduce errors in the examination process. This may necessitate an increase in staff level to permit more time dedication to the examination review processes.

- 3. The Division needs to enhance its written policies and procedures over its examination process. Clearly defined policies and procedures provide a framework for conducting consistent and efficient work, while communicating approved processes and expectations to examination staff. (Page 11)**

The FID accepts this recommendation. FID will enhance current policies and procedures to provide additional guidance to FID staff regarding the examination process.

- 4. The Division needs to formalize in policies and procedures the follow-up process for licensees receiving a less-than-satisfactory examination. The Division considers licensees' violation response letters and other factors when deciding whether its staff will conduct a follow-up examination to verify corrective actions were properly implemented. Considering approximately 33% of licensed payday lenders received a less-than-satisfactory examination rating annually over the last 5 years, performing adequate follow-up on licensees with noted violations of state laws and regulations is important for ensuring consumers are adequately protected against unfair or unlawful financial practices. Furthermore, documenting this process is important because licensees receiving less-than-satisfactory examinations should receive close regulatory supervision due to their increased risk of non-compliance. (Page 13)**

The FID accepts this recommendation. The Division's follow-up examination program is an enhancement to the statutorily required examinations implemented by the Division. Current policies and procedures will be enhanced to provide additional guidance to FID staff making follow-up examination decisions. Follow up exam determinations are made based on the nature, volume and severity of violations. If correction of technical or minor violations can be confidently verified by documentary evidence submitted with the licensee's 30-day exam response letter,

the FID does not expend limited resources to conduct a follow-up examination that is time consuming for both the Division and the licensee.

All licensees' locations are examined together; therefore, to accurately reflect the number of licensees that were found not to have a follow-up examination, it is important to note the following:

The audit report states "...a follow-up examination was conducted for 2 of the 13 licensees in 2017. For eight instances, management indicated it relied upon various factors including licensees' corrective action responses to verify corrective actions were taken. For the last three licensees, the Division indicated pending litigation prevented them from conducting a follow-up examination." Six of the eight instances that relied upon licensees' corrective action responses were the same licensee with multiple locations, and FID did not merely rely on a written response but received documented proof the licensee rectified the violations. If a licensee has shown proof they rectified examination violation(s) with the 30-day response letter, the FID does not expend limited resources to conduct a follow-up examination. Additionally, the three licensees pending litigation are the same licensee with multiple locations.

The audit report stated 2 of the 13 licensees that received a less-than-satisfactory examination rating had a follow-up examination conducted. However, based upon the aforementioned information, 6 licensees received a less-than-satisfactory examination rating. FID conducted a follow-up on 2 of those 6 licensees.

5. The Division can improve its performance measures by reporting an outcome-based measure detailing the results of examinations to the Legislature. Over the last 5 years, an average only 67% of licensees providing loan and check cashing services were in satisfactory compliance with state laws and regulations based on the Division's examinations. Current performance measures provide examination output and workload statistics, but do not show the impact examinations are having on licensees' overall compliance with state laws and regulations. (Page 15)

The Division accepts this recommendation and agrees that non-depository examination rating statistical information currently maintained by the Division can be useful to other governmental decision makers. The Division notes that examination rating statistical data is more a measure of the performance of each non-depository industry, than it is a performance measure of the Division. The FID evaluates industry licensee performance, it cannot guarantee the performance of a licensee or an industry. The vast majority of non-depository licensees want to be in compliance, and rectify any violations identified by examination in a timely manner. It is less than 10% of an industry, usually large licensees with numerous licensed branch locations, which are responsible for most of the less-than-satisfactory examination statistics. It is these industry licensees that generate the majority of formal enforcement actions and litigation by the Division.

A centralized tracking system for payday loans can be of significant value to the Division, its licensees, and Legislators. A database would assist licensees with managing loans and determining loan eligibility. It would also help licensees comply with state payday lending laws and help consumers avoid becoming overloaded with debt. Additionally, it would help the Division identify irregular lender activity and serve as an information system for staff preparing for an examination. A centralized

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tracking system would provide regulatory oversight and collect statistical information on licensees providing loan services. (Page 17)

As previously mentioned, the FID does all that it can with the statutory tools, legal support and resources it is given. The automation that a legislatively approved centralized tracking and compliance system could bring to the regulation of NRS 604A industries would be a significant addition to the Division's tools and enhancement to FID resources.

The Financial Institutions Division is confident that the foregoing responses will adequately address the matters stated in the audit report. If there should be any further questions or additional information required in this regard, please do not hesitate to contact me.

Sincerely,



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cc: C.J. Manthe, Director, Department of Business and Industry

Division of Financial Institutions' Response to Audit Recommendations

<u>Recommendations</u>	<u>Accepted</u>	<u>Rejected</u>
1. Establish controls to ensure examinations are performed consistently within established sample selection guidelines, and licensee loan and check cashing reviews are adequately documented, including the population, time period reviewed, and verification of loan listings.....	<u> X </u>	<u> </u>
2. Enhance supervisory oversight to ensure examination workpapers and reports adequately and accurately reflect the work performed	<u> X </u>	<u> </u>
3. Update licensee examination procedures to be inclusive of key aspects of the examination process	<u> X </u>	<u> </u>
4. Develop policies and procedures to formalize the process and time period for follow-up examinations.....	<u> X </u>	<u> </u>
5. Report to the Legislature an outcome-based performance measure for monitoring non-depository licensee examination results	<u> X </u>	<u> </u>
TOTALS	<u> 5 </u>	<u> </u>