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Banking, Commerce and Insurance Committee  
February 26, 2007

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[LB113 LB174 LB368]

The Committee on Banking, Commerce and Insurance met at 1:30 p.m. on Monday, February 26, 2007, in Room 1507 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on LB368, LB174, and LB113. Senators present: Rich Pahls, Chairperson; Chris Langemeier, Vice Chairperson; Tom Carlson; Mark Christensen; Tim Gay; Tom Hansen; Dave Pankonin, and Pete Pirsch. Senators absent: None.

SENATOR PAHLS: Good afternoon. I think we will get started right now. I want to welcome you to the Banking, Commerce and Insurance Committee hearing. My name is Rich Pahls. I am from Omaha and I represent District 31. We will take up the bills in the order that is posted, that would be LB368, LB174, and LB113. To better facilitate today's proceedings I ask you to abide by some of the following procedures and you can see some of them I have on the chart over here. We are asking you to turn off your cell phones and we do have an on-deck chair that the senator is already sitting in, he is ready to go. We have a testifier's box up front, we ask you to fill that out and put it there. Following the introduction of the bill we will hear testimony from the proponents, opponents, and neutral testifiers and I will ask to see a show of hands just to give us an idea of how many people are speaking to the particular bill. As usual, we will try to give equal time to both sides. The closing statement is reserved for the introducing senator. We are asking you to begin your testimony by spelling your first and last names, and if you have written information that you would like to give to us we need at least ten copies. If you do not have ten copies right now hold your hand up and I will have the pages go run those off right as we speak. I see everyone is prepared with their ten copies. Thank you. We appreciate that. The last thing I would like to have you take a look at is to be concise so we can have our meetings move right along. To my immediate right is Committee Council Bill Marienau. To my immediate left is Committee Clerk Jan Foster, and what we will do is we will start with the senators, Senator Pirsch, to introduce themselves.

SENATOR PIRSCH: Hi. I am Pete Pirsch from the 4th District in Omaha, home of Boys and Girls Town.

SENATOR PANKONIN: Dave Pankonin, District 2.

SENATOR GAY: Tim Gay, District 14.

SENATOR CHRISTENSEN: Mark Christensen, District 44, Imperial.

SENATOR HANSEN: Tom Hansen, District 42, Lincoln County, home of the first walking sprinkler (laughter).

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SENATOR PAHLS: I can always count on the Senator to add a little bit of levity to us. Thank you. Appreciate that. We have two pages. One of our pages is Kristine Kubik from Prague, Nebraska and Cora Micek from Hastings, Nebraska. I think we are ready to start with LB368. Senator, I see you are with us.

SENATOR ERDMAN: (Exhibits 1-3) Mr. Chairman, members of the banking committee, my name is Philip Erdman. I represent the 47th District. We didn't invent the walking sprinkler, but we have Chimney Rock and some other neat things so we will hang our hat on that, I guess. I have some letters and information that is being distributed to the committee. The one letter is from the Nebraska Cattlemen. They have asked that I distribute that to you in support of (LB)368. There is also an example of how LB368 may work under 4 basic ideas not specifically limited to agriculture and then there are some additional information regarding what other states have done. LB368 creates the Nebraska Limited Cooperative Association Act which is a new business model for Nebraska. The traditional cooperative business model limits participation to patron members only. Patrons are those who use the services of a cooperative by buying from or selling to the cooperative. State and federal law is applicable to traditional co-ops, limit return on investment and voting control in such a manner as so to restrict the ability of traditional cooperatives to seek investment capital to fund start-up costs, expansion or other activities that require equity capital. A limited cooperative association would combine the traditional cooperative elements of patron ownership, control and distribution of profits based on business done by the patron with the ability to raise investment capital. Investor members earn a return on their investment without participating in the enterprise as a patron. LB368 sets restrictions on allocating voting control and distributions of profits between patron participants and investor participants. Five states, Wyoming, Minnesota, Iowa, Wisconsin, and Tennessee, currently have similar acts. The National Council of Commissioners on Uniform State Laws is in the process of developing a similar uniform law to be presented to all states for enactment. LB368 is largely based on the current uniform law draft. The potential applications for a limited cooperative association include value-added agricultural products, as well as nonagricultural enterprises including but not limited to, information technology sharing, housing cooperatives, food retailing, distribution associations, and management systems. LB368 expressly provides, however, that a limited cooperative association may not be a bank or insurance company as defined by Nebraska statutes regulating those industries. There are a number of individuals here, Mr. Chairman, who wish to provide you some additional background information as how this legislation was drafted and the intent of what this would provide for Nebraskans. I would be happy to try to answer any of those questions, at this point, but recognize that there are others here as well that may be able to provide more in depth responses. [LB368]

SENATOR PAHLS: Question, Senator. I see you are hitting both areas, agriculture and nonagriculture enterprises. [LB368]

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SENATOR ERDMAN: That is correct. It is not designed to be limited to only agriculture. [LB368]

SENATOR PAHLS: Okay. Senator Pankonin. [LB368]

SENATOR PANKONIN: Thanks, Senator Pahls. Senator Erdman, thank you for bringing this bill. Just a question on the five states that have enacted similar legislation, do you know how long some of those have been in place? [LB368]

SENATOR ERDMAN: I do, Senator Pankonin. The handout that I have distributed to you states that I believe, Wyoming began in 2001. Other states followed suit in 2002 and as late as 2005. There are a number of examples in that packet as well, but it is... [LB368]

SENATOR PANKONIN: Of the track record? [LB368]

SENATOR ERDMAN: ...yeah. It is generally there. Some states, obviously, have adopted different variations of it. The more restrictive that it has become in those states the less attractive it is. For example, Iowa has some prohibitions in there that may have cause to it's lack of attractiveness. They have no applicants, at this time, or no actual business models running under this act. Minnesota, on the other hand, has 15 entities that have applied for and are currently operating under this act, and, again, those are within your packet that I have distributed to you. [LB368]

SENATOR PAHLS: Seeing no more questions, I think we are ready for the proponents. I just need a show if hands. How many proponents do we have speaking today? Guys, I can't count that far. Okay, we have a number of them. I am just curious, how many opponents? Okay. Thank you. I can count two hands, that far I can count. Thank you. [LB368]

ROBERT C. ANDERSEN: (Exhibit 4) Senator Pahls, members of the committee, my name is Robert C. Andersen, that is spelled R-o-b-e-r-t initial C Andersen, A-n-d-e-r-s-e-n. I serve as president of the Nebraska Cooperative Council. The council is a trade association representing approximately 90 percent of Nebraska farmer-owned grain and supply marketing cooperatives. Our association strongly supports LB368 which would create a limited cooperative associations as introduced by Senator Erdman. This bill was drafted by our legal counsel, Rocky Weber with the Crosby Guenzel law firm here in Lincoln. Today I will attempt to focus upon the policy aspect of the bill. Upon the conclusion of my testimony I will be followed by Attorney Weber who will focus upon the legal aspects to LB368. During the last couple of weeks I have attempted to visit with many of you to explain the background of this issue, the merits of same, and how this bill provides value to the state as a whole. In Nebraska most of the traditional cooperatives are undergoing a redeployment of cooperative assets. In each

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of the past three decades we have seen the number of local supply and marketing cooperatives decline by about 30-32 percent each decade. This has been brought about due to changes in rail rates for shipping of grain, government programs, and the changing nature of multinational companies that local cooperatives compete with. However, while the number of cooperatives in Nebraska has declined rather rapidly, cooperatives provide necessary service and products for ag producers in over 400 locations throughout the state. In 2001 the state of Wyoming passed legislation authorizing the establishment of new generation cooperatives. At that time it created a lot of questions in the Midwest, including the concern of our association. Those concerns largely revolved around protecting the statutory and regulatory structure that currently supports the traditional cooperative system, as we know it, in Nebraska. Unquestionably, the newly created model in Wyoming wasn't a cooperative in the sense that we have come to understand cooperatives. After studying this, I have come to the conclusion that this was really a limited liability corporation with a cooperative component. Subsequently, in 2003 Minnesota adopted their version of same, followed by Tennessee and Iowa both in 2005, and more recently Wisconsin in 2006. Coupled with the above individual state legislatures seeking and implementing these new generation cooperative laws, the National Conference of Commissioners on Uniform State Laws has undertaken the development of a uniform cooperative marketing act. It is the goal of NCCUSL to provide a uniform law so the states' new generation cooperative business models are materially the same, much like the Uniform Commercial Code or model Business Corporation Act nationwide. A report is scheduled to be released in late 2007. In November, 2005, the Nebraska Cooperative Council board of directors created a special task force to study the implication of any type of new generation cooperative legislation. In essence to study whether or not this should be pursued in Nebraska. Those individuals who served on the council's new generation cooperative task force are listed on Exhibit A before. You will note that this task force included cooperative managers, cooperative producer/directors, regional representatives, along with several nonvoting members, namely the Nebraska Farm Bureau, Nebraska Corn Growers Association, the University of Nebraska Institute of Ag and Natural Resources, and the research analyst for the Ag Committee. The task force met throughout the spring and summer of 2006 to gather information and to hear from both proponents and opponents from other states sharing their perspectives to the merits of same. The task force addressed many concepts and ideas in studying this issue. We didn't want to undertake this just because other states had done so. There had to be an economic value to the farmers and ranchers, and local cooperatives here in the state. In our first meeting we had both proponents and opponents from Washington, D.C., Wisconsin, and Iowa meet with us. I must admit we were quite apprehensive about this concept at our initial meeting, particularly as to whether the introduction of this concept would dilute the existing legal foundations for the traditional farmer-owned cooperatives. However, as we learned more about the concept, the concept became more intriguing and we ultimately became convinced that this structure would be beneficial to farmers and ranchers, to local cooperatives and for the economic

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development of the state of Nebraska as a whole. One of the primary reasons for the states moving forward with their own legislation is value-added ag and the need for start-up capital. Traditional cooperatives can only generate capital by one of two ways, either by patron member investment and/or by borrowing. Farmers have been investing money and committing their ag production to enterprises such as bean crushing plants, ethanol plants, flour processing facilities, and etcetera. In order to purchase or construct the physical assets necessary to participate in value-added agricultural, farmers realized that the largest hurdle they had to overcome was raising sufficient capital to adequately fund the enterprise. Initial value-added ventures typically followed the traditional cooperative model as proscribed by Capper-Volstead, the federal law that most states including Nebraska have followed regarding the limitations on ownership and return on investment. The limitation that exists for the traditional cooperative has in our current economy become an impediment to acquiring sufficient capital investment for a successful venture. Consequently, in an effort to create a business model that remained farmer-owned but allowed for nonfarmer investment the new generation cooperative model was developed. At this point I will discontinue to refer to these entities as new generation cooperatives and will refer to them as limited cooperative associations. This parallels the current referencing within the NCCUSL's draft and is contained within LB368. This legislation would do the following: (1) it would allow farmers to participate in a business model on a patronage basis with nonfarmer investors; (2) make value-added ventures more attractive to investment bankers and other sources of investment capital; (3) provide an avenue for local cooperatives to participate as a patron participant or an investor participant in value-added enterprises in the trade territory that will benefit all of the farmer owners of the local cooperative; (4) provide flexibility for the board of directors to make decisions to return investment to investors early keeping farmer owners for the long term; and (5) provide an economic development opportunities in a number of nonag areas. Consequently, the limited cooperative association model provides a means for a value-added venture to seek and obtain investment capital from any source, while at the same time having patronage participation by farmer members. As our task force concluded its study this past August, we asked the task force members the following three policy questions: (1) is value-added agriculture important to Nebraska; (2) would the envisioned legislation enhance value-added opportunities for the state as a whole; and (3) should the Nebraska cooperatives be in the lead in developing cooperative business models? To each of these three questions we concluded yes that value-added ag is important to state, that this type of legislation would enhance value-added opportunities statewide, and that the council should be in the lead in developing same. I have attached as Exhibit B supporting information titled LB368 Nebraska Limited Cooperative Association Act. I believe this is what Senator Erdman just passed out a few minutes ago that you have in your possession. As members of the Banking, Commerce, and Insurance Committee you are probably wondering what kind of entities have been created in those states that have created these state statutes. For your information I have attached as Exhibit C the data as authored by officials within the USDA Rural Development

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Cooperative Programs listing those new business formations organized through 2005 in Wyoming, Tennessee, Minnesota, and Iowa. It does not contain the state of Wisconsin. This is somewhat dated but it gives you an idea of how it has been used. You will note that these new businesses include ag and nonag. I found this interesting in that it included such areas as technology, media, natural food store, an ag labor cooperative, health solutions, and renewable energy in addition to agriculture. In the course of preparing to have this legislation introduced we have been aware that some groups have taken policy positions critical of the limited cooperative associations based upon what really are, and I consider side issues not germane to the creation of a new business model. First, it has been suggested that cooperatives don't pay taxes and that they have some purported tax advantages. Nothing could be further from the truth. Due to the nature of the issue I have provided you with some data as Exhibit D which provides you with the information concerned with the federal and state income taxes paid, property taxes paid, and the cash revovement made by 35 responding local farmer-owned cooperatives. There are more out there but these are the 35 that responded. Last year the property taxes paid by those 35 cooperatives was over \$7 million. The state income taxes paid last year was about \$1.8 million. The federal income taxes paid was about \$10.5 million and the cash refunds paid back to the patrons last year was \$23.5 million. When I refer to cash refunds I am specifically addressing those cash returns to the members in the form of cash patronage, redemption of deferred equity in cash, and the cash equity redemption of estates. In essence, cash that was put directly back into the local economy. Again, that was about \$23.5 million. While at the same time providing the services, the inputs, the marketing of commodities for those farmer members out there. Also, I would call to your attention that due to the Farmland Industries bankruptcy, a regional cooperative, it has been estimated that Nebraska local cooperatives had to write off over \$40 million. While this has not affected this years income taxes it did effect the income taxes of some of these cooperatives two years ago and three years ago. In fact, some are still carrying that forward. Secondly, it has been suggested that this is being promoted by CoBank, a regional cooperative which loans monies to local cooperatives, and the Farm Credit Services, a regional cooperative that lends monies to producers. First, neither has pushed the Nebraska Cooperative Council to seek this legislation. I want to say that again. Neither has pushed the Nebraska Cooperative to pursue this legislation. In conferring with my counterparts in Wisconsin, Iowa, and Minnesota they too have shared that this was driven locally and not by CoBank or the Farm Credit Services. I have attached a copy of the February 26 communication from Douglas R. Stark, president of the Farm Credit Services of America, and Robert B. Engel, president of CoBank acknowledging that they have not taken a position on this bill as Exhibit E. It has been suggested that LB368 should be amended to include a more restrictive eligibility provision, a state restriction of sorts on a limited cooperative association borrowing monies from the Farm Credit system. This is unwarranted. The legality of such a restriction would raise serious and substantial questions of federal preemption of law. None of the other five states have done this nor does the current NCCUSL model

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contain such a restriction. To do so would discourage value-added ag projects involving existing cooperatives and their members from using the limited cooperative association model and thus restrict the value of the business model in Nebraska. I would call to your attention that the Farm Credit Administration on March 10, 2005 sent a communication to the Iowa Senate concerning that particular movement that was taking place there. I have been advised that another letter may be forthcoming to the committee here in the next few days although I don't know that will materialize, but it has been implied to me that it will be forthcoming. I have attempted to focus upon the policy aspects. I realize that the committee has legal questions such as what does a limited cooperative association provide over a limited liability company? How does this interface with Initiative 300? If LB368 is implemented would local cooperatives seek to liquidate and become a LCA? How does this interface with the Capper-Volstead Act? I would encourage you to submit those questions to our legal counsel, Rocky Weber, who will immediately follow my testimony and focus upon the legal aspects of a limited cooperative association. In closing, the National Conference of Commissioners on Uniform State Laws is addressing this issue and plans to submit their proposal later this year. Committee members, we could have waited until that report was released, but we felt it was important enough to move forward on this to create another tool for value-added ag and economic development in the statewide, at this time. Technically local cooperatives and other producers could create an entity under one of the other states similar acts and register as a foreign business entity in Nebraska, and conduct business in Nebraska and not be considered a Nebraska company. The cooperative industry in Nebraska is an integral part of the economic structure of the state. Advancing the ability of a person to conduct business in a cooperative manner while having access to outside investment is important in Nebraska. We in the cooperative community believe that Nebraska should be a leader and provide new opportunities under this new business model. In closing, we encourage your advancement of LB368. Senator Pahls and committee members, if you have any questions I would be more than happy to respond to them at this time. [LB368]

SENATOR PAHLS: Seeing none, thank you, Robert, for you testimony. [LB368]

ROBERT C. ANDERSEN: Okay. Thank you. [LB368]

SENATOR PAHLS: Yes. [LB368]

ROCKY WEBER: (Exhibit 5) Senator Pahls, members of the committee, my name is Rocky Weber, R-o-c-k-y W-e-b-e-r. I am a lawyer with Crosby Guenzel LLP here in Lincoln and I am a registered lobbyist on behalf of the Nebraska Cooperative Council. I am here today to address the legal and historical foundations underlying the proposal found in LB368, the Nebraska Limited Cooperative Association Act. Before I start that, however, everybody said where they are from and one of your pages was from Creighton, Nebraska. I grew up on a farm seven miles east of Creighton, Nebraska. I

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know Knox County very well and so you are amongst good company here. This act arises out of the need that was discovered in the late 1990s as value-added agriculture started taking off in southern Minnesota and through the Dakotas. The need to allow participation and cooperative business entities by those other than the farmer members of the cooperatives. The farm cooperative structure has been around for over 100 years. In the late 1800s it got its start in Europe and then came to the United States. Over a period of time different laws were associated with the development of cooperatives, but in 1920 Congress passed what is known as the Capper-Volstead Act. By that act Congress said that farmer-owned cooperatives could enjoy limited antitrust immunity if they limited themselves in three ways. Number one, they could be only farmer-owned. Number two, they had to subordinate capital. That meant that they could only pay 8 percent of dividend on return on capital stock. And thirdly, they could not do more of a volume of business with nonmembers than with members. Over the ensuing 80 years almost every state in the nation that has adopted any type of cooperative acts have incorporated all or parts of the Capper-Volstead restrictions into their state laws. In Nebraska one of those restrictions in our current cooperative law is that a cooperative entity may not pay more than an 8 percent dividend to those owners of capital stock, and the owners of capital stock have to be cooperative members. Because of these restrictions it has been very difficult for farmer-owned cooperatives, especially if they want to do a value-added startup project, to access venture capital or any risk capital to get the project off the ground. In the late 1990s the early ethanol plants, and biodiesel plants, and those types of projects in Minnesota and the South Dakotas were typically formed as cooperatives. Once they realized the capital limitations of these entities most of those early entities, very early on, converted to the LLC status so that they had more access to capital and investment capital. In Wyoming in 2001 the Wyoming legislature first passed what we now know as the New Generation Cooperative Act and it was a marketing association bill that for the first time said we are going to marry two principles. We are going to marry the principle of outside investment with the principle of patron participation in a cooperative. Patron participation in a cooperative is that I earn income or earnings from doing business with the cooperative based upon the amount of business I do with the cooperative on an annual basis compared to everyone else. I may earn equity in my local cooperative but I don't earn any return on that equity. Any return I get on an annual basis is returned based upon the amount of business I do. That is the classic subordination of capital principle proposed and promulgated under Capper-Volstead. For the first time in Wyoming and then followed by the states of Tennessee, Minnesota, Iowa and Wisconsin we now have entities available to us where we can bring an outside investment, where there truly is an opportunity for a return on investment for investors, to participate in an economic business model with patrons of a cooperative. And so for the first time consumers and sellers of commodities, and other goods and services can participate without capital intensive requirements on their behalf, find capital to form a business, and move forward in a new type of partnership with more possibility of success because the venture capital is available. I have before you handed out today a summary of the legal and historical framework for limited

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cooperative associations as this bill now references them. Let me just go through some of the salient points of what we have put into this act and this act, again, is modeled largely on the uniform law being considered by the National Council of Uniform Law Commissioners. Much of that law is in turn modeled after the Minnesota act. But in Nebraska under LB368 what we have proposed is that there be two types of participants in these organizations. One would be a patron participant and one would be an investor participant. Unless changed by the articles of organization, patron participants in an LLC would have to have 51 percent of the voting control. By agreement amongst the participants in the company, however, which would be set forth in the articles of organization. That voting control could be reduced to 15 percent on the patron side. Why? Well many times control follows investment. People who invest in companies want to have some ability to control the company to protect their investment. Obviously it would not be much of a tool to entice investors to invest in your company if you could give them no equal control commensurate with their investment. Secondly, 50 percent of the board of directors of the limited cooperative association would have to be elected by the patron participants. Third, with regard to the distributions of income or allocations from the company 50 percent would be required, as a matter of law, to go to the patrons unless, again, by agreement. They agree with the investor patrons that up to 85 percent of the distributions can go to the investor patrons. What this contemplates and what it would allow for is initial investment to be made by venture capitalist to be paid out over the initial period of time that the company is in existence to eventually remove the investors and let the sellers of the goods and services who are part of the company then own and control the company. I have set forth in my correspondence to you today, a comparison of the salient facts regarding LB368 with our Wyoming, Tennessee, Wisconsin, Iowa, and Minnesota laws as well as the current uniform draft that is pending. You have heard me talk today about Capper-Volstead authorization for the traditional cooperatives. Nothing in LB368 is intended to change at all the existing statutory and legal framework for the existing cooperatives in Nebraska. In fact under the new LB368 framework limited cooperative associations would not have Capper-Volstead protection. They would not enjoy the limited antitrust immunity enjoyed by the traditional farmer-owned cooperatives in Nebraska. With regard to taxation, today patronage allocations, and distribution of income to members of cooperatives in the traditional sense, are governed by subchapter T of the Internal Revenue Code. Similar entities formed in other states have asked for letter rulings from the IRS and the IRS has granted letter rulings saying the patron participants of entities like a limited cooperative association may be able to take their income under subchapter T as a patronage allocation and the investor members may be able to take their income as a partner, or member of an LLC would take their income under subchapter K of the Internal Revenue Code. Finally, limited cooperative associations would not qualify as exempt cooperatives under section 521 of the Internal Revenue Code. An exempt cooperative is not a cooperative exempt from taxation. An exempt cooperative is a cooperative that may take nonpatron sourced earnings and allocate the revenues from those earnings to their patrons rather than having to say those patrons can retain

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savings and pay tax at the corporate level. Everything that is allocated to the patrons, however, are indeed taxable to the patrons. The reason the (section) 521 exemption is important is under the Securities Act of 1933 there is a safe harbor from registration for section 521 cooperatives. They do not need to do a federal securities filing to issue securities. Again, limited cooperative associations would not enjoy that benefit of that safe harbor. So while we lose the advantages of traditional cooperatives with the limited cooperative association the exchange is access to investment capital. That is critical for economic development. It is critical for value-added agriculture and there are a number of nonagricultural applications the limited cooperative associations can be used for. I believe in the materials that you have been handed already, we have illustrated at least four examples of how a limited cooperative association can be used in both an agricultural and nonagricultural settings for economic development purposes. That generally provides you with the historical and legal background. Nothing in this legislation is intended to change what the uniform law commissioners are doing. The reason we patterned this after the draft of the uniform law is so that when that comes to Nebraska the amount of rectifying any differences between the two acts would be simple and could easily be accomplished. If you have any questions I would be happy to answer the same. [LB368]

SENATOR PAHLS: Senator Hansen. [LB368]

SENATOR HANSEN: Thank you. Rocky, it is good to see you here today. I have a couple of questions. What is a patron? I know it is defined in there. Just get your... [LB368]

ROCKY WEBER: Sure. A patron is a person who does... [LB368]

SENATOR HANSEN: I am sorry. Not a patron, a participant. [LB368]

ROCKY WEBER: A participant with a limited cooperative association...there are two different kinds of participants. One is the patron participant who actually does business with the limited cooperative association. Let's take an ethanol plant for example. If I am a farmer patron participant of the ethanol plant I will likely have a contract to deliver my grain to the ethanol plant and then based upon those deliveries I will earn a return on how much business I do with the ethanol plant in that year. The other type of participant is the investor participant. This is somebody that may not be related to agriculture at all, or may be from a rural community that wants to certainly support economic development in the community, and they simply have an investment interest in the company and earn only a return on investment. So those are the two types of participants. [LB368]

SENATOR HANSEN: But they are both called participants, right? [LB368]

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ROCKY WEBER: They are both called participants. [LB368]

SENATOR HANSEN: Okay. In section 4 of the bill, and I don't know if you want to look at it or not, but it is what you referred to as the section that says the LCAs don't want to be a bank, and you have to read that in there "except for the purpose of being a financial institution". Is that correct? [LB368]

ROCKY WEBER: Right. [LB368]

SENATOR HANSEN: Is that correct? [LB368]

ROCKY WEBER: That is correct. [LB368]

SENATOR HANSEN: And then we turn over to page 11 section 11 and this is the part that I don't understand for sure. It says "a participant," could be either kind of participant, "may lend money to and transacts other business with the LCA and have the same rights and obligations respect to the loan or other transaction." Now that sounds like a participant could be, the investor type of participant could be, anybody and could loan money to the LCA. Is that correct? [LB368]

ROCKY WEBER: Well no. I would say that a participant has to be a member of the limited cooperative association. They would have to be identified and have either a business relationship as a supplier or a purchaser with the company, and actually own a membership in the company or be an investor and own a membership. So section 11 would not allow any outside person, the limited cooperative association, to lend money or borrow money from any outside person in terms of those types of relationships. I mean lend money, not borrow. Whereas the earlier section saying that these entities may not be banks and for any purpose regulated by the Department of Banking and Finance means exactly that. That they cannot be banks or insurance companies. They cannot with the general public, other than with their members, do business like a bank would do business, loan money, take security, those kinds of things. Only with their member participants would they be able to do that. [LB368]

SENATOR HANSEN: But a bank couldn't be a participant then? [LB368]

ROCKY WEBER: Well a bank certainly could be a participant. Certainly. [LB368]

SENATOR HANSEN: Okay. And then if we flip over to page 35 where we are talking about, and this is something Mr. Andersen said, it starts on line 11 in section 49, it says specifically agricultural product or specified commodity. So are we talking about apartments or are we talking about ag products and specified commodities? Quantities to me mean agriculture products. [LB368]

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ROCKY WEBER: There are other commodities. I mean you could have some sort of a manufacturing entity that would manufacture widgets and those widgets are the commodity which that company is doing business in. I think that is what the intent of that definition is. [LB368]

SENATOR HANSEN: Okay. That is all I have for now. [LB368]

SENATOR PAHLS: Senator Pankonin. [LB368]

SENATOR PANKONIN: Thanks, Senator Pahls. Mr. Weber, I have got two questions. Going back to the taxation, so these would be taxed like an LLC? Explain to me a little bit how the taxation works on this versus the standard. [LB368]

ROCKY WEBER: The taxation for the patron participants would be just the same as cooperative patrons are taxed today on their allocations from their cooperative. What happens is once a cooperative has profits to allocate, and they call it savings, once a cooperative has savings to allocate, it allocates that savings to its members in the forms of patronage allocations or dividends and those allocations, then, are taxed at the patron level, at that individual's tax rate. [LB368]

SENATOR PANKONIN: Okay. [LB368]

ROCKY WEBER: There is a deduction at the corporate level and then the tax is paid at the patron level. On the investor side because there is no patronage aspect there, there is no doing business with the limited cooperative association, they are merely getting a return on their investment. That is then handled like a partnership or limited liability company interest where you get a K-1 return showing your share of those profits that you received from the limited cooperative association. The profits would be split according to the agreement of all the participants as set forth in the articles of organization and bylaws and then subchapter T would handle the patron side, subchapter K would handle the investor side of the taxation. [LB368]

SENATOR PANKONIN: The entity itself would not be taxed then? [LB368]

ROCKY WEBER: It would be like a cooperative that if the entity retains money for working capital purposes, there certainly would be tax paid on that and that is part of subchapter T. As Mr. Andersen said cooperatives certainly do pay taxes. Well what do they pay taxes on? If they can allocate moneys out to their members and their members pay the taxes, what do they pay taxes on? Whatever they retain for working capital purposes they pay tax on that money. So if a limited cooperative association retained earnings, whatever earnings are retained, certainly there would be both state and federal taxes paid on that amount. [LB368]

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SENATOR PANKONIN: Okay. My second question is, it has been discussed that the state of Iowa's plan has not had successful applications, where Minnesota has had 15, Wyoming not quite as many. What do you see from a standpoint of difference between Iowa's and this law? They said it was more restrictive, but why hasn't it been more popular in Iowa in your opinion? [LB368]

ROCKY WEBER: The Iowa legislation, if you look at the powers and purposes of the legislation, there are a lot of small hurdles that must be jumped through in order for these companies to do business. One, is having to disclose to potential participants who are not accredited investors that these investments may be at risk and those kinds of things. Another, would be a limitation on extending credit to your members for a limited period of six months and not being able to take real estate as a security. Those are two types of restrictions, I recall just off hand, that exist in the Iowa act. Other than that I don't know exactly what has gone on that there has been no use of that act there. [LB368]

SENATOR PANKONIN: Okay. [LB368]

SENATOR PAHLS: Senator Pirsch. [LB368]

SENATOR PIRSCH: Well I was invited to inquire as to a couple of things here. How this would interface with Initiative 300, and whether or not local cooperatives would seek to liquidate and become an LCA? So if you could just comment briefly as to those two. [LB368]

ROCKY WEBER: Certainly. With regard to Initiative 300, which is the ban on corporate farming that has existed in Nebraska for the last 26 years, I believe, assuming that Nebraska moves forward with a similar ban on corporate farming a limited cooperative association would be restricted from owning and operating the means of agriculture, either the livestock or farmland, and being involved in production agriculture. Just like any other corporation or limited liability company not involving family members would be limited today. So it does not change anything with regard to corporate restrictions on farming. It would be likewise subject to those things. With regard to converting, and whether or not today's locally-owned farmer-owned cooperatives would be interested in converting to these entities and bringing in outside investors. From a practical standpoint I would guess that there would be no instance that in which that would occur. Under Internal Revenue Code section 361 the revenue service would determine that to be a liquidating distribution to convert from a traditional cooperative to a limited cooperative association would be a liquidating distribution. Each one of those entities would have to take all their depreciated assets, bring them to book value, and recognize all the capital gain on that transaction, and all the members of those cooperatives would have to take the basis of the equity they have earned in those cooperatives, and bring that to a market value and recognize the capital gain on that transaction, and those

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capital gains taxes would be extraordinarily prohibitive in terms of making that transfer from one type of entity to another. [LB368]

SENATOR PAHLS: Senator Carlson. [LB368]

SENATOR CARLSON: Senator Pahls. Mr. Weber, this being the first session that I have experienced in the Legislature I have come to realize that once you are done with your testimony, you are done and there will be others to speak after you and there may be some opposition. Would you comment on opposition to LCA and kind of your interpretation of that? [LB368]

ROCKY WEBER: Sure. From what I understand there is going to be some opposition today and one of those parties appearing in opposition to this bill would be the Nebraska Bankers Association. Right before lunch today, Bob Hallstrom did email to my office and to Bob Andersen's office proposed amendments to LB368 that they have asked us to consider. These are similar to propositions which they have made to us, right before the end of the year they proffered some of those ideas to us. Those amendments, basically, cover three distinct areas and I am going to go in reverse order than what you see them because a couple of these aren't significant anyway with regard to any type of conflict with what we believe. One is the disclosure, the need to disclose to nonaccredited investors the nature of the investments in these entities and to make sure that a written disclosure is made. As a matter of whether or not we object to that amendment generally we don't. These entities are going to have to do private placement memorandums or register with the Department of Banking and Finance at least with a notice filing the fact that they are selling securities and within those disclosures are the same or similar types of disclosures anyway. So that is not objectionable in terms of that amendment with regard to disclosing to nonaccredited members. The second proposal that they have made is that these entities not be able to extend credit to their own members for periods exceeding six months, and that there be no ability to secure the extension of credit with security interest in real estate. The amendment this morning did say that extension could be for an additional six months after the original six months. Then in the second six month period you could secure that with real estate. Particularly with regard to value-added agricultural type projects a six month window is very difficult in terms of extension of credit. From the time credit might be advanced for the purchase of seed and other necessary products, I am going to use just like canola seed is one of the things that is being bandied about, especially in the Panhandle. Many ranchers and farmers have tried canola seed to see if it is a viable crop for biodiesel. Say, for instance, you had this company that put together to raise canola seed for biodiesel. The company may want to finance the purchase of the seed, any unique inputs that need to go on, and all the raising of this canola for the purposes of securing enough of a seed for the production purposes. Whether or not a 6 month or even 9 or 12 month is sufficient is going to be very difficult to tell depending upon the production cycle of whatever commodity it is you are doing. And when we are putting

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together a model business act, I am reluctant to say it is okay to restrict a model business corporation when we don't know what all the proposed applications for it might be. Now is it such that if we could extend credit for a longer period of time, maybe up to a year or so, and be able to secure it through real estate, would that be objectionable to us? Probably not. We could probably work with something like that. But to simply restrict something to six months and then have to go through a renewal cycle, not be able to secure real estate for the first six months, but then try to do it within the second six months seems to be a little burdensome. The primary amendment that they are seeking, however, from what I understand, is that they want to limit the ability of a limited cooperative association to borrow money from a bank for cooperatives or from an agricultural credit bank if the patron participant voting control is less than 80 percent. They do not restrict that to farmer participant voting control less than 80 percent, and the federal regulations that control who Farm Credit Bank or CoBank can loan money to are very clear about the numbers of individuals involved as far as farmers are concerned before they are eligible for that financing. For CoBank at least 80 percent of the members of the cooperative must be farmer members before it can even loan money. So for all the nonagricultural applications of the Limited Cooperative Association Act that wouldn't be relevant in any event, and for value-added agricultural purposes making sure that 80 percent are patron participants, and not allowing for greater percentage than 20 percent of investor participants can certainly reduce the number of value-added projects that could find value in using the limited cooperative association as a business model, and really reduce the economic benefit of this model in agriculture by a significant degree. I also think, just as a matter of law, that the federal regulations clearly set forth who Farm Credit Association and CoBank can lend money to. It is a matter of federal law. A state law interfering in that process could be subject to a challenge on federal preemption purposes. And, again, from an economic business model analysis, what is a good business model for Nebraska, you want a model that is going to have broad application and can be used in agriculture and nonagriculture both. [LB368]

SENATOR PAHLS: Senator Gay. [LB368]

SENATOR GAY: Rocky, I have got a question I guess to get my head around this thing. You had an example, a little illustration to a rural grocery project, and I guess the question that comes to my mind is we have a small town grocery store that investors, patrons, participants could buy into that store. [LB368]

ROCKY WEBER: Right. [LB368]

SENATOR GAY: What I hear in my mind it says what if there are two stores in town and the board decides to go with this one store and then now all of those patrons are going to go? Wouldn't you just run the other guy out of business? Is that fair? Is that keeping competition? And I can see both sides of one store, but when this gets used in

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value-added ag I like the idea. It makes sense. But in some of these illustrations where you used the grocery store or here is one on renters, on maybe it's an apartment complex. Where are we getting into the competition and we are taking away small banks, and bankers, of course, are going to oppose this a little bit. But aren't we taking away some of that competition on nonvalue-added ag? Is that fair? [LB368]

ROCKY WEBER: If you are talking about competition among banks... [LB368]

SENATOR GAY: I am talking about that, but I am talking about if I own a store, or Dave owns a store, and Pete owns a store, and we all own them within a 15-20 mile radius and it is hard enough to survive, and now we choose Pete's and you are going to help him out. Isn't the rest kind of out of the loop here? Will this do more damage than good in rural communities like that? [LB368]

ROCKY WEBER: I guess I kind of view it as putting a tool in the tool box to maybe even level the playing field from the other direction. As a private business owner you can go get an outside investor, form a limited liability company or a corporation, an S corporation or something, and you can bring in outside investment to help capitalize your grocery store, to fund your grocery store or you can choose to go bank at whatever bank you want to go bank at and you have got those things available to you. Where a cooperative, where individuals who do business with the entity want to form together and do business together because there is a savings and a profit realized for them in doing business with that entity, when they are restricted on getting outside capital they don't have the same ability to do business and compete with the private entity that can go and get start-up capital. The reason I used the grocery store example is that that is a real life example. In Arnold, Nebraska several years ago they lost their grocery store, I believe, to a fire. There wasn't another grocery store in the community and they went through several efforts to try to raise enough local money to put a grocery store in, and had some bumps along the way in doing that and this model would have worked very well for that purpose because you would have had towns people, outside investors, and most of them would have probably been patron participants and investor participants as well, that would have been a very easy business model for them to have used. With regard to the housing cooperatives, the rent-to-own type things and everything of that nature, obviously from a banking standpoint, if to the extent they do any type of debt financing, they are going to be going to commercial banks. They are not going to be using the farm credit system for any debt financing in that respect in any event, and in terms of, again, competing with a developer who is going to develop an apartment complex, typically the developer is going to build an apartment complex, he is going to have investors, they are going to seek a return on investment, at some point they are going to sell it to a management company that then earns fees off of rents and management, and as the example I used having some ownership for the renters here and able to slide that scale from a little bit of ownership to a lot of ownership at the end, again, is just a different kind of economic tool. I don't think it provides an unfair

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competitive advantage. [LB368]

SENATOR GAY: Well a follow-up question, if I may. In the case I am using, let's say there are 800 or 1,000 members that are now owners of that, that is different than going to a bank or an individual and say having capital from somewhere else. I think they, we would be at a disadvantage because it would be very powerful to go frequent that. [LB368]

ROCKY WEBER: You are more likely to do business with a company you have an ownership interest in. Yeah. [LB368]

SENATOR GAY: Heck yeah, but I think a good value-added ag economy is great and it would help all of us that way. But that is just something I wanted to throw out there that was going through my mind. Thank you for your answer though. Thanks. [LB368]

SENATOR PAHLS: Seeing no more questions, thank you, Rocky. [LB368]

ROCKY WEBER: Thank you. [LB368]

SENATOR PAHLS: Before we have anymore testimony, Mr. Andersen has given us a very well defined testimony on policy and Mr. Weber has given us an awful lot of good information on the legal aspects. So I am asking for the proponents to give us new or additional information. [LB368]

STEVE ERDMAN: (Exhibit 6) Thank you. My name is Steve Erdman. I am from Bayard, Nebraska. That is Steve, S-t-e-v-e E-r-d-m-a-n and I hope to do just that, Senator Pahls, and I appreciate the opportunity to testify for you today. My goal here today is to share with you some information about two cooperatives that I serve on and one of them, Senator Gay, is a very large grocery store in the Panhandle of Nebraska. So I will begin with that information. As I said, I serve on two board of directors of local co-ops in the Panhandle. One of them is Panhandle Coop and the other one is Stateline Bean Coop. Panhandle Coop is a large established co-op that provides groceries, fertilizer, petroleum, seed, and chemicals, and over 7,000 members. We have over 300 employees in 10 different locations. Panhandle Coop, in the last three years, has returned to their member owners \$1,184,000 in cash dividends, redeemed equity to retired members and estate settlements. The other co-op is Stateline Bean Coop. This co-op was founded in May of 2002. Stateline is a bean marketing cooperative owned by 180 bean growers. Just some of the history about Stateline and why Stateline was formed. Several bean producers had asked the university research and extension center in Scottsbluff to analyze our bean industry and help us understand what efficiencies could be realized in growing and processing dry, edible beans. One thing that was brought to light, by this study, was the fact that the margin that the bean elevators paid for the beans and the price that they sold the beans for was more than

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\$10 per 100-weight. As we analyze this information it was realized that there were profits in processing and marketing beans that we were not a part of from the independent bean companies that were doing business in the Panhandle. Therefore we set out to purchase an elevator to process our beans and we turned to our owners the profits generated from the processing and marketing of these beans. Using the cooperative business model made the most sense to us because we had small and large producers in our group. It allowed both groups of producers to have ownership in a company to add value to their commodity, beans. We sold investments in the bean co-op at 100 100-weight units to our members. Each unit, 100-weight, sold for \$300 or \$3 a bag, \$3 a 100. We sold 3,380 units to raise \$1,014,000 in equity. Our goal was \$1.5 million. We fell short of our goal by nearly \$500,000. During our equity drive there were several business people in the Panhandle in North Platte valley who asked if they could invest in Stateline and the answer was no. If you are not a bean producer you couldn't invest in the company. Since we were nearly \$500,000 short in our equity drive it was very frustration not to be able to allow these people to participate as investor members. We were fortunate in that we received a USDA grant that helped us overcome our shortfall in the start-up costs. The rest of the funding came from debt financing which we had hoped to avoid. Eventually, even with a heavier debt load than what we had liked, we entered into a purchase agreement with KBC Bean Company for their facilities in Gering and Bridgeport, Nebraska. Stateline now is in it's sixth year of operation. It has accomplished greater results than had been projected and perhaps even thought possible for a new business. The co-op has returned in cash dividends to our 180 owners over \$1.4 million or \$78,000 per member, and we have grown their equity from \$1,014,000 to \$1.8 million over that same period of time. In other words the owners have received 125 percent of their original investment back in cash and their \$3 original investment is now worth \$5.33. Stateline has 17 full-time employees and has annual sales of \$12 million. The company last year paid \$57,000 in federal income tax, \$18,000 in state income tax, and in the last 3 years has paid \$45,000 in real estate and personal property taxes. The trend of business consolidation is happening not only in the ag sector it is also happening in banking as well. As banks consolidate more often than not they lose their relationship with agriculture and it's producers making projects like ours even harder to finance. The results for this start-up co-op is second only to the results achieved by some of the ethanol plants. It is safe to say that there will be opportunities to form co-ops like Stateline Bean to help economic development in rural Nebraska. Without the option of being able to take investments from nonproducers they may not be as fortunate as Stateline was to receive a grant and find a bank that will help finance them. Many times cooperatives are the only business small communities have left. The Limited Cooperative Association Act would allow others in the community, besides the producers, to invest their money to help the new venture get started. This business model would have been very helpful to us at Stateline. There were local business people and others who asked if they could make an investment to help us. Had this model been in place they could have invested. I believe that this legislation would be good not only for rural Nebraska but for all Nebraska, and I would ask you to

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advance LB368. Are there any questions? [LB368]

SENATOR PAHLS: Senator Gay. [LB368]

STEVE ERDMAN: Yes, sir. [LB368]

SENATOR GAY: Thank you, Mr. Erdman. This is a great example of value-added ag, I could see this example. You had mentioned when you came up about the store. Can you explain that a little bit? You heard my example. How did that work or short synopsis? [LB368]

STEVE ERDMAN: Panhandle Coop was formed about 65 years ago and they started as a creamery there in western Nebraska and they grew into a grocery store. We, as Rocky alluded to, because we have 7,000 members and the majority of those members are not producers, they are not farmers, we can't borrow money from CoBank. And so we own the grocery store in Scottsbluff. We have one in Torrington, Wyoming and last week on Wednesday we opened a new store in Wellington, Colorado. And so we have three grocery stores. Our annual sales on groceries will be about \$40 million. And so when you do business with Panhandle Coop as a grocery person you don't have to be a producer, but you receive a patronage if you are a member of Panhandle Coop. [LB368]

SENATOR GAY: So those members could have bought into the other one or is that a completely separate entity? [LB368]

STEVE ERDMAN: No, at our co-op. No, we don't have an investment for it. They could not have invested such as that, but we do have a program where they can invest in CI but they couldn't buy into it. Not under this scenario. [LB368]

SENATOR GAY: Okay. Thank you. [LB368]

SENATOR PAHLS: Senator Carlson. [LB368]

SENATOR CARLSON: Senator Pahls. Mr. Erdman, I applaud you for these projects that have taken place... [LB368]

STEVE ERDMAN: Thank you. [LB368]

SENATOR CARLSON: ...and I am all for economic development in rural Nebraska. I am asking you this and if the answer is no, that is okay. It is still a good project. But Stateline has got 17 full-time employees and I am always interested in economic development because we send people from outside of Nebraska to Nebraska so we multiply our taxpayers. Are any of those people come in from out of the state do you know? [LB368]

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STEVE ERDMAN: Senator, we had purchased that company from KBC and Klein Brothers Trading Company is what it was and we took those employees from them. And so we have replaced a few of those employees but we haven't brought anybody in from the outside. [LB368]

SENATOR PAHLS: Senator Pirsch. [LB368]

SENATOR PIRSCH: Just a quick question. Maybe I should have asked this question to the previous testifier. It is somewhat of a legal nature but if you know I would appreciate you answering, and that is technically could your cooperative right now if you had a need or would be leaning towards using this new piece of legislation, could you go out right now and utilize, create an entity under one of the other state similar acts and register as a foreign business entity and essentially conduct operations in much the same manner as you are proposing? Are you familiar with that? Could you comment on that? [LB368]

STEVE ERDMAN: Is your question could we have done that when we started? [LB368]

SENATOR PIRSCH: Well could any of these...the proposition is coming forward because the need exists is the claim and so I am wondering if there exists, right now, the ability to create a foreign entity under one of these other states, say Wyoming, similar acts and register as a foreign business entity in Nebraska and conduct business on that basis. [LB368]

STEVE ERDMAN: All right. I believe you have two questions there, if I understand right. Our company now that has formed Stateline could not make the switch over because it would be tax prohibitive. Okay. So we can't change. Can we start a new company using those other models? I believe we could. I believe we could use those others. I am not a lawyer. You would have to ask Rocky. [LB368]

SENATOR PIRSCH: Sure. [LB368]

STEVE ERDMAN: But I think that is an opportunity that we could do as a foreign entity, go to that state Minnesota, wherever and register there. Because there are a lot of Delaware cooperations formed and they don't live in Delaware. That is my opinion. [LB368]

SENATOR PIRSCH: Okay. Thank you very much. [LB368]

SENATOR PAHLS: Seeing no more questions, thank you, Mr. Erdman, for your testimony. [LB368]

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STEVE ERDMAN: Thank you. [LB368]

SENATOR PAHLS: We won't hold that against him. [LB368]

RANDY ROBESON: (Exhibit 7) Hi. I am Randy Robeson with Frontier Co-op out of Brainard, Nebraska. Chairman Pahls, members of the Banking, Commerce and Insurance Committee, my name is Randy Robeson, R-a-n-d-y R-o-b-e-s-o-n. I serve as the president and general manager of the Frontier Cooperative located in Brainard, Nebraska. Kind of known as the Bohemian Alps. We are a farmer-owned cooperative with 13 locations, serving 2,500 producers in the area located, basically, between Omaha and Columbus, covering 4,400 square miles. Our cooperative has sales of over \$200 million per year, and this past year we returned over \$1.4 million to our members from patronage refunds to equity redemption. Our cooperative is very involved in the grain industry and because of that we are currently thinking about value-added opportunities for our members. This past year I had the opportunity to serve on a statewide task force, made up of cooperatives and agricultural leaders, that was charged with studying proposed legislation concerning value-added cooperatives. We spent a great deal of time studying the issue, hearing from those in favor of such a legislation and from those who oppose such legislation. As we study the concepts that make up LB368 our task force unanimously agreed that LB368 is good public policy for Nebraska. By allowing investor members, cooperatives will have a greater chance of succeeding in a capital intense value-added business. As I mentioned earlier, we are very involved in the grain business. Because of that we have had numerous opportunities for investment, particularly in the biofuels. We all know what has occurred within the ethanol industry within the past few years. We have had numerous opportunities to become involved in some segment of the ethanol industry, but the limiting factor always come down to capital. If we would have the opportunity to bring in investor members there would have been more opportunities for us to add more value to the services we provide our members. We believe that LB368 will provide another tool for rural Nebraska to use in creating and sustaining value-added businesses, and certainly anything we can do to help with rural economic development is all in of our best interests. One of my major job functions as a general manager is to discover and develop opportunities that can strengthen our cooperative. By having the ability to include investor members in a cooperative we may be creating another method of adding value to our business operations, which ultimately benefits our members. I appreciate this opportunity to appear before you and if you have any questions, please ask. [LB368]

SENATOR PAHLS: Seeing no questions, thank you, Randy. [LB368]

RANDY ROBESON: Thank you. [LB368]

SENATOR PAHLS: We have been fortunate you all have been giving us some

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literature, if not I would like to have you spell your name just in case we do miss it.  
[LB368]

BRUCE FAVINGER: (Exhibit 8) Chairman Pahls, members of the committee, my name is Bruce Favinger, B-r-u-c-e F-a-v-i-n-g-e-r. I am a farmer from Minden which is located in south central Nebraska. I also serve as the board chair for Heartland Cooperative out of Hastings. Heartland Cooperative is made up of farmers from a twelve county area in south central Nebraska. Our cooperative has always maintained a strong commitment to our members and that is shown by the fact that in the past three years we have returned over \$2.5 million to our members in the form of patronage refunds and equity redemptions. Randy Robeson mentioned his service on a task force to study the issue during his testimony. I served as well on that same task force. I do not want to repeat his thoughts, but I would add another set of criteria that the task force used when considering the new legislation. Number one, any statute change must be beneficial to Nebraska farmers, and ranchers, and their co-ops. Number two, any change must not adversely impact current state statutes governing supply and marketing cooperatives. As an active farmer I can tell you that the cooperatives in Nebraska are providing value to producers both in the products and services that the cooperatives provide, but also in the fact that the producers own the businesses. This allows the producers to provide input through the elected board of directors for the management of the company. This means the decisions that effect our area are made by a local board of directors in rural Nebraska and not in corporate board room in another state or another country. You all know that the business world changes very rapidly and certainly that this is occurring within the cooperative world as well. In the case of my cooperative, we have recently entered into an agreement with U.S. BioEnergy, a leading ethanol producer. We believe this joint venture will allow our producers to realize some of the benefits of the recent boom in the ethanol industry. I can tell you that without a partner like U.S. BioEnergy there is no way that we could have entered the ethanol business. The start-up costs for such a value-added ventures are significant and are more than what our cooperative could have afforded. Another example is a concept for condominium grain storage. Heartland Cooperative is currently offering this program to patrons of the cooperative. It allows our patrons to own storage space on property owned by the co-op. We will form a limited liability company to administer the program. I believe that the limited cooperative business model would have provided us with more flexibility. Under LB368 farmers and ranchers would be able to form businesses under the cooperative model and include investor members. Certainly this would help with the enormous capital costs with most value-added businesses. If LB368 would have been available at the time, this would have been one more option for my cooperative to consider in our efforts to return more value to our cooperatives. Just as the advent of limited liability companies provided opportunities for many business ventures, we believe that LB368 can provide one more tool that can be used to help farmers and ranchers capture more value and stimulate economic development in the rural areas of our state. Thank you for the opportunity to share my thoughts. I would be glad to respond to any questions. [LB368]

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SENATOR PAHLS: I see no questions, thank you, Bruce, for your testimony. [LB368]

BRUCE FAVINGER: Thank you, Senators. [LB368]

KEN BOSWELL: (Exhibit 9) I am Ken Boswell. I am a farmer from Fillmore County and I currently serve on Nebraska Farm Bureau Federation's board of directors. I also serve as a member of the Aurora Coop's board of directors. I am here today on behalf of Nebraska Farm Bureau Federation to offer our support to LB368. At our annual meeting last December, Nebraska Farm Bureau voting delegates adopted policy supporting the establishment of a new generation cooperative model in Nebraska to enhance value-added agriculture by attracting investment capital while maintaining farm patronage participation in the business. During the last 10-15 years value-added agriculture has become an increasingly popular topic among agricultural producers. The desire by agricultural producers has grown to be able to keep more of the value of the commodities they produced as those commodities moved through the stream of commerce. Farmers continue to look at ways to invest money and committing their agricultural production to enterprises such as bean crushing plants, ethanol plants, flour processing facilities, beef packing plants, etcetera. In addition, other factors in the agriculture of economy have been driving this trend of more producer interest in value-added agriculture. First, access to markets for growers has become more difficult as concentration among food processors and retailers has accelerated. Second, independent family farms feel threatened by the continued consolidation in agriculture. Therefore, we believe new generation co-ops are one way to help bridge the gap between commodity-oriented producers and consumer-focused markets. However, one of the major hurdles to start-up or to construct the physical assets necessary to form a value-added agriculture project is raising sufficient capital. Using the existing cooperative model, organizers are limited by the requirements that the cooperative be farmer-owned and controlled, and that the return on investment be limited to 8 percent per annum. As farmers are reaching retirement age and some of the value-added co-ops that have been formed in the past, they are having trouble meeting patronage requirements because they are getting out of farming as they reach retirement age. But yet they still have a stock in the value-added venture. To address this problem a new generation co-op business model would be able to blend the traditional structure of a farmer-owned cooperative that provides for farmer control and patronage allocation participation with a traditional limited liability company. States in the upper Midwest that allow these types of business arrangements have seen many successes particularly in projects related to ethanol and livestock, both of which are a major part of Nebraska's agriculture economy. In conclusion, we believe the new generation cooperative model, as presented in LB368, provides a means for a value-added agriculture venture to grow in Nebraska which directly benefit farmers and ranchers. Be happy to answer any questions. [LB368]

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SENATOR PAHLS: Seeing none, thank you, Ken, appreciate you testimony. Again, asking you to spell your name, for some of you who are new to us. [LB368]

SCOTT MERRITT: (Exhibit 10) Mr. Chairman, members of the committee, my name is Scott Merritt, that is spelled M-e-r-r-i-t-t. I serve as the executive officer for the Nebraska Corn Growers Association. On behalf of our organization I would like to extend our support for LB368. I will just kind of highlight some of my written testimony to move along and the handouts include a study that was conducted by National Corn that I will refer to. I will admit I was one of the biased members to support this when the task force started. When I was asked to serve on the task force because of some of the work that was done in the study that was handed out. But I will say that the task force spent a lot of time going over the pros, the cons, working to make sure that we were uniform with federal regulations, and it was very in depth work but I still remain a very pro and supportive of this concept. NCGAs interest in new generation co-ops was sparked by the study that has been handed out to you a couple of years ago conducted by National Corn that is entitled taking ownership of grain belt agriculture. There was four key points that were identified in this study to look at the future of rural economic development in the Midwest, particularly. I will just read one of the points that I think brings us to this. It was to reform producer-owned business structures to improve tax efficiency, easily raise capital, and offer investor liquidity. I think that is a key point of where we are headed with the new generation concept. Our state has had tremendous success in the ethanol industry. I don't think anyone can question that. But if it has had one downfall that we have identified is it lacks a lot of local ownership and I think some of the issues that have been identified here are part of that, and we all understand as these entities create wealth and equity in a local community or in a local area, a lot of times that wealth and equity stays in the area and regenerates time and time again to provide more economic benefit. I would clarify though that our leadership does not view this model as something radical, as something totally indifferent, but simply a business model that each entity as they begin their process will need to look at to see if it is a viable tool for them. We support this business model and we think it will allow for more individual investment, it will allow producers to move more upstream in their ventures, meaning more farther down the food chain that we believe is probably the future as we move away from more commodity agriculture. So on behalf of our organization we would like to support LB368, and if there are any questions I would be happy to answer. [LB368]

SENATOR PAHLS: Scott, I see no questions, thank you, appreciate your testimony. [LB368]

SCOTT MERRITT: Thank you. [LB368]

DAN RICE: Chairman Pahls and committee, thank you for the opportunity to speak with you today. My name is Dan Rice, D-a-n R-i-c-e. I am a producer that lives just south of

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Lincoln in Firth, Nebraska. We have a limited liability company that was formed in the year 2000 and it was formed from four different entities, corporations that have been milking dairy cows for generations that come to a point, where for efficiency reasons and for compliance with the EQ regulations, we had chosen to dairy together. I am also coming representing the dairy industry as a whole. I am the chairman of the American Dairy Association of Nebraska and Dairy Council. The dairy industry in Nebraska is at a serious crossroads. In 1995, just 10 years ago, we had over 1,000 dairies in the state of Nebraska. Today we are less than 350, and the reason is mainly lifestyle and lack of capital to maintain added value ventures that are possible. LB368 gives us opportunities for added value ventures. Personally, in our own dairy we recently started marketing our own milk in Nebraska limited to Lincoln and Omaha for financial reasons. If we had the ability to bring in some outside investment. We are starting to and working towards national and international sales of our dairy products. However, we are very limited in capital and that is tying our hands very much. So that would be an example where this could really help the dairy industry. Also in our operation we currently have a composting operation and with the interest in environmental and renewable resources we would like to take our compost operation to the next step, and that is combining our dairy by-product with food wastes out of cities such as Lincoln and Omaha, and generating a methane by-product to generate electricity. And this is another area where if we could bring in some outside capital it would greatly help us in that venture. So we feel as a dairy industry that the passing of this bill would greatly help the dairy industry. Thank you and I would be willing to answer any questions. [LB368]

SENATOR PAHLS: Seeing no questions, thank you, Dan, for your testimony. [LB368]

WILLIAM B. BEVANS: Good afternoon Senator Pahls, members of the committee. My name is William B. Bevans, W-i-l-l-i-a-m B. B-e-v-a-n-s. I am president and chairman of the board of the Nebraska Turkey Growers Cooperative in Gibbon, Nebraska, and Nebraska Turkey Growers have been in the value-added business for over 75 years. We process over 4 million turkeys, which is about 60 million pounds a year and market them under our Norbest label. In addition to whole birds we produce a variety of cut up products, including bone and breasts and hind quarter roasts. We also do some cooking and produce smoked whole birds, smoked breasts, and drumsticks. We make a fully cooked roasted turkey which you simply thaw and heat. We produce specialty products for resale by such gift marketers as Harry and David. We have a real need in our operation to update equipment and facilities, and add more cooling and cooking equipment to grow our ready-to-eat product lines. Our aging infrastructure requires major renovation including our electrical and ammonia systems. We need more space for processing and fabrication. In short, we have a huge need for capital at our plant. Our major source of capital is borrowing from CoBank, but in order to finance plant equipment, and expansion, and operations we exceed what the bank can loan without a capital infusion. An infusion of capital is very difficult for our producer members to do. We are a small group of growers of about ten farms. The growing end of our business is

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also very capital intensive. We have recently asked our members to increase production to fully utilize the capacity we have in the plant, and our growers have responded by adding about 10 million pounds to our production schedule this year. This required an investment of almost \$6 million in facilities on the farms in the last two years. With financial commitments like these on the farm it is difficult to make additional capital commitments to the plant, and if some of our own members are able to invest in the plant there is the issue of how to compensate them for an investment beyond that which is made by the membership as a whole. This bill addresses precisely that dilemma and also provides for other interested investors to participate in our business. Those may be either individuals or other business entities that would benefit from a partnership with our cooperative such as a freezer company may want put a freezer in connection with our processing plant, or a feed company may be interested in investing in our processing facilities in order to have the feed business from growing turkeys. I think LB368 creates a very useful mechanism for raising capital needed in our operations and like operations in Nebraska, and I urge you to support this bill. Any questions? [LB368]

SENATOR PAHLS: Seeing no questions, thank you, William. [LB368]

WILLIAM B. BEVANS: Thank you. [LB368]

SENATOR PAHLS: Appreciate you testimony. I think that concludes our proponents. Opponents. [LB368]

ROBERT J. HALLSTROM: (Exhibits 11 & 12) Mr. Chairman, members of the committee, my name is Robert J. Hallstrom. I appear before you today on behalf of the Nebraska Bankers Association to testify in opposition to LB368. I certainly do not anticipate taking as much time as the supporters of this legislation did today. But I did have sufficient time to bone up on the stories of David versus Goliath and Daniel in Lion's Den. So we are going give it the old college try. I want to make it clear for the record, the NBA does not object to the stated objectives of LB368 which are to promote rural economic development and to enhance the development of value-added agricultural programs. I think it was interesting to note that virtually every witness before you today, while the supporters initially did indicate that this was a bill that was much broader than simply value-added agricultural programs, virtually every example that was provided to the committee today consisted of value-added agricultural programs. We think there are ways to resolve our issues and concerns with the bill if there is somewhat narrower scope than is embodied in the bill as introduced. We have expressed in our written testimony a number of reasons for our opposition. First, there is no reason to rush to judgment on this bill. It is patterned after the model act that was referenced from the National Conference of Commissioners on Uniform State Laws which is not even been finalized yet. It is my understanding they are still dealing with what to exactly call the name of the act and the entities to be created thereunder. In looking at the some 150-200 page proposal the comments and the sections of the

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proposed model act itself are replete with all kinds of new amendments, new commentary and so forth. Whether or not it is going to be done anytime soon is probably anybody's guess. I note on page 2 of my testimony, in the middle of that I note for your attention some language that is in most of the other five states that have adopted this language which, again, aligns itself more closely with the stated purposes of value-added agricultural programs. Specific language in the powers and purposes clauses that relate to marketing, manufacturing, processing of agricultural products and the like which perhaps narrows the scope more to the banker's liking. We are also concerned, and we have made it clear to the cooperatives in visiting with them and we have extensive discussions with them. We just haven't come to an agreement at this point on how to proceed, is our concern that the new entities could be used a spring board through the adoption of federal legislation to allow CoBank to expand the traditional entities to which it is authorized to lend. We have already seen, a number of years ago, federal legislation introduced which would if adopted allow CoBank to, essentially, lend to these types of entities. The very parameters upon which these entities are created would have been addressed in that proposed federal legislation. Also would have deemed anything to be a cooperative under state law would it likewise be eligible for expanded CoBank financing. So we have some concerns in that particular respect. I would also note that the Farm Credit System has recently come forward with what they refer to, I believe, as the Horizons program. This type of entity being available for lending from the Farm Credit System is a plank or a cornerstone of that very program as I understand it as well. The last thing that I would like to comment on before I talk about the amendments that we have is the fact that we don't believe that these new entities should be involved in long-term operating lines of credit for farms or businesses, particularly if they have any access to the government-sponsored enterprise subsidized funding source that we have raised in concerns in my last discussion on CoBank and the Farm Credit System. As a result, one of the components as Mr. Weber noted of the amendments that we have proposed are to limit the duration of any loans or extensions of credit that are associated with the sales of goods and services of these new cooperative enterprises, and to also limit their ability to secure these loans with real property. I was encouraged to hear Mr. Weber say that maybe there is a little bit longer duration of a loan and perhaps some limitations on security utilizing real property that they perhaps would entertain, if I didn't misread his comments, and would certainly pledge to continue working in that respect with their organization. But the other aspect, we have got language that would restrict the ability as does federal law currently for these new entities to obtain access to CoBank financing. We would further expand it to indicate that no Farm Credit System lending activities should occur with regard to these new entities. Mr. Weber and others have suggested, Mr. Andersen, that there may be federal preemption. If there is, what do they have to fear? We put the language in state law. If it is preempted, it is of no affect but it certainly provides some mechanism for the state to make a policy determination that to the extent we have control, we would prefer not to see these entities have that subsidized form of financing. I also would note, I find it somewhat interesting, that when

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asked what has restricted Iowa from creating these entities that some indication has been given to the fact that there are disclosures on investment products and some restrictions on the length of loans. Until just before the start of the legislative session when this legislation was first passed by the NBA I don't believe the cooperatives in Nebraska were aware that those restrictions existed under Iowa law. So I would suggest it is probably somewhat anecdotal to suggest today that that is the very nature of them having restrictions on the ability to create these types of entities and enterprises in the state of Iowa. Again in closing, the amendments that we have, and I do have that as a handout in bill-drafter form, address the CoBank and the Farm Credit System issue, the disclosures with regard to any investment products, and the limitations on the lending activities. I would note that we have expanded the limitation on lending activities to effectively provide for a renewal if it is not paid at the end of the six month duration that we have suggested. We have provided flexibility for renewal and if there is a troubled loan of sorts, at that point as well, we would also after that six month initial period provide for the ability to take additional security in the form of real property. With that, I would be happy to address any questions of the committee. [LB368]

SENATOR PAHLS: Senator Langemeier. [LB368]

SENATOR LANGEMEIER: Thank you, Chairman Pahls, and Bob, thanks for your testimony. In going through your handout that you just handed us, what is the concern with CoBank and Farm Credit making these loans? [LB368]

ROBERT J. HALLSTROM: The current situation, Senator, is that my understanding of the federal law and regulations is that CoBank is restricted to making loans only to what you would refer to as a traditional agricultural cooperative. The supporters talked about the restrictions on dividends, the restrictions on 85 or 80 percent farm patronage involvement. So that federal law probably will, for the moment, prohibit the ability of CoBank to make loans to these new entities. However, as I have also suggested in my testimony, CoBank has already attempted in the Farm Credit System through their Horizons program are already setting the stage to make changes in federal law that would authorize them to make loans to these types of enterprises. [LB368]

SENATOR LANGEMEIER: So it is your belief we should sit back and wait for federal law either to be enacted or not before we do anything? [LB368]

ROBERT J. HALLSTROM: I wouldn't necessarily, even though we are objecting and opposed to the legislation, wouldn't suggest that taking action should be conditional upon that. I am only suggesting that in accord with our amendments some protective provisions be placed in state law. The supporters have suggested it could be preempted but the protection would be to put into state law that they shall not be eligible for CoBank or Farm Credit System financing. [LB368]

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SENATOR LANGEMEIER: Okay. But there has been also federal law that change how banks can be held, too, correct? [LB368]

ROBERT J. HALLSTROM: That is correct. [LB368]

SENATOR LANGEMEIER: From C to S corporations and hopefully to limited liabilities. [LB368]

ROBERT J. HALLSTROM: Yes. We are not yet to limited liabilities because of some of the tax problems and tax issues through the Internal Revenue Code. [LB368]

SENATOR LANGEMEIER: But with that you have gotten some federal tax relief as well as now a bill in revenue to get some state relief to go to S corporations, correct? [LB368]

ROBERT J. HALLSTROM: That is correct. [LB368]

SENATOR LANGEMEIER: Okay. On here when you talk about lowering it down to six months, why don't you want security of real property until the delinquency of that first six months? I mean what is the problem with... [LB368]

ROBERT J. HALLSTROM: Senator, the general proposition is, I think, the traditional ag co-ops have been involved in short-term financing of their goods and services. They have not gotten into or expanded themselves much into the operating lines of credit for farms or businesses. We just think that if these expanded entities are going to have significant amounts of equity capital, significant ability to get into competition with some enterprises in the manner in which Senator Gay proposed, that there ought to be some limitations on how they can loan their funds in competition with financial institutions if they are getting them, particularly, from a subsidized government sponsored enterprise. [LB368]

SENATOR LANGEMEIER: Okay. I agree with the short-term nature of their lending, but I guess I have a problem with not allowing them to have the same protections to the assets they put out. As a potential patron I would want to make sure they could secure the assets that they are lending out to their people, wouldn't I? Wouldn't that be fair? [LB368]

ROBERT J. HALLSTROM: Well, Senator, there is probably some merit to that. I don't think the traditional ag cooperatives have operated, I could be wrong, but I don't sense that they have operated on that basis. They sell goods and services. They have an open account or some form of extension of credit with payment terms, and interest accrual, and so forth. The flexibility that we have attempted to provide them, which goes beyond what we had initially talked with the co-ops, is to say if you get to the end of a

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six month term and the payment conditions are not being met that at that point the ability to go out and seek additional security in the form of real property would be authorized. So it is a compromise, if you will, from our initial position. [LB368]

SENATOR LANGEMEIER: Okay. Thank you. [LB368]

ROBERT J. HALLSTROM: Thank you. [LB368]

SENATOR PAHLS: Senator Pirsch. [LB368]

SENATOR PIRSCH: Yeah. Could you comment on the proposition that these producers could create an entity under the laws of a foreign jurisdiction, say Wyoming, and conduct business in the state under that type of a... [LB368]

ROBERT J. HALLSTROM: Senator, I wouldn't dispute that from a legal perspective. I obviously have not done the research to determine what they can or can't do, but it would appear logical that they could create that type of entity. Now, again, in those other states it is not as crystal clear that the authority or the powers that are granted are near as broad as the proposed legislation in Nebraska has been. The other thing that throughout the comments here, and perhaps I just need to talk to the supporters to get a little bit more clarity in my own mind, I am not exactly sure why the traditional limited liability company doesn't work. Perhaps there are some tax issues or other scenarios, but we heard examples through the supporter's testimony that the ethanol plants have all been made with LLCs. There has been some very successful projects with the grocery stores and others that have worked within the traditional ag cooperative, so I am not sure why they couldn't just set up a traditional limited liability company in Nebraska and go about their business. [LB368]

SENATOR PIRSCH: And just as a follow-up to that, the conducting business under an LLC would not be as objectionable as opposed to the way this particular bill is written because of the structure, the financing, is that correct? [LB368]

ROBERT J. HALLSTROM: The structure of the entity would make it without question, irrespective of changes in the federal law, that they would not be eligible for CoBank financing. And depending upon the type of entity they may or may not be eligible for Farm Credit System financing as well. [LB368]

SENATOR PIRSCH: I see. So it is that type. Okay. [LB368]

SENATOR PAHLS: Senator Carlson. [LB368]

SENATOR CARLSON: Senator Pahls. Bob, in listening to your testimony and the testimony from the cooperatives, on your amendment lines 19 and 22, would you

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entertain changing "6" to "12"? [LB368]

ROBERT J. HALLSTROM: I would be more than happy to sit down and visit with Mr. Weber and the cooperatives as to exactly how they would like to see that resolved or adjusted. I certainly have no objections and am open to those types. I think the main thing is long-term operating lines of credit type of financing has not been what a cooperative has traditionally been involved with and that would be the basis. The language that we have here was lifted, Senator, directly from the Iowa law. There are restrictions on the powers and purposes of the new cooperative entities that were taken directly from Iowa law in that respect. [LB368]

SENATOR CARLSON: Thank you. [LB368]

SENATOR PAHLS: Senator Langemeier. [LB368]

SENATOR LANGEMEIER: One more question then. I think these questions are helping me get this fully in my mind, Bob. Two issues here, number one the length of time that co-ops can loan out money, and you believe that this new limited corporation would have that as a goal or an opportunity even though it says in section 4 that these aren't created for the purpose of being a financial institution? [LB368]

ROBERT J. HALLSTROM: Yeah. There is a difference between...we have seen in a lot different venues, Senator, that a lot of people like to lend money but they don't want to be determined to be a financial institution because of the regulations that are accompanied by that status. So while I appreciate the fact that they can't be a financial institution or an insurance company, there is not as much stock in that as it is to how they are actually going to operate, how are they going to lend, what is the source of funding that they are competing with traditional financial institutions pursuant to. [LB368]

SENATOR LANGEMEIER: Okay. That was the first part and the second part is the ability to borrow from CoBank, which this is all new to me, CoBank and Farm Credit Services. What are the attitudes of the bankers to lend to these type of agencies? Are co-ops something banks look forward to seeing come in their door to lend to or not? [LB368]

ROBERT J. HALLSTROM: Senator, I don't know. I would have to check and see whether or not that...the CoBanks are, I think, the primary source of credit for the co-ops and that is what they are limited to exclusively, and that is one of the concerns as we have seen CoBank, as our understanding, looking to spread their wings and get more entities eligible for them to provide financing for. [LB368]

SENATOR LANGEMEIER: Okay. Thank you. [LB368]

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SENATOR PAHLS: Seeing no more question...Senator Pankonin. [LB368]

SENATOR PANKONIN: I just have one more, Senator Pahls, thank you. Mr. Hallstrom, you might explain just, historically, why the CoBanks or the Farm Credit System, what the difference is, and their rates, and their source of funds. Because this historic thing, some might not understand. [LB368]

ROBERT J. HALLSTROM: Yeah. Senator, the primary issue with regard to Farm Credit System is that they have access to subsidized funding, if you will, as a government sponsored enterprise. So they have the ability to compete on what we would traditionally call an unlevel playing field. So in providing funding for any type of business or farming operation they will have a leg up, if you will, on the traditional financial institutions cost of funds that it takes for us to get money out of the marketplace and back into the hands of businesses. So I think there is that issue. We have seen the Farm Credit System under the Horizons program looking to expand the entities beyond and above the traditional agricultural setting and communities of less than 2,500 for residential financing. All of those things would be greatly expanded if the Farm Credit System Horizons program is expected by Congress as part of the farm bill or as part of separate legislation. So I think that is where we have if these folks, the new entities are out with the source of funding coming from a subsidized government-sponsored enterprise that they will be better able to compete on that basis for those funding projects. [LB368]

SENATOR PANKONIN: Thank you. [LB368]

ROBERT J. HALLSTROM: Thank you. [LB368]

SENATOR PAHLS: Thank you, Bob. [LB368]

ROBERT J. HALLSTROM: Thank you. [LB368]

LARRY RUTH: I am in a neutral position. [LB368]

SENATOR PAHLS: Neutral, good. [LB368]

LARRY RUTH: I perhaps have jumped the gun here. I am not sure if there is any other opposition or not. [LB368]

SENATOR PAHLS: No, no, no. Let's see, anymore opponents? Neutral. That is what I was figuring you would be. I apologize. [LB368]

LARRY RUTH: (Exhibit 13) Thank you, Senator Pahls and members of the committee, my name is Larry Ruth, R-u-t-h. I appear today in a neutral capacity for information

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purposes only. I am one of Nebraska's commissioners to the National Conference of Commissioners on Uniform State Laws. That was referenced several times in previous testimony as being the base document or the draft which you have before you. John McCabe was here several weeks ago and spoke with you about Uniform Trust Code. We also spoke at that time about the Uniform Prudent Management of Institutional Funds Act, and the NCCUSL, sometimes called that, has been involved with 55-60 different draft bills that have been passed in Nebraska. I only come to you to let you know that the NCCUSL continues to look at this issue and draft. I think we are up to the 11th draft now on this particular subject. It will be coming to the annual meeting in July. It started back in February of '04 and I just went through the different memos and drafts, and I passed that out to you to let you know that there is a group of people from across the country that have been working on this bill for three years and that is not unusual. That is typically what it takes for a major bill of this nature to be considered. It started in '04. We will have perhaps a conclusion with the 12th draft probably in '07, this summer. I think what you have in front of you as LB368 is one of those last last drafts. I have not talked with Mr. Weber, but my assumption is that it was along the 10th or 11th draft that got incorporated into bill LB368. But there are still tweaks being done with it and I just mentioned to you, Senator Hansen, that one of the very issues that you raised is on the definition of a participant, and in the latest draft that is going to be looked at by a committee here next week, it divides up the term participant between those who are patron participants and those who are investor participants, and then avoids the confusion that you apparently had when you were looking at it and clarifies that. That is the kind of thing that has been taking place and will continue to take place all the way up through this summer. I only bring this information to you to let you know that there is more work that will be done on it, that will continue to be worked on over the summer, and then you will see a final draft probably of some kind, a final, final in very final form toward the end the year. The question that really comes to you as it relates to our further work is whether you wait that final action or you proceed and you give the added flexibility that might be wanted now. That is not for us to decide. That is for you to decide. But the types of things that we will do in the last six months, such as definition of participant, and some perhaps reviewing of different interest groups and how those issues can be negotiated will be in the last drafts. I would also say that the final draft will then be a uniform act. It will be presented to all the states for their consideration and then when a uniform act is promulgated in Nebraska, or California, or somewhere those people who are interested in engaging in interstate commerce can understand that if they have a uniform act in California it is going to be very similar to a uniform act adopted in Nebraska, which is in essence why we have the uniform laws is to recognize those issues which have uniform application, and probably the best example there is the Uniform Commercial Code which now covers all the states and is very similar in all the states. So I only bring this to you for your further information as you go forward in your deliberations, and I don't know much about the subject matter. [LB368]

SENATOR PAHLS: Larry, let me ask you a question. Then with the information you

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have given me are you trying to tell me to act or to wait and see? [LB368]

LARRY RUTH: I am not going to tell you either one or make any recommendation that Mr. Weber has that access and committee staff, rather the staff for the Senator has access to the changes, and I am going to leave these with you because some of them are very minor and they are ones that would be probably incorporated into a final act in another year or two if you were to revisit it. I just bring it to you for your further information really. It is a lot of steam on this bill and if you feel it is important enough to move forward with it that is certainly what you should be doing. [LB368]

SENATOR PAHLS: Yeah. Okay. Any question for Larry? Thank you, appreciate it. [LB368]

LARRY RUTH: Thank you. I will leave this most recent draft with you. [LB368]

SENATOR PAHLS: I am assuming there are no more hands up out there. I thought I saw one go. Did I see a hand? Come on. [LB368]

RON MORAVEC: Good afternoon, Senator Pahls, members of the Banking Commerce and Insurance Committee. My name is Ron Moravec, R-o-n M-o-r-a-v-e-c, chief deputy Secretary of State. I am not going to engage you in a heavy debate that you have heard for the last hour and a half. But as the filing office where all of this paperwork will end up ultimately, that of the business services section of the Secretary of State's office, we just have a few comments, potential concerns about things in the bill as it exists that may be an issue. One of those right now the bill proposes that a name chosen by this cooperative association, the standard for selecting it is that of distinguishable upon the records that are within the Secretary of State's office. In other words you wish to form an entity, a corporation, you call or submit a name to the business services division and ask if that name is available for use. Presently, the standard that the Secretary of State offices use legislatively is that as the same as or deceptively similar to, and that standard of same as or deceptively similar to has with the exception of seven or eight years been the standard that has been used in Nebraska since the initial adoption of the corporation act back in 1959. In 1995 the standard was changed to distinguishable upon our record. But then again in 2003 it was changed back to the same as or deceptively similar to. We would ask that you give consideration in this matter to keep the same name selection standard so that it is uniform throughout whatever type of entity is involved. Possibly as the Secretary of State is going to be filing a lot of reports under this act, it may be beneficial to the office if the Secretary of State was given the authority to establish rules and regulations to carry out the enforcement of the act. At this point I do not see that contained within the act. The limited cooperative associations are required under LB368 to file an annual report. Again, that would be a decision for this committee and the Legislature to decide, but with one exception the standard we now use legislatively is biannual filing of reports and to now say that in this instance it shall

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be an annual report may be beneficial, may not. It will certainly create more filing and filing fees for those entities involved. Another situation is that the Secretary of State is designated, I guess you would say, as a default agent for service of process in the state of Nebraska. Again, with the exception of one other type of entity, the statutory language placing the Secretary of State as the default service of process has been eliminated and we would ask that the committee and the Legislature give consideration to removing the Secretary of State as a service of process location, if the registered agent or the agent of the LCA cannot be located. There is some language in the act that in filing of the records one of the provisions, section 19 of the act, indicates a record authorized to be delivered to the Secretary of State for filing under this act shall be captioned to describe the records purpose and be delivered to the secretary for filing. Again, maybe a little more definition of what that means would be beneficial so that the business services records division would have an understanding of what specific type of documents are to be filed and what may be rejected. With that, I would conclude unless there are some other questions. [LB368]

SENATOR PAHLS: Senator Hansen. [LB368]

SENATOR HANSEN: Thanks, Senator Pahls. Ron, on the first part where you said name recognition things I will give you an example, Ag Valley Coop and Ag Valley LCA on one sign, is that acceptable? [LB368]

RON MORAVEC: I am sorry, Ag Value what? [LB368]

SENATOR HANSEN: Well, Ag Valley Coop and Ag Valley LCA. [LB368]

RON MORAVEC: Probably not. [LB368]

SENATOR HANSEN: Probably not. [LB368]

RON MORAVEC: Yeah, because we disregard the corporate designation, LCA or whatever other example you gave and you have basically two same words describing it. [LB368]

SENATOR HANSEN: Yeah, but that is an established co-op and then they form an LCA. [LB368]

RON MORAVEC: They may have to take a fictitious name to do business. [LB368]

SENATOR HANSEN: Okay. One other thing, being a freshman Senator down here in the first year on the committee I see one glaring error, that we have no place for a post office box. [LB368]

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SENATOR PAHLS: You are so bad. [LB368]

RON MORAVEC: I would add that to the list, Senator. [LB368]

SENATOR HANSEN: That would go on page 22 line 12. [LB368]

SENATOR PAHLS: I am glad you are making me smile because we are two hours on this bill. Any questions other than post office box information for Ron? Seeing none, I thank you, Ron. [LB368]

RON MORAVEC: Thank you, Senator. [LB368]

SENATOR PAHLS: Senator, for closing. [LB368]

SENATOR ERDMAN: Mr. Chairman, members of the committee, I appreciate your attention this afternoon and recognize that there is some work to be done. Let me go over a few brief comments that I think help to clarify. LB368 is not an amendment to an existing business model. It is a new business model. Currently in the state of Nebraska, and you have heard today we have LLCs that are operating under ag industry and they are obviously some that are operating under nonag industries. You have cooperative business models used for specific production agriculture and you have some that are not used for specific production agriculture. The Limited Cooperative Act shouldn't be treated any differently than those other two business models. We don't limit their scope specifically to the industry in which they are engaged in, and I believe it would be shortsighted and inappropriate to ignore those historical and legal standards that we use in other areas in adopting this act. Panhandle Coop is an example of a cooperative that is not specifically a production agricultural cooperative. They have got grocery stores. They compete with Wal-Mart. They compete with Albertsons. They compete with Safeway and they are owned by the patrons who shop there, such as myself. So there is some of this discussion that I think is healthy. The thing that I will point out though is that the limited cooperative model has absolutely no advantage to the people in the community from forming an LLC under current law. They can do that now. And so it is a matter of making sure that as we give you examples that you understand that there are certain examples in existing law where that could happen. One of the issues that was brought up was a community of Bayard, we went without a grocery store for a year and a half. We didn't know what to do and if it wouldn't have been for an individual who had the investment and the ability himself to do it we wouldn't have a grocery store. And so there are some other applications to law that this bill would apply to that are applied to in other states. For example, in Minnesota the act that they passed is very broad and it was the basis for the discussion on the national level for the uniform law. It wasn't the Iowa law and, in fact, the language that has been brought to you by the Nebraska Bankers Association is in no other act but in Iowa. It is not found in Wisconsin. It is not found in Tennessee. It is not found in Wyoming. It is not found in Minnesota. One state

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doesn't make it a standard, doesn't necessarily make it right. However, the groups that are involved in supporting this legislation are willing to continue to work with them and educate those interested parties on the law and the intent. Wisconsin law allows for lending to and borrowing from members, and we can provide you with the citations for those laws as well. This is not a model act. It is a uniform law. One of the things that I have picked up very closely on Mr. Ruth's testimony was that even the UCC isn't universal. It is similar. Regardless of what comes out of the national proposal, whatever comes out of the commissioners' draft, we are going to amend it. We are going to amend it for things such as what the Secretary of State's office has brought to say that is not how we technically file things, that is not how this is set up. We are going to have those opportunities. The idea is that it be similar. It is based on the most recent draft and we have been working closely to make sure that we follow that process as much as possible. Only Tennessee and Wyoming limit the scope of their act to marketing only. Again, it goes back to the idea that was adopted. It doesn't make sense to limit this in my opinion. The access to governmental sponsored entities, if you grabbed a list as a registered appraiser in the state of Nebraska, you look at the businesses that we do business with and who our clients are. Regardless of who the bank is, and Senator Langemeier can probably confirm this, a lot of times it ends up at Fannie Mae, Freddie Mac, you go down the list. Access to governmental sponsored entities is broad and it is readily available to a number of entities. The provisions in this law or in the federal law that apply to this act regarding cooperatives, and CoBank, and Farm Credit, there are existing provisions that govern when those entities are eligible for that type of financing. So we go through this process and I think a lot of this is education, but, again, it is also an opportunity for us to have these types of discussions. I will close with this, an argument was made well, we don't really need this, at this time, because of all of the LLCs that are being formed to produce ethanol plants in the state of Nebraska, and candidly a lot of the testimony today was based on value-added agriculture. That is generally what has driven these proposals in other states. However, in the information that I have shared with you, you will find that there are medical entities that are formed under this. There are housing entities formed under this act. It is broader than simply value-added agriculture. But what was one of the comments that you heard today is why this would be a value specifically for Nebraska in the current climate that we find ourselves in, in value agriculture, local ownership. Local ownership. Private placement on a national level to bring a facility into a place like western Nebraska to build a 220 million gallon ethanol plant is a fantastic opportunity for that community. But under the existing process we are not envisioning the LLC opportunity of investment with the cooperative model of patronage. Those two aren't in those discussions now. It would be an advantage for the state of Nebraska to follow the lead of these other states and figure out how to merge the best of those ideas balancing the interests at hand and provide, whether you are an agricultural producer, whether you are a grocery store, or whether you are someone else with a different idea with the tools that you need to be successful in this state. That is what we are trying to accomplish with (LB)368. Does it apply to value-added agriculture? It absolutely does. Does it apply to other entities? It

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absolutely should and we are willing to work with the groups that are here and as you have heard a number of the folks, this has been an ongoing process. It started in 2005, it has been 18 months in the process. The national commissioners have been going at this for over two years now. This is going to be something that we should do. The question is how and we are willing to work to figure out what that looks like, and in keeping with one of the comments that Senator Langemeier said, it is a disservice to the state, I believe, to sit around and wait. And so I am hoping that we can work together to resolve some of these issues and move forward expeditiously. Thank you, Mr. Chairman. [LB368]

SENATOR PAHLS: Any questions? Thank you, Senator. That will close the hearing on LB368. [LB368]

SENATOR PAHLS: Senator Janssen, I think we are ready for you. [LB174]

SENATOR JANSSEN: Okay. Whenever you are ready just let me know. [LB174]

SENATOR PAHLS: I am sorry. I thought I had...we are ready. Okay. Let's begin. [LB174]

SENATOR JANSSEN: Good afternoon Mr. Chairman, members of the banking committee. For the record my name is Ray Janssen. I represent the 15th Legislative District, the pathfinder district. I am here today to introduce to you LB174. This bill would make three significant changes regarding the relationship between the issuing bank of credit and debit cards and merchants who are authorized to accept these cards. First, LB174 would provide for an additional disclosure of the rules and rates that are contained in contracts between banks and the merchants. Under this bill a merchant would have to be given the complete rules referenced in the contract. The merchant would also have to be informed when a rule has been changed and would then receive a copy of that rule. A complete schedule of interchange fees, credit and debit card transaction rates, and any other fees that are charged merchants who would also have to be provided to the merchant. Second, these contracts would not provide an issuing bank with the authority to charge a merchant or deduct from the merchant's account the cost of a debit card transaction because the cost of the transaction is higher than the predetermined amount. The third thing, the bill would prohibit charges or fees to be applied to the sales tax portion of any credit or debit sale. I believe there are probably people here who would testify after me who can further explain the needs for these changes. With that, I would try to answer any questions you may have and I hope you don't have as many testifiers as you had on the last bill. Any questions? [LB174]

SENATOR PAHLS: Any questions for the Senator? Thank you. Are you going to be around for closing? [LB174]

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SENATOR JANSSEN: I may waive closing. I will stick around for a little bit, Rich, because I want to see what is happening over next door, see if we are still on the state song. [LB174]

SENATOR PAHLS: Let me hear you sing the one they are proposing. Thank you, Senator. I would like to see just hands of those who are the proponents. I see four, five. Opponents? Two. Okay. People in neutral. You are in much better shape Senator Janssen. You may come forth and I am going to ask again for you to spell your name for us. [LB174]

STEVE MOSKOVITS: (Exhibit 1) My name is Steve last name Moskovits, S-t-e-v-e M-o-s-k-o-v-i-t-s. I am with No Frills Supermarkets as their controller and CFO. Thank you for your time this afternoon. As a merchant who accepts debit/credit processing in our retail business I wanted to shed a little light in support of today's bill (LB)174. I think everybody here is aware from the consumer's side how the credit card works. Everybody carries a credit card, takes it to the store, charges, pays for their goods, and I think they understand their side of the fee structure, i.e. you may be charged a monthly fee for your account from your bank, you may be charged a transactional fee based on certain transactions, you may be charged interest, you may be charged if you go over limit. Some people have had that experience. I think not a lot of people understand the other side of it and that is the side that the retailer experiences, and that is the discount and interchange fees that are charged to the retailer to accept credit and debit, and that is part of what we wanted to go into today and I prepared some analysis of some particular stores that can illustrate my points. The discount and interchange fees that the retailer faces are charged in two different ways. First off, we contract with the bank to process on our behalf and they charge us a transactional fee or click charge for the transactions that they process on our behalf. In addition, on the credit side, for example, you are charged interchange which is through Visa, Mastercard, American Express or whoever the issuing bank is and they in essence pass through the costs of participating in those organizations to promulgate Visa, Mastercard, American Express they have set up to get the retailers to accept it and they charge the bank that we process and they pass that onto us. So in essence, again, the consumer doesn't necessarily see this even know what interchange is, but it is a cost of our doing business and it is something that adds to the cost of your goods and services that you purchase everyday. To kind of magnify or show you the extent of what it costs. We are a chain in Omaha. We have 16 stores and in the upcoming year our budget is about \$1 million that we will be paying for electronic processing of credit, debit and EBT. So it is not a small component at all. As a matter of fact, over the last two to five years next to health costs bank interchange fees are the second largest increase in costs that face us as a retailer. So it is something that is very important to us and very important to the ultimate consumer. One of the things then that I have laid out, and I went and analyzed a couple of our stores just to show the impact and the increases that we have been experiencing. I have picked a couple of different stores to analyze and look at from our chain. One of which is a store that is a

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lower demographic, more benefit, food stamp, cash and check, and much lower user of credit. The second one I used is an example of more of an affluent credit/debit typical customer where they use it to more extent. So the first one I looked at and I compared over a period of time just to see how much increase there has been in credit and debit usage. The first store, again, is one that still more than half the people use cash and check, over 20 percent are using EBT. So almost three quarters of your transactions are not through credit and debit. Looking at that from several years ago that has increased anywhere from 7-10 percent. So there has been a modest increase over the last couple of years, but it is still more cash and check. The second store I looked at, again, has seen an increase of about that same over that time frame and so everything has just kind of slid in step, if you will. Looking at the first store that is a heavy check and cash customer user you will see that I have analyzed and looked at what our fees are for electronic processing of credit, debit and EBT. Starting in 2002 and moving forward to last year, and you will note that we started at \$26,000 a year up to \$35,600 the next year, \$41,300 the following year, \$54,817, \$52,891 in '06. So in just four years you will see that the amount that we paid doubled for that particular store for processing of transactions. In looking at that store sale volume, the store sales were up 11.7 percent over this period. So putting this in perspective, again, we have a particular store that sales are only up 11.7 percent on an annual basis. Looking above as to how we are shifting to credit/debit usage you will see that we are shifting only about 10 percent to additional electronic usage. Yet the fees that we have paid doubled over the four year time frame. That is a problem for retailer and obviously a problem that gets passed onto the consumer. There is a myriad of reasons why this happens, one of which obviously are increases in interchange rates and fees that are passed on to us. Additionally what a lot of people don't know or understand either is with all the new products and different cards that are offered out there that those are charged to the retailers at a higher rate. So when someone presents a card that is a frequently flyer card where they earn benefits or miles we pay a higher rate for that, almost a third more than we would if it was a regular card from that same bank through the rules of Visa. If they have a cash back program, again, I think most people out there, most consumers think that the banks paying for that, or the airlines paying for that, or it is just a part of somebody else that is doing business. But actually every time you present that card to the retailer that retailer is paying a higher amount on that particular card. And, again, these rules and regs change all the time, Visa International, Mastercard, they issue new cards, they issue new requirements, new regulations and as a retailer we simply bear the cost of doing business. The other thing is you don't always know as you are retailing accept a card, obviously, what structure you are going to get paid. We have an overall framework that tells us here is your base rate as a supermarket what you are going to be charged. But different cards get charged and you don't know then until after the end of the month when you get your statement and they tell you how many cards are charged at what rate. Some may be a business card which are charged at a higher rate. Some are rewards cards that are charged at a higher rate, and again some are just charged at the basic rate that you would have been expected them to be charged. Again, as a retailer

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and as you know almost it is universal now that credit/debit are here to stay, everybody else is using it. So it is not really a solution to say well, you don't have to take the card because to be in business and competitive with all of your other businesses you have to do what they do to stay in, survive when the customer expects you to take that as a medium of payment. So what we are here to talk about are at least some ways to help and, again, some of the issues that I brought up may need additional look or exploration, or a different level as to what we can do about it. But I think the proponents of this bill are looking to at least help stem what we are seeing as a huge increase in the cost of doing business. Very quickly back to my analysis, in store B that was a store that as I show is a heavier user of credit cards and actually pays twice as much per year as the first store that I showed at over \$114,000 a year that gets passed back as a cost of doing business and, again, that store wasn't there in 2002 so we don't have the analysis on the increase. One of the components of the bill that we are looking at that I would think would be relatively easy for the committee to look at, and that is looking at the application of the interchange fee on the state sales tax. As you know, as a retailer we collect and we are licensed to collect sales tax on behalf of the state of Nebraska which is simply a pass through. At the register the customer is charged a sales tax. We have to do the record keeping, the collection and then we do the remittance. As you know, we get paid a nominal amount of money on a monthly basis to handle the record keeping. But as more and more people are using credit to make their purchases we, in fact, are bearing the carrying cost and also being charged the interest on the discount interchange on the transactional piece for the tax. Again, that is not money that we keep. That is not money that is part of our sale. It is simply a pass through that we are collecting on behalf of the state. So it would seem to us that that would be a very quick remedy that the state could look at by eliminating the ability to impose interchange rates on that piece of the transaction. Additionally as I alluded to before, we have a myriad of different rules, regulations, changes when interchange does change we get a notice of the overall change. But, again, it is not always clear cut to us as a retailer when cards don't qualify for best premium pricing, when they are charged at a different rate, or why they don't qualify and those are things that as a retailer and as part of what this bill is trying to do is to make sure that that information is clear cut, available, and promulgated to us ahead of time to know exactly the reasons behind the distinctions in how we are charged on the various cards. With that, I am available for any questions. [LB174]

SENATOR PAHLS: Let's start over here with Senator Hansen. [LB174]

SENATOR HANSEN: Thank you, Senator Pahls. Steve, are the fees that are on the cards, are they negotiable from one bank to another? What I want to find out is if the free market should be able to take care of this problem. [LB174]

STEVE MOSKOVITS: The interchange piece is not. As I said, when you contract with your bank to process they charge a transactional fee which is what I call a click charge, just a number of cents per transaction as a fixed amount. That is something that you do

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negotiate with your bank based on volume, how much business you give them and that type of thing. The interchange rates are set by Visa, Mastercard, American Express. Those are imposed upon your bank and it is a pass through from the Visa bank to your bank to you. So those are not negotiable. No matter who does your processing that component would be the same. [LB174]

SENATOR HANSEN: So does No Frills grocery store, can you say we don't accept this card and that card but we accept all others? [LB174]

STEVE MOSKOVITS: Under the rules of Visa, for example, if you take Visa you are required to accept all Visa cards with the Visa emblem. You are not allowed to say I don't want to take that card because I will be charged more. In addition, I am not allowed to surcharge. I cannot directly charge somebody for using a credit card. So if someone has a reward card that I pay more I can't tell them that I am going to charge them more for their service. I am required to charge them equally as I would any other customer. [LB174]

SENATOR HANSEN: One last question, how about your return check fee? Is that different between banks? [LB174]

STEVE MOSKOVITS: Return check fee? [LB174]

SENATOR HANSEN: Well a no good check, a returned check. [LB174]

STEVE MOSKOVITS: Okay. You mean the amount that the bank charges me if a customer bounces a check? [LB174]

SENATOR HANSEN: Yes. [LB174]

STEVE MOSKOVITS: That would be negotiable between banks. Correct. [LB174]

SENATOR HANSEN: Okay. Thank you. [LB174]

SENATOR PAHLS: Senator Christensen. [LB174]

SENATOR CHRISTENSEN: Did I understand right? It might be one rate for Discover, one rate for the business Discover, and another rate for the mileage Discover or Visa or whoever? [LB174]

STEVE MOSKOVITS: That is correct. [LB174]

SENATOR CHRISTENSEN: So just all over multi-levels. [LB174]

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STEVE MOSKOVITS: Yes. [LB174]

SENATOR PAHLS: Okay. Senator Pankonin. [LB174]

SENATOR PANKONIN: Thanks, Senator Pahls. Kind of following with what Senator Hansen said, Steve, I guess I am wondering here when we talk about legislation to solve this and just a follow up. I have got a farm equipment business. We do sell parts and stuff over the counter and I have looked at these cards and we don't accept them. We are one of the few businesses probably that doesn't accept them for this very reasons. For the volume I do I don't think the fees are there, but yet I don't think it has cost me hardly any business. We just tell them we don't take the card and we get people that don't have the cash or check with them, they have to come back or whatever, they may be not happy, sometimes my employees aren't happy. I don't care. I am not paying these fees. So to say that you have got to do it, I don't buy it, and I am surprised that market wise you can't get together with other retailers. There is not enough market power to...maybe not No Frills does it but to say we have got to have a better situation. We have got to do this legislatively you think? [LB174]

STEVE MOSKOVITS: Well, again, we talk about retailers getting together we have done so and looked at the bank that you are doing business with, and on the transactional side we have been able to get reductions. But, again, the group you are talking about here compared to a Visa or Mastercard not nearly enough clout to do anything in that regard. So what we are looking for is protection, at least within our boundaries to say this is something the state really should look at helping the retailers within the state and what needs to be done. [LB174]

SENATOR PANKONIN: I missed the opening. Do other states have this exact type of legislation then? [LB174]

STEVE MOSKOVITS: I am not familiar with other states that have it. I know others have looked at it. I can't answer that question. [LB174]

SENATOR PANKONIN: Okay. [LB174]

STEVE MOSKOVITS: And to your point just briefly on why we feel we need to take it. Again, I am not familiar with the business you are in, but again with the food business clearly people have to eat, people are going to make choices every single week and find a place that they want to do business. It is a recurring, repetitive transaction for them. So for that segment of the customer and, again, as you see it is a growing segment for most of our demographics across the spectrum, as more and more people are induced or incentivized to use credit by the credit card company. Anyone who wants to use debit or wants to use credit won't consider using us if we don't take their method of payment. [LB174]

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SENATOR PANKONIN: Okay. But my question to you would be what if you had a policy, it is 5 percent less on your bill if you pay with cash or check? Couldn't you do that as a business strategy? [LB174]

STEVE MOSKOVITS: You are not allowed to under Visa to charge higher amounts to anyone using a credit card. You would not be allowed to continue to take credit. [LB174]

SENATOR PAHLS: Steve, I have a question then. There are some grocery stores I go to that will give me a discount on their gas, one is HyVee. You get three cents off or whatever or sometimes ten cents off a gallon. You go to Bakers, you go to another Kwik Shop. Let's say I buy \$100. I use a credit card, how much is that costing you roughly? [LB174]

STEVE MOSKOVITS: If you spend \$100 in our store? [LB174]

SENATOR PAHLS: And I use a credit card, how much is that going to cost you? [LB174]

STEVE MOSKOVITS: You are looking at somewhere, depending again on which type of card you use, it could be between 1.5 and 2 percent. So on, you are talking about \$100, \$2. [LB174]

SENATOR PAHLS: Would it be possible to, if I don't use the card, give me half the money back? Am I just making this too complicated? [LB174]

STEVE MOSKOVITS: Well, again, I would have to explore that. I know that gas stations in the past have done discounts or incentives to use cash as opposed to a surcharge. [LB174]

SENATOR PAHLS: I was just trying to figure are the other options. Okay. Over here. [LB174]

SENATOR CARLSON: Senator Pahls. Steve, sitting here listening to you it sounds like taxation without representation. It sounds like other people are making the decision for you, and aside from what Senator Pankonin indicates they do, just tell me what are the advantages of allowing credit cards other than everybody else is doing it? [LB174]

STEVE MOSKOVITS: Well I think again for a large segment of customer that has become their method of payment. For example, debit card has replaced checks for a lot of people. They don't carry a checkbook. All they want is one statement at the end of the month. They don't want to have to write checks. Again, some people get float when they use credit and that is something that they have found attractive. Different reasons

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for a variety of different customers. But again what we found is a marked increase in the customers that request...and believe me when we put it in it was a struggle. We frankly really looked hard and probably weren't the first grocery store chain to put it in for that very reason. It is an extra cost to doing business and the grocery business every penny counts. [LB174]

SENATOR PAHLS: Senator Langemeier. [LB174]

SENATOR LANGEMEIER: Chairman Pahls, thank you. Thank you for testimony, Steve and they kind of alluded to what my question is, if I am getting 2 percent back on my credit card why don't you give me 2 percent back on cash and I would be more than happy to pay cash. But my real question is, on here you gave us the electronic processing from 2002 the \$26,000 to the 2006 \$52,000, what would be some correlating numbers for bad checks and debt in that same group? [LB174]

STEVE MOSKOVITS: For that particular store, and I did look at that, and our bad checks have been relatively flat for that particular store. What you find with checks, you know the people who write bad checks will continue to write bad checks and they generally aren't interested in using the credit/debit approach. What you find are you have shifted the customers who are writing good checks to a different media of payment and, again, when you talk about checks there is a couple of big differences. With the bank we do negotiate what we are able to pay for checks that they process. It is a fixed, it is not a percentage, and lastly we have the right when it comes to checks to scrutinize checks, and to turn checks down, and help reduce our bad check loses which we don't have with the credit transactions. But to answer you question on this particular store which is a lower demographic store, over the last three or four years I looked and out bad check losses have been very flat. And so we have not seen a corresponding help, if you will, in reduction in bad checks. [LB174]

SENATOR LANGEMEIER: Thank you. [LB174]

SENATOR PAHLS: Senator Pankonin. [LB174]

SENATOR PANKONIN: I have got a follow up question, Senator Pahls, I thought of. Steve, in other words you feel like you have no alternative businesswise to go to someone else and say can you give me a better rate or whatever on these transactions. In other words, you feel there is just not business alternative you have? [LB174]

STEVE MOSKOVITS: Well I will tell you this, we have it so we have changed our processing bank, and we have looked at three or four other processing banks, and it is quite clear that the interchange that you are charged, that they are charged by the Visa bank is a pass through and it is not negotiable. That is a pass through from above that they just pass onto us and that is nonnegotiable. But what they charge us to handle our

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transactions is something that they can negotiate based on the volume, where again the associations that we can put together to give more volume to them. [LB174]

SENATOR PANKONIN: So the only alternative you have is to raise prices, obviously, to try to cover for the expense. [LB174]

STEVE MOSKOVITS: That is the ultimate result. Yes. [LB174]

SENATOR PANKONIN: But doesn't everybody else then if everybody is trying to take these cards? Isn't that level playing field for the rest of the industry then? [LB174]

STEVE MOSKOVITS: It may be a level playing field but consumers are the ones...and ultimately it is not necessarily level within the classes of consumer then either and that is one of the things to look at. If you are saying that you have rewards program where you get miles the people that are buying with food stamps, and the people that are buying with cash and check, have the same increase in overall prices because we are not charging a different price to a different person based on the median which they pay. So the overall level of prices are higher. So if someone who is paying with food stamps, for example, is potentially paying higher for groceries than they would have otherwise and, again, looking at the third part of the bill which addresses simply the interchange fee on tax, that seems something well within the jurisdiction of the state that to us should be something that most people could agree on rather easily, I would think. [LB174]

SENATOR PAHLS: Senator Langemeier. [LB174]

SENATOR LANGEMEIER: One more quick question. Now I am just curious. We have talked a lot about banks and you talked about the click fee as they process this. Can you do that through a credit union? [LB174]

STEVE MOSKOVITS: Could we process... [LB174]

SENATOR LANGEMEIER: Could you bank at a credit union and run your process through for your Visa or does that have to be a bank? [LB174]

STEVE MOSKOVITS: I guess I am not sure. I don't know that. We run our ATMs through a credit union. I am not sure we couldn't. But, again, I think based on the relationships in the economies we have found that we have got a better deal from larger banks as we have negotiated and looked at that. But I am not sure if we had any credit unions. [LB174]

SENATOR LANGEMEIER: Just curious. Thank you. [LB174]

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SENATOR PAHLS: Senator Gay. [LB174]

SENATOR GAY: Steve, you had mentioned Papillion is the area I am from and there is a Target, they are always pushing their cards on you every time you check out, you want a card. You have got Baker's. You have got your place. You have got Wal-Mart, the whole thing. So the competition is very tough and I know this is something you cannot just say well, we don't want to participate. But I guess it goes back to what Senator Pankonin was talking about, there are other opportunities negotiating. I didn't know you couldn't negotiate, that is inflexible with the card companies. That sounds tough. But good sized business you could be negotiating with some of the banks, couldn't you and say we want a lower fee? Because you are no small business. [LB174]

STEVE MOSKOVITS: Well and I will tell you we have done that and that is why when you look at 2005-2006 on my sheet you see a reduction. That is because we did change our processor, and we have stemmed the tide on increases, and actually saw a reduction. It is not just us. We have pooled with some other large retailers as part of an association, if you will, and have a contracted rate for all parties. And so we have gotten the click charge down to, believe me, numbers I never would have thought we could have. That being said, as the usage is the usage, you are still twice what you were just four or five years ago. We have done that simply to keep it from increasing and to reduce slightly. That piece is a small piece compared to the interchange fee that is the pass through cost. [LB174]

SENATOR GAY: Thank you. [LB174]

SENATOR PAHLS: Thank you, Steve, appreciate your testimony. [LB174]

STEVE MOSKOVITS: Thank you. [LB174]

SENATOR PAHLS: Next proponent. I am going to ask you to spell your name, please. [LB174]

LARRY BAUS: Good afternoon Senator Pahls, members of the committee. My name is Larry Baus, L-a-r-r-y B-a-u-s. I am an owner/operator of two neighborhood grocery stores here in Lincoln. I have been in the grocery business over 40 years. A lot of changes have happened in that amount of time. One of the things that as Steve talked about, and I won't try to go over the same testimony that he had, but kind of give you a new perspective as a small business person, one of the changes we have had is credit cards. We hesitated about taking credit cards about 12 years ago for the same reasons. We knew it increased our costs, but our customers were the ones that told us to take credit cards. They kept coming in and saying do you take Visa, do you take Mastercard and at the time we said no, we don't. But we also saw a slight erosion of our sales so at that time we decided to put credit cards in. And there is an expense involved in putting

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the credit card machines in themselves and the transaction fees with the bank and everything else that goes with that. It does increase the cost of doing business, but it did help us to keep our sales from eroding. Ten years ago about 5 percent of our business was credit cards. Today it is about 35 percent of our business, or total sales. That transfers to about a 2 percent increase in the cost of doing business and our only recourse, obviously, is to raise prices. And that is an industry wide problem or situation with increasing the cost of goods, and Steve alluded to a lot of our customers are not credit card users. Obviously 35 percent of them are. So the other portion also pay for that increase and that includes fixed income people, lower income people as well. What we are looking for with this legislative bill is not to fix the credit card system necessarily, but to allow disclosure so we can see what kind of fees we are paying. So we have some recourse and possibly, at some point, we can affect some change in the industry. But it would give us a little more control over what we are trying to accomplish. As it currently stands we have been force fed these fees and we have no recourse and little or no control over them. This is the first step in trying to fix the system that is really, really unfair to retailers and consumers alike. With that, is there any questions? [LB174]

SENATOR PAHLS: Do we have any questions? Senator Pirsch. [LB174]

SENATOR PIRSCH: With respect to that narrow question of inadequate disclosure, this bill would function to require credit card companies and the member banks to provide a copy of the rules that merchants agree to abide by. In your perception is that a problem? Is there a problem that merchants are not having a clear understanding of what the agreement, as it were, what the fees are and the fee structure when they get involved with these type of processes? [LB174]

LARRY BAUS: Yes. That would be fair at this point because we do not know what the fees are charged by Visa, Mastercard, Discover. We know what our fees are through our bank, what our transaction fee is, or as Steve said the click fee. But the actual fee for each type of card, we know it is higher for certain types of cards. We don't know what that is and it has not been disclosed to us. [LB174]

SENATOR PIRSCH: Yeah. Could you relate, because I think you are pretty good example of an individual. You have two kinds of a small business, right, two neighborhood groceries here in Lincoln and are these are just general stores much along the lines of... [LB174]

LARRY BAUS: Yeah. They are neighborhood grocery stores. One is Village Market at 13th and Arapahoe, and the other one is at 33rd and A, Wagner's Food Pride. [LB174]

SENATOR PIRSCH: Okay, and this was about 12 years ago that you first started flirting with the idea of... [LB174]

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LARRY BAUS: Putting credit cards in, yes. [LB174]

SENATOR PIRSCH: And when did you then go ahead and make the determination that you were going to go ahead and accept Visa and Mastercard? [LB174]

LARRY BAUS: It was about 12 years ago. [LB174]

SENATOR PIRSCH: Twelve years ago. Okay, and you can either speak to back then or as it exists here today, I take it you have been consistently current the whole 12-year period with Visa or Mastercard? [LB174]

LARRY BAUS: Yes. [LB174]

SENATOR PIRSCH: And when you made that determination then what types of contact did you have then as far as being made aware of what the fees and the schedules are going to be for using this service? [LB174]

LARRY BAUS: Well at that time, we were told of course about the transaction fee with the credit card processor that we chose at that time, it was Concord I believe, and we were going to charge the grocery's rate, discount whatever that would be... [LB174]

SENATOR PIRSCH: Who were you interacting with at that point? Who was disclosing this? [LB174]

LARRY BAUS: Concord was the credit card processor. [LB174]

SENATOR PIRSCH: Okay. [LB174]

LARRY BAUS: And at that time they told us what the rate would be but, at that time, I don't believe there were even rewards card even in existence at that time, or what that fee would be. I can't recall exactly. But it was pretty straight forward. It seemed straight forward to us at the time. But we were not aware of this, you know, there is 1,000 page rule books that are in existence that we were not even told about at the time. And at the time, it seemed like as a small portion of our business and it was something we were not necessarily concerned with. We thought, at the time, also that this is great, this is going to take care of some of our bad check problem and our check processing costs as it turned out it really has not done that. I have to kind of relay the same story that Steve had. I looked at the same things with our bad checks and the bad check writers are still there. They haven't gone away. The people who are fiscally responsible have just changed from checks to credit cards and, in essence really, it would have been cheaper for us to go with checks if it had been possible. [LB174]

SENATOR PIRSCH: Yeah. But I wanted to focus just on that because part of the bill

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would call for greater disclosure and so that is why I want to key on. And you commented that, at the time, you interacted with this Concord processor, which I think you have indicated you have changed over the years. But at the time that you interact with your processors they never indicated to you, or did they indicate to you, that there was additional rules that may or may not apply, a rule book? I think you refer to it as a 1,000... [LB174]

LARRY BAUS: We were not made aware of that. No. [LB174]

SENATOR PIRSCH: Okay, and how did you first become aware that the rates that you understood to apply would not apply? [LB174]

LARRY BAUS: It was kind of just through communication with other retailers and with our (Nebraska) Grocery Industry Association and all these fees were different and they were changing, and we would get this long list of credit card fees at the end of the month from our processor and they were significantly growing and... [LB174]

SENATOR PIRSCH: So you would notice that the fees were higher than that which you thought they were going to be? [LB174]

LARRY BAUS: Right. [LB174]

SENATOR PIRSCH: And when did that take place that you noticed that the fees were not what you thought they were going to be when you originally signed up with Concord? [LB174]

LARRY BAUS: It wasn't just one big revelation. It was over a period of time where you just said well, there really a lot more than we thought it would be, and as it became more of a larger portion of our business it became more of a concern to us, and that is when we started looking at it and addressing it. [LB174]

SENATOR PIRSCH: When did that occur about, do you remember exactly? [LB174]

LARRY BAUS: I can't tell you when that would be. It is fairly recent I would say. [LB174]

SENATOR PIRSCH: Okay. Thank you very much. I appreciate it. [LB174]

LARRY BAUS: Thank you. [LB174]

SENATOR PAHLS: Seeing no more questions thank you for your testimony, Larry. [LB174]

LARRY BAUS: Thank you. [LB174]

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KATHY SIEFKEN: (Exhibits 2 & 3) Senator Pahls and members of the committee, my name is Kathy Siefken, Kathy with a K, Siefken is S-i-e-f-k-e-n, representing members of the Nebraska Grocery Industry Association and I am sort of batting clean-up here with the grocers and then other people will follow. I am trying not to repeat what has already been said so you have got a handout. There are some statistics and some information that has been talked about already today, but this way you have got it in writing in front of you. A couple of the other points that I wanted to point out, Steve had talked about you get a statement and that is one of the handouts here, you get a statement at the end of the month and this is the statement for our...we also process credit cards as a retailer because our members want to pay for a few things. We don't do it very often because we don't encourage it. The only reason this is as high as it is because it was during January when we had our silent auction at our legislative reception and people wanted to pay with credit cards, and there is a perfect example of if we hadn't had credit cards available I am not sure that some of those people would have known how they were going to pay for the items that they got that evening. But I just wanted to show you if you look on page 1, in the second series of numbers there, it shows the different interchange rates and it has it listed Mastercard, Visa and if you look down in the second section there, Visa. If you follow that very first one across that is the most expensive transaction there is and if you go over to the count we had more of those type of credit cards than any other credit card and this is typical. People are being enticed into using the reward programs because they get incented to do that. Anyway I just wanted to show this to you so you had a better picture in your mind as to what was going on. Actually what LB174 does is three things. One of them is it would require that the retailers that are accepting credit cards be provided with a copy of the rules. The rules are a document according to our national. It is about 1,000 pages. No one has a copy of the rules. As a matter of fact on July 19, and it is in here someplace, on July 19 of last year there was a Senate Judiciary Committee hearing and the senator from Pennsylvania who is chairman of that committee, Senator Specter, asked Visa and Mastercard to provide a copy of the rules and they said you betcha, we will do that. We still do not have a copy of the rules and when you have a segment of your business that is as big as the Visa-Mastercard is in the grocery industry the least they can do is provide us with the rules and that is what this bill does. And providing us with a copy of the rules, they don't have to give it to each and every one of us. All they have to do is put it on the Internet so that we have got access to it. That is what this bill says. That we should have access to the rules. I don't think that is asking for too much. It also says that if they change the rules since we are the other player in this game we should have notice of any changes to those rules. We don't get notice of any changes. That is just not right. As a matter of fact, I found out this morning that Rule 96 apparently has been changed, and Rule 96 has to do with the predetermined...that is the segment of this bill that we haven't talked about yet, but it has to do with the predetermined limit on the credit cards and they have changed that. We have no idea if they have changed it to help us or to hurt us. We don't know. Chances are we won't get notice of that. Again,

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what is right about that? If there are rules and we are one of the parties in the game I think we should know what the rules are. The other thing that I wanted to add is that the interchange fees that are being charged, according to our national association, are over \$30 billion per year. That is a lot of money. Only 13 percent of that \$30 billion is actual processing costs and this is research that has been done, again, by our national. What that equates to is an average of about \$300 per year per family for every family in the United States. This is huge. Another statistic I want to leave you with is the fact that since 2001 the rates have increased 85 percent. In any other business, that I am aware of, when your volume of usage goes up the cost usually goes down. As the grocers testified earlier, their costs have gone up to half of their transactions are now via credit card. Yet we have seen an increase in rates up to 85 percent and those are the monies that are used to pay for the junk mail and for enticing people into using rewards cards and to pay for those trips. And basically, what that equates to the people in Nebraska when it comes to food, which is a basic necessity, the cost of food is being increased approximately 2 percent across the board and the low income, the people without credit cards, those are the people that are helping to subsidize the fees that are being paid to credit card companies. So with that, if you have any questions I would be happy to try to answer them. [LB174]

SENATOR PAHLS: Senator Pankonin. [LB174]

SENATOR PANKONIN: Thanks, Senator Pahls. Kathy, I have got several questions. You talked about being a national issue and your national association has worked on. What is the status on the national legislation? [LB174]

KATHY SIEFKEN: We have talked to Senator Hagel. He was instrumental in getting the Senate Judiciary Committee hearing last summer. We are still waiting. [LB174]

SENATOR PANKONIN: Okay. [LB174]

KATHY SIEFKEN: The federal government moves at a very slow pace. [LB174]

SENATOR PANKONIN: I know that. Even if you had a copy of this 1,000 pages of rules what would you do with it? [LB174]

KATHY SIEFKEN: We would turn it over to our attorneys and have them look at it, and probably bring to light all of the rules, even those that are questionable. [LB174]

SENATOR PANKONIN: So you just told me the federal government couldn't get a copy of the rules. No one can get a copy of the rules. I don't know. You have got lawyers. Why don't you get a copy of the rules. That is interesting. The third thing is that it is your understanding, as well, if a merchant signs an agreement to take cards they cannot give a cash discount then. [LB174]

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KATHY SIEFKEN: That is true. As a matter of fact if I can give you a for instance... [LB174]

SENATOR PANKONIN: So to me if we try to pass a law to allow that the problem puts the most pressure on these companies more than anything. [LB174]

KATHY SIEFKEN: That would help. [LB174]

SENATOR PANKONIN: Because I mean like Senator Langemeier said if he went in, if I went in...I know I use these Infinity cards. Why not? I know how the system works, but if I could get a cash discount I would take it every time. [LB174]

KATHY SIEFKEN: But it is illegal for us to do that. As a matter of fact, one of my small retailers in Omaha called because his third party provider came into his store because he was turned in by one of his customers because he was going to surcharge because he couldn't go the other way, and the third party processor came in and threatened him with a \$10,000 fine and they were going to pull his authority to take credit cards. So they mean business. [LB174]

SENATOR PANKONIN: So wouldn't that solve it more than this stuff if you could give that cash discount? Do you think your industry would like that? [LB174]

KATHY SIEFKEN: I am not sure if it would solve it or not. We still don't have the rules. [LB174]

SENATOR PANKONIN: Well if the federal government can't get the rules why would they give it to the state of Nebraska? [LB174]

KATHY SIEFKEN: If everybody jumps on board, and the more people that demand it, the more apt you are to get the rules. In addition to that, there are 20 other states that are introducing this very legislation. [LB174]

SENATOR PANKONIN: Has it passed anywhere in your knowledge? [LB174]

KATHY SIEFKEN: It was just introduced this year. No. I am not sure even hearings have been held on all of them. [LB174]

SENATOR PAHLS: Kathy, I have a question. I am a little bit confused now. You are telling me it is illegal... [LB174]

KATHY SIEFKEN: I am sorry. [LB174]

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SENATOR PAHLS: You are telling me it is illegal to give me a cash discount? [LB174]

KATHY SIEFKEN: No, I am telling you it is illegal for us to surcharge. So if you come in and you want to use your... [LB174]

SENATOR PAHLS: Yeah. I see what you are saying. [LB174]

KATHY SIEFKEN: Because what we do is we set what the price is and if you use a credit card we couldn't surcharge you for \$100 the \$2.50 that is would cost us to process that transaction. [LB174]

SENATOR PAHLS: Okay. To me the answer is like I know a gas station in Omaha you go there, they give you 3 cents to a gallon if you pay cash. [LB174]

KATHY SIEFKEN: I am not sure that we can do that. [LB174]

SENATOR PAHLS: I have seen people in the audience...I better not tell this too loud because I will lose my discount. Okay. I will move on. [LB174]

KATHY SIEFKEN: I think it is against the...those hidden rules that we haven't been able to read, I think it is in the rules that you can't do that. [LB174]

SENATOR PAHLS: Oh really. Okay. I know they have been doing this for a while, but I will move on. Senator Gay. [LB174]

SENATOR GAY: I just had a question on that. They keep talking about the discount and I see them, too. Are those people that have their own banks or they are so big that they can go cut a deal with the credit card company? Sometimes you go to a store and they have a gas pump outside and get 3 cents off per gallon if you do this or whatever. Do they have their own bank or what are they doing? Like other case Target does that. They are always pushing their credit card and then say you can get a 10 percent discount. So it is being done. Maybe we are talking different... [LB174]

KATHY SIEFKEN: Well they have their own credit card but that is a different bank. I don't know if they own their own bank. Jim Otto is here. Maybe he knows. [LB174]

SENATOR GAY: Maybe they are just so big they can do that. I don't know. [LB174]

KATHY SIEFKEN: It could be that they are so big they can do that and they may be giving up their portion of the fee to entice people to come in. [LB174]

SENATOR GAY: Well why would they be pushing those cards all the time if they weren't getting something out of it? It is not for my convenience. If I were... [LB174]

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KATHY SIEFKEN: But there are some credit cards out there that don't charge you the \$30 late fee and if you are late you get charged \$2. Those are the cards that people will go in and shop in those stores just because they know if they are late they are not going to get dinged \$30-\$35. [LB174]

SENATOR PAHLS: You are enlightening me because I didn't realize all these things are out there. [LB174]

KATHY SIEFKEN: That is what we want to do is enlighten you. [LB174]

SENATOR PAHLS: Yeah, I know but I don't use credit cards for the most part. Senator Pirsch. [LB174]

SENATOR PIRSCH: I just want to have a sense of this magnitude of the problem as you survey it. I think one of the retailers had previously testified other than, I think it was the CEO of No Frills had testified that it was his second biggest cost driver other than health care cost, I think insurance. Is that, speaking on behalf of Nebraska Grocery Industry, do you find that to be also a major cost driver in you industry? [LB174]

KATHY SIEFKEN: Yes. Absolutely. When Larry was up here testifying he told you that he went from a \$4,000 per year cost to \$30,000 and that is a small store. It is happening statewide, and as a matter of fact until the last couple of years the small grocers that would call and talk to me about what should I do with credit card, who should I go with, should I get it? We told them hold off as long as you possibly can, do not take credit card until you are at a point when you are losing customers and now I think we are almost 100 percent, I think, everybody is taking credit card. Everybody is taking credit card. So yes, it effects everybody. [LB174]

SENATOR PIRSCH: Okay, and with respect to the issue of disclosure then what is the typical...do you have familiarity with what is being as a new grocer nowadays are adding these, are you familiar with what types of material or marketing is going on to sign up the merchants, or what is the state of disclosure currently typically? Do you have an understanding of that? [LB174]

KATHY SIEFKEN: The state of disclosure, what are they providing now? [LB174]

SENATOR PIRSCH: Well the purpose of the bill is to create greater disclosure is what I understand it to be. And so I am trying to get an understanding of what the baseline is now. What is happening now that is inadequate if you understand? [LB174]

KATHY SIEFKEN: Right now when a new merchant signs up for Visa/Mastercard they are given a form to sign that tells them that their rate is going to be anywhere from, I

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think our grocers are 1.2-1.4 and any other rates are listed in the rules which have been provided to them. Now here is the kicker, you don't get to take Visa or Mastercard until you sign the agreement but they still don't give you the rules. Now they say that they will give you the rules if you don't share them with anyone. I don't know the legal language for that. You probably know that, the nondisclosure. So there is a nondisclosure clause in there also. So even if you do get the rules you can't share them with somebody down the street, you can't talk to anyone about them. So we are just asking for the rules. [LB174]

SENATOR PAHLS: Find the person who has the rules. Senator Carlson. [LB174]

SENATOR CARLSON: Senator Pahls. Kathy, if you look at the third item here that this bill would ask that they charge not be applied to the tax portion. I can understand that. It is just a total at the bottom and that is what it is based on, and I don't know enough about programs and so forth to realize if this is a problem or not. Is it feasible that the added expense of being able to do that is going to end up raising what you are charged by the bank if this is broken up? [LB174]

KATHY SIEFKEN: Potentially it might, potentially. We don't know and there is really no way to know that. All of the various systems in the front ends of the stores would have to receive another download. The software would have to be written. But if Nebraska would push this it would roll over into other states. Somebody has got to start and this is basically protecting the consumer. Going back and... [LB174]

SENATOR CARLSON: Well that is one thing when you bring the consumer because you mentioned the consumer before and they go for these reward cards. But if we are stupid enough to do that you can't solve that and this bill isn't going to solve that. [LB174]

KATHY SIEFKEN: Well that is true and you know people kind of will go one way or the other. They will either say okay I am done with this, I have had enough, I'm not going to play into this game or they are going to say okay, everybody is in this game and I am going to get everything that I can. But you know who that leaves at risk? The very people that can't afford to subsidize the credit card companies, the low income, the people that aren't eligible for credit cards. [LB174]

SENATOR PAHLS: Senator Gay. [LB174]

SENATOR GAY: Thank you. I know you are speaking for the Grocery Industry. But I guess the question would be why then, it is a high volume, high transaction, probably narrow margin industry, but when I go to an Applebee's or a lot of these are national again, I can't write a check anyway. They don't want me writing a check and they want me to use my debit card. They want me to use my Visa card. Why is that and everyone

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that has testified so far has been from that industry you are talking about? Why are they then going the complete opposite way and saying don't write a check here? I know they don't want a bounced check and fool with all their big national companies. But they are going completely the opposite way and here you are telling us that this is all bad, yet they continue to do that. What are they doing different? What are they getting that you are not getting? [LB174]

KATHY SIEFKEN: I can't tell you that because I don't represent the restaurant industry. But Jim Otto is here and he is going to be coming up to testify. [LB174]

SENATOR GAY: All right. Thank you. [LB174]

SENATOR PAHLS: Okay. Senator Langemeier. [LB174]

SENATOR LANGEMEIER: Chairman Pahls, thank you and thank you for your testimony. What can we do to these credit card companies if they just say nice law, nice green paper? I guess at that point it would be yellow but what are you going to do to them? [LB174]

KATHY SIEFKEN: There are \$10,000 penalties in here, so penalize them. [LB174]

SENATOR LANGEMEIER: Who is going to penalize them? How are we going to get that collected if we can't get a piece of paper from them? [LB174]

KATHY SIEFKEN: I don't know. How would we do that? When you get them into the court system maybe... [LB174]

SENATOR LANGEMEIER: Who is going to get them in the court system? Is the state of Nebraska going to take them to court? I don't think so. We are not going to spend tax dollars on this. Who is going to take them to court to enforce this? I am well aware it is the Attorney General but I am waiting for an answer. [LB174]

KATHY SIEFKEN: The Attorney General. [LB174]

SENATOR LANGEMEIER: That is one more reason to throw this away today and disregard it. We don't need one more thing for the state to prosecute that we can't get on a federal level. [LB174]

KATHY SIEFKEN: But it will save the taxpayers in Nebraska a lot of money in the long run. One court case via the Attorney General versus a 2 percent increase in the cost of goods in everything that is sold in this state. So if you are looking to protect the citizens of the state of Nebraska I would say that that would be the reason to go ahead and pass this law. [LB174]

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SENATOR LANGEMEIER: Thanks for your testimony. [LB174]

SENATOR PAHLS: Thank you, Kathy, appreciate your testimony. [LB174]

TIM KEIGHER: Good afternoon. It is still afternoon. Chairman Pahls, members of the committee, my name is Tim Keigher, that is K-e-i-g-h-e-r. I appear before you today in support of LB174 on behalf of the Nebraska Petroleum Marketers and Convenience Store Association, and check with you afterwards. I want to know that one where you are getting that discount at. I'll try not to repeat anything that has been said. Maybe try and help clarify a few things. And the chargeback issue is one thing that, at least in the petroleum industry, under current practice when a customer purchases gasoline using a credit or debit card, the credit card companies are preauthorizing that transaction. And Visa and Master card set a limit of \$50 and \$75 respectively. Some pumps are able to shut a person off at that dollar amount. In fact I have had friends complain to me that as the price of gasoline went up, first of all they complained about that which I have a lot of control over. But secondly, they are driving SUVs and they go to the gas station, and the pump is shutting off at \$50 and they want to get \$65 or \$70. [LB174]

SENATOR CHRISTENSEN: That is a quarter of a tank. [LB174]

TIM KEIGHER: Yeah, a quarter of a tank, yeah. The other things, the interchange fee plus the processing fees, at least in the petroleum industry, account to about 2.5 and as high as 4.5 percent of a charge on the retail price of gasoline. So at \$2.50 a gallon gas that is anywhere from 6-10 cents a gallon. Seventy percent of the transactions for gasoline are credit card these days. Ten years ago that used to be anywhere from 55-45 to 60-40. In regard to the question that has come up, facilities that are offering a discount. I think if you look at the grocery stores as an example. They are offering a discount for shopping with them. If you shop with them you get a discount on gas. It is not whether you pay with credit or you pay cash, it is being loyal to them. So I think there is a distinct difference there. At least in the fuel industry, you are being charged the discount rate on the fuel taxes. Okay. The state of Nebraska's fuel tax is 27.1 cents a gallon. The federal tax is 18.4 cents. That is 45.5 cents. So 2 percent on that would be almost a penny. I guess with that...not trying to repeat anything. We are just trying to bring light to this issue. It is a national thing with our national association, the Petroleum Marketers Association of America and the National Association of Convenience Stores. I know that there are several states that are pushing similar legislation. It has been difficult to get something done on the federal level and we are looking to see if anybody is willing to help us in this plate. With that, I'll try and answer any questions you may have. Oh, I guess one thing I could add, it is illegal, the contract, to my understanding being told by an attorney in DC that represents the retail fuel industry, it is illegal to surcharge for a different price between a gallon of gas for cash and a gallon of gas for credit. Now you talk about they are offering a discount for cash, that has been

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questioned as to whether that has been legal or not. It does go on. I know I have had members call as the price of gas has went up and say hey, the credit card fees are eating me alive but I have got a percentage of people who want to pay with cash and I want to encourage people to pay with cash, can I do that? The state of Nebraska Weights and Measure Department does allow a discount for cash and the reason that they...well, they don't allow you to give cash back. You have to post the price of the cash and the credit transaction. Prior to my time they passed that law and I was told that the problem was a customer would come in, pump gas at \$2.50 a gallon. He was going to pay cash and he was going to get a nickel discount and if the customer didn't ask for the discount back the clerk was keeping it. So we have some rules that try to prohibit that. But with that, I will try and answer any questions. [LB174]

SENATOR PAHLS: Okay. Senator Pirsch. [LB174]

SENATOR PIRSCH: I'll just because you are in a slightly different industry. One that is not probably as capital intensive as grocery stores and so probably more people move in and out of your industry. What is your understanding of the typical exchange of information or communication that the card issuers, processors have with the owners of gas stations or petroleum marketers? [LB174]

TIM KEIGHER: I would agree with the previous testifiers. I have worked on looking at trying to put credit card programs together for the members of our association. It is very difficult to try and figure out what all the fees are. There is a laundry list of them. I think things do change rapidly. It is very difficult to compare one processing program to another and I have heard my members complain about that. They will get a charge that comes on their statement that they will say well, I was never aware that this type of a transaction had a different charge than the others. [LB174]

SENATOR PIRSCH: But I mean before the actual bill comes to us. I am trying to get an understanding of what up front information as when you sign up with us this will be the fee schedule that we will impose. Is something disclosed at all right now in all cases, and what is that if you do know? [LB174]

TIM KEIGHER: You know I have never seen a copy of it myself. I think that as the previous testifier said, if you are in the retail business credit cards are very prevalent in retail today, and I think that too many people are probably going in and signing on the bottom line saying I know need to take credit cards to be in the retail fuel business, the grocery business, whatever business it is and probably aren't reading what they get now, let alone any rules that they are unaware of. So I am not positive what all the rules are. [LB174]

SENATOR PIRSCH: Okay. Thank you. [LB174]

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SENATOR PAHLS: Seeing no more questions, thank you, Tim, for your testimony. [LB174]

TIM KEIGHER: Thank you. [LB174]

JIM OTTO: (Exhibit 4) Senator Pahls, members of the committee, my name is Jim Otto, O-t-t-o. I am here on behalf of the Nebraska Retail Federation and the Nebraska Restaurant Association. I am a registered lobbyist for both, in support of the intent of LB174. First of all, I will be very, very brief. I wanted to just simply point out the third portion of the Statement of Intent of the bill, and that was what Senator Carlson brought up that separating the charge for tax. And I just wanted to point out, first of all my apologies to Senator Langemeier. He's already been through this on LB423. There was a bill to actually take the amount of sales tax collection allowance back to the way it was prior to the year 2001. Somehow, I don't understand it, that bill got indefinitely postponed. It might have something to do with \$3.5 million. I don't know. That could have been it. But I do want to take any opportunity I can to explain just exactly what occurs. In the grocery business you have heard maybe 30 percent of credit card transactions, 70 percent in the petroleum gas business. We think somewhere around 60 percent of all retail transactions, restaurant transactions are credit card transactions. The point we want to make is on a \$100 sale in the city of Lincoln or the city of Omaha there is \$7 in tax. The average rate to the credit card company is about 2 percent. So our point is that retailers and restaurants actually remit more sales tax than they collect after you take the discount fee on the sales tax portion. The third point in this bill tries to address that in a different way. We tried to take it back to the way it was prior to 2001 when there was more reimbursement given to the retailer for collecting the tax. Our point is that retailers and restaurants are basically the tax collectors of sales tax for the state of Nebraska and they don't get reimbursed anywhere near what is cost them. In fact, they don't get reimbursed the amount that they are actually submitting. With that, I'll submit to any questions. [LB174]

SENATOR PAHLS: Do we have any questions? Senator Langemeier. [LB174]

SENATOR LANGEMEIER: Thanks for your testimony. The other bill had come under bad light. Senator Janssen was part of that so I am not alone. If we take that third component in this, and I know it is a little different because you still won't be whole even with the third part. You will just be losing less on the sales tax on the credit card portion, correct? [LB174]

JIM OTTO: Correct. [LB174]

SENATOR LANGEMEIER: Okay. That is what I want to clarify. Thank you. [LB174]

SENATOR PAHLS: Senator Carlson. [LB174]

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SENATOR CARLSON: Senator Pahls. In your initial statement, Jim, I don't know, what is the different between supporting a bill and supporting the intent of the bill? [LB174]

JIM OTTO: Well I'm not sure the bill..the intent of the bill...well, you brought up a good point, Senator, that I don't know for sure if you can actually separate that, if that is a feasible thing to do, to separate out that tax. I mean I have to say I think that is pretty tough. So we do support the intent. [LB174]

SENATOR PAHLS: Senator Gay. [LB174]

SENATOR GAY: Question then, why are they encouraging... [LB174]

JIM OTTO: In the restaurant business I think it has proven, Senator, that you might buy more food, order another round of drinks, you might have a more tendency to do that if it is on your credit card than if you have to dig the cash out of your pocket. [LB174]

SENATOR GAY: So it increases the volume. [LB174]

JIM OTTO: Increases the volume, increases the sales tax. [LB174]

SENATOR GAY: So it is not a... [LB174]

JIM OTTO: And I think that they found that they did not lose any business. I think Applebee's is specifically one of the restaurants that does not accept checks. I don't know for sure how many restaurants do not accept checks. More and more of the chains are not accepting checks. Local restaurants will opt to. [LB174]

SENATOR GAY: A lot. [LB174]

JIM OTTO: But they have gone through the studies. [LB174]

SENATOR GAY: It increases volume. Right? [LB174]

SENATOR PAHLS: Seeing no more questions, thank you, Jim, for your testimony. Any more proponents? Opponents? How many opponents do I see? One, two. Okay. We have two. [LB174]

ROBERT J. HALLSTROM: (Exhibit 5) Chairman Pahls, members of the committee, my name is Robert J. Hallstrom. I appear before you today as a registered lobbyist for the Nebraska Bankers Association to testify in opposition to LB174. A lot of the issues that are contained within my testimony have already been touched upon with regard to what interchange is, what a payment card transaction structure is in terms of the merchant,

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the cardholder, the issuing bank, the acquiring bank, and the charges and fees that are associated with that type of transaction. So given the lateness of the hour I won't walk you through what a primer of Interchange 101 again. What I do want to make clear for the record is...and I appreciate Mr. Otto's comments candidly about why some of the restaurants are requiring credit cards to be utilized rather than checks or any other form of payment, and it is that less the perception be conveyed today that merchants get nothing out of this system. To the contrary they do. Merchants get a great deal and have gotten a great deal out of a system that has been put together by financial institutions in the payment system, spending a great deal of money for the infrastructure to respond to the demand of consumers requesting the convenience of being able to utilize credit cards and debit cards for the payment for goods and services. What the merchants get out of this system is the convenience of having that payment, quicker checkouts, they have reduced fraud, there are significant restrictions on the amount of liability that goes back against the cardholder which ultimately rests with the party that guarantees payment, and that is another benefit that the merchants derive from this system, which is guaranteed payment. Instead of taking a snapshot today and listening to the supporters complain about what the fees are that are associated, I would like you to roll back a few years when credit cards were first coming into play. Think about what the businesses were like then. The businesses were accepting checks, there were bad check charges, they had an accounts receivable department, they probably had more employees than they perhaps have to have today. There were significant costs associated, bad checks, carrying charges for inventory because they weren't getting paid as quickly. All of those things are part and parcel of the bundle of benefits that are derived by merchants from the use of credit cards. I would like to run through then real quickly the issues of the bill. Senator Janssen described three components of the bill. The first one is increased disclosure or transparency requirements. From everyone that I have talked to it appears that we may be living in the past in terms of crying foul with regard to the disclosure of the rules. What hasn't been noted today is there has been not only federal hearings with regard to the credit card and the debit card industry, but there has been class action litigation on a number of fronts with regard to some of these very issues. In response to that Visa and Mastercard, in particular, have made their rules available to the industry. There may be a nondisclosure agreement that has to be signed by the merchants but nonetheless by simply qualifying, signing that agreement and getting on the Internet and the web site for Visa and Mastercard, those rules as I understand them, are readily available. As a result, if that is in fact the case, which I would submit to you it is, there is no need there is no need for the first component of the bill. The second component is the restriction on chargebacks based on a predetermined amount certain transactions. In talking with the representatives in the industry, and Mr. Keigher suggested the problem that has been faced, in particular, by the petroleum marketers and the convenience stores, my understanding that there was a short term glitch in the system that resulted last summer when the gas prices spiked and the infrastructure did not catch up quickly enough. The rules did not catch up quickly enough to now acknowledge that a common standard fill up of your tank for automatic

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fuel tanks may have been more than \$50 which was the predetermined amount that was set by Visa. As my understanding from talking to people in the industry that that is or will be very shortly cured by changes to the infrastructure. Mastercard and Visa have both upped that amount to \$75. I would submit that is why you see the gas stations putting a maximum limit on how much you can put into the tank before the pump shuts off. I would also suspect that that is also a fraud deterrent as prices go up. I think I have heard Mr. Keigher testify at other hearings, rightfully so, that as the prices of gas go up the likelihood of people driving away without paying at all come into play as well. Thus the placement of those restrictions on the amount you can pump. Final issue has to do with removing the payment of sales tax from the calculation of the discount and the credit card or debit card transaction. I think as you might imagine that when you look at the way that the industry has evolved and the infrastructure has been put into play. What you need to understand, as I understand the system, is that the transaction is determined on a gross purchase amount. So the entire amount of both the purchase price, whether it is gas, whether it is food, whether it is groceries and the sales tax are all added together. That is how the system works today. You can probably try to put together a system that would bifurcate those two transactions. What you might see from the merchants perspective is that may be two transactions instead of one and therefore they will pay that click charge, they will pay that transaction fee so there will be some increased charges in that regard. They may also separate that out so that they have to ask the person to pay cash for the sales tax because the system won't accommodate that type of division of the transaction itself in the sales tax. That will slow down checkouts. That will also adversely impact the Department of Revenue audit trail, I would suspect, if we have to go to collecting sales tax on a cash basis. The bottom line is the systems do not currently accommodate. There would have to be a significant influx of investment to get the systems to accommodate that type of division of sales tax from the purchase price and, again, we probably see that the consumer ultimately will be inconvenienced, the merchants won't like it either and it will increase cost ultimately to the overall system. I might also just as a little backdrop let the committee know that some of these issues, number one, I think I do agree with some statements that were made earlier that this probably if it calls out for a solution at all needs to be done at the federal level. I don't think a state-by-state analysis and different changes are going to make much difference in this particular market. We may have differences of opinion on what that federal legislation should be or if it should be enacted at all. But that is where any solution of this type of nationwide system would have to come into play. But a lot of this started with the merchants crying for caps or price controls, and that ultimately I would suggest that maybe where they would like to go which defies the free market system that Senator Hansen referred to earlier in one of his questions. And so you look at that issue and we have had some experience, I think it is over in Australia, with putting caps on interchange fees and what they have found out from some significant studies is that the consumer did not benefit one iota. What happened was the merchant who is deriving all of the benefits I referred to earlier reaped all the benefits of a cap on interchange rather than the consumers. So we simply do not believe we should go down

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this path in any respect. We think some of the problems they have identified have already been resolved and that the sales tax issue is one that is beset by problems. Be happy to address any questions. [LB174]

SENATOR PAHLS: Bob, you are telling me though I can find the rules somewhere? [LB174]

ROBERT J. HALLSTROM: My understanding, Senator, is that if you sign with either the acquiring bank, which is the bank for the merchant, or Visa, or Mastercard whoever the ultimate company is issuing the card, that you sign a nondisclosure agreement and their rules are on the web site and readily accessible to merchants under those conditions. And my understanding also, you saw the heads nodding in the back of the room, just to clarify for the record is that there is a prohibition on surcharging for the use of credit cards, but you clearly can give a cash discount for people that pay cash rather than using a credit card. [LB174]

SENATOR PAHLS: You know I feel better right now. [LB174]

ROBERT J. HALLSTROM: And you should. [LB174]

SENATOR PAHLS: I was getting a little worried. I was messing somebody's life up. Yes, Senator Langemeier. [LB174]

SENATOR LANGEMEIER: Thank you, Chairman Pahls. Can you provide us that information to the web site to make appropriate contact on that? [LB174]

ROBERT J. HALLSTROM: I don't have it now, Senator, and I think that the one issue is that I don't think you and I can get access to that information. I think you have to be a qualified merchant that is in the system and one that has signed, as I understand it, the nondisclosure agreement. So it is not available to everyone in the public but the merchants can get them under those conditions. [LB174]

SENATOR LANGEMEIER: But you can get me to where that password or identity would have to be in place. [LB174]

ROBERT J. HALLSTROM: I can get you the web sites. I assume I can probably track down something of that nature and I will make every effort to do so. [LB174]

SENATOR LANGEMEIER: Thank you. [LB174]

SENATOR PAHLS: Seeing no more questions, thank you, Bob, appreciate it. [LB174]

ROBERT J. HALLSTROM: Thank you. [LB174]

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JULIA PLUCKER: Good afternoon Mr. Chairman, members of the Banking, Commerce and Insurance Committee. My name is Julia Plucker, J-u-l-i-a Plucker is P-l-u-c-k-e-r. I am a registered lobbyist appearing on behalf of the Nebraska Credit Union League. We actually agree with most of the testimony provided by Bob and the Nebraska Bankers Association. So I am real excited to be able to say that since most of the time we don't. [LB174]

SENATOR PAHLS: He just left. [LB174]

JULIA PLUCKER: Well good. I get a gold star from Bob today. I don't want to reiterate the points that he made but another quick point that I don't think is brought up. Our interpretation of this bill's language is that it requires credit unions, who by the way Senator Langemeier, are allowed to issue and process credit card transactions. So that answers your earlier question. It would require us to send notification to each and every merchant that could possibly swipe a member's card forcing them to predict where a member is going to shop. We also have heard that this information is available online at the credit card companies and we think that that is where the information should come from, not the issuing banks or the small credit cards which have been able to, because of the credit card system, compete with the larger financial institutions and issue our own credit cards. That is all I have got and I would be happy to answer any questions. [LB174]

SENATOR PAHLS: Any questions? Thank you, Julia, appreciate your testimony. Any more opponents? Neutral? That will close this...oh, I am sorry, Ray. You told me you were waiving away and I just waived you out of my mind. I am going to waive you back in. [LB174]

SENATOR JANSSEN: Thank you. I wasn't going to close but I will now. [LB174]

SENATOR LANGEMEIER: Can you sing a song for us? [LB174]

SENATOR PAHLS: Did you go back to learn that song for the Nebraska state song? [LB174]

SENATOR JANSSEN: No. This was more interesting. Thank you for your patients this afternoon in hearing this bill. It is a big problem. It is a problem probably across the whole United States and you look at the largest retailer in this country or probably in the world. Do they use a local bank? No. They use it as a transfer station and that particular company, as large as they are, have negotiated a special price, .9 of 1 percent. Compared to the lowest rate that any merchant can get is 1.2 percent. I wish Bob was still here. You know, Bob, I would go back to the old days anytime. Things were a lot simpler then. But if enough states introduce legislation like this and follow that idea

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maybe that will help the feds get off their can and look at into this. With that, I appreciate your indulgence in listening to my idea today. I appreciate it. Thank you. [LB174]

SENATOR PAHLS: Okay. Any questions for the Senator? Thank you, Senator. [LB174]

SENATOR JANSSEN: You bet. [LB174]

SENATOR PAHLS: That now concludes the session on (LB)174. [LB174]

SENATOR LANGEMEIER: Chairman Pahls, you are recognized to open. [LB113]

SENATOR PAHLS: Good afternoon. Senator, members of the committee, today I bring forth LB113. This would enact a new section in Chapter 8 article IV of the banks and banking statutes to provide that an industrial loan company or an industrial bank shall not establish or operate a branch in the state. An industrial loan company or industrial bank would be defined as a company that is chartered by another state to make consumer loans, or commercial loans or to accept deposit insured by the FDIC, but not to accept demand deposits, and owned by a commercial entity that is not a bank holding company or a financial holding company subject to federal law. Now there does appear to be some question of the provision of the statute 8-2105 that would effect this issue. It also in addition to the congress, United States government may also be involved in some of these issues dealing with this bill. So I think we do have an amendment coming forth. So I leave you to any questions. [LB113]

SENATOR LANGEMEIER: Are there any questions for Chairman Pahls? Seeing no questions, you are off the hook. Are you going to stick around and wait for closing? [LB113]

SENATOR PAHLS: Yeah. [LB113]

SENATOR LANGEMEIER: Go ahead. [LB113]

ROBERT J. HALLSTROM: (Exhibit 1) Senator Langemeier, members of the committee, my name is Robert J. Hallstrom. I appear before you as registered lobbyist for the Nebraska Bankers Association in support of LB113. LB113 has evolved out of some interest that has arisen when Wal-Mart and some other large retailers, commercial enterprises have made application primarily in the state of Utah to receive industrial loan company charters, and simultaneously requesting FDIC insurance coverage from the Federal Deposit Insurance Corporation. There has been some concern, both at the federal level and at state levels, with regard to what these industrial loan companies that are commercially owned might be able to do in terms of the activities that they can undertake, and in terms of their ability to branch from state-to-state. What has happened on the federal level is the FDIC has issued a one year moratorium on any

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applications to be acted upon by that agency that happened to involve commercial enterprises making application for industrial loan company charters. Historically, congress and the banking industry has an agreement, has decided that they mixing of banking and commerce should not occur. Banks cannot own commercial enterprises and we think the rules ought to be applicable, as well, to commercial enterprises not getting involved into the banking industry. With regard to the issue at hand today we have introduced LB113 which simply put, would prohibit out-of-state industrial loan companies from locating or establishing a branch in the state of Nebraska. Subsequent to dealing with Senator Pahls and having this bill introduced we communicated with the department of banking here in Nebraska and from those communications came to the determination that we may be and probably do not need LB113 in it's green copy form. The reason that we do not as Senator Pahls alluded is that we already have a statute on the books under chapter 8-2505 that says an out-of-state bank may not acquire or locate a branch in the state of Nebraska. That particular provision was adopted after congress enacted the Interstate Banking and Branching Efficiency Act, I believe, of 1994. And under that congressional enactment they basically said that the states could have limitations placed on the ability of banks from other states to branch within their borders and also could put restrictions on the ability to enter their borders by way of acquisition. What Nebraska did in response to that was, number one, they said if you want to come into our state from out-of-state through acquisition you may only come in by acquiring a bank that has been in existence for at least five years. With regard to the branching issue we specifically adopted the provisions of (section) 8-2505 that said no out-of-state bank shall establish or locate a branch in the state of Nebraska. With that on the books we came to the conclusion that the green form of LB113 was not necessary. What we did in communicating further with the department of banking though looked at the provisions of (section) 8-2102 which define out-of-state bank. At the time that congress passed their federal Interstate Banking and Branching Efficiency Act they did define bank, and for our purposes they defined bank to include state and national banks, and industrial loan companies. Since the adoption of the Nebraska act which provides a definition of out-of-state bank without defining bank, Nebraska has taken action to repeal any references to industrial loan companies in our statute which, I think, quite frankly was going back to, I read the statutes of any reference to commonwealth which was an industrial loan company. We think based on that there could be some questions raised as to how broad the coverage of bank is under our state statute and we have proposed an amendment which is attached to our testimony that would strike the original sections of LB113 and replace them with a simple amendment to section 8-2102 that provides that bank means a bank as defined in 12 U.S.C. 1813, which is the definition of bank for purposes of the Interstate Banking and Branching Efficiency Act of 1994. And with that, we would respectfully request the committee to adopt that amendment and to advance LB113 to General File. Be happy to answer any questions you might have. [LB113]

SENATOR LANGEMEIER: Are there any questions? [LB113]

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SENATOR PIRSCH: You had indicated banks, of course, can't own commercial enterprises. Can you comment a little bit more about the rationale underlying that? [LB113]

ROBERT J. HALLSTROM: Well part of the issue, and I think maybe it's brought home most clearly with regard to the Wal-Mart and the Home Depot types of applications, that the concern, I think, has to do or is rooted in a conflict of interest, in this particular case, that if a commercial enterprise has access and ability to control the financial purse strings of some of their competitors. In my testimony I have envisioned what has commonly been addressed with regard to the Wal-Mart situation that if Wal-Mart can come in, and because of it's economies of scales and other positioning drive banks out of the market, and then be the only avenue for other commercial competitors to come in and seek financing. That type of conflict of interest does probably not serve the market well. [LB113]

SENATOR PIRSCH: Thank you. [LB113]

SENATOR LANGEMEIER: I'll ask a question then. How does it relate to lending institutions owning real estate firms? Pinnacle Bank owns a real estate company named Pinnacle Realty. Are they not in direct competition with every other real estate company in the state that is bringing their customers to those banks for lending? [LB113]

ROBERT J. HALLSTROM: But they are not involved in operating a commercial enterprise. They are involved in the management and brokerage angle of that selling transaction, Senator. I think that is the distinction. It is not the operation of a commercial enterprise and obviously that is, as you know from the federal discussion, that is a two-way street. The realtors are already in both markets, and national banks cannot currently do that which is the issue before congress at this juncture. [LB113]

SENATOR LANGEMEIER: Thank you. Any other questions? Seeing none. [LB113]

ROBERT J. HALLSTROM: Thank you. [LB113]

SENATOR LANGEMEIER: Mr. Yost. [LB113]

KURT YOST: Senator Langemeier, members of the Banking, Commerce and Insurance Committee, my name is Kurt Yost, K-u-r-t Y-o-s-t. I am the registered lobbyist for the Nebraska Independent Community Bankers and very briefly, today the last day of hearings on banking issues, I appear before you today in support of LB113 as amended. I have had several ask me through the course of the past two months why I have not gotten up. I have tried to be respectful of your time. Mr. Hallstrom does a wonderful job representing the banking industry of the state of Nebraska on most

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issues. We do like to weigh in, however, on bank structure issues, and we do definitely see this as a bank structure issue. So with that, we would support LB113 as amended, Senator Langemeier. [LB113]

SENATOR LANGEMEIER: Are there any questions? Seeing none. [LB113]

KURT YOST: Thank you. [LB113]

SENATOR LANGEMEIER: Late in the day helps. Are there any other proponents? Opponents? Neutral testimony? Senator Pahls, you stuck around, you just as well close. [LB113]

SENATOR PAHLS: Twenty minute closing here. [LB113]

SENATOR LANGEMEIER: Senator Pahls waives closing and that will end the hearing on LB113. Thank you all for coming. [LB113]

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Disposition of Bills:

LB113 - Advanced to General File, as amended.

LB174 - Held in committee.

LB368 - Advanced to General File, as amended.

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Chairperson

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Committee Clerk