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Banking, Commerce and Insurance Committee
January 17, 2012

[LB714 LB836 LB852 LB853 LB854]

The Committee on Banking, Commerce and Insurance met at 1:30 p.m. on Tuesday, January 17, 2012, in Room 1507 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on LB714, LB852, LB853, LB854, and LB836. Senators present: Rich Pahls, Chairperson; Beau McCoy, Vice Chairperson; Mark Christensen; Mike Gloor; Chris Langemeier; Pete Pirsch; and Paul Schumacher. Senators absent: None.

SENATOR PAHLS: Good afternoon. We do have a couple of senators who are on other business. They will be here soon. 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, which is, sometimes I call the Millard. I have the pleasure of serving as Chair of this committee. The committee, we will take up the bills as posted. That would be (LB)714, (LB)852, (LB)853, (LB)854, and (LB)836. To better facilitate today's meetings, I ask that you abide by some of our following procedures, and I have put...they're on a board over there, and it will make things work much faster if you would take a look at those, just for a second, instead of having me read them. If you have communication that you want to give to the committee, we need at least 10 copies. If you don't have 10 copies right now, wave your hand, and we'll have one of the pages run some off. I see no hand waving. Thank you. I appreciate that you are well-prepared. And I will introduce Bill Marienau, he is the legal counsel, keeps us on track legally, and Jan Foster, she is the one that makes sure all the paperwork is in and we, again, are following the rules so I introduce those two. And now what I'm going to do now is have the senators introduce themselves starting all the way over here.

SENATOR SCHUMACHER: Paul Schumacher, District 22, Columbus and Colfax, Stanton counties.

SENATOR LANGEMEIER: Chris Langemeier, Schuyler, District 23.

SENATOR PIRSCH: Pete Pirsch, Legislative District 4.

SENATOR McCOY: Beau McCoy, District 39, Omaha and Elkhorn.

SENATOR GLOOR: Mike Gloor, District 35, Grand Island.

SENATOR CHRISTENSEN: Mark Christensen, District 44, Imperial.

SENATOR PAHLS: And behind us over there, we have Michael Killingsworth from Lincoln and Matt McNally from Norfolk. Those are our pages, so if you do need some additional help, they are willing to do that. Well, I think we will get the hearing going. The first bill is (LB)714 by Senator McCoy. [LB714]

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SENATOR McCOY: Thank you, Chairman Pahls. I am Beau McCoy, B-e-a-u, M-c-C-o-y, and I represent the 39th District. I am here to introduce LB714 to you which adopts the January 1, 2012, Uniform Standards of Professional Appraisers (Practice), or USPAP. It's a little different person up here introducing this bill than in the past. I'm a little shorter with a little darker hair than Senator Langemeier, but he's done a great job in his years in the Legislature of introducing this legislation, and hopefully I'll take it from here. New standards must be adopted every other year now, instead of every year in the past when this legislation has been brought. It carries an emergency clause. Mr. Marienau has put together in your summary, in your packets, some very good information on what this bill will reference in reference to the Dodd-Frank, Wall Street Reform, Consumer Protection Act, along with Financial Institutions Reform, Recovery and Enforcement Act as it's been updated. I believe there will be at least one other person behind me to testify. And again, this is really just an update on the time frame for the USPAP. With that, I would answer any questions if there are any. [LB714]

SENATOR PAHLS: Seeing none, thank you, Senator. And just a reminder, for anybody who is going to testify, you do need the pink...I think it is pink. I'm color-blind, so something that looks like this. Okay, testifiers. [LR714]

JOE WILSON: Good afternoon. My name is Joe Wilson, W-i-l-s-o-n, and I am the interim director for the Nebraska Real Property Appraiser Board, and I would like to thank Senator McCoy and Senator Langemeier. Senator Langemeier, in particular, for his hard work over the years. This is basically just a housekeeping bill, and like the Senator said, it is going to get us in compliance with Dodd-Frank and FIRREA. And with that, I'll answer any questions. [LB714]

SENATOR PAHLS: Seeing none, thank you for your testimony. [LB714]

JOE WILSON: Thank you. [LB714]

SENATOR PAHLS: Any more, any other proponents? Opponents? Neutral? Closing...the good senator waives closing. That takes care of (LB)714. The next bill that we are dealing with is LB852 by Senator McCoy. [LB714]

SENATOR McCOY: Thank you again, Chairman Pahls. I am Beau McCoy, B-e-a-u, M-c-C-o-y, and I represent the 39th District, and I'm here this afternoon to introduce LB852 which harmonizes a reference relating to corporate purposes under the Business Corporation Act and eliminates language in the definition of professional services in the Professional Corporation Act. LB852 is brought to me by the Secretary of State's Office, as they have identified a problem with current law. This bill strikes the language that creates the gray area on page 3 of the green copy of the bill. And in that, you will see, if you look at that, it's not clear if someone should form under a PC or a business

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corporation and creates a situation where anyone who holds a license may think they need to form under a PC, and current statute includes the words "including but not limited to," which can cause some confusion. And of course, the Professional Corporation Act was created in 1969 for those who are not able to form under the Business Corporation Act. And the Secretary of State's Office will be following behind me on this legislation to explain a little bit more detail the situation as they see it and hopefully how this piece of legislation will clear up any of that confusion for those out there across the state. Thank you. [LB852]

SENATOR PAHLS: Any questions for the senator? Seeing none, thank you. Proponents? How many proponents do we have? One. How many opponents? How many neutral? Okay, it looks like we have one person testifying. Good afternoon. [LB852]

COLLEEN BYELICK: (Exhibit 1) Good afternoon, Chairperson Pahls, members of the committee. My name is Colleen Byelick. It's C-o-l-l-e-e-n, B-y-e-l-i-c-k. I'm the general counsel for the Secretary of State's Office. As this committee is aware, last session we visited the topic of professional corporations with regard to real estate professionals. And although that particular issue was settled last session, it still seemed that there was some confusion in this area based upon that hearing and other discussions. The Secretary of State's Office is, you know, the core administrator of laws regarding business entity formation, and so we are here kind of looking to clarify the laws further, if we can. Basically, what the bill does is it changes the term "personal services," which is used in the Business Corporation Act to the term "professional services," which is the term actually defined in the Professional Corporation Act, and then it clarifies the professional service definition in the Professional Corporation Act by only listing the specific licensed professionals intended to be covered by the term and eliminates some of the ambiguous language surrounding that term. We're hoping that these changes clarify the law in this area and that licensed professionals have a better idea of who needs to form a professional corporation and what actually the law is intended to cover. And so our..that is...our hope with this bill is that we can just clarify the law in this area. If there are any questions, I would be happy to answer them. [LB852]

SENATOR PAHLS: Senator Pirsch. [LB852]

SENATOR PIRSCH: With respect to current...the current language is personal services, right? [LB852]

COLLEEN BYELICK: Right. [LB852]

SENATOR PIRSCH: And so with respect to types of businesses or whatnot that are currently eligible, who would be thus excluded when you go to a specific listing of professional organizations? [LB852]

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COLLEEN BYELICK: We would get questions in our office, for instance, for someone that is a barber, because they're providing a personal service, they're licensed to do that service, but we don't think that was the intent, that they should have to form a professional corporation. I think the intent was more geared toward the learned professions, attorneys, doctors, CPAs, that sort of professionals who is meant to be covered by the Professional Corporation Act and not some of these other licensed entities. Because if you get into licensed entities, there are hundreds of licensed professions in this state, and we don't think that they were all meant to be covered by the Professional Corporation Act. [LB852]

SENATOR PIRSCH: You said in, in real life, you're saying farmers are...were...I'm sorry, I may have missed that point. What was the profession you... [LB852]

COLLEEN BYELICK: No, barbers. Barbers. [LB852]

SENATOR PIRSCH: Barbers, I'm sorry. I had a little problem hearing you. Okay, and so the barbers felt that they must, is that right? [LB852]

COLLEEN BYELICK: Well, there was confusion there. They would call our office and say, am I supposed to be a professional corporation, and we would look at that definition and say, you know, we don't think you were meant to be encompassed in that Professional Corporation Act, but if you look at this definition, it's sort of unclear. [LB852]

SENATOR PIRSCH: How long has this paradigm been in effect? [LB852]

COLLEEN BYELICK: I think since the '70s, '72. [LB852]

SENATOR PIRSCH: Has it been a consistent problem percolating up year after year after year, or is this a few isolated incidences? [LB852]

COLLEEN BYELICK: Well, I guess I would have to reference that with I've been with the office since 2006, so since I've been with the office, we've been getting these types of calls. Last year, in the situation with realtors that came up, which kind of made us take a second look at the laws and see if there was any area that we could, you know, make some clarity, find some clarity in. [LB852]

SENATOR PIRSCH: And the relative detriments then of that, being a piece, can you talk about that relative to... [LB852]

COLLEEN BYELICK: Right. Well, you're limited in that you're still personally liable for the professional services that you render, so you don't have the complete corporate

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umbrella that you would if you were a business corporation. So there are some differences there. All the shareholders have to be professionals. You all have to be providing the same professional service, so there is limitations to being a professional corporation that you don't have in the Business Corporation Act. [LB852]

SENATOR PIRSCH: I see. Okay. I don't have any other questions. [LB852]

SENATOR PAHLS: Senator Schumacher. [LB852]

SENATOR SCHUMACHER: How is the list of people who are still included derived? I mean, is there some uniform standard? One thing that jumps out is pharmacists are not in this list, and they kind of...feels like the same kind of thing. [LB852]

COLLEEN BYELICK: Kind of a, similar to a medical doctor type of profession. What we did is we kept the list as it had been originally drafted but just took out the ambiguous language. So our thought was that we didn't want to bring other people in that weren't originally included, and we didn't want to exclude anyone, and so that is kind of where we, how we came up with the list. [LB852]

SENATOR SCHUMACHER: So if they're not on this list, they use a standard business corporation? [LB852]

COLLEEN BYELICK: Right. Yes. [LB852]

SENATOR SCHUMACHER: I have nothing further. Thank you. [LB852]

SENATOR PAHLS: Just for a point of clarification, you're just saying this is to clarify, not any major changes... [LB852]

COLLEEN BYELICK: No, no. We're not trying to change the law. We're just trying to clarify it and help those, as they are reviewing the laws, comply with them and understand what the laws are, so. [LB852]

SENATOR PAHLS: Okay. Seeing no more questions, thank you, Colleen, for your testimony. [LB852]

COLLEEN BYELICK: Thank you. [LB852]

SENATOR PAHLS: Seeing no more...no proponents? Opponents? Neutral? Senator...the good senator closes. That finishes the session on LB852. Now we are ready for LB853. [LB852]

SENATOR McCOY: Thank you, Senator Pahls. I am Beau McCoy, B-e-a-u, M-c-C-o-y,

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and I represent the 39th District. I'm here again this afternoon to introduce LB853. Currently, Social Security numbers and federal tax ID numbers are not required on Uniform Commercial Code financial statements filed with the Secretary of State, but when included, are required to be entered into the UCC database. The purpose of LB853 is to remove the requirement that the Secretary of State enter Social Security numbers and federal tax identification numbers into the Uniform Commercial Code records maintained by the Secretary of State's Office. Eliminating this requirement will reduce the amount of sensitive personal and business information in the UCC database. LB853 also removes the requirement that the Secretary of State provide information from the Uniform Commercial Code records over the telephone. Searches of the Uniform Commercial Code records are available electronically, by mail, or in person. LB853 was brought to me by the Secretary of State's Office, and they will be following behind me to explain the bill in a little more detail. Thank you. [LB853]

SENATOR PAHLS: Seeing no questions, thank you, Senator. We are now ready for proponents. [LB853]

COLLEEN BYELICK: (Exhibit 1) Members of the committee, again, my name is Colleen Byelick, it's C-o-l-l-e-e-n, B-y-e-l-i-c-k, the general counsel for the Secretary of State's Office. First, we would like to thank Senator McCoy for introducing LB853 on behalf of the Secretary of State's Office. As Senator McCoy mentioned, LB853 removes the requirement that we data enter Social Security numbers and federal tax identification numbers into our UCC computer database. These numbers are not currently required on our UCC financing statements, but if provided, we are then required to enter them into our system. As we are all aware, this is sensitive, personal information that can be used for personal and business identity theft, and we are simply trying to remove this information from our records and protect this type of personal information. The other change in this bill deals with providing information from our UCC database over the telephone. Our searches of our records are still available electronically online or in-person or by mail. We feel that there is a more, greater chance for miscommunication when things are communicated verbally over the telephone, and that is why we would ask for this change. We would urge this committee to advance LB853 to the floor. Thank you, and I would be happy to answer any questions you may have. [LB853]

SENATOR PAHLS: Senator Schumacher. [LB853]

SENATOR SCHUMACHER: As I read this, this removes the requirement that you enter future data into the system. To the extent it's problematic to have that kind of personal information in a system, what happens to the existing data if we take this away? [LB853]

COLLEEN BYELICK: We, at this point, the existing data is still there. We are looking at a plan to redact that type of information. As of July 1, 2013, there will not even be an option for someone to give us a Social Security number on the financing statement.

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There will not even be a box for that number. So what we're looking at is coming up with a plan of redaction to remove that information from our record that coincides with that July 1, 2013. So that is something that we're working on and planning on, but not something that we're currently doing. [LB853]

SENATOR SCHUMACHER: Do you feel that you would need any specific authorization from the Legislature... [LB853]

COLLEEN BYELICK: We may. [LB853]

SENATOR SCHUMACHER: ...to make those changes in the present? [LB853]

COLLEEN BYELICK: We may, and... [LB853]

SENATOR SCHUMACHER: That's down the road. [LB853]

COLLEEN BYELICK: ...that's one of the things that we're still evaluating. [LB853]

SENATOR SCHUMACHER: Okay. Thank you. [LB853]

SENATOR PAHLS: Senator Pirsch. [LB853]

SENATOR PIRSCH: Can you comment about the ways that the database is currently being used and who has access to that? [LB853]

COLLEEN BYELICK: There is an ability for someone to have online access. They have to be a subscriber with Nebraska.gov, so they pay a subscription fee, and then they pay a searching fee. But it is open to the public, and if they were to view or display a filing, and that filing contained a Social Security number, they would be able to view it. [LB853]

SENATOR PIRSCH: And do you know what that fee is? [LB853]

COLLEEN BYELICK: It's a \$50 fee to be a subscriber. [LB853]

SENATOR PIRSCH: Okay, and then if...so with \$50...comment is how often do you see this? You don't require it, do you, in your current forms, right? [LB853]

COLLEEN BYELICK: No, we don't require the Social Security number. [LB853]

SENATOR PIRSCH: But people are voluntarily... [LB853]

COLLEEN BYELICK: Providing it. [LB853]

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SENATOR PIRSCH: ...inexplicably even though there's no space to... [LB853]

COLLEEN BYELICK: Currently, there's a statutory form that we have to accept, and on that statutory form, there is a spot that they can put Social Security numbers, and it does say that it's optional, but some people still provide it. [LB853]

SENATOR PIRSCH: And you don't think that you have the unilateral ability to eliminate that. [LB853]

COLLEEN BYELICK: That spot on the form will be eliminated as of July 1, 2013, because of some legislation that occurred last year. [LB853]

SENATOR PIRSCH: Okay. [LB853]

COLLEEN BYELICK: So that is going to go away, so the amount of information in our system, this type of information should decrease. But from now until then, we would also like to stop entering it into our system. [LB853]

SENATOR PIRSCH: And then with the Social Security number, is there also similarly a federal tax identification number space? [LB853]

COLLEEN BYELICK: Yes. [LB853]

SENATOR PIRSCH: And that is similarly going away in 2013? [LB853]

COLLEEN BYELICK: Yes. [LB853]

SENATOR PIRSCH: So you're talking about this is a one year...I mean, hopefully people won't go to the extent of providing information not requested, even optionally, but kind of a one year. [LB853]

COLLEEN BYELICK: Right. This is sort of an abundance of caution that if people are going to continue to put this, that, you know, we stop entering it into our system. [LB853]

SENATOR PIRSCH: Okay. Thank you. [LB853]

SENATOR PAHLS: Senator Schumacher. [LB853]

SENATOR SCHUMACHER: Who sets that \$50 fee and who gets it? [LB853]

COLLEEN BYELICK: Actually, it's part of a contract with the State Records Board, and Nebraska.gov, who is the network manager, gets that \$50. [LB853]

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SENATOR SCHUMACHER: So a private company gets that \$50. [LB853]

COLLEEN BYELICK: A private, yes. [LB853]

SENATOR SCHUMACHER: Has that been adjusted at all over time seeing there is so much volume now? [LB853]

COLLEEN BYELICK: It has not been adjusted for a long time. [LB853]

SENATOR SCHUMACHER: And that fee is set at \$50 by then agreement with... [LB853]

COLLEEN BYELICK: Yes. It's in contract. [LB853]

SENATOR SCHUMACHER: And how often does that contract come up? [LB853]

COLLEEN BYELICK: It has come up from time to time throughout the years. I think the first contract was in 1998, but the same vendor has gotten that contract each time it has come up. I think the current contract is a four-year contract, and then there may be some extension years on it, but I would have to go back and look at the specific dates to tell you the specifics on it, but... [LB853]

SENATOR SCHUMACHER: Has it ever been reduced even though computer usage and availability has gone way up? Has the fee ever been reduced commensurate with usage? [LB853]

COLLEEN BYELICK: I don't think the fee has ever been reduced, no. [LB853]

SENATOR SCHUMACHER: Thank you. [LB853]

SENATOR PIRSCH: Just incidently, who is the vendor on that? Do you know? [LB853]

COLLEEN BYELICK: It's Nebraska Interactive, or they are commonly known as Nebraska.gov. [LB853]

SENATOR SCHUMACHER: And they are a subsidiary of who? Do you know? [LB853]

COLLEEN BYELICK: There is a parent company that is by the name of Nebraska Interactive. They're... [LB853]

SENATOR SCHUMACHER: And they are a subsidiary of who? Nebraska Interactive? [LB853]

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COLLEEN BYELICK: I don't know. The Nebraska company is called Nebraska Interactive, LLC. There is a parent company behind that company. [LB853]

SENATOR SCHUMACHER: That is not a Nebraska company? [LB853]

COLLEEN BYELICK: Exactly. [LB853]

SENATOR SCHUMACHER: Thank you. [LB853]

SENATOR PAHLS: Seeing no more questions, thank you. Any more proponents? Opponents? Neutral? [LB853]

ROBERT HALLSTROM: Chairman Pahls, members of the committee, my name is Robert J. Hallstrom. I appear before you today in a neutral capacity on behalf of the Nebraska Bankers Association on LB853. I certainly do not expect that we have any exception to the issues with regard to the Social Security numbers and the tax identification numbers with the issues of identity theft and so forth, but I did want to preserve a place mark, if you will. I haven't had a chance to visit with the bankers with regard to the second change in the bill, which has to do with the elimination of the telephone inquiry for information from the Secretary of State's Office. I suspect with the electronic and mail options that we will probably be okay, but since I have not gotten that authorization, I did just want to let the committee, and particularly Senator McCoy, know that we're looking into that issue. And with that, I'd be glad to take any question. [LB853]

SENATOR PAHLS: Senator Pirsch. [LB853]

SENATOR PIRSCH: Is it the thought that you're not aware of how heavily that phone option is used, or is it the thought that there is...it is used heavily, but you want to know... [LB853]

ROBERT HALLSTROM: It's the thought that I don't know the answer to that question. When we have our bankers together, we will find out if that is something that is significantly used, if they are concerned about, as the Secretary of State representative suggested, that there is maybe some room for error when you're having oral communications. It may not be an issue, but I just wanted to go on the record to let the committee know that we are looking into that issue, and I will get back to Chairman Pahls or Senator McCoy if there is any reason for us to be concerned about it. [LB853]

SENATOR PAHLS: Seeing no more questions, thank you. [LB853]

ROBERT HALLSTROM: Thank you. [LB853]

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SENATOR PAHLS: Senator McCoy. The good senator waives closing. Thank you. We are now ready for LB854. Senator McCoy. [LB853]

SENATOR McCOY: (Exhibit 1) Thank you, Chairman Pahls. I am Beau McCoy, B-e-a-u, M-c-C-o-y, and I represent the 39th District of the Legislature. I'm here again this afternoon to introduce LB854 to the committee which limits the time period an administratively dissolved corporation, professional corporation, nonprofit corporation, limited cooperative association, and limited liability company may reinstate. Currently, an administratively dissolved entity may be reinstated at any time after paying back fees and delivering an application for reinstatement. When the reinstatement is effective, it relates back to and takes effect as of the date of revocation, and a company can resume carrying on its business as if the revocation had never occurred. Under the proposed legislation, an entity would only be able to reinstate within three years after the effective date of the administrative dissolution. Business identity theft is a growing national issue, and limiting the time for reinstatement removes shelf entities dissolved by law and which have long ceased doing business from being reinstated by unrelated third parties and used for nefarious purposes. The bill also provides a delayed operative date to allow entities the opportunity to review their records and reinstate where appropriate. I have a cleanup amendment here for the committee to take a look at. A couple of things were noticed after we had the green copy, which are just essentially minor technical changes, which just makes the language consistent. It changes "dissolution" in the green copy to "revocation," and I believe Secretary Gale, I believe, will be testifying behind me, and will probably explain, perhaps, a little more of that where we need to change that from dissolution to revocation, as we're only allowed to revoke a foreign company, but not dissolve it, so that was one technical change we needed to make in the amendment. There is also a slight change by striking section 8 which sunsets on January 1, 2013, when, of course, LB854 would take effect. And again, LB854 was brought to me by the Secretary of State's Office, and again, I believe Secretary Gale will be following behind me to go into this in a little more detail. And with that, I will end. Thank you. [LB854]

SENATOR PAHLS: Seeing no questions, thank you, Senator. Proponents? How many proponents do I see? One. How many opponents? How many neutral? One neutral. [LB854]

JOHN GALE: (Exhibit 2) Good afternoon, Chairman Pahls and members of the Banking, Commerce and Insurance Committee. I'm John Gale, J-o-h-n, G-a-l-e, Secretary of State for the state of Nebraska. I appreciate Senator McCoy introducing LB854 as well as LB852 and (LB)853. These are all matters that are just issues that we want to bring to your attention and hopefully address legislatively, and this bill, LB854, really deals with an issue of integrity and an issue of accountability. The essence of this bill is that we want to place a finite limit on the period of time in which business entities can

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reinstate. As you know, the state of Nebraska is the sovereign, and the sovereign grants authority to business entities to be formed. It's an act of delegation of authority. You cannot have the right to create a limited liability company or a right to create a corporation unless the sovereign delegates it to you. And in return for that exercise of delegation of authority to people to create business entities with the advantages that come with business entities, the state has various requirements, and those requirements date back many decades, but were codified in the uniform model Business Corporation Act and the model uniform legislative Limited Liability Company Act. One of those requirements is to file now biennial reports with the Secretary of State's Office reidentifying the business, identifying its address, identifying its registered agent, paying the filing fee for that biennial report, and paying the occupation tax. And the tax is part of what you impose on them for their right to conduct business as a business entity under your laws, so there is a cost involved, and it's a fairly modest cost, but there is a cost involved for doing that. If the entity fails to file that required report and to pay the associated fees, the law allows the Secretary of State to administratively, involuntarily dissolve that entity, and it loses its good standing. Now "good standing" is a term of art in the law and in the legislation. It means that you have the ability to conduct your business under the terms and conditions of the legislation. It means that you can secure a loan. It means that you can sue or be sued. It means you have perpetual authority to exist. It means you have the ability for transferability of interest of your company. So it's...good standing means you are current with your obligations with the state. You have filed the disclosures, the biennial reports, you have paid your fees, and you have a current registered agent who is, of course, the person that can be sued by your public, your citizens who may have a remedy. They can go to our records and know who they can sue if that entity has committed some negligence or recklessness or financial impairment. They are easily identified. These are things you require. This is accountability. These entities have to be accountable. However, we have tried many ways to make sure that we capture as many business entities as possible before they lose that good standing. So we have asked the Legislature in the past to go to biennial reports rather than annual reports. We've asked the Legislature for the authority to give us the right to send out more notices, which is an expensive thing when you're dealing with tens of thousands of entities. We now give every entity three notices between January and April that they will be dissolved if they do not meet their requirements for biennial report and to pay their taxes. They also can now file online, so we've made many steps in that direction. If a company does not file in a timely fashion, then they are subject to dissolution. They lose their good standing, and all they can do under the law is wind down. In effect, it's like almost a bankruptcy. They cannot continue to grow and prosper and expand. Their job is to wind down and end their business. That is all they can do once they're dissolved. However, under Nebraska law, there has been this peculiarity that probably goes back to the early model laws, and that is there is no limit on the ability of a corporation who has been dissolved to reinstate. So currently, if you've been dissolved by law, you can stop filing your biennial reports, you can stop paying your occupation tax, and you can continue to do business say for 10, 20, 30

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years. And then you find that you may be subject to liability, you cannot get a loan you want to get, you cannot enter into a contract because you're not in good standing. They can reinstate back retroactively to the date of dissolution and regain their good standing for that period of time, so they are in effect a hidden entity until they reinstate. Now, two things are happening. Number one, you're losing the accountability. They're out there existing and doing business. They're not accounting to you to know who they are, who their officers are, who their directors are, who their registered agents are, and they're not paying the taxes you require, and yet, they continue to do business and can reinstate at any later date. We don't think that is good accountability under your reporting system. Secondly, because of this growing issue that Senator McCoy mentioned of business identity theft, LLCs in particular, but corporations too, are nationally becoming a huge issue. The National Association of Secretary of State have resisted federal legislation for years to try to impose some very onerous burdens on the state to eliminate shell and shelf entities. What are they? They are entities that have been dissolved, but they're still out there as kind of a phantom entity, and criminals can recapture those by buying the hollow shell, the shell entity, and reactivating, reinstating that entity back to the day of dissolution, and then conduct criminal business in the name of this company that had a good name, it's gone out of business. But as long as you allow it to sit on a shelf for 10 or 20 years, and for a criminal to reinstate it after the owners are long gone has become a huge issue nationally. Billions of dollars supposedly are being run through these shell or shelf entities that were dissolved but continue to exist because there is an unlimited date for reinstatement. So we're asking you as a committee to look at this, and for reasons of both accountability to you and to the citizens, so that they're easily identified, and we know who has good standing and who doesn't, and also to ensure that our entities, unlike Wyoming, which has had a huge scandal over this issue, do not have problems with shell and shelf corporations. We would ask that you impose this limit of three years on the ability of a company to reinstate itself after dissolution. Thank you. [LB854]

SENATOR PAHLS: Senator Pirsch. [LB854]

SENATOR PIRSCH: You reference an incident in Wyoming then. Can you flesh that out in terms of what happened there, and have there been any, I guess, similar scrapes here in Nebraska that you're aware of? [LB854]

JOHN GALE: We haven't had, Senator, at least that we know of, in Nebraska, the kind of criminal conduct that was uncovered through an investigation in Wyoming. And it was simply this, that there wasn't any limit on the reinstatement power of LLCs, in particular, is what they were looking at in Wyoming, and they tracked down a number of Russian, Ukrainian, east European criminals who were using it to launder drug money, to launder terrorist money through these entities that were reinstated and looked like they were still the original company that had a good name and was owned by people who operated an honest business who were dissolved, left the business, but the entity is still sitting there.

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And it was being purchased by...I think the purchase price was like \$1,000 for these criminals to purchase an entity, and then they put up straw men as their new directors and their new officers. But they regained the integrity, they regained the creditworthiness of that original company and can then proceed to open up bank accounts and do business as any other business in good standing, so I could get you a copy of the Wyoming report. [LB854]

SENATOR PIRSCH: Yeah. I guess what I'm thinking, if there is such a bad actor out there in the world who is looking, if we're limiting it to 3 years, and they just want a shell of any type, there will still be plenty of 3-year-old shell or 2.5-year-old shells out there, won't there, for them to choose from? [LB854]

JOHN GALE: Well, we're...from our investigation, I'm going to say in 2011, the nonprofit and the LLCs that had to do the biennial reporting, there were approximately 5,500 that were dissolved administratively, and of those 5,500, about 1,500 reinstated in the same year. The vast majority of those that are dissolved administratively simply disappear and go out of business. Those that are legitimate businesses, forgot to file on time, reinstate. The idea of the three years is to allow the legitimate businesses who have simply missed their deadline, and their lawyer or their CPA or somebody catches it, three years has, from our studies, seemed to be an adequate time to recapture virtually all of those that are still in good standing, I mean, still in business and want to retain their good standing. So the three years is for the benefit of the ongoing businesses who want to remain in business. If you dissolve without any ability to reinstate as of the date of filing, then these 1,500 good businesses would not be able to reinstate their standing, so it's a balancing act. [LB854]

SENATOR PIRSCH: Oh sure, and I understand there has to be some sort of a period then where, if you're suggesting that there is, that it can't be just unlimited. But in terms of...in terms of you don't want to eliminate, on the good side, you don't want...there are some companies who just missed the deadlines, and they'll pick up, and you're suggesting three years is long enough so that you're not punishing, so to speak, the good. I guess the question is on the back end, now you want to eliminate the bad actors. Are they going to...will they simply instead of picking a company that's been dissolved for ten years or six years, and they probably want one with still some lingering goodwill, right, or some memory out there? [LB854]

JOHN GALE: Correct. I would think. [LB854]

SENATOR PIRSCH: Won't they, wouldn't they be more enticed or have an appetite for 2.5-year dissolved corporations as opposed to 5- or 6-year corporations anyhow, or is that not true? [LB854]

JOHN GALE: That is hard to answer to know whether they would or they would not. I

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would say what we're trying to do by this step is to at least eliminate the unlimited ability to reinstate 30 years down the road or 20 years down the road. You're right. You would think there would be more goodwill to capture a more current dissolved company than an older one. At the same time, the records of that company may not be as available to nefarious characters as one that is 10 years old or 20 years old, where the family is long gone, the lawyer and the CPA are probably retired, and it's still on somebody's shelf with all the records there. So there is probably a certain degree of protection for those records for several years as that family business has maybe gone out of business, but the family still has the records or their lawyer still has the records, so they're not lost. [LB854]

SENATOR PIRSCH: IRS purposes for seven years after (inaudible) so. [LB854]

JOHN GALE: Correct, which would be a good reason for the CPAs to hang onto the records. [LB854]

SENATOR PIRSCH: Yeah. Thank you. [LB854]

JOHN GALE: Thank you. [LB854]

SENATOR PAHLS: Senator Schumacher. [LB854]

SENATOR SCHUMACHER: I have a few questions. The three-year number, what was the reasoning behind three instead of two or five? [LB854]

JOHN GALE: Well, we looked at a National Association of Secretary of State study and survey on what all the states are doing, and a number of states do have a limitation, but the limitation is all over the board. It's six months, one year, two year, five years, ten years, and so three years seemed to us to address the issue that Senator Pirsch is talking about, and that is don't leave the window so wide that you haven't closed the door, which is what I would think a ten-year limitation would be. And yet three is not as short as a number of the states that have six-month, one-year, two-year, three-year provisions, so we thought the three, and there is no magic about it, Senator. It just seemed like it was a reasonable compromise between the ability of ongoing businesses to get reinstated without losing their status and to shut the door as much as we could on bad actors. [LB854]

SENATOR SCHUMACHER: When they come in to get reinstated after they've let it lapse for a few years, they've got to pay the back fees, and is there penalties, too, they've got to pay in order to get reinstated? [LB854]

JOHN GALE: Well, there is the back filing fee as well as the back occupation tax fee, and I think there is an interest on that, but there is no penalty other than an interest on

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back due amounts. [LB854]

SENATOR SCHUMACHER: Then I guess what kind of runs through my mind here is a practical situation where a young person, or maybe an older person, decides they're going to become a businessperson. They're going to open up a roofing company or a beauty salon or something like that, and they're all gung-ho about making money and being in the free enterprise. And as so many times is the case, it fizzles after a year or two. They maybe didn't even pay the attorney to set it up to begin with (laugh), and they surely don't want to pay an attorney to go through a dissolution, so they just get a job at the local five-and-dime or factory or whatever and just forget about the corporation. And they think everything is all swell and good, and they get dissolved because they don't send the form in and the \$13 or whatever it amounts to. Then lo and behold, they find out in year four that when they were pounding on the roof the hammer fell off and it hit somebody, and they thought the person just walked away with no injuries and no complaints. And all of a sudden, a lawsuit is filed against them because you have four years on a action for accidents, and you have five years on a screwy contract you might have forgotten you entered into. And so suddenly what they thought was protected under the corporate shield is unavailable to them, and they really wish they would have had that for the four or five years to have the protection they thought they were buying originally. It seems to me that five years, which is a contract statute of limitation and also more than the four-year tort limitation, would be a better number than three so people could get back under the umbrella of the corporate safety if they got caught in a pinch when their company went bad. [LB854]

JOHN GALE: We looked at that, Senator, and there are so many statute of limitations for so many different kinds of violations or property rights or personal injury, other contract cases, it's difficult to decide which of those really is meaningful when you have an entity that has dissolved. And when you dissolve, you wind down your business. You're supposed to give notice to your creditors, so if they have some interest in whatever assets you have, again, kind of like a bankruptcy, so you have to give notice of that to your creditors so that they can make a claim or sue you at that time. I guess our understanding of the law, from our research, is that as long as the entity was in good standing at the time of the incident that is being complained about, you still have the protection of the corporate shell. [LB854]

SENATOR SCHUMACHER: Okay, then finally the last question. When you say that the bad actors go out and find a corporation on somebody's shelf, certainly an accountant or lawyer can't sell his client's property. So the shareholders or directors or owners of that underlying corporate entity would have to be the people that were being dealt with. Is that correct? [LB854]

JOHN GALE: In Wyoming, they were called formation agents, and I don't know if that is really a licensed profession or not. I doubt that it is, but they are people who engage in

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representation of entities, and they're not lawyers and they're not CPAs. I suppose they would be like the incorporators that the lawyers and CPAs use them. I won't compare them to CT corporations, but kind of the same idea, a nonlicensed business entity that represents these companies and acquire the paperwork and the corporate records and the LCC records. You know, as attorneys, we both have had those things sitting on our shelves for a long time. Sometimes the family members come and get them. Sometimes when you clear your shelves of old paperwork, those old corporations go out in the trash, too, and maybe somebody goes through the boxes. I don't know how all they acquire them, but the company...these formation agents in Wyoming were the ones that were selling these shelf or shell entities. [LB854]

SENATOR SCHUMACHER: But if it was just incorporated, never became a viable business where shares were divvied out to shareholders and undertook businesses, then it would have no reputation to be stolen or anything else. I mean, I'm missing something I think there as to how this thing gets off somebody's desk and back into circulation without paying the original owner something for it. [LB854]

JOHN GALE: And maybe they do. I would be happy to furnish you with the Wyoming report too. It goes into more detail than I want to go into for you here today, but it was alarming to see how this kind of a business can thrive as kind of a black market for entities that...apparently, it's billions of dollars that get moved through drug accounts and through terrorist accounts internationally, and the Department of Treasury, the FBI, the IRS are all really gunning to shut down shell and shelf entities nationwide. If it's not done state by state, it will be done federally, and as Secretary of State, we would rather try to address the issue in our home state rather than in Congress. [LB854]

SENATOR SCHUMACHER: One last follow-up question, let's say that there's a company called ABC Pro, Inc. It goes, doesn't pay its fees, three years later it's dissolved. The name ABC Pro, Inc. is now available for anybody who wants to come to your office and file. And so they can pick it up by filing, you know, a cheap filing fee with your office, and they are ABC Pro, Inc. How does this solve the problem? [LB854]

JOHN GALE: Well, if you're a legitimate CPA, legitimate attorney, and you have a shell entity that somebody formed and they didn't ever really go into business and they kind of abandoned it with you and you can use it at the end of the year if somebody has a crisis, needs an entity short-term to get into for tax purposes, they do get used for those purposes. [LB854]

SENATOR SCHUMACHER: You're making almost with this thing more convenient for me, because I just go through the list of dissolved entities, find a name that looks nifty, and send you a filing fee, and I now have it. I don't even have to go find a lawyer or shell entity. That is all done in the Secretary of State's Office for me. [LB854]

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JOHN GALE: Well, in our office, we don't know what is legit and what is not legit. There is no way for us to know who the bad actors are. And so what we're simply saying is that if they can't be reinstated, they will never present, pose the problem of being bad actors posing as good citizens to use them for illegitimate purposes, and so... [LB854]

SENATOR SCHUMACHER: But their name will be available for a bad actor to use just by asking. [LB854]

JOHN GALE: Well, once they're dissolved and unable to be reinstated, their name is no longer available to them. [LB854]

SENATOR SCHUMACHER: To them. [LB854]

JOHN GALE: The name is put on open record and anybody else as a citizen can acquire that name. [LB854]

SENATOR SCHUMACHER: Right, and if I'm a crook, now I don't have to go find the original owner. I can just go to your office and claim the name. [LB854]

JOHN GALE: Well, the name isn't what they're looking for. I think it's the status, the records of the entity, knowing who the past officers were, knowing who the past registered agents were. I think that adds a little more credibility to their filings when they file all of those past biennial reports that are due. So just having the name alone doesn't, you don't know what the... [LB854]

SENATOR SCHUMACHER: I wouldn't have to file a past biennial report if I set up a new corporation with an abandoned name. [LB854]

JOHN GALE: I'll be happy to talk to you privately about it, Senator. [LB854]

SENATOR SCHUMACHER: I'm just probing here. [LB854]

JOHN GALE: Obviously, we have a different point of view on it. We think that this bill would significantly help to shut down, and that seems to be the position of all of the federal law enforcement authorities as well. [LB854]

SENATOR SCHUMACHER: Thank you. [LB854]

SENATOR PAHLS: Is this happening throughout the states? Are the states doing what you're doing, trying, attempting to do now? [LB854]

JOHN GALE: They are, Senator. We have been working with the American Bar Association, working with uniform law committee nationally, working with the State

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Conference of State Legislators on this very issue to try to come up with solutions that states can address rather than letting Congress address it and impose some pretty onerous burdens on our businesses. [LB854]

SENATOR PAHLS: Okay, so you're looking more at having the states do it instead of the federal government? [LB854]

JOHN GALE: Exactly. [LB854]

SENATOR PAHLS: And you're telling me other states are doing it and are following the same patterns that you're following. Is that...? [LB854]

JOHN GALE: Correct. [LB854]

SENATOR PAHLS: Okay, so you're not out there really plowing new ground. [LB854]

JOHN GALE: Well, I certainly don't see myself as being on the spear point of this issue, because all of the Secretaries are trying to deal with it. [LB854]

SENATOR PAHLS: Okay, okay, okay. Senator Pirsch. [LB854]

SENATOR PIRSCH: And thanks, and yeah, I would appreciate knowing that, too, the trend or other states who are implementing these kinds of things as well. But just a couple of questions, and we can get that information later with respect to the other states. But with respect to the value to bad actors then, is it possible that the information, the kind of, I guess confidential information that they're after, is that being obtained from the CPAs or is that because once they have that reinstatement that they can then go to the governmental entities, and the governmental entities will provide them information that essentially...I mean, is it from the CPAs or from governmental actors that they're deriving this kind of information? Do you know? [LB854]

JOHN GALE: My guess would be that once they are on file with the government entities and back in good standing, that they can go to any bank and open bank accounts. They can go to the IRS and get an updated tax ID number. So I think once they're in good standing with the state authority that does the corporate work, then they can go just to any other government entity and get further enhancement of their good standing. They are particularly interested in being able to open bank accounts and use them to transfer money. That is their biggest interest, and the federal government is trying to address that through the bank security laws to get the banks who right now have to report anything suspicious. They have the SALs, the Suspicious Activity Reports, SARs that they have to file, so it's being addressed kind of from both ends, but.. [LB854]

SENATOR PIRSCH: And then just one final one. With respect to the aspect that you

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can dissolve domestic corporations, right, but when it comes to foreign, you cannot dissolve, correct? [LB854]

JOHN GALE: Correct. We can just simply revoke their license to do business... [LB854]

SENATOR PIRSCH: Yeah. [LB854]

JOHN GALE: ...and we do support the technical amendments that Senator McCoy referred to. [LB854]

SENATOR PIRSCH: Is there any problems with that sort of status, though, I mean dealing specifically with these out-of-state then...I'm sorry, these foreign corporations? Would that present a problem for enforcement with this? Or with the amendments, do you think we have that covered? [LB854]

JOHN GALE: I think with the amendment, we have that covered. What was happening in the first draft was that the Bill Drafters were using involuntary dissolution as applied to foreign corporations, and we can't dissolve them. We can simply revoke their status to do business. [LB854]

SENATOR PIRSCH: And then if somebody wants to reinstate the revocation then, once you revoke company ABC or what have you and they...there's a process for undoing that? [LB854]

JOHN GALE: Well, that's a good question, Senator. To my knowledge, the same three-year limitation would apply to a foreign entity that wanted to come back after having been revoked, but I would have to confirm that. I would have to check and confirm that for you. [LB854]

SENATOR PIRSCH: Okay. [LB854]

JOHN GALE: And I will do that. Did you want a copy of the Wyoming report? Did you ask for that? [LB854]

SENATOR PIRSCH: Sure. Yeah, whenever, it's... [LB854]

JOHN GALE: Senator Schumacher, you had asked for that too? [LB854]

SENATOR SCHUMACKER: Yes, please. [LB854]

JOHN GALE: Okay. [LB854]

SENATOR PAHLS: Seeing no more questions, thank you, Secretary. [LB854]

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JOHN GALE: Thank you, Senator. [LB854]

SENATOR PAHLS: I saw one neutral. Good afternoon. [LB854]

KATIE ZULKOSKI: Good afternoon, Chairman Pahls, members of the Banking, (Commerce and) Insurance Committee. My name is Katie Zulkoski, Z-u-l-k-o-s-k-i. I'm testifying today on behalf of the Nebraska State Bar Association to address exactly the situation that Senator Schumacher brought up earlier about the protections that a corporation in forming or an LLC. The protections is one of the reasons that you would file such an entity that are then no longer available to you once you have been dissolved and are not able to reinstate. If we allow under the statutes, as Senator Schumacher said, certain claims to be brought against a corporation after that three-year period, and if we do not then allow the corporation or the LLC to be reinstated, they have no way to answer those claims as the corporation. So the Bar Association's recommendation would be to use a time period that is longer than the recommended three years that is included in this bill, something that would match the statues of limitations that we allow people to bring claims against these corporations. Our recommendation would be ten years. We have talked to Senator McCoy about this, and he certainly is aware of the issue as well. [LB854]

SENATOR PAHLS: Okay. So you you're saying ten years... [LB854]

KATIE ZULKOSKI Um-hum. [LB854]

SENATOR PAHLS: ...is what you're saying. Now I don't want to rehash all the questions again. What we...do you have any new information to give to us of the questions that were posed to Secretary? [LB854]

KATIE ZULKOSKI: My only comment would be that the Secretary made a comment about if you...if corporate protection is available if you were a corporation in good standing at the time the incident arose, that our concern is a little different in that the corporation is unable to answer if they're not in good standing. Whether or not the corporate protection is available and whether you can answer the claim, those are separate concerns, so I certainly cannot disagree with him on the corporate protection side. But we still think the corporation should be able to reinstate so that they could answer a claim. [LB854]

SENATOR PAHLS: Okay. Again, I'm just getting to the point. [LB854]

KATIE ZULKOSKI: Um-hum. [LB854]

SENATOR PAHLS: How many years are you suggesting or your... [LB854]

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KATIE ZULKOSKI: Ten years. [LB854]

SENATOR PAHLS: Ten years. Five years? [LB854]

KATIE ZULKOSKI: Five years would be better than three years. [LB854]

SENATOR PAHLS: Okay, so we're like negotiating right now. Right? (Laughter) No, no, no. I'm not, but I just. Okay, do you have any different information to give to us other than the Secretary of State? [LB854]

KATIE ZULKOSKI: I do not. [LB854]

SENATOR PAHLS: So you're telling me for the most part, other than the years, you are in agreement with what they are proposing. [LB854]

KATIE ZOLKOSKI: We absolutely understand the purpose of the bill. We just think we should be careful as to the time limit that we would say for reinstatement. [LB854]

SENATOR PAHLS: Okay, thank you. Senator Pirsch. [LB854]

SENATOR PIRSCH: I guess, and I appreciate your testimonies. You recommend ten years. Obviously, the tort statutes that Senator Schumacher... [LB854]

KATIE ZULKOSKI: Um-hum. [LB854]

SENATOR PIRSCH ...referenced are four and five years. I think the Secretary of State referenced there are...that was thought about, but there were other considerations in terms of possible, I guess, issues out there that may have other differing, I don't want to say statute of limitations, but time periods where they may affect rights and responsibilities. So you recommend ten years. I'm supposing that...is there any larger, other than the tort claim, you know, tort claims are out there, why you're saying ten years as opposed to six years? [LB854]

KATIE ZULKOSKI: The attorneys that we had look at this that practice in the business entity world indicated that there were claims related to real estate that would be ten years and that ten years would cover all statutes of limitations. Five certainly comes a lot closer with the torts and the contract claims. [LB854]

SENATOR PIRSCH: Okay. Thanks for explaining. Thanks. [LB854]

SENATOR PAHLS: Senator Schumacher. [LB854]

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SENATOR SCHUMACHER: Would the ten-year one be action for repossession of real estate and adverse possession actions? [LB854]

KATIE ZULKOSKI: I think that would be exactly what I'm referring to. [LB854]

SENATOR SCHUMACHER: Thank you. [LB854]

SENATOR PAHLS: Thank you. [LB854]

KATIE ZULKOSKI: Thank you. [LB854]

SENATOR PAHLS: Seeing no more testimony, Senator McCoy. The good senator closes on LB854. [LB854]

SENATOR McCOY: All right. We'll move on now to LB836. Senator Pahls. [LB836]

SENATOR PAHLS: Thank you, Senator McCoy and members of the committee. My name is Rich Pahls, P-a-h-l-s. I represent District 31, which actually is Millard of Omaha. LB836 was introduced at the request of the Nebraska Bankers Association. The bill would clarify that the state and political subdivisions may invest or deposit their funds in interest-bearing deposits through a local bank or savings and loan in a deposit placement...using a deposit placement service such as Certificate of Deposit Account Registry Service or Insured Cash Sweep. By these means, all the public funds have full FDIC protection as required by Nebraska law. Now, I'm going to use this in like terms I understand. Let's say I am a...I'll use an example. Let's say I am the Millard School District and we have \$100 million that we need to invest. I go to the old Millard Bank that I went through many years ago, but by now it's been changed several times. I would go there and say I have \$100 million that I need to have taken care of, and I want it invested in an interest-bearing account. Well, they can only...by \$250,000, that is what the FDIC approves. So they can handle \$250,000 of it, but the rest of it they cannot, because that is the way the ball bounces. So what they do by using this registry, they would go out to other banks, and they would trade, basically, that money for certificate of deposits, and that money would flow back to the bank in Millard, and the other banks would have...let's say three of the banks would have \$250,000, so all \$1 million of it would be covered, and that would be deposited in an interest-bearing account in the Millard Bank, and that is how it basically is covered, and the Millard Bank would be the custodian of that account. That is what we're actually trying to make happen by using this registry. And I think Bob can explain to you how many banks are involved in that when he comes up to testify for this bill, or if I'm making some incorrections, I'm sure he can straighten them out. [LB836]

SENATOR McCOY: Any questions for Senator Pahls? Seeing none, move on to proponents for LB836. [LB836]

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ROBERT HALLSTROM: (Exhibits 1 and 2) Vice Chairman McCoy, members of the committee, my name is Robert J. Hallstrom. I appear before you today as a registered lobbyist for the Nebraska Bankers Association in support of LB836. Spelling of last name, H-a-l-l-s-t-r-o-m. I might digress a little bit to just give the committee a background of the manner in which public funds deposits have traditionally been treated and protected when they're deposited in Nebraska-chartered financial institutions, banks, and savings and loans. The state agencies or political subdivisions are authorized to deposit public funds in banks and savings and loans that are chartered or have previously been chartered in the state of Nebraska. Depending on the type of account, there are varying degrees of FDIC insurance coverage that is available. For example, until the end of 2012, funds that are deposited into a non-interest-bearing transaction account have unlimited FDIC insurance coverage. All other accounts that are interest-bearing have the \$250,000 FDIC insurance coverage level that Senator Pahls referred to. Traditionally, the rule has been to the extent that those public funds are in excess of the FDIC insured amounts, the bank is required to either provide securities or deposit-guarantee bond for the safekeeping of that excess balance over and above FDIC coverage. There was a change in 2004 that provided an alternative method that essentially allows a bank and a governmental entity to avoid both having to furnish securities, or to monitor the collateral in the case of the governmental entity, and that was the CDARS program, the Certificate of Deposit Registry Asset Service (sic: Certificate of Deposit Account Registry Service) that was referred to by Senator Pahls, that basically allows, and I've got an example on page 2 of my written testimony that says, if you have \$1 million, if that is in a non-interest-bearing transaction account, it's all FDIC insured, end of story, nothing more is required. If it's placed into an interest-bearing certificate of deposit or time deposit, the second alternative is for the bank to cover \$250,000 of that with FDIC insurance coverage and furnish securities or a deposit guarantee bond is required by law for the balance of the account. What was authorized in 2004 is the use of a deposit placement service, which essentially says, when I get \$1 million in, \$250,000 stays in-house, it's FDIC insured. I, in \$250,000 increments, go out to three other banks that are participating in the deposit placement service, place those funds there where each of those accounts are also fully insured by the FDIC, and in return or exchange, I get three separate \$250,000 deposits back into my financial institution. So all of the funds that are public funds are FDIC insured. The local bank has retained the customer relationship, and the requirement for additional securities to be pledged is removed as well as the requirement for monitoring that. In 2011, July 21, 2011, pursuant to the Dodd-Frank Act, for the first time banks were allowed to pay interest on business checking accounts, so we now have public fund money market deposit accounts, if you will, that could be interest-bearing. They would be subject to a \$250,000 FDIC insurance deposit limitation. The deposit placement service that was referred to by Senator Pahls, the Insured Cash Sweep program, basically provides the same type of treatment for interest-bearing transaction accounts or interest-bearing money market deposit accounts as I described in my \$1 million

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example for certificates of deposit and time deposits. So we are essentially taking existing law, just expanding it to make sure that the entire array of interest-bearing accounts that can be utilized for public funds will be subject to being utilized under these deposit placement programs. I have submitted an amendment for consideration by the committee. Some questions were raised as to whether or not the use of the word "shall," as opposed to "may," was somehow saying that this deposit placement service would be the only manner in which you could hold public funds in interest-bearing transaction accounts. That certainly is not the intent nor has it been the practice, but the amendment that we have will clarify that both the traditional method of \$250,000 of insurance with securities pledged for the balances available continues to be available to financial institutions as well as the system or methodology under the deposit placement service program. With that, I would be happy to address any questions of the committee. [LB836]

SENATOR McCOY: Senator Gloor. [LB836]

SENATOR GLOOR: Thank you, Mr. Chairman. Mr. Hallstrom, I think I understand how this helps the bank or savings and loan, but how does that...how does this find its way down as benefit to the state or political subdivision? [LB836]

ROBERT HALLSTROM: I think that the state agencies or political subdivisions that have used the program have been very pleased with it, Senator. There are obligations taken on by the governmental entities to monitor collateral. If you are furnishing securities, the state statute requires that the securities be pledged in a certain percentage above and beyond the amount of the deposit that exceeds FDIC insurance coverage, so a diligent governmental entity will have some monitoring system periodically that they will ensure that the securities that have been pledged by the bank are, in fact, those that are authorized by the statute and in the amounts that are required by the statute. So in that respect, there is some type of benefit to the governmental entity from not having to employ that type of review of the securities. [LB836]

SENATOR GLOOR: Okay. Thank you. [LB836]

SENATOR McCOY: Any other questions? Oh, Senator Schumacher. [LB836]

SENATOR SCHUMACHER: A couple. What is the CDARS program? [LB836]

ROBERT HALLSTROM: Well, I butchered it without looking at it. It's the Certificate of Deposit Account Registry Service, and it is a company that was established, and I think, Senator, probably initially in its inception was looking at providing a method for individual customers who wanted to have the ability to have full FDIC insurance coverage for their deposits because state law prohibits banks from pledging securities for private deposits. We're mandated to do so for public deposits, but we're prohibited

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from doing so for private deposits, so I think that is where the inception of the idea for a private company to develop this deposit-placement service where participating financial institutions, in essence, exchange or swap accounts of like amounts so that there is full FDIC insurance coverage all the way through for the accounts, and it evolved into a mechanism that makes sense and is beneficial in the public funds arena as well. [LB836]

SENATOR SCHUMACHER: So basically, you take the \$1 million to the bank, and that banker then subs out three-quarter-of-a-million-dollar bites to different banks... [LB836]

ROBERT HALLSTROM: Correct. [LB836]

SENATOR SCHUMACHER: ...kind of leveraging their access to the FDIC? [LB836]

ROBERT HALLSTROM: Exactly, and in return, gets the money back so that the money for purposes of making loans, reinvesting in the community, the bank still has the full amount of funds locally. [LB836]

SENATOR SCHUMACHER: Explain that step to me. I'm a little sketchy on what is happening there. So the money goes to bank one, bank one deposits that in bank two, three, and four, gets CDs back... [LB836]

ROBERT HALLSTROM: Yes, of like amount. [LB836]

SENATOR SCHUMACHER: ...of like amount. And then how does the money get back from banks two, three, and four to the community? [LB836]

ROBERT HALLSTROM: Well, it's subject to withdrawal, just as if it would normally be, in the receiving bank. [LB836]

SENATOR SCHUMACHER: Who owns the CDs then from banks two, three, and four? [LB836]

ROBERT HALLSTROM: The original political subdivision. [LB836]

SENATOR SCHUMACHER: Okay. So really, what the bank is doing is just kind of brokering that, those three other CDs. [LB836]

ROBERT HALLSTROM: In essence. [LB836]

SENATOR SCHUMACHER: And the FDIC obligation... [LB836]

ROBERT HALLSTROM: I wouldn't say brokering in terms of FDIC regulatory parlance,

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but... [LB836]

SENATOR SCHUMACHER: Right, but middle-manning the thing, managing, whatever, agenting... [LB836]

ROBERT HALLSTROM: Yep. [LB836]

SENATOR SCHUMACHER: ...and then the local subdivision is the one who would have the claim on the FDIC in the event one of those banks fizzled. [LB836]

ROBERT HALLSTROM: And full access to their funds during the period of time that they're in those financial institutions. [LB836]

SENATOR SCHUMACHER: Thank you. [LB836]

SENATOR McCOY: Senator Pirsch. [LB836]

SENATOR PIRSCH: Just from a big-picture perspective, these are...such transactions in over \$250,000 are somewhat common, correct? [LB836]

ROBERT HALLSTROM: Yes. [LB836]

SENATOR PIRSCH: And just looking at alternatives, if this type of structuring doesn't exist then, and because you only have the capacity to \$250,000, what is the alternative that is taking place now? [LB836]

ROBERT HALLSTROM: Well, the alternative is that the bank can and does, in some cases, retain, in my example, the entire \$1 million in-house, let's call it. So they've got the entire \$1 million in the bank of deposit, \$250,000 is insured by FDIC, and state law, to the extent that the bank has a balance of public funds in excess of the FDIC insured amounts, has to furnish securities or provide a deposit guarantee bond for the protection and safeguarding of that excess balance. [LB836]

SENATOR PIRSCH: I would assume those are eventually passed along to the customers, the bank, and the community. Any transactional costs, in other words, cost for existing and doing banking by a community bank ultimately has to be borne by the people in the community. [LB836]

ROBERT HALLSTROM: I would assume, Senator, that the cost of having to furnish securities are arguably built into the rate that is paid or in some form or fashion is sent on down the line. [LB836]

SENATOR PIRSCH: Thank you. [LB836]

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SENATOR McCOY: Senator Schumacher. [LB836]

SENATOR SCHUMACHER: How does the fact that the bank under this mechanism relies on the FDIC for security and under the other mechanism goes out and has to buy a bond or a thing, how does that affect the bank's balance sheet and their ability to leverage their equity? [LB836]

ROBERT HALLSTROM: I don't think it has any impact, Senator, if I'm tracking your question. The bank still maintains and has the same amount of deposits in their facility as they would if they had accepted the \$1 million up-front and not farmed out the \$250,000 increments to other financial institutions. You still have \$1 million in deposits on your books from which: a) you have to maintain capital; b) you have for lending purposes, etcetera, etcetera. [LB836]

SENATOR SCHUMACHER: I think I understand. Thank you. [LB836]

SENATOR McCOY: Any other questions for Mr. Hallstrom? Seeing none, thank you. [LB836]

ROBERT HALLSTROM: Thank you, Senator. [LB836]

SENATOR McCOY: Any other proponents of LB836? Any opponents? Any neutral testifiers for LB836? Seeing none, Senator Pahls, closing. [LB836]

SENATOR PAHLS: Yeah. Just one fast statement here. I think whoever established this service found a niche. It's that simple, so those of you who are going to retire sometime, find your niche (Laughter). Thank you. [LB836]

SENATOR McCOY: Thank you. I believe that concludes today's... [LB836]