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Banking, Commerce and Insurance Committee
January 30, 2012

[LB963 LB964 LB965 LB1004]

The Committee on Banking, Commerce and Insurance met at 1:30 p.m. on Monday, January 30, 2012, in Room 1507 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on LB963, LB964, LB965 and LB1004. Senators present: Rich Pahls, Chairperson; Beau McCoy, Vice Chairperson; Mark Christensen; Mike Gloor; Chris Langemeier; Pete Pirsch; and Paul Schumacher. Senators absent: Ken Schilz.

SENATOR PAHLS: Are we on? Fellow Senators, we are on, just to let you know. I want to welcome you to the Banking, Commerce and Insurance Committee hearing today. My name is Rich Pahls. I'm from Omaha, and I represent District 31. We are going to take up the bills as posted. I will read them off. It will LB963, (LB)964, (LB)965, they made it convenient the way they put them in order there, and LB1004. To better facilitate today's meetings, I'm just going to have you take a look at a few of the procedures we would like to have everyone follow. It would make everyone's life easy if you would do that. If you have written testimony that you need to submit, please have 10 copies available. If not, you do not have 10 copies, wave your hand, and we will send a page to get some. I see no hands waving. Also, I'm asking you if you do testify today, you do give that form to Jan sitting over here. And we'll move right on to I'll introduce committee counsel, Bill Marienau, who keeps us legal, and Jan Foster, who keeps us going on the right path, hopefully. And I think we'll start now with introductions. I know Senator Schilz will be absent today. Senator Schumacher, I think, is testifying right now. Then we'll start with you, Senator Langemeier.

SENATOR LANGEMEIER: Senator Chris Langemeier, Schuyler.

SENATOR PIRSCH: Senator Pete Pirsch, District 4, Douglas County and parts of Omaha.

SENATOR McCOY: Beau McCoy, District 39, Omaha.

SENATOR CHRISTENSEN: Mark Christensen, District 44, Imperial.

SENATOR PAHLS: And Senator Gloor is also testifying right now. For those...I think everybody here has been around long enough to know that senators come and go. And our pages are Michael Killingsworth; Michael, wave your hand, if you do need some help, and Matt McNally also. I think we are ready to begin, and we will start with our first one, (LB)963. And I'll be introducing this on behalf of the Department of Banking and Finance. And my opening of this bill will be, we'll let the director speak to us. We are ready when you are, Director.

JOHN MUNN: (Exhibit 1) Chairman Pahls, members of the Banking, Commerce and

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Insurance Committee, my name is John Munn, last name spelled M-u-n-n, director of the Nebraska Department of Banking and Finance. I'm appearing today in support of LB963 which was introduced at the request of the department. LB963 contains four substantive updates to the laws relating to depository financial institutions that are under the jurisdiction of the department. Two of these updates result from the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act signed into law by the President in July, 2010. Section one of LB963 would amend section 8-141 of the Nebraska Banking Act, which is the bank lending limit statute to authorize state banks to engage in derivative transactions in the manner and to the extent of credit exposure determined by the department. State banks may currently engage in derivative transactions, but under section 611 of the Dodd-Frank Act may only continue to do so until January 21, 2013, unless the state specifically incorporates the authority to do so into its lending limit statute. National banks will operate under similar federal restrictions. The amendment includes definition of the terms derivative transaction and loan that mirror the federal definitions. This section carries an operative date of January 21, 2013. Section 613 of the Dodd-Frank Act prompts the updates to the Interstate Branching by Merger Act of 1997 contained in sections 14 through 21 of LB963, and the harmonizing amendments to the Nebraska Banking Act found in sections 2 and 3 of that bill. Current law authorizes a Nebraska bank to branch across state lines only if it purchases a bank in another state that is at least five years old and converts the offices of the acquired bank to its own branches. Once the interstate merger is complete, the Nebraska bank is allowed to establish additional branches in that state. Out-of-state banks have the same limitations on branching into Nebraska. Dodd-Frank preempts these restrictions and allows banks to establish branches outside their home state without first having to purchase another bank. The amendments proposed by LB963 will rename the act as the Nebraska Interstate Branching and Merger Act, provide clear authority for de novo interstate branching, retain the ability of Nebraska banks to acquire and be acquired by an out-of-state bank, coordinate the powers that may be exercised by Nebraska banks operating in another state with those that an out-of-state bank may exercise in Nebraska, and repeal the obsolete sections. The bill also contains several updating amendments to this act that are not necessitated by Dodd-Frank. These include clarifying the authority of the department to conduct examinations of Nebraska branches of out-of-state, state-chartered banks extending the department's authority to determine whether the proposed name of a bank or bank branch is confusingly similar to the name of an existing bank office to branches in Nebraska of out-of-state banks, and updating the statute setting limits on deposits that can be controlled following an interstate merger transaction to conform to amendments made in prior years to section 8-910 of the of the Bank Holding Company Act. The next substantive proposal that I want to discuss is set forth in section 5 of LB963 with coordinating language updates in sections 6 through 10. Section 8-209 currently requires trust companies and depository financial institutions with trust powers that have offices in Nebraska to pledge securities to the department. The amendment would require out-of-state trust companies and entities without a Nebraska office that may be appointed as trustees in Nebraska to pledge

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securities to the department to be held against losses in the pledging entity's administration of trusts. As an out-of-state trustee with no Nebraska location may now serve as a trustee for Nebraska property without pledging securities, this amendment should improve the safety of trust funds so held. The fourth and final portion of LB963 is the reenactment of the wild card statutes for banks, savings and loan associations, and credit unions. These statutes provide equal rights, powers, and privileges between Nebraska's state-chartered depository financial institutions and their federal counterparts, but are required to be reenacted on an annual basis due to the Nebraska Constitution. Sections 4, 11, and 21 contain these updates. I want to thank Senator Pahls for introducing LB963. I'll be happy to answer any questions. [LB963]

SENATOR PAHLS: Senator Pirsch. [LB963]

SENATOR PIRSCH: Thanks for your testimony here today, Director. With respect to the feature for your preempting, well, Dodd-Frank's preempting the restriction allowing banks to establish branches outside their home state without first having to purchase another bank. I guess you called that Nebraska Interstate Branching and Merger Act. And it...okay, so it's retaining the ability of Nebraska banks to acquire and be acquired by out-of-state banks, right? That's not changing with that respect. [LB963]

JOHN MUNN: Correct. [LB963]

SENATOR PIRSCH: So it's just the...you don't have to purchase another bank. Is this going to be, is this a pretty sweeping move within the evolution of the industry, or is this liable to have, you know, very great transformative effects upon the industry in another five or ten years from now, or not really marginal? [LB963]

JOHN MUNN: It's hard to speculate. I know one reason for the legislation was federal thrifts have been able to do this for years, to branch into other states without purchasing their way in. In effect, de novo branching, and that has been done in Nebraska in the past. Hard to tell. May have a greater impact near our state's borders around the state. [LB963]

SENATOR PIRSCH: Okay, and the only other question that I wanted to ask at this time with respect to your, the first update from Dodd-Frank that deals with authorizing state banks to engage in derivative transaction, the manner extent...so the definitions you say mirror the federal definitions. Is that out of, is that what the federal act requires, or is that something that just out of prudence you've adopted? [LB963]

JOHN MUNN: Just out of prudence, because we do have nationally and federally chartered institutions operating in Nebraska, so we're trying to be in sync as much as we can for our state-chartered institutions. [LB963]

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SENATOR PIRSCH: Thank you. [LB963]

SENATOR PAHLS: Senator Langemeier. [LB963]

SENATOR LANGEMEIER: Thank you, Chairman Pahls, and Director, thank you. [LB963]

JOHN MUNN: Um-hum [LB963]

SENATOR LANGEMEIER: I have a question about in your testimony page two on that section 5, and you talk about trustees. [LB963]

JOHN MUNN: Um-hum. [LB963]

SENATOR LANGEMEIER: Prior to Dodd-Frank, could a lending institution act as a trustee in Nebraska if they didn't have a location here? [LB963]

JOHN MUNN: Well, I don't know that Dodd-Frank had any impact on this, so my answer would be yes, they could. [LB963]

SENATOR LANGEMEIER: So they could, if they were not a financial institution located in Nebraska, they could be a trustee for real estate within the same. [LB963]

JOHN MUNN: Correct. [LB963]

SENATOR LANGEMEIER: Thank you. [LB963]

SENATOR PAHLS: Senator Pirsch. [LB963]

SENATOR PIRSCH: Since I kind of broached the topic, and I'll be quick. With respect to the nature of derivative transactions that are currently...under current law, banks are allowed to operate in that fashion. But what is the limitations that have been set out for restrictions in terms of derivative? Obviously, a number of different types of derivative transactions, but what is permitted currently, and what is not permitted? [LB963]

JOHN MUNN: Sure. Just to give you an idea of the volume of derivative transactions currently used by Nebraska state-chartered banks, and this is available because it's a required entry on the call report, we supervise about \$29 billion of Nebraska banking assets in the 175 banks that we supervise. Total derivatives among those banks, as of September 30, were about \$766 million, so relatively small. The vast majority, there's several types of derivatives, the vast majority, as you expect, are industry contracts as far as trying to... [LB963]

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SENATOR PIRSCH: Mostly hedges? [LB963]

JOHN MUNN: ...exactly, to try and protect an institution from significant swings in interest rate. What's going to be necessary between now and January 21 of next year is to get our arms around what the credit risk is in a derivative transaction. And I don't see any one state going off and creating its own algorithm in that regard. I think it's something we're going to want to work with very closely with other state regulators and also with federal regulators, because like each of our state-chartered banks, it's also supervised by either the FDIC or the Federal Reserve Bank of Kansas City, so we want to be on the same page with other regulators. But to identify the impact it's going to have depends how credit risk is defined. [LB963]

SENATOR PIRSCH: Well, they're certainly very complex and a lot harder to regulate than your traditional type of banking activities, but... [LB963]

JOHN MUNN: And they got a terrifically bad name. I'm not here to argue of their worth, but over the last three or four years with the sub-prime mortgage loans, there were derivatives used in placement of those. And derivatives are as strong in at least two ways. The strong is the underlying instrument that's being derived, and then also the strength of the counterparty. And in those cases, our banks deal with counterparties, major banks across the country where that's not a concern. [LB963]

SENATOR PIRSCH: Are we doing any substantive amount of credit default swaps? [LB963]

JOHN MUNN: No, no, our banks are not. [LB963]

SENATOR PIRSCH: Okay, and I suppose the best way to then approach that, there will be a, maybe a NAIC, I'm not...strike that. But a kind of, well, I guess that's, that's the question I put to you. Is it going to be the states coming together with sort of a model in terms of regulator, or is it going to be a federal congressional model that's imposed? [LB963]

JOHN MUNN: Well, selfishly, I hope it falls to a federal...well, a panel called the Federal Financial...Federal Financial Institutions Examination Council, in which the heads of the federal regulators and then one representative state financial regulator serve on that council. I've represented all the states for four years on that. I hope this ends up on our plate in that venue. The FFIEC was formed by Congress to try and promote uniformity in financial supervision. [LB963]

SENATOR PIRSCH: So you'll just come back to us in future years and ask us to adopt the standards. [LB963]

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JOHN MUNN: Well, I'm not sure that it will need to be made a part of statute. You know, because what we're looking for is a definition of derivative, the credit risk in a derivative. [LB963]

SENATOR PIRSCH: So you would have the inherent authority to deal with that? [LB963]

JOHN MUNN: I may. I'm not...and it might come to you anyway. [LB963]

SENATOR PIRSCH: Okay. Thank you, Director. [LB963]

SENATOR PAHLS: Seeing no more questions, thank you for your testimony. Proponents? [LB963]

JERRY STILMOCK: (Exhibit 2) Good afternoon, Chairman Pahls, members of the Banking, Commerce and Insurance Committee. My name is Jerry Stilmock, and I appear before you today on behalf of my client, the Nebraska Bankers Association, in support of LB963. As testified by Director Munn, LB963 contains a number of provisions supported by the NBA, which include the wild card provision, requiring out-of-state trust companies without a Nebraska office to pledge securities to the department. Implementing a couple of provisions of Dodd-Frank, particularly to amend the state charter bank lending limits to include credit exposure from derivative transactions and the issue of de novo interstate branching. Each year, we support the department's efforts to renew the state-chartered bank and savings and loan wild card statutes to incorporate any changes in federal laws as they relate to rights, privileges, powers, benefits and immunities for our Nebraska banks. In addition, the two provisions now that consider need to be changed because of Dodd-Frank. First, the act requires state law to regulate the manner and extent to which banks may engage in derivative transactions involving credit exposure. LB963 addresses this requirement of federal law by authorizing state banks to engage in derivative transactions in the manner and to the extent of credit exposure determined by the director of the Banking Department. The provisions of (LB)963 relating to state bank lending limits take effect on January 21, 2013, as allowed by federal law. As the last series of questions by Senator Pirsch and Senator Munn...Senator Pirsch and Director Munn, pardon me, Director, that we're hopeful that maybe we do get some guidance from either Congress or the federal regulators to provide the definition of credit exposure. Secondly, then the Dodd-Frank would preempt provisions of state law that place restrictions on the ability of an out-of-state bank to branch into Nebraska on a de novo basis. Prior to the passage of the federal act, Nebraska adopted the most restrictive laws allowed with respect to de novo branching activities of an out-of-state bank by only allowing entry into Nebraska by an out-of-state-bank which had acquired a Nebraska financial institution that had been in existence for at least five years. The NBA had been continually opposed to efforts to remove the ability of banks to restrict entry out-of-state banks, but federal law now

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preempts that, and those restrictions have now been removed, thereby allowing those de novo banks to come into Nebraska. In closing, we, on behalf of the Nebraska Bankers, would like to thank Director Munn and his staff for the cooperation and sharing of the LB963 in advance and incorporating many of the technical suggestions that we at the NBA had. For the reasons stated by myself and Director Munn, we would ask the committee to advance the bill to General File. Thank you. [LB963]

SENATOR PAHLS: Seeing no questions, thank you for your testimony. [LB963]

JERRY STILMOCK: Thank you, Senator. [LB963]

SENATOR PAHLS: Proponents? [LB963]

BRANDON LUETKENHAUS: Mr. Chairman, members of the Banking, Commerce and Insurance Committee, my name is Brandon Luetkenhaus. It's B-r-a-n-d-o-n, last name L-u-e-t-k-e-n-h-a-u-s, and I'm here on behalf of the Nebraska Credit Union League. Our association represents 96 percent of the 71 credit unions in Nebraska, and therefore 435,000 members. And I appear before you today in support of LB963. I want to thank Senator Pahls and Director Munn for their work on this legislation. We're particularly interested in the wild card provision that's renewed each year. This provides our state charters the same powers, rights, and privileges as our federal charters, and so that helps to promote our dual chartering system where credit unions can move from a federally charter to a state or state to a federal. For this particular reason, we do support LB963 and would urge the committee to support it as well. [LB963]

SENATOR PAHLS: Seeing no questions, thank you for your testimony. Proponents? Opponents? Neutral? That will close the hearing on (LB)963. We will begin our hearing on (LB)964. Director. [LB963]

JOHN MUNN: (Exhibits 1 and 2) I might ask for a glass of water if I may, and I might encourage a round of waters, as this next one is a (laugh) little lengthy. [LB964]

SENATOR PAHLS: And also, would you...will you prop open the doors, and the outside doors? Maybe some air flow will help. I think we're ready. [LB964]

JOHN MUNN: Chairman Pahls, members of the Banking, Commerce and Insurance Committee, my name is John Munn, last name spelled M-u-n-n. I'm director of the Nebraska Department of Banking and Finance. I'm appearing today in support of LB964, which was introduced at the request of the department. LB964 proposes the adoption of the Nebraska Money Transmitters Act and the concurrent repeal of the existing Nebraska Sale of Checks and Funds Transmission Act. This legislation will enhance and modernize regulation of the industry which is engaged in the transmission and sale of money, including electronic payment instruments, stored value, travelers'

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checks and money orders. Nebraska initiated its regulation of this industry in 1965 along with 19 other states in response to what the legislative history describes as several gigantic money order swindles uncovered in the states of California, Georgia, South Carolina, and Tennessee. The original Nebraska Sale of Checks Act has been amended a number of times since 1965, including 2001 revisions that renamed the act to more accurately reflect that jurisdiction of the act extended to electronic funds transmission. However, most of these amendments were technical in nature, and the substance of the act has remained largely unchanged since it was first enacted 46 years ago. There has been significant growth in the industry over that time. When I became director of the department in January of 2005, the department licensed 30 companies. Today the department licenses 61 different companies offering services from approximately 2,200 physical locations in Nebraska. Most of the increase can be attributed to advances in technology, an increased number of issuers of prepaid stored value, and an increase in the diversity of Nebraska's population. In 1965, most of the instruments sold were paper instruments like travelers' checks and money orders. Today, some licensees do not issue paper instruments at all. Instead, these licensees transfer funds electronically from various store fronts or provide services over the internet which can be accessed by customers through their computers or portable devices. Licensees such as PayPal facilitate the purchase of goods, and licensees such as American Express offer prepaid cards for global use. As technology continues to evolve, we expect more companies to offer even more innovative services. Nebraska's population continues to diversify, and that has further contributed to the increase in the number of licensees. More and more companies provide funds transmission services targeted to immigrant communities in Nebraska, including those of Hispanic, Vietnamese, and Somali origin. Members of these communities support family members in their native countries and use the services of licensees such as Sigue and Dahabshill to transmit funds globally. In preparing this legislation, the department reviewed other states' laws and learned the majority of the states have updated their laws based on a model legislative outline issued by the Money Transmitter Regulators Association, a group of state regulators. We also reviewed the Uniform Money Services Act issued by the National Commissioners on Uniform Law in 2000 and amended in 2004, which has been adopted by six states. Our research led us to the conclusion that the North Dakota Money Transmitter Act enacted in 2005 provides the most appropriate model for Nebraska. Wyoming, South Dakota, and Minnesota have all enacted extremely similar versions of this act. LB964 incorporates certain provisions of the current act including the fee structure, bonding structure and net worth requirements. Despite the movement towards uniformity, these particular issues will vary significantly between the states. The amounts we currently require in these three areas are in the middle range of amounts other states require. We had no compelling reason to revise the current amounts. The bill also incorporates procedural statutes that are found in the current act and in other acts under the jurisdiction of the department. LB964 retains application, change of control and appeal procedures, and provisions regarding surrender, expiration and cancellation of a license. The Nebraska Money Transmitters Act will define money

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transmission as a business for the sale or issuance of payment instruments or stored value, the receiving of money or monetary value for transmission to another location by any means, and certain bill payment services. Payment instruments may be written or electronic, while stored value is monetary value evidenced by an electronic record, but not an instrument. These definitions are key to the coverage of the act and provide uniformity in regulation across state lines. LB964 contains a significantly updated list of exemptions compared to current law, reflecting the growing use of electronic monetary transactions. The bill will exempt governments and government agencies including the United States postal service, contractors providing governmental electronic benefit transfers, and operators of specified limited payment processing systems. Financial institutions are exempt, exempted under current law, and would continue to be under LB964 along with their subsidiaries and holding companies. A major distinction between the new act and current law relates to the licensee-agent relationship. The existing act makes only minimal reference to agents and provides no separate regulatory authority or guidance for the entities that conduct business on behalf of the licensee. The new act adopts the uniform term and definition of authorized delegate in place of the term agent. Authorized delegates and licensees must enter into written contracts. Conduct standards for authorized delegates are set forth including adherence to a licensee's written procedures and the handling and remission of money owed to the licensee. The department is given new authority to cancel an authorized delegate's contract and take other disciplinary action against those entities. Thirty-six other states and three territories have similar enforcement authority as to authorized delegates. LB964 provides the department with the ability to monitor liquidity of licensees, which is an important consumer protection factor. Money transmitters collect money from a customer and then pay that money to another party, either when the recipient claims the electronic transfer or presents the payment instrument. Therefore, the illiquidity of a licensee poses a significant risk of harm to consumers. LB964 mandates the licensees keep sufficient liquid funds in permissible instruments to cover such obligations and to report those holding to the department annually. The act then declares these funds to be held by the licensee in statutory trust on behalf of its customers. This is an important distinction in the event a licensee files for bankruptcy protection. Bankruptcy courts use state law to determine the debtor's property rights. Since these funds are declared to be the property of the customers, they would not constitute property of the bankruptcy estate and could not be used to pay other creditors of the debtor. Thirty-four states and three territories have identical requirements regarding permissible instruments...excuse me, permissible investments. All current Nebraska licensees hold a similar license in a state that already has a permissible investment statute, so no additional burden is imposed. After LB964 was introduced, the department was contacted by Ezra Levine, counsel for the Money Services Round Table, a group composed of the larger money transmitters who suggested three clarifying revisions. We believe those revisions provide clarity to the bill. I would offer committee amendment AM1756 at this time, and those copies were distributed. The amendment would remove the phrase, "or authorized delegate," from the definition of controlling person. This phrase is

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superfluous, as the bill makes no further reference to a controlling person of an authorized delegate. The second change amends the definition of money transmitter by adding the phrase, "but does not include bill payment services in which an agent of the payee receives money or monetary value on behalf of that payee." This clarifies that a money transmitter does not include an agent of a payee who receives funds on behalf of that payee. Finally, the phrase "or authorized delegate" is replaced with "in this state" in section 25 of the bill to clarify that the amount of the surety bond is based on the number of locations within this state and not the number of authorized delegates that the licensee has in this state. The business of money transmission will continue to develop and expand in the coming years. I believe that LB964 provides the state with the tools to monitor these advances and protect our consumers under a more uniform and less burdensome regulatory system. I want to thank Senator Pahls for introducing LB964 and ask the committee to advance the bill with the offered amendment. I would welcome any questions. [LB964]

SENATOR PAHLS: Senator Pirsch. [LB964]

SENATOR PIRSCH: Okay, so the reach or the breadth of this then, LB964, would go towards transmission and sale of money, electronic payment instruments, stored value, travelers checks and money orders. It doesn't reach the network, so to speak, like software like TESIS or Heartland or anything along those lines? [LB964]

JOHN MUNN: What's their function? [LB964]

SENATOR PIRSCH: Well, the financial transaction network. [LB964]

JOHN MUNN: No. [LB964]

SENATOR PIRSCH: This is just purely, essentially cards and what not that are, okay. And...well, that's all the questions I have. Thanks. [LB964]

SENATOR PAHLS: Seeing no questions, a lot to digest here. Thank you. Proponents? Opponents? Neutral? [LB964]

KATHY SIEFKEN: Chairman Pahls and members of the committee, my name is Kathy Siefken, K-a-t-h-y S-i-e-f-k-e-n. I am the registered lobbyist and executive director of the Nebraska Grocery Industry Association. And we actually own and operate a money order company from, and it is a wholly-owned subsidiary of the Nebraska Grocery Industry Association. And the reason I'm testifying neutral is because we really understand that you do need to update definitions and make clarifications at times. However, this bill was...what this bill does is it completely repeals an existing act, and it drops new language as replacement. And as far as I can determine, the Banking Department did not come to anyone in the industry that is being regulated by this bill. In

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our opinion, and in working with other regulatory agencies, we have always been invited to the table to talk about any changes, especially wholesale changes like this that completely repeal an act and adopt a new language. There was a section that I was particularly concerned about, it was section 25. I visited with Bill this morning, and he made me feel a little bit more at ease with that language and the fact that the director is bringing an amendment. And there were three things that were suggested by Ezra Levine, who is really the money order specialist and the money transmitter specialist, and we recognize him as such in the United States. He probably knows more about money transmitting and the laws and regulations in the nation than anyone else. So that made me feel a little bit more at ease, but the fact is, we were not invited to the table. We did not have an opportunity to discuss any of the changes that this brings about, and for that reason, we can't support the bill. If you have any questions, I'd be happy to try to answer some. [LB964]

SENATOR PAHLS: Well, one question I have, if you have conflict with the bill, because as I read it, it has not really been played with much for quite a long time. [LB964]

KATHY SIEFKEN: Correct. [LB964]

SENATOR PAHLS: And you've given Ezra Levine a lot of credit. I do not know the person, but you've given him, it seems to me that his suggestions are clarifying. [LB964]

KATHY SIEFKEN: Yes, and so since Ezra has taken a look at it, and those are the suggestions that he's made to clarify, we would support that simply because Ezra is someone that serves as a consultant to our industry. So I approve that, however, in the state of Nebraska there wasn't even an interim study. There was no notice that this was coming, and there's a lot of information that is apparently being changed in the bill. And industry probably, I'm suggesting that industry should have been given a chance to provide some input. I'm not sure that we would have made any changes, but it would have made me feel more comfortable knowing that we had an opportunity to sit down and look at each section and know what each section change is really doing. [LB964]

SENATOR PAHLS: Okay, and I understand the need to feel part of it, but I don't see a number of people as opponents or even neutral speaking to this. So what is this then, just a general lack of concern on their part then? [LB964]

KATHY SIEFKEN: I can't speak for everyone else. I can only tell you that the people that I spoke to in the state of Nebraska that represent these different entities didn't seem overly concerned about it. I, on the other hand, want to know that I am representing the people I'm representing very thoroughly before I can just let something go. [LB964]

SENATOR PAHLS: Okay, and I understand where you're coming from. Do you have any, I don't know how long you've studied this bill, have you any particular parts of it you

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said then they missed the boat? [LB964]

KATHY SIEFKEN: When you, when you completely repeal an existing section of law and then replace it with another law, it's very difficult to go back and forth and figure out what the changes are. [LB964]

SENATOR PAHLS: Okay. [LB964]

KATHY SIEFKEN: And so I started looking at it the end of last week. I talked to Patty, she forwarded...over at banking, and she forwarded the section-by-section changes. I went through those. There were three areas that I was concerned about. I talked to Bill this morning, and he helped me understand what those sections did. So without having more input than that... [LB964]

SENATOR PAHLS: Okay. [LB964]

KATHY SIEFKEN: ...it's not something that we would support, nor would we really oppose it if it is clarification only. But I don't know exactly what changes are made and what are not... [LB964]

SENATOR PAHLS: Okay. [LB964]

KATHY SIEFKEN: ...because of the way the bill was, the original language is repealed and the new one is dropped in. [LB964]

SENATOR PAHLS: Okay. [LB964]

KATHY SIEFKEN: It's difficult to see that. [LB964]

SENATOR PAHLS: Okay, okay. Seeing no more questions, thank you for your questions...your testimony. [LB964]

KATHY SIEFKEN: Thank you. [LB964]

SENATOR PAHLS: Any other neutral? That will close the hearing on (LB)964. We are now ready for (LB)965, and Director, I'd like to have you come forth. I think we are ready, Director. [LB964]

JOHN MUNN: (Exhibit 1) Chairman Pahls, members of the Banking, Commerce and Insurance Committee, my name is John Munn, last name spelled M-u-n-n. I'm director of the Nebraska Department of Banking and Finance. I'm appearing today in support of LB965, which was introduced at the request of the department. LB965 would amend and update three sets of consumer finance laws under the jurisdiction of the

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department, the Nebraska Installment Sales Act, the Residential Mortgage Licensing Act, and the Nebraska Installment Loan Act. The first nine sections of the bill apply to the Nebraska Installment Sales Act. This act governs transactions in which a buyer acquires goods or services pursuant to a contract that permits payments over time. Companies which purchase these contracts from the seller of the goods or services are known as installment sales companies or sales finance companies, and are required to be licensed with the department. As an example, automobile financing companies such as GMAC or Ford Motor Credit are licensed in Nebraska. The licensing process is the subject of these amendments. LB965 proposes to transition the current manual licensing process for installment sales companies onto the electronic Nationwide Mortgage Licensing System and Registry, which I will refer to as the NMLSR, in 2013. The NMLSR is a nationwide licensing and information sharing system developed by state regulators and the mortgage industry, which allows entities and individuals to complete one application and submit it to any state that is a member of the system. The system maintains licensing, testing, and disciplinary records. Regulators have instantaneous access to information posted on any licensee or applicant which benefits both our licensing and enforcement functions. The NMLSR became operational January 2, 2008, with Nebraska being one of the original eight states on the system that day. Mortgage banker firms were the first entities to be licensed through the system. As the capabilities of the NMLSR have increased, installment loan companies and individual mortgage loan originators are also being licensed or registered through the system. Since 2008, every time that the licensing resources of the NMLSR has expanded, the department came to the Legislature requesting the authority to process additional applications and licenses through the system. That is the case today. The NMLSR has informed the states that it will be capable of processing applications and licenses for other state-regulated financial service entities and industries. As a result, the department believes that the licensing process for installment sales companies should be transitioned onto the NMLSR, primarily because most of our licensees operate on a regional or nationwide basis and would benefit from the efficiencies of the NMLSR. To accomplish the transition, LB965 proposes these updates to the Installment Sales Act: Defining necessary terms, including breach of security of the system and Nationwide Mortgage Licensing System and Registry. Providing for a change in the annual license renewal date from October 1 to December 31, and allowing a processing fee payable to the NMLSR. Allowing license renewal fees and processing fees to be collected by the NMLSR, and to provide that licenses which expire on October 1, 2012, will be renewed until December 31, 2013. Providing authority for the department to participate in the NMLSR for purposes of the Installment Sales Act and establishing the requirement that installment sales companies be licensed through the NMLSR. And providing guidelines for confidentiality of information and supervisory information sharing through the NMLSR. These amendments are based on requirements currently included in the Residential Mortgage Licensing Act and the Nebraska Installment Loan Act. LB965 will also update the definition of Nationwide Mortgage Licensing System and Registry in these two acts to include the phrase, "other state-regulated financial services entities

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and industries." Two of the proposed amendments to the Nebraska Installment Sales Act are not prompted by the transition to the NMLSR. Section 5 updates the requirement for prior notice of a move of a licensee's office from 10 to 30 days, and expands the statute to allow a licensee to move outside of its county without having to be relicensed. The current restriction is obsolete. Section 7 is a housekeeping amendment to update language relating to the disposition of administrative fines. LB965 proposes amendments to the Residential Mortgage Licensing Act in response to rules released in 2011 by the United States Department of Housing and Urban Development, HUD, relating to mortgage bankers and mortgage loan originators. These federal rules will be enforced by the Consumer Financial Protection Bureau in accordance with the Dodd-Frank Act. As background, the Residential Mortgage Licensing Act implemented the federal Secure and Fair Enforcement for Mortgage Licensing Act of 2008, commonly referred to as the SAFE Act, which is incorporated into Title V of the Housing and Economic Recovery Act of 2008 and signed into law on July 30, 2008. The SAFE Act mandated that the states adopt a system of licensure for mortgage loan originators by July 31, 2009. The NMLSR, which existed prior to the SAFE Act, was enhanced to meet the requirements imposed by the SAFE Act. HUD had issued interpretative guidance related to certain SAFE Act issues in the intervening years that were incorporated into Nebraska law. The 2011 HUD rules made substantial revisions to the exemption from licensing provisions. Earlier, HUD guidance was narrowly drafted in this area. The current exemption for attorneys has been expanded to provide that attorneys representing clients in legal matters may negotiate residential mortgage terms as part of that legal representation. The exemption for individuals has been expanded to include purchase money mortgage transactions provided that the individual does not repetitively or habitually provide such financing. LB965 further proposes new exemptions for government entities. The Nebraska Investment Finance Authority, or NIFA, employees of the government or NIFA, who act as mortgage loan originators, loan processors, or underwriters in accordance with their official duties, and certain nonprofit organizations and specified employees of those organizations. The HUD rules authorized state to provide an exemption for employees who act as the mortgage loan originator on behalf of certain nonprofits. LB965 implements this exemption by providing that a nonprofit organization which promotes affordable housing or provides homeownership education or similar services and meets requirements that include providing or identifying residential mortgage loans with terms favorable to the borrower and comparable to mortgage loans and housing assistance offered under government assistance programs, may apply to the department for a certificate of exemption. Employees of the nonprofits that receive this certificate are also exempt from the act in connection with any mortgage origination activities conducted on behalf of their employer. LB965 includes the right to an appeal hearing if a certificate is denied, and the department is given the authority to examine the nonprofit's records, revoke a certificate, and to rely on certain reports. The testing requirements for mortgage loan originators will be amended in accordance with the 2011 HUD rules. The SAFE Act is inconsistent regarding the number of times an individual may take a qualifying test after failing

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before a six-month waiting period is imposed. The model state law on which our act is based contains the identical wording and inconsistency as the SAFE Act. One section provides for a total of four tests before waiting, another indicates a total of three. When implementing testing, the NMLSR was structured to give the benefit to the test taker and allowed four total attempts. The 2011 HUD rule, however, set the limit at three total attempts, and therefore, the amendment is necessary. The final change brought about by the 2011 HUD rules is to law providing for an automatic denial of a mortgage loan originator application if the person was convicted of any felony or certain misdemeanors involving fraud and dishonesty. The only exception to the automatic denial is if the individual has been pardoned for that crime. HUD has determined that an expungement should be given the same treatment as pardons, because in many states, an expungement and a pardon have the exact same legal effect. The department may still consider the circumstances of the underlying crime in determining whether to grant an application. LB965 proposes several amendments that are not HUD based. The most substantive of these is a new section authorizing the department to issue emergency orders to suspend, limit, or restrict the license of any mortgage banker or mortgage loan originator without notice or hearing upon the occurrence of specified events such as failing to increase the amount of a surety bond, failing to comply with a condition of the license, having its license suspended or revoked in any state for fraud, or refusing to permit a regulatory examination. This section provides for notification requirements, appeal rights, and emergency hearing provisions, and requires the department to initiate additional proceedings against the licensee after six months unless a hearing was requested or the license was surrendered or expired. The remaining amendments allow a mortgage banker licensee that is a sole proprietorship to request inactive status for a period of up to 12 months, clarify the standards under which an inactive mortgage loan originator licensee may return to active status, and set an advertising standard for mortgage bankers. These updates will promote more efficient regulation of the act. I want to thank Senator Pahls for introducing LB965, and I'll be happy to answer any questions. [LB965]

SENATOR PAHLS: You did say there are nine sections to this bill. It's look like the heat has gotten us. (Laughter). Seeing no questions, thank you. Any proponents? Opponents? Neutral? Any warm people out there? That concludes the hearing on LB965. It looks like we may need to pause a little bit before the next one. [LB965]

SENATOR LANGEMEIER: I think she's going to do it on behalf of the Senator, correct? [LB1004]

SENATOR PAHLS: Are you going to be? Great, great. That's what I was going to ask that we would do that. Thank you. [LB1004]

PEG JONES: Thanks. I didn't even have time to get nervous. My name's Peg Jones, P-e-g J-o-n-e-s. I'm Senator Schumacher's legislative aide, here to introduce LB1004. I

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don't know whether to read Bill's summary or ours. It's a simple bill. It would open up credit unions to...or local governments or state to deposit funds in credit unions. Any questions? I couldn't answer, but (laugh) I can write them down. [LB1004]

SENATOR PAHLS: Seeing no questions, thank you. Thank you for your introduction. Proponents? [LB1004]

BRANDON LUETKENHAUS: (Exhibit 1) Chairman Pahls, members of the Banking, Commerce and Insurance Committee, my name is Brandon Luetkenhaus, L-u-e-t-k-e-n-h-a-u-s, and I'm here on behalf of the Nebraska Credit Union League. Our association represents 96 percent of the state's 71 credit unions and their 435,000 members. I appear before you today to offer our association's support of LB1004. I want to thank Senator Schumacher for introducing what we believe to be important commonsense legislation. LB1004 would rightly include Nebraska's credit unions as a permissible depository for public funds by our political subdivisions in Nebraska. Nebraska credit unions are locally owned, not-for-profit financial institutions that are owned by their members. From a public policy perspective, we believe there are numerous benefits when allowing local governments to deposit funds into federally insured not-for-profit credit unions. First, we believe doing so would increase competition for public funds deposits and therefore produce better rates of return for public dollars. According to DataTrac, an average...the average Nebraska credit unions are currently paying 14 basis points higher on one-year certificates than Nebraska banks. Secondly, the deposits would stay in the local community and therefore could be used in making loans to the citizenry. Third, communities would have greater local control by having the ability to choose for themselves where they would like to deposit their public funds, whether that be a bank, a credit union, or mutual savings bank. And fourth, communities would be able to retain and possibly increase jobs in their communities by supporting the local businesses that serve their people, including their local credit union. Furthermore, 25 states, other states, already expressly authorize public deposits in local credit unions including most recently New Jersey. Governor Chris Christie signed a bill last year to allow credit unions in New Jersey to accept public funds. In Nebraska's state statutes, credit unions are the only federally insured financial institution which are not included on the list of permissible depositories for public funds. Every Nebraska credit union is federally insured by the National Credit Union Administration, or NCUA, through the Share Insurance Fund. That means that each account at a credit union is federally insured up to at least \$250,000, as bank accounts are through the FDIC. Both Credit Union Share Insurance Fund and the FDIC have the full faith and backing of the United States Government. Since the Share Insurance Fund...Credit Union Share Insurance Fund has been in existence, no member has ever lost a penny of federally insured funds. At the end of the third quarter in 2011, the equity ratio for the Credit Union Share Insurance Fund was 1.31 percent, according to the NCUA, while the FDIC reported their fund to have a .12 equity ratio. So I believe any indication that the Share Insurance Fund of credit unions is somehow

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weaker than the FDIC, I believe, is incorrect. LB1004 adds credit unions to the definition of what is a qualified financial institution. As a qualified mutual financial institution, state statutes do not require that the state or political subdivision become an owner nor acquire voting rights in order to deposit public funds in such an institution. Federal laws governing NCUA deposit insurance, or the Federal Credit Union Act, authorize federally insured credit unions to accept deposits from nonmember public units and political subdivisions. A credit union would not need to change their charter, nor their bylaws, to accept public deposits. You may hear those opposed to this bill argue that because credit unions don't pay taxes, political subdivisions in Nebraska should not be allowed to deposit public funds into credit unions. First, I believe this to be somewhat of a misleading statement. Credit unions do pay taxes including real estate and property taxes, personal property taxes, payroll taxes, and our state-chartered credit unions additionally pay the state's deposits tax as well as state sales tax. I think it's important to note as well that when you're looking at what local governments bring in, many of the receipts come from property taxes and taxes that are assessed on both banks and credit unions. To give you some brief background, in 1937, Congress provided credit unions with a federal tax exempt status because of their not-for-profit cooperative structure. This federal tax status was affirmed by Congress in 1951 and reaffirmed in 1998. Credit unions do not have profits, and therefore, have no profits to tax. Whatever earnings a credit union has go back to its membership in the form of dividends, lower loan rates, higher deposit rates, additional services, fewer and lower fees. The amount that is foregone each year by Nebraska credit unions due to their federal tax status is estimated to be \$2.6 million from the Credit Union National Association. We believe it's duplicitous to use the federal tax issue at the state level, especially when you consider that there are 86 Nebraska banks that have elected Subchapter S designation and therefore do not pay federal income tax to the tune of what's estimated to be somewhere around \$84 million a year. That is nearly 33 times the amount of the tax break that credit unions receive at the federal level, so that would beg the question, should Subchapter S banks be allowed to deposit public funds if there is certainly a litmus test on public funds and who pays taxes and who doesn't. Additionally, a top legislative priority for banks, according to the Independent Community Bankers Association website in 2012, is pushing legislation that would actually greatly expand the ability of Nebraska banks and other banks across the country to elect to be a Subchapter S bank and therefore avoid federal income tax. They want to raise it from a maximum of 50 shareholders to 100 shareholders to become a Subchapter S bank. Also, in 2008, the banks were the beneficiaries of billions of dollars in direct taxpayer bailout through the Troubled Assets Relief Program, or TARP, as you all know. In Nebraska, I believe there was nine banks that accepted TARP money. Credit unions were not part of TARP and received no taxpayer bailout in that regard. LB1004 is commonsense legislation that simply allows local governments in Nebraska to choose which financial institution would best serve their needs when it comes to public funds. Our local officials who are charged and trusted to oversee public funds should also be trusted to decide how best to invest those public dollars so as long as those

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investments are protected. As you consider the merits of LB1004, I would ask you to consider two questions: 1) Does the bill make good fiscal and business sense for local governments, local communities? 2) Are the public funds that are being considered federally insured? We urge this committee to advance LB1004 to General File so that the whole Legislature may consider this bill. Thank you for your consideration, and I would be happy to try to answer any questions you might have. [LB1004]

SENATOR PAHLS: Senator Christensen. [LB1004]

SENATOR CHRISTENSEN: Thank you, Chairman. Thank you, Brandon. On this sheet where you compare financial institution deposit taxes by credit...state credit unions, federal banks, Sub S, personal property, on down the line here. Then below that, you make a statement, state of Nebraska does not afford state-chartered credit unions any preferential tax treatment. The state does offer tax credit to Subchapter S shareholders. Explain that. [LB1004]

BRANDON LUETKENHAUS: Well, Nebraska credit unions pay the state's deposits tax, as do banks, and they also pay state sales tax as state-chartered credit unions do. And most recently, which I have a form from the Department of Revenue as a Statement of Nebraska Financial Institution Tax Credit, which I believe this was passed several years ago, that allows Subchapter S shareholders to have a tax credit at the end of the year for their portion of income from the Subchapter S bank. And so that's something that credit union members don't get. Certainly, when dividends are allocated to those credit union members, but Subchapter S shareholders do get a credit. So when you look at that chart, state-chartered credit unions pay really the same taxes that any Sub S bank in Nebraska pays, and there's 86 current banks that are Subchapter S. [LB1004]

SENATOR CHRISTENSEN: It's a...you mentioned that taxes are paid by shareholders on credit unions, but not as profit on the business like a bank. Did I understand that correctly? [LB1004]

BRANDON LUETKENHAUS: Yeah, at the federal level, credit unions are federally tax exempt, so they don't pay corporate income tax. Subchapter S banks, when they elect to be Subchapter S, they don't pay taxes on their federal income either. [LB1004]

SENATOR CHRISTENSEN: Since federal credit unions don't pay financial institution deposit tax, then how do they get theirs guaranteed, because isn't that make sure a depositor is in...his money's guaranteed to come back if the institution goes under? [LB1004]

BRANDON LUETKENHAUS: Well, Senator, the way that credit union members and bank customers...credit union members are insured through the National Credit Union Administration, through the Credit Union Share Insurance Fund, and that's very similar

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when you talk about FDIC. It's essentially the same insurance. It's two different federal government agencies, but they essentially do the same thing. They insure every member's account up to \$250,000 for those members, so if an institution went belly up and you had \$250,000 in a credit union, you'd be insured through the National Credit Union Share Insurance Fund, and it would be the same for banks through the FDIC. [LB1004]

SENATOR CHRISTENSEN: So they're really insured, it's just through a different agency. [LB1004]

BRANDON LUETKENHAUS: Exactly. [LB1004]

SENATOR CHRISTENSEN: Because your chart almost makes it look like they're uninsured, because it says federal institution deposit tax, no on federal credit unions, yes state banks and subassets. Why? [LB1004]

BRANDON LUETKENHAUS: Financial institutions deposit taxes, the tax that's levied on state-chartered credit unions and state-chartered banks, so that's who pays the financial institution's deposits taxes. [LB1004]

SENATOR CHRISTENSEN: Because I don't understand how the sales and use tax works. Like the feds don't pay, and everyone else does. Seems, where's the sales tax come in? [LB1004]

BRANDON LUETKENHAUS: Well, because credit unions are...if you're a federally chartered credit union, you're exempt from federal income tax and therefore exempt from state sales tax. That's not the case for state-chartered credit unions. State-chartered credit unions do have to pay state sales tax. [LB1004]

SENATOR CHRISTENSEN: Okay, and we've discussed in the past, and you hit on it a little bit that there would be no change to credit union's bylaws, whether they are the voting or nonvoting, if this passed. [LB1004]

BRANDON LUETKENHAUS: That's correct. Both the Federal Credit Union Act allows credit unions to accept public deposits and doesn't require...that's what they call in the Federal Credit Union Act as nonmember entities, which are political subdivisions and public units. And then in LB1004, it also makes note that credit unions are, would be considered mutual, mutual financial institutions. And therefore, they could have nonmember deposits, including political subdivision deposits. [LB1004]

SENATOR CHRISTENSEN: Okay, thank you. [LB1004]

SENATOR PAHLS: Senator Langemeier. [LB1004]

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SENATOR LANGEMEIER: Thank you, Chairman Pahls, and Brandon, thank you for your testimony. A bank can go borrow, if they don't have enough deposits on hand to make a loan, they can borrow from Federal Reserve. How does a credit union get their money if they don't have enough? [LB1004]

BRANDON LUETKENHAUS: Credit unions can go to the Federal Reserve as well to borrow money, but they can also go to the central liquidity fund at the national level and get liquidity that way. They can also go to Federal Home Loan Bank and get liquidity for say, mortgage loans, to make mortgage loans. So there's many avenues in which they can get money to help lend. [LB1004]

SENATOR LANGEMEIER: Thank you. [LB1004]

SENATOR PAHLS: Seeing no more questions, thank you for your testimony. [LB1004]

BRANDON LUETKENHAUS: Thank you. [LB1004]

SENATOR PAHLS: Proponents? [LB1004]

GINI GORACKE: (Exhibits 2 and 3) Good afternoon, Senators. My name is Gini Goracke. I'm from the village Meadow Grove. My first name is spelled G-i-n-i. My last name is G-o-r-a-c-k-e, and I also manage the Meadow Grove Federal Credit Union. The letter that you're getting, that was drawn up from our village clerk who dearly wanted to be here this afternoon, but she had to stay in Meadow Grove and conduct business, she could not get away. And in her letter were a lot of examples just like Brandon mentioned, so I won't repeat those, and the letter is on behalf of the Meadow Grove village board, who are very much in favor of this bill. And the picture that I gave you pretty much says it all. We are a town of 300 people. The door on the right is the city clerk, or village clerk's office. The door on the left is our credit union. You can see they are literally about 20 feet apart, and she has to drive to the next town to make her deposits every week. She has to take time off out of her business and go drive to the next town. And that's pretty much my testimony, is this picture. Like Brandon said, this bill is pretty much common sense to enable our village clerk to make her deposits right next door at the Meadow Grove Federal Credit Union. And I'd like to thank you, Senators, for your consideration in advancing this bill, LB1004. [LB1004]

SENATOR PAHLS: Senator Christensen. [LB1004]

SENATOR CHRISTENSEN: Thank you, Chairman. Thank you for coming today. I've got a community in my district, Palisade, I think is in the same situation you have been. I had a bill a few years ago similar that people in the town would like to deposit money locally, wouldn't they? [LB1004]

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GINI GORACKE: Very much so. [LB1004]

SENATOR CHRISTENSEN: And you know, they like to do business at home best they can, they have a lot of pride in their community. [LB1004]

GINI GORACKE: Very much so. [LB1004]

SENATOR CHRISTENSEN: And pretty much, equal to what I would be comparing Palisade to Meadow Grove here. [LB1004]

GINI GORACKE: Yes. [LB1004]

SENATOR CHRISTENSEN: Because they don't have a bank, and they just have a credit union. [LB1004]

GINI GORACKE: We don't either. (Laugh). [LB1004]

SENATOR CHRISTENSEN: Okay, thank you. [LB1004]

GINI GORACKE: You're welcome. [LB1004]

SENATOR PAHLS: Senator Pirsch. [LB1004]

SENATOR PIRSCH: What's...how far is the next town? [LB1004]

GINI GORACKE: About, it's nine miles to Battle Creek where she deposits her money right now. [LB1004]

SENATOR PIRSCH: Thank you. [LB1004]

SENATOR PAHLS: Seeing no more questions, thank you for your testimony. [LB1004]

GINI GORACKE: Thank you, Senator. [LB1004]

SENATOR PAHLS: Yeah. Any more proponents? Seeing none, opponents? [LB1004]

JERRY STILMOCK: Chairman Pahls, if I may have leave to submit a testifier sheet, another one. I only grabbed one when I came up. May I do that upon completion? [LB1004]

SENATOR PAHLS: Yes, yes. [LB1004]

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JERRY STILMOCK: (Exhibit 4) Thank you. Chairman Pahls, members of the Banking, Commerce and Insurance Committee, my name is Jerry Stilmock, J-e-r-r-y, Stilmock S-t-i-l-m-o-c-k, and I appear before you today as a registered lobbyist for the Nebraska Bankers Association in opposition to LB1004. LB1004 would authorize state and federally chartered credit unions to accept deposits of public funds by the state and local political subdivisions up to the amount of \$250,000 insured by the National Credit Union Administration. The credit union industry has attempted to piggyback onto existing law authorizing mutual savings and loans to accept the deposit of state and local political subdivisions. While credit unions may desire similar treatment accorded mutual savings and loans, when it comes to eligibility to accept public deposits, we believe similar treatment is not warranted. There is a significant distinction to be drawn between mutual savings and loans and credit unions. Savings and loans pay federal and state income taxes, and federally chartered credit unions do not. In addition, in order for a credit union to be eligible for the deposits of the state or local political subdivision, it's my understanding, I believe, that it must amend its charter and bylaws in order to restrict the rights of the state or political subdivision as an account holder. These restrictions provide that the state or political subdivision must waive its voting rights in the credit union, must waive its right to share in the profits of the credit union, and must waive its right to share in any distribution of the assets in the event of dissolution of the credit union as a condition to placing deposits with the credit union. The notions of membership governance and membership profit sharing are at the very heart of what credit unions claim of entitlement to the multibillion-dollar exemption from federal and state income taxes which federally chartered credit unions currently enjoy. Allowing credit unions to receive deposits from nonmembers moves them yet another step away from their roots. We would submit that if the credit union industry is not willing to contribute to the public taxation, public coffers by paying its full share of income taxes, they should not be allowed to feed from the public trough by being able to hold public deposits. In addition, it is widely recognized that banks serve their community, their entire community, and are subject to extensive Community Reinvestment Act laws and regulations. By contrast, credit unions are generally viewed as serving a defined membership and are not subject to the Community Reinvestment Act regulation. Public funds serve a very important function of providing additional liquidity required by community banks to fund the loan demand in their community, helping families achieve their desires of home ownership, and helping to finance agricultural operations and small businesses, which leads to additional investments and job creation for our state. Allowing tax exempt, advantaged credit unions to be eligible to compete for public funds will be detrimental to local communities, as credit unions would have an unfair competitive advantage in bidding for public funds and would continue to grow at the expense of the taxpayer. Some may view limiting credit union access to public funds to the amount insured by the NCUA as a compromise of sorts. However, it actually serves to exacerbate the competitive advantages granted to the tax-exempt credit unions. While the first \$250,000 of any public deposit would be protected by deposit insurance, any public funds in excess of \$250,00 have a significant carrying cost, as they must be

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protected through the pledging of securities or the purchase of a deposit guaranty bond, both of which add to the costs incurred by banks and savings and loans maintaining deposits...public deposits in excess of \$250,000. LB1004 would allow credit unions to only have to compete for the least costly portion of public funds. Supporters of similar legislation introduced in previous years have claimed that a bank's ability to claim Subchapter S status provides the same tax benefits as federal credit unions enjoy from their tax exempt status. A critical distinction, Senators, between Subchapter S banks and credit unions is that bank shareholders are required to pay taxes on Subchapter S earnings whether or not those earnings are distributed in the form of dividends or capital gains. By contrast, pursuant to the full tax exemption from federal and state income taxes, federal credit unions, by their retained earnings, rather than distributing them to their members can avoid taxation completely and use the retained earnings to grow their institutions or build new buildings. In closing, deposits represent the part of raw materials that fuel the banking industry in Nebraska. If those raw materials are siphoned off to other financial providers who do not pay federal or state income taxes, as the case of federal credit unions, or a reduced share of these taxes, as the case for state credit unions, these taxpaying banks and savings and loans will be left with a smaller base from which to generate income and pay taxes. For these reasons, we would respectfully request the committee to indefinitely postpone LB1004. Thank you, Senators. [LB1004]

SENATOR PAHLS: Senator Christensen. [LB1004]

SENATOR CHRISTENSEN: Thank you, Chairman. Thank you, Jerry. You mentioned credit unions don't pay state and federal taxes. According to the sheet I'm looking at, banks pay federal corporate tax, but Sub S don't. Is that an accurate statement? [LB1004]

JERRY STILMOCK: I believe that's correct. [LB1004]

SENATOR CHRISTENSEN: So we're really just comparing the banks that pay the federal, and that's why we see quite a few Sub S, and according to this sheet, nobody pays Nebraska corporate tax. Is that correct? [LB1004]

JERRY STILMOCK: It's my understanding the bank deposit tax touches upon and is...the corporate income tax is factored into the bank deposit tax for banks, Senator, is my understanding. [LB1004]

SENATOR CHRISTENSEN: So you're saying there's not a separate Nebraska corporate tax, but you think there's some additional developed into the institutional deposit tax? [LB1004]

JERRY STILMOCK: Into the deposit tax, yes, Sir. [LB1004]

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SENATOR CHRISTENSEN: Okay. I've never heard that one. Another thing you mentioned, so I grabbed the bill and looked at it again. You said that credit unions could only go up to the first \$250,000. It says not to exceed the insured amount of the National Credit Union Administration. Could the credit unions buy additional guaranty bond insurance like a bank does to go higher? [LB1004]

JERRY STILMOCK: My understanding, Senator, would be the bill would have to be amended in order to allow something like that to happen. [LB1004]

SENATOR CHRISTENSEN: So they could only go up to the first \$250,000. If a community had more than that, then it would have to go to a bank anyway. [LB1004]

JERRY STILMOCK: It would have to go elsewhere, Sir, yes. [LB1004]

SENATOR CHRISTENSEN: And that's, no matter how small the town, that's likely to occur. You take a lot of property tax and different things in if that's the county seat that doesn't have a bank in it, which happens in my district. So you're saying they could end up doing...probably bypassing the credit unions anyway because they couldn't handle their needs? [LB1004]

JERRY STILMOCK: Under existing law, yes. If I stayed with your question, Senator, or your statement. [LB1004]

SENATOR CHRISTENSEN: Yeah, I guess what I was saying, it's likely more than \$250,000 will come in at a time on property tax times, which is public funds. So if the county wanted to deposit, they could only go up to \$250,000 in the credit union, and they could take it all over to the banks, so they're probably not going to use the credit unions anyway. The only ones that might use this would be the villages like Meadow Grove and my district, Palisade, and things that direction then. [LB1004]

JERRY STILMOCK: I can't dispute your statement. The only thing I could do is remind the members of the committee or to those committee members that are new, is that I thought we, through some efforts in your office and the Nebraska Bankers Association, we were able to resolve the Palisade issue. [LB1004]

SENATOR CHRISTENSEN: Correct. [LB1004]

JERRY STILMOCK: And to Senator Schumacher joining us, you know, we would extend that same working relationship. I know that's...obviously, that's not the tenor of the bill, but we're prepared to do the same thing. [LB1004]

SENATOR CHRISTENSEN: I wondered if you'd offered the same there. I still got locals still like to support their local community, but the situation is definitely better than it was.

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[LB1004]

JERRY STILMOCK: Yes, Sir. [LB1004]

SENATOR CHRISTENSEN: Thank you. [LB1004]

JERRY STILMOCK: Thank you, Sir. [LB1004]

SENATOR PAHLS: Any more questions? Seeing none, thank you for your testimony. [LB1004]

JERRY STILMOCK: Thank you, Senators. [LB1004]

SENATOR PAHLS: Proponents? (sic: Opponents?) [LB1004]

KURT YOST: Chairman Pahls, members of the Banking, Commerce and Insurance Committee, my name is Kurt K-u-r-t, Yost Y-o-s-t. I am the registered lobbyist and president of the Nebraska Independent Community Bankers Association. We too appear today in opposition to LB1004, as we have for several years. The credit union industry has brought this discussion before this committee on numerous occasions, and we've had pretty much the same discussions with the same concern from the small village of Meadow Grove, and we've talked about the ability of mobile banking and other alternatives to assist communities such as that. Senator Christensen brings the question of monies in a Sub S situation. All be it, a Sub S corporation does not pay corporate income tax. I think it's widely known that those monies trickle down to the stockholders who pay them in form of individual income tax. And in the case of bankers and others in a business situation, those can be significant numbers, but they are not paid as a corporate tax. You're 100 percent correct, Senator Christensen. [LB1004]

SENATOR PAHLS: Senator Christensen. [LB1004]

SENATOR CHRISTENSEN: Thank you, Chairman. Thank you, Kurt. So is there really any difference between money funneling down to an individual and him paying income tax on this than the shareholders paying on it like in a credit union? [LB1004]

KURT YOST: Probably not. Probably not. I think my point was to...so that we aren't confused that Sub S corporations aren't paying any tax. (Laugh). [LB1004]

SENATOR CHRISTENSEN: I understood that they would pay as an individual. [LB1004]

KURT YOST: Okay, all right. Super. [LB1004]

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SENATOR CHRISTENSEN: I didn't state that, but I wanted to make sure there wasn't anything I was missing that is different for an individual to pay it than a shareholder to pay. [LB1004]

KURT YOST: No, no. Right. [LB1004]

SENATOR CHRISTENSEN: Okay, thank you. [LB1004]

SENATOR PAHLS: Senator Langemeier. [LB1004]

SENATOR LANGEMEIER: Chairman Pahls, thank you. Mr. Yost, if the bank would pay me a little more interest on my CDs, that follow-down tax wouldn't be such an issue (laughter), but let's talk about something else here that you said. You talked about mobile banking and other options that might be out there for Meadow Grove. You know, I've been on this banking committee eight years, and I think I've heard that eight years in a row. And then at the drop of the gavel of this hearing, nothing ever happens. At what point do the bankers wake up and go fix this problem in Meadow Grove? [LB1004]

KURT YOST: You know, I'm not sure, I'm not sure which way the lady from Meadow Grove is going to do her banking, but I would certainly think that an arrangement...an arrangement was made in Palisade, and you all have passed the legislation that created mobile banking. There could be something done there, Senator Langemeier. And I don't know the specifics, but, and the geography. And I'm not sure whether it's Tilden, or you know, which way Meadow Grove goes to do their banking business. But Tilden's in the neighborhood as is...I'm just not sure where she could go. I'm not sure what's east short of Norfolk. [LB1004]

SENATOR LANGEMEIER: Thank you. [LB1004]

SENATOR PAHLS: Any more questions? Seeing none, thank you. Proponents, or excuse me, opponents? To the neutral? [LB1004]

BETH BAZYN FERRELL: Chairman Pahls, members of the committee. For the record, my name is Beth B-e-t-h, Bazyn B-a-z-y-n, Ferrell F-e-r-r-e-l-l. I'm with the Nebraska Association of County Officials. We're appearing here neutral because when our board discussed this bill, we thought it would probably be something that would really be most beneficial to villages. But since then, I have spoken to a county treasurer who had an instance, I think something similar to what Senator Christensen was talking about. In this particular county, there is no...there is a credit union in the county, but there is no bank in the county, so they bank 36 miles away. This particular treasurer is the only one in her office, and so there's some logistics involved when she needs to go to the bank to make a deposit. She said that if...they looked at putting money in the credit union. The cash that comes to the county from their senior meals program. It's a small community,

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but they don't like to have that amount of cash on hand when people pay for their meals with cash. Their auditor told them that they couldn't use the credit union, so she said that they probably, if they had an opportunity to use a credit union that's there in the town, they would use it for those kinds of deposits, but they would probably still leave their main banking in the bank in the county that's adjacent. I'd be happy to try to answer questions. [LB1004]

SENATOR PAHLS: Senator Christensen. [LB1004]

SENATOR CHRISTENSEN: Thank you, Chairman. I guess Beth, you almost disappoint me a little bit. Anybody from the county ought to support their county, and it's disappointing to me to hear that you'd just as soon bank out of the county as in your own county. I guess I would love to have you respond to it. [LB1004]

BETH BAZYN FERRELL: Okay. The treasurer in this instance said that the credit union in their county was quite small, and they didn't want to get into a situation. She said, in fact, the credit union probably would prefer if they kept their larger deposits elsewhere so that they wouldn't have to deal with the pledged collateral situation, but that was the only reason that she gave. [LB1004]

SENATOR CHRISTENSEN: So you only represent one county, or do you? [LB1004]

BETH BAZYN FERRELL: We represent all of the counties. This was just the instance that we were provided with as an example. As I understand it, most counties, there is a bank within the county. Although, for example, in Blaine County, there is not a bank in the county seat. There's one in Purdum, which is a ways down the road. So in the more rural counties, there are a lot of different examples of different instances. [LB1004]

SENATOR CHRISTENSEN: Well, I understand there's...a lot of counties even have a bank in them, but they don't in their hometown. That's my example of Palisade, Meadow Grove here. But I'd like to see you be encouraging to your home counties, because if we don't take care of our own counties, who's going to? So thank you. [LB1004]

SENATOR PAHLS: (Exhibits 5 and 6) Any more questions? Thank you. Thank you. Any more in the neutral? Okay, I would like to read into the record the League of Nebraska Municipalities support LB1004. Also, trying to read here, the Southwest Public Power District and the Nebraska Rural Electric Association support LB1004. We are ready for closing. [LB1004]

SENATOR SCHUMACHER: Thank you, Senator Pahls, members of the committee. I apologize for not being here for opening. I was tied up in another hearing where we were trying to make some money for the state. Briefly, on a couple points, the issue of the insurance of deposits, whether or not safe deposits, looks like it's about six of one

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and half-a-dozen of the other. The idea that a bank, if it uses its retained earnings to build a building or a new facility of some kind, well, the bank, if it does that, it can deduct that, depreciate it, it doesn't pay income tax on that investment, and neither does the credit union. This seems to me not to be so much an issue of economics as an issue of some type of general principle. With interest rates at zero percent, banks can borrow money from the fed at near zero percent. They don't pay depositors any amount of interest either. The amount, the economic consequence of this, is near zero, as is the fact that probably the number of communities that it affects is near zero. There is some safety concerns in those smaller communities that don't have a bank depository. Not only for their water bills that they collect, and their various other assessments, and their keno money and things like that. It's nice to have a place where you can drop that off at night so your business or city hall isn't broken into. And a credit union, or any facility, if banks would do it, that's fine too, but that is nice to have. It puts our people at risk if there's a lot of money sitting there. It puts property at risk, probably a good reason, at least under some limited context, to use a facility in town if one is available to them. Subchapter S money does, in fact, trickle down to the shareholders. But interest payments, to the extent they're able to be made out of any excess revenues, trickle down to the members of a credit union. And in both cases, taxes are paid at the same rate. They aren't capital gains that are paid at the same ordinary income rate. So I'll take any questions with that. [LB1004]

SENATOR PAHLS: So you're telling me economically, either way we go, it's a wash. [LB1004]

SENATOR SCHUMACHER: For economics, yes, particularly with interest rates at zero. [LB1004]

SENATOR PAHLS: Seeing no questions, thank you. [LB1004]

SENATOR SCHUMACHER: Thank you. [LB1004]

SENATOR PAHLS: That will close the hearing on LB1004. Thank you. [LB1004]