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Banking, Commerce and Insurance Committee
January 21, 2014

[LB668 LB687 LB712 LB714 LB788]

The Committee on Banking, Commerce and Insurance met at 1:30 p.m. on Tuesday, January 21, 2014, in Room 1507 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on LB668, LB687, LB712, LB714, and LB788. Senators present: Mike Gloor, Chairperson; Mark Christensen, Vice Chairperson; Kathy Campbell; Tom Carlson; Tommy Garrett; Sara Howard; Pete Pirsch; and Paul Schumacher. Senators absent: None.

SENATOR GLOOR: Welcome to the Banking, Commerce and Insurance Committee. I'm Mike Gloor, I'm the senator from Grand Island, chairing the committee. We'll...there are agendas posted outside. We'll take up the bills as they are listed on that agenda. We've got a few rules of the road here. You'll see that they're posted up there, but I'll go ahead and run through them quickly just as a reminder. Please turn off your cell phones. Usually for this august a group, I don't have to remind that. But I heard one ring a little while ago, Mr. Yost, and so I know that occasionally people forget.

KURT YOST: Sorry about that, Mr. Chairman.

SENATOR GLOOR: So please check your cell phones and put them on the off or vibrating position. Move to the reserve chairs when you're ready to testify. The order of testimony will be introducer, proponents, opponents, and those in a neutral capacity. And then the senator who has introduced it will be allowed to close. We'd ask testifiers if you would sign in. You've got a sign-in sheet. If you haven't, you can pick them up on either side. Be sure and hand them to the clerk or to the pages when you come up here. Spell your name as you begin your testimony for the record before you testify. We probably know who you are, we really don't care about the spelling so much. But the poor transcriptionists who have to keep a record of it need some help. We don't use lights, or at least we haven't used lights in this committee very often, but we'd still ask that you try and keep your testimony to about five minutes. Oh, if you have written materials, we need ten copies. If you need ten copies, we'll have the pages run some copies for you. But grab the pages, get their attention so we can have those ready before you provide your testimony. If you have any problem with that, let us know. We can always get it out to the committee a little later. We'll start with introductions. To my right is committee counsel, Bill Marienau. Committee clerk is Jan Foster who is over there at the end of the table, chief cook and bottle washer keeping track of things. And I'll ask committee members to introduce themselves starting with Senator Garrett.

SENATOR GARRETT: I'm Tommy Garrett from District 3.

PAUL SCHUMACHER: Paul Schumacher, District 22.

SENATOR PIRSCH: Pete Pirsch, District 4.

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SENATOR CAMPBELL: Kathy Campbell, District 25.

SENATOR CHRISTENSEN: Senator Christensen, District 44, Imperial.

SENATOR CARLSON: Tom Carlson, District 38.

SENATOR HOWARD: Sara Howard, District 9.

SENATOR GLOOR: And our pages are Emily Schiltz from Sioux Falls and Steve Schubert who's from here in Lincoln. We're glad to have them for us. We'll take up the bills in order, as I said previously, and we always...it's a tradition in this committee that we start with a bill that's introduced by one of our more august members of the Legislature, and Senator Hadley was picked for that particular...by roll of the dice, I believe, or something along those lines. Senator Hadley, welcome to the Banking, Commerce and Insurance Committee. [LB668]

SENATOR HADLEY: Senator Gloor, members of the committee, my name is Galen Hadley. That's G-a-l-e-n H-a-d-l-e-y. And I'm privileged to represent the 37th District in the Legislature. I just happened to be looking at the name tags up here and I was just going to say, Mr. Marienau, you must have been around a long time because yours looks like it's beginning to fade a little bit there. So you might want to think about getting a new one. [LB668]

SENATOR GLOOR: Thirty-five years. [LB668]

SENATOR HADLEY: Thirty-five years? Well, it looks like it's about that. [LB668]

SENATOR GLOOR: And since we're talking automobiles, one retread I believe, during that period of time. [LB668]

SENATOR HADLEY: Thank you. I bring...I know it's a active phrase that we use a lot that this is a relatively simple bill, and I do believe it truly is. LB668 is the product of discussions among the Nebraska New Car Dealers Association, the Nebraska Department of Motor Vehicles, and the two bankers' associations. Current law provides for a method of dealing with personal property that has been left for repair at a business that fixes or enhances that personal property. In the event the owner of the property fails to come back and pick up the property, the law provides for a method of notifying the owner and any lienholder to either pick up the property or have it sold to satisfy the reasonable cost of repair. LB668 does not change anything about the current process. An issue has arisen regarding any such item of personal property which has a certificate of title and a lien on that title. The bill clarifies that any existing lien on that title is extinguished if the lender has received written notice of the sale and has failed to

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exercise the lender's right to redeem the property. The current practice under law is to cancel any such lien. The bill only confirms the current practice. The changes only impact the lender. Basically, the purpose of this bill is to allow the company that is doing the repairs the ability to sell the item that they've done the repairs on without having a lien on it. In essence, if the lien is not extinguished, it would be almost impossible to sell the item because of the lien. This has been the current practice, but there was a question that came up with one banker about extinguishing the lien. So we want to make it clear in the statute that, in essence, the sale of the property for the repair bill does extinguish the lien that the lienholder has on the item. With that, I'd be happy to answer any questions you might have. [LB668]

SENATOR GLOOR: Thank you, Senator Hadley. Are there questions for Senator Hadley? Seeing none, thank you, Senator Hadley. Will you stick around and close? [LB668]

SENATOR HADLEY: I will stick around. [LB668]

SENATOR GLOOR: Okay. We'll now move to proponents. Senator Schumacher, had you come in after we did our introductions or were you here to...okay. [LB668]

SENATOR SCHUMACHER: No, I was here for introductions. [LB668]

LOY TODD: Senator Gloor, members of the committee, my name is Loy Todd, that's L-o-y T-o-d-d. I'm the president and legal counsel for the Nebraska New Car and Truck Dealers Association. I can tell you that Senator Hadley did a terrific job of describing this legislation. It is...this is really just confirming the practice that's been there longer than I've been around. I certainly haven't been around as long as committee counsel, but I'm starting to scare that number. And what happened here is something that happens occasionally. We've all...all of us in the industry have known the law for, you know, 20, 30 years and practiced that way. And then somebody asked a question, which forced us to do something that attorneys generally don't like to do, and that's actually go back and read the law. And it wasn't just drafted as clearly as it should have been back then and it's because the question was, is the lien really extinguished? And the answer has been that it always has been, but we thought we ought to have the law say that. And because we do give a written notice, a registered letter to any lienholder, if we fail to do that, then the lien would not be extinguished. And when you...when one of my dealers takes a vehicle in and does repairs on it, they've enhanced the value and, thus, deserve to be paid. And if the lender is notified, they have a right under current statutes to come in and take the property themselves by paying the bill. So the lienholder has the opportunity to protect themselves, has elected not to do that, and instead stood on the original debt with the owner. And then any...once the vehicle or item of personal property has been sold, then any excess proceeds are turned over to the county treasurer, under current law, and available to the owner. So...and we're not changing

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any of that. The rights of every party stays exactly how it has been historically and how it's been treated historically. We just wanted to clarify that the lender had the same status as we've always had. I think...I know of no opposition to this. It truly is clarification. If there ever is a consent calendar, I would strongly urge you to promote this in that regard. So thank you. [LB668]

SENATOR GLOOR: Thank you, Mr. Todd. Any questions? Senator Carlson. [LB668]

SENATOR CARLSON: Thank you, Senator Gloor. Mr. Todd, this is a concern of mine, and it may concern several others on the committee as well. I noticed that you put your coat in a close position to where you're sitting. Are you worried about a quick getaway? [LB668]

LOY TODD: Exactly. [LB668]

SENATOR CARLSON: Okay. That eases my mind. [LB668]

SENATOR GLOOR: Senator Schumacher. [LB668]

SENATOR SCHUMACHER: Thank you, Mr. Todd. Thank you, Chairman Gloor. In the event that the person that did the work on the vehicle or whatever puts out an outrageous bill, something that's clearly unreasonable or in the process of this sale procedure, accepts a bid that is not reasonable. What's the remedy of the owner of the property or the creditor under those circumstances? Is...they just lump it or does he...can he complain about the bill? At what point does he complain? And at what point does the lienholder get a chance to say, wait a minute. You didn't sell that property for enough. [LB668]

LOY TODD: Sure. The current statute, which we're not changing, requires that to be a reasonable charge--and it's statutorily stated as a reasonable charge--and in the event there is a disagreement about it, we won't have this abandoned property situation. And either the repair...the artisan or the...and the owner of the property can either litigate those things through anything from replevin to simply breach of contract or the standard remedies in those kinds of cases. This bill does nothing to change those relationships or that practice. And as a further stopgap, the Department of Motor Vehicles in their practices, they won't allow the repair person to actually be a purchaser. It has to be a third party, and they're supposed to--under the code, the Uniform Commercial Code--they're supposed to make commercially reasonable attempts to sell the property. And that can be examined by any court at any time in that regard. There is a 90-day delay between the time that these rights can be exercised under the underlying artisan's lien statute. So what has to happen is the repairs be made, the abandonment begin, and 90 days have to go by without anybody coming to get the property. Under the process, then, the lienholders and the property owner are notified by registered mail. If

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that fails to happen, there can be no conveyance and there's no passage of the property. And this isn't just titled vehicles, this is anything from your watch to a piece of farm equipment or whatever. It's an item of personal property that has been repaired and enhanced. And so...I'm sorry, Senator. [LB668]

SENATOR SCHUMACHER: So to protect...I mean, for a lender to protect himself, he'd have to show up at the sale and if he thought it was selling too cheap, he'd bid it in? Is that his protection? [LB668]

LOY TODD: No. His first protection is that he can simply come in and buy it. He can pay the bill and take it. And under the statute, the person doing the repairs can give it to them, give them possession. And then they take it away and deal with their debtor however they might in that regard. So everyone involved in the process has the opportunity to protect themselves. And only in failing to do so or electing...and what normally would happen, if the lender decides that the property isn't worth it, they'll simply ignore it and not participate. Or they can come in and purchase it in any commercially reasonable manner. [LB668]

SENATOR SCHUMACHER: Thank you. [LB668]

SENATOR GLOOR: Other questions? [LB668]

SENATOR GARRETT: How is the property normally sold? [LB668]

LOY TODD: There's a variety...I can only really speak to my car dealers. Normally, they try to sell it on the lot just like they would sell anything else. They...and what I advise them--because once in a while they'll ask--when this...it's fairly rare, but when it happens, I always tell them, sell it like you'd sell your own inventory. And then if there are excess proceeds...but you have to understand that in 99 percent of these cases, it's marginal. It's...there just isn't that kind of value in there. If something's worth--and I'm going to make up some numbers--but let's say it's a \$3,000 repair bill on a \$10,000 vehicle, somebody's going to show up or the lienholder is going to be there or, you know, there is value. That's pretty rare. When people elect not to come back, it's one where it's a close call or they've lost interest in it or...this is--I don't want to use the term abandoned because that's a whole different set of laws, and so I want to be cautious about that, but it truly is a property owner and a lienholder when that happens who just don't see the value. There aren't many circumstances where money is turned into the treasurer and they go to chase somebody down. [LB668]

SENATOR GLOOR: Any other questions? Thank you, Mr. Todd. [LB668]

LOY TODD: Thank you. [LB668]

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SENATOR GLOOR: Other proponents? [LB668]

ROBERT HALLSTROM: Chairman Gloor and members of the committee, my name is Robert J. Hallstrom. I appear before you today as registered lobbyist for the Nebraska Bankers Association in support of LB668. The spelling on my last name is H-a-l-l-s-t-r-o-m. Mr. Todd had approached the Nebraska Bankers Association earlier last year with this perspective in terms of the sale of these automobiles that had been repaired and had indicated that there were...there was at least one situation where the lienholder, for whatever reason, did not release their lien which, as Senator Hadley suggested, makes it quite hard to sell the vehicle if you're not going to have clear title. The treatment that is provided under the amendments to (section) 52-603 are much like any other foreclosure proceeding. If you've had notice and an opportunity to participate in the proceeding and to protect your interest by bidding at the ultimate sale, then your liens are extinguished and released. We have no objections to those. We did make one request, which is a change in section 2 of the bill. Mr. Todd testified that the proceeds ultimately go to the county treasurer. We simply inserted that when the automobile or the personal property is sold, if there is more after the repairs are paid for that would otherwise go to the lienholder, to pay the lienholder directly up front rather than making us chase our tail to go to the county treasurer to find the proceeds. And with that, we would support the bill and be happy to answer any questions that the committee might have. [LB668]

SENATOR GLOOR: Thank you. Any questions for Mr. Hallstrom? Senator Pirsch. [LB668]

SENATOR PIRSCH: Just to clarify, so the proceeds would go to the lienholder to the extent that it is an amount up to the lien, correct? [LB668]

ROBERT HALLSTROM: Yes, and any balance goes to the county treasurer as it always has. [LB668]

SENATOR PIRSCH: Yep. Thank you. [LB668]

SENATOR GLOOR: Seeing none, thank you. [LB668]

ROBERT HALLSTROM: Thank you. [LB668]

SENATOR GLOOR: Other proponents? Seeing none, we'll move to those in opposition to the bill. Anyone in a neutral capacity? Senator Hadley, you're recognized to close. [LB668]

SENATOR HADLEY: I will just take a minute. I do believe it is a simple bill. I would appreciate moving it out and if we do have a consent agenda this year, I will certainly

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make sure that is on there. Or if you have any type of committee bills that it could be tacked onto, I think it is worthwhile. Thank you. [LB668]

SENATOR GLOOR: Okay. Any final questions for Senator Hadley? Thank you, Senator Hadley. [LB668]

SENATOR HADLEY: Thank you. It's always a pleasure to be in front of this august committee. [LB668]

SENATOR GLOOR: And with that, we'll close the hearing on LB668 and move to LB687. Senator Christensen. [LB687]

SENATOR CHRISTENSEN: Thank you, Chairman Gloor and members of the Banking, Commerce and Insurance Committee. I'm Senator Mark Christensen, C-h-r-i-s-t-e-n-s-e-n, I represent the 44th Legislative District. I'm here to introduce LB687. LB687 was brought to me by the Real Estate Commission. LB687 would primarily change the sequence of steps required to obtain a real estate salesperson or broker license. The bill would require the submission of an application for a licensee to precede the fingerprint-based criminal background check. This step was necessitated by the FBI's new emphasis that applicants receive a written notice of rights pertaining to background checks and the State Patrol's changed process with regard to the custody of cards and the collection of their fee. With that, I'd be glad to answer any questions, but also following me will be Teresa Hoffman, Deputy Director of the Real Estate Commission, can also answer them questions. [LB687]

SENATOR GLOOR: Thank you, Senator Christensen. Any questions for Senator Christensen? Senator Campbell. [LB687]

SENATOR CAMPBELL: Thank you, Senator Gloor. Senator Christensen, they're changing their procedures for everybody, aren't they? [LB687]

SENATOR CHRISTENSEN: Yes. [LB687]

SENATOR CAMPBELL: Okay. And when...did it go into effect already, do you know? [LB687]

SENATOR CHRISTENSEN: No. It's just they want to rearrange this... [LB687]

SENATOR CAMPBELL: Okay. [LB687]

SENATOR CHRISTENSEN: ...for...because the FBI doesn't want them fingerprint cards hanging out there before they've had an application and notification of the background check. [LB687]

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SENATOR CAMPBELL: Thanks a lot. Thank you. [LB687]

SENATOR GLOOR: Other questions? Thank you, Senator Christensen. Proponents to the bill? [LB687]

TERESA HOFFMAN: Good afternoon. [LB687]

SENATOR GLOOR: Good afternoon. [LB687]

TERESA HOFFMAN: (Exhibit 1) Mr. Chairman, members of the committee, my name is Teresa Hoffman, that's T-e-r-e-s-a H-o-f-f-m-a-n. And I am the deputy director for education and licensing with the Real Estate Commission. I am here to represent the commission in speaking in favor of this bill, which was introduced by Senator Christensen at the request of the commission and has its full support. LB687 is primarily about timing. As Senator Christensen said, the fingerprint-based criminal background reports that are mandatory for all applicants seeking a real estate salesperson or broker's license. Those reports must be completed prior to the application for licensing at the current time. However, the recent audits by the FBI and the State Patrol of our procedures in this regard have revealed that these entities have changed their emphasis and requirements so that our procedures for both resident and nonresident must change. LB687 would allow us to take that application for license prior to the applicant pursuing that criminal background report process. And this, in turn, would allow us to incorporate the applicant's notice of rights with regard to the criminal background report right into the application procedure, thereby making certain that every applicant had received that notice and satisfying the FBI's concern. Additionally, we could collect the fee the State Patrol charges for the background reports as a part of the application process, remitting it on to the State Patrol as an interagency transfer of funds with proper billing documentation from the Patrol; that is a pass-through of funds. The remaining two changes in the bill simply codify some of the timing aspects of the licensing process. It doesn't change what's been in practice for 20 to 25 years, but it does put them into statute. The bill has been reviewed in open public meetings of the commission, has been reviewed by the Nebraska Realtors Association. We are unaware of any and do not expect any opposition to the bill. And I would like to thank Senator Christensen for introducing this legislation on the commission's behalf and would be glad to answer any questions that any of you may have. [LB687]

SENATOR GLOOR: Thank you, Ms. Hoffman. Just curious, I guess. Did the State Patrol change their procedures because of the FBI? I mean, this is really driven by the FBI, is it not? [LB687]

TERESA HOFFMAN: It is my understanding that that is true. The FBI does an audit of agencies so they came to see us for the second time since we've been doing this

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procedure. And they also sat down with the State Patrol. So it is my understanding that that is what precipitated it. [LB687]

SENATOR GLOOR: Okay. Thank you. Other questions? Seeing none, thank you for your testimony. [LB687]

TERESA HOFFMAN: Well, I was ready for you. Thank you. [LB687]

SENATOR GLOOR: Be careful. You might get what you ask for in this committee sometimes. Other proponents? [LB687]

KORBY GILBERTSON: Good afternoon, Chairman Gloor, members of the committee. For the record, my name is Korby Gilbertson, it's spelled K-o-r-b-y G-i-l-b-e-r-t-s-o-n. I'm appearing today as a registered lobbyist on behalf of the Nebraska Realtors Association, and we do support the bill. The Realtors Association reviewed it and think that it makes common sense to have an application on file, so. I'd be happy to try to answer any questions. [LB687]

SENATOR GLOOR: Thank you. Any questions for Ms. Gilbertson? Seeing none, thank you. [LB687]

KORBY GILBERTSON: Great. Thank you. [LB687]

SENATOR GLOOR: Other proponents? Any opponents to the bill? Anyone who wishes to speak in a neutral capacity? Senator Christensen waives closing, and we will close the hearing on LB687. And I will now turn the gavel over to Senator Christensen as Vice Chair. [LB687]

SENATOR CHRISTENSEN: Go ahead. [LB712]

SENATOR GLOOR: Thank you, Senator Christensen. Good afternoon, committee members. I'm Senator Mike Gloor, M-i-k-e G-l-o-o-r. I'm presenting to you LB712. LB712 is a repeat of a similar bill called wild-card bill that we present every year. It's been brought to us by the Director of Banking and Finance. The Department of Banking is the chartering authority for our state-chartered financial institutions. When it comes to our most commonly recognized depository financial institutions we have what is called the dual chartering system. That means having both state and federal banks, savings and loan associations, as well as credit unions. The Legislature along with the Department of Banking and Finance have long done what they can to preserve the strong and vibrant legal and regulatory environment for our state-chartered financial institutions. Our public policy has included the principle that our state-chartered financial institutions should not find themselves in a disadvantageous position in relation to their federal counterparts. Accordingly, the Legislature annually passes the so-called

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wild-card bills at the urging of the department. These bills, by explanation, provide state-chartered institutions shall have all the rights, powers, privileges, benefits, and immunities, which may be exercised by their federal counterparts doing business in Nebraska as of January 1 of the current year. Why do we do this every year? That's necessitated by our state constitution. The separation of powers clause of our constitution provides that the powers of our government be divided into three branches, legislative, executive, and judicial. The courts say that the clause prohibits one branch from encroaching on the duties and prerogatives of the other branches or from improperly delegating away its own duties and prerogatives. The courts further say that the power of the Legislature to make laws requires judgment and discretion which cannot be delegated to the executive branch or to outside authorities such as the United States Congress. The Nebraska Legislature may lawfully adopt a reference or, excuse me, may adopt by reference an existing law or regulation of another jurisdiction, including the United States. But the adoption by reference can only be of an existing federal law or regulation, not a federal law or regulation now existing or to be adopted in the future. That's why the date is put on in the wild-card laws and why that date is changed every year. It is as if the Legislature takes a snapshot of relevant federal financial institution laws as of the most recent January 1, then incorporates that federal law by reference within state law for purposes of the regulation of our state-chartered financial institutions. The bill has three sections, one for banks, savings and loan associations, and credit unions. The savings and loan association wild-card has been around since 1971, the credit union wild-card has been around since 1977, and the bank wild-card since 1999. The passage of LB712 will help keep our state-chartered financial institutions competitive with their federal counterparts. And with that, I would ask for you to move along LB712. Thank you. [LB712]

SENATOR CHRISTENSEN: Thank you, Senator Gloor. Is there any questions for Senator Gloor? Senator Carlson. [LB712]

SENATOR CARLSON: Thank you, Senator Christensen. Senator Gloor, this is almost like an annual sunset date, isn't it? It kind of functions that way. We have to renew it every year. [LB712]

SENATOR GLOOR: Well, we wouldn't have to. I would say, from what I understand and Mr. Munn is from the Department of Banking is here, but if there were no federal changes, we wouldn't be required to have a wild-card, but that seems highly unlikely. So I'd also say the difference is were we not to adopt this, it would only be those small portions of the federal regulations that we wouldn't be updating. It isn't as if we'd be throwing out all of our statutes as relates to our financial institutions. [LB712]

SENATOR CARLSON: So this really addresses any federal changes that were made in 2013? [LB712]

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SENATOR GLOOR: Yes. [LB712]

SENATOR CARLSON: Okay. [LB712]

SENATOR GLOOR: That's how I would characterize it. If that's incorrect, I'm sure someone will correct us. [LB712]

SENATOR CARLSON: Okay, thank you. [LB712]

SENATOR CHRISTENSEN: Are there any other questions? Seeing none, thank you. [LB712]

SENATOR GLOOR: Thank you. [LB712]

SENATOR CHRISTENSEN: And we'll take the first proponent. Go ahead. [LB712]

JOHN MUNN: (Exhibit 1) Vice Chairman Christensen, 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 LB712, which was introduced at the request of the department. LB712 contains the annual equal rights updates for Nebraska's state-chartered depository financial institutions, all of which are under the jurisdiction of the department. Traditionally known as the wild-card laws, this legislation essentially provides the same rights, powers, and privileges to state-chartered financial institutions as those enjoyed by like federally chartered financial institutions doing business in Nebraska. Due to state constitutional restrictions on delegation of legislative authority, the statutes need to be amended annually to provide a current reference date. The reference date provided in LB712 is January 1, 2014. Within the bill, section 1 provides equal rights between our 175 state-chartered banks and the national banks chartered by the Office of the Comptroller of the Currency. Section 2 provides for equality between the one state-chartered savings and loan association and those chartered by the Office of the Comptroller of the Currency and formerly by the Office of Thrift Supervision. And section 3 provides the same rights for Nebraska's 17 state-chartered credit unions as those held by federal credit unions chartered by the National Credit Union Administration. LB712 carries the emergency clause. As I and previous department directors have testified through the years, wild-card legislation is sensible legislation in that it provides parity for our state-chartered financial institutions with their federal counterparts without the need to enact state legislation for each specific power or privilege. The savings and loan wild-card has been in effect since 1971, while the credit union statute was first enacted in 1977. The bank wild-card was adopted in 1999. The annual enactment forestalls any constitutional challenges. Under each of these sections, there is no exemption from the payment of any taxes imposed by the state. I want to thank Senator Gloor for introducing this legislation. I'll be happy to answer any

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questions. [LB712]

SENATOR CHRISTENSEN: Thank you, Director Munn. Is there any questions? I have one. So what changes have occurred that...what are we, in this blanket approval, allowed to change from last year? [LB712]

JOHN MUNN: I'm personally aware of none since January 1, 2013. But anything within the realm of how a bank, a state-chartered bank figures its lending limit, what investments are permissible for depository financial institutions, our purview over economic development pursuits that a state-chartered bank would undertake that may be to its advantage to do something in a manner a federally chartered institution would do. Those are the types of things that may be buried deep in federal legislation, but this pulls them into our statute. [LB712]

SENATOR CHRISTENSEN: So you're not aware of any changes, we're just updating this according to statute. [LB712]

JOHN MUNN: Right. Right. [LB712]

SENATOR CHRISTENSEN: Okay. Yes, Senator Schumacher. [LB712]

SENATOR SCHUMACHER: Thank you, Senator Christensen. Can it work the other way, too, that if the feds have withdrawn some authority, that by doing this we're restricting our banks in some way to be consistent with the feds? Or is this... [LB712]

JOHN MUNN: Yes. Yes. If...for instance, on the lending limit statute. The federal approach is preferable if the bank tends to have a sizeable amount of undivided profits, where our lending limit statute in Nebraska focuses on capital and surplus. If the federal government changed that at all to make it less permissive, then we might turn around and introduce that kind of legislation in this body. [LB712]

SENATOR SCHUMACHER: And is that...would that kind of thing be included in the type of updating we're doing here? [LB712]

JOHN MUNN: Yes. Yes, you couldn't wild-card to a federal statute that was no longer in effect. [LB712]

SENATOR SCHUMACHER: Thank you. [LB712]

JOHN MUNN: Uh-huh. [LB712]

SENATOR CHRISTENSEN: Are there any other questions? Thank you, Director. [LB712]

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JOHN MUNN: May I respond to Senator Carlson? I think this is more of a sunrise rather than a sunset statute. [LB712]

SENATOR CARLSON: Okay, during January. [LB712]

ROBERT HALLSTROM: Vice Chairman Christensen, members of the committee, my name is Robert J. Hallstrom, H-a-l-l-s-t-r-o-m. I appear before you, again, as registered lobbyist for the Nebraska Bankers Association in support of LB712. The NBA traditionally comes in and supports the annual wild-card update bill, and we do so again this year. Senator Carlson, I would suggest with the gridlock that Congress is facing currently, it very well could be that there will be years on end when no changes are made that need to be substantively updated through the wild card. But we appreciate the fact that state-chartered banks can automatically bootstrap onto the benefits and privileges that national banks are granted by Congress. I'd be happy to address any questions. [LB712]

SENATOR CHRISTENSEN: Thank you, Mr. Hallstrom. Is there any questions? I have one. [LB712]

ROBERT HALLSTROM: Yes. [LB712]

SENATOR CHRISTENSEN: How do you know what changes have occurred so that you don't want to make sure that we don't adopt something we shouldn't? So when changes occur federally, how do you find out about them if they're buried deep in other legislation so we don't approve something here we don't want to? [LB712]

ROBERT HALLSTROM: Well, we track federal legislation just as we do state legislation and, hopefully, are on top of any changes that may be made by Congress that affect national banks that would benefit state-chartered banks. We have, from time to time, gone in--and I think Director Munn referenced the alternative lending limit issue that we have--we came in and changed the state law specifically to allow state-chartered banks to take advantage of which either one benefited them the most in terms of their lending limit capacity. So we have done some things to tweak or make nuances in the bill when that was in the best interest of state-chartered banks and other banks operating in the state of Nebraska. But we, hopefully, are aware of those changes that are made. And I think in response to Senator Schumacher's question, if there was something that was adverse that we felt state-chartered banks ought to have some different rule of law apply than what Congress has provided to national banks, that we may come in and have state law perhaps approach that in a different manner unless federal law preempts state law action in that particular area. [LB712]

SENATOR CHRISTENSEN: Okay, thank you. Are there any other questions? Thank

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you, Mr. Hallstrom. [LB712]

ROBERT HALLSTROM: Thank you. [LB712]

BRANDON LUETKENHAUS: Mr. Chairman, members of the Banking, Commerce and Insurance Committee, my name is Brandon Luetkenhaus, L-u-e-t-k-e-n-h-a-u-s. I'm here on behalf of the Nebraska Credit Union League. Our trade association represents Nebraska's 69 credit unions statewide and their 440,000 members. We are in support of LB712. We want to thank Director Munn as well as Senator Gloor for the introduction of this bill. We, too, are in support of our state-chartered credit unions having parity with the federally chartered institutions. So with that, we are in support of LB712, and I would answer any questions you might have. [LB712]

SENATOR CHRISTENSEN: Thank you, Brandon. Is there any questions? Seeing none, thank you. [LB712]

BRANDON LUETKENHAUS: Thank you. [LB712]

SENATOR CHRISTENSEN: Are there any other proponents? Any opponents? Anybody like to speak in the neutral? And Senator Gloor waives, so that will end the hearing on LB712. And we'll open the hearing on LB714. Senator Gloor. [LB712]

SENATOR GLOOR: Thank you, Senator Christensen. Committee members, I'm Mike Gloor, G-l-o-o-r. LB714 would provide for outright repeal of Nebraska Revenue statutes, sections 8-155 and 8-156. These sections of law establish a statute of limitations and notice requirements relating to forged, altered, or raised checks. However, similar provisions relating to the statute of limitations for forged and altered checks exists within the Uniform Commercial Code. The statutes being repealed under LB714 predate adoption of the Uniform Commercial Code in Nebraska. Section 8-155 establishes a statute of limitations. Section 8-156 contains notice requirements relating to forged, altered, or raised checks that a bank has paid and charged to the account it's deposited. Section 8-155 requires the depositor to notify the bank of any forged, altered, or raised check that the bank has paid within one year after notice to the depositor that the "vouchers representing payments charged to the account of depositor" are ready for delivery or if no such notice has been given by the bank within one year after the return to the depositor of the said voucher representing such payments. The phrase "vouchers representing payments charged to the account" is not a term of art currently used in the banking industry and raises uncertainty regarding its meaning under the statute. On the other hand, under the Uniform Commercial Code, without regard to care or lack of care of either the customer or the bank, a customer who does not within one year after the statement or checks are made available to the customer discover and report the customer's unauthorized signature on or any alteration of the check is precluded from asserting against the bank an unauthorized signature or alteration. This one-year

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statute of limitation under the Uniform Commercial Code is identical to that provided under section 8-155. The Uniform Commercial Code has been adopted in all 50 states. The statute of limitations provided under the Uniform Commercial Code are widely recognized as the prevailing rule of law. The Uniform Commercial Code provides balanced protections to banks and their customers with respect to each party's responsibility and liabilities when a forged or altered check is involved and the provisions of sections 8-155 and 8-156 may be repealed without causing harm to either banks or, more importantly, to their customers. And with that, I would ask for the approval and option of LB714. Thank you. [LB714]

SENATOR CHRISTENSEN: Thank you, Senator Gloor. Are there any questions for the senator? Seeing none, thank you. [LB714]

SENATOR GLOOR: Thank you. [LB714]

SENATOR CHRISTENSEN: Are there any proponents? [LB714]

ROBERT HALLSTROM: (Exhibit 1) Vice Chairman Christensen, members of the committee, my name is Robert J. Hallstrom, H-a-l-l-s-t-r-o-m. I appear before you today as registered lobbyist for the Nebraska Bankers Association in support of LB714. There's only one way to tell this story, and Senator Gloor has pretty much covered the field. So I don't have too much more to add with regard to the substance. I will note that this came to our attention by a practicing attorney who had contacted the NBA and brought the statute to our attention. It's much like the issues buried deep in federal law. This is one that's buried deep in state law, nobody has paid much attention to it. It has language, as Senator Gloor alluded to, and I've got the statute 8-155 attached to my testimony making reference to the term "vouchers representing payments charged to the account of a depositor." We rather imagine in today's parlance, that's the account statement or the information regarding checks that are written on an account. But it doesn't necessarily mean that, and it comes from a day long since past when this statute was adopted, I think initially, in 1919. My hunch is that when the UCC was adopted in Nebraska and subsequently amended, nobody gave a second thought to repealing these statutes which have virtually identical statute of limitations provisions as those contained under Uniform Commercial Code 4-406(f), which is also attached to my testimony. I would note that the Uniform Commercial Code, in addition to the absolute one-year statute of limitations, does have provisions that allocate rights and responsibilities between the bank and its customer in terms of the banks being responsible for checks, for example, that are unauthorized, not properly payable, a forgery has occurred. The customer's countervailing obligation to look at their account statement or the truncated information that they get within 30 days and timely report that there has been a forgery or some type of alteration. And there can be a statute of limitations that may run in less time than one year under those provisions of the Uniform Commercial Code. But, again, the one year statute of limitations clearly is addressed in

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the Uniform Commercial Code. All 50 states have adopted the Uniform Commercial Code, and presumably these statute of limitations provisions. And with that, we would believe that 8-155 and 8-156 no longer serve a purpose and can be safely and comfortably outright repealed as proposed under the bill. [LB714]

SENATOR CHRISTENSEN: Thank you, Mr. Hallstrom? Are there any questions for Mr. Hallstrom? Mr. Hallstrom, I'll ask one. Did I hear you right, where we used to have one year to find fraudulent spending out of our account, it's now 30 days? [LB714]

ROBERT HALLSTROM: The Uniform Commercial Code since its adoption of those provisions under article 3 and 4 do have a provision that basically states that the bank has an obligation to provide its account statements or truncated information therefrom to the bank customer. And the customer under the code has 30 days to report information in order to avoid responsibility for subsequent forgeries. The initial forgery absent, negligence on behalf of the bank or the customer may be the bank's responsibility. But for subsequent forgeries, if the customer--the way the UCC handles that in all 50 states--is if the customer has the account information and the ability to be able to recognize I've had forged checks and timely, within that 30-day period after receipt, notifies the bank, then the customer can avoid responsibility for those subsequent forgeries as well. [LB714]

SENATOR CHRISTENSEN: Okay. Thank you, that helped me understand it better. Are there any other questions? Senator Schumacher. [LB714]

SENATOR SCHUMACHER: Thank you, Senator Christensen. Mr. Hallstrom, we're dealing in a changed world. And now when you get your canceled checks back, you don't get the--in most cases--the original canceled check where you can take a good look at it. You get something that's been reduced to the size of a postage stamp and you might need a magnifying glass to notice whether it's your signature or even your check blank for that matter. As a practical matter, is the time limit under the UCC enough for an ordinary customer to catch that there's a problem? [LB714]

ROBERT HALLSTROM: I certainly believe so, Senator. At 30 days from the time, if there is a question of someone with my eyesight requiring something more, they can certainly get that quickly from the bank to check and verify other information and get the actual account statement, perhaps, if necessary. But the UCC tells the basic information that needs to be on there, plus a copy of the check also needs to be provided. [LB714]

SENATOR SCHUMACHER: And do the bankers, if you would make a request would you get a visible-size copy of the check in order to examine it? [LB714]

ROBERT HALLSTROM: I would certainly hope so. [LB714]

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SENATOR SCHUMACHER: Thank you, Mr. Hallstrom. [LB714]

SENATOR CHRISTENSEN: Thank you, Senator Schumacher. Are there any other questions? Senator Carlson. [LB714]

SENATOR CARLSON: Thank you, Senator Christensen. Senator Schumacher's question brings that up to me because I recall when we would get the actual canceled checks back. Then it went to pictures of the checks and, at least in my experience, they're big enough that I can read them. But then I've got one that I get nothing other than the amount of the check. So did we change that law in Nebraska? [LB714]

ROBERT HALLSTROM: Not that I'm aware of, Senator. The Uniform Commercial Code says that you have to have certain basic information, and I think it's the number of the check, the designated payee, and the amount of the check, and the date of the check is the... [LB714]

SENATOR CARLSON: But not necessarily a copy of the check? [LB714]

ROBERT HALLSTROM: I don't recall that the...whether the Uniform Commercial Code requires that. As far as I know, most banks' practice is...all of my bank account statements I get copies of the actual items. [LB714]

SENATOR CARLSON: Okay. Thank you. [LB714]

SENATOR CHRISTENSEN: Thank you, Senator Carlson. Are there any other questions? Thank you, Mr. Hallstrom. [LB714]

ROBERT HALLSTROM: Thank you. [LB714]

SENATOR CHRISTENSEN: Are there any other proponents? Are there any opponents? Anybody wish to speak in the neutral? Would Senator Gloor like to close? He waives. Thank you, that will close the hearing on LB714, and I'll turn it back over to the Chairman. [LB714]

SENATOR GLOOR: Thank you, Senator Christensen. We'll now move to LB788. Senator Schumacher. [LB788]

SENATOR SCHUMACHER: Thank you, Senator Gloor. Members of the committee, I am Paul Schumacher, S-c-h-u-m-a-c-h-e-r, representing District 22 in the Legislature. And I am here today to present LB788 to the committee. LB788 started out what we thought was going to be a fairly uncontroversial, straightforward proposition. And that was that bondholders of our political subdivisions get priority when it comes to paying them. Our political subdivisions are allowed, unlike the state, to run up debt in the form

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of bonds. And they use those bonds for all kinds of things, basically public improvements, to use a financing vehicle for construction projects, and all kinds of good things. It's to their benefit to have a low rate of interest on those bonds. Generally, the financial markets award low rates of interest to bonds that are really, really secure, and are going to be paid and punish uncertainty with a higher rate of interest. In our system, normally operating, the bondholders get paid. The bondholders are not necessarily banks. They are private pension funds, private investors, IRAs, 401(k)s, all kinds of things end up holding those bonds. And the people purchase those bonds with an expectation that they are first in line, they're going to get paid. That expectation may not, however, be the case in the event the subdivision declares bankruptcy. And what began to raise this issue was the recent events in such cities as Detroit. And questions come up, are the rules the same once you jump into bankruptcy court? Are the priorities of payment the same? Are bondholders still number one? Well, one says, why even worry about this? And here in Nebraska, we know, certainly, that Omaha and Lincoln would never be concerned about defaulting on their bonds because they're 100 percent certain they're not going to declare bankruptcy. And the only people that would terribly concerned about that would be folks who thought in the back of their mind, it might be a possibility someday. So this appeared to be a fairly easy proposition of the probability of any Nebraska municipality or subdivision declaring bankruptcy is, hopefully, next to impossible. And there would be no controversy with regard to this measure. That does not appear to be the case. And I think further our first negative testimony will be in regard to this bill for this year before this committee. What happens now, if the law is not crystal clear, and the subdivision runs into the bankruptcy court, and all the hands come out saying pay me, pay me, pay me, and there isn't enough money, is the bankruptcy judge says, well, what's the state law on this? Right now it is kind of believed--but certainly far less than a certainty because we have an argument today. If we were changing nothing, there would be no argument today--that the bondholders will get paid and get preference from their streams of revenue, whether it's revenue from a sewer project or a water project or from the full faith and credit of the municipality that they will be paid first. But it's no longer a certainty because we do not have a clear law making it a certainty and telling that bankruptcy judge, listen, you pay these bondholders the priority they would have had were there no bankruptcy. In that case, if there is no law, the bankruptcy judge says, well, what would the court say? What's kind of the existing mood in the state in the law? And there have been a few cases, one named Hollstein, in which suggested that the bondholders probably would win in that catfight, but certainly not certain. This piece of legislation calls upon the Legislature to deal with the problem of being honest with our bondholders, the people who have given their savings, their sweat and blood to finance the operations of our subdivisions. And it says, declare as a clear matter of law that the bondholders come first. And when you do that, you resolve the issue as the bondholders have always expected and, quite frankly, as I think we all expect. If we do not choose to resolve the issue clearly by making a clear statement that the bondholders come first, then I believe under our securities law, we have an obligation to the purchaser of the bonds to make it very clear and to disclose, so that

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there's no questions and no omissions, that in the event of a bankruptcy, they may not come first. That's only what honest people would do rather than lead them to believe that somehow they're going to have a preference when, in fact, they do not. However, if we take that route of honesty with the bondholders and make that declaration be part of the bond prospectus to also protect the officers and directors and councilmen of the issuing institutions, then we can expect to pay a higher rate of interest because we are pointing out to people, what in fact is the case, that maybe they're going to come in number two. Maybe they will share in a pot rather than getting preference on the pot. So the decision that this puts squarely before is, do we want the bondholders to have priority in the payment in the remote, remote, remote situation of one of our municipalities going under? And if we don't want them to have priority, are we prepared to pay in the financial markets the little increase in interest rates that bondholders will require in order to compensate them for their increased risk? And that's our decision and that's what this bill brings to a head. We can clarify it, we can give that bankruptcy judge instructions as to how we want it handled, and he will honor...he or she will honor it. Or we can say to the bondholders, you know, it's anybody's guess. But in that event, we should require that the bondholders be made aware that we are not willing to guarantee their position. I'd take any questions. [LB788]

SENATOR GLOOR: Thank you, Senator Schumacher. Just a quick question. I would agree that the rate may go up to address the risk, added risk, but do we have any experience--and maybe you don't know this, but a testifier behind you might--of what that's translated to in some states? I mean has anybody actuarially said you could be talking about anywhere from a blank percent to blank percent range of increase? [LB788]

SENATOR SCHUMACHER: I don't know. I would guess that the rating industry and the underwriters who come forward, they would be the folks to ask that question to, but certainly, to the degree there is any risk at all...and there's obviously some, because otherwise there would be no opposition to this. If it didn't make any difference, it wouldn't make any difference. There is obviously some, and that would be factored into the interest rate. [LB788]

SENATOR GLOOR: Okay. Senator Campbell. [LB788]

SENATOR CAMPBELL: Thank you, Senator Gloor. When you talk about...this is really any political subdivision or just municipalities? [LB788]

SENATOR SCHUMACHER: Anyone that issues bonds, is my understanding. Not SIDs, I don't think SIDs are included in this one. [LB788]

SENATOR CAMPBELL: You're way ahead of me there... [LB788]

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SENATOR SCHUMACHER: Okay. [LB788]

SENATOR CAMPBELL: ...because that was going to be my next question. So it's the most--what would we say--major political subdivisions? [LB788]

SENATOR SCHUMACHER: The big ones are cities. [LB788]

SENATOR CAMPBELL: Counties? [LB788]

SENATOR SCHUMACHER: I think county bonds are included in this. I'd have to check, and perhaps one of... [LB788]

SENATOR CAMPBELL: I would assume that they are from the experts that I've had. But you're...but it's not SIDs? [LB788]

SENATOR SCHUMACHER: SIDs, I believe, are excluded from this. [LB788]

SENATOR CAMPBELL: Okay. [LB788]

SENATOR SCHUMACHER: I think they're covered in another section. [LB788]

SENATOR CAMPBELL: Yes, they certainly have declared bankruptcy. Thank you, Senator. [LB788]

SENATOR SCHUMACHER: Yeah. [LB788]

SENATOR GLOOR: Other questions? Senator Howard and then we'll go to Senator Carlson. [LB788]

SENATOR HOWARD: Thank you, Chairman Gloor. Senator Schumacher, you'll have to forgive me, it's been a while since law school. [LB788]

SENATOR SCHUMACHER: It's been longer for me. [LB788]

SENATOR HOWARD: Could you help me remember the lienholder priority listing for a bankruptcy for a political subdivision? Who goes first? [LB788]

SENATOR SCHUMACHER: I think the bondholders go first. Now there may be some labor things that maybe has preference. [LB788]

SENATOR HOWARD: Uh-huh. [LB788]

SENATOR SCHUMACHER: Outstanding wages or something like that, but bondholders

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are right up there near the top. [LB788]

SENATOR HOWARD: Okay. That's what I was checking out. So they're already at the top? [LB788]

SENATOR SCHUMACHER: Or very near the top. I don't know about wages. [LB788]

SENATOR HOWARD: Okay. [LB788]

SENATOR SCHUMACHER: But there's...in the priority list--and it's been a long time for me, too, and maybe one of the testifiers behind me will know exactly the rating--bondholders are very near the top. And I think they are the top for certain streams of revenue on revenue bonds and also when you get into above the levy limit--and that's kind of a complicated wrinkle that I believe one of the testifiers are going to go into--but bondholders are in a pretty good spot. [LB788]

SENATOR HOWARD: Okay, thank you. [LB788]

SENATOR GLOOR: Senator Carlson. [LB788]

SENATOR CARLSON: Yeah, thank you, Senator Gloor. Now, Senator Schumacher, does LB788, if adopted, put the bondholder at the top of the list in terms of security? [LB788]

SENATOR SCHUMACHER: It puts it at...it keeps it basically as it was prebankruptcy. It keeps it at the top of the list, out of the dedicated revenues and, I think, out of the revenues that are allowed above the levy limit for bonds. [LB788]

SENATOR CARLSON: Now it appears there is certainly a difference between a AAA bond and a junk bond. But they...regardless, they'd both hold the same position in LB788? [LB788]

SENATOR SCHUMACHER: A...that's just a rating. You can have a AAA bond turn into a junk bond if all of a sudden it looks like the city is going to go...doesn't have the revenue or going to have difficulty. I don't think the rating on the bond has anything to do with its priority. The bankruptcy court doesn't ask was this a AAA rated bond. That's just a private rating that's assigned to it. The... [LB788]

SENATOR CARLSON: Okay, but the rating on the bond determines the degree of confidence the person has that buys the bond. [LB788]

SENATOR SCHUMACHER: Right. [LB788]

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SENATOR CARLSON: But there's no differentiation made in this bill for that? [LB788]

SENATOR SCHUMACHER: No. [LB788]

SENATOR CARLSON: Okay. [LB788]

SENATOR SCHUMACHER: No, because that's a private thing that's assigned. This might make a bond go from AAA rated to, you know, AA+ or something. But that's just a grade that some private rating agency throws on it. The rankings on any bonds are determined by, I think, what they call a bond indenture and that puts it...I mean, if you've had a series of bonds that you've put ahead of the revenue and then a second series on second spot, I suppose that would determine which...how you were paid as between bondholders... [LB788]

SENATOR CARLSON: Okay. [LB788]

SENATOR SCHUMACHER: ...just like a person's second mortgage on your house. [LB788]

SENATOR CARLSON: Okay, thank you. [LB788]

SENATOR GLOOR: Other questions for Senator Schumacher? Seeing none, thank you, Senator Schumacher. [LB788]

SENATOR SCHUMACHER: Thank you. [LB788]

SENATOR GLOOR: We'll now move to testimony; proponents first. [LB788]

ROBERT HALLSTROM: (Exhibit 1) Chairman Gloor, members of the committee, my name is Robert J. Hallstrom, H-a-l-l-s-t-r-o-m. And I appear before you today as registered lobbyist for the Nebraska Bankers Association in support of LB788. LB788 is designed to enhance access to capital markets for governmental units by providing that general obligations bonds, notes, and other financing obligations of governmental units have a lien on bond-pledged revenue sources, as defined in the legislation. Following me today in my testimony will be Mr. Sam Moyer from the Heritage Bank in Aurora. This issue arose on our radar screen when Mr. Moyer and others brought to our attention their concerns with respect to what is the state of the law with regard to protections that bondholders, whether they're banks, individual investors, or others have in the event that a local political subdivision were to file bankruptcy. We've seen many instances, unfortunately, in recent years: Detroit, Michigan; Harrisburg, Pennsylvania; Central Falls, Rhode Island; Jefferson County, Alabama, that have given rise to these types of questions--legitimate questions--to be asked and answered. And in the course of looking into the chapter 9 bankruptcy law--which, by the matter, we've got a copy of

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(section)13-402 attached to my testimony--which authorizes Nebraska political subdivisions to file for chapter 9 bankruptcy protection. Nebraska is 1 of, I believe, 29 states that has some express or implied authority for political subdivisions to file bankruptcy. And what we found in the course of our research was that, as Senator Schumacher suggested, prior to the filing of a bankruptcy petition under chapter 9, the bondholders have the protections of the full faith and credit taxing authority--inherently unlimited taxing authority, if you will--to provide protection to ensure the payment of those bonds. However, it's less certain once the bankruptcy is filed where the bondholders end up. And every indication is that they can be treated as general, unsecured creditors, a vast and significant difference from where they were immediately before the filing of the petition. And there is an exception to that rule, and that is...the exception is that if there is a statutory lien authorized under state law, that then the bondholders will maintain that preference or priority and ensure the payment. As we look at the statutory lien, my testimony indicates that 28 states appear to recognize some form of statutory lien, so those protections are evident. Most recently, the state of Rhode Island within the last two or three years, on the cusp of the Central Falls, Rhode Island, bankruptcy had passed legislation that is very similar to what is being proposed here in Nebraska under LB788. And my testimony at page 5, I believe, has a chart that goes through everything I've just talked about in terms of the treatment of general obligation bondholders, the need for the statutory lien to provide that absolute protection or preference with respect to payments. Also in my testimony, I've gone through some information that's entitled "Nebraska Precedent for Bondholder Protection." And, Senator Campbell, you were starting to ask questions about the sanitary and improvement districts. The reason that they are...the primary reason they are excluded from LB788 is that we already have a court decision, the Hollstein decision that is attached to my testimony, that essentially was a certified question of law from the Eighth Circuit Court of Appeals to the Nebraska Supreme Court. And the question that was certified was, in the event of an SID bankruptcy, would the warrants or the bondholders have preference or priority? The court in that case looked at the statutory framework, decided that there wasn't an express statutory lien, if you will, but that they interpreted the statutes to essentially say there was a limitation, a general limitation, on how much taxing authority could be exercised by the SID for purposes of paying warrants, but seemingly unlimited taxing authority to pay the bondholders. And based on that distinction, they determined in essence that the preference would lie with the bondholders rather than the warrants. LB788 is designed to essentially provide that same type of statutory lien protection under Nebraska law. I believe that a strong argument could be made, although we want to make it crystal clear under the provisions of LB788, that similar to the ruling in Hollstein in comparing the statutes, that if you look at the tax levy limit statutes in Nebraska, they provide a 50-cent taxing authority for the general obligations--not general obligation bonds, but general obligations--of the political subdivision, whereas the payments or the tax levy that's authorized for bonds are excluded from that limitation. So, again, the argument, if pressed, would be we have once again seemingly given unlimited authority for the payment of bonds and only

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limited, definite taxing authority ceiling for other obligations of the municipality. I've got to suggest that a funny thing happened on the way to the forum. We certainly have been involved with discussions with the League of Municipalities. We felt, clearly, that they ought to have a vested interest in this, and we'd hoped it would be a positive interest, but I think you're going to probably hear something different with the witnesses that follow me today. And that's all good and fair and I did encourage you to hear them out and listen to their stories, but from talking to some of the representatives, some indications have been that this really isn't a problem. We don't expect any bankruptcies in Nebraska. We haven't seen any adverse impact on our bond ratings, although there's been a couple of issues up in Omaha that I'd draw your attention to with regard to downgraded bond ratings that probably should be taken into consideration. And I think if that's the case, then take them at their word. If they don't think there's going to be any bankruptcies on the horizon or any time soon, then the passage of LB788 from the municipalities' perspective should not cause one iota of difference, but I think that's a little bit shortsighted. I think what's more apt to happen in today's marketplace is that investor confidence is going to be impacted in general obligation bonds with the growing knowledge of what's happening in other communities and counties across the state with respect to the bankruptcies. And it will ultimately have an adverse impact on the bond ratings, the rates of interest that must be paid to purchase those bonds with a lessening investor confidence. And at the end of the day, more interest means more taxpayer funding required to pay off those bonds. So we think that this is a good, prudent approach to ensure that municipalities will have access to capital markets at reasonable rates into the future. And it's a good thing for Nebraska to make that clarification in the law. I would also note that Richard "Dick" Pedersen from the Baird Holm law firm is here today. He assisted in the drafting of the technical niceties of the legislation to ensure that, to the best of our ability, we had things in good working order. And he will be here to testify in a neutral capacity and can address any technical questions that the court may have regarding the impact of lienholder priorities and so forth, and the impact and the application of the law as drafted. I'd be happy to address any questions of the committee. [LB788]

SENATOR GLOOR: Thank you, Mr. Hallstrom. Senator Campbell. [LB788]

SENATOR CAMPBELL: Thank you, Senator Gloor. Mr. Hallstrom, I just wanted to kind of be very specific about your testimony. To date, the bond agencies or the rating agencies haven't issued any statement with regard to this, they've just sort of indicated that it may affect? [LB788]

ROBERT HALLSTROM: I think that's a fair statement, Senator. I have seen...and it may not be right on point because there may have been other issues involved. But one thing that comes to mind, there's a bond insuring company in Alabama--in light of the Jefferson County, Alabama, bankruptcy--that has indicated that they are strongly considering not insuring bonds based on what's transpired in the state of the law with

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regard to bankruptcy policies and practices and procedures under state law in Alabama. It may be apples and oranges, but at least there's those types of statements. I think any...and Mr. Moyer may be able to provide his own reference and information with regard to what he's reading out in the national publications about what they expect to be the impact of these bankruptcies, not just in the communities or in the states where they occur, but some type of trickle-down effect that may impact bond ratings and the rate of interest required on bonds. [LB788]

SENATOR CAMPBELL: Because at some point, you wonder whether they would say, well, the state has legislation protecting this, then we will take that into consideration on the bond rating? [LB788]

ROBERT HALLSTROM: I would certainly think that's a possibility, you know, and in light of what's happened in Rhode Island where Rhode Island took this step and, at least for the moment--even though I think the ruling may be on appeal--the initial ruling has upheld the design and objective of the Rhode Island legislation that very well you could see bond rating agencies coming out and saying, if you've got that magical language in your statute, it is going to be on the plus side of where you end up in terms of bond ratings and ultimately the pricing for those bonds. [LB788]

SENATOR CAMPBELL: Thank you. [LB788]

SENATOR GLOOR: Other questions? Seeing none, thank you. [LB788]

ROBERT HALLSTROM: Thank you. [LB788]

SENATOR GLOOR: Other proponents? Good afternoon. Good to see you. [LB788]

SAM MOYER: Senator Gloor, good afternoon. Members of the committee, my name is Sam Moyer, M-o-y-e-r. I am president of Heritage Bank with our main offices in Aurora, Nebraska. I'm here today to support LB788. As Mr. Hallstrom indicated earlier, I became aware of this issue several years ago and brought this matter to the attention of the NBA. I'd like to thank Senator Schumacher for proposing the bill or sponsoring the bill. And I'm also amazed at the knowledge he has of the effects of this bill, and I think I can make him a banker if he retired someday. Senator Schumacher and Mr. Hallstrom both gave you a very good understanding of our position on the bill and support of the bill. I would just add a couple different points. I think it's been the historical presumption of buyers of GO bonds in Nebraska for the last 25 years that the bondholder did have a priority. The...there is such a thing as a revenue bond, and in a revenue bond the...there is a pledge to a trustee of a set of revenues. With a GO bond, there isn't that pledge. Historically, the GO bond has found to be a safer instrument because the full faith and credit of the political subdivision has been pledged to pay for the bond. The revenue bond is supported by the revenues of a particular facility, whether it be a sewer and

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water facility or whatever is happening. Based on that historic priority for GO bonds, they've had a lower interest rate than a revenue bond. Today a case can be made that a revenue bond actually has better security than a general obligation bond because the revenue bond actually has a pledge of revenues to a third-party trustee, where a GO bond doesn't have a pledge of revenue. And that's what this statute is attempting to alleviate or correct. The statute provides a statutory lien giving preference to the bondholders in a chapter 9 proceeding. Not only is it an issue of enhancing the access to the capital markets and reasonable rates, I think probably the biggest issue is keeping this decision out of the bankruptcy courts' hands and certainly out of a bankruptcy judge's hand. Bankruptcy judges are given tremendous latitude, tremendous latitude. And if you follow what's been going on in some of the national cases, it's been extremely interesting. But I think this is an issue for the Legislature. I think it's an issue for an elected body of people. I don't think it's an issue for an unelected judge who doesn't report at all to the Nebraska people. So I'm asking you not to leave this issue to a bankruptcy court or a bankruptcy judge or a bankruptcy judge interpreting cases from other states. I think this ought to be a Nebraska issue. I think the priority ought to... I think LB788 ought to be passed and supported and give that priority. With that, I think this issue... I think all we're doing here today is clarifying how it's going to be handled in Nebraska. And I'd appreciate the Legislature doing that instead of allowing bankruptcy court to. I'd be happy to answer any questions. [LB788]

SENATOR GLOOR: Thank you, Mr. Moyer. Questions for Mr. Moyer? Seeing none, thank you. [LB788]

SAM MOYER: Thank you. [LB788]

SENATOR GLOOR: I appreciate your coming, Sam. Other proponents? We'll then move to opponents of the bill. Good afternoon. [LB788]

PAUL KRATZ: (Exhibits 2 and 3) Thank you. My name is Paul Kratz, K-r-a-t-z. I'm the city attorney for the city of Omaha. What's being handed out to you are two letters, one from the city of Lincoln, the other from the League of Nebraska Municipalities, opposing this bill. They, along with the city of Omaha, also oppose this bill. Let me suggest that this bill is doing something very unique that I don't think we've ever seen in this state before. And it's essentially putting a lien on taxes, on taxes that people pay. The bankers will now have a lien on those taxes. Prior to this bill, as is mentioned earlier, bonds are backed by the full faith...GO bonds are backed by the full faith and credit of a city or municipality. A revenue bond is backed by the particular revenue that's produced from that particular entity. Now we are switching that to the taxes, your taxes, my taxes, will essentially have a lien on. Why this is important is, as was mentioned also in bankruptcy, this will create a priority. It'll be a secured lien in bankruptcy, which means the bondholders in all likelihood will get paid 100 percent on their dollars. That's certainly good for the bankers, but look at the other people involved. At least up in

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Omaha and in other places, you have pensions, retirees who are counting on their pensions to live out to the rest of their lives. And bankruptcy, if this bill goes through, it's more likely that the pensioners will be crammed down much more than anybody else. If this bill...if the law stays the way it is now, then that's correct as been testified. The bankruptcy court could cram down the bondholders and also cram down the pensioners, but at least it would be a more even split as opposed to all the money going to the bondholders. Up in Omaha, we issue anywhere from \$25 million to \$100 million of bonds a year. I...my finance people and I go before two rating agencies each year, Moody's and Standard and Poor's. We discuss very thoroughly the finances of our city, the issues of our city, what they would like to see for protection. Never has anybody...any of those agencies mentioned that we should have...the state should allow a secured interest for bondholders on tax revenues. That's never even been mentioned. Again, (inaudible)...people that buy our bonds have never mentioned that issue. I suggest if it does become an issue, that's the time for the municipalities to come to this committee and suggest a change, not at this point in time. Again, I would urge that this committee not pass forward LB788. Thank you. [LB788]

SENATOR GLOOR: Questions from any committee members? Senator Christensen. [LB788]

SENATOR CHRISTENSEN: Thank you. Explain to me, doesn't this benefit you from the standpoint of making sure bond rates are cheaper? [LB788]

PAUL KRATZ: I don't think it does, no. We've...again, it's never been mentioned. Our rates are pretty low the way they are now. It's never been suggested that if we had this type of authority in the state that the rates would go lower. And I think as Senator Gloor mentioned earlier and asked for is some empirical study to that effect. I've never seen any. And from a practical experience, it's never been requested. So I don't think it will affect the rates at all. [LB788]

SENATOR CHRISTENSEN: Is there anything that limits how much money a city can borrow, how many bonds they can put up? [LB788]

PAUL KRATZ: There are some limitations. I can't tell you what they are right offhand. [LB788]

SENATOR CHRISTENSEN: I guess my concern is, I have a whole different view of the U.S. economy than a lot of people. I expect a major dip, and I speak major. I wouldn't be shocked to see 5,000, 7,500 on the Dow. [LB788]

PAUL KRATZ: Uh-Huh. [LB788]

SENATOR CHRISTENSEN: And is that not going to throw a huge amount of cities into

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bankruptcy? [LB788]

PAUL KRATZ: I mean, I can't speak for the other cities. I think Omaha feels pretty comfortable the way we manage our lending, our borrowing, excuse me, with the tax dollars that are coming in. And certainly, as in the past--assuming 2008, for example--and subsequently, our taxes...tax rates went down. We collected less taxes, but we were able to adjust our operation to meet those obligations. So yeah, I agree, there may be a dip in the future. There probably will be a dip in the future, and it will be up to the city to manage to that. [LB788]

SENATOR CHRISTENSEN: I guess I just get concerned because there's been zero accountability on the federal end of things, the debt... [LB788]

PAUL KRATZ: That's true. [LB788]

SENATOR CHRISTENSEN: ...the last 10, 20 years has just gotten out of control. I don't care which party is there, but it's been out of control. And I just watch...give you a little background on what I do. I watch, having been a commodity trader, but U.S. dollars not being used as a trade in currency anymore. [LB788]

PAUL KRATZ: That's correct, yep. [LB788]

SENATOR CHRISTENSEN: And when we lose that--you go back to Great Britain--when they lost it, we took a 25 percent dip immediately in the economy or inflation hit 25 percent, just boom. And I'm not saying this bill is good or bad. All I'm saying, I'm very concerned. And so I don't know what the right approach is, but that's why I'm throwing questions at you as well as considering what the bankers have said because I just hope Nebraskans are smarter than the other cities and the federal government. Thank you. [LB788]

PAUL KRATZ: I suspect we are. Let me respond just briefly. I understand the overall concept of the economy. I'm not sure how this bill plays into that or not, except it'll give the bondholders, the large financial institutions that buy bonds, priority over everybody else. [LB788]

SENATOR CHRISTENSEN: I understand what you're saying there. My point was, if the economy drops drastically, people lose jobs, there won't be the funding to get for the cities, which could put them in trouble. That's why I was asking about the limits on the amount of bonds and debt that a city could take. Is Nebraska any smarter than the other...Nebraska cities any smarter? Do we have limitations or can we be as reckless as Detroit, state of California, U.S. government? That's why I was asking about the limits and my concern to the economy. [LB788]

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PAUL KRATZ: I think, at least from the standpoint of Omaha, we're aware of those type of issues. We try to manage our debt, we do manage our debt, and without increasing property taxes. If there is an issue, that is, if the economy does go down, we will manage it. We have the flexibility now to, obviously, to layoff people, to shrink our operations. And we've done that in the past, and we're prepared to do that in the future. [LB788]

SENATOR CHRISTENSEN: Good. Thank you. [LB788]

PAUL KRATZ: Uh-huh. [LB788]

SENATOR GLOOR: Thank you, Senator Christensen, Mr. Kratz. Senator Pirsch. [LB788]

SENATOR PIRSCH: Yes. Thanks for your testimony here today. [LB788]

PAUL KRATZ: You bet. [LB788]

SENATOR PIRSCH: I just have a question, maybe get your opinion on it with respect to the Hollstein case was put forward within the specific context involving an SID, but put forward as an analogy to say that within that context, the SID then was...that it was a clear question of law that, at least within the SID context, that those bondholders did have priority. And with...do you agree that there is a similar analogy then with respect to--it's not expressed here--that bondholders would have priority even without the specific? Or is it a cloudy, unknown outcome should that matter be litigated? [LB788]

PAUL KRATZ: First of all, I'm not familiar with the Hollstein case. I'm sorry, I just haven't read it. [LB788]

SENATOR PIRSCH: Well, that's okay. [LB788]

PAUL KRATZ: Secondly, SIDs are, to me, a different animal than cities and they're, frankly, much more risky. And in Omaha you've seen a fair amount of bankruptcies with SIDs, not with the cities or towns or municipalities. As far as what would happen in a bankruptcy, I'm not a bankruptcy expert. I'd leave that to the court. I have seen in Detroit and some other places where they...let me...in Detroit, they've crammed down the bondholders. A couple of the California cities, they did not cram down the bondholders. So it's probably up to the court. [LB788]

SENATOR PIRSCH: Yeah. And you said in some cities with similar setups the bondholders did not take... [LB788]

PAUL KRATZ: As I recall, I think in two California cities they did not get crammed down.

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In Detroit, I think they are. [LB788]

SENATOR PIRSCH: Okay. [LB788]

SENATOR GLOOR: Senator Carlson. [LB788]

SENATOR CARLSON: Thank you, Senator Gloor. Mr. Kratz, right? [LB788]

PAUL KRATZ: Yes. Yes, sir. [LB788]

SENATOR CARLSON: You said something to Senator Christensen, I think, that I just want to ask you about. I think you said in Omaha, you're prepared to shrink your operation. Did you say that, if necessary? [LB788]

PAUL KRATZ: I said that, and we have done that in the past. In the mid-2000s, we reduced the number of civilian employees and reduced a little bit the fire and police employees, but not to the same extent. [LB788]

SENATOR CARLSON: And why did you do that? [LB788]

PAUL KRATZ: Because tax revenues decreased. I shouldn't say decreased, they did not increase to the extent that we thought; that's because of the economy. So as a result, revenue was less so we adjusted our operations to meet the revenue. [LB788]

SENATOR CARLSON: Okay. And that makes sense. Now when things turned the other way, then, was it necessary to expand again, because it sounds like that's what happened. You shrunk and then when you could, you expanded because you said... [LB788]

PAUL KRATZ: No. Frankly, we haven't expanded. [LB788]

SENATOR CARLSON: Okay. All right. But you said we're prepared to shrink if we need to. And so... [LB788]

PAUL KRATZ: Yeah. I guess maybe the question is how much further can we shrink? [LB788]

SENATOR CARLSON: Okay. [LB788]

PAUL KRATZ: But we have not expanded to the same level we were in the mid-2000s. [LB788]

SENATOR CARLSON: Okay. Thank you. [LB788]

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PAUL KRATZ: Uh-huh. [LB788]

SENATOR GLOOR: Senator Christensen. [LB788]

SENATOR CHRISTENSEN: Thank you, Chairman. Why are sanitary improvement districts under different rules, and why are they riskier? Are the ratings on them just quite a little higher then? Because in this one letter from Steve Hubka it says, "I also note with the exception of Sanitary Improvement Districts, municipal bankruptcies have not been a problem in Nebraska." So is that saying sanitary improvement districts have been a problem? [LB788]

PAUL KRATZ: There...I shouldn't say...I don't know the numbers, but there have been a fair amount of bankruptcies with the SIDs. I can't tell you how many. The differences, you know, are several. One, obviously, their interest rates are higher because they're not backed by the full faith and credit of a city. They're backed by the SID, they're backed by the developer and the land, the value of the land whatever that may be. Now they do have the taxing authority, and they can impose taxes on their SID. But on the other hand, if the SID is not built out and the value isn't there, that's where you end up with problems. It essentially happens when a developer goes in, creates an SID, and it doesn't develop out quickly enough. [LB788]

SENATOR CHRISTENSEN: So it's not a city...sanitary improvement districts aren't city led, they're contractor led? [LB788]

PAUL KRATZ: Developer led, yes, sir. [LB788]

SENATOR CHRISTENSEN: Developer led? Okay. That helps me. Thank you. [LB788]

PAUL KRATZ: Okay. [LB788]

SENATOR GLOOR: Other questions? Thank you, Mr. Kratz. [LB788]

PAUL KRATZ: Thank you. [LB788]

SENATOR GLOOR: Good afternoon. [LB788]

JOHN CORRIGAN: Good afternoon. Good afternoon, Mr. Chairman, members of the committee. My name is John Corrigan, C-o-r-r-i-g-a-n, and I'm an attorney in Omaha with the firm of Dowd, Howard and Corrigan. I'm here on behalf of the Nebraska AFL-CIO as well as the Nebraska Professional Fire Fighters in opposition to LB788. There's been, obviously, very good discussion among the testifiers today as to the relative strengths and weaknesses of this concept. But I would...you know, first, I want

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to give you some figures on who actually holds these bonds. I looked it up the other day. The Federal Reserve says 44 percent of all municipal bonds are held by individual investors; 25 percent are held by mutual funds; and roughly, 31 percent held by banks and insurance companies. Why would you want to hold, as an individual investor, a municipal bond? Tax-exempt status. So the lower interest rates that they might pay out as opposed to a corporate bond, are more advantageous because of the tax-exempt status. Now, obviously, there are great risks for individuals who hold those type of investments if there is a bankruptcy. And nobody is here to testify that we want to see those people lose because their money is very important to make sure our communities are vibrant and strong. Just today, the Lincoln Journal Star issued an editorial saying that the voters should vote for \$153 million in bond issues to improve the school system. The problem is that in order to provide services, the government that we expect, that cannot be done without people. And those people should not be placed in a second class...as second-class people when it comes to determining who gets in line and who gets paid if there is a bankruptcy. In effect, this legislation is placing a value judgment. We value money and those who risked dollars over those who risked the best years of their lives, and risked life and limb in the service of their citizens. I'm talking about public safety, I'm talking about teachers, I'm talking about nurses. Anybody who is employed by a public agency is now asked to get in line and maybe you'll get paid, and maybe you won't. But they certainly are going to pay those who risk their dollars. Now their dollars are important, but that is for the court to decide. And I think it's important that the court has...the bankruptcy court has the ability to decide that if there is the unlikely event of a bankruptcy in the municipal setting, that everybody takes a haircut, not just the people who had the unfortunate life circumstances to have been only able to risk their bodies and the years of their lives as employees in order to have the status of a creditor of a particular city or county or other municipality. Part of the problem, I feel, in this legislation is that it is separating or creating these two classes of people. And I believe that to be unconstitutional under article I, section 16 of the Nebraska Constitution, which provides that, "no...law impairing the obligation of contracts, or making any irrevocable grant of special privileges or immunities shall be passed." If you're not...one, you're impairing the obligation of contract because those people who agreed to work for 30 years and get a pension from the employer...that's a contract, and it's enforceable, and it is a vested right. And that contract is now, according to the Nebraska Legislature, voidable. Whereas, a contract that that same employer had with the bondholder is not voidable, they can't get out of it. Now I also believe that you clearly are creating a special privilege and an immunity for those bondholders that doesn't exist and you have not created on behalf of the individuals who find themselves in a place of being second in line after giving the best part of their lives in order to earn the benefits that are incumbent upon their service. So with that, I'd be happy to answer any questions and ask that you please oppose LB788 on those grounds. Thank you. [LB788]

SENATOR GLOOR: Thank you, Mr. Corrigan. Are there questions? Senator Carlson.
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SENATOR CARLSON: Thank you, Senator Gloor. Since we're not...in this question, I'm not talking about Omaha, but I would ask you, in the case of Detroit and the pension plan and the money is not there now to carry out the specifics of that pension plan, who's supposed to honor it? [LB788]

JOHN CORRIGAN: Well, my understanding of the Detroit pension plan is that they're about 90 percent funded. There is money there to honor it. The money is going to be shared among the bondholders, so the pension holders are not getting the amounts that are in the pension fund. Those are assets of the city that's going to be distributed among all the creditors. Which, obviously, that's not ideal, but in the bankruptcy context, if everybody is going to...if somebody is going to take a hit, everybody is going to take a hit. And, ultimately, that is the obligation of the citizens of the entity either through taxing or through selling off assets or reorganizing their debts. And that's exactly what they did. And whether they needed to is also, you know, a large question. The labor...my side of the table says that was a bankruptcy of choice, but whether that's true or not, I guess that's a matter that's being litigated. But who's ultimately responsible to pay those benefits or those pension obligations? The city is. And the city, the only way that they can escape that payment is to take those...all of their creditors to bankruptcy. And, in fact, what this legislation is doing is saying, you know what? We're going to encourage bankruptcy, because now you can tell your bondholders, don't worry. You won't have to take a haircut, we can make sure that all of our other creditors will be the ones that have to take a loss. And I just don't think that's...that's not a way to be operating business. As, you know, we talk about Nebraska values, we're all in this together, and, in effect, what this bill is saying is, we're not in this together. In fact, if you were fortunate enough to have money to risk, you have no risk. [LB788]

SENATOR CARLSON: So you're saying that if this happened in Omaha, the bondholders should have no more protection than the employees who are depending on that pension plan, and that everybody should take their share of the hurt. [LB788]

JOHN CORRIGAN: If that happened, yes. I think that that is...and I, again, I think I'm not familiar exactly with the Hollstein case, but I would expect Mr. Hallstrom to be. As I understand the holding in that case as it was elicited today, they're simply saying there is a limit on your ability to tax for purposes of general obligation, but no limit on your ability to tax in order to pay off existing debts or to pay the bondholders. The problem from our perspective is--and I'm sure you all are familiar with it is--you read the bond prospectus and the employer will send it out and say, hey, these bonds are backed by the full faith and credit of the city of Lincoln or the public schools or the city of Omaha and the taxing authority. And look, here's our levy limit, and here's where we're at in relation to that levy limit so, if we need to, we can raise taxes. But they never do, they never want to, nobody will vote for anybody who did. And so there's this always constant pressure as to where that money is going to come from. And as the city or, you

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know, the employer in good times, yeah, they go ahead and pay down their debts. In bad times, they might extend their debts. But to say that that case somehow acknowledges to the situation, I disagree because right now they do have that authority to raise taxes to pay off debts or to right their ship with regard to unfunded liabilities. But nobody wants to exercise that authority. And the people obviously don't want them to because they don't elect somebody that tries to do that. That person usually gets unelected. [LB788]

SENATOR CARLSON: Okay. Thank you. [LB788]

JOHN CORRIGAN: You're welcome. [LB788]

SENATOR GLOOR: Other questions? Senator Campbell. [LB788]

SENATOR CAMPBELL: No. [LB788]

SENATOR GLOOR: Senator Howard. [LB788]

SENATOR HOWARD: Thank you, Chairman. Mr. Corrigan, can you help me sort of parse through this? My mother was a social worker for 34 years for the state, and she has a pension. And during those 34 years, she paid into that pension. And so under this legislation, in your view, if she had paid into her pension, but the state of Nebraska, for whatever reason, went bankrupt the bondholders would be able to have a taker's right before my mother's 34-year-old pension? [LB788]

JOHN CORRIGAN: Well, I don't think that the state situation is quite apt. But let's say that your mom worked for Douglas County... [LB788]

SENATOR HOWARD: Okay. [LB788]

JOHN CORRIGAN: ...and Douglas County decided to go bankrupt. And she had 34 years, paid into the system 9 percent, 10 percent, 12 percent of her pay going into that system every year. And then the benefit that she earned is supposed to be paid out. Under this proposal, any bondholders of debt that had been issued by Douglas County would have, one, priority over payment of those benefits, and they might have a lien against existing authority of Douglas County to tax its citizens in order to pay those debts. As I understand it, that's...they have the right to the first dollar. So not only payment of existing wages or, you know, keeping the lights on at the county hospital. But, certainly, those pensioners would be exposed to reduced benefits to the point of zero, if need be, in order to make sure that those individual investors, those mutual funds, and those banks and insurance companies who hold that debt get paid. [LB788]

SENATOR HOWARD: Thank you, Mr. Corrigan. Thank you. [LB788]

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JOHN CORRIGAN: Okay. [LB788]

SENATOR GLOOR: Senator Pirsch. [LB788]

SENATOR PIRSCH: Do you have a feeling of the state of the law right now? Is it absent, you know, this legislation, is the state of the law, in your opinion...or do you have one, that the Hollstein analogy probably applies, and that these bondholders would probably take already? Or is it cloudy and there's no way to tell or is it...or do you think that it probably would go the opposite and that that's a clear result? Do you have a feeling about what the state of the law is? [LB788]

JOHN CORRIGAN: I don't. I have...you know, we followed the bankruptcy cases out in California. And I think that Mr. Kratz's recitation is correct, that even though there were adjustments to existing contracts in California, the bondholders did not lose out and neither did the pensioners in those cases. Detroit is probably the...in some of the Rhode Island cases as well, the best examples of, you know, in Rhode Island where pensioners settled their cases, came out with an agreed-upon resolution. Many of them did, in any event, and bondholders also agreed to take less. I just think that based on what was said about the Hollstein case, I don't think that that solves the issue by any stretch of the imagination because it is an SID and it was so different, one. And two, if they said...the bankruptcy court said what I'm understanding the Nebraska Supreme Court to have said in the Hollstein case, it wouldn't mean, necessarily, that the bondholders had a lien, what would take first priority. It would just mean that the cities or for the, you know, the city in that example, has an unlimited taxing authority to pay off those debts, not limited by levy limits. And if that's the case, do you really think they're going to exercise that authority? I don't know. But, you know, the bondholders are people with a lot of savvy and experience. And they're able to read those prospectuses, they're able to read the Moody's and Standard and Poor's resolutions to determine whether there's a good bet or not, but they're making a bet. When our members go to work for an employer for 30 or 40 years, they're not making a bet. They can't just go out and find another game to play. This is the game. And so we think that to say the bondholders should be placed in a separate and better class is a value judgment that Nebraska shouldn't make. [LB788]

SENATOR GLOOR: Other questions? Seeing none, thank you, Mr. Corrigan. [LB788]

JOHN CORRIGAN: Thank you. [LB788]

SENATOR GLOOR: Anyone else who wishes to speak in opposition? Anyone in a neutral capacity? Good day. [LB788]

RICHARD PEDERSEN: Good day. My name is Richard Pedersen, R-i-c-h-a-r-d

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P-e-d-e-r-s-e-n. And I've been practicing as a bond attorney for approximately 40 years. And I guess I'm the funny thing that happened on the way to the forum. Obviously, a piece of legislation as complex as this needed someone to draft it. And when I was called upon by the Bankers Association, I said, well, at least here's a chance for the bond attorneys, the one who have to read the law, interpret the law, describe the law, and then give opinions on the law, to have some degree of certainty as to what the law is going to say and to make it fit with our legal situation with respect to bonds in Nebraska. And so I agreed to do that for Mr. Hallstrom on the condition that I would arguably be working for the league. And when the league saw what I drafted, obviously, the legal commission said or the committee of league members that was considering the proposal determined that opposition was appropriate, at least at this time, and so I'm testifying in a neutral capacity. I don't want to be...I'll try not to say anything either too favorable or unfavorable. One thing you should be aware of--and this is an unusual thing--the National Association of Bond Lawyers has an annual tax and securities law meeting in Boston this year, and they have set on the agenda a general session for an hour that is to discuss general obligation bonds, the different kinds of general obligation bonds, and distinctions that are to be made. Members of the rating agencies, I expect, will be present at that seminar. And they may start, after that discussion is over, to think about distinctions between the laws of different states as to which laws provide the best protections. And it is possible that the city of Omaha or city of Lincoln when they next go to the rating agencies--and they're the principal municipal borrowers that go to the rating agencies in Nebraska--they may get different questions, and their position on the bill may change. We are kind of at a crossroads. It's my understanding that the Detroit situation has not been resolved yet. There are two different things that happen in bankruptcy. You can classify claims and then if claims are classified, they may have different voting rights depending on how the judge views the various respective rights of a class with respect to the assets that are involved. Then with municipalities, you're always talking about a flow of cash or other revenues. That's one thing that happens. The other thing that is provided for in the Bankruptcy Code is in sections 928 and 902, and that is, in (section) 928, you can have a continuing lien under certain defined circumstances for future tax revenues. And that's under section 928. Section 902 has several categories of what are called special revenues. And the ones that are specifically described are taxes specifically levied to finance one or more projects or systems, but they talk about being payable from or distinguished from taxes levied to finance the general purposes of the debtor. Nebraska law fits fairly closely into that context. We have a, under section 77-3442, a series of judgments made by this Legislature as to what's an appropriate level of taxation for general fund purposes, and that's the 50 cents on the dollar that is provided for in that section, and then an exception is made for the payments for bonded debt. The Hollstein case is an analogy, which you could conceivably argue in bankruptcy today would provide for the bondholders to be treated as a separate class, but not necessarily as a secured class. And treated as a separate class so that they might have rights with respect to how they're to be treated in a plan that's to be feasible and fair, realizing that the Bankruptcy

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Code's purpose is not to do anything other than to see that the creditors are appropriately taken care of. And it's not so much for the benefit of the municipality, although it has to recognize the obligation. You know, none of us--I'm from Omaha--would be very happy if we found our police protection was all of a sudden inadequate or fire protection. There's always, in the judgment of the bankruptcy court, going to be the question, okay, we've got to pay for the basic services that keep the city alive and the revenue stream alive. Otherwise, it's no good for the bondholders, it's no good for the pensioners. And so that judgment is always going to be there in terms of who sets the tax level. In a petition and plan to be judged feasible, the taxing authorities have to exercise...they don't have...they can't just say, well, I won't be elected, I'll be thrown out of office. They have to exercise their taxing jurisdiction to the fullest amount that the court deems feasible. And in the bankruptcy area in...with respect to sanitary and improvement districts, our bankruptcy judges have set a level, and it's a lot higher than what those of us who live inside the city of Omaha find ourselves paying. Ninety cents on the dollar is basically where our bankruptcy judges have said, okay, you're in a Sanitary and Improvement District, that's the tax level that's going to be required of you, but no more than that because after that, it becomes unworkable. You've got a bunch of vacant lots that people think they're going to have to pay taxes in excess of 90 cents on the dollar, they're not...no one is going to move in, there will be no houses built, the whole thing will be self-defeating. But the bankruptcy judges have kind of determined on that level and it seems to have worked so far at least in terms of working out settlements. Sanitary and Improvement Districts are excluded from this legislation because they've got a lot of experience, they've got Nebraska case law that is the basis for which the bankruptcy judges have made their decisions, and it's a system that seems to work, and so it's not included in this particular legislation. Just a few comments on the bill itself. It does grant a security interest for the preexisting indebtedness. In other words, let's say Omaha has \$250 million worth of debt outstanding, this bill does grant a security interest in favor of those bondholders. You can't just take the next set of bonds and give them the right to have a security interest in that stream. Otherwise, you would be impairing the promises, really, that have been made by the city of Omaha or city of Lincoln, city of Grand Island, any particular community, which has said in the bond forum that the full faith and credit of the city, let's say Grand Island, are hereby irrevocably pledged. If we were to create a lien priority for bonds only going forward, you'd find that we were likely to be substantially impairing, if not technically impairing--but substantial is what matters in the case of impairment of contracts--the contracts with those existing bondholders. I think that's about all I'd...I would like to entertain technical questions. Again, I'm not saying vote for it or vote against it. There are value judgments that you can tell from the prior testimony that the Legislature has to make in this particular area. You're really weighing, on the one hand, the potentially higher credit costs that cost everybody, including costs that have to come out of tax dollars that can go to satisfy unfunded pension liabilities. And on the other hand, you're making a value judgment that the law is likely to develop in an area where we're finding that bondholders, banks, institutions, and individuals are going to expect

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greater protection. If you don't give that protection it will, at least, be problematic. Any questions? [LB788]

SENATOR GLOOR: Me. Pedersen, thank you for your testimony. When you first walked up here with book in hand, you had a look to you that told me you were either an attorney and that's a book with a number of statutes in it or you're a minister and you're going to tell us the answer is in that Bible you have at hand. Something along... [LB788]

RICHARD PEDERSEN: It's probably in both books, but... [LB788]

SENATOR GLOOR: It may be the Bible of your profession, I might say that. [LB788]

RICHARD PEDERSEN: That's probably right. [LB788]

SENATOR GLOOR: There are...I'm sure there are those in the audience who know you and know of you. I do not. But in my several years now of hearing testimony in this committee and others, I can't recall hearing of anybody who was engaged by the proponent for a bill who wrapped themselves in the mantle of the, now, opponent of the bill and is providing the... [LB788]

RICHARD PEDERSEN: It's the best I could do. [LB788]

SENATOR GLOOR: Yeah. Could you help me with your background and help me understand what brought you to this point today with us? [LB788]

RICHARD PEDERSEN: Well, I practiced in the area of giving bond opinions, looking at disclosure documents for now 40 years for the firm of Baird Holm, which is one of the three or four firms in the state that practice in that area. And, of course as you may gather, there's...over the time that I've been practicing, there's really developed also a national community of bond attorneys largely because the tax laws were the same. The state laws are all over the map and vary greatly, but the federal tax laws are the principal reason why bond attorneys get together. [LB788]

SENATOR GLOOR: And so you usually are engaged by municipalities as relates to bonding. Is that true? [LB788]

RICHARD PEDERSEN: We're all over the map. [LB788]

SENATOR GLOOR: Okay. [LB788]

RICHARD PEDERSEN: The principal source of our employment would largely, historically have been underwriters coming to us looking for our opinion in order to be able to market bonds. But in that representation, over the years we've come to

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represent a variety of cities as well. [LB788]

SENATOR GLOOR: Okay. That does help me put it...your testimony into context. [LB788]

RICHARD PEDERSEN: Okay. [LB788]

SENATOR GLOOR: Other...Senator Campbell. [LB788]

SENATOR CAMPBELL: Thank you, Senator Gloor. Mr. Pedersen, thank you very much. I can recognize your rather tenuous position here. Neutral is probably a good spot. [LB788]

RICHARD PEDERSEN: It's best as I can do. [LB788]

SENATOR CAMPBELL: Earlier I asked if...and I realize this is an opinion question, but will the national rating agencies start looking at these bankruptcies and say, if a state has this... [LB788]

RICHARD PEDERSEN: Mr. Kratz... [LB788]

SENATOR CAMPBELL: ...there's a greater protection for us? [LB788]

RICHARD PEDERSEN: Mr. Kratz will probably be the first one to find out. And I can't say. We do know they're asking harder questions about tax-supported bonds. And because Rhode Island adopted, under very difficult circumstances, a bill that's sort of the predecessor, we used it as a model. And in the Central Falls bankruptcy, the bondholders were left to one side, and Mr. Corrigan would be quite right to say that people who were forced to take less than 100 cents on the dollar were the various pensioners in the state. Very important to note that Rhode Island's law came into being, I think, at the behest of their treasurer who was very active. And, of course, Rhode Island is a state that borrows; Nebraska does not. Nebraska...we can borrow \$100,000 and I think that's it. There are some other odd cases like highway bonds, but we can't borrow. And, of course, the treasurer of Rhode Island--I'm just basing this on national news media so it's no better than the evening news, okay? She realized that if we didn't...if the situation wasn't fixed, the next time Rhode Island went to market to borrow for their needs, they would be in difficult straits. So Central Falls, difficult community, in decline like Detroit itself, lots of pensioners, you know, where the liabilities are immense. And to a certain extent those pensioners going to Florida and not paying their tax dollars back...their income tax dollars back to the state. I think those situations were a little more easily resolved in the state of Rhode Island than might be the case here. [LB788]

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SENATOR CAMPBELL: What little experience I've had with bond rating people, they really want stability. [LB788]

RICHARD PEDERSEN: Well, they're looking for security. Nebraska has offered that to them over the years, and we would hope it would continue to. Senator Christensen, if you're right, we're all in trouble. But we've had a very good record, I think, in terms of little bankruptcy. You need to see SIDs as part of why Omaha is so solvent. It hasn't...in order to have development and economic progress, it...the city hasn't had to risk its dollars. It's been able to rely on individuals willing to risk money, both developers and investors, for higher rates of return, but at much higher risk, and with Omaha only being able to take over the area when it decides it's financially feasible. And that's been very good for--obviously, I'm from Omaha--this has been a very good system for us because Omaha has to worry about our own infrastructure inside the city and done a lot of progressive things like the civic center and all the things that go with the College World Series, all those wonderful things, but calling for debt, getting with fire and police pensions, but it's not had to worry about this whole other area of how do you finance development going on, on the outskirts of your city. That's all been left to smaller developers and to investors who are willing to risk their funds for a much higher rate of return. [LB788]

SENATOR CAMPBELL: Thank you. [LB788]

SENATOR GLOOR: Thank you, Mr. Pedersen. Other questions? Senator Carlson. [LB788]

SENATOR CARLSON: Thank you, Senator Gloor. And thank you for your presentation. I want to just look at a possible circumstance here and you can explain how this can happen. Senator Howard talked about her mother having been 34 years (inaudible), so let's take a city other than someplace in Nebraska. And people like Gwen Howard have worked 34 years and there's a whole class of them that've worked 34 years, and they've contributed 9 percent, 10 percent, or 11 percent of their salary over that period of time. We've got the historical return on rather moderate investments, so we know what that is. So when they're ready to retire just with their contributions and a moderate rate of return, there should be a given amount of money in their help fund. Now if that's all that's in there, which apparently happens sometime, how can that happen? [LB788]

RICHARD PEDERSEN: Well, it's... [LB788]

SENATOR CARLSON: Or even worse, it's not even in there. [LB788]

RICHARD PEDERSEN: It's Senator Christensen...I have to decide here, if the stock market goes to 5,000 from it...and I can recall watching evening discussions on Wall Street Week or something like that where they were talking about 800, not 5,000. This

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was back in the late '70s. The pension funds are in a defined benefit plan. Money is contributed and the pension provider says, we're going to pay Ms. Howard's mother X per year and maybe with adjustments for inflation so that she's got a fixed income that she can rely on that looks like Social Security. Okay? That's a defined benefit plan. Her contributions go into that, but they're invested, and if those investments go sour, then there's the unfunded portion, which the city in the defined benefit plan agrees to pay come hell or high water. They take the investment risk. In the defined contribution plan--which is probably the most common plan in the smaller cities in the state of Nebraska and is the type of plan that we have for police and fire, I think, on a statewide basis--in the defined contribution plan, you put your money in, you're the investor, you're going to get out whatever the investment was, and if the investments go sour, we're investing with Senator Christensen. And, you know, that can happen. The dominant form of pension benefit, as I understand it, in private enterprise has switched from long ago being a defined benefit plan to being the defined contribution plan. And so all of us are really sitting at risk on the stock market and the bond markets. And, you know, you talk to somebody sitting out on the street and they'll say, what are these public employees talking about? My pension looks like a defined contribution plan. And that's, you know...but on the governmental side and some institutional sides, even with some of the larger corporations, you're dealing with defined contribution plans, and those are the risk of the employer. [LB788]

SENATOR GLOOR: Thank you, Mr. Pedersen. I appreciate it. [LB788]

RICHARD PEDERSEN: Anything else? [LB788]

SENATOR GLOOR: Thank you. [LB788]

RICHARD PEDERSEN: Thank you. [LB788]

SENATOR GLOOR: Anyone else who would like to speak in a neutral capacity?
Senator Schumacher, you are recognized to close. [LB788]

SENATOR SCHUMACHER: Thank you, Senator Gloor and members of the committee. Imagine yourself about, oh, 50 years old or so, and you talk to your financial advisor, stockbroker, whatnot, banker. And you're told, you know, you probably should get out of equities a little bit and start moving into bonds because you're getting older and you want to make sure that you have a safe place to put your pension money, your retirement fund, and stock market might do what Senator Christensen says. Certainly, no one discounts that that's a possibility. And so put it in something secure where at least you know your principal is safe. And you'll get a low rate of interest, but you'll at least get interest and you won't be a pauper in your old age and your savings squandered away. Now, broker then says to you, but before I sell you this thing called a bond, I've got to show you something. And it's a piece of paper that says disclosure.

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And we'll use some of the language used today. If there is a bankruptcy, you will take a haircut along with the holders of the unfunded defined benefit pension liabilities of the issuer. Are you pulling out your wallet to buy those bonds? Or you can look to one of the 25 or 30 states who says, that's not the case here. Or are you going to say, I think if I'm going to put my money there in that Nebraska institution, I'm just going to have to have a little more return on investment? Think of the numbers we've been told. Forty-four percent of the holders of bonds are individuals, they're savers, people who have built their own pensions, public employees who have put their money into a defined contribution plan. That's their nest egg. They weren't negotiating for it. They weren't trying to see if a public body would take on unfunded obligations in exchange for a lower salary now. That's their savings. Twenty-five percent, I believe the number was, mutual funds. Who is that? It's the same people, people who have saved, people who got into this deal not thinking that suddenly their savings would be diluted with what might be the reckless expenditures and deals made by a city who got carried away with promising everything now and not raising the taxes in order to fund the now. Banks and insurance companies...I think we're being signaled. Lots of people have their savings in insurance policies. So what we're boiling down to--and this has been a pretty good discussion, the committee is going to have to make a decision--is are we going to protect the pensions and the savings of those people, real people with real hearts? Or are we going to make them unwillingly, in the unlikely circumstance of a bankruptcy, contribute to the unfunded and perhaps recklessly incurred obligations of a political subdivision unknowingly? Well, the very least folks, at the end of today if we do nothing else, we should do those investors a favor and let it be disclosed that our municipalities are not willing to stand behind their obligations and their promises with their full faith and credit in bankruptcy, out of bankruptcy, whatever. I'll take any questions. [LB788]

SENATOR GLOOR: Any final questions? Thank you, Senator Schumacher. [LB788]

SENATOR SCHUMACHER: Thank you. [LB788]

SENATOR GLOOR: (Exhibits 4 and 5) And we will close the hearing on LB788. And that ends our hearings for today. I'm going to ask members of the committee, if you would, to...we'll take a ten-minute break and then reconvene here for discussion on our bills in Executive Session. And there are some other business matters to discuss. [LB788]