MINUTES

MONTANA HOUSE OF REPRESENTATIVES
52nd LEGISLATURE - REGULAR SESSION

COMMITTEE ON BUSINESS & ECONOMIC DEVELOPMENT

Call to Order: By **REP. BOB BACHINI, Chairman,** on January 21, 1991, at 9:00 A.M.

ROLL CALL

Members Present:

Bob Bachini, Chairman (D)
Sheila Rice, Vice-Chair (D)
Joe Barnett (R)
Steve Benedict (R)
Brent Cromley (D)
Tim Dowell (D)
Alvin Ellis, Jr. (R)
Stella Jean Hansen (D)
H.S. "Sonny" Hanson (R)
Tom Kilpatrick (D)
Dick Knox (R)
Don Larson (D)
Scott McCulloch (D)
Bob Pavlovich (D)
John Scott (D)
Don Steppler (D)
Rolph Tunby (R)
Norm Wallin (R)

Staff Present: Paul Verdon, Legislative Council
Jo Lahti, Committee Secretary

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed.

Announcements/Discussion: HB 157, HB 209, HB 241 were to be heard today. Executive action was taken on HB 209.

HEARING ON HOUSE BILL 157

Presentation and Opening Statement by Sponsor:

REP. JESSICA STICKNEY, HD 16, Miles City, explained HB 157 clarifies that if a mortgage payment includes an amount placed in a reserve fund to ensure payment of taxes and insurance on the mortgaged property, return on investment of money in the reserve fund must be credited to the fund; also it clarifies that if the fund exceeds 110 percent of the amount needed to pay taxes and insurance the mortgage payment must be decreased until the figure

is 110 percent or smaller. It amends Section 71-1-113, MCA. The interest on the reserve fund must be credited to the mortgage holder. This is good and fair legislation. She asked favorable consideration.

Proponents' Testimony:

MS. STICKNEY read a letter urging support of HB 157 from **Tom W. Clarke, Miles City,** who was unable to attend this hearing. **EXHIBIT 1. Mr. Tom W. Clarke** is an insurance agent; he owns his own company, has been an independent insurance agent, and is a substantial business man in Miles City. A reserve fund for payment of taxes and hazards insurance is held by the mortgage banking firm. This fund could become sizeable. The mortgage banking firm does not credit any interest earned on the fund to the borrower at the present time. HB 157 would require any interest exceeding 110% of the reserve funds necessary to pay taxes and insurance be credited to the reserve fund. It is not fair for the lender to earn interest from the borrower's funds. He would like the Committee to give positive consideration to HB 157.

Opponents' Testimony:

John Cadby, Montana Bankers Association, handed out a question and answer paper. **EXHIBIT 2.** The subject matter of HB 157 is a little more complicated than what would appear on the surface to be rather a simple solution. If it were simple, most states would already have adopted it. An overwhelming majority of states do not require interest on mortgage reserves. The reason is cited in Exhibit 2. For the most part reserves are required on all secondary markets. You have to keep in mind that we are not just talking about out-of-state mortgage companies. Your State Board of Investments holds 3,000 mortgages, and the State Board of Housing holds 11,000 mortgages. Most of these mortgages are for low income home buyers who do not have $2,000 in reserves; more likely they have just a few hundred dollars at any one point in time. If you raise the cost of doing business by passing this bill, obviously that cost is going to be passed on to the consumer, so this cannot be labelled a consumer bill. What they are going to get on one hand is going to be taken away by the other hand. The Board of Housing said they would have to raise interest rates and also origination fees in order to offset this additional expense.

Everybody profits from reserves. That is why they are mandatory throughout the mortgage world. Lenders are assured these taxes are going to be paid. The borrowers are assured the taxes and insurance premiums will be paid even in hard times. This idea got started during the Depression. It saves the counties a ton of money to get one check from the bank, mortgage company or State of Montana instead of thousands of little checks, so the counties love reserves. We are trying to keep that incentive of having the reserves in place. If each home owner had to pay their taxes when

due, there would be a whole bunch of problems. Taxes wouldn't get paid. It would be a mess. The studies here are rather ancient. He hasn't seen any recent studies. Most states have given up on this subject and are ignoring it, but the studies that were done showed there wasn't any money being made either by the secondary markets or governmental agencies like FNMA and Freddie Mac, nor were the lenders. That probably holds true today because these reserves for the most part are not substantial.

On the second page the eight functions that a mortgagee has to perform in processing these reserves are listed, and they are administrative headaches that cost money. The secondary markets now contract with companies to handle reserve accounts. They not only sell mortgages but they contract to companies that specialize in handling reserves. They will go to a secondary market and say 'let us take care of the reserves - you can have the principal and interest - for taxes and insurance premiums'. They will contract to do that for a fee. The mortgagors however don't run into that. They don't see that. They make only one monthly payment to whoever has ownership of the mortgage at that particular point in time.

This is a very complicated situation - you are talking about thousands of mortgages that are in place today. So not only are you kicking in an additional expense by passage of this bill, you would be kicking in an additional expense that affects mortgages that are already in place that have fixed interest rates.

You are also affecting the cost of originating new mortgages for new home buyers and other purchasers. Obviously lenders could refuse to handle reserves on a conventional mortgage. It's easier for banks that are going to hold the mortgages not to handle reserves and tell the borrower to take care of their own reserves for insurance and taxes. If they sell to a secondary market, they don't have any choice. The bank, the S&L or credit union is told what they have to do to sell to a secondary market. If they sell to the State, the State Board of Investments and the State Board of Housing cannot handle reserves. They usually contract with the lender bank to take care of reserves. They just handle the principal and interest. They buy the mortgage from the bank, S&L or credit union. They could charge higher interest rates for new mortgages; charge higher fees on new mortgages, charge fees for shortages in funds. Secondary markets now charge a $60 tax service fee. Today most financial institutions charge a fee if there is less than $300 in a savings account, because the administrative costs to handle small savings account has to be offset with a fee. Most mortgage reserves at any one point in time are not going to amount to more than a few hundred dollars. In fact some mortgage companies are now requiring a payout in November. In other words they all accumulate into reserves until November and instead of paying the counties half in November and half in May, they are paying a total year's taxes in November, wiping that account out. Also, you will have to keep in mind that lenders and mortgage companies usually advance funds if the

reserves are short, and they usually do that without charging a fee.

He urged the Committee to kill this bill as it has been killed many times in the past for various reasons. We don't want to dry up sources of capital in Montana. We don't want to create a disincentive to provide mortgage money in Montana from these secondary markets. We want to make it as attractive as possible to get that capital into Montana, and by not imposing an interest on reserves it will help to keep that flow of capital coming into Montana, and that is going to benefit the consumer more than anything else.

Michael P. Varone, Vice President of Northwest Bank and Past Chairman of Montana Bank Association, Retail and Real Estate Committee, said **Mr. Cadby** has covered all the issues very well and he is in full agreement with what he has said. In the banking industry they set up reserves for many reasons and most funds are already put into that special entity. One reason is to control the delinquency problem. If they do require interest to be paid on reserves, it will most likely dry up the secondary markets and also banks would not require reserve accounts. If they do not require reserve accounts, delinquencies will rise. Now most mortgage companies and investors usually stay away from the Western part of the United States because of the real estate climate we have today. The administrative cost on this, if this measure passed would be passed on to the consumer. An average loan would run in the neighborhood of $50,000, loan cost about $400. So maximum interest using a 6% interest rate would probably be about $118, basing that on a whole six-month period, but those monies come in on a monthly basis. Given that cost and all the administrative costs that are involved as a lender and as an investor, that would be offset to the consumer. This bill should be defeated.

Jock Anderson, Montana League of Savings Institutions, opposes HB 157 for the same reasons as previously stated by **Mr. Cadby.** To summarize, at least within classes here there are no true winners in this type of legislation. The borrowers as a class will not be winners. The cost that may be saved by paying interest is going to be reallocated either to front end fees on loans or higher interest rates. Maybe within one class of borrowers there may be winners and losers. One can hypothesize that people with large houses who pay larger taxes are going to have more money in the reserve account than the rest of the accounts and therefore sacrifice more in the way of lost interest since escrow accounts basically cost the same to administer regardless of how large or small they may be. An argument can be made that large borrowers are paying more than small borrowers. To that extent the payment of interest would be required and costs allocated from the wealthier people to the lower income people. But across the board no net gains to borrowers are seen from this type of legislation. Obviously the lenders would be losers in Montana because they lose a small amount of their ability to compete with the 37

states that don't have this type of legislation. They have to make loans that will qualify to sell to the secondary market, and they are competing against those other states for those sales.

County government is going to be a big loser. People don't appreciate what a big role reserve accounts play in the collection of property tax. It is in that sense a mandatory budgetary process where everybody pays a certain amount each month to ensure that the money owed to the county is there when due. To the extent that legislation like this encourages lenders to get out of reserve accounts you expose the county to the loss of that kind of revenue. The business community generally is not going to benefit. This is not a life or death issue, but every little bit hurts. Anytime you raise the cost of lending, the cost of credit, then our State is damaged just by that small amount. No winners will be found in this legislation. You are going to find some losers, and notwithstanding the fact that it has a certain amount of merit on the surface, it should be examined closely and be given a do not pass recommendation.

Tom Hopgood, Montana Association of Realtors, said this has been adequately explained by the preceding opponents to HB 157. This would have an adverse effect on the availability of money for the purchase of housing in Montana. For that reason the Association opposes the bill as it has done in the past.

Roger Tippy, Independent Bankers Association of the State, said all his testimony has already been given. They oppose the bill.

Questions From Committee Members:

REP. BENEDICT asked if the interest we are talking about is the interest accrued on the reserve account during the year? **Mr. Cadby** answered it is the interest on the reserves that are accrued during the course of the year for payment of property taxes and insurance premiums. **REP. BENEDICT** asked if the interest calculated on those reserves is offset by the paperwork that has to be done every month to process the reserves. **Mr. Cadby** said the administrative costs that are incurred to handle these reserve accounts would have to be recovered through a fee or higher interest rates if interest were paid out on the reserves. **REP. BENEDICT** continued, if you didn't handle the reserves and everybody handled their own reserves, the counties would have to deal with hundreds and hundreds of individual tax payments. When you pay taxes, do you pay for a whole bunch of people at one time? **Mr. Cadby** said they pay with one check from a computer printout listing thousands of mortgages.

REP. RICE asked **Mr. Cadby** to bifurcate the two changes made in this bill. One is the additional over 110% deposit that must be used to decrease the fund; and secondly, return on investment must be returned to the depositor. Does the Bankers Association also object to having the reserve fund decreased until the figure is 110% or smaller? **Mr. Cadby** answered they are already doing

that today. Under current law you are not allowed to retain more than 110% of the anticipated outlay of money for taxes and insurance premiums, so any excess is refunded by secondary markets. That particular condition is not necessary.

REP. CROMLEY asked about the $400 figure, what was that for? **Mr. Varone** said he calculated the reserve requirement on over a $100,000 mortgage; he cut it in half and arrived at $400. If you were to figure interest on $50,000, the majority of the loans in the Western area are running around $60,000 right now, and used the $400 figure and gave it a whole 6-months interest at 6%, which is above average, and just multiplied that out as an interest figure, at the maximum you would get $118. If you had $400 in there on a constant six months which you won't because every time you make a payment a portion of that payment goes in the reserve account for taxes and insurance, accumulating a little each month. **REP. CROMLEY** asked if that is based on 6%. **Mr. Varone** said the average balance is about $400 at 6%. **REP. CROMLEY** asked if that wouldn't be $24. **Mr. Varone** said maybe for a month, but it is done on a six-month period. **REP. CROMLEY** asked if that would be a savings. **Mr. Varone** said that is correct.

Closing by Sponsor:

REP. STICKNEY said this issue has come up in other sessions. The bill in the last session was totally different from this one. It passed both houses and was finally killed in the Senate through the technical amendments which sent it back to committee where it languished in that particular committee of the Senate last year. It seems to have some merit. Consumers think it is only fair. In this day and age of computers and the kind of technical advances that all modern institutions are part of, she hardly thinks this will cause a hardship with paperwork. We are also talking about a large mass of reserve accounts on which interest is being earned. She reiterated that this is the borrowers' money which is held in reserve, and it seems to be only fair that the consumer should get the interest on that. She urged the Committee to take serious consideration of this and give it a Do Pass recommendation.

HEARING ON HOUSE BILL 241

REP. TIM WHALEN, HD 93, Billings, chief sponsor, carried this legislation in the 1987 and 1989 sessions. HB 241 is an act providing for the disclosure of loss and expense experience by property and casualty insurers; and provides a penalty. The genesis of this legislation came about between the 1985 and 1987 Legislatures. Beginning about 1985 the insurance industry engaged in a very heavy lobbying effort, not just in this state, but in states around the country to get states to change their civil justice system which provides remedy to people who feel that they are aggrieved, so that it was more difficult to go to court and remedies were more restrictive. Nothing came out of the 1985 session. There was stalemate. In 1985 a special session was

called to deal with the liability issues and there was stalemate until 4:00 o'clock in the morning on Easter Sunday, so since nothing could be accomplished in the Legislature, an interim committee was formed to study the issues until the 1987 Legislature for the purpose of restricting people's access to the court.

They came up with a series of bills that included proposed tort reform measures, but they also came up with a bill that required property and casualty insurers to report certain types of information on their loss experience in Montana, how much they were paying out, how much they were paying in administrative expense as far as adjusting claims, paying lawyers to defeat claims, advertising costs, etc. That was a recommended bill out of that interim committee. Most of the tort reform bills passed in some form, but the insurance reporting bill did not. He carried the bill in 1987 and again in 1989. In 1989 the bill was lost in the appropriations committee because there was probably a $10,000 appropriation on it to give the Insurance Commissioner money that was needed in order to store these information data files in her office. HB 241 requires the property and casualty insurers, which is fire and auto essentially, to report each year what they pay out in claims in Montana, what they reserve for future claims in Montana, and how much they pay out in administrative expenses.

The guts of the bill are on Page 3 which essentially tells what the bill applies to. The bottom of Page 3 and carrying to 4, and the top of Page 5 tells the type of information required to be reported. There will probably be some opposition by the insurance lobby. He has no proponents for the legislation. There is no natural constituency for this type of legislation. Most people don't understand insurance issues and don't follow them. This legislation is worthy of the Committee's attention.

Proponents' Testimony: None

Opponents' Testimony:

Gene Phillips, attorney, Kalispell, represented the Alliance of American Insurers and the **National Association of Independent Insurers.** They oppose HB 241. These two casualty and property companies write 26% of the insurance coverage in Montana for total premiums of $142 million dollars, so this bill is of significant importance to them. There should be a fiscal note attached to the bill. A fiscal note two years ago set forth the estimated cost of this particular legislation at an increase over current cost of about half a million dollars each year, so the cost of this is substantial. Perhaps that is one of the reasons why the appropriations committee turned down the bill. He said they oppose HB 241 because the insurance industry already does more data reporting to the State and to federal regulators than any other segment of the economy. He urged a Do Not Pass recommendation. **EXHIBIT 3**

Ms. Jacqueline Terrell, representing the **American Insurance Association** which is a national trade association, is a Helena attorney. **EXHIBIT 4** The Association represents about 30% of the market share in Montana. They oppose HB 241. There are some technical problems. The bill seeks information so that fair and appropriate insurance rates can be effected to protect Montana insurance consumers and make property and casualty insurance more available in Montana. This is inadequate and very discriminatory, not fair or appropriate. The growing proportion of commercial risks is not insured by the kind of carriers that are likely to be the target of this collection of legislation. It also requires the Commissioner only to store this information to make it available. **REP. WHALEN** represented in his opening comments this bill requires Montana information only. The bill requires information in Montana and from the United States. It is not clear from reviewing this version whether that information can be for the United States or broken down by state, or whether that is to be a collective figure. That information is already available from other documented creditable sources. Insurance companies want to respond positively to the call for data relevant to the tort system; the information is already available that would serve the needs of policymakers not as regulators. She asked a Do Not Pass recommendation.

Roger McGlenn, Executive Director of the Independent Insurance Agents Association of Montana, said they are not insurance companies. He does not represent insurance companies. He represents independent agents on main street Montana who in turn represent Montana insurance consumers needs. They stand in opposition because they were anticipating an adverse effect through cost and availability of insurance in Montana with the passage of HB 241. There is a need for a fiscal note. The Independent Agents of Montana have historically stood in support in the Legislature of increased staffing and funding of the insurance department. Currently, only 70-73% of every dollar that the industry agents and companies pay for insurance regulation in Montana is appropriated in the insurance department.

If restaffing and funding is necessary, data which is available in other areas should not be stored. Things like infield investigation to investigate complaints that are filed with the insurance department in Montana, should be funded before funds are spent for storing available data. It took them over two years after getting an agreement with the appropriations committee to get enough funding to get an actuary in the insurance department which they recently got in the spring of 1990. He asked the Committee to look at Section 33-16-202 which is recording and reporting the loss expense experience and powers the insurance commissioner has under that to respond to concerns raised by HB 241.

They feel the increased cost to gather and store this information would be incredibly onerous, and as is well known insurance companies don't pay these costs with insurance company money,

they pay it with money that insurance consumers pay to them. They also feel it would decrease availability of insurance in Montana. Montana has .3 of 1% marketing area which is a very small marketing area. The Independent Agents realize, recognize and document market withdrawals in good times and in bad in Montana. They feel this bill would encourage further withdrawals making it more difficult for them to provide a competitive full service to Montana insurance consumers. He urged the Committee to identify and evaluate the effect and the cost of this bill, and its effect on insurance affordability and availability in the state. He hoped the Committee agrees this should not pass.

Steve Browning appeared on behalf of the **State Farm Insurance Company** in opposition to HB 241. He had not had a chance to contact State Farm. In terms of the applicability of this bill, the sponsor indicated that it would cover auto, home and fire policies. They are all listed in the bill, but those seem to be the principal ones. Everyone has auto, home and fire coverage on their property. Likely when you got that coverage you talked to your local agent and more than a few companies offered that coverage, and as consumers you may have found there were different rates and terms for these policies. There is considerable competition on those three lines of insurance.

It is irrefutable when you read the bill that the insurers would pay extra money to provide this information which will cost them money apart from what it is going to cost the state to handle this in terms of the fiscal impact. Since it will cost the insurers more money, they will likely raise their premiums to pay for this. If they don't, they are going to be making less profit since they are for profit companies.

One of the premises of this bill is that the companies are making undue profits. Maybe you have someone who can tell you the value of stock for insurance companies that are stock companies, whether insurance companies are a great buy, are they soaring in value, are they reaping a great deal of profit from the sales they make? Another point, look at some of the data that is going to be required and ask if this is really going to be good data. Can you get this on a state basis? On Page 4, line 3 talks about net investment income in Montana. If this is a company that sells insurance beyond Montana as most hazards companies do, do they keep that on state lines? When they talk about costs, advertising, general office expenses, taxes, how valid would that be? Taxes information could be quite easily obtained on a state basis. How valuable would this information be even if you wanted to do this? They stand in opposition to HB 241.

John Cadby, appearing as a representative of **Bank Service, Inc.**, said this is an agency owned by the associations that serve the banks who purchase insurance and also sell insurance. They have about 50 small rural banks that have bank owned agencies. During the last hard market 1985-86 they came to us pleading for help because they could not find insurers. One agency was down to one

insurance company because he does not write enough volume. He only writes about $75,000 in premiums in a year. They are trying to cluster those agencies so they can get insurers to come into Montana, We don't need bills that help drive out insurers. One insurance company says if another hard insurance market cycle which is predicted by the end of this year occurs, they are going to set a minimum floor of one-half million dollars per year premiums, so a lot of little insurance agencies won't be able to find insurance companies to write for. They want to make it attractive for insurance companies to come into Montana, not drive them out.

Questions From Committee Members:

REP. LARSON asked why someone from the Insurance Commissioners' office wasn't here. **REP. WHALEN** explained because the chief legal counsel who appears and testifies at all these hearings is in Idaho visiting her mother who is ill. **REP. LARSON** asked if the information required by this bill is readily available. **REP. WHALEN** said no, it isn't available. The statutes referred to generally provide statistical data, it doesn't provide individual data. Testimony seemed to talk about information already being available, and that it is a terrible burden providing this information in an individualized and detailed manner. The trustworthiness of that type of testimony could be questioned.

REP. DOWELL asked about **Mr. Phillips** testimony of a half million dollars in costs. **REP. WHALEN** explained that when the bill was first introduced in 1987 it had provisions in it requiring the insurance commissioner not only to accept this information, but to also word it so it was easily understood by the public. They did put out a half million dollar fiscal note although it did not come out of the LFA's office. In 1987 there were some politics being played with fiscal notes. In 1987 it had about $5-10,000 impact so it went to appropriations and never came back. The money has all been taken out of HB 241. All the Insurance Commissioner has to do now is receive the information.

REP. DOWELL heard the information this bill would require referred to 'as of no use and useless data'. In what way would the people of Montana benefit from this information? **REP. WHALEN** answered he did a little bit of quick math based on the testimony. Gene Phillips indicated that his Alliance underwrites 26% of the property casualty insurance for a total of $142 million a year based on costing somewhere between one-half million and $600 million dollars a year being paid by Montanans to out-of-state property and casualty insurers. That is exclusive of all the other lines that are being written. If that amount of money is spent on insurance, and we talk about the same amount of Montana state taxes being a burden on businesses and individuals, it is appropriate to look at these types of expenditures which impose a similar burden on Montanans.

HB 241 requires data on how much the companies in Montana are

underwriting each year, how much their reserves to claims are which is important because claims don't always come in all at once. They come in over a period of time so reserves have to be able to cover claims at any time. It also requires information about how much is spent in Montana to adjust claims, how much is spent on advertising, is spent for lawyers to beat claims, that sort of information. The whole justification for this bill is that the insurance industry didn't come in here in 1985 and 1987 and said you ran us out of business in this state. There have been some of the same implied threats in testimony today. If you don't change the civil justice system and make it much more difficult for people to have access to their own courts in this state for the purpose of obtaining remedy against insurers or insurance companies, they will leave. Although that kind of statements were made, no information was furnished that would allow the legislators at that time to evaluate whether or not those were fair statements to be making. If they are going to ask for something substantive to be done to deny rights to Montana businesses and individuals, we have a right to information as a basis for insisting that we make those kinds of changes.

REP. BENEDICT said he was uncomfortable with the precedent that it sets in regard to business down the road, not just the insurance industry, but other retail businesses. Would you be willing to introduce legislation that would target the legal profession next to report their costs when setting fair and appropriate rates for services they offer? **REP. WHALEN** said the insurance industry is exempt from the antitrust laws of this country, so they can fix prices and pull up markets and essentially set oligapolistic and monopolistic type prices as opposed to competitive types of prices. They can do that legally as a result of the McCarran-Ferguson Act which exempts the insurance industry from regulation. The reason the insurance industry asked for that was because it was much easier for the insurance industry which has considerable power to come in and whipsaw those small states into refraining from regulating them by playing them against one another. The testimony here is that because Montana constitutes only .3 of 1% of the insurance market the implied threat is that if you do anything significant to regulate us, we will be gone. It is important to realize this is just a reporting bill, and won't do anything except evaluate the threats they continue to make. As far as the legal profession is concerned, that is something that is competitive. A person can shop around for insurance now.

REP. SONNY HANSON asked how insurance companies establish their rates. Are they predicated on a several state area, or the income and expenses of claims, or do they just do an individual state by state map. **Ms. Terrell** said in a short answer to a complex question, how insurance is rated depends on a particular line of insurance. Auto insurance is rated on a more specific locale. In some states and in some areas auto insurance premiums will vary from city to city or a small geographic region to another geographic region. Malpractice insurance rates are generally

determined on state by state basis. The St. Paul Companies which is the only for profit medical malpractice insurer who writes in Montana, sets their rates for Montana physicians on Montana data. Montana data is not sufficient in all instances to provide a stable basis for setting that rate, so it may be modified in part by national trends. There is a common myth problem impression that all malpractice rates are based on states like California and Florida where malpractice insurance premiums are sky high. That is not what is happening. The St. Paul looks at what is happening generally in the nation and then looks at Montana specifically and sets its rates for Montana physicians based on that rate. The St. Paul bases its national rates on the ranking of 40 companies. They only write in 42 states, so that makes that premium rank even lower. They do not write insurance in all 50 states, so it is 40 out of 42. Their rating of Montana ranks 46 out of 50.

REP. SONNY HANSON asked how this would be applied for a savings and loan that has a joint insurance association located in another state and the savings and loan actually handles the products within the state. It is not an individual corporation, it is handled as sort of a brokerage operation, but through the banking institutions. They then use it for automobiles or anything else of this nature. Have you specifically addressed this? **REP. WHALEN** said that is a new issue this year. He isn't familiar with the differences and distinctions between a joint stock company and associations, etc. There are three or four different ways in which an insurance company can form itself. There may be a distinction between lending institutions compared to insurance companies which are regulated by the insurance commissioner's office, or they may just be associated with one another in such a way that those regulations may not be applicable. This bill would apply to property and casualty insurance carriers that actually underwrite risks. He doesn't know if these lenders are actually underwriting risks. Some barriers were put in place in the 30's trying to insulate lending institutions from getting involved with some of these other types of activities because of the situation created with the stock crash of 1929.

REP. CROMLEY said you mentioned there is no requirement other than just the reporting. There is no indication the auditor's office would be evaluating the information for public service groups. **REP. WHALEN** said Section 3 asks only that the commissioner is to store the reports. **REP. CROMLEY** said the Montana Trial Lawyers had been mentioned, are other groups to receive this information? **REP. WHALEN** said the Trial Lawyers are the ones he is aware of. There is a national organization called National Organization of Insurance Consumers, the Ralph Nader group, who might be interested in the reports.

REP. CROMLEY said market withdrawal was mentioned. Do you have any specifics on this? **Mr. McGlenn** defined 'withdrawal'. It does not mean removing your license from Montana; in other words,

totally leaving and having the insurance department cancel your license to operate in the state. Market withdrawal is when an insurance agent no longer makes a product available for a specific line of insurance for all lines represented. Many insurance companies represent or sell insurance to national accounts like K-Mart, Circle K, etc., so they must be licensed in every state where the insured does business. Over the last three years there has been significant withdrawal, and it may not be unique to Montana; for example, Aetna Life and Casualty, the largest independent insurer in the United States, no longer makes personal liability available in Montana. Transamerica Insurance Company has withdrawn significantly from the marketplace, United Pacific Reliance has withdrawn from the marketplace. Home Insurance Company has taken their products off the marketplace. His members don't represent these companies any more. There are others also, and they have withdrawn from other states, too. They take perception of the marketplace and that greatly assists them in determining whether to make their products available in a certain area.

This bill applies only to admitted carriers, which excludes a significant number of other insurance companies. Admitted carriers are those insurance companies who are licensed to do business in Montana who participate in a guarantee fund. A guarantee fund is when companies combine together. The intent of the companies in the event of insolvency of one of the admitted carriers is they all chip in to pay all claims and expenses for the insolvent companies. There are non admitted carriers which are called surplus lines companies who are not licensed as admitted carriers and don't participate in the admitted carriers fund. There is a separate section of law in regards to those. Risk groups, purchasing groups, and things **REP. HANSON** was speaking to would definitely be questionable for they don't participate in the guarantee fund, and don't fall under the definition of admitted carrier.

REP. SCOTT asked if there is similar legislation in other states. Would this legislation have any effect on this withdrawal in states with similar legislation? **REP. WHALEN** was not familiar with other states. In Montana a very similar statute was adopted in the late 70s, 33-23-311, which applies to professional liability insurance, and it requires virtually the same type of information from malpractice insurers. There has always been a limited number of insurers in that market. Two years ago there were two companies underwriting in that area. A piece of legislation was passed requiring regional rate making in which there was all kinds of claims that would drive the insurers out of that market, but one more insurance company has been admitted since then.

REP. ELLIS said you spoke of having a collection of a mountain of data. Is most of this data required by this bill now kept on a state by state basis, and is it currently available? **Ms. Terrell** said most of the information that HB 241 requires is available in

other places. It may not be in precisely the same form that this bill details, but the information is available. Additionally, there is a model bill which is coming out of the NAIC, the National Association of Insurance Commissioners, which provides for a more uniform method of collecting this data. One of their primary objections to HB 241 is not that the data is being collected, but the fact that it is being done piecemeal, state by state, rather than in some uniform method so that it can be analyzed effectively and completely. This calls for information that does not produce any meaningful conclusions.

Closing by Sponsor:

REP. WHALEN closed by saying the main thing he wanted to leave with the Committee is that this bill came out of the Interim Committee in 1986 to deal with liability issues. This is something that was studied by that Committee and was a bill that was proposed to be drafted for this Legislature. It is not anything thrown together on his own. With the exception of the modification removing all the money out of it. Secondly, there is a similar statutory act on the question of professional liability. He didn't think it would put any great burden on these carriers to provide this information. Oftentimes they would have you believe compiling all this information is done by hand. All of you know that once you have the data base, you have the problem solved. You can call it up with the punch of a button.

HEARING ON HOUSE BILL 209

Presentation and Opening Statement by Sponsor:

REP. NORM WALLIN, HD 78, Gallatin County, sponsor, has spent most of his life in the automobile business. This bill ties in with his experience in that business. HB 209 is an act providing that a security interest in a motor vehicle is perfected on the date the lien notice is delivered to the county treasurer, and amends Section 61-3-103,MCA. Under present law, after the application for title papers are made up for the sale and purchase of an automobile to transfer the application for the new title, and the lien if there is one, is attached to it, it should be at the county treasurer's office within four days. The buyer has an additional twenty days time in which to go to the courthouse to sign the documents necessary to obtain his title and license plates and pay for the transfer, thereby perfecting the lien. HB 209 addresses what has and can happen adversely between the four days when the papers are in the courthouse and the twenty days in which the buyer has to perfect that lien and transfer his title. This has been running along smoothly. The federal bankruptcy law that many people have become familiar with requires the lien to be perfected in ten days. There is a lag in time between the four days and the twenty days, and in many cases the new owner doesn't sign the papers within the twenty days. The treasurer doesn't return those papers to the dealer until at least thirty days have

passed. A lot of things can happen to that lender's equity or interest in the vehicle he is financing. The purpose for this bill is to tighten up that period and say at the time the dealer or the seller takes the papers to the county treasurer's office, if there is a lien, at that time the lien is perfected as against any other claims that might come up against that automobile.

Proponents' Testimony:

John Cadby, Montana Bankers Association, explained HB 209 is the result of the bankruptcy court ruling in Butte last year and others since. The federal law says you have to perfect a lien within ten days of receipt of the documents. Now it takes too long to perfect a lien on a motor vehicle. **EXHIBIT 6** is the actual summary of a case wherein the credit union had a $13,000 loan against a 1989 Mazda. The application for title and lien documents were delivered to the county on March 1, title wasn't issued until August 31, the bankruptcy court ruled the car now belonged to the trustee, so the credit union took a $13,000 loss through no fault of its own; simply due to paperwork. Under HB 209 the lien notice would be taken to the county treasurer who gives the lender a receipt; the lien is perfected at that point in time. It should solve most of the problems or prevent these problems from arising again. He gave the Committee copies of a court ruling **EXHIBIT 7** he made reference to in his testimony above and in **EXHIBIT 6.**

Bob Pyfer, Vice President of the Montana Credit Unions League, said this bill has been accurately presented and they are in support of it. He referred to bankruptcy theories. One is a hypothetical lien creditor theory in the bankruptcy law, and there is also a preference theory. Suffice it to say that a lender who does everything right and in good faith and with all due diligence can lose their lien in a bankruptcy situation. The other important point here is that this does not in any way affect the debtor. The debtor does not benefit from the bill, nor does the debtor receive any detriment from this bill. The ones who gain a windfall because of this quirk of the juxtaposition between our bankruptcy laws and our motor vehicle lien laws are the bankruptcy trustees and the unsecured creditors because when the liens are voided by the trustees the asset acquired simply goes into the pool of assets to be distributed among all unsecured creditors. Trustees have a distinct incentive to avoid liens in any way they can because they are paid a percentage of the amount they can distribute to unsecured creditors. This is not a creditor/debtor bill per se, it is simply a way of avoiding a rather grievous injustice in the bankruptcy laws as between the various creditors.

Daryll (Bud) Schoen, Registrar of Motor Vehicles in Deer Lodge in the Department of Justice Motor Vehicle Division, recognizing the problem that Montana lenders have in perfecting liens on motor vehicles, supports this bill. He will answer questions if needed.

Steve Turkiewicz, Executive Vice President of Montana Auto Dealers Association, a trade association representing 150 Montana new car and truck dealers, supports this bill. You heard the bankruptcy ruling. When someone buys a car and borrows money the lien against that vehicle is not perfected until the title is issued, according to Montana law. If everything works right, it takes thirty days to get a title in Montana. The dealer has four days to get the paperwork to the courthouse to record the documents; the buyer of the vehicle has twenty days to get in to the courthouse and sign those papers which are then transmitted to Deer Lodge. Deer Lodge works its magic on them and out comes a title. Montana law says the lien is not perfected until the title is issued, so that happens in a minimum of thirty days. The federal bankruptcy law says you don't have security interests in that vehicle unless you perfect a lien in ten days. That is where the problem is. Besides the bankruptcy concern there is also enforcement of recourse by our lenders who deal with banks, savings and loans, credit unions, captive credit companies, General Motors Acceptance Corporation. All those require the dealer to get that lien perfected, and the recourse against the dealer is there until such time as that lien is perfected, and it is very disconcerting to be a car dealer who sold a car thirty-forty days ago and get a letter from General Motors Acceptance Corporation or First Bank saying the lienings or titles have not been issued on the fifteen cars you sold a month ago, please send us a check for $85,000! It is the responsibility of the dealers to get that work done, and it is the responsibility of the lenders to get their work done. There is a mismatch between the federal bankruptcy law and Montana law. HB 209 asks this to be changed. When the dealers have met their obligations and the lien is perfected, they maintain their security interests in the vehicle.

Michael Varone, Vice President of the Norwest Bank and past Chairman of the Montana Bankers Association Retail Committee, supports this bill and will answer questions regarding titles.

Opponents' Testimony: None

Questions From Committee Members: None

Closing by Sponsor:

REP. WALLIN closed. There is no cost to anyone involved. The proper paperwork establishes a date the lien is perfected and the title can be obtained.

EXECUTIVE ACTION ON HB 209

Motion/Vote: **REP. CROMLEY moved HB 209 DO PASS. Motion carried unanimously by voice vote.**

ADJOURNMENT

Adjournment: 10:45 a.m.

Bob Bachini

REP. BOB BACHINI, Chairman

Jo Lahti

JO LAHTI, Secretary

BB/jl

HOUSE OF REPRESENTATIVES

BUSINESS AND ECONOMIC DEVELOPMENT COMMITTEE

ROLL CALL DATE Jan. 21, 1991

NAME	PRESENT	ABSENT	EXCUSED
REP. JOE BARNETT	✓		
REP. STEVE BENEDICT	✓		
REP. BRENT CROMLEY	✓		
REP. TIM DOWELL	✓		
REP. ALVIN ELLIS, JR.	✓		
REP. STELLA JEAN HANSEN	✓		
REP. H.S."SONNY" HANSON	✓		
REP. TOM KILPATRICK	✓		
REP. DICK KNOX	✓		
REP. DON LARSON	✓		
REP. SCOTT MCCULLOCH	✓		
REP. BOB PAVLOVICH	✓		
REP. JOHN SCOTT	✓		
REP. DON STEPPLER	✓		
REP. ROLPH TUNBY	✓		
REP. NORM WALLIN	✓		
REP. SHEILA RICE, VICE-CHAIR	✓		
REP. BOB BACHINI, CHAIRMAN	✓		

1-23-91
HB 157

HOUSE STANDING COMMITTEE REPORT

January 23, 1991

Mr. Speaker: We, the committee on Business and Economic Development report that House Bill 157 (first reading copy -- white) do not pass .

Signed: _____
Bob Bachini, Chairman

1-21-91
T.O.B

HOUSE STANDING COMMITTEE REPORT

January 21, 1991

Mr. Speaker: We, the committee on Business and Economic Development report that House Bill 209 (first reading copy -- white) do pass .

Signed: _____
Bob Bachini, Chairman

EXHIBIT 1 Exhibit #1
DATE 1-21-91
HB 157

Testimony of Tom W. Clarke HB 157

Ladies and Gentlemen of the Committee, I appreciate the opportunity to urge your passage of HB 157 amending Title 71 of Montana Code as it regards tax and insurance reserve accounts for mortgage loans.

The world of mortgage loans has changed in recent years. When I bought my first home, 22 years ago, I obtained the mortgage loan through a local Miles City Bank. And they even let me assume the prior owners loan. In more recent years, a loan assumption is pretty rare, and on a new loan, the local banker might close the transaction, but most often the loan is then sold to mortgage banking firms out of Montana. My current home was purchased in 1986, and in the 4+ years that I have owned it, the mortgage has been sold 3 different times, which means I have made out my monthly payment check to 4 different lenders, including one in Illinois, one in New York state, and most recently a firm in San Diego.

Why should that make a difference? After all, the terms of the mortgage are the same, thus regardless of who holds the mortgage, my monthly payment is the same, right? No, that isn't right, because while the loan principal and interest don't change on a fixed rate mortgage, they are just 2 of the elements that make up the monthly payment amount. The other 2 elements of the monthly payment are the allocations for the tax and insurance reserve account. This is the account of borrowers money held on reserve for payment of the property taxes and hazard insurance. This reserve of borrowers money is held by the mortgage banking firm, and by Section 71-1-113 is restricted to a maximum of 110% of the amount needed to pay these obligations, but the lender can reformulate a mortgage payment amount to achieve the 110% and in so doing can be easily holding as much as $2,000, or more, of the borrowers funds, thus these funds amount to a loan from the borrower back to the lender, however the borrower does not get any return on the investment.

So quite simply, HB 157 recognizes that the amounts held by the lender as a tax and insurance reserve are monies that belong to the borrower, and obligates the lender to credit any investment return they get from these funds to the tax and insurance reserve account of the borrower.

I am a businessman, and an axiom of the business world is to treat the customer fairly. I would suggest that for the lender to earn interest from the borrowers funds is not fair. I'm sure you will agree with me that the credit of interest from this money must properly be made to the account of the consumer to whom the money belongs, and I thank you for your positive consideration of this bill.

Exhibit 2

EXHIBIT 2
DATE 1-21-91
HB 157

HB 157

INTEREST ON RESERVES

by MONTANA BANKERS ASSOCIATION

Q. When and why were mortgage reserves created?
A. During Depression to control tax delinquencies and prevent foreclosures. Tax and insurance reserves required by FHA (since 1934), VA, State Board of Investments and Housing.

Q. Where are most mortgages held?
A. By the secondary market. Most are with out-of-state mortgage companies. The State Board of Housing has 11,000 mortgages and the State Board of Investments has 3,000 mortgages.

Q. What could happen to secondary market with HB 157?
A. Out-of-state sources of investment capital would certainly become more costly as mortgages in the 37 states protected by non-interest bearing reserves become more attractive. Supply of mortgage money goes down and interest rates or price of the money goes up.

In-state, e.g. Board of Housing would have to raise interest rates to low income borrowers.

Q. Who benefits from these reserves?
A. Lenders and mortgage companies are assured taxes will be paid thereby protecting their loans. Borrowers are assured taxes and insurance will be paid even in hard times. Counties are assured taxes will be paid on time in lump sum for millions of individual homeowners and checks will not bounce.

Q. Why not let each homeowner pay taxes when due?
A. Borrowers typically DO NOT save and would have to borrow at 12%+ interest to pay taxes. Lenders and mortgage companies would have to research county records to make sure taxes were paid to protect liens. Counties would have to raise taxes to cover additional staff and increased administrative costs.

Q. Do lenders or mortgagees make money off reserves?
A A 1973 study by the general accounting office (GAO) showed a "net loss per unit under a fully allocated cost analysis." GAO study said federal government could and should charge for this service. Many secondary markets contract with tax service companies to handle tax payments. Some pre-pay a full year's taxes in November so there is little left in reserves at the end of December.

Q. What do the homeowners want?
A. A 1973 study by VA of 207,565 homeowners showed 83.6% were satisfied with non interest bearing reserve accounts vis a vis direct payments to counties. Survey showed particular benefit for homeowners with limited financial resources.

Q. What happens when borrowers are delinquent or reserve funds inadequate?
A Deficiencies with borrowers occur frequently so lenders usually advance funds without charge to cover the taxes.

Q. What administration is required for mortgages?
A (1) Collect taxes and insurance 12 times per year and segregate and account for these items.

(2) Obtain tax bills and other special assessments from counties and insurance premium bills from agents or homeowners in a timely fashion, which often requires follow-up.

(3) Pay tax bills to 56 counties and insurance premiums to hundreds of different companies as required. Taxes are usually paid semi-annually but some are now paying annually.

(4) Monitor the reserves to determine if monthly payments are sufficient. Real estate taxes and insurance premiums may increase or decrease and new assessments added.

(5) If a borrower's obligations change - or are expected to change - monthly payments raised or lowered accordingly and borrowers must be notified. Montana law now restricts reserves to 110% of actual taxes and premiums due.

(6) Calculate whether a deficit exists and, if so, arrange for the borrower to make a lump sum payment or increase monthly payments. If excess, refund is made or monthly payments are reduced.

(7) Answer all inquires regarding the mortgage in general and particularly increases in the monthly payment.

(8) Distribute to the borrower an annual statement of taxes and insurance premiums paid for income tax reporting purposes.

Q. What will lenders and mortgagees do if HB 157 passes?
A Refuse to handle reserves and/or charge higher interest rates on new mortgages and/or charge higher fees on new mortgages and/or charge fees for shortages in funds. Secondary market now charges $60 for "tax service" fee. Most banks now charge fees on savings account under $300, or about the same as reserve on mortgages, because administrative costs are higher than interest earned on such small savings.

CONCLUSION:

This bill would cause repercussions to thousands of borrowers, past, present and future. Ramifications of this bill should be given careful study before action is taken. An interim study would be in order.

Ex. 2A
1-21-91

WITNESS STATEMENT

NAME Michael P. Warnke BILL NO. 157

ADDRESS 646 Tamarack

WHOM DO YOU REPRESENT? MBA Retail + R.E. Comm. + Norwest BK Helena

SUPPORT _____ OPPOSE ✓ AMEND _____

COMMENTS:

I do not believe this to be in the best interest of the consumer. If 157 is passed, the cost will increase expense to consumer

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Form CS-34
Rev. 1985

EXHIBIT 3
DATE 1-21-91
HB 241

Exhibit 3

STATEMENT OF
ALLIANCE OF AMERICAN INSURERS
NATIONAL ASSOCIATION OF INDEPENDENT INSURERS
BY
GENE PHILLIPS

Mr. Chairman and members of the committee:

My name is Gene Phillips. I am a lobbyist for the Alliance of American Insurers and the National Association of Independent Insurers.

We, the Alliance of American Insurers and the National Association of Independent Insurers, oppose House Bill 241.

The insurance industry already provides more data than any other comparable segment of the American economy. Insurers long have provided state legislators, regulators, and statistical agents with extensive data detailing their claims experience, financial condition, and rating calculations. In addition to state-specific information, insurers provide data detailing their nationwide operations to federal agencies such as the Internal Revenue Service (IRS) and the Securities and Exchange Commission (SEC), as well as to the National Association of Insurance Commissioners (NAIC). While much of this information has been available for many years, new reporting requirements have been added recently to provide more detailed information for specific lines of business (such as medical malpractice and products liability).

The NAIC has adopted a Model Regulation to Require Reporting of Financial and Statistical Data by Property and Casualty Insurance Companies. It was developed by the NAIC after a year of deliberation to promote uniform state data collection. The NAIC also has adopted a biennial closed claim survey for commercial general liability coverages, which was conducted for the first time in 1990. The

survey included 44 thoroughly researched questions relating to bodily injury and should be sufficient to satisfy any closed claim data requests for general liability coverages that may emanate from this state. Information also is available through the Insurance Services Office (IS)0. It is not necessary to restore information already available through other sources.

Further, we urge you to carefully consider the cost of this legislation. There are approximately 640 companies licensed to sell property and casualty insurance in Montana. This bill seeks specific information 10 lines of liability insurance and five sub-categories of automobile insurance. While Representative Whalen's bill calls for the Insurance Commissioner to store this information and make it available to interested persons and legislative committees on request, any retrieval of this information necessarily contemplates processing and indexing it in some manner. The quantity of information requested alone is staggering. The cost of such storage and processing will be significant.

This legislature has wisely rejected vitually identical bills in 1987 and 1989. We urge you to again reject this proposal and make use instead of the wealth of material available to you before enacting new data collection mechanisms that contemplate only the storage of additional material. If you believe additional data collection is imperative, we urge you to consider the NAIC Model Act.

Submitted to House Business and Economic Development Committee for hearing on House Bill 241, January 21, 1991, 9:00 a.m.

Respectfully submitted,

Gene Phillips

EXHIBIT 4
DATE 1-21-91
HB 241

Exhibit 4

STATEMENT OF
AMERICAN INSURANCE ASSOCIATION
BY
JACQUELINE N. TERRELL
RE: HB 241

Mr. Chairman and members of the committee:

My name is Jacqueline N. Terrell. I am a lawyer from Helena and a lobbyist for the American Insurance Association. The American Insurance Association is a national trade association that promotes the economic, legislative, and public standing of its some 240-member property-casualty insurance companies. The Association represents its participating companies before federal and state legislatures on matters of industry concern.

We, the American Insurance Association, oppose House Bill 241.

The insurance industry recognizes that credible, useful data is important for understanding the changes in the availability and cost of insurance. Absent meaningful input and anlysis, even the most detailed data reporting legislation may fail to result in any useful conclusions. Rather than enacting new and burdensome data reporting requirements in 1991, we hope Montana will utilize the wealth of data already available, as well as new data collected through voluntary insurance undertakings.

For the period 1986--1989, data collection initiatives were advanced and sometimes enacted in conjunction with substantive civil justice reform. On the state level, more than 40 states enacted significant data collection requirements. No two state requirements are identical. Some, such as Florida's, require case-specific information that can be obtained only from an examination of closed-claim files. Others, such as Louisiana's, require detailed expense and profitability statements for sublevel classifications of insurance

(such as athletic associations).

Any new insurance data collection requirement is unlikely to greatly enhance an understanding of the liability system, for reasons that include the following:

(1) The broad collection of past claim data is virtually useless as a way of predicting future claims costs. Such raw data --absent expertly-developed trend factors and underwriting judgments--are not useful in predicting future prices, since individual company expense factors and market variables are interposed between cost projections and pricing decisions.

(2) This particular bill makes no attempt to limit data requested to troubled lines of insurance or to link the losses paid to the premiums written or earned.

(3) A growing proportion of commercial risks are not insured by the kinds of carriers that are likely to be the target of collection legislation. Self-insurers, risk retention groups, and surplus lines companies are not currently represented in any data pool, yet are critical for understanding the total picture.

Further, responding to detailed data requests is likely to be enormously costly, in terms of both expenditures and person hours. An onerous claims data requirement could virtually paralyze an insurer's claims operations, potentially delaying indemnification of needy claims. And at some point these requirements will override the benefits of doing business in a state that represnets only 3/10 of 1% of the market share. The costs of reporting will certainly be relected in future marketing decisions.

EXHIBIT 4
DATE 1-21-91
HB 241

While the stated purpose of Representative Whalen's bill is "to protect Montana insurance consumers, while making property and casualty insurance more available in this state," it fails on both counts. The bill ignores information already to Montana consumers and legislators through other national data collection sources far better suited to efficiently store and analyze the data this bill seeks. Further it ignores the information already collected by the Commissioner of Insurance under Montana law. A careful review of 33-16-105, -202, -203, -204, and 33-23-311, MCA, for example, clearly demonstrate that sufficient data already is available through the Montana Insurance Commissioner to achieve the stated objectives of this bill. To the extent that further information would be useful, that information is already being compiled by various national organizations.

Insurers wish to respond positively to the call for data relevant to the tort system. Yet, uncoordinated insurer data collection requirements may be confusing, counter-productive, and costly. Rather than adding to the array of requirements to which the industry is now responding, legislators should review the wealth of old and new data relevant to the issues now under discussion. These data would serve the needs of policymakers.

Submitted to House Business and Economic Development Committee for hearing on House Bill 241, January 21, 1991, 9:00 a.m.

Respectfully submitted,

Jacqueline N. Terrell

Ex. 5
1-21-91
HB 241

WITNESS STATEMENT

NAME Steve Browning BILL NO. HB241

ADDRESS Box 1697 Helena MT 59624 DATE 1/21/91

WHOM DO YOU REPRESENT? State Farm Insurance

SUPPORT _____ OPPOSE ✓ AMEND _____

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

This bill would require extraordinarily burdensome, expensive and useless reporting.

EXHIBIT 6
DATE 1-21-91
HB 209

Exhibit 6
by John Cadby
Mt Bankers Assn.

HOUSE BILL 209

Mr. Chairman and Members of the Committee:

HB 209 changes the time and place of perfecting a lien on a motor vehicle from the registrar's office in Deer Lodge to the county. The purpose is to speed up perfection of liens so as to comply with the federal bankruptcy law which only allows 10 days for perfection.

Last year the federal bankruptcy court in Montana ruled against a credit union on a $13,480 motor vehicle loan only because the lien had not been perfected in time. In this case, on February 13, 1989 the debtors purchased a 1989 Mazda. The application for title and lien documents were delivered to the county on March 1 as required my Montana law. The registrar at Deer Lodge did not receive the documents until June 5. The actual title and date the lien was perfected was August 4. The debtor filed a bankruptcy petition on August 31.

The bankruptcy judge ruled that the credit union's lien on the Mazda was void and gave the vehicle to the trustee to sell. The credit union lost $13,480 through no fault of its own.

This past year, representatives of Montana Bankers Association, Montana Auto Dealerse Association, and Montana Credit Union Network met with the Attorney General's Motor Vehicle Division and Registrar of Motor Vehicles on numerous occasions to come up with a solution. HB 209 is a simple solution which will protect all lien holders' rights.

Admittedly this is not the total solution because Montana law does allow the purchasers of motor vehicles 20 days to register at the county. On the other hand most motor vehicle sales are handled by dealers and they customarily get the necessary paperwork to the county courthouse within a few days after the purchase. This law will encourage both dealers and lenders to work together to see that the paperwork is expedited and in the hands of the county as soon as possible after the sale of the motor vehicle.

We urge you to pass HB 209.

Exhibit 7

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MONTANA

In re

JAMES R. STEERS, and
JOY L. STEERS,

Debtors,

Case No. 89-41193-007

EXHIBIT 7
DATE 1-21-91
HB 209

GARY S. DESCHENES,
Trustee,

Plaintiff,

-vs-

Adversary Proceeding
No. 289/0119

FIRST LIBERTY FEDERAL
CREDIT UNION,

Defendant.

ORDER

At Butte in said District this 19th day of April, 1990.

On November 7, 1989, the Chapter 7 Trustee/Plaintiff filed a Complaint to Avoid Preferential Transfer in Personal Property and for Turnover of Vehicle. The Defendant filed an Answer on January 2, 1990, admitting most of the material allegations, yet asserting that the Trustee/Plaintiff should take nothing through the Complaint. The parties then filed a Stipulation whereby this matter would be submitted on Stipulated Facts and simultaneous Briefs. This Court approved the Stipulation and the Stipulated Facts and Briefs were filed on or before February 7, 1990. The Complaint is based on § 547 of the Code. Subsequent to the filing of the parties' Briefs, Amicus Curiae Briefs were filed by First Bank Montana, N. A. (First Bank) and

Ross Richardson, panel Trustee. First Bank's Brief supports the Defendant's position and Richardson's Brief supports the Trustee/Plaintiff's position. Upon review of the record, this Court deems this case ripe for decision.

The Stipulated Facts of the Parties are as follows: On February 13, 1989, the Debtors executed and delivered to Defendant a Security Agreement granting a security interest in a 1989 Mazda. The security interest was granted as security for a loan extended to the Debtors in the amount of $13,480.00 to purchase the vehicle. The appropriate title and lien documents were delivered to the Cascade County Treasurer on March 1, 1989 as required by statute. Despite the fact that the registration documents were deposited with Cascade County on March 1, 1989, the State Department of Motor Vehicles (Department) did not receive the registration documents until June 5, 1989. The actual title for the vehicle, noting the Defendant's lien, was subsequently issued by the Department on August 4, 1989. The parties are unaware of any facts indicating that the Defendant caused any of the administrative delay from the registration date of March 1, 1989, to the issuance of title on August 4, 1989. While the parties stipulated Debtors filed a Bankruptcy Petition for relief under Chapter 7 on September 12, 1989, the actual petition date is August 31, 1989.

The Trustee/Plaintiff asserts that the Defendant's lien was not perfected until August 4, 1989, and therefore, the lien is subject to the Trustee's avoidance powers under § 547(b). The Defendant and Amicus First Bank argue that § 547(c) overcomes the

Plaintiff's contentions and case law, together with § 105 of the Code, buttress their positions.

EXHIBIT 7
DATE 1-21-91
HB 209

Section 547(b) of the Code provides:

"(b) Except as provided in subsection (c) of this section, the trustee may avoid any transfer of an interest of the debtor in property--

(1) to or for the benefit of a creditor;
(2) for or on account of an antecedent debt owed by the debtor before such transfer was made;
(3) made while the debtor was insolvent;
(4) made--

(A) on or within 90 days before the date of the filing of the petition; or
(B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and

(5) that enables such creditor to receive more than such creditor would receive if--

(A) the case were a case under chapter 7 of this title;
(B) the transfer had not been made; and
(C) such creditor received payment of such debt to the extent provided by the provisions of this title."

The Stipulated Facts satisfy each of the elements of § 547(b) since under sections 61-3-201(2) and 61-3-103(5), Mont. Code Ann. (1989) perfection of the security interest occurred on August 4, 1989, within 90 days of the filing of the Debtors' Petition. The pertinent Montana Code sections provide for the transfer of title documents to be sent to the county treasurer within 20 days of sale and the transfer documents together with security agreements are then forwarded by the treasurer to the State Motor Vehicles

Department, which issues the new title. Pertinent to this case is 61-3-103(5), which provides:

> "The filing of a security interest or other lien, as herein provided, perfects a security interest which has attached at the time the certificate of ownership noting such interest. Issuance of a certificate of ownership constitutes constructive notice to subsequent purchasers or encumbrances, from the time of filing, of the existence of the security interest."

Under such statutory scheme, the lien is not perfected until endorsed on the title by the Department of Motor Vehicles. In re Davis, 1 Mont. B.R. 79 (1985).

Therefore, the issue before the Court is whether § 547(c)(1) or (c)(3) except the Trustee's § 547 avoidance powers in this case. Section 547(c)(1) and (3) provide:

> "(c) The trustee may not avoid under this section a transfer --
>
> (1) to the extent that such transfer was
>
> (A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and
>
> (B) in fact a substantially contemporaneous exchange;
>
> * * * *
>
> (3) that creates a security interest in property acquired by the debtor --
>
> (A) to the extent such security interest secures new value that was--
>
> (i) given at or after the signing of a security agreement that contains a description of such property as collateral;

(ii) given by or on behalf of the secured party under such agreement;

(iii) given to enable the debtor to acquire such property;

(iv) in fact used by the debtor to acquire such property; and

(B) that is perfected on or before 10 days after the debtor receives possession of such property;"

In Matter of Vance, 721 F.2d 259, 261-62 (9th Cir. 1983), the Ninth Circuit Court of Appeals aptly addressed the interaction between § 547(c)(1) and (3), stating:

"There is no indication in the legislative history that Congress intended section 547(c)(1) to be a general exception covering a variety of transactions. Rather, the legislative history indicates that Congress designed section 547(c)(1) to exclude check or other cash equivalent transactions from the trustee's avoiding powers. Thus, applying section 547(c)(1) to purchase money security interests would expand the scope of the exception far beyond the contemplation of Congress.

Congress specifically provided preference protection for purchase money security interests in section 547(c)(3). That section provides that the security interest must be perfected before 10 days after such security interest attaches. This exception does not protect the Bank's security interest in Vance's trailer because the security interest was perfected fourteen days after the security interest attached.

Even if section 547(c)(1) were to be construed as a general exception for those situations not specifically contemplated by the authors of the Bankruptcy Code, the existence of section 547(c)(3), which

specifically applies to purchase money security transactions, would preclude the application of the general exception to transactions specifically provided for in subsection (c)(3). As the bankruptcy court stated in In re Enlow:

> ' The explicit reference by Congress in Section 547(c)(3) to enabling loans lends further support to the conclusion that Section 547(c)(1) is not applicable to the instant transaction. Through its enactment of Section 547(c)(3) Congress intended to make that section -- not Section 547(c)(1) --applicable to an enabling loan situation.'

20 B.R. at 483. The bankruptcy court in another case applied the traditional maxim 'expressio unius est exclusio alterius' and concluded:

> '11 U.S.C. § 547(c)(3) provides a mechanism by which liens to secure enabling loans might be excepted from avoidance. In so doing it negates the availability of other means of exception. 11 U.S.C. § 547(c)(1) is general; 11 U.S.C. § 547(c)(3) is specific; it refers to "a security interest" such as in this adversary proceeding.'

In re Davis, 22 B.R. at 649. This application of statutory construction techniques is persuasive that Valley Bank should not be able to take advantage of section 547(c)(1).

The Bank contends, however, that subsections (c)(1) and (c)(3) are not mutually exclusive. The Bank refers to the following statement from the legislative history:

> 'Subsection (c) contains exceptions to the trustee's avoiding power. If a creditor can qualify under any one of the exceptions, then he is protected to that extent. If he can qualify under several, he is protected by each to the extent he can qualify under each.'

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H.R.Rep. No. 95-595, 95th Cong., 1st Sess., reprinted in 1978 U.S. Code Cong. & Ad. News at 6329. The Bank argues that this legislative history indicates that Congress did not intend that section 547(c)(3) be the exclusive exception for purchase money security transactions.

The Bank places too much reliance on this legislative history. As one bankruptcy court commented:

> 'The legislative history does not reveal which sections might provide multiple protection or why a transferee would desire to qualify under more than one section because satisfaction of any section excepts the entire transfer from avoidance. Assuming some purpose for multiple protection, however, the legislative history cannot be interpreted, as FMCC argues, to suggest that all exception in § 547(c) are interchangeable and overlap. Each section has distinct prerequisites and to the extent one of those elements is absent, the section is inapplicable. Similarly, those sections that are inconsistent with each other will not be applied to one another.'

In re Murray, 27 B.R. at 449 n. 7. The legislative history does not explicitly state that subsections (c)(1) and (c)(3) overlap. The legislative history does explicitly state that Congress intended section 547(c)(1) to except certain transactions involving payment by check and that section 547(c)(3) excepts certain transactions involving enabling loans. These are distinct types of transactions. The cited legislative history is not persuasive for the proposition that section 547(c)(1) and section 547(c)(3) overlap in their coverage of transactions.

Our conclusion is further supported by the fact that applying section 547(c)(1) to enabling loan transactions would make section 547(c)(3) superfluous. See in re Christian,

> 8 B.R. at 819. If the contemporaneous exchange exception of section 547(c)(1) were applicable to all purchase money security transactions, then the more specific provisions of section 547(c)(3), such as the 10-day perfection requirement, would be meaningless. We are not persuaded that Congress intended this result."

The Vance decision was followed by this Court in In re Northwest Erection, Inc., 56 B.R. 612, 614-15, 1 Mont. B.R. 305, 308 (Bankr. Mont. 1986), wherein this Court stated that it was:

> " * * * bound by the law of this circuit which clearly holds that the perfection of the security interest must be made within 10 days in order to rely on the contemporaneous exchange exception to the preference rule."

In this case, the loan transaction on February 13, 1989, was a purchase money security transaction. As such, § 547(c)(1) is not an applicable exception in this case. Vance, supra at 260-61. The Defendant did not have a perfected security interest within 10 days of the Debtors receiving possession of the 1989 Mazda.[1] It is noteworthy that § 547(c)(3)(B) uses the term "possession," not legal title. The Debtor took possession of the vehicle on February 13, 1989. Accordingly, § 547(c)(3) does not avail the Defendant of an exception to the Trustee's avoidance powers. Northwest Erection, supra at 615.

The Defendant and Amicus First Bank assert that the

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[1]In fact, the necessary registration and title documents were not filed with the Cascade County Treasurer until 15 days after the Debtors received possession of the 1989 Mazda.

Trustee/Plaintiff's position will overrule the intent of the parties who were involved in the subject transactions. This Court is aware that the parties' intent is of critical inquiry under § 547(c)(1). In re Wadsworth Bldg. Components, Inc., 711 F.2d 122, 124 (9th Cir. 1983). As noted above, subsection (c)(1) does not apply to the facts in this case. Morever, under § 61-3-103, supra, perfection does not relate back to the transaction date. Williamson v. Skerritt, 141 Mont. 422, 378 P.2d 215 (1963). The holding of In re Damon, 34 B.R. 626, 629 (Bankr. Kan. 1983) is thus appropriate.

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> "If the creditor fails to perfect within 10 days, § 547(c)(3) is inapplicable; the transfer is deemed to be made whenever perfection occurs, pursuant to § 547(e)(2), the transfer is on account of an antecedent debt, pursuant to § 547(b)(2), and the transfer is avoidable. Creditors failing to perfect within 10 days have argued, however, that even though they failed to comply with § 547(c)(3), the transfer was substantially contemporaneous to the loan advance pursuant to § 547(c)(1). Courts are divided but the better view holds that when funds are advanced at the time or after a purchase money security interest is granted, but the purchase money security interest is not perfected within 10 days after the security interest attaches, the creditor cannot successfully argue the transfer was nevertheless substantially contemporaneous under § 547(c)(1). (citing cases)"

Accordingly, the Trustee's avoidance powers overcome the Defendant's security interest, and as such, the Defendant's lien

is void.

IT IS ORDERED that the Defendant's lien on the Debtors' 1989 Mazda, Title No W166014, is hereby voided and said vehicle shall be turned over to the Trustee/Plaintiff for sale, subject to any proper exemption of the Debtor.

JOHN L. PETERSON
United States Bankruptcy Judge
215 Federal Building
Butte, Montana 59701

Copy mailed to Counsel of Record and Trustee this 19th day of, April 1990

Deputy Clerk (Cert. cc. US Dist. Ct)

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