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ALASKA STATE LEGISLATURE

SENATE BANKING COMMITTEE

POUCH V, JUNEAU 99811

ANALYSIS OF CS SENATE BILL NO. 749 (LABOR AND COMMERCE)

CSSB 749 (L&C) would amend language in Chapter 45 of the Alaska Statutes, Trade Practices, specifically 45.45.010(f). This particular subsection was adopted in 1973 and prohibits a lender from taking an equity participation in a loan transaction entered into with a borrower. There is neither case law nor legislative history to explain its inclusion in existing statutes.

In reviewing federal banking law, the committee finds no such prohibition against equity participation. On the contrary, the Office of the Comptroller of the Currency states in Interpretive Ruling 7.7312:

A national bank may take as consideration for a loan a share in the profit, income or earnings from a business enterprise of a borrower. Such share may be in addition to or in lieu of interest. The borrower's obligation to repay principal, however, shall not be conditioned upon the profit, income or earnings of the business enterprise.

12 C.F.R. 7.7312

Likewise, in reviewing the banking laws of the other 49 states, the committee finds no such prohibition, although Tennessee does have a statute (47.24.102) which restricts a lender's ability to enter in to an equity participation in loan transactions of less than \$1 million.

The committee is concerned about the flow of long-term capital into the state, and finds that the existing 45.45.010(f) inhibits that flow. Present economic conditions, marked by high inflation rates and high interest rates, have forced both developers and traditional long-term lenders to come up with new methods of financing which: (1) provide the lender protection against inflation, and (2) provide the developer an affordable interest rate.

An equity participation allows the lender to participate in the profit, income or earnings from a business enterprise of the borrower, thus providing him with the hedge he needs against inflation. It allows the borrower access to funds with which to develop projects that otherwise would not be economic at the higher interest rates required by traditional financing.

In supporting this legislation, it is the committee's intent that state regulators of financial institutions require lenders and borrowers to abide by the provision of C.F.R. 7.7312 which relates to the repayment of principal. In addition, the committee intends, by the inclusion of credit unions on line 10, to provide parity for all financial institutions doing business within the state. Finally, by inclusion of the limitations on loan amount and term, the committee intends to protect the interests of relatively unsophisticated borrowers.

March 1, 1982

Senator Bob Mulcahy
Chairman, Labor & Commerce Committee
Pouch V
Juneau, Alaska 99811

Re: Senate Bill 749

Dear Senator Mulcahy:

Last year my partners and I encountered extreme difficulty in securing financing for the purchase of the Alaska Pacific Bank Building in Anchorage due to the statute prohibiting equity participation for the lender. We were successful in the long run but only after contacting eighty-two lenders.

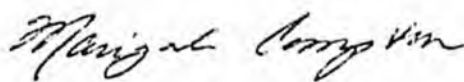
In reading Senate Bill No. 749, I would make the following recommendations for change:

1. "if the term of the loan is less than 15 years" is too restrictive. Most interest sensitive lenders will require a call between the fifth and tenth year. Clarification is needed. Most equity participation loans will have an amortization of thirty (30) years with a call at year ten (10).
2. I would prefer the bill be shortened and end with "less than \$1,000,000." By limiting equity participation loans to loans over \$1,000,000, the legislature is automatically protecting the small, unsophisticated investor from private loan sharks.

In essence, I do not feel that the government should be involved in restricting free enterprise. If a purchaser can obtain a satisfactory yield through an equity participation loan with a lender, the state government should not prohibit such a transaction.

If we wish to keep our economy healthy in Alaska, we must not prohibit buyers from obtaining equity participation loans on whatever terms are accertable to the buyer. Rental rates are insufficient to support the current high interest rates on a straight mortgage. As owners and purchasers of real estate, we need the latitude to negotiate the best loan package available and that is often an equity participation loan.

Please keep me informed as to the progress of Senate Bill 749.
Thank you.


Marigale Compton CCIM

MC/dd

STATE OF ALASKA

DEPARTMENT OF COMMERCE & ECONOMIC DEVELOPMENT

OFFICE OF THE COMMISSIONER

JAY S. HAMMOND, GOVERNOR

POUCH D
JUNEAU, ALASKA 99811
PHONE: 465-2500

February 25, 1982

Honorable Bob Mulcahy, Chairman
Senate Labor & Commerce Committee
Pouch V
Juneau, Alaska 99811

Dear Senator Mulcahy:

RE: SB 749, An Act Relating to Equity Participation

You have requested the position of the Department of Commerce and Economic Development on the above subject bill. First, let me say that, as written, we would find no detrimental impact on the safety and soundness of those financial institutions that we regulate. This is mainly covered by Lines 17 and 18 which provide that the loan principal cannot be conditioned upon profits, earnings or income.

In general, we are in favor of the bill and would support it. We feel that it will encourage financing that would not otherwise be available due to high rates. This legislation would also provide for a new source of participants in lendings, i.e., insurance company, that are otherwise prohibited without this legislation.

Provisions that provide for an exemption on one to four family owner-occupied dwellings will allow new methods of home financing that are springing up in other states. Any of these activities would not create any additional risk that is not already found in lending as it is known today and any risk could be adequately regulated if necessary.

If you wish any further information you may contact Mr. Kirkpatrick direct at 465-2521.

Sincerely,

E. W. Eboch

Edward W. Eboch
Deputy Commissioner

WFK/cw#10R4



Official Business

Alaska State Legislature

Senate

Labor & Commerce Committee

Pouch V
State Capitol
Juneau, Alaska 99811

SB 749; Summary

Allows equity participation in shared appreciation mortgages for loans greater than \$1 million, and with terms in excess of 15 years, and for loans to acquire a one to four family dwelling to be used as the residence of the borrower. The obligation of the borrower to repay the principal may not be conditioned upon the profits, income, or earnings of a business enterprise of the borrower. Amends existing law to facilitate the flow of long term capital within Alaska.

CS for SB 749: Would permit equity participation in loans greater than \$1 million and for terms in excess of 15 years.

HOGUE AND LEKISCH

A PROFESSIONAL CORPORATION

ATTORNEYS AT LAW

437 "E" STREET, SUITE 500 • ANCHORAGE, ALASKA 99501

(907) 276-1726

ANDREW E. HOGUE
PETER A. LEKISCH
WARREN G. KELSO
CALVIN R. JONES
ANN W. RESCH
RICHARD F. DEUSER

March 3, 1982

Senator Bob Mulcahy
Chairman, Senate Labor and Commerce Committee
Alaska State Legislature
Pouch V
Juneau, AK 99811

Re: Senate Bill 749 

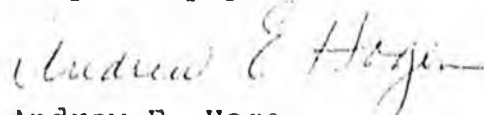
Dear Senator Mulcahy:

Washington Mortgage Co., Inc. (WMC) has asked me to submit the following comments regarding Senate Bill 749.

1. WMC suggests that five (5) years be substituted for fifteen (15) years on the fifth line of the Bill. The reason for this suggested change is that loans that are presently being made in other states have a general term of five to ten years and, in order for Alaska to be competitive in the commercial real estate loan market, it should have a term requirement no more restrictive than the requirements of the present national commercial real estate loan market.

2. The last sentence of Senate Bill 749 appears to be contradictory to the first sentence in that it appears to state that the borrower does not have to repay principal dependent upon the profits, income, or earnings of a business enterprise of a borrower. Obviously, if a borrower has agreed to pay a percentage of profits, income, or earnings in consideration for an otherwise permitted loan and the borrower fails to pay the profit, income or earnings, the lender should have the right to declare a default and require the principal repayment. If the intent of the Special Committee on Banking is to mean something other than indicated above, then that intent should be more clearly reflected in the legislation or in an appropriate committee report.

Very truly yours,



Andrew E. Hogue
Attorney for Washington Mortgage Co., Inc.

AEH/ms

cc: Senator Patrick Rodey, Attention Jim Kelly
Washington Mortgage Co., Inc.

WASHINGTON MORTGAGE CO., INC.
2720 Third Avenue, Suite 300
Seattle, WA 98121
(206) 682-5240

March 10, 1982

Senator Bob Mulcahy
Chairman, Labor and Commerce Committee
Alaska State Legislature
Room 119 Capitol Building
Juneau, AK 99811

Re: Senate Bill 749
Usury/Equity and Income Participation

Dear Senator Mulcahy and Committee Members:

It has come to our attention that the proposed change in the usury law is contingent upon the minimum loan amount being \$1,000,000 and the minimum term of the loan being fifteen (15) years. We have no problem with the minimum loan amount being \$1,000,000; however, we do have a real concern about the minimum term being fifteen (15) years. We feel that this will adversely affect the attraction of long term capital to the State of Alaska.

We recommend a minimum of five (5) years with an alternative of five (5) years for multi-family rental projects and ten (10) years for commercial projects. We hope the following paragraphs will clarify and support this recommendation.

Long term lending has changed over the past few years. Inflation has necessitated lenders to negotiate the term of their loans to much shorter periods with ten (10) years being the maximum today. Multi-family rental housing lending for the past five (5) to ten (10) years has been primarily provided by the thrift industry. Pension funds and life insurance companies have not provided this type financing and, in fact, a majority of the operating policies prohibit lending on apartments.

We have provided a lot of apartment lending in Alaska in the past; however, we have done no apartment lending in the past two (2) years because of your usury law. We feel that it is imperative to have five (5) years as a limitation in Senate Bill '49 for multi-family loans if we are to attract long term capital to your state to overcome your present housing shortage.

Very truly yours,

/s/

Roger J. O'Connell
Senior Vice President

WASHINGTON MORTGAGE CO INC AB
2720 3 AVE SUITE 300
SEATTLE WA 98121



Mailgram®



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SENATOR BOB MULCAHY, CHAIRMAN
STATE LABOR AND COMMERCE COMMITTEE
ROOM 119 CAPITOL BLDG
JUNEO AK 99811

REGARDING SENATE BILL #749 USURY/EQUITY AND INCOME PARTICIPATION.

IT HAS COME TO OUR ATTENTION THAT THE PROPOSED CHANGE IN THE USURY
LAW IS CONTINGENT UPON A MINIMUM LOAN AMOUNT BEING ONE MILLION
DOLLARS. THE MINIMUM TERM OF THE LOAN BEING 15 YEARS.

WE HAVE NO PROBLEM WITH THE MINIMUM LOAN AMOUNT BEING ONE MILLION
DOLLARS HOWEVER WE DO HAVE A REAL CONCERN ABOUT THE MINIMUM TERM
BEING 15 YEARS. WE FEEL THAT THIS WILL ADVERSELY AFFECT THE
ATTRACTION OF LONG TERM CAPITAL TO THE STATE OF ALASKA.

WE RECOMMEND A MINIMUM TERM OF FIVE YEARS WITH AN ALTERNATIVE OF FIVE
YEARS FOR MULTI/FAMILY RENTAL PROJECTS AND TEN YEARS FOR COMMERCIAL
PROJECTS. WE HOPE THE FOLLOWING PARAGRAPH WILL HELP CLARIFY AND
SUPPORT THIS RECOMMENDATION.

LONG TERM LENDING HAS CHANGED OVER THE PAST FEW YEARS INFLATION HAS
NECESSITATED LENDERS TO NEGOTIATE THE TERM OF THEIR LOAN TO MUCH
SHORTER PERIODS WITH TEN YEARS BEING THE MAXIMUM TODAY.

MULTI/FAMILY RENTAL HOUSING LENDING FOR THE PAST FIVE TO TEN YEARS
HAS BEEN PRIMARILY PROVIDED BY THE THRIFT INDUSTRY. PENSION FUNDS AND
LIFE INSURANCE AGENCIES HAVE NOT PROVIDED THIS TYPE FINANCING AND IN
FACT A MAJORITY OF THE OPERATING POLICIES PROHIBIT LENDING ON
APARTMENTS.

WE HAVE PROVIDED A LOT OF APARTMENT LENDING IN ALASKA IN THE PAST
HOWEVER WE HAVE DONE NO APARTMENT LENDING IN THE PAST TWO YEARS
BECAUSE OF YOUR USURY LAW.

WE FEEL THAT IT IS IMPERATIVE TO HAVE FIVE YEARS AS THE LIMITATION IN
SENATE BILL #749 FOR MULTI/FAMILY LOANS IF WE ARE TO ATTRACT LONG
TERM CAPITAL TO YOUR STATE TO OVERCOME YOUR PRESENT HOUSING SHORTAGE.

SINCERELY
R J O'CONNELL
SENIOR VICE PRESIDENT
WASHINGTON MORTGAGE CO INC

1625 EST

March 1, 1982

Senator Bob Mulcahy
Chairman, Labor & Commerce Committee
Pouch V
Juneau, Alaska 99811

Re: Senate Bill 749

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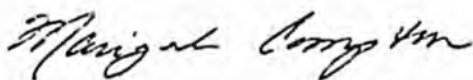
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Please keep me informed as to the progress of Senate Bill 749.
Thank you.


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MC/dd

STATE OF ALASKA

DEPARTMENT OF COMMERCE & ECONOMIC DEVELOPMENT

OFFICE OF THE COMMISSIONER

JAY S. HAMMOND, GOVERNOR

POUCH D
JUNEAU, ALASKA 99811
PHONE: 465-2500

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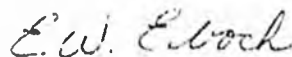
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Sincerely,



Edward W. Eboch
Deputy Commissioner

WFK/cw#10R4

COPY OF TELEGRAM BEING SENT TO MEMBERS OF SENATE
LABOR AND COMMERCE COMMITTEE 3/10/82

WASHINGTON MORTGAGE CO., INC.
2720 Third Avenue, Suite 300
Seattle, WA 98121
(206) 682-5240

March 10, 1982

Senator Bob Mulcahy
Chairman, Labor and Commerce Committee
Alaska State Legislature
Room 119 Capitol Building
Juneau, AK 99811

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Very truly yours,

/s/

Roger J. O'Connell
Senior Vice President

(1)

Under the standard of subsection (e) of this section, the courts have utilized a flexible, ad hoc approach to determine, by an essentially factual inquiry, the extent to which an error in the financing statement would be misleading to one undertaking a reasonable search. *Dietrich-Post Co. v. Alaska Nat'l Bank*, 638 F.2d 117 (9th Cir. 1981).

Where a financing statement and its

underlying loan documents mistakenly identified a debtor as the predecessor partnership rather than the corporation, the financing statement was seriously misleading and the lender had no perfected security interest in the assets of the corporation. *Dietrich-Post Co. v. Alaska Nat'l Bank*, 638 F.2d 117 (9th Cir. 1981).

Article 5. Default.

Sec. 45.09.504. Secured party's right to dispose of collateral after default; effect of disposition.

NOTES TO DECISIONS

Noncompliance with subsection (c). In accord with 1st paragraph in original. See *Hoch v. Ellis*, Sup. Ct. Op. No. 2346 (File No. 4475), 627 P.2d 1060 (1981).

If a sale was deficient with respect to either notice or commercial reasonableness, then a burden is placed upon the secured party to rebut the presumption that the fair market value of the collateral was at least equal to the amount of the outstanding debt. *Hoch v. Ellis*, Sup. Ct. Op. No. 2346 (File No. 4475), 627 P.2d 1060 (1981).

The burden is on the secured party to prove by clear and convincing evidence the value of the collateral. *Hoch v. Ellis*, Sup.

Ct. Op. No. 2346 (File No. 4475), 627 P.2d 1060 (1981).

If the secured party fails to rebut the presumption that the fair market value of the collateral was at least equal to the amount of the outstanding debt, then the presumption leads to the conclusion that the entire debt is discharged. *Hoch v. Ellis*, Sup. Ct. Op. No. 2346 (File No. 4475), 627 P.2d 1060 (1981).

Factors in determining value of collateral. — The local economic market at the time of sale is a recognized factor in determining the value of the collateral. *Hoch v. Ellis*, Sup. Ct. Op. No. 2346 (File No. 4475), 627 P.2d 1060 (1981).

Chapter 45. Trade Practices.

Article

1. Interest (§ 45.45.010)

Article 1. Interest.

Section

10. Legal rate of interest

Sec. 45.45.010. Legal rate of interest. (a) The rate of interest in the state is 10.5 percent a year and no more on money after it is due except as provided in (b) of this section.

(b) No interest may be charged by express agreement of the parties in a contract or loan commitment which is more than five percentage points above the annual rate charged member banks for advances by the 12th Federal Reserve District on the day on which the contract or loan commitment is made. A contract or loan commitment in which the principal amount exceeds \$25,000 is exempt from the limitation of this subsection.

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(c) Repealed by § 3 ch 84 SLA 1973.

(d) Repealed by § 2 ch 94 SLA 1981.

(e) Repealed by § 4 ch 146 SLA 1974.

(f) No bank, savings and loan institution, pension fund, insurance company or mortgage company may require or accept any per cent of ownership or profits above its interest rate.

(g) Loan contracts and commitments covering one- to four-family dwellings may be prepaid without penalty, except federally insured loans that require a prepayment penalty.

(h) If the limitations on interest rates provided for in this section are inconsistent with the provisions of any other statute covering maximum interest, service charges or discount rates then the provisions of the other statute prevail. (§ 25-1-1 ACLA 1949; am § 20 ch 143 SLA 1968; am § 2 ch 69 SLA 1969; am §§ 1, 2 ch 94 SLA 1969; am §§ 1, 2 ch 239 SLA 1970; am §§ 1 — 3 ch 84 SLA 1973; am §§ 1 — 4 ch 146 SLA 1974; am § 1 ch 110 SLA 1976; am § 1 ch 159 SLA 1976; am § 2 ch 107 SLA 1980; am §§ 1, 2 ch 94 SLA 1981)

Cross references. — As to alternate technology and power resource loans, see AS 45.88.030(e).

Effect of amendments. — The 1981 amendment, effective July 27, 1981, in subsection (b), deleted "dated after June 4, 1976" following "contract or loan commitment" and substituted "on the day on" for "that prevailed on the 25th day of the month preceding the commencement of the calendar quarter during" preceding "which the contract" in the first sentence and substituted "\$25,000" for "\$100,000"

preceding "is exempt" in the second sentence. The amendment also repealed subsection (d) which read "Notice of the annual rate charge member banks for advances by the 12th Federal Reserve District prevailing on the 25th day of the month preceding the commencement of each calendar quarter required for the maximum interest rate computation under (b) of this section shall be provided by the Department of Commerce and Economic Development."

NOTES TO DECISIONS

Cited in *State v. Alaska Continental Dev. Corp.*, Sup. Ct. Op. No. 2254 (File Nos. 4121, 4122), 630 P.2d 977 (1980).

Chapter 50. Competitive Practices and Regulation of Competition.

Article 4. Unfair Trade Practices and Consumer Protection.

Sec. 45.50.471. Unlawful acts and practices.

NOTES TO DECISIONS

Similarity to federal law. — The prohibition in this section against "unfair methods of competition and unfair or deceptive acts or practices in the conduct of

trade or commerce" is substantially similar to that contained in section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. § 45(a)(1); *Metaska Mold, Inc. v.*

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

I. REQUEST
 Bill/Resolution No. SB 749
 Title An Act relating to equity participation
 Requested by Labor and Commerce Date _____

II. FISCAL DETAIL
 Agency Affected Commerce and Economic Development
 Program Category Affected Consumer Protection
 BRU, Program, Or Subprogram(s) Affected Financial Institutions
 (Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87
100 PERSONAL SERVICES	0					
200 TRAVEL	0					
300 CONTRACTUAL	0					
400 COMMODITIES	0					
500 EQUIPMENT	0					
600 LAND & STRUCTURES	0					
700 GRANTS, CLAIMS, ETC.	0					
TOTAL	0					

FUNDING (Thousands of Dollars)

GENERAL FUND	0					
FEDERAL FUNDS	0					
OTHER (Specify Source)	0					

POSITIONS

FULL TIME	0					
PART TIME	0					
TEMPORARY	0					

III. ANALYSIS (See Fiscal Note Preparation Instruction, Section III)

IV. DATE February 18, 1982 PREPARED BY Willis F. Kirkpatrick, Director
 AGENCY Banking, Securities, Sm. Loans, & Corp.
 Original: Legislative Finance PHONE 465-2521
 cc: Budget and Management
 Prime Sponsor (First Legislator Named)
 33-001 (Rev. 12/81)