02-03-017

IN RE: House Judiciary Committee, Public Hearing, House Bills 1249 and 1586, Open-End Mortgages

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Verbatim record of the Public Hearing held at One Oxford Centre, Fourth Floor Auditorium, 301 Grant Street, Pittsburgh, Pennsylvania, on Thursday,

October 1, 1987
10:00 a.m.

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Honorable H. William DeWeese, Chairman

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ALSO PRESENT:

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John Connelly, Esquire
Special Counsel of Judiciary Committee

Amy Nelson
Research Analyst of Judiciary Committee

Mary Beth Marschik
Staff of Representative Moehlmann

INDEX TO SPEAKERS

(Whereupon, the hearing commenced at 10:10 a.m.)

CHAIRMAN DEWEESE: Good morning, ladies and gentlemen and welcome to the October 1 public hearing of the House Judiciary Committee regarding House Bills 1249 and 1586. The event will be divided into two segments, and this afternoon, we will be back with Representative Olasz and other legislation that will commence at 1:30.

On behalf of Representative Dawida, Representative Josephs, the Majority, Minority Counsel, and other members that we anticipate will join us, thank you for coming to Pittsburgh and sharing with us some of your perspective concerning some very complicated legislation. I quite frankly as Chairman of the Judiciary Committee am inundated by hundreds of pieces of legislation. I don't recall any that are more difficult for me to fathom. But that's one of the reasons we're here today, and I welcome you all.

To lead off our witnesses, and we're not too far behind, especially on legislative time, I would like to welcome David B. Ward, Esquire, Senior Vice President for Government Relations for Beneficial Management Corporation. David and Mike Catarano, Government Affairs Representative of the corporation will be joining him.

MR. WARD: Thank you, Mr. Chairman. I represent Beneficial Mortgage Corporation of Pennsylvania and its affiliated companies which have been making open-end real

estate loans in Pennsylvania since 1985 under the existing priority of liens law. We presently have in excess of 85 million dollars of this type of loan outstanding, and the Bills in question would affect those type of loans and, of course any new loans made after the date of enactment.

There are two general types of loans that provide for advances after a mortgage has been recorded, both of which have been used for many years. The first is construction loans where money is advanced as a project is built according to a schedule and where repayment generally doesn't start until after the project is completed. That type of loan has a finite fixed dollar amount of money that is put out.

The second is an open-end or revolving loan where instead of one series of advances, there is multiple advances contemplated with regular repayment and with additional advances at a later date. This type of loan, the amount of money to be advanced is really indefinite, although there is a limit set as to the total amount outstanding at any one point in time, commonly called credit limit.

Each of the Bills in question deal with both of those types of loans and lien priority law that applies to them. The two types of loans are dealt with differently, and really there is no controversy, I don't think, as to construction loan portions, although there is a great deal of

controversy as to the open-end, revolving loan portion.

I think it is important to note that the Bill 1249 which was, has been sponsored by, or I shouldn't say sponsored but has been pushed by the Pennsylvania Bankers' Association originated according to the documents filed by them with this Committee because of a concern in the construction loan area. I refer you to the March 30, 1987, PBA statement that was submitted to this Committee, and I have distributed copies for your convenience.

If you refer to page two of that statement, it describes the background of the problem. And, that section as I read it, deals only with the interpretation of the obligatory advance contract concept in construction loan agreements. This problem is solved in both of these Bills as I see it. Section 8144 of House Bill 1249 and Section 8143 of House Bill 1586 are identical and solve the construction loan problem in the same way. We have absolutely no objection to that.

With respect to open-end loans, the PBA's statement makes reference to an Ohio statute, and in effect, says let's adopt the Ohio way of doing things without really indicating to me anyway what the problem is and what the resolution of the problem is by doing that. We have had, as just aside, an opinion from a major Columbus, Ohio law firm that said they would certainly not recommend that any

other State use the Ohio law as a model as they considered it a defective law. There is active consideration going on in Ohio to repealing or amending that law to fix it.

Despite the lack of a problem, House Bill 1249 would turn the law upside-down in our opinion. And, one thing I want to point out at the outset is this is not a consumer issue, although there is a problem with consumers which I will get to later. The issue in lien priority is one of conflicting claims between creditors to the security given to a debtor for a loan after there's a default and the creditors are dividing up the value of the security.

Just as another aside, but to point out that purchase money mortgages have been excluded by 1249, but it really doesn't matter for purposes of my discussion because any lien priority issue involves the same questions, the dispute between creditors. It's not significant whether it's first, second, third or fourth in time in recording the mortgages. It's still a dispute between the creditors.

My question is, what is the basis for giving priority to one creditor over another. That is the purpose of these Bills is to set rules for deciding which creditors get paid first. The first criteria in who gets paid is obviously time. The creditor who advanced the money first would get paid first. This seems to be a fair test if the later creditors are given some reason to know that the loan

has been paid, and accordingly, we have a recording statute procedure that we always had which gives creditors notice as to when advances have been made.

Advances made after the recording of the mortgage are where we get into the questions that we're involved with today. Under both types of future advance contracts, construction loans were revolving loans, the common law had to decide whether advances made after the date of the mortgage, the first mortgage, should be given priority over loans made by some other lender at a later date than the date of the mortgage, but after the later advance.

Under the circumstances, the common law came to a logical and morally correct conclusion in our opinion. If the open-end lender had contractually obligated himself to make the future advances and the mortgage he recorded showed that to be the case, then a later lender should not be entitled to lend on the security of that same property and expect to have priorities over advances the first lender makes to comply with his obligation.

That is the basis for the lien priority laws as it exists in Pennsylvania today and in virtually throughout the United States. Put another way, if the lendar has placed himself at risk and has agreed that the borrower has the authority to draw down money at a later date, then

that lender should be protected against claims of later lenders when advances are made that comply with the obligation.

As a corollary, you have actual notice situation and the law today provides for that if the first lender has actual notice that a later lien has been put on the property, then advances made after that would become voluntary advances and they would not be given priority which is as it should be and essentially as the law is today.

I have seen no logical reason to put forward in 1249 which eliminates this role as to why it should be changed.

In the construction loan area, the concern is uncertainty as to how closely you must comply with the obligatory concept in order to retain your priority and that problem is solved by both of these Bills. It gives some additional flexibility to construction loan lenders, and I think solves the construction loan problem.

House Bill 1586 unlike House Bill 1249, does not go beyond the construction loan problem in resolving loans and turns the law upside-down. What 1586 does, we think, is clarify the law to state explicitly the types of conditions that a lender can put on his obligation without making that obligation simply a usury and thus, no longer obligatory under the laws' eye, and it preserves the same sound moral

base that the current law has.

In other words, if the lender has placed himself at risk by obligating himself to make an advance, then he is entitled to protection of claims of later lenders. If he is not obligated to make those advances, then I ask what would be the justification for giving priority. In our opinion, absolutely no justification for doing it.

CHAIRMAN DEWEESE: What would be their opinion? What would be the other opinion?

MR. WARD: I really don't know. I really have not seen any justification given for giving that competing creditor priority where he has made advance to which he has absolutely no obligation. That's a fundamental error with this Bill.

The consumer issue, I think, is as follows. Beyond a whole set of practical problems with notices and debates over whether notices have been given properly within the time periods and so forth, the real problem for the consumer is that a lender can now tie up the borrower simply by typing open-end. This would be under 1249, if it's adopted. The first lender can tie up the borrower simply by typing open-end mortgage on the top of his loan document at the top of the mortgage having absolutely no risk because he is not obligated to advance any more money than he advances the day he makes the loan. For example, he could

advance $1,000, type open-end mortgage on the top of the mortgage, and give him a credit line of a million dollars with no obligation to make any advance beyond the original thousand dollars. That customer's property is then tied up to the tune of a million dollars and that customer, that borrower can not, has absolutely no right to any future advances, but he does have the obligation whenever he would want to make a later loan with another lender to go back to that first borrower, send him notices, wait throughout time periods, and there is some debate whether he has to wait three days or eight days, whether that five-day period comes while the recision period is running or after it's, or in addition to it, but the borrower now has to wait under 1249, to get his money from a second lender, and he has to notify the first lender, and he has to go to the expense of getting advice on how this complicated law works, and I think it would take a team of lawyers to tell him what to do all because we changed the rules and eliminated the obligatory advance concept.

I want to point out too to you, to the Committee, that when we're giving these notices of limitation in House Bill 1249, we're always talking about, the way they structured it, the third mortgage. We're talking about creating a system that is viable only for the third mortgage, not second, because the first mortgages are excluded from it.

Purchase money mortgages are, which is 90 percent of the time, a first mortgage.

Then, we have a second mortgage lender, and instead of, under today's system, that the second mortgage lender being paid off which is what happens when another second mortgage loan is made at a competitive rate, they want to leave this mortgage on the books and send a notice of limitation and have a third mortgage outstanding, which to us -- and there is no reason there couldn't be a fourth, fifth or sixth mortgage.

To create a system that would urge borrowers and lenders to create stacked mortgages in our opinion is just simply not sensible. There is no reason we should have a priority law that is based on the concept of every mortgage being a third mortgage before that law comes into play.

If we leave the obligatory advance concept in the law as it is today, which House Bill 1586 would do, then lenders can not willy-nilly call their loans open-end mortgages. Under present law, if the borrower wants to borrow more money at better rates, he can do so by simply paying off that first mortgage. We have made tens of thousands of mortgages in Pennsylvania. We have had tens of thousands of mortgages paid off in Pennsylvania that very, very way. They are being paid off today. The system works. We shouldn't change it drastically.

CHAIRMAN DEWEESE: The other side is saying it doesn't work. Why are they saying it doesn't work?

MR. WARD: I have seen nothing. Again, I point to the PBA statement. There is no indication to me that there is any problem in the revolving loan area that is solved by this Bill. We certainly don't see one. We got 85 million dollars of loans outstanding, seven or eight thousand loans. We had those loans since 1985, open-end type of loans here. We make them. They are paid off on a constant, on-going basis. We see no problem at all.

We litigated the priorities here in Pennsylvania with no problem. Everyone understands what the law is, and it works. It's the law that is in 90 percent of the country. We don't see any reason to change.

To summarize very quickly, the question of what advances are obligatory under construction contract can and should be resolved without drastically changing the law relating to open-end or revolving loans.

The law of priorities deal only with conflicts between creditors. The only reason to give one priority over the other is if his advance is made earlier in time or is made due to an obligation of the lender and should, therefore, relate back in time to the date of the recording of the mortgage.

There is no reason to give one creditor priority

over another if he has taken no risk whatsoever but has simply typed, open-end mortgage on a piece of paper as could be done under House Bill 1249.

There is, furthermore, no reason to drag borrowers into a confusing and complicated scheme of notices and delays simply because the law would have to have a way of destroying the riskless priorities that could be created under House Bill 1249. Why have third and fourth mortgages at all?

The existing law works, and we would submit that House Bill 1586 would retain the existing law. If this Committee is so moved to bring a Bill out, that 1586 would serve the public and the mortgage business far better than House Bill 1249.

CHAIRMAN DEWEESE: Thank you, Mr. Ward. You are well within your time limit. We have five or six minutes with no problem for questions. The prime sponsor of one of the measures, Mike Dawida, any observations, comments, questions?

REPRESENTATIVE DAWIDA: I would like to make a suggestion, Mr. Chairman, knowing your willingness to be novel and creative. I would suggest that we listen to all the testimony on both sides, and if the people would be willing to stay, then ask questions. I think we -- we're not used to dealing with banking bills on this Committee.

I think what would be better is if we allow both sides to speak and then ask them questions at the same time, if they would be willing.

CHAIRMAN DEWEESE: That makes a lot of sense to me. Babette, no objections?

REPRESENTATIVE JOSEPHS: No. That sounds good.

CHAIRMAN DEWEESE: If you gentlemen will linger.

MR. WARD: Yes, absolutely.

CHAIRMAN DEWEESE: Thank you very much. And, thank you very much -- I want to take one thing from Joe Biden. He kept thanking people for staying on time and keeping it within the parameters of our schedule. Thank you very much for doing that.

Felix Cohen, Esquire, Pennsylvania Financial Services Association, welcome.

MR. COHEN: Thank you. I have a stack of documents if you will tell me whom I should give them.

CHAIRMAN DEWEESE: Amy, our research analyst.

REPRESENTATIVE DAWIDA: Mr. Chairman, I would like to make one other point since you are talking about Joe Biden. I did well in law school, but I didn't finish in the top. I wanted that on the record.

CHAIRMAN DEWEESE: I went to the same one that Higgenboggen went to.

MR. COHEN: I will certainly stay within my time

limit even if measured on legislative time.

A little background since I am not a frequent visitor to these chambers or this Committee. My name is Felix Cohen. I work at the Pittsburgh headquarters of Signal Financial Corporation where I am a Senior Vice President, the Corporate Secretary and the General Counsel.

Before I worked for Signal, I was a law clerk in the U.S. Courts, an associate of one of the largest Pittsburgh firms, the firm of Buchanan Ingersoll.

I am a member of a number of professional and industry organizations such as the American Financial Services Association, which is the national industry association of finance companies and other consumer lenders. I am also the Chairman of the Law Committee of the Pennsylvania Financial Services Association, and it is in that capacity that I speak to you this morning.

The Pennsylvania Financial Services Association is the industry's association of finance companies and other lenders who engage in the consumer finance business in Pennsylvania. The Association's membership includes approximately 115 companies, it tends to vary from time to time, representing more than 650 discreet lending offices in the State.

Our membership ranges from the industry giants with national presence such as Beneficial and Household to

the smallest one-office, independent mom-and-pop type loan company.

The position of the Pennsylvania Consumer Finance Association with respect to the matter of lien priority is, quite simply, that in the best of all possible words, we would certainly favor the existing common law.

Our support for the existing common law, not unlike the support that you heard Dave Ward offer a moment ago, is based upon its recognition of a basic principle of equity. Lien priority for a given lender should follow the risk of loss of funds to which the lender is exposed.

When a lender has made a commitment to disburse funds in the future, which is what an open-end mortgage law is all about, and he can't evade that commitment to disburse funds by his own actions, that is to say, his commitment is in some sense obligatory, he should be treated with respect to lien priority just as if he already disbursed those funds because he is going to have to sometime in the future. His priority for the disbursement of those funds should be effective as of the time that he becomes committed.

But, when a lender makes no such commitment for disbursement in the future or makes a commitment which he retains the ability to evade by changing his mind as it were, our Association sees no reason in fairness or in law for that lender to be able to gain a lien priority retroactive

to the time of his originally made document for that phantom commitment.

Pennsylvania Courts, Pennsylvania lenders, Pennsylvania title companies, have recognized this distinction between obligatory and voluntary commitments to lend funds in the future with relatively little trouble and we are quite comfortable with that circumstance.

Several years ago, some lenders identified a flaw in the law as it applies to loans such as the typical construction loans in which future advances are contemplated over a stated schedule, but turn out to be made on a different schedule because of the delays in construction or a number of various reasons.

To the degree that such off-schedule advances would be deemed voluntary rather than obligatory under present law and that's not entitled to retroactive priority, we are quite ready to support an amendment to the law which would address that shortcoming.

House Bill 1249 would be quite palatable to our Association membership if it was limited only to addressing that flaw.

If you read the supporting documents for 1249, you can come away with the impression that is what it is limited to. Unfortunately, if you read the Bill, you discover that's not quite the case. Bill 1249 appears to act

like its predecessor, House Bill 841, which you may remember from last year's session, it appears to alter the common laws.

It correctly amends Section 8144 of existing law for the off-schedule construction loans. But it also changes the common law by providing lien priorities for lenders who choose to add certain stated labels to their mortgage documents regardless of whether those mortgage documents do or do not include the obligatory commitment to disburse funds in the future which we believe should be the only equitable and legal condition for enjoying such priorities.

Bill 1249 also includes language which we read to require advance notice to existing open-end lien holders of any proposed extension of credit to that borrower by some other creditors.

CHAIRMAN DEWEESE: Could you amplify that for a second? That last sentence, that was sort of crucial.

MR. COHEN: As I read 1249, and there may be a debate in the room, which you will have to resort to some of the other persons who will offer testimony to clarify, as I read 1249, it requires that a person who has the intent to borrow funds from an unrelated lender who is not holding an open-end mortgage secured by this borrower's property has to send a notice in advance to the holder of the open-end

mortgage secured by this borrower's property has to send a notice in advance to the holder of the open-end mortgage saying, I'm about to deal with your competitor. You have five days to do something. I am not sure of the purpose of that notice provision. It can charitably be viewed, I suppose, as a means to lock down the scope of the prior open-end mortgage lien priority.

You in effect cut off the old lien priority and give the new lender in the game a new priority because he has given the old lender notice that if he makes any more advances, he does so at his peril. It can also be viewed, and since we are in some sense competitors as well as participants in the same industry, it is easy to view this way as well. That can make the mortgage loan marketplace much less hospitable to new lenders on the scene who want to come in and make a junior mortgage loan behind an existing open-end mortgage loan.

He has to send notice to somebody and wait to see if that somebody goes to work on his borrower to change the borrower's mind. This is not unheard of.

CHAIRMAN DEWEESE: Thank you.

MR. COHEN: We believe that if 1249 were to become law, it would be all too easy for open-end lenders to use that notice period to hard-sell their borrowers into staying on their books regardless of the merits of any

proposed new financing from any new lender on the scene. Bill 1586, on the other hand, accomplishes two things, two different things.

One, it amends existing law with respect to the off-schedule construction loans very much the same way that 1249 does, and I don't think anybody has any problem with that.

Two, it attempts to codify the existing common law with respect to lien priorities. It does not attempt to change the common law.

It is true, there are six enumerated conditions set out in the first section of Bill 1586 which don't appear in a list anywhere in the common law. Those six conditions are defined in Bill 1586 as not destroying the obligatory nature of future advances in any given mortgage.

They are included, as I understand it, in recognition of the economic realities of making loans over extended time periods in dynamic markets.

They are in the nature of unanticipated future developments. For example, default by a borrower, sale of the property on which the mortgage is taken by a borrower, the departure from a lending business of a particular creditor who made the loan in the first place, and such things. None of them is a condition which can be controlled or envoked by the lender as a means to evade an obligatory

commitment that he had in the past. We believe 1586 is fair. We believe it substantially does not change the common law. And, if amendments to the statutory law in this area are deemed necessary by the Committee and by the Legislature, we support 1586.

We see flaws in 1249. We are not sure what 1249 is meant to accomplish, but we see flaws in it which we believe would do violence to our participation in the market-place. That concludes my prepared remarks. I can remain for a while if there are going to be any questions later.

CHAIRMAN DEWEESE: Okay, sir. Thank you very much.

Karl Wenk, Vice Chairman of Provident National Bank. Good morning, Karl.

MR. WENK: Good morning, Mr. Chairman, members of the Committee. As my prepared statement will reveal, I am a former Vice Chairman of the Provident National Bank. I retired from that institution at the end of last year.

I am a member of its Board of Directors, and I might add at this point, that the Provident is affiliated of the Pittsburgh-based PNC Financial Corporation. I also serve as President of the Pennsylvania Bankers' Association during its fiscal year ended June 30, 1986, and served on the PBA Executive Committee until July 1987.

During my service with the PBA, I became very

familiar with open-end mortgage bills of the type which you are now considering. This subject is one of particular interest to me because of my involvement with consumer credit both during my career as a banker and during an earlier period of 20 years as a consumer finance company executive.

I appreciate the opportunity to appear here today to present the views of the PBA which I had some hand in shaping while I was an active office of the Association.

As you know, the question as to whether our State should authorize an open-end mortgage and, if it does so, what type of instrument it should be, have been pending in the General Assembly since February 1984, when a Bill was introduced at the request of the Committee of the Bar Association to alleviate some of the technicalities arising out of court decisions that had complicated construction mortgage financing.

PBA is, of course, very interested in the affect of the pending Bills on construction mortgages since its members are heavily involved in that activity. The main point of our interest here today, however, is the affect of the Bills in the consumer credit field.

The introduction of the 1984 Bill happened to coincide with an increased desire by borrowers and lenders of all types for a mortgage facility that would permit lines

of credit to be secured by home equities even though advances under the lines might only be made from time to time.

One reason for that desire was the large increase in home equities resulting from general growth of home values which provided a larger reservoir of bankable collateral for many potential borrowers. Interest in the subject was further intensified as a result of the 1986 revision of the Federal Internal Revenue Code which provides for a general elimination of deductions for interest payments on personal loans while preserving the deduction for home mortgage interest payments.

Pennsylvania law traditionally has not provided a method for making future advances secured by a mortgage which method is efficient, relatively inexpensive, and, I emphasize this point, very reliable. The reason is that a mortgage may secure only a loan made at the time of the mortgage or at a later date pursuant to a binding commitment.

This is sometimes referred to as the obligatory advance doctrine. Without a binding commitment which obligates the lender to make an advance, a loan made under a mortgage previously recorded is subject to any liens that have been filed between the date of the recording and the date of the advance.

I should add at this point that in our discussions of this subject, we have learned that there does not seem to

be a unanimity of viewpoint among lenders as to what constitutes a binding or obligatory commitment. Most experienced real estate lawyers, however, hold the view that the binding requirement does not leave very much space for any ifs, ands and buts as to whether a loan will in fact be made in accordance with a commitment.

For example, there is a Pennsylvania Supreme Court decision that in the common situation in a construction loan in which advances are on a schedule based on the stage of completion of the project, an advance made by a lender prior to the scheduled date will be deemed an optional rather than an obligatory advance so that it will not be covered by the lien of the mortgage from the date of recording but only from the date of the advance.

Such a strict law does not permit much latitude in making a future advance commitment subject to continuing review of the amount of commitment and other qualifications. If a future advance loan is to remain dependent on the availability of home equity as collateral, the only choices that the lender has are either to incur the time and expense to check the records before each advance to determine if there are prior liens or to give a binding commitment that can not be withdrawn even if there is an adverse change in the credit standing of the borrower before the advance is actually taken down.

These factors have not prevented all banks from offering home equity credit programs but obviously the difficulty of assuring lien priority restricts the amounts that are committed and heightens the credit standards that prudent lending requires to be applied.

A Bill which eliminates the obligatory advance role and permits a mortgage to cover optional future advances will solve these credit problems while at the same time, freeing the construction mortgage lending field from the technical thicket that now surrounds it.

An optional advance open-end mortgage would permit a lender to give a borrower a line of credit for a stated amount that could be on a revolving credit basis and require only a single check of the real estate records to determine the lien position for all advances under the line. The ability to retain some discretion about the future advances would enable the lender to have future credit reviews before additional advances are made so that the level of credit risk that has to be undertaken can be adjusted appropriately.

With such an instrument for obtaining collateral security in a simple, less expensive, reliable way, lenders can prudently make more credit available for more borrowers at lower costs.

There is one aspect of an open-end mortgage

instrument as to which there is a very sharp difference of treatment in the Bills before you. By its nature, an open-end mortgage establishes a continuing relationship between the borrower and the lender so that all credit extended at any time can be covered by the lien of the mortgage as of the date of its recording.

The question arises as to how a borrower may terminate that relationship if the borrower wants to do so. Ordinarily, a mortgage simply remains on record until the amount secured is paid in full, as in the case of the ordinary purchase money first mortgage.

That procedure, however, would be very disadvantageous to a borrower on an open-end mortgage. If the borrower has no balance outstanding or if the amount of the outstanding balance is much less than the amount that could be borrowed against the value of the property, the borrower is effectively prevented from taking advantage of more favorable loan terms that might be offered until that mortgage is satisfied of record or the maximum amount which the mortgage can cover is reduced to the current balance.

Lenders have an interest in the borrower's position in this matter because it very sharply affects the competition for loans and thus is not in the consumer's best interest. If a potential customer has had an earlier transaction with a lender which has an open-end mortgage on

record, it will obviously be more difficult for a new lender to obtain business from that person because it would be subject to the delay of the person first having to obtain a recorded satisfaction of the first open-end mortgage before the new lender can obtain effective security in the same real estate.

It is our conclusion based on experience that the normal procedure for satisfying recorded mortgages, if applied to the open-end mortgage, would have the practical consequence that the first lender to obtain an open-end lien will have in effect obtained a new monopoly on the mortgager's future business.

PBA is very firmly of the view that there should be an open-end mortgage instrument available for all lenders, but that it should be an instrument that will not clog competition for loans which would be a disservice to both consumers and the lending industry.

We think there is a readily available solution to the problem which has met the test of experience in our neighbor State of Ohio. That is the provision in House Bill 1249 which enables a borrower to give notice to terminate an existing open-end mortgage on record if there is no outstanding debts or to limit the lien of that mortgage to the outstanding balance if there is one.

This procedure was proposed by PBA as essentially

a mirror copy of a statute that has been law in the State of Ohio since 1967. We strongly support it as a workable procedure for Pennsylvania as well. It is obviously very much in the interest of consumers on its face. It is also very much in the interest of lenders such as the banks who want to maintain competition in the market for consumer credit and preclude effective monopolization of customers.

Mr. Chairman, that concludes my prepared testimony. I too will remain and be available for questions subsequently.

CHAIRMAN DEWEESE: Thank you very much, sir. Thank you.

The next gentleman is John J. Brennan, General Counsel.

MR. BRENNAN: We don't have a separate statement. That is a joint statement.

CHAIRMAN DEWEESE: You also will linger?

MR. BRENNAN: (Nods head affirmatively.)

CHAIRMAN DEWEESE: Melvin Breaux, Drinker, Biddle and Reath. Melvin, you are here representing the savings and loan industry?

MR. BREAUX: Yes, Pennsylvania Association of Savings Institutions.

CHAIRMAN DEWEESE: Good morning, Melvin.

MR. BREAUX: Good morning, Mr. Chairman, Committee members.

CHAIRMAN DEWEESE: Melvin, will you introduce the gentleman next to you? We don't know him.

MR. BREAUX: This is James Stoup, the Executive Director of the Association, the Vice President of the Association.

I am a member of the Philadelphia law firm of Drinker, Biddle and Reath. I practice in their banking group. Our firm represents the Association, and I'm here testifying on behalf of the Association. I would like to state from the outset that it's the Association's position that we can live with either of these Bills, 1586 or 1249. We think they are quite similar, and, honestly, we don't see all of the controversy that other people tend to see with the two Bills.

We do feel, however, that 1249 is a better Bill. It calls a spade a spade and we like the provision in 1249 which allows the borrower to terminate the relationship at any time by giving the appropriate notice to the creditor.

As we see it, the purpose of House Bills 1249 and 1586 is to permit lenders in Pennsylvania to make available to Pennsylvania consumers lines of revolving credit secured by Pennsylvania -- secured by mortgages on consumers in real estate. As we see it, we have a problem of what I say new technology bumping up against laws that don't cover it.

In the old days, construction loans, construction lending was the only kinds of loans where the lender took a mortgage but did not advance all the funds to be borrowed at one time. He would disburse the funds over a period in the future. With respect to consumer loans, you didn't have those kinds of loans. Specifically, banks that made consumer loans disbursed all the funds immediately and so you didn't have a problem or requirement with respect to loans being made in the future.

Now there is a new product available. Consumers have become aware that they have great equity in their property. Mr. Chairman, I am departing from my prepared testimony to kind of respond to the statements that have been made earlier. They are becoming aware that they have equity in their property, and they want to take that equity out to a certain extent by making loans, and they don't want to take the entire amount out at one time, but they want a contractual relationship with the lender in order to be able to take out a specified amount from time to time over a period of time either accessed by a credit card or accessed by a check or whatever.

It so happens that because of the lien priority question, this kind of product is difficult to offer because if the lender agrees to lend the borrower $25,000 as a maximum line of credit, but the borrower wants it over time,

the mortgage is filed for $25,000. There is a serious question as has been noted earlier as to whether the lien priority of each future advance would relate back to the date that the mortgage is recorded. That has been the problem in the construction loan industry, and it is a problem in the, let's say, home equity loan industry now that it's becoming prevalent.

There are many lenders in Pennsylvania and outside of Pennsylvania who wish to offer this product but are not doing so because of the lien priority issue. There is in Pennsylvania as has been noted, the obligatory advance doctrine. But that doctrine is not clear. You can not rely on it because you never can tell when a loan is obligatory or not as has been noted in the construction industry. If the lender is supposed to make advances according to a schedule and does not comply with that schedule, it could be that that advance is not obligatory, and, therefore, its lien priority would not relate back to the date of the recording of the mortgage and that advance would become juniored to a subsequent creditor's lien.

The same problem could occur with respect to these consumer loans. I don't see this as being an issue of unfairness on the part of the creditors to change the obligatory advance doctrine by saying that so long as the borrower, the homeowner and the creditor agree that the

maximum amount of the loan will be $25,000 and that the borrower can make advances from time to time and that the maximum amount is specified in the notice in the mortgage and the mortgage is of record so that all future creditors can see that, well there is a lien against this property for $25,000, so I am going to make my credit decisions accordingly.

I think that that's fair from the standpoint of the consumers as well as from the standpoint of the borrowers and of the standpoint of subsequent creditors because it's all there, of record, that this is the amount that is outstanding against this property.

I think 1249 is a superior Bill in that it does not lock in the consumer to the original lender. It has the provision that if the consumer gets a loan from a second lender, and that loan, that mortgage is recorded, then the second lender can give notice to the first lender, and after that notice is received and five days have passed, the first lender will not be able to make any future advances which would enjoy a superior lien position over the subsequent lienor's credit.

That's an important point. There has been testimony, I believe, that this notice requirement would require the second lender to give notice to the first lender before the loan is made. As I read 1249, that is not

the case. The borrower would have to have applied for the loan. The loan would have had to have been granted and the mortgage recorded, a fait accompli, in order for the second lender to then give a notice to the first lender that I have made a loan. You are noticed of any future advances that you make will not have priorities over my loan.

I think that's an important point and simply requires a reading of 1249 to see. I don't see any problem at all with that. I think that 1249 also is honest in that it purports to be a change of the common law by stating that it applies to both obligatory as well as non-obligatory mortgage loans. Again, it gives the provision for the borrower or subsequent creditors to terminate the first creditor's interests with respect to future advances by giving the notice.

On the other hand, I think 1586 does essentially the same thing. It purports to maintain the distinction between obligatory and non-obligatory, but it then goes on to define almost all advances as being obligatory.

So, we feel that we can live with 1586, but we think that 1249 is the better way to go. There also was mention of the difficulty under present law or the ability under present law now without the notice provision of a borrower having a lien with respect to future advances kept from his property. It seems to us that an open-end mortgage

-- suppose there is an open-end mortgage on property of, let's say, $24,000 maximum, but the amount taken down by the borrower is only $10,000, I am not aware of any way that that borrower could compel the first lender that holds that $25,000 lien to remove the lien with respect to the difference between 10 and the 26,000 under the current law. That's why I think we need a provision such as the one in 1249 which gives the right to the borrower or a subsequent creditor who has actually made a loan and gotten the judgment to give a notice thereby terminating the right of that lender, of the first lender, to make subsequent advances that would enjoy lien priority superior to that of the subsequent creditor's loan.

I think I've covered the main points that I wanted to cover, Mr. Chairman. I would like to reiterate the point that I made earlier that we are familiar with both Bills. We had worked with John Brennan and PBA with respect to House Bill 1249, and they have been receptive to suggestions we had made as to changes of the Bill early on. We had a talk with David Ward and his people and provided our input with respect to 1586 and again, we do think that they essentially do the same job except from a different approach, and we lean somewhat towards 1249.

Thank you. I will stick around.

CHAIRMAN DEWEESE: You might be the referee.

Robert J. Jackson, Vice Chairman, Real Property, Probate and Trust Law Section, Pennsylvania Bar Association. This looks like the Bar Association walking in right here. You are right on the dot.

MR. JACKSON: We thought it was 11:20.

CHAIRMAN DEWEESE: You are right.

MR. JACKSON: We're happy to be here.

CHAIRMAN DEWEESE: But, you are on. What we have done as a suggestion of Representative Dawida was -- you are Bob?

MR. JACKSON: Bob Jackson.

CHAIRMAN DEWEESE: We decided that we would take everyone's testimony and then have a roundtable discussion. So thank you very much for being here. You are right, you are 17 minutes early.

MR. JACKSON: That's unusual.

CHAIRMAN DEWEESE: We were a few minutes late getting started, but we are all caught up. We were scheduled to go until noonish. If you can give us five, ten, fifteen minutes, whatever your pleasure, we'll roll up our sleeves and knock it around and try to educate the Committee.

MR. JACKSON: That sounds great. I think it's a lot better than what I have written here.

First of all, I would like to thank you for allowing us to come and present the position of the Pennsyl-

vania Bar Association on the Bills.

My name is Bob Jackson. I am from Media, Delaware County. I am a member of the Bar. I am currently Vice Chairman of the Real Property Division of the Real Property, Probate Section of the Pennsylvania Bar.

I have been in private practice in Media, Delaware County for 15 years. Prior to that, I was counsel at Gulf Oil Corporation for about six years.

Turning to the Bills 1249 and 1586, as the Chairman has indicated, this is all about lien priorities, lien priorities on mortgages. Back in 1984, the Bar Association merged with the Real Property Division came up with a suggestion and as a result, a Bill was introduced; House Bill 1931 of the 1984 Session. That Bill passed the House, went into Committee in the Senate and remained in the Committee until the end of that particular session.

In many ways, the earlier Bill that PBA had sponsored or had recommended rather, was similar to the two Bills under consideration today. The primary purpose of that Bill and these two Bills is to enable a lender whose loan is secured by a lien on real estate mortgage to continue to make advances to the borrower without the danger of an intervening lien; that is, a later lien coming ahead of in terms of priority in any particular advance.

Let's look just for a moment at the current state

of the law in the Commonwealth. Under current law, in Pennsylvania, a mortgage creates a lien on the real property it covers from the time it is recorded or if it is a purchase money mortgage, from the time it's delivered to the mortgagee so long as it's recorded in ten days thereafter. If that occurs, all sums advanced prior to the recording or delivery as well as those advanced later to the extent that the lender is obliged to make those payments, have a priority which relates back, goes back to the date of the recording.

In the typical loan to finance the construction, the lender for obvious reasons will advance money as the building goes along to pay subcontractor, materials. If the lender is obligated by agreement, common law, contract law, if the lender is obligated to make those advances, then with respect to other creditors who later come along even though they come along and have their lien prior to the time the money is actually given under the first mortgage, that advance is still protected in terms of its priority.

It relates back to the filing. And, the later coming liens are behind it in terms of priority. If the advances that the construction lender is making or any open-end lender is making, is non-obligatory, then the intervening liens, that is the second mortgage, the judgment creditor, are prior in terms of payout to the advances later made to the extent they are non-obligatory.

In that event, there is serious danger that the construction lender, if it's a construction mortgage, will never recover the advances later made because if the property is sold at foreclosure, other creditors who came later will get paid first, and there may be nothing left for the lender. Therefore, the motivation to the lender at that point, seeing these later creditors, is to not advance the non-obligatory advances which could result in the building remaining unfinished.

Of course, if the advances are obligatory, the lender would be encouraged to make the advances so that the building would get completed.

Construction loans are probably the instrument, the circumstance that brings this all into focus. Usually, in construction lending, that is lending as the building progresses, the loans are obligatory, the advances are obligatory. But, most lenders out of good common sense, are going to say in their mortgage instruments that they need not advance the money if when the advance is to be made, the borrower is in default, the borrower's credit has gone down, the value of the security has diminished.

This puts the borrower in a dilemma under Pennsylvania law because it could very well develop that a Court would look at those advances conditioned as they are on default, failing credit, failing value as being non-

obligatory.

So that if the lender advances and faces those circumstances, he may find himself subject to the intervening liens. Looking at that prospect, the lender may simply say, look, I am not going to go into this any deeper. I am going to let the building be where it is. That results in perhaps an eyesore, an unfaith eyesore, and is clearly a situation that is not in the best interest of the economy of this Commonwealth.

Accordingly, if the Bar Association even though it has not passed on these particular Bills, nevertheless has passed on the intent and supports the intent of these Bills. The difference between the two, and you really have to go back and forth over them a couple times, and I am happy you are having a give-and-take session because I think a lot of it needs to be drawn out that way, is that 1249 would protect mortgage advances whether or not obligatory, while 1586 would protect only obligatory advances while providing that advances are obligatory even though they are subject to one or more of six enumerated conditions.

1249 is very similar to the 1984 Bill, House Bill 1931. It would protect advances obligatory or non-obligatory except that non-obligatory advances would not be prior to any liens of which the mortgagee is given notice unless the advance is made for the completion of construction

of the building financed by the mortgage.

It seems that that thread varies through both Bills. In other words, payments that are made out of the necessity to get the project done are protected, it seems to me, under both. It would also permit the mortgagor to limit the indebtedness to advances already made or future obligatory advances.

1249 is obviously a more comprehensive set of guides. It does deal with more than simply the lender's point of view. It endeavors to look at some protection to intervening lien holders to laborers, to materialmen and indeed, to afford some protection to a mortgagor or the guy borrowing the money himself by setting up a mechanism to stop it, to stop the revolving credit, to stop the first position lender from continuing to make advances.

I think that the bottom line in my personal view, speaking as Bob Jackson, both Bills accomplish the desired result. The 1586 Bill by defining as it does obligatory and the 1249 Bill by also defining in some sense obligatory but at the same time, providing a mechanism where you can continue to lend to complete the project and/or until you get notice from a junior lien holder.

In short, the PBA does support both of the Bills. This Committee may want to consider combining the two, taking from one to the other at least one section.

CHAIRMAN DEWEESE: We have been asking these outfits to do that for a long time.

MR. JACKSON: Pardon?

CHAIRMAN DEWEESE: We have been asking these entities to amalgamate their positions for a long time. Heretofore, they have been quite tentative about doing that.

MR. JACKSON: Mr. Chairman, I don't know the entities you mean.

CHAIRMAN DEWEESE: I mean the finance people and the banking people.

MR. JACKSON: It seems to us that there is merit to that suggestion. The Bill that we had prepared back in '84, took more the tenor of the 1249 Bill because we felt, if I remember the debates at that time, that while it is a good idea to protect the lenders and get on with construction, and gentlemen and ladies, it's a very real problem, it's a very real problem with lenders in the Commonwealth to make a construction loan and to be sure that its advances are going to be secured.

Recognizing that is a laudable object and something we all should pursue. We're nevertheless cognizant of the materialman, the laborer, the intervening lender and the mortgagor himself.

I don't know that given the choice of having no Bill and going back to the drafting table or adopting either

one. I think I would prefer to get a Bill enacted. We need it. We have been at this for four or five years in the PBA. We who practice daily with lenders and construction development, it's a necessary Bill.

So, I would not like to see the Bill referred back for further revision, rather I would like to see something adopted if we could. Either one, I think, is a good Bill. Get something adopted, and then if refinements are needed, we can refine it.

But, I think it's urgent. There is an urgency that we get something accomplished.

That's about the sum of what I have to present. I want to thank you for letting me testify on these matters. I will welcome the opportunity to join in the give-and-take session if you want that now.

CHAIRMAN DEWEESE: We're on time. We're rolling. Let me just give you a perspective of my own. I am a politician and not able to discern some of the more recondite things I heard this morning, that I read last night, and that I was told about earlier. I am aware that Mr. Rappapore engineered the first effort, and I am also aware that Mr. Pratt, both gentlemen my predecessors, was quite involved in the last effort.

Today, we still have two Bills, and again, I am speaking from a layman's perspective. Both of them deal

with the construction problem, and there seems to be some agreement along those lines. There may be a way to draft legislation that would be agreeable to Matt Ryan, Jim Mandarino, Ed Zimprelli and John Stofford. I don't know, but I am hopeful that that might be able to happen especially with the superb staff that I have on the Judiciary Committee and the bipartisan harmony that we have enjoyed so far. We might be able to help at that level.

The second level, the open-end mortgages and the lien priorities have given us fits, and just from a politician's perspective with the lobbying juggernauts of the big finance corporations and big banks going 100 miles an hour and wheeling and dealing with the State Capitol, I don't see, just from my perspective, I don't see a resolution of this problem that would be able to pass in the House of Representatives, pass in the State Senate, and have Bob Casey put his imprimatur upon it. I just don't see that.

But, it's still early in the day. We got a give-and-take session. I am looking forward to it. I just wanted to share my perspective. We're here. Rappapore and Pratt were unsuccessful at pushing it all the way through. Maybe or probably because there was an agreement on the second question. Again, I have seen things happen in Harrisburg. This Committee is not going to spend innumerable hours and days upon something if the big lobbying efforts are

going to be coming at it. One team gets half the votes, and the other team gets half the votes. It's not going to prevail. That could change.

With that as an overview, and wanting to help, I appreciate the fact that we have the prime sponsor of one of the measures with us this morning. As soon as I welcome Dave Mayernik, State Representative from Allegheny County, Ross Township section of Allegheny County, welcome, David.

REPRESENTATIVE MAYERNIK: Thank you, Mr. Chairman.

CHAIRMAN DEWEESE: David is the Secretary of the Judiciary Committee. I would like to welcome Mike Dawida and ask Mike to lead off the questions, and let's get this discussion rolling. I tell you what. Dave and Karl and all of you, just sort of come up. Come up around the table in a semi-circle, please. We got lots of time, so I congratulate everybody on sparing us the time. We'll take a brief recess first.

(A recess was held from 11:22 a.m. to 11:31 a.m.)

CHAIRMAN DEWEESE: We're going to get started again. We have 30, 35, 40 minutes. Whatever we need. As I said, Representative Mike Dawida of the Carrick section of the City of Pittsburgh and a long-time veteran of this Committee and prime sponsor of the Bill, I suggest you lead off.

REPRESENTATIVE DAWIDA: Mr. Chairman, this is an interesting issue. We had a hearing on the surrogate method and it affected nobody. We had three cameras and radio stations and numerous people. Now, we have something that affects virtually hundreds of thousands of people in Pennsylvania but has no emotion and no TV people. So, we can, I think, be very candid with each other. I hope we can lay the cards on the table.

My interest of being the prime sponsor of a subject such as this is very simple. I am concerned about consumers. I have never been overly fond of banks. Tom, I'm sorry about that. But, since I was 12 years old, I have not liked banks or savings and loans. I come from a humble upbringing, I suppose. None of us liked banks.

What I am interested in is finding a way, a vehicle for consumers to get a better shot at this thing. My question to the opposition on this issue, and then you all on the other side can please respond, is that is this truly a turf battle where you are concerned about competition, or are there really genuine reasons why we shouldn't do anything with these Bills? Do you understand my point?

A turf battle we deal with all the time in the Legislature. That is, I have my piece of the action. I control this piece of the action. I don't want anybody in on that. And, we deal with that all the time.

Cosmetologists are fighting barbers. We deal with literally, you are not allowed to cut hair of this person. Is this that kind of issue where the finance companies don't want the banks and savings and loans creating competition, or is there a high order?

Are you providing the consumers with a good as deal as they can get?

MR. WARD: I would be happy to respond.

CHAIRMAN DEWEESE: I think for the record, this is David Ward. And when anybody -- so Susan will have a good idea who is who and what is what, whenever you respond, please give your first name even if it is the second or third time.

MR. WARD: Felix reminds me that I can get emotional about this.

REPRESENTATIVE DAWIDA: This Chairman got real spent the other day. We saw it all; raw, naked emotion.

MR. WARD: This is a turf battle in one sense. As I tried to say, the lien priority law is a fight between creditors. The borrower has defaulted on his loan, lost his security, being sold at foreclosure. You are splitting up the proceeds between creditors. That is what the fight is about. In that sense, it is a turf battle. It's deciding who wins or who loses in the creditors. When you back up, that has some impact on how you make these loans

and how you engage in this business.

I think that from our perspective and I think this is quite few, that Felix Cohen and myself are the only two people here that represent people who are really in this business and have been in this business for a long time. When Mr. Wenk was talking, it seemed to me he started out the same. Maybe I misunderstood. That this Bill is going to authorize for the first time, open-end mortgages in Pennsylvania and give it its first imprimatur as a valid way of doing business. I'd point that out.

We started this business in 1975. I am a Pennsylvania lawyer, a member of the Bar. I participated in and was very close to the drafting of the secondary mortgage loan law of Pennsylvania which was adopted back, I think, in 1980 or '79.

MR. COHEN: Proposed in '79, adopted in '80, effective in '81.

MR. WARD: I helped write that law. We have been in the business. We're doing business under this obligatory advance concept today. If there is a borrower issue, it's attempted to be proposed as though it's necessary to change the law so the borrower can break into the loan and limit the secondary mortgage loan that's on the books, the open-end loan, and get in there and borrow from another borrower.

I don't know the numbers in Pennsylvania because I didn't look them up. I have looked recently in California where we did exactly the same kind of business. In California last year, in '86, we had 700 million dollars of loans paid off that are exactly like this. Seven hundred million dollars paid off by competitors. That's breaking into the loans. In Pennsylvania, that number, we got 85 million outstanding which probably is in the neighborhood of 25, 30 million dollars were paid off by creditors in Pennsylvania last year. It got to be.

There is no problem there from a consumer point of view as far as I can see. Nobody in this room has said that they want to get into the third mortgage business. But, when you give these notices under this 1249, when you give your notices, you are always making a third mortgage loan. You are not making a second. You are leaving the second on the books. You are making a third mortgage loan. Then the guy can come along and give notice to the third mortgage and the second mortgage lender and make a fourth and fifth.

Why do that? Doesn't make any sense. What you do in the lending business is pay that guy off, that prior lien, and make the loan at a better rate in a competitive fashion. It happens every day.

REPRESENTATIVE DAWIDA: Mr. Wenk, he mentioned

you. Do you want to defend yourself?

MR. WENK: I will make an observation at the outset. In his testimony, Mr. Jackson made some frequent references to PBA. I think that a note should be made that's the Pennsylvania Bar Association.

CHAIRMAN DEWEESE: This Committee is aware of that.

MR. WENK: And, not the Pennsylvania Bankers'. The second thing I want to call to your attention is of the five people who testified this morning, I am the only one that suffers the disadvantage of not being able to pack the name Esquire.

CHAIRMAN DEWEESE: Neither does the Chairman.

MR. WENK: Welcome aboard. I would defer, therefore, on legal considerations to others. But, I do note in reviewing the information that was prepared by your Committee with respect to today's hearing, that in the Bill analysis covering House Bill 1249, the second paragraph of the analysis section leads off with the following sentence. The Bill contains certain protections for the borrower as well as for other potential creditors of the borrower.

I reviewed the Bill analysis of House Bill 1586 and found no conflicting statements. Our position is that the borrower is entitled to control his borrowing. He is entitled to shift his allegiance from one lender to another,

and he should be entitled to reduce the amount of any open-end mortgage to the amount of the outstanding balance at any time if he so chooses to do. That's what we have tried to provide for the borrower and in our version of 1249.

REPRESENTATIVE DAWIDA: Mr. Ward.

MR. WARD: If I could point out that the borrower today, under existing common law in Pennsylvania, has absolute right to limit the amount of advances on open-end mortgages with the obligatory advance concept of basic fundamental law of Pennsylvania.

CHAIRMAN DEWEESE: Say that again, please.

MR. WARD: I will elaborate. By giving actual notice to the creditor and saying, I do not want any more money under your loan, that guy is cut off. Now, we just litigated this in Pennsylvania.

CHAIRMAN DEWEESE: That's contrary to testimony we heard earlier then.

MR. WARD: If I can give you a brief hypothetical fact situation in litigation. You have a lender with us with an open-end loan under current law. The borrower, the second lender, gave us notice, sent us a letter and said, your borrower has taken a loan from us. He doesn't want any more money from you. Here's your check back, case closed.

Our manager called the guy up. They went ahead and made the loan, the second lender. Our manager called him

and said, hey, we got a good line of credit. You can get more money from us too, and I will still have priority if you want the checks. The borrower said, heck, that is a good idea. We sent him the checks. The borrower cashed the checks. He is now later in time, but it should relate back under the open-end law.

We got into a priority situation when there was default. We lost the case. We did not have priority as to those later checks because we had actual notice that that borrower had borrowed from someone else and recorded a mortgage. That's the law. It always has been. It is consistent with the obligatory advance concept. We lose. We don't get priority, and that the second lender gets priority and the borrower got his money from both of us.

Our manager was wrong. He didn't understand our rules and violated our rules, and we lost the money because of it. That's the law today. The borrower can get out from under this any time he wanted to.

REPRESENTATIVE DAWIDA: Any comment?

MR. BREAUX: I am not aware of the case. Was that case reported?

MR. WARD: It is not a reported case.

CHAIRMAN DEWEESE: Babette Josephs from Philadelphia, member of the Committee. Was that question answered satisfactorily?

MR. BREAUX: Yes.

CHAIRMAN DEWEESE: Bob Jackson?

MR. JACKSON: This is Bob Jackson. In view of your question, I think it is important to explore for a moment whether or not the contract to advance those later sums made that advance obligatory.

MR. WARD: The second advance in this situation made after that actual notice was received as the Courts say and correctly is no longer an obligatory advance because the contract is in effect been breached by the borrower. He has given up his right to draw down money on that account, and you have -- as a first lender, have been relieved of the obligation. Therefore, the advance that is made later becomes a voluntary advance and does not have priority. That's the way the law works. It's very simple, understandable, morally correct in my opinion, justifiable and we shouldn't change it.

CHAIRMAN DEWEESE: Babette and then John Connelly, Special Counsel to the Committee. Babette.

REPRESENTATIVE JOSEPHS: Mr. Ward, if the lender -- if the borrower in your hypothetical does pay off the first lender when he or she borrows from the second institution, what is that procedure? What do you have to go through?

MR. WARD: Under the secondary mortgage loan law, regardless of whether it's open-end or closed-end loans, it

doesn't make any difference, when you pay off your prior lender, prior secondary mortgage lender, that lender under Section 6614(g) of the secondary mortgage law referred to in my testimony is required to release that mortgage as of record within ten days of receiving the payment and the notice to close the account.

MR. JACKSON: And, request that it be closed.

MR. WARD: And, request that it be closed.

REPRESENTATIVE JOSEPHS: If I am the homeowner, I need a check from the second person I am borrowing from?

MR. WARD: Yes. You need a check and send the check with a letter to the prior borrower.

REPRESENTATIVE JOSEPHS: And, some type of form I would probably need --

MR. WARD: Simply a form letter.

REPRESENTATIVE JOSEPHS: I would consult an attorney for that. I should consult an attorney?

MR. WARD: No. That next lender, the competitive lender is the guy who is going to do this for you because it's his own interest to have that loan paid off. He wants to clear that record. He sends that letter off and this doesn't have anything to do with open or closed-end, any mortgage. He got to send that off and get that loan paid off and out of the way. Then he makes a record of his own mortgage. That's how he assures himself that that loan is

no longer a priority problem for him because it's been paid. Is this the way the system works today. That's how those 700 million dollars of loans referred to in California and whatever number in Pennsylvania which I failed to check get paid off all the time. I guarantee you today some place in Pennsylvania, we're going to get a letter and a check on an open-end loan and pays us off and closes that account.

REPRESENTATIVE JOSEPHS: I have done this myself. I wanted to clarify that. Thank you.

CHAIRMAN DEWEESE: John Connelly, Special Counsel to the Committee.

MR. CONNELLY: Mr. Ward, the factual situation you are talking about involves existing trial Court decision in the case; is that what you're talking about?

MR. WARD: Yes.

MR. CONNELLY: Did this involve the payoff of the existing balance to your company or merely stopping the line of credit? The letter that was received by your company was a letter from another lender?

MR. WARD: Yeah.

MR. CONNELLY: That factual situation seems to be a clear distinction. You don't have notice from the borrower. You have notice from a subsequent lender who is not a party to that contract.

MR. WARD: No. The notice is from the borrower.

Notice from the lender doesn't mean anything.

MR. CONNELLY: I thought you indicated that came from the subsequent lender saying here's your check. He's borrowing from me.

MR. WARD: I think I was speaking loosely. That letter will have to be signed by the borrower. A notice from another lender doesn't mean anything. Our contract is with the borrower.

MR. CONNELLY: This borrower who sent back the check saying, I don't want any more credit line, I'm finished --

MR. WARD: Correct.

MR. CONNELLY: -- went to a subsequent lender who loaned money and your manager said, well, we still have this line. All right.

CHAIRMAN DEWEESE: The letter was prepared by the second lender?

MR. WARD: Yes, I think it was. I am sure it would have been. That's the normal competitive way.

CHAIRMAN DEWEESE: Mike, again, your line of questioning?

REPRESENTATIVE DAWIDA: I want to hear -- it sounds to me like this Court case does something to lessen the need for our legislation.

MR. BRENNAN: Sure. You get a law suit. It's

not going to help banks, mutual savings banks, S&L to be reassured that if you go into Court with an open-end mortgage, you are going to win. That's exactly the real-life meaning of what is in the bank's statement about something that is reliable. Now, in point of fact, that is pretty slippery stuff to try to bet on that. Take Ms. Josephs' case or any man and woman walking out on the street here. If they have on record any mortgage which under either Bill is going to be called open-end mortgage, the next lender coming along, let's say that person out here sees signs around from Union Trust or Equibank or Mellon, Pittsburgh National, and offering a deal and say, wow, I would like to get in on that. I got a property that goes $30,000 of equity, and I got this $5,000 mortgage outstanding on an open-end mortgage.

What has to happen? That person has to go to that bank, to that first open-end lender who says, I want my $5,000. You get the $5,000 back. But when and how? They then go to Pittsburgh National and say, to take an example, we're going to get rid of this open-end mortgage. You got to inform the guy sitting at the desk or inform the woman sitting at the desk. They are going to say, oh, yeah. Well, while that mortgage is on record, if we lend you on the basis of a mortgage, we run the risk of anything that happens in between. Who is going to come ahead of us? Our lawyers who don't seem to be able to read the law, in fact,

this is true throughout all of Pennsylvania with all the big banks I can assure you, they will tell you that that is very, very risky to rely on that second mortgage with an open-end purporting to be obligatory on the record.

Because if the first open-end mortgage has another advance made on it, you are going to lose it. That's why you are not seeing a whole lot of banking programs. They are in place. It's not just finance companies making open-end credit loans. They are being offered in a very limited way. In most cases, the open-end mortgage is being offered to customers for whom the banks don't really need the mortgage. Number one are the customers.

REPRESENTATIVE DAWIDA: That brings back my original thought. First you, and then you. How do the customers, consumers, benefit?

MR. BRENNAN: When this deadlock developed, we reached for the Ohio statute. I put this together, and this came off the xerox machine after which a couple extra items were added. We are told that the banks start putting open-end clause routinely in every mortgage. We don't know what banks would have done that. It's beyond our imagination. We got rid of that problem. We excluded purchase money first mortgage. We got a complaint that the time period for the notice was not enough for somebody to cut an open-end credit line. We made it five business days which is

longer than the Ohio version.

But the critical point here is that you are talking about a customer, a person walking up and down the street here, who has went on record to be able to do something conveniently, quickly and in a way that the second borrower or second lender strike that, the second lender is going to be able to really put out cash and say, I got a good position on that property.

We're not here to stop anybody from doing business by any means and we are here very much to hope that we can get into the business in a way that the banks can not today do on the advice of their lawyers whether in Pittsburgh or Philadelphia or Bethlehem or Erie or Williamsport or Harrisburg. It's coming in the same way. It's relatively easy for lawyers to get to that conclusion when you see some of the devastating cases that are recorded cases.

REPRESENTATIVE DAWIDA: Counselors Ward and Cohen, why wouldn't consumers be better off with more people in this field?

MR. WARD: They will be, and they are in the business. To say that they are not here in Pennsylvania is crazy. Savings and loans and banks are in the business in a big way.

MR. COHEN: I get one in the mail every three days.

MR. WARD: Let me tell you this. If we're going to just xerox the law which there is not much now of this and that to be somewhat sarcastic, if we're going to xerox the law, let's go xerox New Jersey. New Jersey law which was passed about two years ago was essentially identical to 1586 with the construction loans, apart from the construction loan part of it which wasn't. It didn't have the same issue over here. But on the revolving loan side, it's essentially identical to 1586. Believe me, you have the most active second mortgage market in the State of New Jersey with the banks, savings and loans, financial companies, and I will bring you the Star Lender any day of the week from New York and show you that thousands of ads of competitive rates. They are knocking our socks off on rates. It's one --

CHAIRMAN DEWEESE: Banks are?

MR. WARD: Yeah, they are beating the hell out of us.

CHAIRMAN DEWEESE: What is the competitive situation in Pennsylvania with banks and financial companies?

MR. WARD: The same thing. We're having trouble. We're an inefficient lender, if you will, in this business. We have trouble competing because of it. The lien priority law in Pennsylvania, in fact, would help us lock out some of the competition. We don't believe in passing laws that

way. We simply do not.

MR. BREAUX: I would like to respond.

CHAIRMAN DEWEESE: Real quickly though I want to ask a yes or no question and then you can respond.

Mr. Wenk and Mr. Brennan, you are or are not competitive with these folks?

MR. WENK: We are not competitive in the minimum amount of credit which we will consider under one of these loans. We do not rely upon collateral security that would tie it up so it can't be used elsewhere. There are many banks in Pennsylvania who refuse to make revolving credit loans secured by real estate for the reasons Mr. Brennan pointed out. Typically, you will find the smaller communities where that type of facility is probably needed, even more than in large cities.

MR. BREAUX: The only way to make loans with future advances is to rely on the obligatory advance doctrine, and it's just too risky to rely on the doctrine. There is too much uncertainty in that doctrine. And, that's why many institutions in Pennsylvania are not offering them. If legislation would pass that cleared up those uncertainties or eliminated those, you would have many more loans in this field.

I think the consumer benefit comes in in that this is a product that consumers definitely want. These

Bills would help additional lenders to offer the product at a better rate for consumers because, a, it's secured lending and it gives the consumer some tax benefits in the Federal tax statute. And, because the risk is less, the rate is going to be better. There is very definite consumer benefit here in enacting this legislation to clarify this area of obligatory advance doctrine because you never can know without the losses at the end whether or not an advance is obligatory or not. You got two good Bills before us now. I see no need to go look at New Jersey, New York or some place else. We have been working on these for many years.

MR. BRENNAN: You got a state a few miles away where you got a whole generation of experience here.

CHAIRMAN DEWEESE: One quick thing and then John Connelly and Mike Dawida.

Ninety percent of the country isn't doing what Ohio is doing?

MR. BRENNAN: I am not sure. Maybe we should do research.

CHAIRMAN DEWEESE: That's not my statement. That was somebody else's.

MR. WARD: I made the statement.

MR. BREAUX: More and more States are passing laws to address this issue of obligatory advance doctrine to try to get rid of the uncertainties in that doctrine.

CHAIRMAN DEWEESE: John Connelly and then Mike Dawida.

MR. CONNELLY: Mr. Breaux, what are the uncertainties that you perceive? Let me give you a factual situation. An individual has $30,000 in equity in a piece of real estate and gets a traditional home equity type loan, second mortgage with a checkbook, checkwriting authority up to the $30,000 and a second mortgage recorded in that amount. Is that obligatory?

MR. BREAUX: It probably is to begin with. There is a lot of conditions in the loan agreement. For example, the borrower must repay the loan by a certain date. Maybe makes a payment once a month. Suppose the borrower makes his payment on the fifth of the month. He is five days late. He is delinquent. Is he in breach of the contract? That raises the question, is the loan obligatory.

If I make an advance after he fails to make a payment on time, is he in default or maybe missed the entire month's payment. But I know he is good credit. I am going to make an advance anyway. There has been an intervening creditor's lien. He takes the position that my subsequent -- my future advance does not relate back to the date of recording of the mortgage because my lien, my advance, was not obligatory because my borrower was in breach at least technical breach under the contract. I didn't have to make

it non-obligatory, and therefore, I am at a loss.

MR. CONNELLY: It sounds like Mr. Ward's litigation exactly.

MR. BREAUX: I don't think it is at all.

MR. WARD: May I make a comment?

CHAIRMAN DEWEESE: Please.

MR. WARD: 1586 fixes that problem. It clarifies what conditions can happen and what happens when there is.

MR. BREAUX: Precisely. But common law does not.

MR. WARD: It clarifies what the common law cases have decided over long periods of time. It really resolves the uncertainty and would allow any savings and loan to do this business with a great deal of confidence in what can and can't be done under open-end contracts.

MR. CONNELLY: The difference between the two is the obligatory versus non-obligatory open-end mortgage; is that correct?

MR. BREAUX: I am not sure that it's that simple because it seems to me that the approaches are different, but the result is the same. As I said earlier, in 1249, the distinction between obligatory and non-obligatory is dealt with honestly by saying we got to get rid of this until we get notice from the borrower that we want to terminate future advances. 1249 purports to maintain that distinction between obligatory and non-obligatory. It really doesn't. It expands

tremendously the definition of obligatory.

MR. BRENNAN: You are getting rid of an uncomfortable fact by trying to say it isn't so. We can reserve all kinds of discretion.

CHAIRMAN DEWEESE: The gentleman from the Pennsylvania Bar Association, Bob Jackson.

MR. JACKSON: Thank you, Mr. Chairman.

At the risk of bringing down the owl of both sides and not having a stake on either side in this particular debate, it occurs to me that there is two issues that we're discussing here. One issue has to do with giving a broader definition and more latitude and more certainty in what is obligatory and what is non-obligatory. I think both sides agree that that's a good effect.

MR. COHEN: That would be helpful.

MR. JACKSON: That's helpful for everyone. It seems to me where the divergence is is whether or not there should be a mechanism, a statutory mechanism, to put certainty into the termination of a lien.

CHAIRMAN DEWEESE: Notice?

MR. JACKSON: Whatever that is. In 1249, it's a notice mechanism. It seems to me that the banks are happy with the prospect of having either Bill in terms of giving them some certainty in their lending policy with respect to obligatory. But it seems that the opponents of

1249 are suggesting that if you create a very easy mechanism whereby an entrant into the business can simply give a form notice to the prior lender that it stops here which the banks would like to see because then they would know where they stood with respect on the record to future lending. This would open the door to some sort of competition that heretofore didn't exist, or would be damaging to your industry.

MR. COHEN: No.

MR. WARD: No.

MR. JACKSON: It seems we have one issue.

CHAIRMAN DEWEESE: How would you do that?

MR. JACKSON: How would I do it? I think you ought to have a mechanism.

CHAIRMAN DEWEESE: If you were up here with me and Babette and Mike.

MR. JACKSON: If I were sitting there, and again at the risk of wreaking the ire of everyone, I would definitely suggest you need a mechanism, a certain mechanism, a sure mechanism, whatever you choose that to be whereby a lender, a consumer, can know how he can stop this revolving line and freeze the balance, and the subsequent lender can know with certainty how he can then step in in a junior position. I don't see that that's wrong in any sense. That's what our laws are all about, notice. Going into a

transaction with your eyes open. That's motherhood and Girl Scouts.

MR. BREAUX: The ability not to be locked in.

MR. JACKSON: But, I think you have one issue here. The issue is, do you put certainty in the cutoff. That seems to me to be the issue.

MR. BRENNAN: You haven't made us mad yet.

CHAIRMAN DEWEESE: The visage of the gentleman, Mr. Ward, looks quite constraint, however. Go ahead.

MR. WARD: I think there is one issue here. The question is, do you reward a creditor for taking no risks. That is the issue. This is a risky business, guys. I say it to the savings and loans and banks. There is no way to get into the open-end lending business without taking some risks. That's why you get paid. And, damn it, if there is no risk, you shouldn't get any money. It's a risky business. Clarity at all is fine. 1586 gives you some clarity. I want to refer to a section in 1249 that I haven't brought up before. My written statement says it makes my head hurt.

Subsection E of Section 8143 on page four of the Bill says this section is non-exclusive and shall not be construed to change existing law with respect to the priority of the lien or advances made pursuant to a mortgage, except, except, except. This says to me that if you got two or three

or four competing creditors where we're sitting there divvying up the spoils on the foreclosure, that one set of laws is going to apply to Beneficial if I write my contract with obligatory advances and where I take some risks and if the banks take no risk and write theirs without any obligatory advances but open-end, they apply another set of priority rules. Now, you are going to be sitting there with two different types of lender, banks or whoever it might be operating under two different sets of rules with one fact situation.

CHAIRMAN DEWEESE: You are saying this would not be good law to have two things?

MR. WARD: It's mind boggling to me. How's a judge going to resolve which priority law does he apply to which advance, et cetera, et cetera.

CHAIRMAN DEWEESE: Legal counsel, Mr. Brennan and Mr. Jackson, because that's something that I don't understand either.

MR. BRENNAN: I think the Hoosiers across the way were very, very smart to have put that in.

CHAIRMAN DEWEESE: Buckeyes.

MR. BRENNAN: It turns out today you hear from lawyers who are perfectly happy with the existing laws. It works just fine. There are some others of us who don't think that and have never thought that, and we certainly do

support the Bar Association insofar as construction mortgage loans are concerned. It ought to be changed. But, for those who are unhappy today with the obligatory future advance doctrine, this keeps it for them. There is no problem with having both, a voluntary and an open-end.

If there is existing business going on as we hear about going on, it can continue right under that under the perfectly lovely law we have today. But, in the meantime, you will have done something through what the Ohio people proved through experience can work which justifies using a copy machine to get the benefit of it and not try to invent something brand new.

REPRESENTATIVE DAWIDA: You haven't answered his question. Maybe Mr. Jackson will.

CHAIRMAN DEWEESE: We're going to continue ten more minutes. At 12:15, I will adjourn the meeting.

MR. JACKSON: I don't think this is an unusual provision in legislation. You have a lot of mortgages other than this kind of mortgage. There is a lot of other kinds of mortgages. I think that a clear import of that language is, for example, the Bill itself is an amendment to an existing priority lien statute. It's not new. It's an amendment. What we're doing is reserving all of the other liens of all of the other mortgages as they are provided in the statute case law. It's simply saying when you are dealing

with this kind of an advance and you have these kinds of questions that are posed in the conditions, the enumerated conditions, then you have this kind of priority. So, I don't think that's needed.

CHAIRMAN DEWEESE: This language is as repugnant to you as to Mr. Ward?

MR. JACKSON: I think it's absolutely necessary language.

CHAIRMAN DEWEESE: It's a challenge of being a non-lawyer Chairman of the Judiciary Committee.

MR. JACKSON: Unless some Court would like to take this language and extrapolate it into another kind of mortgage.

CHAIRMAN DEWEESE: Mike, did you have something?

REPRESENTATIVE DAWIDA: I still haven't heard the answer. Obviously, I am not on your side, but I haven't heard it.

CHAIRMAN DEWEESE: Mr. Breaux.

MR. BREAUX: I was going to say as a person that didn't draft either of the Bills, it seems to me the language in Section 3 of Mr. Ward's Bill does the same thing of the section that he is criticizing. Maybe he can tell me where I am wrong. But, Section 3 of 1586 appears to do essentially the same thing unless I am incorrect.

MR. WARD: Section 3 is a grandfather clause, if

you will, of saying it doesn't apply to existing loans. What this says is, if the existing law, and there is a contrarying different existing law that applies to open-end mortgages today, stays in effect, that's what that says. That law stays in effect, not changed now, you got open-end lending with two sets of priority law.

MR. BREAUX: I read both as being from the grand-fathering clause.

MR. JACKSON: I think --

MR. WARD: I may be wrong, but the judge is going to have to decide it.

CHAIRMAN DEWEESE: That's what we're doing here. You folks want some sort of statutory clarification rather than a judicial vitriment on what is obligatory.

MR. WARD: Could I have one final --

CHAIRMAN DEWEESE: Or you don't. You do or you don't.

MR. BRENNAN: That's very essential. I couldn't stress more that we think to bring definite to this and reliability is really very, very crucial and that this system will permit you to do that. What objection it would be to the public would not to be able to chop off an existing open-end mortgage is not something that we can share very readily.

CHAIRMAN DEWEESE: David Ward.

MR. WARD: One final comment. If we're going to just adopt somebody else's law, which is what Mr. Brennan suggests, let's try New Jersey. That works, and everybody is happy with it. In Ohio, the Ohio Financial Services is an association that is actively trying to repeal that law because it doesn't work. The notices are not given. They are not complied with. Nobody really understands what the law is. They're trying to get rid of it. It doesn't work in Ohio. I reject that.

MR. BRENNAN: The only reason Ohio was selected was it answers the point of objection which immediately strung up on the Bar Association, put a Bill in only with construction admittedly and certain agreements on that. But, consumers consult and there was a Mexican standoff that developed very quickly as to what the affect was going to be on competition.

CHAIRMAN DEWEESE: Still going on today, the Mexican standoff?

MR. BRENNAN: That discussion came. The idea of copying what the Ohio system was. New Jersey doesn't have such a thing. No New Jersey law is going to satisfy it. The Bankers' Association people have stuck on this as the consumer discount companies have been stuck on saying it shouldn't be there. It is 99 and a half percent competition. That's what's involved.

CHAIRMAN DEWEESE: Bob Jackson, Dave Ward and then Mike Edmiston and then we're going to end up unless Mike Dawida or Babette has something else.

MR. JACKSON: Bob Jackson on the Pennsylvania Bar Association.

It's necessary that I say that in light of the discussion.

CHAIRMAN DEWEESE: An objective person here in the room.

MR. JACKSON: If I might suggest this. Any language deficiency in this Bill such as the retaining provision or the provision that retains existing law in other mortgages can be cosmetically corrected. That's not a big problem. There is no debate on that. I don't think anybody wants to keep respectively the old law having to do with the vaguitries of whether you have an obligatory or non-obligatory defense of advance. Everybody that I know of wants to get rid of that. It seems to me that your Committee has got to wrestle with the gut issue of whether or not you are in favor of having a mechanism to cut off borrowing that the borrower relies on and subsequent lender relies on. You can debate that issue all day. The sides are both good. But, until you wrestle with that issue and land that issue, I don't think you can resolve this. I think that's where it is. The language is easy. I would volunteer my

committee to do the drafting of any changes working in harmony with the two groups, assuming that that issue could be resolved. I think you got to resolve that.

CHAIRMAN DEWEESE: Again, speaking from a pure politician's perspective, what if there aren't enough votes in the Legislature either side of the building and not any inclination on the part of the Governor to go along with either side, what if we made everybody, not everybody, but these folks probably wouldn't be as happy as these folks would be, what if we did something with the construction loan aspect of these Bills and continued to march? Now, these folks could continue to lobby, and phase two that we didn't get solved would have to be reconciled at a different time. Again, from a pure politician's point of view, if these people have a problem with construction loans, and these people do also, maybe we can solve that one, and then phase two, the Mexican standoff to use the gentleman's Hispanic metaphor, will perpetuate.

MR. JACKSON: The Bar Association would certainly support that position.

CHAIRMAN DEWEESE: That was my question, and that's a good answer, I think. Okay. Now, David Ward, and Mike Edmiston and then, we'll close it off. We're almost on time.

MR. WARD: Two quick comments. I think Mr.

Jackson's comments were well reasoned and are academic. He is not in the business and doesn't have a problem. I don't think the borrower's notice thing is a major issue, and I don't think you have any evidence to show that it is. I want to just say on competition, I don't want anybody to have the impression on the Committee that I am here trying to defend some competitive advantage that we would have. That is absolutely not the case.

CHAIRMAN DEWEESE: They think it is, right?

MR. WARD: If they do, they can't articulate what my competitive advantage is over them under existing law or if 1586 passes. I would like to hear an articulation of what Beneficial's competitive advantage is going to be. It doesn't exist.

I can pose on the other hand a major problem to the borrower in the same notice provisions. It's something he is not obligated to do now to protect his rights, but would be obligated to do to get into this morass of notice if you pass 1249. We're not in here looking to save some special competitive advantage we have. It's absolutely not true.

CHAIRMAN DEWEESE: The advantage you have some people would say is the fact that you are taking the risks.

MR. WARD: We're willing to take the risk in the business. We have for the past 12 years, and it works. We

would like to see that law clarified to reduce those risks which 1586 definitely would. It would reduce the risk to a very manageable level. It does not eliminate risk. That is just not possible.

CHAIRMAN DEWEESE: Michael Edmiston, Chief Counsel.

MR. EDMISTON: I have a question that I particularly would want to hear the response from Mr. Brennan, Mr. Wenk, and Mr. Jackson. As to 1586 and the conditions that it sets forth in developing its concept of what's open-end obligatory agreements that are set forth on page two, I am wondering in particular, Mr. Brennan and Mr. Jackson, how you would characterize that listing of conditions in a context of the case law as you understand it to have developed to this point. Do you see an expansion? Do you see language that is so new or different to the guidelines the Courts have provided us as to present more problems than answers?

MR. BRENNAN: You know, you can't be dogmatic about what the Courts are going to do in the future. But, that is a very strong objection we have to trying to have what is essentially a self-contradictory definition to say something is obligatory when it clearly wouldn't be obligatory. This goes so far that the lender can even go out of business. Now, what is a guy or gal with the second mortgage

on the record, open-end mortgage, blockades any other loans against that property does the day they walk down the street and sees out of business is left to the imagination. But, there is so much latitude in this, and I think it's an essential flaw in saying what is really discretionary is now going to be called obligatory under our statutes which breeds nothing but a lot of trouble. We think the Court at a real risk would make shredded wheat out of it.

MR. JACKSON: I disagree with that. I disagree for this reason. As lawyers, we get these kinds of words to work with. At least to me, it gives certain comfort. I can go not to the limit, but I will sure go a lot further with these words as I would without them. There is no mathematical certainty. But, by the same token, I will direct your attention to what are even more negative words.

MR. BRENNAN: Before you leave yours, you mean to say something obligatory without any restrictions whatsoever on what you can declare to be default --

MR. JACKSON: If the Legislature says it is, it is. Let me suggest to you, if you look at 1249 and you look at the words used there with respect to obligated, they say the occurrence of non-occurrence or the existence or non-existence of any fact or circumstance. I would like you to show the distinction to me of the definiteness of that as opposed to the definiteness of this. In my view,

for whatever it's worth, both of these Bills handle the obligatory, non-obligatory situation not perfectly but 150 percent better than we have it today. It gives me, as a draftsman, a whole lot of comfort to have this language to rely on.

CHAIRMAN DEWEESE: Plus they help with the construction loan problem.

MR. JACKSON: Absolutely. I think either one will get me out of the bin.

MR. CONNELLY: Just a point to be made.

CHAIRMAN DEWEESE: The last point, and I'll sum it up.

MR. CONNELLY: I think everyone agrees here the Court has made law where there is a statutory gap. Would we all agree to that? What we got now is the uncertainty from the banks' point of view what the Court is going to do next with each individual factual situation. That's the risk you people maintain you are taking that you people at this point aren't prepared to take. If this Committee passes some statutory language, the Court is constrained to interject their own opinion. I think they have done it in a legislative void. But, as a passing comment, we're now left with filling the legislative void. It's a question of how clearly we can fill that gap.

That, as I presume, Mr. Ward, is the risk that

you continue to discuss you are taking. The risk of what the Court will do with the existence of circumstances.

MR. WARD: That risk is there. There is absolutely no question about it. I don't think the Legislature, at least on the evidence presented to them, should say, hey, the Courts have been all wacky on the way they have done it in the past 100 years in Pennsylvania. Let's throw it all out and start out with a new concept. That's what 1249 does.

MR. CONNELLY: That's clearly a legislative perogative.

MR. WARD: Absolutely, it is. It seems to me that the Legislature should look at how the law developed in a workable, practical sense that does in fact work today.

MR. CONNELLY: The concept is starried decisive legislatively rather than judicially. I think that would to some degree stifle progress.

MR. BREAUX: Mr. Chairman, could I have 30 seconds?

CHAIRMAN DEWEESE: Yes, sir. Then, that's it.

MR. BREAUX: I think the pressing need for legislation is probably from the person in the area of home equity loans rather than construction lending, although we need it in both. Construction lending has been there for decades. Lenders pretty much know Court cases. They know how to deal with it. There is a greater degree of certainty

in that area because it is a much older area than the area of home equity lending. That's why I am not sure I would put my priority totally on construction and let home equity loans go by the wayside. Consumers want home equity loans. I think the lenders of Pennsylvania ought to be able to offer loans to them with a reasonable degree of certainty.

CHAIRMAN DEWEESE: I appreciate very much your input and Mr. Jackson's input because they are arguments that have some degree of neutrality about them, some degree of neutrality about them. Obviously, we need that kind of input. I will say it for the third and final time during this hearing, but I say it as a pronouncement at most of our gatherings.

We are politicians and we have to come up with something that is going to pass. Something that is going to be agreeable. Mike knows it very well, and so does Babette. We don't have support, we don't have votes, then what we're doing is wasting our time and your time.

So, on scale of ten, even if your comments are blazingly accurate, we would still be advancing three or four points on that scale if we took care of the construction problem because it's in both the Bills. With Mr. Jackson's legislative ledger germane and ingenuity, we might be able to come up with some language to take that up to maybe four and a half or five on the scale with some other language that

could be agreed to.

I don't think we're going to come up with a solution that is going to make everybody happy except probably the people on the right-hand side of the table because if we do nothing, they are exultant, I guess. Not exultant, they want to move a little bit forward.

MR. COHEN: We like certainty also.

CHAIRMAN DEWEESE: The bottom line proverbially is as Chairman, I am not being bombarded and I don't know whether Mike is or not, and I don't know if Mr. Caltagirone who is the sponsor -- by the way, Mr. Caltagirone has another Bill being considered by another Committee in another part of the State. That's very unusual to be the prime sponsor of two Bills at one day.

But, anyway, Tom could not make it today. So, I apologize for his absence. But, I am not getting pummelled by people in my office whether it's mail or phone calls or personal visits saying that we have a cataclysmic problem in the Commonwealth. I am being talked to by representatives of each side as well as savings people and the Bar Association.

So, we're going to move forward hopefully to help rectify this problem and probably with some input from you gentlemen and ladies in the Pennsylvania Bar Association. But, until Mr. Dawida's side of the issue or Mr. Caltagirone's side of the issue, and I think in fairness to both of them,

they have put forth legislation, but they are not from the discussions I have had, locked in stone. They are willing to modify and be flexible and be sensitive to some changes.

Unless there is an overpowering wave of feeling that one Bill is preferable to the other Bill, I am going to sit down with Mr. Dawida, Mr. Caltagirone and work out something to at least take this problem up a few steps because that's the obligation as I see it. Now, if the bankers have -- again, I am talking as a politician. If they have 50, 80, 100, 150 representatives banging on my door saying this is a good idea and this is not such a good idea, then it's a different story. Especially if there is a simultaneous effort in the Senate.

I don't want to waste anybody's time popping out something that is going to be emasculated on the floor and rejected by one of the chambers and not embraced by the Governor. But, I think we can advance.

With that conclusion, thank you very much. The public hearing is in recess until after lunch when we will come back and take up House Bill 219 which deals with assaulting athletic officials.

(Whereupon, the hearing terminated at 12:26 p.m.)

I hereby certify that the proceedings and evidence taken by me at the Public Hearing on House Bills 1249 and 1586 of the House Judiciary Committee are fully and accurately indicated in my notes and that this is a true and correct transcript of the same.

Susan L. Mears

Susan L. Mears, Reporter/ksh