Memorandum

To:	Alaska Industrial Development and Export Authority Randy Ruaro, *Executive Director* Mark Davis, *Special Counsel*
From:	Thomas Toepfer, *Managing Director*, PFM Financial Advisors LLC Matt Schoenfeld, *Senior Managing Consultant*, PFM Financial Advisors LLC
CC:	Leslie Krusen, *Partner*, Orrick, Herrington & Sutcliffe
Date:	April 25, 2025
Re:	Financial and Credit Rating Considerations of House Bill 53 and Senate Bill 57

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Background

The Alaska Industrial Development and Export Authority (AIDEA) is a public corporation of the state of Alaska and exists as a separate and independent political subdivision within the Department of Commerce (AS 44.88.020).

AIDEA's statutory mission is to **create economic development and jobs**, to fight unemployment which the legislature found to be a "serious menace to the health, safety, and general welfare" of Alaskans in areas of high unemployment and the entire state. AS 44.88.010(a)(1) and (a)(2). AIDEA pursues this mission through its Loan Participation Program and the Direct Finance Program, along with a number of other financial tools (AS 44.88.080).

AIDEA Dividend Statute and Rules Based Payments to the Treasury

For over 28 years, the Alaska Legislature has followed a tradition of a rules-based system for payments from AIDEA to the state Treasury in the form of a dividend formula.

In 1996, the legislature passed Senate CS for CS for HB 526 (FIN) AM S. The bill established the AIDEA dividend statute in law. Per AS 44.88.080 AIDEA pays an annual dividend to the Treasury of at least 25% but not more than 50% of unrestricted net income. The legislature has control over how the dividend funds are used through the appropriations process.

The legislature intended this rules-based system to provide the Board of AIDEA with some authority to set a dividend amount between the "goal posts" of 25% and 50% net income, while insulating AIDEA from ad hoc draws above and beyond the dividend amount declared by the Board.

Section 1 of HB 526 entitled "FINDINGS, POLICY, and INTENT" sets out a legislative finding that (emphasis added):

> "It is the policy and intent of the legislature that the financial integrity of the Alaska Industrial Development and Export Authority remain secure so the authority can continue to fulfill its vital economic development mission for the state. The legislature finds that this Act fulfills this intent."

Consistently, following a rules-based system for fund transfers from AIDEA to the Treasury is a basic best practice for the Legislature to follow and is required to provide the financial stability AIDEA needs to invest, survive, and grow over time.

Proposed HB 53 – Introducing Significant Credit Risk through Appropriation of AIDEA's Unrestricted Revenues

Proposed HB 53 Section 8(b) reaches beyond the dividend payment stating that "all unrestricted loan interest payments, loan commitments fees and other unrestricted receipts received by or accrued to" AIDEA are appropriated by the Legislature. While in its current form these receipts would be appropriated back to AIDEA as corporate receipts, it introduces the risk that in the future these unrestricted revenues would be appropriated to other (non-AIDEA) purposes. This presents a significant risk to AIDEA's ability to conducts its business, to its credit rating and to its ability to leverage its cash flows to borrow and invest in impactful, job creating economic development projects. HB 53 Section 8(b) undermines AS 44.88.080 and the Legislature's intent of financial integrity described above.

Financial and Credit Considerations

Impact on AIDEA Credit Rating and Borrowing Cost

Ad hoc draws or appropriating unrestricted AIDEA revenues to other purposes, will have a negative impact on AIDEA's credit rating, resulting in higher borrowing costs, further straining its financial resources. After the legislature appropriated a $2 million draw from AIDEA's revolving fund in 2019, Moody's Ratings reacted severely, downgrading AIDEA's credit rating by two notches from Aa3 to A2. The rating agency voiced concern that the state could divert funds or "push funding burden" onto AIDEA. **Moody's stated that factors that could lead to further downgrades was if the state would force AIDEA "to absorb financial burdens"**.

In the current market, we estimate that the downgrade from Aa3 to A2 increases interest rates for AIDEA by approximately 0.20% on average (10 bps per notch downgrade). Diverting additional funds from AIDEA could further impact AIDEA credit rating and its future cost of borrowing.[1]

The rating agencies assess the credit worthiness for AIDEA. Similarly, banks and investors undertake their own credit review and assessment. As stated on PFM's memo supporting the initial legislation for AS 44.88.080, "any removal of revenues from AIDEA degrades the security of future payments to bondholders".[2] Ad hoc draws (on reserves) or redirecting unrestricted AIDEA revenues (beyond the dividend payments) will significantly weaken AIDEA financial integrity and hurts its ability to access the debt capital markets including direct bank lending.

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[1] AIDEA does not currently carry a credit rating as AIDEA has currently no Revolving Fund Bonds outstanding. Assumes taxable interest rates
2 See PFM's 1996 memo attached.

Impact on Revolving Loan Capacity

Diverting funds from AIDEA to pay for government services impacts AIDEA's stability and is damaging for future AIDEA operations. For instance, AIDEA provides loans as economic drivers from job creation in Alaska, and interest earned, and principal repaid on the loans can be reinvested in additional loans (revolving loan pool). We calculate that an initial $1 million 20-Year loan from AIDEA[3] with reinvestment of interest earnings and amortizing principal into new loans, would generate $3.2 million of additional loans and $2.0 million of interest income of which about $505,000[4] would be remitted to the State in the form of dividends over 20 years. In simple terms, for every $1 million of funds AIDEA can make over $4.2 million of loans in a 20-year timeframe. Diverting $1 million from AIDEA today will reduce AIDEA reach and economic impact as well as future dividends to the State which only compounds with time.

Impact on Direct Investments and Partnerships

Ensuring AIDEA funds are not diverted is critical for AIDEA to advance its mission of jobs and economic development. AIDEA often partners with project proponents or investors on projects that require substantial investments or guarantees (and currently has hundreds of millions of dollars of projects in its pipeline) including Cook Inlet projects. AIDEA must be able to maintain certainty of its reserves to be able to make these types of substantial investments. If AIDEA's funds are diverted through ad hoc draws it will limit the investments AIDEA can make and impact the trust and creditworthiness AIDEA has with its partnerships with investors, banks, and others.

Summary

Ad hoc draws and the diversion of revenues from AIDEA outside the dividend formula will result in significant negative financial consequences, including potential credit rating impacts and higher cost of borrowing, reduced lending capacity, a reduction of future dividend payments to the state, and limit AIDEA's ability to make major infrastructure investments either in terms of direct investments or in partnerships.

[3] *Assumed interest rate of 6.63%*
[4] *Assumes 25% of interest earned is remitted as dividend to the State*

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May 6, 1996

Valorie Walker
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Via Fax 907-269-3044

Dear Valorie:

I have reviewed the proposed amendment to AS 44.88.088 which provides a statutory framework for an annual dividend to the State of Alaska's General Fund from AIDEA's "net revenues". While any removal of revenues from AIDEA degrades the security of future payment to bondholders, the framework which is established in this amendment is far superior to an approach which would leave unspecified future dividends up to the annual budget process. The proposed amendment deals with several important aspects which will be regarded as strong points in the credit markets. These important aspects are:

1. The dividend approach is in statute. This is much better than having an undetermined yearly process.

2. The amendment leaves control with the Authority's Board. This will be considered important as it maintains control within the business process rather than the political process.

3. The amendment establishes a maximum dividend. Much of the concern of the credit markets is that too much will be taken too quickly. The "maximum" dividend controls the process and makes it more predictable

4. Lastly, the amounts suggested in the amendment are reasonable.

Again, the new language is much better than a yearly budget process and should help soothe concerns that have been raised by the credit markets.

If you have any questions regarding my comments, please feel free to call.

For Public Financial Management, Inc. / Gardiner & Clancy, LLC

Patrick H. Clancy