

HOUSE FINANCE COMMITTEE
March 29, 2001
2:06 PM

TAPE HFC 01 - 66, Side A
TAPE HFC 01 - 66, Side B
TAPE HFC 01 - 67, Side A

CALL TO ORDER

Co-Chair Williams called the House Finance Committee meeting to order at 2:06 PM.

MEMBERS PRESENT

Representative Bill Williams, Co-Chair
Representative Con Bunde, Vice-Chair
Representative Eric Croft
Representative John Davies
Representative Richard Foster
Representative Bill Hudson
Representative Ken Lancaster
Representative Jim Whitaker

MEMBERS ABSENT

Representative Eldon Mulder, Co-Chair
Representative Carl Moses
Representative John Harris

ALSO PRESENT

Dan Fauske, Executive Director, Alaska Housing Finance Corporation (AHFC), Department of Revenue, Anchorage; John Bitney, Legislative Liaison, Alaska Housing Finance Corporation (AHFC), Department of Revenue, Anchorage; Joe Dubler, Chief Financial Officer, Alaska Housing Finance Corporation (AHFC), Anchorage, Department of Revenue; Steve Kantor, ARIMAX Financial Advisors, Alaska Housing Finance Corporation (AHFC), Anchorage, Department of Revenue; Les Campbell, Director, Budget, Alaska Housing Finance Corporation (AHFC), Department of Revenue, Anchorage; Robert Brean, Director, Research & Rural Development, Alaska Housing Finance Corporation (AHFC), Department of Revenue, Anchorage.

PRESENT VIA TELECONFERENCE

None

GENERAL SUBJECT(S):

GOVERNOR'S CAPITAL BUDGET
Alaska Housing Finance Corporation (AHFC)

Tobacco Securitization

The following overview was taken in log note format. Tapes and handouts will be on file with the House Finance Committee through the 22nd Legislative Session, contact 465-2156. After the 22nd Legislative Session they will be available through the Legislative Library at 465-3808.

LOG	SPEAKER	DISCUSSION
	TAPE HFC 00 - 66 SIDE A	
000	Co-Chair Williams	Called the House Finance Committee meeting to order and noted that the Committee would hear an overview provided by the Alaska Housing Finance Corporation (AHFC) and the Tobacco Securitization.
		ALASKA HOUSING FINANCE CORPORATION
064	DAN FAUSKE, EXECUTIVE DIRECTOR, ALASKA HOUSING FINANCE CORPORATION, DEPARTMENT OF REVENUE	Noted that AHFC's Capital Improvement Projects (CIP) reflects the needs of the Corporation and the pursuit of its mission through the goals and objectives of the corporation's strategic plan. The corporate departments have reviewed prior year's budgets to determine if there are any unfinished projects/programs that are on the on going need additional funds to be completed or should be extended.
190	Mr. Fauske	Stated that the CBR was developed by AHFC staff and recommended for inclusion in the Governor's budget submission to the Legislature. Each project/program has been reviewed and prioritized by the Budget and Housing Policy committee and presented to the Board of Directors for approval.
266	Mr. Fauske	Noted that there are no line item increases requested in this year's budget.
291	Mr. Fauske	Proceeded with an overview of the "Draft FY2002 Capital Budget". [Copy on File].
405	LES CAMPBELL, DIRECTOR, BUDGET, ALASKA HOUSING FINANCE CORPORATION (AHFC),	Noted that he would provide an overview of each fourteen-budget request. He referenced the handout (*).

	DEPARTMENT OF REVENUE, ANCHORAGE	
495	Mr. Campbell	Spoke to the items in the draft request: * The Supplemental Housing Development Program Stated that the purpose of the program was to supplement federal housing funds provided to Regional Housing Authorities to ensure safe, decent, affordable housing throughout Alaska.
575	Mr. Campbell	* Low-income weatherization program. The purpose of the program is to provide cost effective energy improvements to homes of low-income families.
626	Representative Hudson	Asked what type of heating systems would be used.
644	Mr. Campbell	Explained the entire range of systems.
658	ROBERT BREAN, DIRECTOR, RESEARCH & RURAL DEVELOPMENT, ALASKA HOUSING FINANCE CORPORATION (AHFC), DEPARTMENT OF REVENUE	Added that in the Bush areas, AHFC is encouraging the use of monitor stoves. He referenced the basic operations manual used so that there are no safety hazards.
752	Representative Foster	Acknowledged the importance of the program.
768	Representative Hudson	Commented that the monitor stoves have cut his oil bill in half. He supported this program in particular for Rural Alaska.
804	Co-Chair Williams	Asked who paid for the maintenance.
816	Mr. Bream	Noted that was part of a grant program. He reminded members that AHFC was dealing with low-income families. He commented on the importance of education.
862	Mr. Brean	Interjected that there is no one under contract that does furnace maintenance.
896	Mr. Campbell	* Paxton Manor Replacement The purpose of the program is to provide funds for the replacement of 24 units of family housing in

		Sitka.
973	Mr. Campbell	* Chugach View Renovation - Phase 2 The purpose of the project is to complete the major renovation, including building improvements, and to ensure code compliance, for 120 senior housing units.
1040	Representative Davies	Asked about the funding history.
1049	Mr. Campbell	Noted that this was federal receipt from FY01.
1065	Mr. Campbell	*Senior Citizen's Housing Development fund (SCHDF). The purpose of the program was to provide funds for the development of senior citizen housing.
1115	Mr. Campbell	* Senior and Statewide Deferred Maintenance and Renovation. The purpose of the project is to reduce deferred maintenance and address small renovation projects, in accordance with AHFC's 10-year plan, at several facilities utilized by senior citizens.
1176	Representative Croft	Asked about the bond receipts associated with the request.
1189	Mr. Campbell	Replied those would be General Obligation (GO) Bond receipts.
1210	Representative Lancaster	Asked who would manage the senior housing.
1226	Mr. Campbell	Advised it would be private operators building and managing these places.
1243	Mr. Campbell	* Housing and Urban Development (HUD) Capital Fund Program (formerly CGP). He noted that the project would renovate and modernize public housing units.
1294	Mr. Campbell	* HUD Federal HOME Grant Program The purpose of the program is to expand the supply of affordable, low and moderate income housing and to strengthen the ability of the State to design and implement strategies to achieve an adequate supply of safe, energy-efficient and affordable housing.
1372	Mr. Campbell	* Federal and Other Competitive Grants The purpose of the program is to allow AHFC to apply for HUD, other

		federal agency, and private foundation grants that target the housing needs, and supportive services, of low-income and special needs groups. AHFC will also apply for energy related grants as they relate to housing. When required, AHFC will provide the needed matching funds. Some of the funds received will be passed through to local non-profit sub-grantee organizations that deliver housing and/or services.
1433	Representative Hudson	Inquired how much HUD money does the State currently receive.
1446	Mr. Campbell	Believed it was around \$480 million dollars. He noted that not all of that money comes to AHFC.
1463	Mr. Campbell	Added that some of the funds go to the regional housing authorities and others to private developers and the project-based programs. He added that AHFC is one of the main sources of those funds.
1501	Mr. Campbell	* Competitive Grants for Public Housing He noted that the purpose of the program was to allow AHFC to apply for HUD, other federal agency, and private foundation grants that target the housing needs of low-income and special needs groups. AHFC will also apply for grants to prevent crime and substance abuse in public housing and assist public housing families attain economic self-sufficiency. When required, AHFC will provide the needed match.
1556	Mr. Campbell	* Energy Efficiency Monitoring Research The purpose of the project is to conduct research, analysis, information dissemination and interchange among members of the industry, as well as between the industry and the public.
1605	Mr. Campbell	* State Energy Program (SEP) Special Projects. He noted that the purpose of the project is to allow the State to participate in special project grants offered by the Federal Department of Energy to promote

		energy related technologies and research.
1637	Mr. Campbell	* Homeless Assistance Program-Mental Health Bill The purpose of the program is to support programs that prevent homelessness by providing assistance to families in imminent danger of becoming homeless, or those who are currently homeless.
1669	Mr. Campbell	* Beneficiary and Special Needs Housing - Mental Health Bill The purpose of the program is to provide funds for Alaskans non-profit service providers and housing developers to increase housing opportunities to Alaska Mental Health Trust beneficiaries and other special needs population throughout Alaska.
1728	Representative Davies	Noted the sum total of the projects was \$22.9 million dollars. He voiced his concerns with the 1st time homeowners program.
1760	Mr. Fauske	Explained that the mortgage program and the arbitrage program are separate programs. The arbitrage program totals about \$170 million dollars. Those dollars are separate and must be spend by mirroring the intent of the original bonds issued. Those bonds are mortgage bonds. The bond yield must stay within a certain amount for the rate of the life of the bond. AHFC has been buying down interest rates so that the earnings stay within those parameters.
1858	Mr. Fauske	Emphasized that dollars do affect programs. He referenced the subsidized portion of the bonds - the arbitrage portion of the loans. The economy has changed and AHFC is attempting make homeowners out of those that cannot otherwise purchase homes. He pointed out that most of the money is used by the urban areas because that is where most of the State's people live. As the monies dwindle, he stated that there is only one source of revenue.
1935	Mr. Fauske	Pointed out that AFHC is attempting

		to be competitive. The bonds are being structured to maximize arbitrage, thus maximizing yield. Taxable, first time homebuyers have used the arbitrage program the most. The goal of AHFC is to provide a dividend to the State. It is difficult to do that at this time.
2011	Mr. Fauske	Spoke to the low-income borrower, which often times needs, a subsidy to get the other programs to work.
2038	Mr. Fauske	Responded to questions if the State had created programs that are not necessary. He stated AHFC had not. He emphasized the incredible need in the State programs. He noted that if business can be generated through State agencies, then the State could receive a dividend.
2110	Mr. Fauske	Believed that AHFC could not continue at the current level. He addressed the affordability issues across America and how the discussions are occurring about arbitrage. Alaska has utilized funding for affordability. He spoke to changes to the FY98 format. He recommended that restriction be lessened.
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010	Representative Davies	Asked if when the agreement was made between the Legislature and AHFC, was arbitrage taken into consideration. He questioned if the \$103 million dollars should be revisited.
096	Mr. Fauske	Spoke to maintenance and how to spend corporate receipts. He agreed that it should be revisited.
254	Mr. Fauske	Addressed fiscal planning and how important AHFC's investments have been for the State's economy. He pointed out that was a compliment not only to the Board, but also the Legislature by recognizing the needs and then factoring that into the program.
276	Mr. Fauske	Pointed out the low default rate that AHFC has had.
309	Representative Croft	Asked about the arbitrate surplus as being corporate receipts. He asked what had shifted.

350	Mr. Fauske	Replied that there are several different types of applications.
383	STEVE KANTOR, ARIMAX FINANCIAL ADVISORS, ALASKA HOUSING FINANCE CORPORATION (AHFC), DEPARTMENT OF REVENUE	Addressed the bonds and the Internal Revenue Service (IRS) involvement. He commented that in the nature of housing, it is difficult to predict interest rates. It is pre decided over the life of the bond issue. He spoke more on the arbitrage earnings.
501	Representative Croft	Clarified that the range should be an appropriate charge so that it is not given away.
530	Mr. Kantor	Replied that the corporation wants to guarantee that the money would be used for what it was intended.
558	Representative Davies	Spoke to the low interest loans.
570	Mr. Fauske	Noted that nowhere in the United States is there an arbitrage program like the one that exists in Alaska. He noted that market conditions have been capitalized. Alaska has utilized \$40-\$60 million dollars a year. The State has been very fortunate.
638	Representative Croft	Asked what has changed.
664	Mr. Kantor	Explained that the corporation has been able to land mortgages at a fixed rate and borrow at a variable rate. He added that earnings have increased on bond mortgage rates. AHFC was concerned with the rate of earnings. He pointed out that the interest rates have now been fixed, which resulted in a limited amount earned.
793	Representative Davies	Inquired if that amount related to the total amount available.
		TOBACCO SETTLEMENT SECURITIZATION
844	JOE DUBLER, CHIEF FINANCIAL OFFICER, ALASKA HOUSING FINANCE CORPORATION (AHFC), DEPARTMENT OF REVENUE	Provided an overview of the Tobacco Settlement. He referenced the Alaska Housing Finance Corporation -Tobacco Settlement Payment Securitization, March, 2001" handout. [Copy on File].
898	Mr. Dubler	Overview of the Tobacco Settlement: * The Master Settlement Agreement (MSA)

		<p>* Options for spending the Settlement Money</p> <p>* How Securitization works</p> <p>* General Obligation vs. Tobacco Revenue Bonds.</p>
943	Mr. Dubler	<p>Stated that the MSA was signed on November 23, 1998 and included 46 state and the four largest cigarette manufactures. The agreement requires the Participating Members (PM) to make unadjusted payments exceeding \$6.2 billion dollars over the next 40 years, with additional payments in perpetuity. Payment is for the recovery of all claims and costs of the states.</p>
956	Mr. Dubler	<p>Stated that most cigarette manufacturers are now parties to the MSA. In total the Pm's comprise approximately 99.7% of the domestic cigarette market, indicating that the MSA is acceptable to the tobacco industry. Mr. Dubler advised that there are benefits of the MSA from the State's perspective:</p> <ul style="list-style-type: none"> • Alaska should receive large cash payments annually in perpetuity; • The MSA is an industry-wide settlement with payments based on total domestic cigarette shipments nationwide; • The MSA has been financed by higher cigarette prices, making it similar to an excise tax on cigarettes.
994	Mr. Dubler	<p>MSA Payments:</p> <p>* MSA Payments are based on domestic cigarette shipments.</p> <p>* Payment is adjusted annually for several factors, including inflation and volume of domestic cigarette shipments.</p> <p>* Payments are allocated to states based upon percentages specified in the MSA. Alaska's initial and annual payment percentage is .3414187%.</p>
1056	Mr. Dubler	<p>MSA Payments:</p> <p>* Initial Payments - made up front</p>

		<p>by the OPM through 2003; * Annual Payments - made by the OPM and SPM based on market share, in perpetuity; and * Strategic Contribution Payments - are payments in 2008-2017 to reimburse states for their contributions to the legal costs associated with the MSA.</p>
1079	Mr. Dubler	<p>Commented on the MSA Payment adjustments, which are adjusted each year for a number of factors. The adjustments apply to certain payments. Some adjustments are expected to have little or no impact on Alaska's payments. He noted that other adjustments could be significant.</p>
1100	Mr. Dubler	<p>Referenced Page 8, the Total MSA Payments to the State of Alaska. The aggregate amount of payments expected through 4/15/2025 is \$788.471 million dollars.</p>
1146	Mr. Dubler	<p>Spoke to the options for spending the settlement money: * Spend as you go * Trust built over time which would work like the Permanent Fund, with the MSA payments deposited to the Trust and a portion of income from the Trust used in future years for targeted expenditures; or * Securitization, which involves borrowing money with the MSA payments as collateral and source for repayment of bonds. The proceeds from the issuance of the bonds could be spent or put into a trust fund/endowment.</p>
1184	Co-Chair Williams	<p>Inquired if the money could be spent any way the State decides.</p>
1200	Mr. Fauske	<p>Acknowledged that was correct.</p>
1216	Mr. Dubler	<p>Referenced page 10 - The Tobacco Transactions completed and anticipated.</p>
1233	Mr. Dubler	<p>Noted Page 11, the Tobacco Settlement Asset-backed bonds, Series 2000. The first payment would be in FY03. The final projected payment would be in FY23, which would make better value of the bonds.</p>
1307	Representative	<p>Inquired the percentage of Alaska's</p>

	Hudson	total receipts that would authorize this.
1327	Mr. Dubler	Explained that 40% of the bonds were purchased; the payments will dwindle off.
1350	Vice-Chair Bunde	Asked when the next bonds would mature.
1364	Mr. Dubler	Replied that the State has sold 40% of the bonds off, making the structure good until fiscal year 2023. He added that this year would not include the extra.
1408	Representative Croft	Understood that the State was selling some of its risk.
1426	Mr. Dubler	Explained that the State sells all or a portion of their expected tobacco payment-funding stream to a special-purpose entity, whose sole purpose is to issue bonds backed by those payments. Northern Tobacco Securitization Corporation (NTSC), not the State or AHFC, would be the sole entity legally responsible for paying the debt service on the bonds. be effectively transferred.
1458	Mr. Fauske	Questioned additional costs.
1466	Mr. Kantor	Commented that the State and AHFC are legally separate from NTSC and would not put their own credit ratings at risk through the tobacco bond issuance. The mechanism affords the State and AHFC protection from problems resulting from reduced, stalled or halted payment streams from the MSA.
1511	Mr. Fauske	Noted that even when backed by a GO, it is still based on a revenue stream, which would under utilize a better-perceived revenue stream. He indicated that a small premium would be paid for that security. He emphasized that there is no benefit to the State to use up its GO credit.
1570	Representative Hudson	Commented that last year, the Legislature had authorized \$176 million.
1601	Mr. Kantor	Explained that had been projected out from what the 40% would look like over time, and thus, placing \$93 million dollars in proceeds back to the State.

1629	Representative Hudson	Asked if there were other opportunities.
1636	Mr. Kantor	Advised that there is no certainty on how the expected amount, which would be coming back from the bonds.
1658	Representative Hudson	Asked the balance.
1664	Mr. Kantor	Reiterated that 40% had been allocated.
1673	Representative Hudson	Questioned if the \$116 had been determined this year, would the State then be able to appropriate into that fund.
1695	Co-Chair Williams	Asked what was happening with smokers at this date.
1704	Mr. Kantor	Replied that the AHFC consultants have updated their projection to be good for over the next forty years.
1737	Vice-Chair Bunde	Interjected that this year, the tobacco industry had put \$8 billion dollars into tobacco advertising.
1773	Representative Hudson	Added that these concerns are the same as the GARVEE.
1785	Mr. Fauske	Added that the tobacco industry is doing very "well" these days. He acknowledged that was a strange irony. However, the State wants the continued payment.
1813	Mr. Dubler	Explained how securitization works - Page 12. * Securitization, in the case of the tobacco settlement is the process of issuing bonds that are backed by the MSA payments. * Securitization provides a sizeable up-front payment, rather than smaller payments spread over a number of years. For immediate pressing needs or special projects, securitization provides access to cash now. The approach is no different than borrowing money based on your future earnings to purchase a house, and paying it back over the next 30 years.
1854	Mr. Dubler	Addressed the Benefits of Securitization - Page 14 * Securitization transfers the risks associated with the MSA payments to the buyers of the bonds, including the reductions in

		cigarette sales; bankruptcy of any or all of the Pm's; invalidation of the MSA; a possible increase in the federal cigarette tax; individual lawsuits against the industry and states; and the impact of the additional volume reductions attributable to national smoking prevention and public education campaigns and significant additional restrictions related to the tobacco industry's marketing, advertising, and lobbying.
1870	Representative Croft	Asked the maximum timetable
1881	Mr. Dubler	Believed it would be 2030.
1888	Representative Croft	Asked the reduction in the payments expected to stretch?
1915	Mr. Kantor	Suggested the number was close to 75%.
1938	Representative Croft	Commented that if the only risk sold was that it would be over 75%, and then there was not much of a risk.
1964	Mr. Kantor	Advised that investors still felt that the risk was too great.
1982	Mr. Fauske	Interjected that at this point, the market place is better. There are dropping interest rates and more investors with a better perception on the bonds. He commented that the day bonds were priced; there had been a dip, due to the sale of a major coal company.
		TAPE HFC 01 - 67, Side A
19	Mr. Dubler	Observed that judgments against the tobacco companies could bankrupt companies, affecting the bonds.
104	Representative Hudson	Summarized that there is \$5 million dollars of equity. He asked if the 60 percent could be available on the time schedule if it were not used.
226	Mr. Kantor	Stated that it would be available on the time schedule and as indicated.
248	Mr. Dubler	Discussed page 15 - The Uses of Proceeds <ul style="list-style-type: none"> • On what and how the money spent determines the tax status of the bonds. Tax-exempt bonds generally have

		<p>lower interest costs than taxable bonds, reducing the cost of the financing to the State.</p> <ul style="list-style-type: none"> • If Bond Proceeds are spent on qualifying capital projects or other qualifying expenditures, interest paid on them will be exempt from federal income taxes. • If Bond Proceeds are spent on operating items, or the earnings of a trust/endowment fund created with Bond Proceeds are invested in taxable securities yielding above the cost of the bonds, the interest paid to holders of the bonds will be taxable.
300	Mr. Dubler	Discussed page 16- General Obligation versus Tobacco Revenue Bonds. He noted that even though GO Bonds have lower interest costs than Revenue Bonds, there are compelling reasons to use Revenue Bonds. The State has a limited GO bond capacity. By not selling the bonds, he maintained that the State is holding an investment in the tobacco industry. Revenue bonds are an attractive source when revenue is restricted.
385	Representative Davies	Referred to page 7.
405	Mr. Dubler	Explained that MSA are payments that reimburse the State for their tobacco litigation fees.
474	Mr. Dubler	In response to a question by Representative Davies, he stated he could not give an example of a capital project not using their tax-exempt status.
520	Mr. Kantor	Suggested that private capital projects would be questionable.
595	Representative Davies	Observed that the endowment consideration had been discussed and he asked if that would be a qualifying expense.
637	Mr. Kantor	Explained that would depend on the structure. It is possible if it is related to health related cessation.

670	Mr. Dubler	Noted that the IRS has checked the issue of proceeds, scrutinizing those programs closely.
690	Co-Chair Williams	<u>ADJOURNMENT</u> The meeting was adjourned at 3:45 P.M.