

MINUTES
SENATE FINANCE COMMITTEE
January 31, 2002
9:45 AM

TAPES

SFC-02 # 3, Side A
SFC 02 # 3, Side B
SFC 02 # 4, Side A

CALL TO ORDER

Co-Chair Pete Kelly convened the meeting at approximately 9:45 AM.

PRESENT

Senator Pete Kelly, Co-Chair
Senator Jerry Ward, Vice Chair
Senator Loren Leman
Senator Lyda Green
Senator Gary Wilken
Senator Alan Austerman
Senator Lyman Hoffman
Senator Donald Olson
Senator Dave Donley

Also Attending: JOHN BARNETT, Executive Director, Board of Storage Tanks Assistance; LARRY DIETRICK, Director, Spill Prevention & Response, Department of Environmental Conservation; PAT DAVIDSON, Legislative Auditor, Legislative Budget & Audit Division, Legislative Affairs Agency; JOHN BITNEY, Legislative Liaison, Alaska Housing Finance Corporation, Department of Revenue; DAN FAUSKE, CEO/Executive Director, Alaska Housing Finance Corporation, Department of Revenue; HEATHER BRAKES, staff, Senator Therriault

SUMMARY INFORMATION

SB 153-UNDERGROUND STORAGE TANK LOAN FUND

The Committee heard from the sponsor and a committee substitute was adopted as a working draft. The bill was held in Committee.

SB 181-SMALL COMMUNITY HOUSING LOANS

The Committee heard from the sponsor, Alaska Housing Finance

Corporation, and Legislative Audit. The bill was held in Committee.

SB 115-EXTEND BD. OF STORAGE TANK ASSISTANCE

The Committee heard from the sponsor and the bill was held in Committee.

#SB153

CS FOR SENATE BILL NO. 153(RES)

"An Act replacing the storage tank assistance fund with the underground storage tank revolving loan fund and relating to that revolving loan fund; repealing the tank cleanup program and the tank upgrading and closure program; and providing for an effective date."

This was the first hearing for this bill in the Senate Finance Committee.

Senator Leman stated this bill proposes to "phase out" the current clean up grant program by the year 2004 because "the expectation is these grants would be accomplished by that time." He continued the proposed committee substitute would change the underground tank assistance fund into a "revolving loan fund supported by loan repayments and income earned on the money in the fund."

Senator Leman moved for adoption of CS SB 153, 22-LS0696\L, Cook as a working draft.

There being no objections, the working draft was ADOPTED.

Co-Chair Kelly commented that Senator Leman has supplied an "excellent sectional analysis." [Copy on file]

JOHN BARNETT, Executive Director, Board of Storage Tanks Assistance, informed the Committee he supports this committee substitute and feels the proposed changes are warranted. He stated the Board of Storage Tank Assistance "urges passage" of this bill as it has language that specifies "who is eligible for a loan, based on the federal requirement of self-insurance." He stated if "someone is self-insurable, they are not eligible to get a loan from the state."

Mr. Barnett stated the self-insurable language of this bill would disqualify fourteen of the companies that have expressed interest

in getting a loan. He continued of these fourteen applicants, "thirteen are Chevron corporate owned facilities." He voiced the Board supported this bill because "it would reduce the loan application list." He stated that the Board and the Department concur the grants could be "wrapped up by 2004."

Senator Olson asked how many "applications are being considered" at present and how recently they were submitted.

Mr. Barnett stated currently there are four completed applications for the loan program, and approximately "fifty-seven have expressed interest" in applying for a loan. He detailed the process of applying for the loan, and speculated this would result in "forty to forty-five applicants and the loans could reach as high as a quarter of a million dollars depending upon the size of the cleanup and the level of contamination at the site."

Senator Hoffman asked how much funding would be made available annually under the revolving loan program.

Mr. Barnett responded that the "amount of funds available would be dictated by the number of applications and the amount of money currently in the fund." He stated "there are sufficient funds available in the storage tank assistance fund that would roll-over into this revolving loan fund to handle all of our initial expected needs" unless some site "turns out to be very, very contaminated." He noted that a lump sum is not given out for cleanup in this loan process, but would be phased over time, in order to prevent overpayment. He informed "sometimes the estimates are pretty high, and the cleanups will come in a lot lower due to basically technology improvements and such like that."

Senator Hoffman commented in a revolving loan system, a specified amount of money would be loaned out and the returns on those loans would give back an "estimated amount of funds to be available to be reissued." He asked, once the revolving loan fund is established, how much money would be available on an annual basis.

LARRY DIETRICK, Director, Division of Spill Prevention & Response, Department of Environmental Conservation, replied an "initial capitalization" of \$5 million was passed in SB 128 in FY 00 and the Department is working off that balance" currently. He informed, based the prospect of fifty-seven loan applicants with only four completed loans in the door, the projection of the "the amount available for both the loans and the grants" is anticipated to be \$3.4 million at the end of FY 02. He continued if the clean-up grants are completed in FY 03 as projected in the committee substitute, and these grant costs are deducted from the \$3.4

million balance, approximately \$2.1 million would be available for the revolving loan fund at the end of FY 03.

Mr. Dietrick stated the Department does not have a rate of return "experience yet with just four applications in the door," but is working with the Division of Insurance to determine the rate of return as well as what the terms and length of the loans might be. He stressed the Department feels it is "adequately capitalized to get started" and then "see what that trend will be."

Mr. Barnett stated one problem that might be experienced would be that some of the applications coming in under the current grant program may reach their cap, and if a site "is quite contaminated," the cost of cleanup might exceed the grant. In this scenario, he stated, the applicant might have to come for a revolving loan that they would be responsible for paying back. As the "sunset of the grant program" gets closer," he stated, the Department would be able to see "the level of interest in the loan program, as right now it is kind of hard to gauge."

Co-Chair Kelly ordered the bill HELD in Committee.

#SB181

SENATE BILL NO. 181

"An Act making the interest rate for the Alaska Housing Finance Corporation's small community housing mortgage loans the same as the interest rate on mortgage loans purchased under the corporation's special mortgage loan purchase program from the proceeds of the most recent applicable issue of taxable bonds before the origination or purchase of the small community housing mortgage loans."

This was the third hearing for this bill in the Senate Finance Committee.

Co-Chair Kelly commented that lively debate surrounded this bill last year, and he had held the bill for more thorough discussion, and to enable the Alaska Housing Finance Corporation (AHFC) an opportunity to "fully discuss the bill in order for the Committee to know the exact impacts as they see it."

Co-Chair Donley stated SB 181 would eliminate the Housing Assistance Loan Fund (HALF) program. He noted the HALF program was designed approximately twenty years ago to address higher costs

that existed at the time in housing construction in small communities. He informed that a Division of Legislative Budget and Audit report [copy on file], conducted in September of 2000 recommended the elimination of this program. He referenced the supporting reasons denoted in the audit, such as: it was not based on need; a \$400,000 loan; loans not based on any assessment of actual costs in those areas; an arbitrary population methodology as to whether a community is under 6,500 people; loans not limited to residences, but including apartment complexes; not limited to people who are low income; and no limit on house size. He summarized HALF is "highly unfairly discriminatory" based on an "arbitrary population amount that doesn't make any logical sense."

Co-Chair Donley continued that the Alaska Boundary Commission cited HALF as "a disincentive to the formation of local government." He cited an Alaska Boundary Commission report [copy not provided] released in 1998 stated "this program as a major impediment to the formation and consolidation of local government in Alaska."

He explained that in some areas of Alaska, "people on one side of a street that aren't in a community of 6,500 politically get a one percent discount on their building loan, and the people on the other side of the street who happen to be in a community that is over 6,500 don't get it." He stressed "this is illogical and not good public policy."

Co-Chair Donley stated this population requirement has been cited as a factor in communities "not getting organized." He continued these reasons support why this "program does not fit the needs of Alaska," and additionally the audit states there are "alternative programs available in the area for folks who truly had needs." He explained some of those programs such as: the Rural Enhancement Loan Program; the Interest Rate Reduction for Low Income Borrowers; the Energy Efficiency Interest Rate; the First Time Homebuyers Tax Exemption; and the Veterans discount program. He stated some of these programs offer lower rates than HALF. He reiterated the audit recommends elimination of the HALF program because alternate programs are available.

Co-Chair Donley informed he had worked on the committee substitute over the interim and changed it to "more of a needs-based program," that would "only apply to communities that had high housing costs, only for folks who were two times below the poverty level, and would only apply to single family homes and duplexes."

He stressed this committee substitute would change the program into a "much more public policy directed loan program where it actually made some sense going to people who needed it rather than people who are building large apartment complexes" or expensive houses. He

informed that this committee substitute would also "reduce the disincentive for organization, formation and unification of local governments" which is a "very important goal for long range benefit of the state."

Co-Chair Donley stressed this is a complex issue and he did not expect the committee substitute to be adopted today, but rather, he hoped to refresh Committee members' memories, hear public commentary, and "see if this proposed committee substitute is possibly the way to go."

Senator Ward informed he is a licensed real estate agent and his son-in-law works for AHFC, and noted this program "affects all of the Kenai Peninsula which I represent." He stated he has received significant response from his district and appreciates the time the sponsor has allowed for discussion. He commented "the concept of tightening the program up is not out of hand," but stressed there is a great deal of concern in the real estate industry in his district about possible changes to HALF. He stated that not everyone owns a home, but "have to live in apartments, for one reason or another, and this is a reality in my district."

Senator Hoffman asked Co-Chair Donley to clarify Item 2 in the sponsor statement that states the elimination of HALF would generate "additional earnings at AHFC" each year.

Co-Chair Donley reported AHFC "disputes that there would be savings," and their "position is that the number of the loans would go down" resulting in AHFC having "reduced revenue if enough loans were not made." Co-Chair Donley noted the audit cites there are other loans available to fill the needs, and "it is hard to believe" that AHFC "can't be competitive on their own for reasonable loans without having the statutory one percent reduction."

Co-Chair Donley, responding to Senator Hoffman's question, stated the savings projection is based on "how much money the state is not receiving because it is charging a below market interest rate for these loans." He voiced less revenue was possible "if people do not go get these loans," and "AHFC would have their own opinion about how much that would be." He reiterated the number mentioned in Item 2 was based on "the amount of the subsidy that would no longer be there for loan programs."

Co-Chair Kelly summarized "the heart of the argument" is that Co-Chair Donley thinks this committee substitute "would result in a small net increase while Alaska Housing believes it will have a potential of resulting in a large net decrease."

Senator Olson asked Co-Chair Donley if the private sector has taken a stance on this bill: specially, bankers or real estate agents.

Co-Chair Donley responded he "would imagine" that someone who lives in a small community and wants to borrow more than \$200,000 "would not want this program to go away." He detailed how much a person could save over the life of their HALF loan.

Senator Hoffman asked whether commercial businesses would support this bill.

Co-Chair Donley responded this could be answered through the public testimony process.

Senator Ward opined "bankers tend to adapt to whatever programs are available."

Senator Austerman, referring to the dispute of "what is saved or not saved," asked if the legislative audit states this committee substitute would save dollars.

Co-Chair Donley said the audit did not address the committee substitute; but did recommend elimination of the program. He recapped the reasons cited in the audit in support of elimination.

Senator Austerman, referring to notes he took during hearings held on this bill the prior year, stated that according to AHFC there would be a \$19 million net loss if the HALF program were eliminated. He commented it is his understanding that Co-Chair Donley's report states there will be a net savings, while AHFC states there will be a net loss.

Co-Chair Donley reiterated if AHFC charged the full market rate on its current loans, the result could be "a half a million dollars in additional revenue." He stated this would help maintain the dividends that AHFC pays to the state. He noted AHFC has indicated it would be paying "\$96 of the \$103" million to the "citizens of the state as a dividend of their operations," and suggested a net loss was generated due to advertising expenses.

Co-Chair Donley stressed keeping revenues up would continue to maintain high dividend levels to "help reduce the fiscal gap." He stated AHFC avows if the one percent discount is disallowed, people would not use this loan program, and AHFC would lose revenue.

Co-Chair Donley stated the audit identifies that other loan programs are available if people do not use this program. He

asserted "even AHFC" would not "suggest there would be a total loss of the entire amount of net revenue from this program" since people currently have the option to use other programs.

Co-Chair Kelly clarified the audit states there are other programs currently available, and AHFC predicts that borrowers may opt to choose them resulting in AHFC losing money. He stated "we are not talking about AHFC necessarily competing with private industry, but rather is competing with other quasi-governmental entities in these areas." He stated "AHFC agrees with the auditor that there are other programs available, they are just not ours and that is where the net loss comes from."

Senator Austerman asked if the Division of Legislative Finance could prepare a comparison of the net loss and net gain "theories" for the Committee.

Co-Chair Kelly asked Division of Legislative Finance staff to compile an analysis for the Committee.

Senator Hoffman noted many people have fixed incomes and if they have to pay a higher interest rate, they might "built smaller homes, borrow less money, or go to other programs." He stated this would "defeat the purpose of trying to get more income that could potentially reduce the amount of income that AHFC has and therefore have an impact on the dividend."

Co-Chair Kelly concurred with Senator Hoffman.

Co-Chair Donley stated Senator Hoffman's argument may be correct, but "if it were correct, from a public policy stance, this would argue for no limitation on the size of the community." He continued if the program's success is based on "how much money we are making off this program," it should "not discriminate and the population cap should be removed." He continued if this were the situation, the program should be opened up to all Alaskans so "more money can be made." He continued that currently the "population cap" "bears no public policy connection to the "goals that were enumerated for this program" and "doesn't bear any connection to the argument that this is an income producer for the state."

Co-Chair Kelly stated AHFC is espousing "the public policy is that AHFC would be able to make more money;" whereas Co-Chair Donley opines AHFC should be able to generate revenue throughout "their portfolio." He affirmed AHFC is making a "business decision that they can make more money by way by cutting rates across the board." He continued by having lower rates, AHFC can compete with Fannie Mae and Freddie Mac in larger communities.

Senator Hoffman voiced acknowledgement that the cost of building a home is higher in rural Alaska than it is in Anchorage, and if the goal is to "make the playing field level" whereby people can afford equal homes, "this one percent makes more sense" because of the higher cost of construction in Rural Alaska.

Co-Chair Kelly affirmed that "leveling the playing field" applies not only to square footage, but also to insulation values and those kinds of things.

Senator Hoffman stressed Rural Alaska does not participate in the Tax Exempt First Time Homebuyers program to the extent as Anchorage, which had approximately 65 percent or approximately \$240 million of those loans last year, compared to the rural areas with under \$200,000. He informed certain loan "programs are more adaptable to rural areas and other programs are more adaptable to Anchorage."

Co-Chair Kelly asked for clarification that the First Time Homebuyers program is not available to Rural Alaska.

Senator Hoffman replied it is available to all areas of the state, but "is more adaptable or more suitable for communities like Anchorage."

Co-Chair Donley recognized there are higher construction costs in some areas of the state, however, "this statute does not recognize this and makes an arbitrary cutoff" regardless of higher or lower construction costs. He continued he would "support legislation or public policy that was limited to those areas where there were higher construction costs."

Senator Ward supported Co-Chair Donley's comments that addressed construction costs as he has personally experienced this. He noted that the house he is building in Nikiski is going to cost one third of what he would pay to have that same house built in Anchorage. He commented that it does not cost as much to build in Nikiski as it does in Anchorage, "mostly due to the paying of the improvements and the ground itself."

Senator Lemman stated construction costs are higher in the rural areas of the state; however, construction costs are only one element of the cost of the home and other costs include property. He inquired if an analysis has been done on the cost of property in different areas of the state, and how it would impact the total cost of a construction project.

Senator Hoffman explained that in Bethel the cost of an average lot is \$30,000; however, that does not include water, sewer, a road or other factors. He detailed the costs incurred to obtain these necessary services, and supported the need to know what services are available when looking at construction costs.

Senator Wilken asked Co-Chair Donley if this new bill would limit the size of apartment complexes.

Co-Chair Donley replied this committee substitute would limit the size to single family residences and duplexes that are owner occupied.

PAT DAVIDSON, Legislative Auditor, Legislative Budget & Audit Division, Legislative Affairs Agency, informed the Committee that her Division reviewed the "original purposes of HALF" and found that over time, "other than the higher cost of construction, the other barriers to home ownership in small communities have been dealt with." She informed that the Division reviewed the actual loan portfolio and compiled the aforementioned report that reflects the "distribution of the loans by geographic locations," "overlaid with the actual construction indexed on Anchorage as 100 percent." She stated the Division also looked at the medium income and the average borrowers' income in each of the regions. She summarized the findings that "the bulk of program was not going to areas of high construction, and it was going to borrowers who had higher than the medium income for that area." She stated that because of these findings, the audit recommended either modifying the program to "focus it on the remaining barriers to home ownership" or eliminating the program. She clarified the audit "did not look at the impact of the revenue stream to AHFC comparing mortgages made through this program verses what the next best investment alternative for those funds were."

Senator Wilken, referring to page 8 of the audit, asked Ms. Davidson to explain the graph.

Ms. Davidson explained the graph reflects the "distribution of the actual loan portfolio across geographic regions of the state" and detailed how the areas score in relationship to construction costs in Anchorage and the percent of the total loan portfolio for that region.

AT EASE 10:30 AM / 10:34 AM

Senator Austerman inquired about the source of the information on the costs of building, specifically the reference stating it is cheaper to build in Juneau than it is to build in Anchorage.

Ms. Davidson replied this information is based on the United States Department of Housing and Urban Development Schedule of Building Costs and the AHFC 1999 Construction Costs Survey.

Co-Chair Donley clarified that according to AHFC, loans in the Housing Assistance Loan Fund are not available to large apartment complexes, and are limited to "no larger than a duplex."

He continued that the current statute does not contain language that stipulates a limitation on the size of an apartment. He voiced appreciation to AHFC for establishing this guideline, and asserted that the proposed committee substitute would be consistent with current loans and would put the limitation in statute.

DAN FAUSKE, CEO/Executive Director, Alaska Housing Finance Corporation, Department of Revenue reminded that the Legislature had considered the matter of these loans several years prior in a similar bill, SB 150.

SFC 02 # 3, Side B 10:37 AM

Mr. Fauske continued that last year, AHFC was directed by Co-Chair Kelly to work with Co-Chair Donley and Senator Hoffman to review a proposed committee substitute by Co-Chair Donley to address this loan issue in such a way as not to reduce net income. He stated an analysis was completed. He informed, to address the challenge of not reducing net income, AHFC took their current program loan portfolios and applied the proposed formula to it. He said, based on the interpretation of the proposed formula, the results indicate an 83 percent reduction in the amount of business AHFC would have had. He stated "this is where the number comes that causes us deep concern."

Mr. Fauske, in addressing the issue of other entities "doing the business," expressed that AHFC is in a competitive situation in many parts of the state. He informed that the federal government concentrates on the "conventional market," and has kept "Fannie Mae" and "Freddie Mac," out of the Tax Exempt, First Time Homebuyers market. He stated federal programs present a "significant challenge in some parts of Alaska such as the Railbelt down on the Kenai," but are "very limited" in the "rural" rural areas of the state.

He stressed in the "case of losing business" to other loan entities, the question goes beyond the audit information. He noted

the construction cost audit "excluded the cost of land or infrastructure." He stated this explains "why the building costs in Southeast are less than Anchorage," and "when you add back land and infrastructure, you will see that the numbers change."

He noted "there have been significant improvements in the housing industry across the state." He informed that another aspect that affects AHFC's competitive situation is that "Fannie Mae and Freddie Mac and other programs do not have energy rated restrictions." He continued "there is a state law that prohibits AHFC from buying a loan for a mortgage where the energy standards don't meet state standards." He explained this affects the competitive situation when AHFC competes with the \$6 trillion industry that Fannie Mae, which does not offer energy rate subsidies, represents.

Mr. Fauske informed the Committee he had been a member of the Fannie Mae advisory board, and had questioned why the federal government did not initiate federal standards for energy efficiency.

Mr. Fauske detailed the fees that AHFC pays to banks. He explained that banks originate a loan, but then sell them to a big secondary market that includes Fannie Mae or Freddie Mac, AHFC, and Country Wide.

Mr. Fauske compared AHFC interest rates to other industry secondary markets leaders. He stated closing costs and other instate loan-servicing fees AHFC pays are good for the economy of the state.

Mr. Fauske stated another factor the audit does not address, but which "discussion really needs to hinge on" is the dividends paid to the state by AHFC. He said this dividend should be a concern as it reflects net income, and "is a business decision."

Mr. Fauske informed he has encountered very few people who have a problem with the "fairness of city verses borough" issue, and he considers this program well received and used extensively. He stated this program is the source of \$20 million of net income to the state, and he agreed with Co-Chair Donley that perhaps this program could be expanded statewide.

Mr. Fauske mentioned that in 1992, Alaska Housing Finance Corporation paid the state of Alaska general fund approximately \$190 million for this loan portfolio, so "the state has not only received the cash upfront for the loan portfolio," but also receives "the dividend that is paid to the state to pay for the net income dividend calculations and the money that is transferred

back."

Co-Chair Kelly asked Mr. Fauske for further clarification.

Mr. Fauske informed that when the Alaska State Housing Authority (ASHA), AHFC, and the Rural Loan Program were merged, AHFC paid \$190 million to the state of Alaska for the entire loan portfolio. He continued that in 1995, AHFC established a transfer plan, which set up a dividend schedule and payments to the state of a portion of the Corporation's net income. He noted that a "good piece of AHFC's income" is produced from the HALF program. He summarized that "the state has received not only the cash," but additional benefits from the dividend program as well.

Mr. Fauske noted the section of the bill refers to transferring any monies left in the fund to the new program, and he clarified the projected balance of \$430 million is not cash but is instead 30-year loan assets from which the state would receive payments.

Mr. Fauske stated he would like the program expanded. He detailed that the "vast majority" of many "federally mandated programs" are received in the Anchorage area because of the cost of housing, the income of people and other factors, and that rural areas do not meet these program guidelines.

Mr. Fauske stated he is addressing these housing guideline issues with the United States Congress and noted income levels and housing acquisition have been addressed in the first draft of the federal Millennium Housing Commission report. He stated that many Alaskans are denied access to these programs because of these guidelines.

Mr. Fauske explained that AHFC created a taxable first time homebuyers program with no income restrictions to assist Alaskans because they do not qualify for federal programs. He stated this is the program that competes directly with the large secondary mortgage lenders, and stressed this program "represents a good working aspect of the corporation."

Mr. Fauske stressed the HALF program is not unfair, but rather he "views it as an equitable situation to try and eliminate some of the higher cost areas." He agreed that costs have come down in some areas of the state but have gone up in others, and he feels this program "levels that playing field."

Mr. Fauske continued he would like to see this program become bondable instead of the current revolving loan program. He informed this would enable AHFC "to re-loan the money as it comes in" thereby exceeding the original amount "due to the business

activity." He detailed the necessary changes involved in making the program bondable such as changes in state statutes; down payments; and mortgage insurance.

Mr. Fauske summarized he would like to see the HALF program remain, as "it works very well." He detailed the HALF program's activity this year, and informed the Committee that the Board of Directors recommendation for the dividend transfer plan was based on statute. He read the details of the dividend transfer plan as defined in statute. He commented that the transfer plan was based on a net income of \$103 million, and this past year, the net income was \$96.3 million.

Mr. Fauske specified the audit conducted by the Division of Legislative Budget and Audit determined there "needs to be a great deal of care given to the amount of withdrawals taken from the corporation" and a concern as to AHFC's "ability to meet its fiscal requirements by FY 05 or FY 06." He noted this means AHFC "needs to carefully monitor and watch the amount of money that is going out of the Corporation." He stressed he knows of no other entity in the state "paying dividends in excess of what it earned." He said the audit suggests the need to carefully monitor the money withdrawn from the corporation as to not "exceed what might be prudent." He informed this recommendation "led to the decision to reduce the transfer plan to the amount of net income which is \$96.3 million."

He reviewed the history of AHFC's net income and summarized that net income has been on the increase in spite of declining interest rates. He stated in terms of real net income, "two years ago it was \$82 million, last year it was \$89 million and this year it will be in the mid \$90's." He clarified, of this year's \$96.3 million, \$7 million was "windfall from the Bank of America settlement," and if "you look at real net income, we are at \$89 million." He stated the loan portfolio has gone from 26,000 loans in 1997 to a current 30,239 loans, "a significant jump in business;" and the main factor to the downturn in net income for the Corporation is the Federal Reserve lowering interest rates "eleven times this year."

He continued that one of the "most significant line items other than mortgage income" on the corporation's income statement is the investment income based on short-term securities the Corporation owns. He informed that the Corporation does not own equities. He disclosed that the rate of return has decreased since the transfer fund's inception in 1995. The Corporation has gone from a rate of return in 1995, when the dividend transfer fund was established, of "6 percent to a current 2 percent." He expressed the Corporation has done a good job in "increasing activities, keeping its net income on the incline even though we have had significant downturns

in interest" rates. He commented the lower interest rates are good for Alaska in that they provide for low cost loans that promote investments.

Mr. Fauske requested a "business decision to be made here as to the purpose of this program," and if the purpose is to make money, it does not mean "we have to give the farm away." He stressed the current program "makes sense, is not abused, and touches a lot of people across the state of Alaska." He stated one area the Department could improve upon is in extreme Rural Alaska and that "is just a difficult nut to crack."

Senator Hoffman asked if AHFC had paid fair market value for the portfolio in 1992. He also asked how the poverty level specified in this committee substitute, combined with the "125 percent factor," affects the loss of program revenue.

Mr. Fauske responded the payment would best be described as "bulk rate" as it was not discounted, nor was it the market rate an investor might have paid. In answer to the second question, he explained the 125 percent provision would result in an 83 percent decrease in business.

JOHN BITNEY, Legislative Liaison, Alaska Housing Finance Corporation, Department of Revenue, detailed how the calculations that projected the 83 percent reduction in business were conducted. He stated these calculations indicate that 17 percent of the applicants who would have received loans would not qualify under the new provisions. He said this analysis was based on rate scales, election districts, qualifying communities based on population caps, and other factors.

Mr. Bitney stated the Department has not concluded their analysis on the impact of the poverty level provision, but expressed this provision would limit the applicants even further.

Senator Olson asked about the percent of defaulted loans.

Mr. Fauske responded the default rate is approximately 3.2 percent.

Mr. Bitney clarified that AHFC considers defaults to be foreclosures and "that rate is basically zero." He continued that the delinquency on a statewide basis is approximately three percent on all loans, both rural and urban. He continued the rate is also tracked by regions, and that the rate is increasing to four or five percent in Ketchikan; however, the area around Dillingham and the Yukon Kuskokwim is lower than three percent.

Senator Olson asked if AHFC expected any impact on the default rate if the bill is passed.

Mr. Fauske responded AHFC does not know what impact the changes would have on the default rate of future business, but there would be fewer loans and subsequently, less opportunity for individuals in some regions.

Co-Chair Kelly stressed the need to determine the true impact of this bill, and questioned the "huge" differences of fiscal impacts presented by the sponsor and AHFC. He voiced frustration at not being able to reach a conclusion on this issue.

Senator Wilken asked where the information AHFC provided on the Home Housing Assistance Program is located in the packet, and asked Mr. Fauske to verify that AHFC has a \$480 million portfolio with \$20 million net income, which is approximately four percent, and asked if the income figure is "net;" factoring in the cost of running the program.

Mr. Fauske responded the figure is net.

Senator Wilken asked if the cost of administering the program would have to be subtracted from that figure.

Mr. Bitney said that the net income reflects the service fees paid to banks, which is the "most substantial administrative cost."

Senator Wilken verified the net income reflects the loan servicing costs.

Senator Wilken commented one reason he supports this bill is because for the "third year in a row," the Local Boundary Commission has identified "this particular program as an impediment to consolidating governments," and in fact, the Local Boundary Commission asked AHFC last year, "to try to do something with this program so it would not impede the consolidation or organization of government."

Senator Wilken asked what the AHFC Board of Directors is doing to "remove the incentive to not organize."

Mr. Fauske stated AHFC is adhering to state law that specifies the community population requirements to qualify for loans.

Mr. Bitney informed that AHFC did address consolidation based on regulation, and is researching ways to expand the program, with statutory changes, to address the boundary issue in the event that

an area is annexed or expanded, residents are not disqualified from the program who would have qualified prior to the annexation.

Mr. Bitney informed Senator Wilken that the information he is seeking is on page 5, and is referred to as the Rural Owner Occupied Program.

Co-Chair Donley asked Mr. Fauske if the revenue loss of 83 percent as projected by AHFC would be altered if the poverty level percentage were lowered to 110 from 125.

Mr. Fauske responded it would.

Co-Chair Donley inquired about the process AHFC used to determine how many people would use other programs, and how much the numbers were discounted in light of the fact that currently people could use other programs.

Mr. Bitney explained the First Time Homebuyers program limits the purchase price of a home in Anchorage to \$179,000, and less than that amount in other regions of the state. He stated this is the main limitation to people obtaining this loan program as homes in this price range are very limited.

Co-Chair Donley inquired about the "ordinary loan programs" AHFC offers.

Mr. Bitney stated these programs are in competition with federal programs such as Fannie Mae, and because of "the economy of scale" of these larger loan programs, AHFC cannot offer as competitive an interest rate, and borrowers "gravitate towards that lower interest rate loan."

Co-Chair Donley asked if any of these "ordinary loans" are being made.

Mr. Fauske replied yes, and mentioned the Taxable, First Time Homebuyers loans, offering variable rates, saw a "downturn up to and after September 11th." He stated the federal government programs "really stepped it up a notch in terms of an economic stimulus" after the terrorist attack on the United States that occurred on September 11, 2002 and noted AHFC has also reduced rates, depending on the variable rate market. He stressed AHFC could be very competitive with federal agencies. He cited there has been an increase in loans in the last thirty days as loan rates have been adjusted. He commented that other programs are more competitive on rates and may be less restrictive, and summarized this is a consumers' market and the loan industry is very competitive.

Co-Chair Donley remarked AHFC does not know for certain whether people "would go to your ordinary loan program or to other low-income loans verses federal programs. They might, but you're not sure." He continued that the "same process" might be occurring with the HALF program.

Mr. Fauske responded this could be happening. He stated that AHFC is a business and the question is "do we want to have business or do we want to give the business to other people." He stated "he is opposed to that, as an Alaskan and as the CEO." He continued if "AHFC is not held to producing the net income," the state would need to "develop policies to promote business," not take it away

Mr. Fauske assured the Committee that under this bill, "business activity will go down."

Co-Chair Donley asked if the Board is "restricted in lowering their interest rate for the regular mortgage loans, such that you couldn't just reduce the other loans by the one percent that the statutory HALF calls for." He stated this would result in significant new business and "make a lot more money just with ordinary loan programs."

Mr. Fauske replied the "problem lies in that we are comparing a revolving loan fund to a bond fund." He detailed the costs involved in a bond program, and that sometimes the rate to consumers might drop below the bond cost; whereby the Corporation would need to be subsidized. He said the state had a previous program that was used to subsidize loans. He reiterated the current revolving loan programs states the rate be set at one percent below the market rate, and this program "is easier to manage as you do not have any bond debt behind the rate."

Co-Chair Donley asked, in addition to being limited by the amount of current funding and the population cap, what other limitations are there on expanding the HALF program.

Mr. Fauske advised that in order to expand, the current HALF program would need to be a bondable program "consistent with what investors on Wall Street see when they buy mortgage revenue bonds." He stated this is "do-able," but must be a program that is "easily accessible to Wall Street."

Co-Chair Donley asked what limits there might be if AHFC expanded the program to give an interest rate discount to everyone in the state.

Co-Chair Kelly commented this might change the nature of program.

Mr. Fauske explained if this program is expanded statewide "to get away from the city verses borough Boundary Commission, let's just take it statewide and let's adopt the definition of the federal government for Alaska, where everything outside of Fairbanks, Anchorage, and Juneau is rural."

Co-Chair Donley commented that would make good business sense, but would not be good public policy, as it would discriminate against people in Anchorage, Fairbanks and Juneau. He continued that the state should look for a program that does not arbitrarily draw "lines on the map" and benefits all Alaskans.

Mr. Fauske responded he feels the current program works well in addressing the issue of higher costs of construction in rural Alaska.

Co-Chair Donley stated that the current loans are not issued only to people who live in areas of higher costs, and his concern with the program is the question of whether loans are truly based on need or just based on arbitrary numbers.

Co-Chair Kelly stated that the areas of the state with the "bulk" of loan activity are areas that have the most competition from other loan entities; thereby, making AHFC more competitive regardless of the cost of construction and income level.

Mr. Fauske affirmed this is correct.

Senator Austerman asked if the program would have to become a bond program in order to expand the program.

Mr. Fauske explained it would be "very difficult" considering the current funds available in the program to expand without changing to a bond program, as "funds would need to be generated from elsewhere." He stated, however, it could be "done with a different approach."

Senator Austerman summarized this meant the state would need to put more money into the current revolving loan program or AHFC would need to change to a bond-based program.

Mr. Fauske concurred.

SFC 02 # 4, Side A 11:25 AM

Senator Hoffman asked how much additional revenue would be generated for the state if the program were changed to a bond program.

Mr. Fauske stated he did not have a projection, but would be able to get an answer for the Committee.

Senator Hoffman commented the higher cost of living in Rural Alaska is not addressed in this bill.

Co-Chair Donley responded the committee substitute does address this and explained that if the costs are over a certain level, the interest rate percentage is adjustable. He continued it also addresses lower income levels. He explained that the program could be further "limited to those areas that have a higher cost of construction and also for folks who truly need the extra assistance."

Mr. Fauske noted AHFC watches Anchorage "very closely" as it is a very vibrant market, and construction costs appear to be increasing there. He stressed that "down the road," Anchorage will be facing some "tough issues" as land availability decreases and prices go up.

Co-Chair Donley voiced appreciation for the time the Committee has spent on this issue, and stated he would continue to work on the committee substitute and would explore expanding the program to make more money for the state and to the benefit of all Alaskans.

Ms. Davidson suggested AHFC investigate splitting the loan program into two sections: one to "maintain a loan fund" to address high cost areas, and a new loan fund with the mission of generating income.

Co-Chair Kelly noted that Mr. Fauske was making note of Ms. Davidson's suggestions.

Co-Chair Donley stated it might be a wise "investment policy for some of our savings accounts" to fund some sort of program of "discounted loan mortgages for homes for Alaskans." He commented it might be an "interesting analysis" "since the state is tax exempt in its actions verses pure investments paid to the citizens that are subject to federal taxes." He stated "reduced housing loans might be a better benefit to the state's citizens."

Co-Chair Kelly stated this bill would be brought back before the Committee as a title and a bill number with the criteria that the

committee substitute must be "income and inclusive." He noted the Committee had "their level of education on the program raised today." He continued that any changes to the bill would be entertained, but the "removal of the one percent program is no longer an option."

Co-Chair Kelly ordered the bill HELD in Committee.

#SB115

SENATE BILL NO. 115

"An Act extending the termination date of the Board of Storage Tank Assistance."

This was the first hearing for this bill in the Senate Finance Committee.

HEATHER BRAKES, staff to Senator Therriault, highlighted the details of the bill, which would extend the Board of Storage Tank Assistance an additional two years. She informed that the current "Board is in its wind-down year of 2002." She referred to a Division of Legislative Budget and Audit audit [copy on file], which concludes the Board should be re-established as it plays an integral role in promoting compliance throughout the state with federal regulations and the benefits thereof. She summarized the audit as recommending extension of this "independent board."

Co-Chair Donley voiced concern about taking action on this bill in light of continuing discussion about the Storage Tank Assistance program in SB 153.

Co-Chair Kelly said this bill would be readdressed after action on SB 153 was concluded.

Co-Chair Kelly ordered the bill HELD in Committee.

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ADJOURNMENT

Co-Chair Pete Kelly adjourned the meeting at 11:37 AM