

SENATE FINANCE COMMITTEE
February 15, 2010
9:03 a.m.

[9:03:12 AM](#)

CALL TO ORDER

Co-Chair Stedman called the Senate Finance Committee meeting to order at 9:03 a.m.

MEMBERS PRESENT

Senator Lyman Hoffman, Co-Chair
Senator Bert Stedman, Co-Chair
Senator Charlie Huggins, Vice-Chair
Senator Johnny Ellis
Senator Dennis Egan
Senator Donny Olson
Senator Joe Thomas

MEMBERS ABSENT

None

ALSO PRESENT

Deven Mitchell, Executive Director, Alaska Municipal Bond Bank Authority, Department of Revenue; Ted Leonard, Executive Director, Alaska Industrial Development and Export Authority; Bryan Butcher, Director, Government Affairs and Public Relations, Alaska Housing Finance Corporation, Department Of Revenue; Joe Dubler, Director of Finance, Alaska Housing Finance Corporation

PRESENT VIA TELECONFERENCE

None

SUMMARY

SB 269 ECON. STIMULUS BONDS: REALLOCATION/WAIVER

SB 269 was HEARD and HELD in Committee for further consideration.

SB 270 AK HOUSING FIN CORP DIVIDEND

SB 270 was HEARD and HELD in Committee for further consideration.

[9:03:21 AM](#)

#sb269

SENATE BILL NO. 269

"An Act relating to the waiver of volume cap of recovery zone economic development bonds authorized by 26 U.S.C. 1400U-2 and reallocation by the Alaska Municipal Bond Bank Authority of the waived volume cap; relating to the waiver of volume cap of recovery zone facility bonds authorized by 26 U.S.C. 1400U-3 and reallocation by the Alaska Industrial Development and Export Authority of the waived volume cap; increasing the total amount of bonds and notes that the Alaska Municipal Bond Bank Authority may have outstanding; relating to revenue bonds issued by the Alaska Municipal Bond Bank Authority; and providing for an effective date."

[9:03:45 AM](#)

Co-Chair Stedman brought the meeting to order and thanked participants for coming on a holiday. He went over today's schedule.

[9:04:56 AM](#)

DEVEN MITCHELL, EXECUTIVE DIRECTOR, ALASKA MUNICIPAL BOND BANK AUTHORITY, DEPARTMENT OF REVENUE, explained the different issues in the bill. The first issue deals with the Alaska Municipal Bond Bank Authority and the need for statutory revisions in the program and the second issue deals with temporary opportunities related to the recovery act. He introduced the PowerPoint presentation, Alaska Municipal Bond Bank, Alaska Industrial & Export Authority, February 15, 2010 (copy on file).

Mr. Mitchell reviewed the Alaska Municipal Bond Bank, page 2, which is a public corporation of the state of Alaska created in 1975 to provide access to capital markets for Alaska communities through the use of state support. The summary statistics from FY2001 through FY2009 are presented with community's savings in the amount the communities would have otherwise had to pay in addition to their original obligation payments. He indicated that there are benefits to Alaska communities from the program. Mr. Mitchell moved to the Bank Statute Changes, page 3 showing the bond bank increase borrowing limit by \$250 million. He noted there is a \$750 million cap increase from \$500 million about four years ago. He noted that as of June 30, \$162.8 million of the cap remains. There are applications for another \$40 million with additional applications expected to total \$100 million.

Co-Chair Stedman referred to the list of outstanding loan amounts for communities around the state totaling \$564 million. He requested a time frame when the communities will pay off this debt. He mentioned that the city of Sitka's \$34 million loan will be paid off in seven years and wondered if there would be the authority to reuse the money on other projects.

Mr. Mitchell replied that it is a revolving authority that exists under the borrowing cap. He commented that the program is mature at this point meaning the debt is level and will continually step down to a zero balance in thirty years. The borrowing of the communities has outpaced the maturity of the outstanding obligations.

Co-Chair Stedman requested additional information showing how the authorization will step down to give the committee a better understanding of the incremental increase to \$250 million and how much room will be out in five to ten years. Mr. Mitchell agreed that could be done. Co-Chair Stedman also asked for the cost of the debt to the communities.

Mr. Mitchell agreed he could put together a schedule showing the aggregate debt services by community showing how the maturity looks over time. Mr. Mitchell continued that in addition to increasing the borrowing limit, the statute eliminates restrictions on Revenue Bond issues of the program and eliminates restrictions on leases of the program. These changes are requested by communities that currently have opportunities to finance capital projects. If the bond bank were not available the communities would have to borrow at higher interest rates. He referred to the Sitka hydro project that is looking to refinance about \$21 million worth of bonds. The refunding can benefit in gross dollars of \$1.7 million by the bond bank participating in the transaction.

Co-Chair Stedman explained that the community of Sitka wants to refinance an old hydro project, lower the debt service, and use the savings to pay additional debt service for the next increment of raising a dam face. The local electrical rates will not change.

Senator Olson questioned what was the anticipated default expected over the next ten to fifteen years in looking at the increased borrowing rate. Mr. Mitchell expected a zero default. He reported that the program is not a grant program, but a loan program. He declared that in the history of the bond bank there has never been a default where a community has not paid. The intent of the program is to provide lower costs to the communities that need it the most.

Senator Olson asked if all the communities on page 2 were into revenue bonds or other types of bonds. Mr. Mitchell responded that the bonds were primarily general obligation and revenue. Senator Olson asked for the breakdown of the bonds. Mr. Mitchell responded that there were more general obligation bonds than revenue bonds.

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Mr. Mitchell continued his presentation with the History and Applicable Laws for Recovery Zone Bonds, page 4. He explained that the American Recovery and Reinvestment Act of 2009 created opportunities to provide the incentives for both public and private partnerships, but within a limited window. After the end of the calendar year, the allocations will no longer be available for use.

Mr. Mitchell continued with the Build America Bonds, page 5. He remarked this is a structure of financing available for any tax exempt financing. Where otherwise they would sell tax exempt bonds, now would sell taxable bonds where the federal government provides a 35 percent subsidy on the interest expense on those bonds. He informed the committee there may be an extension to the program, but at a lower subsidy rate. He moved to the Recovery Zone Bonds, page 6. He mentioned that the economic development bonds are identical to the Building American Bonds except it boosted a 45 percent subsidy on the interest expense. This significantly increases the value on the long end of the loan. He informed that \$90 million has been allocated to the state of Alaska. Mr. Mitchell explained that the recovery zone facility bonds provide the opportunity for municipalities to offer tax exempt financing to businesses investing in their communities. He stated that \$135 million has been allocated the state of Alaska.

[9:19:09 AM](#)

Mr. Mitchell observed that the Recovery Zone, page 7 is for a community that declares itself a recovery zone with a required resolution from the local city council.

TED LEONARD, EXECUTIVE DIRECTOR, ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY, explained that the original recovery zones were allocated by the U.S. Treasury based on June 2008 employment declines. The U.S. Treasury looked at employment populations in cities and counties, but in the unorganized areas of Alaska the census area was used to allocate the portion.

Mr. Mitchell referred to the Recovery Zone Allocations on page 8. The economic development bond total is \$90 million with facility bonds at \$135 million based on the employment statistics.

Co-Chair Stedman asked for more information on why the Yukon-Koyukuk Census Area and the Wade Hampton Census areas were zero.

Mr. Mitchell responded that those areas did not have a decline in employment statistics for the qualifying period. He referred to page 9, Why Legislation? to explain the disconnect between allocations and potential projects. The failure to use the allocation money will result in a loss of funds on January 1, 2011. He explained that current allocations will guarantee the loss of a substantial volume cap. This bill establishes a framework and legal basis to ensure this limited resource is used.

Mr. Mitchell referred to the Alaska Municipal Bond Bank Recovery Zone Statutes on page 10 providing for communities in census areas to receive consideration immediately upon the bill becoming effective. It provides for boroughs to waive allocations that are not needed or cannot be used immediately.

Co-Chair Stedman elaborated with an example on page 8 of Prince of Wales-Outer Ketchikan Census Area for \$1.9 million in economic development bonds and \$2.9 million in facility bonds. He asked for an explanation on how the mechanism would work.

[9:25:23 AM](#)

Mr. Mitchell responded that upon the bill's passage there would be an immediate outreach to census communities querying if there were any planned capital projects. Based on the response an allocation would be made to those communities with projects. He explained that if a borough has not used the allocation then it will be waived automatically so it can be refocused to other community projects. There is the concern that areas of increased unemployment would be penalized, but he reiterated that although this is not the intent of the bill it would be allowed to make sure allocations are used.

[9:28:38 AM](#)

Mr. Leonard remarked that the Alaska Industrial Development and Export Authority Recovery Zone Facility Bonds on page 11 are specifically designed to be used with businesses in conjunction with banks. This can be used for industrial, commercial, retail, and office. Facility bonds cannot be used for rental housing, airplanes, health clubs, liquor stores, race tracks, luxury boxes, gambling facilities, or massage parlors. There is one allocation of \$29 million by the Fairbanks North Star Borough to the Alaska Port Authority for the natural gas project.

Co-Chair Stedman asked if these would be available for community fishing quotas. Mr. Leonard responded he was not sure, but noted it does not say it cannot be used for that.

Co-Chair Stedman restated it would be used for fishing permits not the equipment. He added there has been discussion of using funds to help some communities buy community quotas to create jobs.

Senator Thomas inquired where this is addressed in the bill.

Mr. Leonard specified that it is in the federal statutes.

Mr. Leonard continued on page 12 with the Features and Uses. The bonds are issued for private projects with the interest tax-exempt. These bonds would be issued as a conduit private activity bond and the debt service is funded by the private business that owns and uses the property.

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Mr. Leonard continued with the Recovery Zone Regulations on page 13 with the goal of ensuring all the allocations would be used in recovery zones and areas of high unemployment and economic distress. One of the benefits of the bill is that it allows AIDEA and the bond bank to work with other entities not in the recovery zone.

[9:33:40 AM](#)

Senator Huggins inquired if Alaska could have state-wide projects. Mr. Leonard replied that the area would have to be designated as a recovery zone. The criteria must be logical and make sense.

Senator Huggins voiced his concern if this will make sense later on. Mr. Leonard responded that was a concern of AIDEA who wanted to be a participant in order to look at the state as a whole. Based on the criteria and public hearing process, it should have the mechanism on why the decisions were made.

[9:36:03 AM](#)

Senator Huggins questioned if that did not happen, what was Mr. Leonard's confidence level in the mechanism to make this work.

Mr. Leonard responded that if it does not happen then AIDEA estimates there will be a 50 per cent loss of the cap. He added that almost every state has a reallocation process. He noted that the first thing is to be sure that each project meets the qualifications to be a project. Businesses can not

just ask for money without a firm and verified project that meets requirements for unemployment. He emphasized that there are processes in place to verify that the project is feasible in the area and meets the criteria for unemployment or distress and also has the resources to monitor it. Regulations could also state that if it is not being used by a certain date then it could be pulled back. AIDEA is hoping to have a list of projects so that if allocations are not used, then another project could be brought forth to use the allocation.

Co-Chair Stedman questioned if the allocations not used in the unorganized areas would flow into Anchorage and Matsu.

Mr. Leonard replied that it could. Co-Chair Stedman believed that it would most likely flow to areas with the structure to handle the project, but did not meet the federal criteria. Mr. Leonard agreed that specific areas within a larger metropolitan area could be looked at as distressed.

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Co-Chair Stedman referred to the Department of Commerce zero fiscal note and an \$80,000 fiscal note from the Department of Revenue and the Alaska Municipal Bond Bank for legal counsel, financial advisory service, and travel.

SB 269 was HEARD and HELD in Committee for further consideration.

[9:40:10 AM](#) AT EASE

[9:41:13 AM](#) RECONVENED

[9:41:23 AM](#)

#sb270

SENATE BILL NO. 270

"An Act relating to the dividend paid to the state by the Alaska Housing Finance Corporation; and providing for an effective date."

BRYAN BUTCHER, DIRECTOR, GOVERNMENT AFFAIRS AND PUBLIC RELATIONS, ALASKA HOUSING FINANCE CORPORATION, DEPARTMENT OF REVENUE, explained that sponsor statement.

SPONSOR STATEMENT

Senate Bill 270 will modify the Alaska Housing Finance Corporation's transfer plan statutes to reflect federal changes in generally accepted accounting principles.

House Bill 256 passed in 2003 that set in statute a transfer plan for AHFC to pay an annual dividend to the state of Alaska. The yearly dividend would be lesser of \$103 million or 75 percent of the Corporation's net income for the previously completed fiscal year minus bond repayments for state capital projects.

In 2006, Senate Bill 236 passed that made the first adjustments to the transfer plan. This bill changed the definition of "net income" to "adjusted change in net assets", which reflected federal changes to generally accepted accounting principles.

SB 270 will make another modification due to federal changes in generally accepted accounting principles. It will add to the definition of "adjusted change in net assets" to include "temporary market value adjustments to assets and liabilities made during the base fiscal year". This change will allow for a true dollar figure for the Corporation's dividend to be calculated from rather than inaccurately high or low numbers based on how interest rate swaps are now considered.

Co-Chair Stedman asked for an explanation of the interest rate swap.

JOE DUBLER, DIRECTOR OF FINANCE, ALASKA HOUSING FINANCE CORPORATION, explained that an interest rate swap is a derivative financial instrument where the corporation enters into a contract with a counter party where they are paid a fixed rate in exchange for a variable rate. The variable rate is based on an index. This allows for the selling of variable rate bonds to hedge the change of interest rates over the 30 year time period bonds are typically sold. The Alaska Housing Finance Corporation has lowered the costs of funds by entering these interest swaps.

Mr. Butcher remarked that SB 270 is a simple bill. Co-Chair Stedman inquired if there have been any problems collecting on the swaps. Mr. Dubler responded that currently the swaps are marked to market every quarter for financial statement presentation. If the swap out was closed today than it would require a payment to the counter party.

Senator Olson asked who would want an interest rate switch in light of the low interest rates on the world market. Mr. Dubler answered that these swaps were entered into in 2001 through 2006 when the corporation saw the majority of the mortgage activity was from home buyers. The mortgage market started offering very sophisticated loan products to all borrowers that caused the Alaska Housing Finance Corporation concern. The corporation decided to take on the risk themselves because they had the expertise to take on these types of transactions and pass the benefit to the borrowers

in the form of a lower interest rate. Most for-profit corporations enter into some sort of interest rate hedge.

[9:49:27 AM](#)

Co-Chair Stedman remarked that many parties were caught by surprise by the derivative market. Mr. Butcher remarked that the corporation had three swaps with Lehman Brothers, but when Lehman Brothers went bankrupt, the corporation wrote them a check to purchase out of the position. The three swaps were rebid and several million dollars were made in the transaction.

[9:50:38 AM](#)

Co-Chair Stedman reported a zero fiscal note from the Department of Revenue.

Senator Thomas asked if this was being made during base fiscal year or on an annual basis.

Mr. Butcher responded that the adjustments are made annually. This makes an adjustment from the financial statements to what was originally agreed to in the transfer plan. Accounts have made a lot of changes over the years that have affected the agreement with the legislature over what the dividend would be on an annual basis. The general accounting principals have been modified to require the corporation to include changes in the market value of certain interest rate swaps. This was not part of the original deal with the legislature. SB 270 asks to back this modification out.

Senator Thomas inquired if it would be broader with the changes.

Mr. Butcher explained there was another motivation from 1997 that required the corporation to bring booking marketable debts securities to market. The change was immaterial to the corporation's financial statements. The swap situation could have large swings in value from quarter to quarter and the corporation did not want a \$10 million net increase in one year affecting the dividend, then maybe a \$10 million decrease for the following year also affecting the dividend.

[9:53:53 AM](#)

Co-Chair Stedman questioned the corporation's intention of going forward with derivatives.

Mr. Butcher responded that they would not be entering into any more in the near future. The corporation's debt issuance for this calendar year will consist mainly of some federal bonds through 2010.

Co-Chair Stedman questioned the reason for not doing it anymore. Mr. Butcher replied that the interest rate swaps entered to date have been swaps that change a variable rate debt into a fixed rate obligation of the corporation. The variable rate debt market in the world has had some issues with liquidity in the past year and a half. There have been a lot of bond holders putting the bonds back into the corporation and they have had to come up with the cash to pay off their position. The variable rate interest rate today is almost non-existent due to the shortage of liquidity.

Co-Chair Stedman asked if these are standardized or non-standardized contracts. Mr. Butcher remarked that the general terms are standardized, but each firm has their own way of doing business. Co-Chair Stedman asked Mr. Butcher to explain the difference between a standardized and non-standardized contract.

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Mr. Butcher explained that the liquidity facilities are an agreement where the provider supplies liquidity for a variable rate debt obligation. Bond holders have the right every seven days to put the bonds back into the corporation; therefore the corporation must have the money to pay those bonds off. Since the corporation does not usually have that large a sum of money available an agreement is entered into with a bank to provide liquidity in case a bond holder wants their money. There are then further agreements between the corporation and the bank.

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Co-Chair Stedman understood the standardization, but the transparency was not as apparent as many thought hence the world financial situation. The state of Alaska did not get hit as bad as many areas in the country, but comfort levels are still not high.

SB270 was HEARD and HELD in Committee for further consideration.

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ADJOURNMENT

The meeting was adjourned at 10:02 AM.