

SENATE FINANCE COMMITTEE

March 2, 2017

9:02 a.m.

9:02:46 AM

CALL TO ORDER

Co-Chair MacKinnon called the Senate Finance Committee meeting to order at 9:02 a.m.

MEMBERS PRESENT

Senator Lyman Hoffman, Co-Chair
Senator Anna MacKinnon, Co-Chair
Senator Click Bishop, Vice-Chair
Senator Donny Olson
Senator Mike Dunleavy
Senator Peter Micciche
Senator Natasha von Imhof

MEMBERS ABSENT

None

ALSO PRESENT

Gene Therriault, Energy Policy Assistant, Alaska Energy Authority.

PRESENT VIA TELECONFERENCE

Brenda Applegate, Controller and Assistant CFO, Alaska Industrial Development and Export Authority (AIDEA); John Springsteen, Chief Executive Officer and Executive Director, Alaska Industrial Development and Export Authority, Department of Commerce, Community and Economic Development.

SUMMARY

SB 57 AIDEA:DIVIDEND TO STATE;INCOME;VALUATION

SB 57 was HEARD and HELD in committee for further consideration.

#sb57

SENATE BILL NO. 57

"An Act relating to the dividends from the Alaska Industrial Development and Export Authority; relating to the meaning of 'mark-to-market fair value,' 'net income,' 'project or development,' and 'unrestricted net income' for purposes of the Alaska Industrial Development and Export Authority; and providing for an effective date."

Co-Chair MacKinnon introduced two guest pages: Meadow Stanley and Maisy Messing.

9:04:21 AM

GENE THERRIAULT, ENERGY POLICY ASSISTANT, ALASKA ENERGY AUTHORITY, (AEA) discussed the PowerPoint, "Alaska Development Finance Authority; SB 57 Proposed Language Changes to Modernize AIDEA's Dividend Statute" (copy on file).

Mr. Therriault highlighted slide 2, "AIDEA's Dividend: History, Goal, Statutory Language, and Two Accounting Problems Working to Fix." The goal was to bring stability and predictability to the Alaska Industrial Development and Export Authority (AIDEA) dividend calculation. He remarked that there were two current problems. The market valuation issue was triggered by some new general accounting standards rules. The dividend penalty dealt with infrequent right-downs of projects funded with outside sources.

Mr. Therriault addressed slide 3, "Dividend Statute Language Needs Modernizing, As Accounting Rules Have Evolved Over Time":

3 Accounting Transaction Types, 3 Causes Dividend Problems:

1. Entries from "real transactions" that actually occurred, they are historic in nature. Examples: booking what was paid for an asset, revenue that is generated, payroll that is paid, taxes paid, what was cash received and why, etc.

2. Entries from "estimates and allocations". Examples: booking depreciation and amortization expenses which recognizes and records that an asset used up some of

it estimated useful life over the period of operations.

3. Entries from "market value adjustments". These are entries related to transactions that didn't happen, but, AIDEA must record them for the audit as though they did to comply with G.A.S.B. and have a G.A.A.P. audit. (SB 57 proposes to update the existing "excluding..." statutory language and remove G.A.S.B. "market value" impacts on the AIDEA dividend calculation) Example: booking the gain or loss that would have resulted from selling your marketable securities on the last day of the year (GASB 31).

Mr. Therriault looked at slide 4, "Sec. 44.88.088. Payment of dividend to state":

The Pertinent Language:

The authority shall adopt a policy for payment of a dividend... to the state each fiscal year.
The amount of the dividend payable... may not be less than 25 percent nor more than 50 percent of the net income ...for the base fiscal year...

..."net income" means the change in net position, or the equivalent term under generally accepted accounting principles, ... as set out in the audited financial statements of the authority for the base fiscal year, excluding amounts attributable to intergovernmental transfers, capital contributions, grants, or impairment losses on development projects financed under AS 44.88.172;

Mr. Therriault highlighted slide 5, "Dividend Problem 1: "Market Value" Adjusting Entries":

Problem 1:

1. G.A.A.P. keeps evolving, requiring booking/recording "market value" adjusting entries. Essentially, act like something happened that didn't happen, and book it as though it did...
2. The result: AIDEA's "net income" swings, sometimes materially, which means the State's dividend swings sometimes materially year-over-year, SB 57 will correct this.

3. Ultimately, the dividend payment is a cash based transaction. (Paying it when cash hasn't been earned is a problem -- for AIDEA. Not paying it when cash has been earned is a problem -- for the State.)

Mr. Therriault addressed slide 6, "Problem 1 Analogy of 'Market Value' Entries Impacts."

Mr. Therriault looked at slide 7, "Money Based Tax Payer Analogy."

Mr. Therriault highlighted slide 8, "Form 1040 Impact Analogy." He showed an example of a 10-40 tax form. He stated that the example suggested that the individual had wages of \$100,000, some investment income, dividends, and the bottom showed a total of \$109,000 net income. That number would then go into their tax calculation, and write a check to the federal government.

Mr. Therriault discussed slide 9, "GASB Statements 31, 68, 72, and 75." He stated that the slide showed what would be required of that individual based on the AIDEA dividend's current accounting rules.

Mr. Therriault looked at slide 10, "Form 1040 Analogy - Add GASB Impacts":

(Now adjust your 1040 total income as if "GASB Type" adjustments were required at year-end)

Senator von Imhof remarked that the gains could not be recorded when the asset was sold. Mr. Therriault deferred to Ms. Applegate for accounting information.

[9:10:07 AM](#)

BRENDA APPLGATE, CONTROLLER AND ASSISTANT CFO, ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY (AIDEA) (via teleconference), agreed with Senator von Imhof. She explained that the unrealized gains and losses became an adjustment to the carrying basis of those investments going forward. She stated that there would be a realized gain or loss on the books when the investment was sold, which would be the difference between what was actually paid for the investment and the sales proceeds. The unrealized difference would flow back to the unrealized gains and losses in the year of sale.

Senator von Imhof surmised that the changes would result in a large gain with a significant appreciation of an asset over time and a large dividend. Ms. Applegate replied in the affirmative.

Senator von Imhof wondered how the elimination of the four GASB rules would "smooth out" the dividend over time. Ms. Applegate replied that it would allow for payment of a dividend on the available cash for the dividend, rather than the paper gains and losses that would fluctuate over time. She remarked that there could be a large gain on an appreciated marketable security, but it would be real cash.

JOHN SPRINGSTEEN, CHIEF EXECUTIVE OFFICER AND EXECUTIVE DIRECTOR, ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY, DEPARTMENT OF COMMERCE, COMMUNITY AND ECONOMIC DEVELOPMENT (via teleconference), furthered that the change would allow for more predictability and better planning.

Mr. Therriault addressed slide 11, "SB 57 Impact To 1040 Analogy":

The "market value" unrealized adjustments would be excluded from "Net Income."

Senator Micciche remarked that the GASB rules was related to transparency, and stressed that changing the rules eliminated some of the transparency for the public. He, however, understood that the changes would make the process easier for AIDEA. He queried an explanation to the public of the reason for "sidestepping" the most recent GASB recommendations for recording the transactions. Mr. Therriault replied that AIDEA would continue to follow the rules in order to get its audited financial statement. He stated that the change was to the statute that instructed AIDEA how to calculate the dividend. He remarked that the legislature would instruct AIDEA on what number to run through the dividend calculation. He pointed out that the request was to change the dividend calculation to true cash rather than an inflated or artificially deflated number.

[9:16:11 AM](#)

Vice-Chair Bishop surmised that the attempt was utilize actual dividends to achieve a "smoothing" affect; rather than addressing the "peaks and valleys" in order to

calculate a dividend. Mr. Therriault agreed, and furthered that the next two slides would help illustrate Vice-Chair Bishop's comment.

Mr. Therriault discussed slide 12, "AIDEA's Net Income, Pre-G.A.S.B. 31 "Market Value" Adjusting Entries." He noted that the graph line moved up and down depending on the amount of AIDEA activity.

Mr. Therriault highlighted slide 13, "GASB 31 Impact to Net Income." He remarked that the graph had the impact of GASB-31 overlaying the current situation. He noted that, starting in 1998 at the initiation of GASB, there was a suggestion that the true net income was artificially low. The GASB rule had artificially inflated the true net income. He furthered that the rule also sometimes artificially depressed the true net income. The peaks and valleys were getting steeper over time. He stressed that the GASB rule would be followed to produce the audited financial statement.

Mr. Therriault addressed slide 15, "Dividend Problem 2: "Dividend-Penalty" Effect Adjusting Entries":

Problem 2:

1. When the value of a project has been determined to have been permanently reduced, G.A.A.P. requires recording an adjusting entry between the Balance Sheet and the Income Statement to reduce some or all of the value of an asset or a project from AIDEA's Balance Sheet.
2. The resulting entry reduces net income. The consequence could either reduce the State's dividend from a project it funded or have AIDEA adjusting its dividend calculation to offset the reduction in project value.
3. Thus, there could be up to a 25 percent to 50 percent "dividend penalty" from an adjusting entry. SB 57 will correct this.

[9:21:04 AM](#)

Senator Micciche noted that there would be a feasibility study, instead of an actual "environmental impact study" (EIS). Mr. Therriault agreed.

Senator Micciche wondered whether the reference to GASB-68 and GASB-75 was merely for example purposes. He wondered whether those rules had an impact on AIDEA. Mr. Therriault replied that they would have an impact on AIDEA. He deferred to Ms. Applegate.

Ms. Applegate furthered that AIDEA had implemented GASB-68. She explained that AIDEA was part of the Public Employees' Retirement System (PERS). She remarked that, as employer under the state, AIDEA had a portion of the pension costs and were required to follow the same accounting guidelines as the rest of the state. She explained that AIDEA recorded a portion of the pension expense that was calculated under GASB-68, and reduced the dividend amount. She explained that GASB-75 was the other post-employment benefits portion.

Senator Micciche assumed that the state had carried the employment burden, and opposed to AIDEA carrying that burden individually.

[9:23:11 AM](#)

Mr. Therriault discussed slide 16, "Hypothetical State Funded Non-172 Project, if Stopped, Impact to "Net Income". He remarked that should AIDEA have written off the project in FY 16, the graph displayed the situation.

Mr. Therriault looked at the Sectional Analysis (copy on file):

Section 1: Section 1 amends AS 44.88.088(b) to include a definition for "mark-to-market fair value" adjustments that are mandated by the General Accounting Standards Board (GASB) and Generally Accepted Accounting Principles (GAAP). It then adds these adjustments and noncash accounting entries relating to pension obligations and benefits to the existing statutory list of items that are to be excluded from "net income" prior to calculation of AIDEA's dividend to the state treasury.

Section 1 also adjusts the existing scope of project losses that are to be excluded from the definition of AIDEA's statutory net income (dividend base). The Legislature previously instructed that amounts attributable to intergovernmental transfers, capital

contributions and grants were to be excluded so as not to impact the dividend base. Additionally, losses on development projects financed under AS44.88.172 were also excluded. However, the prior policy instruction did not anticipate periodic write offs for projects financed outside of AS44.88.172 with funds from non AIDEA sources. In these limited cases, project losses would affect AIDEA financial statement net income which could, in turn lower the calculated dividend.

Finally, Section 1 applies the mark-to-market adjustment, noncash pension and other postemployment benefit adjustments and redefined project loss exclusions discussed above to all AIDEA funds subject to the dividend statute to remove unnecessary volatility from the yearly dividend.

Section 2: Section 2 provides for an immediate effective date.

[9:27:38 AM](#)

Senator Micciche understood the purpose of the bill, and expressed support for the legislation. He remarked that the bill expanded AIDEA's categories of projects. Mr. Therriault replied that the changes acknowledged that there had been additional funds added over the years, so those funds were added to the list. He deferred to Mr. Springsteen and Ms. Applegate.

Mr. Springsteen agreed with Mr. Therriault.

Ms. Applegate stated that the current dividend statute applied to projects financed under the Section 172 statute. She stated that AIDEA had been participating in projects that did not fit into the Section 172 statute, so there was a desire to include the projects in the bill language.

[9:29:34 AM](#)

AT EASE

[9:32:09 AM](#)

RECONVENED

[9:32:13 AM](#)

Senator Micciche wondered whether the purpose of the bill was to modernize the dividend statute or to expand the scope of AIDEA's ability to participate in energy projects up to and including existing facilities in the state. Mr. Therriault replied that the bill allowed for predictability to the calculation of the dividend. The bill did not expand AIDEA's authority to participate in any projects beyond the current statutes.

Co-Chair Hoffman looked at line 5 and line 23, on page 2, and wondered why impairment was excluded. Mr. Therriault deferred to Ms. Applegate.

Ms. Applegate explained that the word, "losses" was intended to include impairment. She furthered that AIDEA would also like to capture within the word, "losses" was related to whether AIDEA were to sell a project at a loss. The impairment loss would be on a separate line item from a loss on the sale of an asset.

Co-Chair Hoffman noted that the Arctic Infrastructure Development Fund listed AS 44.88.810, and that same fund was defined later in a different statute. He queried those differences in definition. Mr. Therriault replied that the first one was an overall acknowledgement of the overall section of statute that set up the program. The other was a specific project as listed in the section.

Co-Chair MacKinnon remarked that AS 44.88.900 was a list of definitions in statute.

Co-Chair MacKinnon looked at page 16, Section 1, AS 44.88.088 was the actual dividend calculation.

Mr. Therriault, in response to Co-Chair Hoffman's question, looked at Section 4 referenced the definition section for all the investment tools that AIDEA was given. He explained that it was were the definition of a development project within each tool.

Senator von Imhof looked at slide 13, and felt that the legislation's intent was relating to the volatility in the market related to the large fluctuations of assets. She argued that suggesting the changes would not necessarily eliminate the volatility, because there would still be cash volatility. She explained that a financial event was the point at which the dividend would be paid. She stressed

that investments took a long time to mature. She wondered whether there was a simulation under the current proposal. Mr. Therriault deferred to Ms. Applegate.

Ms. Applegate agreed to provide that information.

Co-Chair MacKinnon CLOSED public testimony.

9:39:40 AM

AT EASE

9:40:13 AM

RECONVENED

SB 57 was HEARD and HELD in committee for further consideration.

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ADJOURNMENT

9:40:35 AM

The meeting was adjourned at 9:40 a.m.