

SCOMM

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ALASKA INDUSTRIAL DEVELOPMENT AUTHORITY

FEB 2 1984

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January 30, 1984

Representative Rick Uehling
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Dear Representative Uehling:

As you may recall, this fall a hearing was held by a subcommittee on loans and there was considerable discussion on assistance to the small borrowers.

Our SBA purchase program has been active in this area and a bill is pending in the legislature which would perhaps be of assistance to some Alaskans. We support the intent of this bill, but would like to offer a technical amendment which would read as follows:

*Sec. 2. AS 44.88.159(c) is amended to read:

(c) The interest rate on a loan purchased by the authority with money in the small enterprise loan account that is not from the proceeds of the sale of a series of bonds is the lesser of (1) the prevailing prime rate adopted by the United States Small Business Administration, or (2) [EQUAL TO] the most recent index of Aa corporate bond yield averages as published by Moody's Investors Service. However, if the interest rate established in accordance with this subsection would be less than 10 percent, the interest rate on the loan is 10 percent.

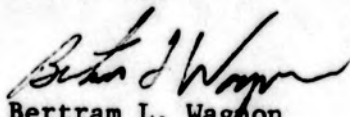
Our reason for suggesting such an amendment is that it is possible that someone might construe the existing language to be interpreted to mean that once the lesser of 1 or 2 fell below 10% no loans could be made. Our suggested alternative would hopefully clarify any such ambiguity.

Representative Uehling
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The effect of this bill would be to reduce our purchase rate on SBA loans from the present 12.7% to 11%. The Authority feels this is a responsible piece of legislation in that we only purchase the U.S. Government guaranteed portion and the yield should reflect the risk as well as move with the market which it does under S.B. 254.

If I can answer any questions please advise.

Sincerely,



Bertram L. Wagon
Executive Director

BLW:mr

Sectional Analysis of SBA Bill

Section 1: This section deletes the reference to a project, as defined in AS 44.88.220. This deletion is requested to ensure that there is no difficulty with the Authority purchasing the SBA guaranteed portion of working capital and inventory loans. Presently, it could possibly be interpreted that the Authority is prohibited from buying these loans because of the project description of AS 44.88.220(6).

Section 2: This section is an effort to resolve the difficulty of differential rates being applied to the same loan program. Presently the maximum rate allowed by the U.S. Small Business Administration (SBA) on loans guaranteed by them is the prevailing prime rate plus: 2-1/4% if the loan is less than seven years; or 2-3/4% if the loan is longer than seven years. The present AIDA "buy rate" for the SBA guaranteed portion is Moody's Aa corporate index - in essence, AIDA is loaning funds to the banks at this rate. The bank may then add 1-1/2% to this rate for loans under \$100,000, or 1% to this rate for loans over \$100,000. Generally, there has not been a problem, but with two different rates, particularly one being a "short term" rate (SBA/Prime) and one being a "long term" rate (AIDA/Moody's Aa) the potential exists for the rates to be such that AIDA effectively cannot buy these loans. For instance, the present (mid-March) rates are: Prime = 10.5%; Moody's Aa = 12.4%. For a loan of less than 7 years, the SBA ceiling is 12.75% (10.50% + 2.25%). AIDA will "buy" this loan (i.e. provide funds to the bank) at 12.4%, and allow the bank to charge 1 to 1-1/2% in excess of the 12.4%. Since the SBA ceiling is lower, it will be the effective rate. So the bank would have to loan funds to the borrower at 12.75%, and get funds from AIDA at 12.4%. This spread is inadequate to induce the bank to sell SBA loans to AIDA. This does not mean that a bank will not make an SBA loan based upon some other source of funds, however it does significantly lessen the possibility that a bank will make an SBA loan (the SBA estimates that AIDA purchases 70% of all new SBA guaranteed loans in Alaska).

A simple way to eliminate this problem would be to tie the AIDA rates to prime. However this could create a situation where a borrower was confronted with rates in excess of 20% (prime exceeded 20% during 1980 and 1981, and peaked at 17% during 1982). Section 2 represents a compromise. It sets the AIDA buy rate at the lesser of prime, or Moody's Aa, with a 10% floor. This should allow AIDA to "stay in the SBA business" even if Moody's Aa exceeds prime, as in the example, but still protects the borrower from the egregious rates that could result from being strictly tied to prime. The rationale for the 10% floor is that if rates drop below 10%, AIDA assistance should not be needed.

Suggested amendment: for S.B. 254 is: (see attached page)

*Sec. 2. AS 44.88.159(c) is amended to read:

(c) The interest rate on a loan purchased by the authority with money in the small enterprise loan account that is not from the proceeds of the sale of a series of bonds is the lesser of (1) the prevailing prime rate adopted by the United States Small Business Administration, or (2) [EQUAL TO] the most recent index of Aa corporate bond yield averages as published by Moody's Investors Service. However, if the interest rate established in accordance with this subsection would be less than 10 percent, the interest rate on the loan is 10 percent.

Our reason for suggesting such an amendment is that it is possible that someone might construe the existing language to be interpreted to mean that once the lesser of 1 or 2 fell below 10% no loans could be made. Our suggested alternative would hopefully clarify any such ambiguity.

Introduced: 4/14/83
Referred: Labor and Commerce
and Finance

1 IN THE SENATE

BY JOSEPHSON AND V. FISCHER

2

SENATE BILL NO. 254

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

4

THIRTEENTH LEGISLATURE - FIRST SESSION

5

A BILL

6

For an Act entitled: "An Act relating to loans made or purchased by the
Alaska Industrial Development Authority; and provid-
ing for an effective date."

8

9 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. AS 44.88.158(b) is amended to read:

11 (b) The authority may use money in the small enterprise loan
12 account to purchase the guaranteed portion of a loan made by a private
13 financial institution after June 30, 1981, to a small enterprise [TO
14 PAY THE COST OF A PROJECT, AS DEFINED IN AS 44.88.220], if the loan is
15 guaranteed by the United States or an agency or instrumentality of the
16 United States, including, but not limited to, the Small Business
17 Administration, the National Marine Fisheries Service, and the Farmers
18 Home Administration.

19 * Sec. 2. AS 44.88.159(c) is amended to read:

20 (c) The interest rate on a loan purchased by the authority with
21 money in the small enterprise loan account that is not from the pro-
22 ceeds of the sale of a series of bonds is [equal to] the lesser of (1)
23 the prevailing prime rate adopted by the United States Small Business
24 Administration, or (2) the most recent index of Aa corporate bond
25 yield averages as published by Moody's Investors Service, except that
26 an interest rate established under this subsection may not be less
27 than 10 percent.

28 * Sec. 3. This Act takes effect immediately in accordance with AS 01.-
29 10.070(c).