

S

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254



ALASKA INDUSTRIAL DEVELOPMENT AUTHORITY

1577 "C" STREET • SUITE 304 □ ANCHORAGE, ALASKA 99501-5177 □ (907) 274-1651

March 7, 1984

Senator Richard I. Eliason, Chairman
Senate Labor & Commerce Committee
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

RE: Senate Bill 254

Dear Senator Eliason:

We would like to again offer our support for S.B. 254, a bill which would amend the rate charged borrowers on federally guaranteed loans purchased by the Authority. The Authority believes this is a good bill, which will correct a problem that has arisen from time to time, as explained in the attached sectional analysis (Attachment A). We do have a minor amendment that we would like the committee to consider. This amendment, shown in Attachment B, would not change the intent of the bill, but would, in our opinion, add clarification.

The effect of this bill would be to reduce our purchase rate on SBA loans from the present 12.8% 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.

We have been informed that Senator Pettyjohn will be offering an amendment to S.B. 254 that would mandate that all applicants for AIDA financing must be residents of the State for at least one year before an application could be made. Statute changes of this nature have been suggested previously and now, as then, we oppose such changes.

Our opposition is based upon two major considerations. First, any type of durational residency requirement always seems to raise constitutional questions, and we would not want the Authority's operations impeded because of a court battle over such an issue.

Senator Richard Eliason
March 7, 1984
Page 2

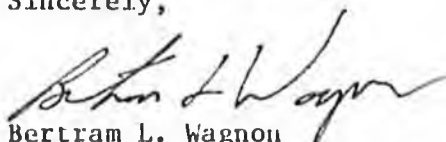
Second, and much more important in our view, restrictions of this nature appear to run counter to the rationale for the existence of AIDA. The legislative findings and policies directing AIDA speak to such factors as decreasing unemployment by "the establishment and expansion of industrial, manufacturing, and business enterprises in Alaska. . .". In our mind it is clear that the Authority's mission is to both expand existing businesses and attract new businesses, both of which should help to increase employment. It is true that in stimulating new business ventures in Alaska, the business involved may not have been in Alaska for a full year prior to application. But please note that the project itself must be in Alaska, hence the new economic activity will take place in our State, regardless of where the owners come from. Further, since most of our financing is of a long term nature, any new-to-Alaska business people must be willing to make a long term commitment to doing business in the State.

In point of fact, most of our applicants could easily meet the one year residency requirement. However, there are exceptions and we see nothing to gain by excluding this new source of economic activity and jobs. Indeed, even if this does increase the level of competition in an industry, we believe that is a favorable development in a competitive economy such as ours.

To summarize, the Authority strongly supports S.B. 254, however we do believe that the clarifying amendment we have suggested should be adopted. Further, we oppose the imposition of any residency requirement, since we believe it would be counter to the purpose of AIDA.

Thank you for the chance to comment.

Sincerely,


Bertram L. Wagnon
Executive Director

BLW:RL:mr



ALASKA INDUSTRIAL DEVELOPMENT AUTHORITY

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ATTACHMENT A

SECTIONAL ANALYSIS OF SB254

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.

ATTACHMENT B

SUGGESTED AMENDMENT FOR SB254

*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.

SB 254: An Act relating to the interest rate purchased by the Alaska Industrial Development Authority

Senate Bill 254 proposes amendments to AS 44.88.159(c) which deals with the setting of interest rates for the purchase of SBA loans by the Authority. The current law mandates that this rate be equal to Moody's Aa corporate bond yield. The necessity for a change is due to the fact that the SBA places an interest rate cap based upon the prime rate and, with the dramatic fall in the prime rate over the past six months, we are approaching the ceiling.

The Moody's rate is what is referred to as a "mellow" rate in that it does not move either up or down as fast as prime. For example, when prime was at 20%, Moody's was at 15.5%. However, as prime fell Moody's, being a "mellow" rate, did not fall as fast and currently stands at 11.8% while prime is at 10.5%.

This legislation is intended to give the Authority a limited flexibility in setting the interest rate and at the same time preserving the integrity of the program by setting the rate at the lesser of prime or Moody's Aa with a 10% floor.

The bill, as drafted, has a technical flaw in that it may be construed to mean that, if prime falls below 10%, no loans could be made. This is not the intent and a suggested amendment is attached making it clear that if prime falls below 10% the loan rate will be 10%.

*Sec. 2. AS 44.88.195(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.

The board of directors of the Alaska Industrial Development Authority and the Administration recommend approval of this measure with the suggested amendment.



Richard A. Lyon, Commissioner

Date: 5/16/83

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.

STATE OF ALASKA 1984 LEGISLATIVE SESSION
FISCAL NOTE

Revision Date: _____

REQUEST
Bill/Resolution No.: SB 254
Title: Relating to loans made or
purchased by AIDA
Sponsor: Josephson
Requestor: Senate Labor/Commerce
Date of Request: _____

FISCAL DETAIL
Agency Affected: Commerce & Econ. Development
Program Category Affected: Development
BRU, Program or Subprogram(s) Affected:
Alaska Industrial Development Authority

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 84	FY 85	FY 86	FY 87	FY 88	FY 89
OPERATING						
100 PERSONAL SERVICES						
200 TRAVEL						
300 CONTRACTUAL						
400 SUPPLIES						
500 EQUIPMENT						
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS						
800 MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0
CAPITAL						
REVENUE						

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL						

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

SOURCE OF FUNDS TO OFFSET FISCAL IMPACT OF BILL:

ANALYSIS: Attach a separate page for analysis

Prepared By: Bertram Waynon, Executive Director Phone: 274-1651
Division: Alaska Industrial Development Auth. Date: 12/13/83

Approved by Commissioner: Richard A. Lyon Date: 12/29/83
Agency: Commerce and Economic Development

Distribution (by Agency preparing fiscal note):

Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)

12/1/83

SB 254 TITLE & SPONSOR SUMMARY

14:20 5/22/84 PAGE 1 OF 2

AMENDED TITLE:

AN ACT RELATING TO LOANS MADE OR PURCHASED BY THE ALASKA
INDUSTRIAL DEVELOPMENT AUTHORITY;
AND PROVIDING FOR AN EFFECTIVE DATE

PRIME SPONSOR: JOSEPHSON.

CO-SPONSORS: FISCHER, V. .

CURRENT STATUS: 4/14/83 IN (S) LABOR & COM REFERRAL: FINANCE

SB 254 SENATE ACTION

14:20 5/22/84 PAGE 2 OF 2

DATE SEQ PAGE

LEGISLATIVE ACTION

DATE	SEQ	PAGE	LEGISLATIVE ACTION
04/14/83	01	0698	FIRST READING -- COMMITTEE REPORTS LABOR & COMMERCE FINANCE RULES

*** ** ** *** ** **



ALASKA INDUSTRIAL DEVELOPMENT AUTHORITY

1577 "C" STREET • SUITE 304 □ ANCHORAGE, ALASKA 99501-5177 □ (907) 274-1651

January 30, 1984

Senator Rick Halford
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Dear Senator Halford:

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.

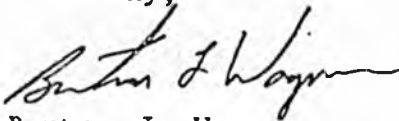
Our reason for suggesting such an amendment is that it is possible that someone might construe the existing language to be interpreted to mean that once the lesser of 1 or 2 fell below 10% no loans could be made. Our suggested alternative would hopefully clarify any such ambiguity.

Senator Halford
January 30, 1984
Page 2

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,

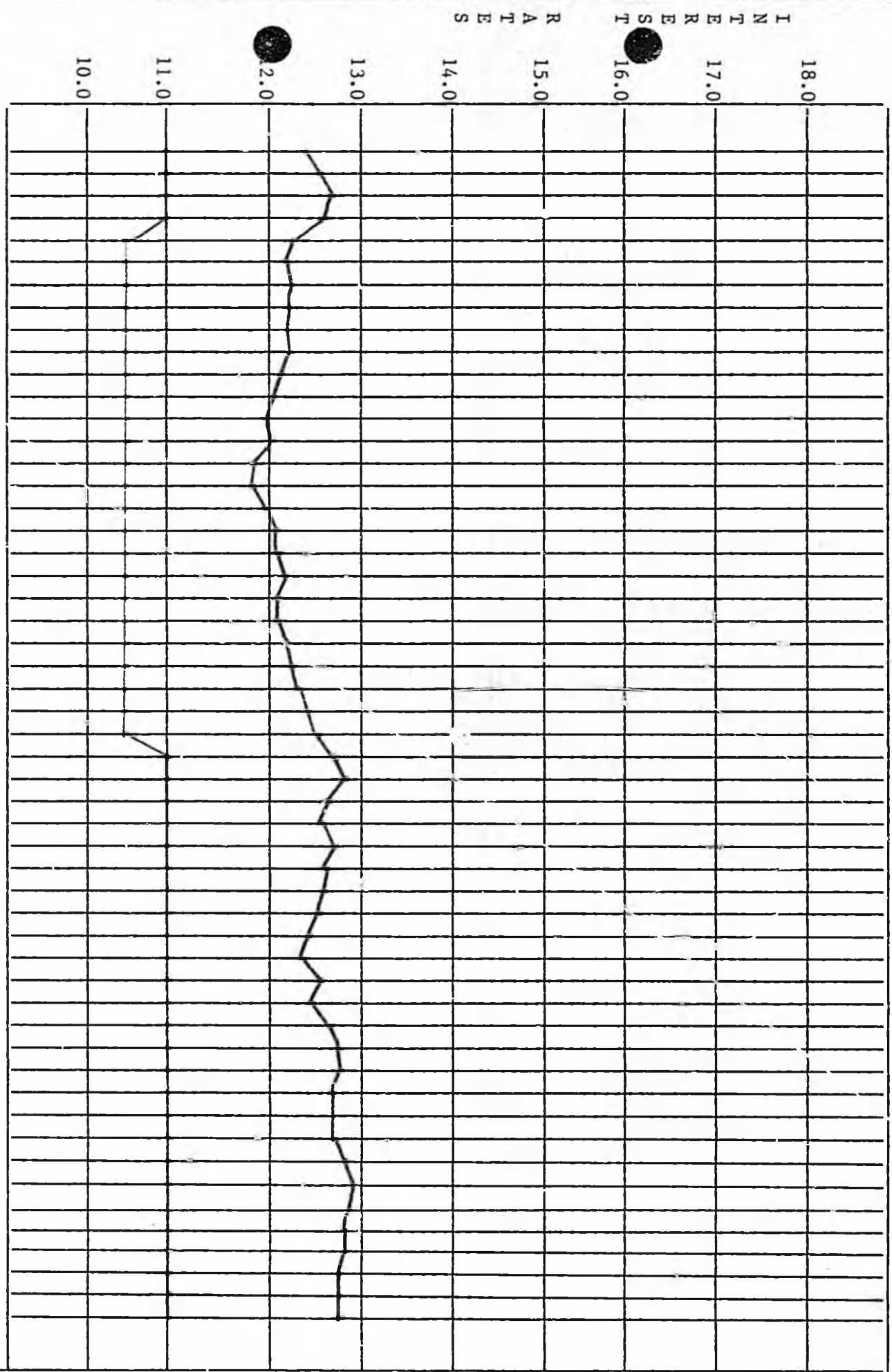


Bertram L. Wagnon
Executive Director

BLW:mr

Rate Comparison Chart
January 1983 - January 1984

Key
Moody's (red)
Prime (blue)



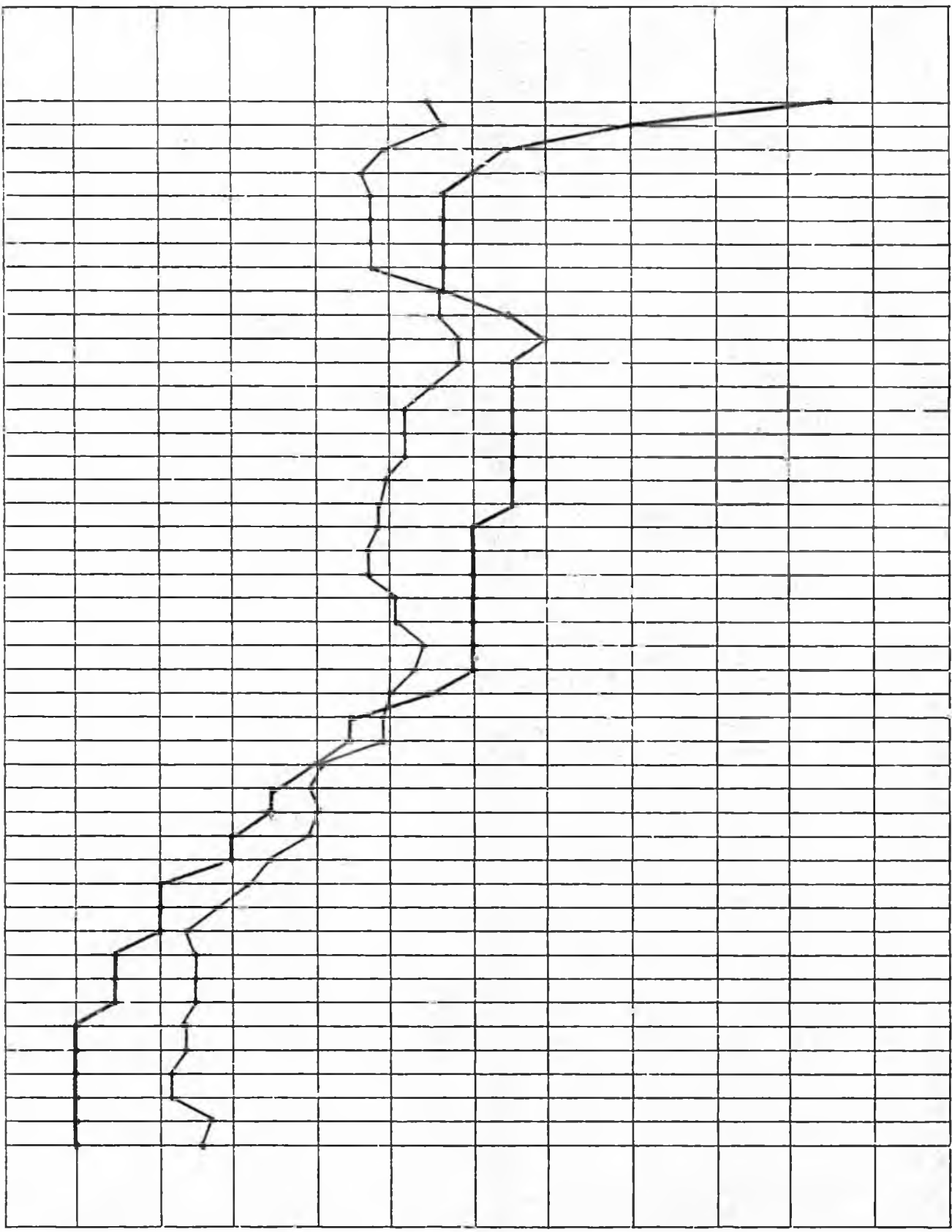
Alaska Industrial Development Authority
 Rate Comparison Chart
 September 1981 - February 1983

I
N
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21.0
20.0
19.0
18.0
17.0
16.0
15.0
14.0
13.0
12.0
11.0
10.0

DATE

- 9/15/81
- 10/15/81
- 11/15/81
- 11/23/81
- 12/14/81
- 12/21/81
- 12/28/81
- 1/04/82
- 1/11/82
- 2/01/82
- 2/15/82
- 2/22/82
- 3/01/82
- 3/08/82
- 3/15/82
- 4/05/82
- 4/19/82
- 4/26/82
- 5/03/82
- 5/17/82
- 6/01/82
- 6/14/82
- 7/05/82
- 7/12/82
- 7/19/82
- 8/02/82
- 8/09/82
- 8/16/82
- 8/23/82
- 8/30/82
- 9/06/82
- 9/13/82
- 9/27/82
- 10/11/82
- 10/18/82
- 11/08/82
- 11/15/82
- 11/22/82
- 12/06/82
- 1/03/83
- 1/10/83
- 1/17/83
- 2/07/83
- 2/14/83
- 2/21/83



Key
 Moody's (red)
 Prime (blue)

Vice Chairman Harper asked if there were any questions or comments and there were none.

Deputy Commissioner Terry Elder entered the meeting at this time.

Vice Chairman Harper then requested a roll call vote.

Upon roll call vote: Mark Lewis - yes, Robert Heath - yes, Lee Coffman - yes, Terry Elder - yes, and with Michael Harper abstaining from voting.

7. DIRECTOR REPORTS/COMMENTS

A. Outstanding Eligibility Resolutions/Bond Sale/SBA Reports

Executive Director Wagon reviewed the summary of eligibility resolutions. He said they are issued basically to determine whether the Authority feels, on a preliminary basis, they qualify for tax-exempt financing. Mr. Wagon stated that approximately 50% of the eligibility resolutions become reality.

Mr. Wagon reviewed the bond sale report with the Board. He said the Authority anticipates having another bond sale perhaps in April.

The Executive Director summarized the SBA report. Mr. Wagon said that statutes mandate that on the SBA program, the Authority's buy rate is Moody's AA Index. Mr. Wagon said that, "SBA places a cap on their rate, but the cap is not based off of Moody's it's based off of prime. The cap reads as follows: term of seven years or less - prime plus $2\frac{1}{4}$, term of greater than seven years - prime plus $2\frac{3}{4}$. Right now we're running a prime of 11% as of yesterday, and if you add $2\frac{3}{4}$ to that you're at 13.75. Moody's AA is running at 12.6 as of last week and I add my 1 to that and it's 13.6. So on the over sevens I'm OK, on the under we have a minor tilt. I understand prime is moving at $10\frac{1}{2}$, if that's the case we could have a problem; and the only remedy I see if it continues to stay out of whack will be legislation. We've done some research and worked on it. I've met with Frank Cox, at SBA, to get his opinion. We've run some graphs of Moody's versus prime to see how far they fall out of sync and when. The obvious answer is to dump Moody's and tie it to prime. That may be the appropriate thing to do, but the Moody's rate does have an interesting characteristic, it's a mellow rate. When prime was at 21, Moody's was at $15\frac{1}{2}$ - which is kind of nice in that maybe when times are bad that's when we're (AIDA) supposed to be helping people out. Yet one of the other characteristics of the Moody rate is that it is a 30-year rate and now that prime's at 11, Moody's is not dropping down fast - and it's now 12.6. By mellow I mean it doesn't move as fast and it kind of stays in a more middle band. If the problem continues, rest

AS44.88.158 DOCUMENT= 1 OF 1 PAGE = 1 OF 2
CHAPTER = 44.88
SECTION = 44.88.158
TITLE = 44

HEADINGS TITLE 44.
STATE GOVERNMENT.
CHAPTER 08.
ALASKA INDUSTRIAL DEVELOPMENT AUTHORITY.
ARTICLE 3.
FINANCIAL PROVISIONS.

CITATION SEC. 44.88.158.

CATCH LINE

SMALL ENTERPRISE LOAN ACCOUNT.

TEXT

(A) A SMALL ENTERPRISE LOAN ACCOUNT IS ESTABLISHED IN THE ENTERPRISE DEVELOPMENT FUND. THE ACCOUNT MAY BE COMPOSED OF MONEY OR ASSETS APPROPRIATED OR TRANSFERRED TO THE AUTHORITY, INTEREST ON INVESTMENTS AND LOANS OF THE SMALL ENTERPRISE LOAN ACCOUNT, THE UNPLEGGED INCOME OF THE ENTERPRISE DEVELOPMENT FUND, AND OTHER MONEY OR ASSETS DEPOSITED IN IT BY THE AUTHORITY.

(B) THE AUTHORITY MAY USE MONEY IN THE SMALL ENTERPRISE LOAN ACCOUNT TO PURCHASE THE GUARANTEED PORTION OF A LOAN MADE BY A PRIVATE FINANCIAL INSTITUTION AFTER JUNE 30, 1981, TO A SMALL ENTERPRISE TO PAY THE COST OF A PROJECT, AS DEFINED IN AS 44.88.220, IF THE LOAN IS GUARANTEED BY THE UNITED STATES OR AN AGENCY OR INSTRUMENTALITY OF THE UNITED STATES, INCLUDING, BUT NOT LIMITED TO, THE SMALL BUSINESS ADMINISTRATION, THE NATIONAL MARINE FISHERIES SERVICE, AND THE FARMERS HOME ADMINISTRATION.

(C) THE AUTHORITY MAY PURCHASE LOANS ORIGINATED BY THE ALASKA RURAL REHABILITATION CORPORATION WHICH ARE MADE TO

AS44.88.158 DOCUMENT= 1 OF 1 PAGE = 2 OF 2

AGRICULTURAL ENTERPRISES. LOANS PURCHASED UNDER THIS SUBSECTION MAY BE SECURED BY SUBSTITUTE COLLATERAL IF THE AMOUNT OF THE LOAN DOES NOT EXCEED 75 PERCENT OF THE VALUE OF THE TOTAL COLLATERAL FOR THE LOAN. LOANS MAY BE PURCHASED UNDER THIS SUBSECTION ONLY FROM MONEY APPROPRIATED TO THE SMALL ENTERPRISE LOAN ACCOUNT FOR THAT PURPOSE.

HISTORY (SEC. 65 CH 106 SLA 1980; AM SEC. 40 CH 115 SLA 1981)

R0601 * END OF DOCUMENTS IN LIST - ENTER RETURN OR ANOTHER COMMAND.