

HB

108

HOUSE COMMITTEE REPORT

2/15

(9)

Date Referred: January 23, 1989

FURTHER REFERRALS: LABOR & COMMERCE
FINANCE

Date of Committee Action: 2-14-89

The RESOURCES Committee recommends that:

HB 108

HOUSE BILL NO. 108

"An Act relating to loans and lending practices of the Alaska Commercial Fishing and Agriculture Bank; providing an exemption for the bank's membership stock and certain other securities issued by the bank from registration under the Alaska Securities Act; and providing for an effective date."

[] be replaced with _____ [] the same title
[] a new title

[] have attached amendment(s)

- do pass
- do not pass
- no recommendation
- individual recommendations
- additional referral to the _____ Committee

ADOPTS: _____ letter of intent

ATTACHES NEW FISCAL NOTE(S):

APPROVES PREVIOUS:

- fiscal impact
- zero fiscal note C + E D
- zero with analysis

- fiscal note(s) published: _____
- zero fiscal notes(s) published: _____

SIGNING DO PASS:

SIGNING OTHER THAN DO PASS:
(Do Not Pass, No Recommendation, Amend)

Cliff Davidson DAVIDSON

George Tacko TACKO

Mike Navarre NAVARRE

W. L. Furnace FURNACE

Scott Sharp SHARP

Bill Hudson HUDSON

Mike Davis M. DAVIS

Scott [unclear]

Cliff Davidson
CO - Chairman's signature

TALKING POINTS ON HB 108 (CFAB)

- Permit drain is a potential problem

-- Studies by the Commercial Fisheries Entry Commission show that in Bristol Bay, there has been a steady loss of permits by local residents since limited entry permits were first issued in 1975

-- In at least some cases, the permits are being sold for the simple reason that some among the first generation of permit holders are beginning to reach retirement age

-- Many would prefer to sell the permit to a family member or other local resident, but find that the local person doesn't have the assets necessary to secure a regular bank loan

-- So, the permit gets sold to someone who can come up with the cash --often someone from outside the rural area or from another state

-- The entry commission says the base of the local fisheries economy in Bristol Bay, to use that area as an example again, is still strong and not yet threatened. But the number of local residents holding permits is declining and it's a situation that requires close watching

-- The documented loss of permits also is a key reason the commission is supporting this bill. It won't end permit drain by itself, but it would be one tool to keep the local economy strong

- How the bill would work

-- This bill would allow CFAB to make a loan to the buyer, with the seller only taking half the proceeds from the sale and joining CFAB as co-lender

-- The seller would earn the market interest rate on the deferred portion of the loan

-- Also, the seller can require the buyer to designate him to retrieve the permit in the event of foreclosure, so there would still be a good chance to keep the permit in the hands of a local fisherman

-- Lastly, the bill would also allow borrowers to pledge more than one permit as security. This would help those holding multiple permits -- but have little ready cash -- who need to borrow money to buy equipment



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P. O. Box 92070
Anchorage, Alaska 99509-2070
(907) 276-2007

RECEIVED FEB 3 1988

February 2, 1989

DELIVERED BY HAND

Representative Cliff Davidson, Co-Chairman
Representative Curt Menard, Co-Chairman
House Resources Committee
Alaska State Legislature
Juneau, Alaska

Dear Co-Chairman Davidson and Menard,

House Bill 108 has been referred to the House Resources Committee for consideration.

This legislation affects the interests of the Alaska Commercial Fishing and Agriculture Bank (CFAB) and its borrowing members, who are resident Alaska commercial fishermen. More specifically, it will create new opportunities or alternative mechanisms through which Alaska residents can acquire or retain limited entry permit ownership.

CFAB is the only private financial institution, and the only entity other than the State of Alaska itself, with the statutory ability to finance the purchase of a limited entry permit and/or to acquire a valid permit lien for collateral purposes. Among the dynamic factors affecting the Alaska commercial fishing industry are a few which increasingly and inexorably tend to create barriers to the purchase of permits by new and/or younger entrants, particularly in Alaska's rural communities. CFAB has developed a concept which can address these barriers in many instances, but the concept cannot be implemented without certain enabling provisions of HB 108.

Our first purpose in writing is to place the matter within a timing context. While there is trafficking in limited entry permits throughout the year, there is an extensive and sharply-defined annual peak of such activity from early March through May. If HB 108 is ultimately to be enacted into law, its benefits to rural Alaska fishermen will be deferred for a year if that enactment is not timely. We respectfully urge that HB 108 receive early consideration.

Our second purpose in writing is to express to you CFAB's willingness and readiness to provide whatever additional information and insights which you believe may enhance the Committee's ability to timely

Alaska Commercial Fishing and Agriculture Bank

Co-Chairmans Davidson and Menard
February 2, 1989
Page 2

and effectively consider HB 108. CFAB's Board of Directors and its management take very seriously their responsibility to carry out the mandates which have been expressed for CFAB by the Legislature; and we view the Legislature as the primary personification of "the State" in its relationship with CFAB. We are most anxious to be responsive. Please understand that we do not presume any particular conclusion to consideration of HB 108 by the Committee or by the Legislature as a whole, but we believe it to be of great importance to Alaska fishermen for those considerations to be both objective and premised on the best information we can provide.

Congratulations for your appointment to this important chair, and best wishes to you and your colleagues for a productive Legislative Session.

Very truly yours,

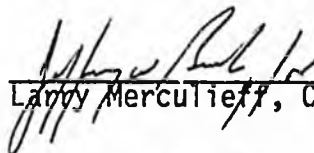


Edward E. Crane
President

EEC:dmy

HB 108: An Act relating to loans and lending practices of the Alaska Commercial Fishing and Agriculture Bank.

The banking section is neutral on this measure. The intent is to facilitate transfers of Limited Entry Permits held as loan security by CFAB. This bill will remove CFAB from securities law regulation for issue of its stock and/or other securities in conjunction with loans to members.


Larry Mercuri, Commissioner

Date: 2/13/89

FISCAL NOTE

REQUEST:

Revision Date: _____
Title: Commercial Fishing and Agri-
culture Bank
Sponsor: Jacko, Grussendorf, et al
Requestor: House Resources

Agency Affected: Commerce & Econ. Dev.
BRU: Banking and Securities
Components: Securities

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 89	FY 90	FY 91	FY 92	FY 93	FY 94
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	-0-	-0-	-0-	-0-	-0-	-0-
CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
REVENUE	-0-	-0-	-0-	-0-	-0-	-0-

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL	-0-	-0-	-0-	-0-	-0-	-0-

POSITIONS:

FULL-TIME	-0-	-0-	-0-	-0-	-0-	-0-
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

No fiscal impact.

Prepared by: L.P. Carroll, Senior Securities Examiner
Division: Banking and Securities

Phone: 465-2521
Date: 02/13/89

Approved by Commissioner: Larry Mercurieff
Agency: Dept. of Commerce and Economic Development

Date: 2/13/89

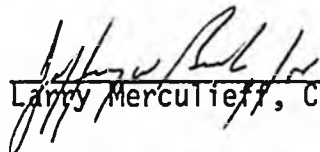
Distribution (by preparer):

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

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HB 108: An Act relating to loans and lending practices of the Alaska Commercial Fishing and Agriculture Bank.

The banking section is neutral on this measure. The intent is to facilitate transfers of Limited Entry Permits held as loan security by CFAB. This bill will remove CFAB from securities law regulation for issue of its stock and/or other securities in conjunction with loans to members.


Larry Merculieff, Commissioner

Date: 2/13/09



Qualitative Examination

License or Certificate Number

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK

(P.O. BOX 92070, 2550 Denali St., Ste. 1201, Anchorage, AK 99509-2070)

Examiner-in-charge

Frank Ruschak

Examined close of business 12/30/87

WILLIS E. KIRKPATRICK

Director

DIVISION OF BANKING, SECURITIES, SMALL LOANS AND CORPORATIONS
STATE OF ALASKA

In compliance with Chapter 81 of the Alaska Statutes as amended June 6, 1987, an examination of the Alaska Commercial Fishing and Agricultural Bank was performed by the Department of Commerce and Economic Development, Division of Banking, Securities and Corporations, that contains financial information prepared in accordance with generally accepted accounting principles.

LOAN PORTFOLIO

Analysis of the examination ratios indicate improvement in the quality of the loan portfolio since the first examination on April 29, 1985. The ratio of adversely classified loans to total loans decreased from 43.70% to 34.98% and the ratio of overdue loans to gross loans decreased from 41.54% to 37.36%. While these ratios are still considered to be above the norms, the trend shows definite improvement.

Of the \$13,965,552 in adversely classified loans, \$12,761,018 are nonearning loans (nonaccrual loans), and of that total, seven borrowers account for \$10,814,726. These seven lines were all granted from 1981 to 1984, prior to the arrival of the present management team. Since four of the seven lines are involved in bankruptcy proceedings, there is little that present management can do to accelerate resolution of these problem lines.

The reserve for loan losses has been increased to \$3,427,597, or 7.70% of total loans, and given loss classifications of \$1,891,586 appear adequate to provide the necessary loss protection.

BANK POLICIES AND PRACTICES

Since 1984, the senior management of the bank has been entirely replaced. As evidenced by the examination ratios and trends, there has been significant improvement in the bank's performance. The problem loans have been identified and are being handled as well as circumstances permit. In addition, a new loan policy was adopted, and the loan approval procedure is more closely controlled and monitored.

It is difficult, at best, to make the higher credit-risk loans as mandated by statute and still remain a viable business. The nonearning loans are the largest impediment to more profitable operations and the accumulation of capital to provide for growth and to meet statutory obligations. The increased competition from commercial banks and other state programs has taken some of the better quality customers, and the bank must contend with borrowers of greater credit-risk, a higher cost-of-funds, and the nonearning loans. Given the depressed economy, there is little more that can be done. However, with the present policies and practices, the condition of the bank is such that it appears capable of withstanding the current economic depression.

State Banking Authority (Signature) Frank J. Puschak by: Terry L. Lutz	State Banking Authority (Signature) William F. [Signature]
Examiner (Signature) Frank J. Puschak	Regional Director (Signature)

ASSETS	AMOUNT	%	LIABILITIES AND CAPITAL	AMOUNT	%
Net loans and leases	41,113	84	Core deposits		
Securities over one year			Time deposits over 100M		
Subtotal	41,113	84	Deposits held in foreign offices		
Interest bearing depository balances			Federal funds purchased and repos		
Federal funds sold and repos			Other borrowings (includes note option)	20,213	41
Telling account assets			Volatile liabilities	20,213	41
Debt securities one year and less	5,390	11	Acceptances outstanding		
Temporary investments	5,390	11	Other liabilities	878	2
TOTAL EARNING ASSETS	46,503	95	TOTAL LIABILITIES	21,091	43
Cash and noninterest bearing depository balances	961	2	Mortgages and capitalized leases		
Acceptances (customers' liability)			Subordinated notes and debentures		
Premises, fixed assets, and capitalized leases	250	nil	TOTAL LIABILITIES AND DEBT	21,091	43
Other real estate owned			Limited life preferred stock	31,800	65
Investments in unconsolidated subsidiaries			TOTAL EQUITY CAPITAL	(3,671)	8
Intangible assets					
Other assets	1,506	3			
TOTAL ASSETS	49,220	100%	TOTAL LIABILITIES AND CAPITAL	49,220	100%

MEMORANDUM INFORMATION (Include the amounts of brokered deposits maturing in one year or less and over one year.)

* Matures on or before July 20, 2000

SUMMARY OF ASSETS SUBJECT TO ADVERSE CLASSIFICATION OR SPECIAL MENTION

ASSET CATEGORY	Special Mention	Substandard	Doubtful	Loss	Total Classified
Loans		12,283		1,682	13,965
Receivables		1,615			1,615
Other Assets		83		209	292
Totals - Current Examination		13,981		1,891	15,872
Totals at 4/29/85 examination		35,891		3,317	39,208
Totals at examination					
Totals at examination					

EXAMINATION RATIOS AND TRENDS

RATIOS	Current Exam.	Prior Exam.	Prior Exam.	Prior Exam.
	11/30/87	4/29/85		
Adversely Classified Assets Total Assets	32.25%	38.78%		
Adversely Classified Loans and Leases Total Loans and Leases	34.98%	43.70%		
Overdue Loans and Leases Gross Loans and Leases	37.36%	41.54%		

COMMENTS:

Examination ratios indicate improvement in reducing adversely classified loans and assets.

Interest Expense	2,240	3,766	6,267	8,387
Net Interest Income	<u>3,334</u>	<u>2,518</u>	<u>4,237</u>	<u>4,524</u>
Non-interest Income				
Overhead Expense	2,440	1,932	2,888	3,260
Provision for Loan and Lease Losses	<u>75</u>	<u>50</u>	<u>1,235</u>	<u>11,242</u>
Provision for Allocated Transfer Risk				
Securities Gains (Losses)				
Net Operating Income (Pre-Tax)	819	536	114	(9,978)
Applicable Taxes	<u>19</u>	<u>226</u>	<u>32</u>	<u></u>
Net Operating Income (After Tax)	800	310	82	(9,978)
Extraordinary Credits (Charges), Net of Tax Effect	<u>19</u>	<u>226</u>	<u>32</u>	<u></u>
Net Income	819	536	114	(9,978)
Other Increases/Decreases	209	220	(348)	(234)
Cash Dividends				
Net Change in Equity Capital Accounts	1,028	756	(234)	(10,212)

COMPONENT RATIOS AND TRENDS

RATIOS	BANK			
	11-30-87	1986*	1985*	1984*
Net Operating Income to Average Assets	1.59%	0.48%	0.09%	(8.72)%
Net Interest Income (TE) to Average Earning Assets	6.51%	4.14%	4.87%	4.22%
Overhead Expense to Average Assets	4.85%	3.02%	3.12%	2.85%
Net Income to Average Total Equity	3.00%	2.01%	0.43%	(31.49)%

COMMENTS:

* Based upon year-end data.

Trend analysis indicates improved earnings, but the increasing trend in overhead expenses means that overhead should be reviewed with the goal of reducing expenses.

ANALYSIS OF LOAN AND LEASE RESERVES

RECONCILEMENT	TO DATE	1986	1985	1984
Beginning Balance	3,291	3,442	5,318	4,140
Gross Loan and Lease Losses	125	889	3,486	10,534
Recoveries	<u>187</u>	<u>688</u>	<u>375</u>	<u>470</u>
Net Loan and Lease Losses (Recoveries)	(62)	201	3,111	10,064
Provision for Loan and Lease Losses	75	50	1,235	11,242
Other Increases (Decreases)				
Ending Balance	3,428	3,291	3,442	5,318

COMPONENT RATIOS AND TRENDS

RATIOS	BANK			
	11-30-87	1986	1985	1984
Loss Reserve to Total Loans and Leases	7.70%	7.41%	5.22%	5.61%
Net Losses to Average Total Loans and Leases	(0.14)%	N/A	N/A	N/A
Recoveries to Prior Period Losses	21.03%	19.74%	3.56%	N/A
Earnings Coverage of Net Losses (X)	(13.20)	2.67	0.37	N/A

COMMENTS:

N/A - Not Available.

A ratio of 7.70% for loss reserve to total loans indicates a conservative and adequate level of reserves.



UNITED FISHERMEN OF ALASKA

211 4th Street, Suite 106
Juneau, AK 99801
907-586-2820

UNITED FISHERMEN OF ALASKA

Resolution 89-1

WHEREAS Alaska has a system of limited entry that regulates participation in many of the commercial fisheries of the state, and

WHEREAS in many of the rural areas of the state there has been a permit drain caused by sales of locally owned permits to persons living outside of the area, and

WHEREAS the permit drain is detrimental to the economies of rural Alaska, and

WHEREAS the opportunity for some Alaskans to obtain financing for the purchase of permits is limited by lending requirements that they cannot satisfy, and

WHEREAS the Alaska Commercial Fishing and Agriculture Bank was created to serve the credit needs of resident Alaska fishermen, and

WHEREAS CFAB has developed a concept that would increase the opportunities for Alaskans to obtain permit financing, and

WHEREAS the implementation of the CFAB concept will require changes to the statute that governs the cooperative,

NOW THEREFORE BE IT RESOLVED that United Fishermen of Alaska endorses and supports the creation of a loan program that will increase the opportunities for more Alaskans to purchase limited entry permits, and

BE IT FURTHER RESOLVED that United Fishermen of Alaska supports the purposes and intents of Senate Bill 82 and House Bill 108.

Theo Matthews
Theo Matthews
President

Feb 14, 1989
Date

FEB 8 1989

**Bristol Bay
Native Corporation**

800 CORDOVA / P.O. BOX 100220 / ANCHORAGE, ALASKA 99510 / (907) 278-3602
TELECOPY (907) 276-3924

February 6, 1989

Honorable Fred Zharoff
Alaska Senate
P.O. Box V
Juneau, Alaska 99811

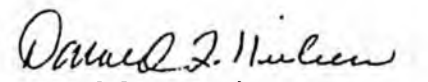


Dear Senator Zharoff:

We understand that you are the prime sponsor, with ten of your colleagues as co-sponsors, of Senate Bill 82. The basic effect of SB-82, if passed, will be to allow the Alaska Commercial Fishing and Agriculture Bank (CFAB) to implement a concept which addresses the financing of limited entry permit purchases. In particular, CFAB's concept would provide a potential means of assisting in a situation where a permit holder is motivated to sell his or her permit to a younger family member or other local resident who is unable to obtain financing under conventionally available terms.

At Bristol Bay Native Corporation, we are very much aware of the increasing difficulty of retaining permit ownership in Alaska's rural communities. Your understanding of the matter is evidenced by the introduction of SB-82. We commend you and your colleagues, and we want to express our support for that legislation and for any effort which will enhance CFAB's ability to be a more constructive factor toward the retention of limited entry permit ownership in rural communities.

Very truly yours,


Donald F. Nielsen
Senior Vice President

cc: Honorable George Jacko
Bristol Bay Native Association

SENATOR FRED F. ZHAROFF

ALASKA STATE LEGISLATURE

P.O. BOX 405, KODIAK, ALASKA 99615 (907) 486-5259

DURING SESSION:


P.O. BOX V, JUNEAU, ALASKA 99811 • (907) 465-3473 • 465-3474

DISTRICT N

ALASKA PENINSULA • ALEUTIAN CHAIN • BRISTOL BAY • KODIAK ISLAND • LAKE CLARK/LAKE ILIAMNA • PRIBILOF ISLANDS • SHUMAGIN ISLANDS

MEMORANDUM

TO: Senator Bettye Fahrenkamp
Chair
Senate Resources Committee

FROM: Senator Fred F. Zharoff 

DATE: January 12, 1989

RE: Senate Bill 82 - "An Act relating to loans and lending practices of the Alaska Commercial Fishing and Agriculture Bank; providing an exemption for the bank's membership stock and certain other securities issued by the bank from registration under the Alaska Securities Act; and providing for an effective date."

I respectfully request that SB 82 be scheduled for a hearing at the Resources Committee's earliest convenience.

SB 82 would allow the Alaska Commercial Fishing and Agriculture Bank (CFAB) to establish a new program that will help keep limited entry permits in the hands of Alaska residents.

The new program will be especially applicable to those situations in which a commercial fisherman wishes to liquidate his fishing operation by selling his or her limited entry permit to a specific resident fisherman -- frequently a younger family member -- who has little cash and who, alone, is not perceived to be sufficiently creditworthy to be granted a permit purchase loan. Under the new program, a seller may share in the credit risk of a CFAB-financed permit purchase by using a portion of the sale proceeds to purchase a participation in the loan involved. The seller's financial interest is protected because of CFAB's ability to foreclose its permit lien in the event of irremediable default. Also, if desired, the seller can retrieve the permit by having the purchaser (the borrower) designate the seller as the person to assume the debt in the event of default and foreclosure.

As an investment, the loan participation certificate will allow the seller to receive the market interest rate on the deferred portion of the sale proceeds.

The program offers an alternative to what is commonly called "permit migration" or "permit drain". Under current circumstances, a rural permit holder -- unable to find a local fisherman with the financial capacity to buy the permit -- concludes there is no alternative other than to sell the permit to an urban Alaskan or nonresident who can raise the cash upfront.

The bill also makes a number of miscellaneous amendments to CFAB's statute.

Attached is a sectional analysis explaining how the bill works. The sections related to the program described above are Sec. 2, (f) in Sec. 3, Sec. 6, and Sec. 9.

Also included is a copy of CFAB's most recent annual report. I have requested position statements from the Commercial Fisheries Entry Commission and the Division of Banking, Securities and Corporations to use as backup information, but have not yet received them. I will provide them to the committee as soon as they are available.

It is crucial that SB 82 be acted on as soon as possible in order for the new program to be effectively utilized by Alaskan fishermen in 1989. Even though limited entry permits are bought and sold throughout the year, the market sees the most activity and peaks in the period between early March and May.

Thank you for your consideration of this request.



SENATOR FRED F. ZHAROFF
ALASKA STATE LEGISLATURE

P.O. BOX 405, KODIAK, ALASKA 99615 (907) 486-5259

DURING SESSION:

P.O. BOX V, JUNEAU, ALASKA 99811 • (907) 465-3473 • 465-3474

DISTRICT N

ALASKA PENINSULA • ALEUTIAN CHAIN • BRISTOL BAY • KODIAK ISLAND • LAKE CLARK LAKE ILIAMNA • PRIBILOF ISLANDS • SHUMAGIN ISLANDS

SECTIONAL ANALYSIS

Senate Bill No. 82 - "An Act relating to loans and lending practices of the Alaska Commercial Fishing and Agriculture Bank; providing an exemption for the bank's membership stock and certain other securities issued by the bank from registration under the Alaska Securities Act; and providing for an effective date."

SECTION 1 PURPOSE.

Explains the rationale behind the bill.

SECTION 2

New paragraph (12) added to 44.81.210(a).

Gives CFAB the power to issue loan participation certificates.

SECTION 3

New subsections (e) and (f) added to 44.81.230.

(e) Allows a borrower to pledge more than one limited entry permit as security for a loan. This will be of benefit to fishermen who have multiple permits and are trying to expand their operations. They will be able to use their limited entry permits as financial assets to leverage the funds they need to purchase vessels, gear, etc. They can diversify and spread fixed costs over more fisheries. This will be of particular benefit to fishermen who have little liquidity, but substantial equity in existing permits.

(f) Allows a borrower to nominate another person to assume the debt on a permit loan. This way the individual who holds a loan participation certificate can take over the loan in the case of foreclosure.

SECTION 4

Amendment to subsection (b) in 44.81.235.

Corrects an oversight in the existing statute by allowing a loan made to purchase a limited entry permit to be included when a single permit is pledged to secure multiple loans.

SECTION 5

Amendment to subsection (c) in 44.81.235.

Corrects an oversight in the existing statute by allowing CFAB to refinance a loan which is made to purchase a limited entry permit. Under the current statute, CFAB may accept a permit as collateral when refinancing loans for fishing vessels, fishing gear, set net sites, and working capital, but not loans which are for the purchase of a permit.

SECTION 6

Amendment to subsection (b) in 44.81.250.

Makes this section of the existing CFAB statute consistent with the amendment in paragraph (f) of Section 3, above, by including a reference to the nomination of a person to assume debt.

SECTION 7

Amendment to subsection (d) in 44.81.250.

Adds reference to loans for the purchase of limited entry permits to the statute regarding CFAB's legal rights during foreclosure.

SECTION 8

New subsection (e) added to 44.81.250.

Describes the procedure CFAB shall follow when it has repossessed a limited entry permit.

SECTION 9

New paragraph (12) added to 45.55.140(a).

Exempts CFAB from the state's securities registration requirements. This restores the exemption CFAB had in statute when it was originally created. The exemption is currently granted to banks, savings institutions, savings and loan associations, trust companies, foreign governments, employee benefit plans, insurance companies, credit unions, nonprofit organizations, and others. The exemption will allow CFAB to offer loan participation certificates and remove the question of whether this transaction must comply with the extensive requirements for securities registration. CFAB will still be subject to annual audits by the Division of Banking, Securities and Corporations, an independent outside auditor, and, upon legislative instruction, by the Legislative Audit Division, as provided for in 44.81.270.

SECTION 10

Immediate effective date.

RECEIVED JAN 12 1989

STEVE COWPER, GOVERNOR

COMMERCIAL FISHERIES ENTRY COMMISSION

P.O. BOX KB
JUNEAU, ALASKA 99811-0302
PHONE: (907) 465-4081

January 11, 1989

The Honorable Fred F. Zharoff
Alaska State Legislature
M/S 3100

Re: CFAB Legislation
SB 82

Dear Senator Zharoff:

Thank you for the opportunity to review your legislation introduced on behalf of the Alaska Commercial Fishing and Agriculture Bank, which I understand has become SB 82.

CFAB's president, Mr. Ed Crane, developed the idea behind the legislation about a year ago, and we have discussed the proposal with him a number of times since then. We are very pleased that CFAB perceived the need and took the initiative to develop this remedy. We also commend you for having introduced this legislation.

SB 82 appears to the Entry Commission to be sound. For those Alaskan fishermen wishing to take advantage of such an opportunity, this legislation should be helpful. In direct response to your question, we would be happy to support this legislation. Please do not hesitate to contact us, if we can provide you with any further information.

Cordially,

COMMERCIAL FISHERIES ENTRY COMMISSION

Bruce Twomley, Chairman
Rich Listowski, Commissioner
Phil Smith, Commissioner

by: _____

cc: Bob Evans
Deputy Chief of Staff
Office of the Governor
M/S 0101



1988 ANNUAL REPORT
ALASKA COMMERCIAL FISHING & AGRICULTURE BANK

Alaska Commercial Fishing and Agriculture Bank

1988 Annual Report

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For more information contact:

Alaska Commercial Fishing and
Agriculture Bank
2550 Denali Street, Suite 1201
Anchorage, Alaska 99503
(907) 276-2007 or (800) 544-2228

Executive Message to Members

May 31, 1988, marked the close of CFAB's first twelve-month fiscal year after seven years of operating on a calendar year basis and a five-month transition "year" which ended on May 31, 1987. While that makes certain kinds of comparisons difficult, your Board of Directors and management are pleased with the results of the year just ended and with the identifiable and measurable indications of continued progress.

Operating Results and Effects

As shown in the Financial Reports section of this Annual Report, CFAB's Fiscal 1988 operations resulted in about \$2,410,200 of proceeds before non-recurring items and before the imputation of any income tax effect. There was one particularly distressing and costly extraordinary event: In late 1987 an Anchorage Superior Court jury concluded that, several years earlier, CFAB had negligently and improperly responded to developments and circumstances which involved a multiplicity of parties, a loan proposal to finance a vessel refurbishing, and an undisclosed seaman's lien. There were \$688,500 of net proceeds available after the effects of that judgment, and the Board of Directors acted to apply that amount to reduction of the unallocated and undistributed 1984 loss. One of our major objectives continues to be to amortize that loss in a manner which will equitably spread the burden over a number of years.

The gradual reduction of that unallocated and undistributed 1984 loss produces a clear benefit to existing and future CFAB member-borrowers. But the effect of that benefit is diffused; no member-borrower is able to identify or calculate a specific effect on his or her loan account. However, the factors and events which led to that reduction do in fact have the additional effect of lessening the demands CFAB must make on those member-borrowers. Accordingly, we were pleased to announce a ½ percent reduction in CFAB's Variable Base Interest Rate effective July 1, 1988. Furthermore, as this message is being written there are plans to implement a second reduction, also ½ percent, effective September 1, 1988.

The Trend Toward Financial Stability

What were these "factors" and "events" which are now generating benefits and relieving pressures for CFAB and its member-borrowers? The answer can be found in a review of earlier Annual Reports. Since 1984, there has been in each report to members a discussion of CFAB's burden of non-performing loans. Each of those non-performing loans represents dollars which CFAB has borrowed and on which it must pay interest; but since the non-performing loan is not itself producing interest, CFAB has necessarily relied on other member-borrowers to carry the extra burden. Any interested observer of the Alaska commercial banking community over the past several years can undoubtedly understand and appreciate the dangers which an excessive volume of non-performing loans present for a lending institution.

Although this report to members is about CFAB's operations in Fiscal 1988, a clearer and somewhat more dramatic view of the significance of non-earning loans and of the slow and difficult process of dealing with them can be gained by comparing data at May 31, 1988, and at May 31, 1985 (which was not an audit date). The following schedule shows the number of borrowers with non-earning loans of \$1,000,000 or more; \$500,000 to \$999,999; etc. as of those two dates.

Size of Loan Accounts	May 31, 1985		May 31, 1988	
	Number of Borrowers	Total	Number of Borrowers	Total
Over \$1,000,000	7	\$20,165,695	2	\$ 5,300,515
\$500,000/\$999,999	4	2,552,087	2	1,548,479
\$250,000/\$199,999	5	1,644,819	3	988,641
\$100,000/\$249,999	11	2,041,415	7	1,051,154
\$50,000/\$99,999	15	1,054,709	9	732,983
Under \$50,000	24	507,587	19	424,833
Totals	66	\$27,966,312	42	\$10,046,605

The reduction of about \$17.9 million in non-earning loans during the 3-year period is certainly a positive indicator of CFAB's relative financial health, but unless that reduction has been the result of cash proceeds or of conversion to an interest-earning asset — rather than the result of charge-offs or of acquisition of non-productive collateral — it has little constructive effect.

The schedule below, then, serves to make more evident what the actual effect of the non-earning loan reduction has been.

	May 31, 1985	May 31, 1988	Change
Investments	\$ 3,200,000	\$ -	(\$ 3,200,000)
Earning Loans and Receivables	56,566,400	31,569,700	(24,996,700)
Total Earning Assets	59,766,400	31,569,700	(\$28,196,700)
Less: Interest-Bearing Debt	67,660,000	18,649,700	(49,010,300)
Net (Deficit) Earning Assets	(\$ 7,893,600)	\$ 12,920,000	\$ 20,813,600

The positive change of nearly \$21.0 million (an amount well in excess of the \$17.9 million reduction in non-earning loans) is a meaningful indication of CFAB's viability today. We believe and intend that Fiscal 1989 will mark the transition from a "rehabilitation" mode to one of controlled growth for CFAB.

Achievements in Overhead Reductions

There is another important element to CFAB's recovery in which we take special pride and which we must mention. It was evident three and one-half years ago that CFAB's basic operating costs — its "overhead" — needed to be drastically reduced, even while we were committing major and sometimes costly resources to the administration and liquidation of non-performing loans. Those operating expenses had averaged slightly more than \$3.2 million annually in the years 1981 through 1984. In calendar 1985, they were reduced to \$2.8 million. There was significant reduction, to \$1.9 million, in calendar 1986. For the five-month fiscal "year" ending in May 1987 those expenses were incurred at an annualized rate of about \$2.0 million. The total for fiscal 1988 was less than \$1.8 million. That represents a 47 percent reduction from CFAB's peak year (1982) for operating expenses, and translates into \$3,300 less annualized costs for **each and every** loan on CFAB's books at May 31, 1988!

While we take pride in the accomplishment just mentioned, there is greater pride in emphasizing to you that it was essentially an accomplishment of CFAB's entire staff. Directors and managers establish objectives and policies, and provide direction, but implementation and achievement requires the constant and committed effort of every single staff member at every level. CFAB's staff today is a small

group, in numbers; but its overall quality and its record of accomplishments are admired within the Alaska financial community. As owners of CFAB, you also should take pride in that staff.

Other Measures of Progress

There are a number of other matters, with varying levels of significance and visibility, which developed or occurred during Fiscal 1988:

- At the end of the year, member-borrowers' equity investment under the "new" Class B Preferred Stock program totaled \$1,053,400. While there is no special meaning to that number, we believe that exceeding \$1.0 million is a notable milestone for the 2½-year-old program.
- As of November 30, 1987, the State of Alaska's bank examiners performed the first annual examination of CFAB in accordance with statutory amendments proposed by CFAB, and passed by the legislature, in early 1987. In every substantive way, the examiners' findings and report were consistent with CFAB's own evaluation of its overall financial condition and of its loan portfolio.
- CFAB's Bylaws were amended by the Board of Directors and distributed to all members in May. There were numerous changes. Particular objectives, which we believe were achieved, were to make the procedures for nominating Director candidates, and for the election of Directors, simpler and more efficient as well as to make it more practically possible for any interested member to become a candidate.
- The exposure and delivery of CFAB's credit services to prospective applicants is being enhanced by our development of a Loan Correspondent program. This program, simple in concept but with significant potential impact, involves the selection and designation of businesspersons or professionals to act as liaisons or points of contact for CFAB in fishing communities around the state. Their role is to provide basic information about CFAB to inquirers and to offer assistance in organizing and preparing loan applications and supporting information, in communications with CFAB, and in finalizing a loan transaction. They are not CFAB employees, and they have no influence on CFAB's

decision-making process; but they can be vital links in what is sometimes a confusing, intimidating, and/or costly application process. As of this writing, CFAB has Loan Correspondents in various communities in Southeastern Alaska and in the Prince William Sound, Southcentral, and Kodiak areas — by the end of 1988, we hope to have the network extended into the Bristol Bay area and Western Alaska.

- For a period from December 1983 through the end of 1985, CFAB had in place a supplemental member investment program known as the "C Stock Redemption Plan." It was intended to accelerate the accumulation of member-borrower equity, in anticipation of the future need to retire the State's equity investment in the Bank. Member-borrowers whose loans were obtained or modified during the period mentioned were participants in the program and continued to make the required investments, so long as their respective loans were outstanding, through the end of 1987.

Because of perceived ineffective or inappropriate features of the C Stock Redemption Plan, CFAB's "new" Class B Preferred Stock program (mentioned earlier) was adopted in January 1986 as a primary vehicle for borrower-member equity investment in the Bank. In early 1988 the Board of Directors concluded that, as a matter of practicality and equitability, the relatively small amount — \$251,919 — of C Stock Redemption Plan investment should be retired, with the proceeds returned to the owning member-borrowers. That was accomplished as of March 31; depending upon the respective circumstances of member-borrowers' loan accounts, the proceeds were paid in cash or applied to outstanding balances or, in instances where the Bank had earlier recognized a loss of principal or interest, were transferred to CFAB's Allowance for Loan Losses account.

- In January 1986, CFAB introduced its Modified Level Payment loan program — a fairly simple concept within which a loan's repayment installment amounts were fixed for three years at a time, even though the interest rate might vary. At the time of introduction, we believed that loan structure might appeal to some borrowers as a desirable alternative to the traditional repayment requirement of fixed principal amounts plus interest. CFAB's borrowers have voted by their actions, however, and by an overwhelming margin they have been selecting the Modified Level Payment plan as most suitable to their needs.

- Since June 1987, and as a result of amendments to CFAB's statute passed by the 1987 State Legislature, the circumstances under which CFAB may accept a Limited Entry Permit as loan collateral have been broadened. We have seen a considerable increase in the demand for such loans, a trend toward establishing permits as more useful assets for Alaska fishermen.

As the prices for which many permits are traded creep higher, and as an increasing number of the earliest permit holders reach retirement age, we have encountered many instances in which the potential or desired sale of a permit to a younger local fisherman — frequently a second generation member of the same family — cannot be completed because the intended buyer is not able to make a cash purchase and has not acquired sufficient resources or experience to warrant normal financing by CFAB. We have developed a concept under which we believe CFAB could properly and constructively provide financing in certain of those cases, but the concept cannot be implemented without further amendment to CFAB's statute. We intend to ask the 1989 State Legislature for those amendments.

The 1988 Annual Meeting

In 1986 and 1987, CFAB held its Annual Meetings in three sessions each — sessions were held in Ketchikan, Cordova, Sitka, Kodiak, and Anchorage (twice). The Board of Directors and management continue to be attracted to the philosophical arguments in favor of holding meeting sessions in local communities, but it has not been a successful approach in terms of overall attendance. We have concluded to hold the 1988 meeting in one session, in Anchorage, only; but we are also exploring the feasibility of re-instituting local and informal meetings throughout the year, involving a limited number of CFAB personnel, in order to provide communications opportunities for more members. We welcome members' suggestions.

Paul A. Huppert
Chairman, Board of Directors

Edward E. Crane
President

1988 Loan Activity and Economic Impact

CFAB's Board of Directors and management continue to believe that the very existence of the Bank is a major and positive factor for participants in the resource industries which it serves — particularly those participants in the seafood industry. The number of sources of financing to that industry, especially to the harvester segment, is quite limited; and CFAB's presence in the market provides a strong competitive element.

During the past three to four years, the focus of CFAB's staff, and of the institution as a whole, has been primarily on rehabilitation and on the management of its non-earning loan accounts. The Bank has not been aggressive in seeking new business, and it appears to have been generally perceived over that period as an unattractive lender. Consequently, CFAB's outstanding loan volume has shrunk dramatically since a year-end peak of \$103.6 million at December 31, 1983.

That shrinkage slowed in Fiscal 1988. At May 31, outstanding loan balances were about 6 percent less than at May 31, 1987. There were 111 new term loans made during Fiscal 1988. Those loans totaled about \$7,706,000, of which \$1,303,000 was to refinance existing loans; the remaining \$6,403,000 was "new" money. Of the 111 loans made, 44 were to existing CFAB members, but 67 involved totally new members. That latter number is gratifyingly high in comparison to the experience of the previous three years.

CFAB's impact is manifested in other ways. In addition to the new term loans mentioned above (most of which were to individual fishermen), the Bank established seasonal revolving lines of credit totaling \$18.3 million for processors during Fiscal 1988. Nearly \$17 million of that amount was in the seafood industry; the remainder was for timber processing. A major percentage of the dollars borrowed by these Alaskan processors is for their purchases from fishermen, so CFAB's position in the flow of proceeds to fishermen from the ultimate purchasers of finished products is extremely important.

Balance Sheets

	<u>May 31,</u>		<u>December 31,</u>
	<u>1988</u>	<u>1987</u>	<u>1986</u>
Assets			
Cash	\$ 126,046	\$ 7,315	\$ 147,410
Temporary investments			4,150,000
Loans and other receivables, net of allowance for loan losses of \$2,197,140, \$3,367,869 and \$3,291,026	39,419,164	41,010,553	41,130,799
Accrued interest receivable	2,001,891	2,384,196	1,306,952
Investment in Spokane Bank for Cooperatives	5,526,629	5,390,548	5,390,548
Bank premises, furniture and equipment, net	169,920	297,266	351,874
Acquired assets held for sale	85,589	83,007	83,007
Other assets	13,389	23,511	28,997
	<u>\$47,342,628</u>	<u>\$49,196,396</u>	<u>\$52,589,587</u>
Liabilities			
Accounts payable and accrued expenses	\$ 138,482	\$ 231,523	\$ 191,979
Accrued interest payable	290,327	388,743	233,634
Class B preferred stock subscriptions	5,700		60,163
Notes payable	18,649,657	21,293,770	25,002,539
	<u>19,084,166</u>	<u>21,914,036</u>	<u>25,488,315</u>
Commitments and Contingent Liabilities (Note II)			
Capital and patronage			
Share capital -			
Class C special preferred stock, \$10,000 par value, authorized 4,000 shares, outstanding 3,180 shares	31,800,000	31,800,000	31,800,000
Class B preferred stock, \$100 par value, authorized 400,000 shares, outstanding 31,287, 39,693 and 40,410 shares	3,128,700	3,969,300	4,041,000
Loans receivable on Class B preferred stock	(2,075,300)	(3,448,700)	(3,698,500)
Class A membership stock, \$10 par value, authorized 10,000 shares, outstanding 1,068, 1,001 and 975 shares	10,680	10,010	9,750
	<u>32,864,080</u>	<u>32,330,610</u>	<u>32,152,250</u>
C stock retirement pool		251,919	184,930
Capital in excess of par value	95,310	89,280	86,940
Contributed capital	144,626	144,626	144,626
	<u>33,104,016</u>	<u>32,816,435</u>	<u>32,568,746</u>
Allocated undistributed patronage	825,691	825,691	825,691
Net proceeds		147,708	535,780
Unallocated patronage deficit	(5,671,245)	(6,507,474)	(6,828,945)
	<u>28,258,462</u>	<u>27,282,360</u>	<u>27,101,272</u>
	<u>\$47,342,628</u>	<u>\$49,196,396</u>	<u>\$52,589,587</u>

See notes to financial statements.

Statements of Net Proceeds

	Year ended May 31, 1988	Five months ended May 31, 1987	Year ended December 31, 1986
Interest Income			
Interest on loans and other receivables	\$5,712,091	\$1,966,333	\$6,119,445
Interest on temporary investments	3,707	30,990	165,143
	<u>5,715,798</u>	<u>1,997,323</u>	<u>6,284,588</u>
Interest expense			
Loss on sale of assets	1,936,013	964,863	3,765,900
Provision for loan losses	37,799	4,526	1,347
	<u>(451,699)</u>	<u>49,300</u>	<u>50,470</u>
	<u>1,522,113</u>	<u>1,018,689</u>	<u>3,817,717</u>
	<u>4,193,685</u>	<u>978,634</u>	<u>2,466,871</u>
Other Expenses			
Salaries and benefits	1,233,697	512,117	1,184,760
Occupancy expense	170,808	82,599	203,379
Depreciation and amortization	92,086	45,422	131,789
Travel, lodging and meals	59,089	25,370	66,219
Professional fees	58,149	84,415	110,181
Office operations	47,182	31,951	64,246
Advertising and promotion	41,129	20,832	67,861
Directors' fees	31,725	7,500	25,650
Telephone and postage	26,899	14,399	40,484
Miscellaneous	22,680	6,321	36,522
	<u>1,783,444</u>	<u>830,926</u>	<u>1,931,091</u>
	<u>2,410,241</u>	<u>147,708</u>	<u>535,780</u>
Unusual Item - Costs and Settlement of Litigation	<u>1,721,720</u>		
Proceeds before income tax expense and extraordinary credit	688,521	147,708	535,780
Income tax expense	274,000	53,000	226,300
Proceeds before extraordinary credit	<u>414,521</u>	<u>94,708</u>	<u>309,480</u>
Extraordinary credit — Utilization of net operating loss carryforward	<u>274,000</u>	<u>53,000</u>	<u>226,300</u>
Net Proceeds	<u>\$ 688,521</u>	<u>\$ 147,708</u>	<u>\$ 535,780</u>

See notes to financial statements.

Statements of Changes in Capital and Patronage

	Share capital	C stock retirement pool	Capital in excess of par value
Balance, January 1, 1986	\$31,809,310	\$ 92,152	\$ 82,980
Issuance (redemption) of stock during the year:			
Class B preferred stock, 25,435 shares, net	(2,543,500)		
Class A stock, 44 shares	440		3,960
C Stock retirement pool:			
Class B preferred stock assessments, net of assessments receivable		92,778	
Reduction in loans receivable on Class B preferred stock	2,886,000		
Loan principal charged against allocated undistributed patronage			
Net proceeds			
Balance, December 31, 1986	32,152,250	184,930	86,940
Amortization of unallocated patronage deficit			
Issuance (redemption) of stock during the period:			
Class B preferred stock, 717 shares, net	(71,700)		
Class A stock, 26 shares	260		2,340
Reduction in loans receivable on Class B preferred stock	249,800		
C stock retirement pool:			
Class B preferred stock assessments, net of assessments receivable		66,989	
Patronage refunds paid			
Net proceeds			
Balance, May 31, 1987	32,330,610	251,919	89,280
Amortization of unallocated patronage deficit			
Issuance (redemption) of stock during the year:			
Class B preferred stock, 8,406 shares, net	(840,600)		
Class A stock, 67 shares	670		6,030
Reduction in loans receivable on Class B preferred stock	1,373,400		
C stock retirement pool:			
Retirement of Class B preferred stock assessments		(251,919)	
Net proceeds			
Amortization of unallocated patronage deficit			
Balance, May 31, 1988	<u>\$32,864,080</u>	<u>\$ —</u>	<u>\$ 95,310</u>

See notes to financial statements.

Contributed capital	Allocated undistributed patronage	Net proceeds	Unallocated patronage deficit	Total
\$ 144,626	\$1,045,365	\$ -0-	\$(6,828,945)	\$26,345,488
				(2,543,500)
				4,400
				92,778
				2,886,000
	(219,674)			(219,674)
		535,780		535,780
<u>144,626</u>	<u>825,691</u>	<u>535,780</u>	<u>\$(6,828,945)</u>	<u>27,101,272</u>
		(321,471)	321,471	
				(71,700)
				2,600
				249,800
				66,989
		(214,309)		(214,309)
		147,708		147,708
<u>144,626</u>	<u>825,691</u>	<u>147,708</u>	<u>\$(6,507,474)</u>	<u>27,282,360</u>
		(147,708)	147,708	
				(840,600)
				6,700
				1,373,400
				(251,919)
		688,521		688,521
		(688,521)	688,521	
<u>\$ 144,626</u>	<u>\$ 825,691</u>	<u>\$ -</u>	<u>\$(5,671,245)</u>	<u>\$28,258,462</u>

Statements of Changes in Financial Position

	Year ended May 31, 1988	Five months ended May 31, 1987	Year ended December 31, 1986
Source of Funds:			
From operations			
Net proceeds	\$ 688,521	\$ 147,708	\$ 535,780
Items not requiring the use of funds:			
Depreciation and amortization	92,086	45,422	131,789
Provision for loan losses	(451,699)	49,300	50,470
Loss on sale of assets	37,799	4,526	1,347
Funds provided from operations	366,707	246,956	719,386
Net proceeds from sale of assets		4,660	1,368
Proceeds from stock issuance	6,700	2,600	4,400
Decrease in cash		140,095	
Decrease in temporary investments		4,150,000	
Decrease in acquired assets held for sale			1,523,157
Decrease in loans	2,762,118	43,403	21,515,111
Recoveries on loans charged off, net		27,543	
Decrease in other assets	10,122	5,486	61,566
Decrease in accrued interest receivable	382,305		808,394
Increase in accounts payable and accrued expenses		39,544	
Increase in accrued interest payable		155,109	
Increase in Class B preferred stock subscriptions	5,700		60,163
Increase in Class B preferred stock assessments, net		66,989	92,778
Increase in Class B preferred stock, net	532,800	178,100	342,500
	<u>\$4,066,452</u>	<u>\$5,060,485</u>	<u>\$25,128,823</u>
Use of Funds:			
Loans charged off, net of recoveries	\$ 719,030	\$	\$ 200,574
Loan principal charged against allocated undistributed patronage			219,674
Increase in cash	118,731		40,637
Increase in temporary investments			950,000
Increase in accrued interest receivable		1,077,244	
Increase in investment in Spokane Bank for Cooperatives	136,081		138,125
Increase in bank premises, furniture and equipment	2,539		14,874
Patronage refunds paid		214,309	
Decrease in accounts payable and accrued expenses	93,041		116,038
Reirement of Class B preferred stock assessments	251,919		
Increase in acquired assets held for resale	2,582		
Decrease in accrued interest payable	98,416		183,146
Decrease in stock subscription payable		60,163	
Decrease in notes payable	2,644,113	3,708,769	23,265,755
	<u>\$4,066,452</u>	<u>\$5,060,485</u>	<u>\$25,128,823</u>

See notes to financial statements.

Notes to Financial Statements

Year Ended May 31, 1988, Five Months Ended May 31, 1987, and Year Ended December 31, 1986

Note A — Summary of Significant Accounting Policies:

Operations: The Alaska Commercial Fishing and Agriculture Bank (CFAB) was incorporated on May 4, 1979 to promote growth of Alaska agriculture and fishing by providing debt financing to resident-owned businesses engaged in harvesting, processing or marketing, and to promote its own growth as a strong user-oriented institution through cooperative ownership and self-governance.

Interest on loans: The accrual of income is suspended on loans for which the payment of interest is contractually past due more than 90 days.

Investment in Spokane Bank for Cooperatives: The investment in Spokane Bank for Cooperatives (SBC) is stated at cost plus noncash patronage notifications. No ready market exists for this investment. Patronage dividends from SBC reduce interest expense to SBC in the year declared.

Allowance for loan losses: The allowance for loan losses is based upon specific identification of uncollectible loans and a general reserve for those loans not specifically identified.

Acquired assets held for sale: Acquired assets held for sale include those assets acquired through foreclosure. These assets are carried at the lower of fair value or the recorded investment in the related loan. Holding costs are expensed when incurred unless such costs increase the fair value of the asset.

Bank premises, furniture and equipment: Bank premises, furniture and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are charged to operations by use of the straight-line method over estimated useful lives of three to ten years. Expenditures for maintenance and repairs are charged to operating expense as incurred. Expenditures for renewals or improvements which extend the life of an asset are capitalized at cost and depreciated as stated above. Upon sale, retirement or other dispositions of property, the cost and accumulated depreciation are removed from the respective accounts and the resulting gain or loss recorded.

Income taxes: CFAB qualifies as a cooperative under Section 1361 of the Internal Revenue Code. Deferred income taxes may arise as a result of differences in the time of reporting for financial and Federal income tax purposes. The most significant difference relates to the allowance for loan losses. Deferred taxes have been offset by net operating loss carryforwards. At May 31, 1988, approximately \$5,500,000 of loss carryforward remains.

Change in fiscal year-end: During 1987, the Board of Directors voted to change from a fiscal year-end of December 31 to May 31 to better reflect the Bank's fiscal operating cycle. Accordingly, financial statements as of May 31, 1987 and for the five-month period then ended are presented.

Reclassifications: Certain reclassifications have been made to 1986 information to conform to 1987 and 1988 presentations.

Note B — Loans:

CFAB's loan portfolio by major category is as follows:

	May 31,		December 31,
	1988	1987	1986
Seafood harvesters	\$27,116,280	\$31,501,629	\$29,994,692
Fish processors	4,037,972	6,900,866	8,702,504
Agriculture and timber	7,638,225	7,605,989	7,596,991
Other receivables	4,899,127	1,818,638	1,826,138
	<u>43,691,604</u>	<u>47,827,122</u>	<u>48,120,325</u>
Less loans receivable on Class B preferred stock	(2,075,300)	(3,448,700)	(3,698,500)
	<u>41,616,304</u>	<u>44,378,422</u>	<u>44,421,825</u>
Less allowance for loan losses	(2,197,140)	(3,367,869)	(3,291,026)
	<u>\$39,419,164</u>	<u>\$41,010,553</u>	<u>\$41,130,799</u>

Notes to Financial Statements *continued*

In accordance with its statutory mandate and authority, CFAB's financing activity is limited to the Alaskan commercial fishing and agriculture industries. This concentration of loans in resource-based industries results in an unusual level of risk exposure.

The loan portfolio includes loans which have been classified as nonaccrual. Nonaccrual loans by major category are as follows:

	May 31,		December 31,
	1988	1987	1986
Seafood harvesters	\$ 3,982,047	\$ 5,776,531	\$ 5,311,987
Fish processors	1,122,643	3,726,235	4,441,655
Agriculture and timber	5,830,615	7,579,151	7,569,743
Less loans receivable on Class B preferred stock	(888,700)	(1,555,400)	(1,539,600)
	<u>\$10,046,605</u>	<u>\$15,526,520</u>	<u>\$15,743,785</u>

Activity in the allowance for loan losses is as follows:

	May 31,		December 31,
	1988	1987	1986
Balance at beginning of year	\$3,367,869	\$3,291,026	\$3,441,130
Charged to expense (income)	(451,699)	49,300	50,470
Recoveries on loans previously charged off	125,318	117,491	688,266
	<u>3,041,488</u>	<u>3,457,817</u>	<u>4,179,866</u>
Loans charged off	(844,348)	(89,948)	(888,840)
Balance at end of year	<u>\$2,197,140</u>	<u>\$3,367,869</u>	<u>\$3,291,026</u>

The allowance for loan losses is re-evaluated by management and increases or decreases are recorded through the current period provision for loan losses.

Loans to directors: To qualify for election to the CFAB Board of Directors, an individual must be a borrowing member. Loans to members who serve on the Board of Directors must be approved by the SBC. Loans to these members totalled \$113,897, \$129,094 and \$141,247 at May 31, 1988 and 1987, and December 31, 1986, respectively.

Note C — Investment in Spokane Bank for Cooperatives:

The Spokane Bank for Cooperatives is a member of the Farm Credit System. The Farm Credit System has incurred losses during 1986 and 1987. Continued losses may result in impairment of the investment in the Spokane Bank for Cooperatives in future years as the result of system-wide loss sharing arrangements in effect among system members.

Note D — Bank Premises, Furniture and Equipment:

The following represents a classification of bank premises, furniture and equipment by major category:

	May 31,		December 31,
	1988	1987	1986
Furniture, fixtures and equipment	\$ 833,146	\$ 868,405	\$ 893,365
Leasehold improvements	147,202	147,202	147,202
	<u>980,348</u>	<u>1,015,607</u>	<u>1,040,567</u>
Less accumulated depreciation and amortization	(810,428)	(718,341)	(688,693)
	<u>\$ 169,920</u>	<u>\$ 297,266</u>	<u>\$ 351,874</u>

Note E — Notes Payable:

Notes payable consists of:

	May 31,		December 31,
	1988	1987	1986
SBC long-term notes with interest rates ranging from 11.232% to 11.28% maturing at various dates to January, 1993	\$10,000,000	\$20,000,000	\$25,000,000
SBC short-term notes and seasonal loan with interest rates ranging from 7.26% to 9.00%, maturing at various dates in 1989	8,649,657	1,293,770	—
Other	—	—	2,539
	<u>\$18,649,657</u>	<u>\$21,293,770</u>	<u>\$25,002,539</u>

Notes to Financial Statements *continued*

The loans are secured by substantially all CFAB assets.

Principal payments required on notes payable are as follows:

<u>Year ending May 31,</u>	<u>Amount</u>
1989	\$8,649,657
1990	-
1991	-
1992	5,000,000
1993	5,000,000

Note F — Employee Benefit Plans:

CFAB has an employee benefit plan as defined under Section 401(k) of the Internal Revenue Service Code covering substantially all employees.

An employee is allowed to contribute up to 15% of his/her earnings to the maximum limit allowed by the Code. Contributions by CFAB to the plan are at the discretion of the Board of Directors. Contributions by CFAB for the year ended May 31, 1988, five months ended May 31, 1987, and year ended December 31, 1986 were \$65,539, \$26,169 and \$57,422, respectively.

The Board of Directors voted to terminate CFAB's floor retirement pension plan during 1986. As of December 31, 1986, the net assets available for benefits under the floor retirement plan was \$34,000. This amount will be refunded to CFAB upon the approval of termination by regulatory agencies. In accordance with generally accepted accounting principles, no gain will be recorded until the regulatory approval of the termination is obtained.

Note G — Capital:

Share capital: Shares owned by the State of Alaska must be repurchased by CFAB on or before July 20, 2000.

Preferential shareholders' rights on dissolution are attached in the order of Class C, Class B and Class A.

The following rights apply to the three categories of stock:

Class C - No voting or dividend rights. May only be issued to the State of Alaska.

Class B - No voting rights. Class B stock may only be held by members of CFAB. Prior to December 31, 1985, all loans required a purchase of Class B stock in an amount equal to 10% of the loan balance; however, this purchase was not funded but was evidenced by notes. On loans made subsequent to December 31, 1985, each borrower is required to make a cash purchase of Class B stock in an amount equal to 5% of the total loan. This investment will remain in place until retired by the Board of Directors.

Class A - No dividend rights. Each member of CFAB must own one share of Class A stock. Each share of stock carries one vote. To vote, a member must be engaged in commercial fishing or agriculture and must be a current borrower or have borrowed from CFAB during the preceding two years or have minimum retained patronage earnings with CFAB of \$2,500.

C Stock retirement pool: Loans made by CFAB during the period December 1982 to December 1985 were subject to a supplemental investment requirement called the C Stock Retirement Program. Members borrowing during that period were required to make annual year-end investments related to their respective usage of CFAB funds during that year. The program was discontinued, with respect to new participants, upon adoption of CFAB's current Class B Preferred Stock investment policy at January 1, 1986. In March 1988, the accumulated investments in the C Stock Retirement Pool, totaling \$251,919, were retired. Proceeds were returned in cash to members whose loans had been paid in full or were applied to the credit of members with outstanding loan accounts.

Notes to Financial Statements *continued***Note H — Income Taxes:**

Income tax expense consists of the following:

	Year ended May 31, 1988	Five months ended May 31, 1987	Year ended December 31, 1986
Current:			
Federal	\$ 136,000	\$ 423,000	\$ 179,800
State	28,000	91,000	46,500
	<u>164,000</u>	<u>514,000</u>	<u>226,300</u>
Deferred:			
Federal	77,000	(380,000)	
State	33,000	(81,000)	
	<u>110,000</u>	<u>(461,000)</u>	
	<u>\$274,000</u>	<u>\$ 53,000</u>	<u>\$226,300</u>

At May 31, 1988, CFAB had available for financial reporting purposes approximately \$5,500,000 of net operating loss carryforward which expire May 31, 2000, if not used to reduce future taxable income.

Note I — Restructure of Loans:

During the year ended May 31, 1988, the terms of nonaccrual loans totalling approximately \$1,500,000 were modified through negotiation, and the loans were restructured as a note receivable. The interest rate on that note receivable was reduced from CFAB's normal lending rate for a period of three years. Interest income of approximately \$130,000 was received and recorded on this note for the year ended May 31, 1988; if the interest rates on the original loans had remained in effect, approximately \$200,000 of interest would have been due during that period.

Note J — Commitments and Contingent Liabilities:

Contingencies: CFAB is a litigant in several legal actions arising from normal business activities including actions related to delinquent loans and foreclosures. CFAB reserves for potential losses on delinquent loans as described in Note A. As to litigation outside of delinquencies and foreclosures, management believes that those actions are without merit or that the ultimate liability, if any, resulting from them will not materially affect CFAB's financial position or its results of operations.

Commitments: CFAB has entered into certain noncancelable long-term operating lease agreements for buildings. Rental expense under these leases totalled \$165,348, \$78,558 and \$192,450 for the year, five months and years ended May 31, 1988 and 1987, and December 31, 1986, respectively. Minimum annual lease payments are as follows:

Year ending May 31,	Amount
1989	\$174,000
1990	43,000

Note K — Subsequent Event:

On July 19, 1988, the Federal Bankruptcy Court in Anchorage confirmed the Plan of Reorganization in connection with the Chapter 11 proceeding of one of CFAB's larger borrowers. CFAB subsequently received approximately \$5.7 million of cash and released all of its claims against the debtor. The entire proceeds were applied to reduce CFAB's borrowings from the Spokane Bank for Cooperatives and, in addition, CFAB's nonaccrual loans outstanding were reduced by an amount in excess of \$3.0 million.



Board of Directors
Alaska Commercial Fishing
and Agriculture Bank
Anchorage Alaska

We have examined the balance sheets of Alaska Commercial Fishing and Agriculture Bank as of May 31, 1988, May 31, 1987 and December 31, 1986, and the related statements of net proceeds, changes in capital and patronage, and changes in financial position for the respective year, five months, and year then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Alaska Commercial Fishing and Agriculture Bank as of May 31, 1988, May 31, 1987 and December 31, 1986, and the results of its operations and the changes in its financial position for the respective year, five months, and year then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Touche Ross & Co.

Certified Public Accountants
July 1, 1988

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Chairman

Robert Waldrop
Vice Chairman

Gilbert Gunderson
Secretary-Treasurer

Hyoung "Henry" Kim
Director

Alan D. Otness
Director

Dean Paddock
Director

Harvey Samuelsen
Director

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Iver Amundsen
Assistant Vice President

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Christina E. Boyce-Lee
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Data Processing Supervisor

Lora C. Smith
Senior Bookkeeper

Deborah A. Tosch-Price
Documentation Paralegal

Godelieve C. Van Lint
Administrative Support Clerk

DeLories M. vonGemmingen
Executive Secretary

REMARKS

HEARINGS ON HB-118, THE ELF LEGISLATION, WILL CONTINUE TOMORROW FROM 3:30-5:00 P.M. THIS WILL BE THE LAST OF THE PUBLIC AND INTEREST GROUP TESTIMONY FOR THIS WEEK.

THE NEXT HEARING ON THIS ISSUE WILL BE SOMETIME NEXT WEEK. OUR STAFF IS TRYING TO ARRANGE MEDIA COVERAGE FOR A QUESTION AND ANSWER SESSION WITH BOTH THE ADMINISTRATION AND AN OIL INDUSTRY REPRESENTATIVE BEFORE THE RESOURCES COMMITTEE.

THE COMMITTEE HAS SUBMITTED 25 KEY QUESTIONS TO BOTH THE ADMINISTRATION AND THE AFFECTED OIL COMPANIES. WE EXPECT ANSWERS TO THESE QUESTIONS ON FRIDAY FEBRUARY 17. IN ADDITION, I WOULD LIKE TO OFFER TO THE COMMITTEE MEMBERS, THE AFFECTED OIL COMPANIES AND THE ADMINISTRATION, THE OPPORTUNITY TO ASK QUESTIONS OF EITHER THE ADMINISTRATION OR THE OIL COMPANIES. WE ARE ATTEMPTING TO BE FAIR AND OFFER EACH PARTY AMPLE OPPORTUNITY TO BOTH ASK AND ANSWER QUESTIONS. THIS OFFER IS AN EXTENSION OF THE PROCESS OF TRYING TO GET TO THE FACTS ABOUT CHANGING THE ELF.