

HB

159

HFIN

FILE

FISCAL NOTE

STATE OF ALASKA
2003 LEGISLATIVE SESSION

Fiscal Note Number: _____
 Bill Version: HB 159
 () Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: DCED
 Title Financial Institutions/Examinations/CFAB BRU Banking, Securities & Corporations (115)
 Component Banking, Securities & Corporations
 Sponsor Rules by Request of the Governor
 Requester House Labor & Commerce Component No. 1233

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Personal Services	(75.0)					
Travel	(3.0)					
Contractual	(48.0)					
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	(126.0)	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES (51137)	(25.0)					
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	(126.0)	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2003) cost: 126.0

Mark this box (X) if funding for this bill is included in the Governor's FY 2004 budget proposal:

POSITIONS

Full-time	-1					
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

This legislation changes the frequency of examinations of people licensed under the Alaska Small Loans Act (AS 06.20), and repeals the requirement for a state examination and evaluation of the Alaska Commercial Fishing and Agriculture Bank (CFAB).

CHANGE IN REVENUE: We anticipate a loss of \$25.0 in revenue as a result of examination fees no longer collected.

Prepared by: Mark Davis, Director Phone 907-269-8452
 Division Banking, Securities & Corporations Date/Time 3/6/03 3:41 PM
 Approved by: Edgar Blatchford, Commissioner Date 3/6/2003
 Agency Department of Community & Economic Development

Amended 3-4

AMENDMENT 1

TO BE OFFERED IN THE HOUSE FINANCE COMMITTEE

BY REPRESENTATIVE CROFT

TO: HB 159

Page 1, Line 13, DELETE:

“* Sec.2. AS 44.81.270(d) is repealed.”

Renumber accordingly

This amendment keeps the requirement for CFAB to submit to annual bank examinations. The argument for not holding CFAB to this standard is the perception that the requirement is overly redundant, that CFAB is subject to independent audit or legislative audit, should one be requested.

CFAB puts forth that the requirement is not overly redundant; that the independent audit only looks at their financial situation, and the bank examiners make sure CFAB is adhering to statute. CFAB argues the bank examinations help them with their accountability to their board (two members of which are appointed by the Governor) and their members and CFAB pays for the examination.

Although the Legislature could request Legislative Budget and Audit to conduct a bank examination, it does not happen on a regular basis. The last one occurred in 1995.

House Finance Committee Vote Sheet

DATE: 3/27/03

SUBJECT: HB 159 - Amendment #1

MEMBER YES NO

JOULE	✓	
MEYER		✓
MOSES		
STOLTZE		✓
WHITAKER		✓
CHENAULT		
CROFT	✓	
FOSTER		✓
HAWKER		✓
HARRIS	✓	
WILLIAMS		✓
TOTAL:		

PASSED: 3

FAILED: 6

FRANK H. MURKOWSKI
GOVERNOR
GOVERNOR@GOV.STATE.AK.US



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OFFICE OF THE GOVERNOR
JUNEAU

HB159
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March 5, 2003

The Honorable Pete Kott
Speaker of the House
Alaska State Legislature
State Capitol, Room 208
Juneau, AK 99801-1182

Dear Speaker Kott:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill that would give the Department more flexibility with regard to the frequency of examinations of financial institutions and the Alaska Commercial Fishing and Agriculture Bank.

Changing the date of frequency of examinations of Small Loan Companies from 12 months to 18 months will bring the schedule for the examinations in line with the rest of the banking code and eliminate the need for additional bank examiners. The bill also eliminates the Division of Banking, Securities, and Corporations' examination of the Commercial Fishing and Agriculture Bank (CFAB). This examination is unnecessary, because CFAB is required by statute to be audited annually by independent auditors and is subject to legislative audit.

I urge your prompt and favorable action on this measure.

Sincerely,

A handwritten signature in black ink that reads "Frank H. Murkowski".

Frank H. Murkowski
Governor

HB159
Financial Institutions/Commercial Fisheries Agriculture Board (CFAB)

Testimony by Mark Davis, Director
Division of Banking, Securities & Corporations
Alaska Department of Community & Economic Development
to the
House Finance Committee
26 March 2003

- On behalf of Governor Murkowski and Commissioner Blatchford, I want to thank the committee for promptly scheduling a hearing of HB159 Financial Examinations/CFAB.
- The proposed bill makes two changes to the banking code.
- The first change extends the frequency of the Division's examinations of Small Loan Companies from 12 to 18 months.
- This change will bring the schedule for the examinations in line with the rest of the banking code and will eliminate the need for an additional bank examiner.
- It will not affect the integrity of the examinations, and the Division will follow its policy that it can examine a Small Loan Company more frequently if that is deemed advisable.
- The second change discontinues the Division's annual examination of the Alaska Commercial Fishing and Agricultural Bank (CFAB).
- CFAB presently receives no State funds and does not accept deposits from the public, as do banks, and credit unions.
- CFAB operates essentially as a cooperative for the benefit of its members, and is required by statute to prepare annually an audit by an independent outside auditor. This report is provided to the legislature.
- HB 159 does not change the fact that by statute CFAB will continue to be subject to a legislative audit.
- In view of the fact that CFAB has paid back all of its state funding, is not a bank lending to the public and is subject to both an independent audit and a legislative audit, an examination by the Division of Banking, Securities and Corporations is unnecessary.
- Banking's operational costs for FY03 are estimated at \$635,069 and revenue generated is estimated to be \$276,000. This will result in costs in excess of revenues to the amount of \$359,000.

History on CFAB Examination

- The Division was invited to examine CFAB on April 29, 1985 to report about the viability of CFAB funding at the request of CFAB's source of funding, the Spokane Bank for Cooperatives.
- Thereafter, Alaska Statutes pertaining to CFAB were amended in 1987 to require an annual examination by division examiners.

THE
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March 19, 2003

Lela E. Klingert
President

The Honorable Frank Murkowski
Governor, State of Alaska
Post Office Box 110001
Juneau, Alaska 99811-0011

Dear Governor Murkowski,

We have reviewed House Bill 159 and Senate Bill 113, each introduced by the respective Rules Committee at your request.

We note that Section 2 of each bill provides for the repeal of AS 44.81.270(d), which authorizes and directs annual examination of the Alaska Commercial Fishing and Agriculture Bank. This is problematic to us, and we are wondering if a modified approach might be crafted; one which would support the bills' purposes and intents while continuing to meet the needs of CFAB and other interested parties.

To that end, we would offer the following points of perspective. They may seem somewhat lengthy, but our purposes are (1) to provide sufficient information to permit full consideration of an alternate approach; and (2) to emphasize that the examination function has been extremely useful to CFAB and its resident member-owners.

AS 44.81.270(d) was the result of 1987 legislation. CFAB had begun operations in early 1980. By the end of 1984, and into 1985, it had become clear that cumulative losses and other effects of inappropriate credit judgments and practices threatened CFAB's failure. During the late '80's, and into the early 90's, CFAB was "in recovery." (At that time, the State of Alaska owned \$32.0 million of CFAB's preferred stock.) Among the ancillary effects of the publicity and perceptions concerning CFAB's circumstances were the generally unfounded yet understandable allegations of a wide range of improprieties within CFAB and the expressed frustrations that "nobody knows what the real story is." These emanated from both the legislative and executive branches, as well as from member-owners, competing lenders, and various media, etc.

Thus, one of the practical, and successful, purposes of the 1987 legislation was establishment of a process by which a professional, credible, and independent

Alaska Commercial Fishing and Agriculture Bank

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The Honorable Frank Murkowski

March 19, 2003

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periodic evaluation of CFAB's loan/asset quality, management, practices, and statutory compliance may be submitted to authorized and interested parties. Over the years many examination reports - or elements thereof - have been noted by, or discussed with, a range of administrators, legislators, lenders, and others. Those examination reports have proven to be extremely useful.

Quite often the value of a safeguard, or a safety element such as a fire extinguisher, may become "invisible" because it has never been called upon. That may be the case here. CFAB has the statutory authority, unique among private lenders, to acquite and administer a consensual lien on a Commercial Fisheries Limited Entry Permit. CFAB has always exercised this authority within a context of fiduciary responsibility, and has attempted to adhere to the spirit, as well as the letter, of the comprehensive statutory limitations. There has never been a sustained, or even substantial, suggestion of CFAB failure in this regard.

Notwithstanding the foregoing, it should not be overlooked that the annual examination has been a most effective means of oversight of this area, and AS 44.81 in general, for the benefit and protection of the thousands of Alaska residents potentially affected. Similarly, these examinations have provided an element of protection for those Alaska residents who are the collective owners of over \$19.0 million of CFAB equity. This is not unlike the efforts undertaken by the State to protect the depositors and/or owners of other institutions.

We note the suggestion that the annual examination is redundant to the statutorily-mandated financial audit. However, those processes encompass significantly different professional disciplines and emphases, and are complementary to each other. Simply put, an examination is focused on the quality/value of assets, whereas an audit is concerned primarily with appropriate accounting for the assets and liability of the subject. If CFAB makes a \$100,000 loan to Bill Jones, who confirms to the auditors that he indeed owes CFAB \$100,000, the auditors are satisfied that \$100,000 has been accounted for. However, the examiners' process is concerned with whether or not it made professional sense for CFAB to make the loan, and with whether or not Bill Jones has the intent and capacity to repay.

We do not consider the annual audit and annual examination, each of which we value, to be at all redundant. For over 15 years CFAB's management has viewed the annual examination to be a necessary and valuable check on its own analyses and judgments. Its officers, while not lacking in confidence, have welcomed the scrutiny of objective and professional eyes. In short, the examination has proved a valuable tool in assuring the effective management of CFAB, to the benefit of Alaska residents. Similarly, CFAB's Board of Directors has utilized the examination and the resultant report and examiners' presentation as an element of its ongoing evaluation of

The Honorable Frank Murkowski
March 19, 2003
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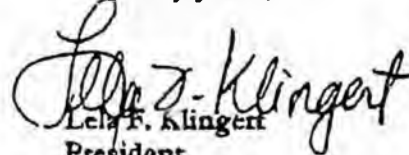
management, in keeping with the Board's fiduciary duty to member-owners. Finally, CFAB's lender - without which CFAB could not function - has clearly viewed the annual examination as an important element of its evaluation of CFAB's creditworthiness.

Your letters transmitting HB 159 and SB 113 suggest that certain fiscal objectives will be served through passage of this legislation. Obviously, we have no insight into the agency finances involved, and would not presume to offer comments in that regard. Neither would we suggest that a reduction in agency net expense is inappropriate. However, we are somewhat confused as to the relevance of AS 44.81.270(d) to that issue. Through 1992 CFAB, like each other state-chartered financial institution, was charged a maximum of \$7,500 (or actual costs, if less) for each examination. Beginning in 1993, premised on a change in the relevant statute, CFAB has been charged - and has paid - what has been expressed as the "actual costs" of each examination. CFAB has paid a total of \$117,684 for the ensuing examinations - an average of \$11,768, with a high of \$16,338 and a low of \$6,308. If those charges have indeed reflected the actual costs of examination, it is difficult to understand how a cessation of those examinations will have a significant fiscal impact.

As a closing observation, we would like to assure that a modification of the required examination interval to 18 months, as your bills provide for other non-banking entities, would be a workable approach from CFAB's standpoint.

Governor Murkowski, we are somewhat troubled at the appearance of "opposing" your legislation; we would have preferred an earlier discussion. CFAB is a private cooperative institution with unique purposes, authorities, foundation, and history, and is charged with serving a public interest. We believe that routine professional examinations are an important element for the protection of the State, the public, the cooperative, and its member-owners. And, of course, CFAB is willing to continue to pay its own way on the same bases as in the past.

Very truly yours,


Leif F. Klingert
President