

**HB**

**159**

SFIN

FILE

# SENATE FINANCE COMMITTEE REPORT

DATE: 4/14/03

REPORTED OUT  
APR 22 2003  
SENATE FINANCE  
COMMITTEE  
HOUSE BILL NO. 159

FURTHER:

DATE TURNED  
IN TO OFFICE: 4/22/03

Finance Committee considered

## HB 159 FINANCIAL INSTITUTION EXAMINATIONS/CFAB

"An Act relating to the frequency of examinations of certain persons licensed to engage in the business of making loans of money, credit, goods, or things in action; repealing the requirement for a state examination and evaluation of the Alaska Commercial Fishing and Agriculture Bank; and providing for an effective date."

and recommends:

- be replaced with \_\_\_\_\_ CS \_\_\_\_\_ (\_\_\_\_\_)
- adopt previous \_\_\_\_\_ CS \_\_\_\_\_ (\_\_\_\_\_)
- attached amendment(s)
- adopt Letter of Intent by \_\_\_\_\_ Committee
- further referral to \_\_\_\_\_ Committee

**Senate Bill:**

same title

new title

**House Bill:**

same title

technical title

new: SCR # \_\_\_\_\_

**NEW FISCAL NOTE(S):**

| Department | Date | Fiscal | Zero | FN# |
|------------|------|--------|------|-----|
|            |      |        |      |     |
|            |      |        |      |     |
|            |      |        |      |     |
|            |      |        |      |     |

**PREVIOUS FISCAL NOTE(S):**

| Department | Date    | Fiscal | Zero | FN# |
|------------|---------|--------|------|-----|
| DCED       | 3/27/03 | ✓      |      | 2   |
|            |         |        |      |     |
|            |         |        |      |     |
|            |         |        |      |     |

APPROPRIATION - no fiscal note

| SIGNATURES AND RECOMMENDATIONS: | DO PASS | DO NOT PASS | No REC | AMEND |
|---------------------------------|---------|-------------|--------|-------|
| <i>John H. Taylor</i>           |         |             | ✓      |       |
| <i>[Signature]</i>              |         |             |        |       |
| <i>[Signature]</i>              |         |             | ✓      |       |
| <i>[Signature]</i>              | ✓       |             |        |       |
| <i>[Signature]</i>              | ✓       |             |        |       |
| COCHAIR: <i>Linda Green</i>     |         |             | ✓      |       |
| COCHAIR: <i>[Signature]</i>     | ✓       |             |        |       |

HOUSE BILL NO. 159

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY THE HOUSE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

Introduced: 3/5/03

Referred: Labor and Commerce, Finance

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to the frequency of examinations of certain persons licensed to engage  
2 in the business of making loans of money, credit, goods, or things in action; repealing the  
3 requirement for a state examination and evaluation of the Alaska Commercial Fishing  
4 and Agriculture Bank; and providing for an effective date."

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

6 \* Section 1. AS 06.20.170 is amended to read:

7           Sec. 06.20.170. Periodic [ANNUAL] examination. The department shall  
8 examine the affairs, business, office, and records of each licensee at least once every  
9 18 months [EACH YEAR]. Examination fees are to be charged to and paid by the  
10 licensee in accordance with AS 06.01.010. The department may maintain an action  
11 for the recovery of the costs in any court of competent jurisdiction, with recourse to  
12 the bonds referred to in AS 06.20.050 and 06.20.080.

13 \* Sec. 2. AS 44.81.270(d) is repealed.

14 \* Sec. 3. This Act takes effect July 1, 2003.

# FISCAL NOTE

REPORTED OUT

APR 22 2003

STATE OF ALASKA  
2003 LEGISLATIVE SESSION

Fiscal Note Number:  
Bill Version:  
(H) Publish Date:

2 SENATE FINANCE  
HB 159  
3/28/03

Revision Date/Time (Note if correction): 03-27-03 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          |                |            |            |            |            |            |
| <b>TOTAL OPERATING</b> | <b>(126.0)</b> | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> |

|                                     |               |  |  |  |  |  |
|-------------------------------------|---------------|--|--|--|--|--|
| <b>CAPITAL EXPENDITURES</b>         |               |  |  |  |  |  |
| <b>CHANGE IN REVENUES ( 51137 )</b> | <b>(25.0)</b> |  |  |  |  |  |

**FUND SOURCE** (Thousands of Dollars)

|                                 |                |            |            |            |            |            |
|---------------------------------|----------------|------------|------------|------------|------------|------------|
| 1002 Federal Receipts           |                |            |            |            |            |            |
| 1003 GF Match                   |                |            |            |            |            |            |
| 1004 GF                         |                |            |            |            |            |            |
| 1005 GF/Program Receipts        |                |            |            |            |            |            |
| 1037 GF/Mental Health           |                |            |            |            |            |            |
| 1156 Receipt Supported Services | (126.0)        | 0.0        | 0.0        | 0.0        | 0.0        | 0.0        |
| <b>TOTAL</b>                    | <b>(126.0)</b> | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> |

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 3/27/03 9:00 AM  
Approved by: Edgar Blatchford, Commissioner Date 3/27/2003  
Agency Department of Community & Economic Development

Frank H. Murkowski, Governor

# Alaska Department of Community and Economic Development

## Office of the Commissioner

P.O. Box 110800, Juneau, AK 99811-0800

Telephone: (907) 465-2500 • Fax: (907) 465-5442 • Text Telephone: (907) 465-5437

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April 3, 2003

The Honorable Gary Wilken, Co-Chair  
The Honorable Lyda Green, Co-Chair  
Senate Finance Committee  
Alaska State Legislature  
State Capitol  
Juneau, AK 99801-1182

SB 113 is the companion  
bill to HB 159.

Re: SB113 "An Act relating to the frequency of examinations of certain persons licensed to engage in the business of making loans of money, credit, goods, or things in action; repealing the requirement for a state examination and evaluation of the Alaska Commercial Fishing and Agriculture Bank; and providing for an effective date."

Dear Senator Wilken and Senator Green:

Senate Bill 113 was introduced by the Governor through the Senate Rules Committee. This legislation makes two changes: it extends the frequency of the Division's examinations of small loan companies from 12 to 18 months, and it discontinues the Division's annual audit of the Alaska Commercial Fishing and Agricultural Bank (CFAB).

These changes will bring the schedule for examining small loan companies in line with the rest of the banking code, eliminate the statutory requirement for the CFAB examination, and will, in turn, eliminate the need for an additional bank examiner, saving a total of \$126.0.

CFAB would like the Division to continue its examination. In light 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, the Department believes the examination by the Division of Banking, Securities and Corporations is unnecessary.

The companion House Bill 159 has been referred to the Rules Committee and we hope the bill will be heard on the House floor and transmitted to the Senate next week.

We respectfully request that you schedule SB113 for a hearing in your committee, and we urge favorable action on this bill. We will be happy to meet with you and other members of the committee to provide any further information you may require. Thank you for considering our request.

Sincerely,



Edgar Blatchford  
Commissioner

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Lela F. Klingert  
*President*

March 19, 2003

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

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*Alaska Commercial Fishing and Agriculture Bank*

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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 acquire 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 complimentary 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  
Page 3

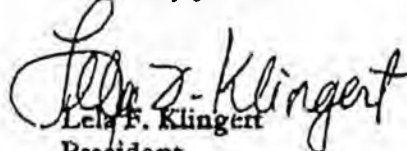
management, in keeping with the Board's fiduciary duty to member-owners. Finally, CFAB's lender - without which CFAB could not function - has clearly viewed the annual examination as an important element of its evaluation of CFAB's creditworthiness.

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,

  
Lela F. Klingert  
President

## **HB159**

### **Financial Institutions/Commercial Fisheries Agriculture Bank (CFAB)**

**Testimony by Mark Davis, Director  
Division of Banking, Securities & Corporations  
Alaska Department of Community & Economic Development  
to the  
Senate Finance Committee  
17 April 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 changes the date of 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.
- HB159 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.

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



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OFFICE OF THE GOVERNOR  
JUNEAU

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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 cursive script that reads "Frank H. Murkowski".

Frank H. Murkowski  
Governor

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



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Sincerely,

A handwritten signature in cursive script that reads "Frank H. Murkowski".

Frank H. Murkowski  
Governor

