

ALASKA LEGISLATURE COMMITTEE FILES 1987-1988 8672

5030 HRES SB 472 - SB 475

8672



5. Re p. 2 "repairs and maintenance": Buyer should promise to maintain in as good or better condition as condition on date of sale. There is concern about buyer cutting expenses by reducing repair and maintenance budget.
- b. Re p 3 "improvements": This provision is contrary to standard lease terms; normally improvements revert to lessor.

May 2, 1988

SB 472 Parent Language

It is the intent of the legislature that the ARLF sell the creamery operation located at 814 Northern Lights and lease-purchase the land and buildings. It is the intent of the legislature that this be completed as soon as practicable.

1. Sale terms of the creamery operating assets. The sales price of the operating assets are to be determined as follows:

Cash - retained by the ARLF

Trade receivables - at book value, less any uncollectible receivables. All trade receivables not collected within 60 days of closing or in excess of \$800,000 to revert back to the ARLF.

Notes receivable - retained by the ARLF.

Other receivables - retained by the ARLF.

Inventories - at lower of cost or market. Based upon physical count at the date of sale.

Prepaid expenses - based upon equitable proration.

Machinery, fixtures and equipment - at depreciated book value less any debt assumed by buyer.

Current liabilities - retained and paid by the ARLF.

Long-term debt - assumed by the buyer and to be paid by buyer.

Intangibles - all intangibles such as goodwill and logos shall be transferred to buyer at date of sale for \$1.00

Other operating assets - all other operating assets not specifically mentioned above shall be transferred to buyer at date of sale for \$1,000.00

The ARLF shall receive a security interest in all operating assets which are sold in an amount equal to the value of that operating asset as determined above. The security interest shall not be released on any operating asset until the amount due on that asset has been paid in full.

During each and every month, until the termination of the lease-purchase agreement, the buyer shall pay to the ARLF an amount equal to 50 cents per hundred weight of milk processed at the creamery, or \$13,000.00 per month, whichever is greater. These payments shall apply first toward the amounts owed the ARLF for the operating assets acquired by the buyer. All of these payments by the buyer shall apply toward the creamery assets in the following order:

- First: Prepaids
- Second: Inventories
- Third: Receivables
- Fourth: Machinery, fixtures and equipment
- Fifth: Intangibles
- Sixth: Other operating assets
- Seventh: Land and buildings

At the end of the fifth year any amount unpaid on the operating assets shall be due and payable in full.

2. Terms of land and building lease-purchase. In addition to the conditions enumerated in the bill the lease-purchase agreement shall include the following provisions:

Collective bargaining agreements - prior to the purchase of the operating assets the lessee shall adopt the collective bargaining agreements in effect between Marquette Maid employees and the ARLF.

Professional services contract - the lessee agrees to the terms of the ARLF contract with Joe Van Treeck dated August 26, 1987.

Insurance - lessee to provide insurance on the building.

Taxes - lessee to pay any taxes due on creamery assets.

Records - the lessee shall submit quarterly financial statements to the lessor.

Repairs and maintenance - lessee to be responsible for all repairs and maintenance to creamery assets.

Alterations - lessee shall not make any alterations or additions to the premises without the prior written consent of the lessor.

Improvements - the lessee shall receive credit at closing for the value of any improvements made by lessee to the land and building during the term of the lease.

Option exercise - lessee shall give lessor sixty days notice of desire to exercise the option to purchase. The balance of the purchase price is due in cash at closing.

Board veto authority - so long as the commissioner retains veto authority over the composition and membership of the board then the lessor shall hold harmless and indemnify any outside board members from any claim, action, or suit arising out of the directors fulfilling their duties as a director.

from Joe Cange

May 2, 1988

SB 472 Intent Language

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Collective bargaining agreements - prior to the purchase of the operating assets the lessee shall adopt the collective bargaining agreements in effect between Matanuska Maid employees and the ARLF.

Professional services contract - the lessee agrees to the terms of the ARLF contract with Joe Van Treeck dated August 26, 1987.

Insurance - lessee to provide insurance on the building.

Taxes - lessee to pay any taxes due on creamery assets.

Records - the lessee shall submit quarterly financial statements to the lessor.

Repairs and maintenance - lessee to be responsible for all repairs and maintenance to creamery assets.

Alterations - lessee shall not make any alterations or additions to the premises without the prior written consent of the lessor.

Improvements - the lessee shall receive credit at closing for the value of any improvements made by lessee to the land and building during the term of the lease.

Option exercise - lessee shall give lessor sixty days notice of desire to exercise the option to purchase. The balance of the purchase price is due in cash at closing.

Board veto authority - so long as the commissioner retains veto authority over the composition and membership of the board then the lessor shall hold harmless and indemnify any outside board members from any claim, action, or suit arising out of the directors fulfilling their duties as a director.

Hal

To: Mark Weaver, Carol Wilson  
From: Bonnie Robson  
Re: SB 472 Intent Language  
Date: May 4, 1988

## Major Problems

1. Re p. 1, last TP and top 1/3 p. 2: Should default in purchase of operating assets occur after, say, one year, some assets would have been paid for in full and released from security interest. State would get back partially stripped creamery. All assets sold must be security for entire debt. Payments received should be applied to purchase of all assets, not individual assets.
2. Re p. 1 "current liabilities": Should prorate liability where portion for future good or service.
3. Re p. 1 "long-term debt": Should be aware that buyer's assumption will not release State from liability absent creditor consent.
4. Re p. 2 "insurance": Insurance on operating assets and liability insurance also necessary.

5. Re p. 2 "repairs and maintenance": Buyer should promise to maintain in as good or better condition as condition on date of sale. There is concern about buyer cutting expenses by reducing repair and maintenance budget.
6. Re p 3 "improvements": This provision is contrary to standard lease terms; normally improvements revert to lessor.

4/28

SB 472

Faren Lee / Soc Corp

→ Coop can't take out a pit loan -

no operating history

Mat Mark's wife is bad

→ If ARIF is good for only 25% need to be

able to purchase receivables - Paul Fischer

objected to that - Halford went along w/

Fischer - later Lee had not ~~had~~ about the

\$750,000 loan - pricing facilities -

- → Coop rules - allowing new members etc.

- → Soc Recs should have a balance sheet for the creamery

- → need a commit' AG to look at the loan + help interest  
by Faren Lee

7-15-11-11-88  
SB 472  
Copy 5/2  
2. TERMS OF LAND AND BUILDING LEASE-PURCHASE. In addition to the conditions enumerated in the bill the Lease-purchase Agreement shall include the following provisions:

Collective bargaining agreements - prior to the purchase of the business assets the lessee shall adopt the collective bargaining agreements in effect between Matanuska Maid employees and the ARLF

Professional services contract - the lessee agrees to the terms of the ARLF contract with Joe Van Treeck dated August 26, 1987

Insurance - lessee to provide insurance on building

Taxes - lessee to pay any taxes due on creamery assets

Records - the lessee shall submit quarterly financial statements to the lessor

Repairs and Maintenance - lessee to be responsible for all repairs and maintenance to creamery assets

Alterations - lessee shall not make any alterations <sup>or</sup> additions to the premises without the prior written consent of the Lessor

Improvements - the lessee shall receive credit at closing for the cost <sup>value</sup> of any improvements made by lessee to the land and building during the term of the lease

Option exercise - Lessee shall give Lessor sixty days notice of desire to exercise the option to purchase. The balance of the purchase price is due in cash at closing.

Board veto authority - so long as the commissioner retains veto authority over the composition and membership of the board then the Lessor shall hold harmless and indemnify any outside board members from any claim, action, or suit arising out of the directors fulfilling their duties as a director.

THE COMMISSIONER

POSSIBLE EFFECTS OF DAIRY FARM FORECLOSURES  
ON MATANUSKA-MAID CREAMERY OPERATIONS

1. The following approximations of milk production by producers can be used to help understand the effects of one or more dairy farm foreclosures on the creamery.

Approximate Milk Production by Producer

Hamilton	10%
Hawemeister	6%
Davis	6%
University	3%
Dairy West	12%
James	11%
Wright	9%
Tucker	26%
Baskin	5%
Hendershot	3%
Rogers	7%
Thom	2%
	<u>100%</u>

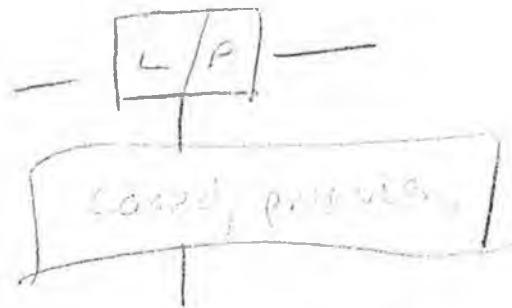
2. Not all dairy producers on this list are nearing foreclosure.
3. Because the foreclosure process is lengthy, with time for appeals and hearings, there would likely be sufficient advance notice to the creamery concerning farm foreclosures for it to accommodate the potential loss of milk.
4. The ARLF might decide to arrange for feeding and milking of cows on foreclosed farms until the property could be resold, so that little disruption in milk production would occur.
5. If necessary, milk from outside the state could be brought in to supplement local production and maintain processing levels. Since outside milk prices have decreased and freight charges to Alaska have declined, purchasing milk from outside would not add to the creamery's financial burden.
6. By further expanding its production of cultured products as well as flavored milks, cheeses, and juices, the creamery could lessen its dependence on white milk sales and sustain or increase business even if less local milk is available.

Liquid ASSETS

Real/Personal Property

\$13,000

\$25,000



1.4

LABNT

PROTECTION  
REQUIREMENTS  
MAY BE SOLID

5-1589T ✓  
Bradley  
5/5/88

Original sponsors: Josephson, Szymanski,  
Halford, et al.

1 IN THE SENATE

BY THE RESOURCES COMMITTEE

2 HOUSE CS FOR CS FOR SENATE BILL NO. 472 (Resources)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FIFTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act authorizing the commissioner of natural  
7 resources to transfer the creamery formerly owned by  
8 Matanuska Maid, Inc."

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

10 \* Section 1. LEGISLATIVE INTENT. It is the intent of the legislature  
11 that the authority granted by sec. 2 of this Act be exercised to

12 (1) promote development of a stable, profitable, and unsub-  
13 sidized Alaskan dairy industry;

14 (2) encourage innovative and efficient management of dairy farms  
15 and processing facilities by the private sector;

16 (3) encourage production and marketing of competitively-priced  
17 Alaskan dairy products in lieu of imported products; and

18 (4) use past investments of public money in the dairy industry  
19 to further the objectives described in (1) - (3) of this section without  
20 depleting the agricultural revolving loan fund.

21 \* Sec. 2. LEASE-PURCHASE AGREEMENT AUTHORIZED. The commissioner of  
22 natural resources may enter into a one-year lease-purchase agreement with a  
23 cooperative composed of Alaska dairy product producers for the ownership,  
24 management, and operation of the former Matanuska Maid Creamery at 814  
25 Northern Lights Boulevard, in Anchorage. The commissioner and the coopera-  
26 tive shall agree on the composition and membership of the board of direc-  
27 tors that manages the Matanuska Maid Creamery unless the commissioner  
28 chooses not to retain veto authority over the composition and membership of  
29 the board. The lease-purchase agreement is renewable annually for 14 years

1 if the lessee has complied with health, product quality, and other terms  
2 and conditions of the lease-purchase agreement and has managed the former  
3 Matanuska Maid Creamery economically, profitably, and efficiently under  
4 the terms of the lease-purchase agreement. The lease-purchase agreement  
5 shall require the lessee to treat each producer of dairy products equally.  
6 The lease-purchase agreement may be negotiated by the commissioner of  
7 natural resources at any time before July 1, 1989, but it is the intent of  
8 the legislature that the lease-purchase agreement be in effect on July 1,  
9 1989. The lease-purchase payment due from the lessee is an amount equal to  
10 \$.50 per hundredweight of milk processed per month at the creamery or  
11 \$13,000 per month, whichever is greater, and the lease-purchase payment  
12 shall be applied to the purchase price. If the cooperative composed of  
13 dairy product producers has continuously operated the former Matanuska Maid  
14 Creamery under a lease-purchase agreement authorized under this section  
15 through June 30, 1999, the commissioner of natural resources shall, at the  
16 request of the lessee at any time after June 30, 1999, but before June 30,  
17 2004, transfer the creamery to the lessee. In valuing the assets of the  
18 former Matanuska Maid Creamery for the purposes of a transfer under this  
19 section, the building shall be valued at its fair market value at the ini-  
20 tiation of the lease-purchase agreement and the land shall be valued at its  
21 fair market value on the date of the request by the lessee for a transfer  
22 under this section.  
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*REDUCED FISCAL NOTE 2/18*

5-1984P

Bradley  
4/29/88

6	G. G. G. G.
13	J. J. J. J.
	G. G. G. G.
	J. J. J. J.

Original sponsor: Judiciary Committee  
by Request

1 IN THE SENATE

BY THE FINANCE COMMITTEE

2 CS FOR SENATE BILL NO. 484 (Finance)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FIFTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act relating to the powers of and loans made by  
7 the Agricultural Revolving Loan Fund Board; and  
8 providing for an effective date."

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

10 \* Section 1. AS 03.10.050 is amended by adding new subsections to read:

11 (d) To facilitate execution of its duties, the Agricultural  
12 Revolving Loan Fund Board may appoint, supervise, and remove a finan-  
13 cial analyst.

14 (e) To encourage the prompt payment of loans, the department may  
15 establish a program of credits for persons who have a loan from the  
16 agricultural revolving loan fund and maintain good financial standing.  
17 The credits may be applied against no more than two percentage points  
18 a year of the interest due on agricultural revolving loan fund loans.

19 (f) A credit may not be granted under (e) of this section to  
20 reduce interest due on a loan if the borrower has an agricultural loan  
21 in default, has a loan that has been rewritten, restructured, rolled  
22 over, or otherwise had its term extended or interest rate reduced, or  
23 has had a land payment or land clearing loan restructured.

24 (g) The director of agriculture shall dispose of property ac-  
25 quired by the Agricultural Revolving Loan Fund Board or by the commis-  
26 sioner through foreclosure, default, or other action arising out of  
27 agricultural loans or the sale of agricultural land. Disposals shall  
28 be conducted under regulations approved by the board. The regulations  
29 shall ensure that the property is disposed of so as to maximize the

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return to the state and shall require that the parcels of land that are composed primarily of cropland soils be restricted to agricultural uses.

\* Sec. 2. RESTRUCTURE OF AGRICULTURAL DEBT. (a) To increase the return to the state, the Agricultural Revolving Loan Fund Board may restructure loans in existence on June 25, 1987, made by the board or by the Alaska Agricultural Action Council based upon guidelines approved by the board. The restructuring may only include reduction of interest to rates below those specified by AS 03.10.030, an extension of the term of the loan, and an improvement to the security interest of the state. It may not reduce the amount of principal and interest owed before the loan is restructured.

(b) The maximum term of a loan modified under (a) of this section is 30 years from the date of restructuring.

(c) Notwithstanding any other provision of this section, the Agricultural Revolving Loan Fund Board may approve an application for restructuring under this section only upon

(1) the applicant's written release of the state, including the Alaska Agriculture Action Council, the agricultural revolving loan fund and the University of Alaska, from all potential liability for actions and omissions occurring before the date of restructuring that relate in any way to a state farm project, land sale, land sale relinquishment, farm loan, or loan application or loan modification application, whether granted or denied by the state; and

(2) assignment by the applicant to the board of the proceeds from the federal government under 7 U.S.C. 1442 (Conservation Reserve Program) and P.L. 88-26 (Feed Grain Act of 1963), as amended.

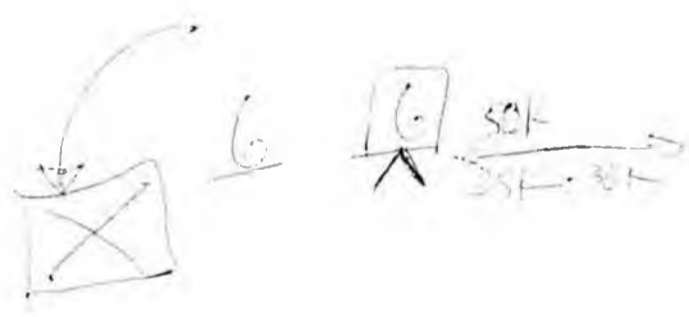
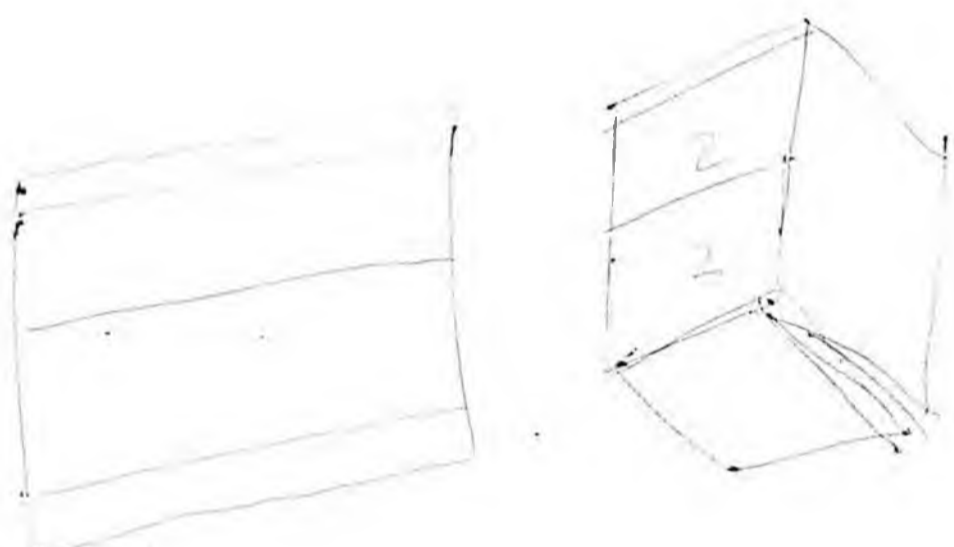
(d) In order to provide an incentive and opportunity to continue milk production, the board shall restructure the debt of any dairy farm that has

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produced at least 30,000 pounds of milk a month since November 15, 1985 and continues to produce 30,000 pounds of milk a month. If milk production falls below 30,000 pounds a month, the restructured debt shall become immediately due and payable. Restructure under this section is subject to the same limitations and conditions as provided in (a), (b), and (c) of this section.

\* Sec. 3. Section 2 of this Act is retroactive to June 25, 1987.

\* Sec. 4. This Act takes effect immediately under AS 01.10.070(c).



March 17, 1988

2665

SB 472

The Resources Committee considered SENATE BILL NO. 472 "An Act authorizing the commissioner of natural resources to transfer certain assets formerly owned by Matanuska Maid, Inc." and recommended it be replaced with

CS FOR SENATE BILL NO. 472(Resources), entitled:

"An Act authorizing the commissioner of natural resources to transfer the creamery formerly owned by Matanuska Maid, Inc."

and attached a Letter of Intent. Senator Coghill, Chairman and Senator Fanning signed "do pass." Senator Sturgulewski signed "do pass with additional information." Senators Eliason, Zharoff, Duncan and Fischer signed "no recommendation."

Zero fiscal note published today from Department of Natural Resources.

## Letter of Intent

for

## CSSB 472 (L&amp;C)

It is the intent of the Legislature that the Department of Natural Resources, when negotiating the lease/purchase of the Matanuska Maid Creamery, should zealously protect the liquid assets of the operation. This protection should take the form of stringent terms and conditions imposed on the cooperative i.e. that the cooperative, on a regular payment schedule, return to the state generated revenues for the purpose of reimbursing the liquid assets. These payments do not apply to the purchase price. It is also the intent and understanding of the Legislature that AS 36.30, the state procurement code, does not apply to the lease/purchase.

SENATE BILL NO. 472 was referred to the Finance Committee.

HB 345

The Health, Education and Social Services Committee considered CS FOR HOUSE BILL NO. 345(HESS) "An Act relating to coroners' inquests" and recommended do pass. The report

Analysis for CSSB 472(Resources) Fiscal Note contd.

impacts of this bill are as follows:

Lease payment income is projected to be \$156,000/year (\$13,000/month). The loss in income from immediate sale of the land and buildings in Anchorage over 20 years at 8% for the current tax value (March, 1988) is \$1,475,500 (\$148,200 /year). The combined value of cash (\$48,000), accounts receivable from milk sales (\$1,770,000), inventory (\$592,200), and prepaid expenses (\$125,000) equals \$2,535,200. The loan fund would receive no payment for this amount after contributing over \$3,000,000 in operating capital and plant improvements over the last three years.

In addition, the recently incorporated cooperative that is seeking the creamery lease purchase has no assets and no financial capacity to provide operating capital or plant maintenance. The exposure to the State of Alaska as owner of the facility would include working capital of \$3,000,000 and replacement of equipment based on depreciation of \$230,000 per year for 15 years to offset obsolescence and provide for future expansion. The projected cost for lease/ sale to a cooperative without the financial capacity to provide capital for operations and expansion totals \$8,868,600.

*DNR says that the bill will have 300k be transferred.*  
*DNR says there should be*

<u>FY 89</u>		<u>FY 90-93 Per Year Loss</u>
156.0	lease income	156.0 lease income
(148.2)	loss of opportunity for sale	(148.2) loss of opportun.
(48.0) ✓	loss of cash	(230.0) depreciation
(1770.0) ✓	loss of accounts receivable	
(592.2) ✓	loss of inventory	<u>(222.2) Loss per year</u>
(125.0) ✓	loss of prepaid expenses	
(230.0)	depreciation	
(3000.0)	loss of capital improvements	
<hr/>		
(5757.4)	Loss for FY 89	
<u>- 1943.0</u>		

*INVENTORY*

*See page 1  
Take up*

DECEMBER 31, 1987

## ASSETS

## Current assets

Cash		47,441.60
Receivables:		
Trade	1,549,860.69	
Notes receivable	382,376.89	
Other Receivables	343,818.13	
	<u>2,276,055.71</u>	
Less allowance for doubtful account	(202,523.00)	
Net receivables		2,073,532.71
Due from Matanuska Maid, Inc.		7,400.02
Inventories		592,182.24
Prepaid expenses		<u>125,391.63</u>
Total current assets		<u>2,845,948.20</u>

## Property plant and equipment

Land		2,360,000.00
Buildings and improvements	316,336.45	
Machinery and equipment	663,051.26	
Office furniture and fixtures	2,000.00	
Office equipment <sup>†</sup>	7,793.40	
Automotive equipment	236,319.93	
Computer equipment	34,570.00	
	<u>1,260,123.04</u>	
Less accumulated depreciation	(497,296.63)	
		<u>762,826.41</u>

## Total property plant &amp; equip

3,122,826.415,968,774.61Note to current assets

The amount indicated in "Due from Matanuska Maid, Inc." consists of labor, supplies and other costs incurred in the administration of the bankrupt estate.

MATANUSKA MAID DAIRY  
BALANCE SHEET

RUN D

DECEMBER 31, 1987

LIABILITIES AND EQUITY

Current liabilities		
Producers payable		241,034.78
Accounts payable		338,071.89
Due to Matanuska Maid, Inc.		25.00
Current portion long term debt		196,680.58
Accrued liabilities		
Salaries and benefits	106,628.75	
Taxes other than income	(1,183.30)	
Insurance		
Interest		
Other expenses	755.23	
Total accrued liabilities		106,200.68
Income taxes		
Total current liabilities		<u>882,012.93</u>
Long term debt less current portion		129,520.62
Stockholders equity		
Common stock		
Paid in capital	5,837,565.00	
Retained earnings	(880,323.94)	
Total equity		<u>4,957,241.06</u>
Total liabilities and equity		<u><u>5,968,774.61</u></u>

NVED

all new

INTENT LANGUAGE - 472

It is the intent of the legislature that the ARLF sell the creamery operation located at 814 Northern Lights and lease the land and buildings and that this be completed as soon as practicable.

1. Sale terms of the creamery operating assets. The sales price of the operating assets are to be determined as follows:

Cash - Retained by the ARLF

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Long-term debt - Assumed by the buyer and to be paid by buyer.

Intangibles - All intangibles such as goodwill and logos shall be transferred to buyer at date of sale for \$1.00.

Other operating assets - All other operating assets not specifically mentioned above shall be transferred to buyer at date of sale for \$1,000.00.

The ARLF shall receive a security interest in all assets which are sold in an amount equal to the value of that asset as determined above. The security interest shall not be released on any asset until the amount due on that asset has been paid in full.

*Carry - 6 yrs to pay back receivables*

During each and every month, until paid in full, the buyer shall pay to the ARLF an amount equal to 50 cents per hundred weight of milk processed at the creamery, or \$13,000.00 per month, whichever is greater. These payments shall apply toward the amounts owed the ARLF for the business assets acquired by the buyer. These <sup>PAYMENTS</sup> sums paid by the buyer shall apply toward the business assets in the following order:

- First: Prepaids
- Second: Inventories
- Third: Receivables
- Fourth: Machinery, fixtures and equipment
- Fifth: Intangibles
- Sixth: Other operating assets

2. Lease-purchase of land and buildings.

PROPOSED LEGISLATION  
TRANSFER OF MATANUSKA MAID CREAMERY FROM THE STATE  
TO ALASKA QUALITY DAIRY COOPERATIVE, INC.

TRANSFER OUT OF STATE CONTROL IS NECESSARY FOR THE FOLLOWING REASONS:

1. The Agricultural Revolving Loan Fund (ARLF) does not have the expertise, time or ability to operate the Matanuska Maid Creamery (Creamery) on a sustained basis.
2. The operation of a wholesale business by the state is not good policy.
3. The Creamery has been a continual financial drain on the ARLF.
4. The Creamery is in a very competitive market which requires that the business be aggressively managed to be competitive in the marketplace.
5. The state ownership of the Creamery limits the Creamery's ability to be aggressive because of the possibility of legal suits regarding pricing, etc, and, the issue of the state competing with private enterprise.
6. Fluid milk is the largest agricultural product produced in Alaska and is an important agricultural product.
7. The dairy farmers have joined together and have established the Alaska Quality Dairy Cooperative, Inc. (Co-op) as a vehicle to operate the Creamery.
8. The dairy farmers' very livelihood depends on the success of the Creamery and they have a genuine interest in the Creamery's success because their livelihood is dependent upon the successful operation of the Creamery.
9. The Creamery is the only creamery existing in Southcentral Alaska and there is no place else for the dairy farmers to sell their milk.
10. The dairy farmers need to have long term assurance of the continued operation of the creamery so that they can be assured of a market for their milk and then develop a long-term plan for their future.
11. The uncertainty of the Creamery operation limits the dairy farmers' ability to obtain outside financing because of the lack of certainty as to whether the creamery will exist in the future to market the farmers milk.

12. The uncertainty also restricts the dairy farmers' desire to improve and increase the size of their herds because without a reliable Creamery to sell to it makes no sense to make additional investment in the dairy industry.

13. Currently, the complete control of the farmers' destiny lies with the whims of a politically appointed ARLF board and Director of Natural Resources.

14. The undermanagement of the Creamery by the ARLF is slowly, but surely, eroding the Matanuska Maid market share; and, the longer this continues the harder it is to regain this market share.

15. The profits in the dairy industry are so small that there is not room for two profit centers, i.e., one at the dairy and one at the creamery. The dairy farmers will not be able to succeed if anyone else other than the Co-op were to acquire the Creamery.

16. The state has made an investment of tens of millions of dollars in the dairy industry and the only way that the farmer can repay the debt and protect the state's investment is to have a viable place to sell the dairy farmers' milk.

17. The industry currently employs directly over 150 people and if the industry fails these jobs will be lost forever.

18. The dairy industry, currently, has only about a 25% market share; but, with aggressive management, the market share can be increased which will add even more jobs.

19. The dairy industry is in a very precarious position and its very existence depends upon the creamery's economic viability.

20. The only way to insure that the dairy industry succeeds is to remove control of the Creamery from the ARLF.

FACTS:

1. The state took over operation of the Creamery on November 15, 1984.

2. The cumulative loss during the three years ended October 31, 1987 has been \$825,157.23. (Exhibit A)

3. The state represented "...that the Anchorage creamery, Palmer store and related fixtures had a value of not more than \$2.6 million." in the bankruptcy disclosure statement of Matanuska Maid, Inc. (Exhibit B).

4. The main assets of the Creamery operation are land and

buildings in Anchorage and Palmer, inventory, and receivables.

5. The dairy producers have joined together to form a cooperative owned equally by all producers called Alaska Quality Dairy Cooperative, Inc.

6. The dairy farmers, through Alaska Dairy, Inc. (ADI), a wholly owned subsidiary of Alaska Quality Dairy Cooperative, Inc., have entered into a contract for a period of one year to provide management oversight for the Creamery.

7. That the market which the Creamery is competing in is such that the Creamery cannot be competitive if it must service a large debt.

PLAN FOR TRANSFER OF CREAMERY TO ALASKA QUALITY DAIRY COOPERATIVE, INC.:

1. Effective January 1, 1989 the entire business operation would be transferred to the Co-op. This to include all assets which are currently under the management oversight agreement.

2. The Co-op be granted a one year lease of the facility located at 814 Northern Lights Boulevard and nine one year options to renew at \$1 per year as long as the Co-op is still in the creamery business.

3. The Co-op be granted an option to purchase the facility at 814 Northern Lights Boulevard after ten years if the Co-op continuously operates the Creamery during the ten year period ended December 31, 1998.

Explanation for Revised Fiscal Note

*from Joe Caze*

CSSB 472 (Resources)

<u>FY 89</u>		<u>FY 90-93</u>	
156.0	Lease Income	156.0	Lease Income
(148.2)	Loss of Opportunity for Sale	(148.2)	Loss of Opportunity
(230.0)	Depreciation	(230.0)	Depreciation
(3000.0)	Loss of Capital Improvements		
<hr/>		<hr/>	
(3222.2)	Loss for FY 89	(222.2)	Loss per year FY 90-93

Lease payment income is projected to be \$156,000 per year (\$13,000 per month). The loss in income from immediate sale of the land and buildings in Anchorage over 20 years at 8% for the current tax value (March, 1988) is \$1,475,500 (\$148,200 per year). The loan fund would receive no repayment for the contribution of over \$3,000,000 in operating capital and plant improvements during the last three years.

The recently incorporated cooperative that is seeking to lease/purchase the creamery has no assets and no financial capacity to provide operating capital or plant maintenance. The exposure to the State of Alaska as owner of the facility would include working capital of 3,000,000 and replacement of equipment based on depreciation of \$230,000 per year for 15 years to offset obsolescence and provide for future expansion.

Alternative Fiscal Note - April 30, 1988

	<u>FY'89</u>	<u>FY'90-93</u>
Lease-purchase payment	156.0	156.0
Reduction of state investment in plant	230.0	230.0
Loss of opportunity for sale*	(192.0)	(192.0)
	<hr/>	
Cash flow benefit to ARLF	194.0	194.0

\* Based upon 8% interest rate and estimate value of \$2,400,000

Mr. Joseph P. Cange  
P.O. Box 90647  
Anchorage, Alaska 99509

April 30, 1988

The Honorable Sam Cotten  
Co-Chair  
House Resources Committee  
Alaska House of Representatives  
P.O. Box V  
Juneau, Alaska 99811

RE: Senate Bill 472, An Act Authorizing the Department of  
Natural Resources to Transfer the Creamery Formerly  
Owned by Matanuska Maid, Inc.

Dear Representative Cotten:

Enclosed for your reference and review, please find a summary of my March 24 presentation to the Senate Finance Committee. In the summary, I have shown the reasons why this bill is critical for the survival of the Alaska dairy industry and, at the same time, I have detailed the cost benefits of SB 472 to Alaska and all Alaskans.

At minimum, SB 472 means jobs for Alaskans and it removes government from business. It provides for the dairy cooperative to lease the real estate and purchase the operating assets from the ARLF for 100% of the value of inventory, receivables, etc.; thus, the ARLF recoups its past investment in the creamery.

There are perhaps other ways to accomplish the transfer of the creamery but, I honestly believe, that there is no better way for the ARLF, Alaskans or dairy farmers than SB 472.

I believe that three and a half years of state control is more than enough and that now it is time to permit the farmers, whose very livelihood is dependent upon this creamery, to have an opportunity to "control their own destiny." Not unlike the thirteen colonies which "believed that their destiny should not be controlled by arbitrary dictation by bureaus in England, too far off to decide rightly and too little interested to have genuine concern,"

The Honorable Sam Cotten  
April 30, 1988  
Page Two

these twelve dairy farmers should have the right to self-determination. I believe that history will prove that in passing SB 472 you will have made the right decision.

I have also enclosed an "alternative fiscal note" which shows that there is a cash flow benefit to the ARLF of \$194,000 per year. This is submitted to refute the fiscal note prepared by DNR which showed a \$3,222,200 fiscal cost during 1989.

SB 472 is a fair, objective and equitable bill and, therefore, I ask your support.

Thank you very much for your time and consideration. I would be pleased to answer any questions that you have regarding this issue.

Sincerely,

Joseph Patrick Cange

Enclosure  
cc: Members, House Resources Committee

# ALASKA STATE SENATE

JOE P. JOSEPHSON  
DISTRICT H ANCHORAGE  
3111 C STREET, SUITE 550  
ANCHORAGE, ALASKA 99503  
(907) 561-7611



WHILE IN JUNEAU  
P.O. BOX V  
JUNEAU, ALASKA 99811  
(907) 465-4525

House Resources  
April 27, 1988

## SPONSOR STATEMENT ON CS SB 472 (Resources)

### What would CSSB 472 do?

1. Directs DNR to enter into a one-year lease with a dairy producers' cooperative for management and operation of the Matanuska Maid Creamery.
2. Legislative intent is that a lease be in effect by July 1, 1989.
3. Monthly lease payment is equal to \$.50 per hundredweight of milk processed or \$13,000, whichever is greater.
4. Lease is renewable annually for 14 years, if lessee complies with health and quality standards as well as other terms of the lease, and has managed the Creamery economically, profitably and efficiently.
5. If Creamery is successfully operated for ten years, DNR shall offer to sell it to the lessee.
6. The lease payments shall be applied toward the purchase price.
7. Sale price for the building is set at fair market value at the time the lease is initiated; price for the land is set at the time sale is requested.

### Why is this bill necessary?

1. Many have asked why the State is in the dairy business. This bill develops a rational process to transfer it to private industry.
2. Since the State's purchase of the Creamery in 1984, the Agricultural Revolving Loan Fund in DNR has pumped \$2,914,788 into the Creamery. The purpose of this bill is to remove that continuing financial drain.
3. DNR is currently working with Alaska Dairy Inc. (a subsidiary of the milk producers coop) to fashion a trial lease to manage the Creamery for one year. This trial, under DNR's watch, provides a smooth transition into the process set forth in SB 472. This bill provides the needed incentive and stability for the private sector to enter into this enterprise.

# STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

STEVE COWPER, GOVERNOR

400 WILLOUGHBY AVE.  
JUNEAU, ALASKA 99801-1796  
PHONE: (907) 465-2400

March 11, 1988

MAR 1

The Honorable Jack Coghill  
Chairman, Senate Resource Committee  
P.O. Box V  
Juneau, Alaska 99811

Dear Senator Coghill:

Subject: Senate Bill 472, which would authorize the commissioner of natural resources to transfer certain assets formerly owned by Matanuska Maid, Inc.

Position: The Department of Natural Resources supports the concept of returning the Matanuska Maid creamery and feed mill to the private sector, but is unable to support this bill for a number of reasons:

X  
o This bill requires the department to enter a lease/purchase contract with a cooperative of dairy producers but makes no provision for protecting state, ARLF, or non-dairy farm public interests, or the interests of dairy producers who are not in control of the cooperative. The department and the Agricultural Revolving Loan Fund (ARLF) Board currently have the authority and the responsibility to sell or lease the Matanuska Maid Creamery and feed mill under terms and conditions that are in the best interests of the state, the ARLF and the agricultural community.

o The \$1 per year lease/purchase option established by this bill makes no provision for a share of any revenue from the creamery or feed mill to be returned to the ARLF.

o The contract required by this bill would prevent other interested parties from purchasing the creamery for a period of twenty years, with no guarantee that the dairy cooperative would purchase the facilities during that time.

X o The contract required by this bill includes no provisions for assuring that the creamery and feed mill are managed economically, and no mechanism for terminating a lease or denying its renewal because of mismanagement. Yet the bill requires the state to lease to a cooperative regardless of its ability to manage.

o The bill does not clearly state which Matanuska Maid, Inc. assets will be transferred to a cooperative; will the real property, facilities, equipment, accounts receivable, cash and inventory all be transferred to the lessee for \$1 per year? If so, how does one lease cash, accounts receivable and inventory?

o There is no existing cooperative eligible to lease the feed mill. This bill invites the hasty organization of groups that have no management experience but are eager to take advantage of the \$1 per year lease/purchase terms.

As you know, the state would like to sell the creamery and feed mill to a buyer who will continue the operations. But the terms of sale should be in the public's best interest as well as the purchaser's and protect the interests of all producers who may wish to have milk processed at the creamery.

Recommendation: If the Legislature determines that requiring the department to lease the creamery and feed mill (with a 20 year purchase option at 1988 prices) to one particular group is in the best interests of the people of Alaska, we recommend that additional conditions be placed in the lease agreement to ensure that the creamery and feed mill are economically managed and that public funds invested in the facilities and property are regularly returned to the ARLF.

We also recommend that if a purchase option is exercised by the lessee, the purchase price be the fair market value at the time of sale. Alternatively, the facility could be sold subject to the condition that it be used for processing dairy products. This would help protect the integrity of the ARLF and the dairy industry by ensuring that the purchaser is interested in continuing creamery operations and developing a viable business rather than speculating on downtown Anchorage and Palmer real estate.

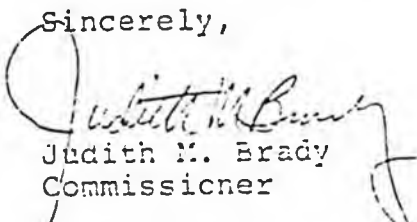
Senator Coghill

-3-

March 11, 1988

I have enclosed background information about the state's assumption of the former Matanuska Maid, Inc. business. Please let me know if I may provide additional information about this matter.

Sincerely,



Judith M. Brady  
Commissioner

Enclosure

cc: Sponsors  
Bob Evans  
Rod Swope  
Mark Weaver

# ALASKA STATE SENATE

JOE P. JOSEPHSON  
DISTRICT H ANCHORAGE  
3111 C STREET, SUITE 200  
ANCHORAGE, ALASKA 99503  
(907) 561-7611



WHILE IN JUNEAU  
P.O. BOX V  
JUNEAU, ALASKA 99811  
(907) 465-4325

March 22, 1988

Judy Brady, Commissioner  
Department of Natural Resources  
400 Willoughby Ave.  
Juneau, Alaska 99801

Dear Commissioner Brady:

I would like to thank you for meeting with Senator Coghill and myself last week on Senate Bill 472, the bill addressing the lease-purchase of the Matanuska Maid creamery. I believe your input was helpful in fashioning a better bill, and that many of your ideas are reflected in the Senate Resources substitute.

I am enclosing a copy of that substitute, along with the Committee's Letter of Intent. I invite you to continue to offer criticisms, additions and deletions as we proceed along the legislative path of this bill.

The bill is up before Senate Finance this Thursday, and I would be happy to talk with you further on any concerns you may have.

With best wishes, I am

Sincerely,

A handwritten signature in cursive script that reads "Joe P. Josephson".

Joe P. Josephson  
State Senator

JPJ:jdf

A SPECIAL REPORT ON THE  
DEPARTMENT OF NATURAL RESOURCES  
POINT MACKENZIE AGRICULTURE PROJECT  
MATANUSKA, MAID DAIRY

February 5, 1988

Audit Control Number

10-4293-88-S

MAR 25 1988

Commissioner, Department of  
Natural Resources

Judith M. Brady

Deputy Commissioner, Department  
of Natural Resources

Lennie Boston-Gorsuch

# STATE OF ALASKA

AUDIT DIVISION  
P.O. BOX W  
JUNEAU, ALASKA 99811-3300

## THE LEGISLATURE

BUDGET AND AUDIT COMMITTEE

February 5, 1988

Members of the Legislative Budget  
and Audit Committee:

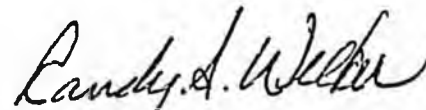
In accordance with a Legislative Budget and Audit Committee  
special request and the provisions of Title 24 of the Alaska  
Statutes, the attached report is submitted for your review.

A SPECIAL REPORT ON THE  
DEPARTMENT OF NATURAL RESOURCES  
POINT MACKENZIE AGRICULTURE PROJECT  
MATANUSKA MAID DAIRY

February 5, 1988

Audit Control Number

10-4293-88-S



Randy S. Welker, CPA  
Acting Legislative Auditor  
Division of Legislative Audit

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PURPOSE OF THE REPORT

In accordance with a Legislative Budget and Audit Committee request and Title 24 of the Alaska Statutes, this special report has been prepared to document Matanuska Maid Dairy's marketing effort and the State of Alaska's involvement in the Point MacKenzie agriculture project.

## AUDITOR'S CONCLUSION

In 1979 an administrative and legislative decision was made to salvage the dairy industry of southcentral Alaska through the development of a dairy project at Point MacKenzie. The economic feasibility of the project was based on assumptions developed from existing Matanuska-Susitna Valley dairy farms and a small test plot at Point MacKenzie. A plan was developed utilizing the small, family-run farm concept, state provision of infrastructure (roads, electricity, educational facilities), low interest loans, deferred payments, and land at less than market value. It was recognized at the time that the economic feasibility of the project was questionable. As stated in a 1980 study by the Office of Management and Budget: "Any combination of earlier interest payments, higher interest rates, higher construction costs and/or lower than required milk production will substantially alter the time required before operations are financially sound... The margin for costly mistakes is minimal."

As discussed in the following sections of this report, mistakes were made. The project has also been affected by circumstances unforeseen in 1980 such as technological innovations in shipping which allowed competitors to ship milk to Alaska faster and cheaper, the bankruptcy of the only creamery market for project milk -- Matanuska Maid and the subsequent reputation and market share loss resulting from that bankruptcy, and the decline in population in southcentral Alaska in recent years.

The result has been that of the original nineteen dairy parcels sold, eight are producing, all of which are currently delinquent on state loans. Those eight dairies are meeting the production expectations for the entire project; however, at current production levels and at current milk prices all farms are not yet economically viable. The Matanuska Maid creamery is in state ownership, run by contracted management. Although Matanuska Maid pays no debt service and sales in 1987 were in excess of \$12,000,000, the dairy operated at a loss of \$850,000, primarily due to state policy decisions to purchase more milk than demand required at a higher than market price.

These questions then arise: Can the dairy industry in southcentral Alaska be economically viable? If not, should the State continue to support the industry for other social and economic reasons? The answers to these questions depend on administrative and legislative policy decisions which need to be made. For all project farms to become viable, production levels and/or raw milk prices must increase. For Matanuska Maid dairy to become viable, prices paid to the producers must be modified based on market conditions. In brief, the road to economic viability in the current policy climate is increased demand or reduced number of suppliers.

An increased demand for local dairy products would greatly aid both the farmer's and the creamery's ability to prosper. As discussed in this report, Matanuska Maid is employing a number of marketing strategies aimed at increasing market share. There are also several pieces of legislation which have been or are currently being considered to encourage this to occur. The 1987 Legislative Session saw the passage of a bill giving a seven percent local bidders preference for agricultural products being purchased with State funds. This legislation should bring contracts with large purchasers of dairy products, such as school districts and Pioneer Homes, within Mat-Maid's reach. Legislation being considered includes SB 105 establishing a standardized method of date-labeling milk products which could also favorably impact demand.

If demand does not increase, the number of suppliers will decline. Inefficient or marginal dairy operations will declare bankruptcy or be foreclosed on by their primary creditor, the Agricultural Revolving Loan Fund (ARLF). The result will be a handful of large, well-managed dairy farms meeting demand. The State could then attempt to recapture investment through sale of the assets.

Should viability not occur as a result of these actions, policy makers also have the option to continue state support of the dairy industry in southcentral Alaska for other value received. Advocates of this view point to the following benefits: Alaskan self-sufficiency; pressure on competitors to provide better quality products at lower prices; jobs for approximately 150 Alaskans; access to fresh, quality produce; and investment protection. Several occurrences in 1987 lent credence to some of these arguments. In December of 1987 shipments of dairy products from the Washington area were interrupted which could have resulted in a shortage of fresh products to the consumer had Mat-Maid not been able to meet the increased demand. Division of Agriculture personnel also claimed that the introduction of Mat-Maid yogurt to the market resulted in a reduced price of competitive products by major retailers.

The State has an investment of approximately \$20,000,000 in the dairy industry at Point MacKenzie. That investment is comprised of an investment in Matanuska Maid Dairy of \$6,000,000, (\$3,000,000 in loans prior to foreclosure and an equal amount in contributed capital and operating funds since that time); \$11,000,000 in loans including land clearing, chattel, farm development and operating; \$1,300,000 for road survey and construction; and \$3,000,000 for electrification. Other indirect costs have been associated with the project in the form of loan moratoriums, investment in meat processing facilities to process cull cows and the sale of State land at less than market value.

Unless demand increases substantially, a decision to ensure profitability for all existing Point MacKenzie dairy farms will require continued subsidization. Those subsidies might be seen through price supports such as those which resulted in Matanuska Maid's \$800,000 operating loss in 1987; production credits for dairy products as proposed in HB 415 which Division of Agriculture personnel predict would cost an average of \$800,000 per year; or further postponement and/or restructuring of installment debt.

## HISTORY OF THE POINT MACKENZIE AGRICULTURE PROJECT

### Concept Origination

The Point MacKenzie agriculture project materialized when two major economic situations coincided, the decline in the number of commercially operated Alaskan dairies and the implementation by the State of an aggressive agricultural development program.

The Matanuska Valley, the center of the state's dairy industry, had supported the production demands of the several small creameries from its development in the 1940s until the 1970s. By this time one creamery, Matanuska Maid, had expanded considerably and become the principal producer of Alaskan dairy products. However, although production capabilities had expanded, supply was dwindling. Population growth and development pressure in the Valley was resulting in many farms being sold for commercial, residential, and industrial development purposes.

Matanuska Maid Dairy management and ardent supporters of a local dairy industry turned to the State for assistance. The Department of Natural Resources had already embarked on an agricultural development program for the purpose of creating a renewable resource base. That program was inaugurated in 1978 with the Delta Barley Project. The concept of a state-sponsored dairy project was suggested and quickly gathered political support.

The Point MacKenzie area, then in Matanuska-Susitna Borough ownership, was recommended because of the size and location of the parcel and the feasibility of developing that particular area as recommended in a University of Alaska study entitled Potential Milk Production in the Pt. MacKenzie Area of Southcentral Alaska. Legislative action was taken in the form of creating the Agricultural Action Council within the Office of the Governor to coordinate the state's agricultural programs and funding for the implementation of the Point MacKenzie project.

### Project Implementation

The planning phase began during the summer of 1980 and continued through the spring of 1981. The Matanuska-Susitna Borough relinquished land rights to the State. A number of state agencies were involved in the implementation phase including the Agricultural Action Council, the Attorney General's Office, and a number of divisions of the Department of Natural Resources including Forest, Land and Water Management, Agriculture and Technical Services.

Implementation was hampered somewhat by conflicts and confusion in the roles each of these agencies were to play. While planning oversight remained the responsibility of the Agricultural Action Council and project funding was controlled by that Council, it did not possess the statutory authority for carrying out the mandate. Coordination with appropriate state agencies, primarily the Department of Natural Resources, was envisioned. The conflict which resulted not only between the Council and the Department, but within divisions within the Department, contributed to complaints and problems with program implementation.

One such problem revolved around the issue of prequalification. While the Department recommended a streamlined prequalification plan, the Council opted for a more detailed regimen including training and education criteria and farm development plans. Another problem arose from the question of land clearing and timber utilization on the parcels being offered for lottery. The Division of Forest, Land and Water Management desired a two-year timber salvage program while the Council proceeded with an experimental land clearing technique, the chaining method. The Council's actions resulted in an attempt to stop the land disposal, both for the waste of the timber resource and the prequalification requirements.

The result was an out-of-court settlement regarding the timber and a temporary court order which allowed the lottery to happen as scheduled on March 6, 1981 conditional on no land exchanging hands. A final court order issued in May of that year voided the lottery on the basis the State exceeded its authority in prequalifying applicants by requiring farm development plans.

The decision was made by the Agricultural Action Council to proceed with a second lottery without prequalifying the applicants. That lottery was held on September 11, 1982. At that time agricultural interest in twenty-nine parcels was sold.

#### Project Statistics

The Point MacKenzie Agricultural Project consists of 31 parcels ranging in size from 301.26 acres to 634.03 and totaling 14,613.08 acres. Twenty nine of the parcels were offered for sale by the State of Alaska, while the remaining two were offered by the Matanuska-Susitna Borough. Nineteen of the parcels are designated as dairy parcels, while the remaining twelve are designated non-dairy. Title to all parcels limits use of the land to agricultural purposes only. Other restrictions include prohibitions against selling, leasing or otherwise assigning a part of the parcel without prior approval of the Director of Land and Water Management. No parcel of land less than 40 acres in size may be created by an assignment of interest.

## Land Clearing and Farm Development

Each parcel owner submitted a Farm Conservation Plan shortly after the lottery for approval by the Division of Agriculture. That plan, along with a stocking rate schedule for dairy parcels, was approved by the Division and became part of the development contracts entered into with the Division of Land and Water Management. Those contracts additionally imposed a development schedule requiring the clearing of land and planting of the first crop on at least 40% of the class II and III soils within the first three years and clearing and planting of 75% of the class II and III soils within six years.

Land clearing financing was available from the Alaska Agricultural Action Council. The Council approved 31 clearing loans for Point MacKenzie totalling \$3,200,000. Draws were taken against them which to date amount to \$2,200,000. Terms for these notes were 8% interest, the majority maturing 2026, with payments beginning in 1986.

Land clearing did not proceed as smoothly as planned because of problems with the smoke produced from burning berm piles. The intense public reaction to the problem resulted in regulations being implemented prohibiting burning when weather conditions would worsen the harmful effects, and also limited the amount which could be burned at any given time. In recognition of an expected slowdown in clearing due to the regulations, the Division of Agriculture, which assumed the clearing loan management responsibilities of the Agricultural Action Council when it was terminated, extended the terms of the clearing loans two years in conformance with ch. 166, SLA 1984. Loan contracts now expire in 1990 with loan repayment to begin in 1988.

The farm development schedule required a minimum acreage of 40% (5300 acres) to be in production by September 11, 1985. An official inspection of progress on these contracts was performed by the Division of Agriculture at that time and found approximately 7,000 acres in production, putting the project, as a whole, ahead of schedule. The development schedule further requires a minimum of 75% (9450 acres) be in production by September 11, 1988. Division personnel estimate that at current the project is close to target at 8,000 to 9,000 acres, though progress on individual tracts varies greatly, either behind or ahead of schedule. Another inspection is scheduled for the summer of 1988.

The development schedule also set out minimum stocking rates for dairy parcels. The number of cows to be regularly milked by November 1, 1985 was 883, and when inspected at that time was found to be 1,061. Again, while project totals were ahead of schedule, individual tract schedules varied greatly. Ten farmers were behind the stocking and

milking schedule; three corrected deficiencies within 60 days, two were in litigation and foreclosure proceedings were begun against the remaining five. The two in litigation were seeking to amend development requirements in the contracts to combine parcels and use one barn and one set of cows to meet the requirements of two separate contracts.

Four of the dairy owners in foreclosure sought an extension of the schedule. A one year extension was granted if the farmer would stipulate that at the end of the extension he would waive all defenses against the state if not in compliance at that time. Four parcel owners signed the stipulation and were granted extensions to the Fall of 1986. In September of that year the court decided the ongoing litigation by decreeing that the commissioner did not have the authority to waive or amend development requirements in contracts. Shortly thereafter another inspection was performed at Point MacKenzie and three of four farmers with extensions and the two previously in litigation were found to be in compliance. At present the State is in foreclosure proceedings against two dairy parcel owners who have not brought their parcels into compliance with contract terms.

The 1986 inspection revealed that some farmers who had been regularly milking in 1985 had ceased milking or were milking a reduced number of cows. Project farmers were notified that to ensure that the "regularly milking" requirement be met, the farm structures should be designed for and operated as a milking structure twelve months a year. It was advised by the Attorney General's Office that to comply with the contract, they must regularly milk the number of cows required by contract daily and continuously from the 1985 deadline at least until the contract has been satisfied and patent is issued. A recent policy issued by the Division of Agriculture, however, states that if the parcel was in compliance at the 1985 inspection or at the end of the stipulated extension the parcel is considered in compliance.

A final inspection is scheduled for September of 1988. Those farmers in compliance at that time and who have completed land purchase payments will be eligible to receive patent to their parcels. Development from that point on will be at the discretion of the owner provided it is consistent with the agricultural restrictions of the land title.

#### Development Costs: Estimated vs. Actual

Estimated development costs were developed and published in the project sale brochure using data developed by the University of Alaska in the 1980 feasibility study entitled Potential Milk Production in the Point MacKenzie Area of Southcentral Alaska. Assumptions made in that study to develop the estimated costs include the following:

1. Sufficient state land is available in the Point MacKenzie area for a dairy farm development project.
2. Land price is \$100 per acre with a \$50 homestead credit making the effective price \$50 per acre to the farmers.
3. Land-clearing costs are \$220 per acre for project farms.
4. The dairy farms will be designed for forage production in the form of silage and haylage; concentrate, hay, and straw requirements will be met by off-farm purchases.
5. Private slaughter facilities are currently available in the Matanuska Valley to handle cull cows and calves from project lands.
6. Electrical power hook-up will be provided each farm.
7. Roads to each farm will be constructed.

The Department envisioned a project of small family-run farms when putting the Point MacKenzie sale together. However, a number of factors contributed to driving the development costs beyond what could be recovered by small farm operations. The majority of these factors, such as the smoke from land clearing, problems associated with soil conditions and waste disposal were simply the result of developing farms in a previously unfarmed locale and learning to deal with the conditions endemic to that region. Historically, farm development in a previously undeveloped area would be a lengthy process of trial and error, but the Point MacKenzie land purchase contract placed a strict development schedule on the farmers. This necessitated additional expenditures to meet the development deadlines.

Although there is agreement that costs exceeded what was projected, there is disagreement between project farmers and Department of Natural Resources (DNR) personnel as to the extent the overages were necessary. State personnel contend that existing debt load is in part the result of bad management decisions by the farmers. It is acknowledged that the State's easy farm credit contributed to the bad management. Project farmers contend that development contracts were based on unrealistic assumptions, and that state management of those contracts has not been sufficiently flexible in times of economic change.

The result of the high development costs coupled with a declining demand for milk resulting from declining population has been an inability for some project farmers to meet their debt obligation to the Agricultural Revolving Loan

Fund (ARLF). The Department, utilizing its authority granted at AS 03.10.020(4), placed the loans in moratorium. That moratorium was ended December of 1986.

Although loan repayment was postponed and all milk produced has been purchased at a subsidized rate, all farms are currently delinquent on loan repayment. Review of dairy financial statements by ARLF personnel during recent applications for loan restructuring indicated not all delinquencies were the result of inability to pay, however. Some, in fact, could be attributed to a lax enforcement policy of the Division as documented in previous financial audits of the Loan Fund by the Division of Legislative Audit.

## MATANUSKA MAID DAIRY

### Background

The Matanuska Maid Dairy is comprised of a creamery in Anchorage and a feed mill and wholesale/retail store located in Palmer. Until the business was acquired at foreclosure sale by ARLF in November of 1985, it was operated by Matanuska Maid, Inc. an agricultural cooperative corporation.

The same economic factors which lead to the initiation of the Pt. MacKenzie Dairy Project, namely an increased demand for dairy products, a reduction in number of producing dairy farms in southcentral Alaska and improved shipping technology from competitive markets, caused financial problems for Matanuska Maid. The creamery expanded its plant to meet the growing demand but found itself with a declining inventory of milk to process. During the period September 1979 through October 1980 Matanuska Maid received four loans from ARLF totalling \$2,900,000 secured by real property, inventory and accounts receivable. A chapter 11 reorganization petition was filed in bankruptcy court by the Corporation in November of 1983 with ARLF receiving permission to foreclose. Through a series of settlement proceedings, title to inventory was obtained, culminating in the purchase at foreclosure sale in 1985 by offset bid from ARLF.

During this period a contract was let with the Small Business Development Center of Washington State University (WSU) to study the feasibility of successfully reorganizing Matanuska Maid Inc. That study, released July 1984, concluded that "With strong fiscal and management control and the assumption of a aggressive marketing posture, reorganization of Matanuska Maid is feasible." That study made recommendations such as waiver of past due interest and principal and a moratorium of future interest and principal against state debts for both the creamery and producers for a period of at least three years. It also recommended consideration of legislation which would limit the shelf life for milk produced in the lower 48 states and transported to Alaska.

The ARLF Board of Directors assumed directorship of Matanuska Maid after foreclosure. Recognizing their lack of expertise in the creamery business, a management contract was let for the day to day management of the creamery. The directorship of the creamery proved to be very time consuming for the ARLF Board. The Board decided that retention of the creamery in state ownership was not in the best interest of the state. Offers to purchase were requested during the spring of 1986 but all were found to be unacceptable.

A new strategy for moving Matanuska Maid from state to private ownership was born in 1987. The incorporation of an

entity named Alaska Dairy, Inc. (ADI) has been proposed to provide oversight management for Matanuska Maid. The ADI board would consist of an ARLF Board representative, four dairy farmers, the director of the Division of Agriculture, the manager of Matanuska Maid and six public representatives. The ADI Board was to assume directorship in January 1988 under a one-year agreement. The agreement specifies that payable accounts will be kept current, the management contract would be honored, and that all profits and/or losses generated by the creamery operation would belong to ARLF. ARLF will provide up to a maximum of \$60,000 a month for the initial six months to cover operating losses. If losses exceed this ceiling milk prices paid to dairy farms must be adjusted accordingly.

The primary motivation in the new strategy is to allow the dairy farmers ". . . to participate in the management oversight for the creamery, which is currently the only entity which will purchase the milk produced on their farms."

#### Milk Pricing: The Double Edged Sword

The price of milk paid to the producers has been the basis of a difficult policy dilemma. The ability of Pt. MacKenzie dairy farmers to produce adequate income to cover operating costs and cover debt incurred, primarily to ARLF, is predominantly effected by the price they receive for milk produced. The ability of Matanuska Maid to be economically viable also depends on that entity's ability to adjust the price of milk paid to producers. As concluded in the 1984 WSU study: "Crucial to the future survival of Mat-Maid are strong controls and a rethinking of the relationship between producers and the creamery. Price paid to producers should be adjusted and modified based upon market conditions and the ability to compete effectively as the creamery is the market extension of the producers rather than a buyer of raw milk at producer-directed prices."

Although Alaska is exempt from federal milk price controls which effectively place both ceiling and floor on the price paid to producers, it competes with producers from the Puget Sound area which are controlled. The Puget Sound area produces one of the largest milk surpluses nationally and Alaska has traditionally been a primary market for that surplus. Thus, prices paid to local producers must be maintained sufficiently low so when added to production and delivery costs the final price to distributors competes with delivered cost of Puget Sound surplus milk. Ironically, the Puget Sound area is also the market for Alaskan surplus, which results in an extremely low price being received for Alaskan milk shipped to that market.

The Division of Agriculture, an advocate for agricultural interests in the state, and the ARLF Board have had to

balance the needs of the dairy farmers with the need to cover operating costs of the creamery. As previously discussed, a number of debt relief methods had been implemented to assist Pt. MacKenzie farmers. The policy decision of the Division of Agriculture in 1987 to not reduce the price of milk to producers when market forces (i.e. increased production from Pt. MacKenzie and decreased market demand due to shrinking population) necessitated it then became, in essence, another form of state support of the Alaska dairy industry. This action resulted in operating losses for Mat-Maid which were covered by ARLF in 1987 in the amount of \$800,000.

The proposed contract between ARLF and ADI would limit the amount of operating losses which will be covered by ARLF to \$60,000 per month. It also includes the following language regarding pricing. "ADI may not increase the price of milk as it exists on November 1, 1987 paid to dairy farms if the creamery shows an operating loss. ADI may lower the price of milk paid to dairy farms at any time; however, ADI will lower the price of milk paid to dairy farms if the operating loss exceeds \$60,000 in any one month during the period January 1, 1988 to June 30, 1988." If this agreement is entered into it will reflect a change in policy for the Division of Agriculture from subsidizing the dairy industry through price supports towards creating a more open market system where price is determined by supply and demand.

#### Marketing: Problems and Strategy

The need for a more aggressive marketing posture by Matanuska Maid was discussed in the 1984 WSU study and has continued to be a source of criticism of the creamery by Alaskan dairy farmers. Since the State assumed ownership in 1984 Matanuska Maid management has been making a significant effort to address this problem. From a virtually non-existent advertising budget, the creamery began spending between \$5,000 to \$10,000 a month in 1986, predominantly in radio and television spots and a total of \$218,000 in 1987.

The creamery has also increased its product lines by 40 items, including introducing two new products in 1986, another two in 1987 with plans for two more in 1988. The new items which have been added are cottage cheese, sour cream, ice cream base which is sold to an independent producer, and yogurt. These products have done well and yield a higher profit margin to the creamery than does the sale of bottled milk.

Plans for 1988 include the introduction of cheese which, for the first time in Mat-Maid history will give the creamery a way of utilizing surplus milk. Other methods of using surplus milk, namely converting it to powdered milk or to butter have not been used because of the high capitalization

cost for producing powdered milk and insufficient fat content to produce butter. The inability to utilize surplus milk lead to the situation in 1987 whereby surplus milk was purchased by Mat-Maid then dumped or exported to Seattle. Once cheese production begins that situation should not occur again.

An additional benefit to cheese production is that it should allow Mat-Maid to participate in a Federal program which will purchase and store the cheese produced in excess of local demand. Although this situation will allow purchase of virtually all milk produced in state, a new pricing structure for price paid to producers will have to be implemented. It is a common industry practice that milk purchased as surplus milk for conversion to a product with a long shelf life is purchased at a lower price than that purchased for conversion to bottled milk.

The most difficult marketing challenge has been the general public which Mat-Maid is attempting to win through advertising, promoting the benefits of locally produced products. They have seen results in the form of increased market share only to have those results reversed by pricing strategies of retail distributors. Though Mat-Maid has attempted to produce a competitively priced product, they cannot control the price charged to the consumer by the retail distributor.

The majority of dairy products sold in southcentral Alaska are sold by the two major retail grocery chains. Both chains distribute Mat-Maid as a secondary product line, utilizing various techniques such as pricing and shelf space allotted to encourage the primary line be sold first. Pull-dating procedures by competitive producers also effects consumer interest. There is currently no governmentally imposed standards for what date appears on the product thus identically dated milk may differ significantly in age. Mat-Maid has adopted a conservative dating policy in an effort to develop and maintain a reputation for quality. Mat-Maid also guarantees repurchase of past-dated products where the primary product line may not. To woo the general public, therefore, Mat-Maid must not only create a public awareness of its product, but demonstrate a superiority of a locally produced product which justifies the price differential charged by retail distributors.

Matanuska Maid continues efforts to become a primary product line with the major retailers while exploring other avenues of distributing its product lines. The corporation has worked with private distributors offering home delivery which has seen a resurgence in popularity recently as well as distributors for restaurants and small stores. The number of small retail operations is limited, however, because of the declining economic condition of the State combined with a Mat-Maid policy of discontinuing service to retailers whose delinquent accounts exceed 60 days.

# STATE OF ALASKA

## DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

STEVE COWPER, GOVERNOR

400 WILLOUGHBY AVE.  
JUNEAU, ALASKA 99801-1796  
PHONE: (907) 465-2400

March 17, 1988

RECEIVED

MAR 22 1988

Mr. Randy S. Welker, CPA  
Acting Legislative Auditor  
Division of Legislative Audit  
P.O. Box W  
Juneau, Alaska 99811-3300

LEGISLATIVE  
AUDIT

Dear Mr. Welker:

I appreciate the opportunity to comment on the preliminary report for the Point MacKenzie Agricultural Project. I compliment you on a thorough effort, and believe that you have provided an accurate perspective on the history of the project and on the new direction being adopted by the Division of Agriculture.

You may wish to consider the following comments and observations:

1) The continued evolution of the Point MacKenzie project is likely to result in the failure of some of the farms, as well as successes for others. Critical factors in this evolution include not only future milk prices and state subsidies (or lack thereof), but also the management ability of individual producers, the amount of private capital available to producers, and the implementation of a restructuring program for existing debt.

A restructuring program has been developed for ARLF borrowers. It effectively reduces debt service on ARLF loans for those who cannot meet original loan terms by providing for repayment at reduced rates of interest over a longer period of years.

2) You note in the third paragraph of page three ("Auditor's Conclusion") that at current production levels and at current milk prices, all farms are not yet economically viable. This statement is true. It is also true that the use of loan funds and personal funds varied considerably among producers. Some undoubtedly made excessive

expenditures for non income producing assets (e.g. homes and unnecessary equipment) while others used a higher percentage of funds for milk cows and other necessary assets -- resulting in higher income potential for the invested dollar. Thus, the fact that a farm is not economically viable may be the result of management strategies that were not as efficient as they could have been.

3) The statement in the third paragraph that Matanuska Maid loans are "in moratorium" probably should be modified. The Matanuska Maid real estate was purchased at a foreclosure sale by offset bid on November 29, 1985. The state now owns the business and assets, and the loans receivable were converted to assets at cost. New funds advanced are considered as investment in the asset, not as loans to a business.

4) With respect to the fourth paragraph of page three, I have already noted that the department believes that it is not likely that all of the operating dairies on the project will prove viable under existing management. Again, this is because of inevitable differences in financial strength and management abilities of the operators, and forces of competition that we believe to be healthy and necessary if efficient farming is to be encouraged.

5) The department disagrees with the statement on page 12 that a lax enforcement policy on loan collections is the reason for the delinquency rate on Point MacKenzie farms. The department has worked for over 14 months to develop and implement a trouble debt restructure program. This was initiated immediately after the period during which Point MacKenzie loans were in legal moratorium, as soon as it became clear that some, if not all, of the Point MacKenzie farmers were financially distressed and unable to make payments. The intent of the department was to develop a program to handle this troubled debt and to minimize financial losses to the ARLF, and we are now both restructuring debt and collecting on loans made to borrowers who do not qualify for restructuring. We will continue this policy and program for all borrowers, including those at Point MacKenzie.

6) Finally, it may be helpful to note that we are continuing to pursue options to place the creamery operation into

Mr. Randy S. Welker

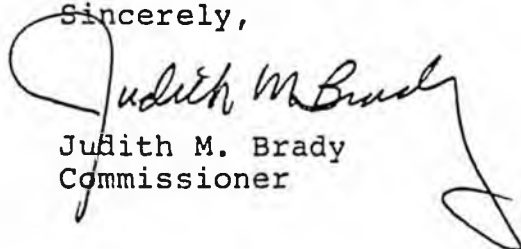
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March 17, 1988

the private sector, and are trying to do so without exposing the state or the industry to undue risk from unqualified management or to an ownership group lacking the assets to operate the business.

I hope these comments prove helpful.

Sincerely,

A handwritten signature in cursive script that reads "Judith M. Brady". The signature is written in dark ink and is positioned to the left of the typed name and title.

Judith M. Brady  
Commissioner

3rd fiscal note

STATE OF ALASKA  
1988 LEGISLATIVE SESSION

BILL VERSION: CSSB 472 Resources  
PUBLISH DATE: \_\_\_\_\_

FISCAL NOTE

REQUEST:

Revision Date: 3/31/88  
Title: Transfer Matanuska Maid Assets

Agency Affected: Natural Resources  
BRU: Agricultural Management

Sponsor: Sen. Resources Committee  
Requestor: Senate Finance Committee

Components: ARLF

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 88	FY 89	FY 90	FY 91	FY 92	FY 93
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-	(3222.2)	(222.2)	(222.2)	(222.2)	(222.2)

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL						

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

This fiscal note adjusts the revenue loss to the state related to transfer of the creamery to a dairy cooperative because the cash, accounts receivable, inventory and prepaid expenses will not be included in the transfer. (See attached explanation).

Prepared by: Hal Ward  
Division: Division of Agriculture

Phone: 745-7200  
Date: 3/31/88

Approved by Commissioner: [Signature]  
Agency: Natural Resources

Date: 3/31/88

Distribution (by preparer):

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

Explanation for Revised Fiscal Note

CSSB 472 (Resources)

<u>FY 89</u>		<u>FY 90-93</u>
156.0	Lease Income	156.0 Lease Income
(148.2)	Loss of Opportunity for Sale	(148.2) Loss of Opportunity
(230.0)	Depreciation	(230.0) Depreciation
(3000.0)	Loss of Capital Improvements	
<hr/>		<hr/>
(3222.2)	Loss for FY 89	(222.2) Loss per year FY 90-93

Lease payment income is projected to be \$156,000 per year (\$13,000 per month). The loss in income from immediate sale of the land and buildings in Anchorage over 20 years at 8% for the current tax value (March, 1988) is \$1,475,500 (\$148,200 per year). The loan fund would receive no repayment for the contribution of over \$3,000,000 in operating capital and plant improvements during the last three years.

The recently incorporated cooperative that is seeking to lease/purchase the creamery has no assets and no financial capacity to provide operating capital or plant maintenance. The exposure to the State of Alaska as owner of the facility would include working capital of 3,000,000 and replacement of equipment based on depreciation of \$230,000 per year for 15 years to offset obsolescence and provide for future expansion.

# STATE OF ALASKA

AUDIT DIVISION  
P.O. BOX W  
JUNEAU ALASKA 99811-3300

## THE LEGISLATURE

BUDGET AND AUDIT COMMITTEE

February 5, 1988

SUMMARY OF: A Special Report on the Department of Natural Resources, Point MacKenzie Agriculture Project and the Matanuska Maid Dairy, February 5, 1988.

### PURPOSE OF THE REPORT

In accordance with a Legislative Budget and Audit Committee request and Title 24 of the Alaska Statutes, this special report has been prepared to document Matanuska Maid Dairy's marketing effort and the State of Alaska's involvement in the Point MacKenzie agriculture project.

### AUDITOR'S CONCLUSION

In 1979 an administrative and legislative decision was made to salvage the dairy industry of southcentral Alaska through the development of a dairy project at Point MacKenzie. The economic feasibility of the project was based on assumptions developed from existing Matanuska-Susitna Valley dairy farms and a small test plot at Point MacKenzie. It was recognized at the time that the economic feasibility of the project was questionable. As stated in a 1980 study by the Office of Management and Budget: "Any combination of earlier interest payments, higher interest rates, higher construction costs and/or lower than required milk production will substantially alter the time required before operations are financially sound... The margin for costly mistakes is minimal."

As discussed in this report, mistakes were made. The project has also been affected by circumstances unforeseen in 1980. The result has been that of the original nineteen dairy parcels sold, eight are producing, all of which are currently delinquent on state loans. Those eight dairies are meeting the production expectations for the entire project; however, at current production levels and at current milk prices all farms are not yet economically viable.

The Matanuska Maid creamery is in state ownership, run by contracted management. Although Matanuska Maid pays no debt service and sales in 1987 were in excess of \$12,000,000, the dairy operated at a loss of \$850,000, primarily due to state policy decisions to purchase more milk than demand required at a higher than market price.

The price of milk paid to the producers has been the basis of a difficult policy dilemma. The ability of Pt. MacKenzie dairy farmers to produce adequate income to cover operating costs and cover debt incurred, primarily to the Agricultural Revolving Loan Fund, is predominantly effected by the price they receive for milk produced. The ability of Matanuska Maid to be economically viable also depends on that entity's ability to adjust the price of milk paid to producers.

The most difficult marketing challenge has been the general public which Matanuska Maid is attempting to win through advertising, promoting the benefits of locally produced products. They have seen results in the form of increased market share only to have those results reversed by pricing strategies of retail distributors. Though the dairy has attempted to produce a competitively priced product, they cannot control the price charged to the consumer by the retail distributor.

These questions then arise: Can the dairy industry in southcentral Alaska be economically viable? If not, should the State continue to support the industry for other social and economic reasons? The answers to these questions depend on administrative and legislative policy decisions which need to be made. For all project farms to become viable, production levels and/or raw milk prices must increase. For Matanuska Maid dairy to become viable, prices paid to the producers must be modified based on market conditions. In brief, the road to economic viability in the current policy climate is increased demand or reduced number of suppliers.

S B

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# HOUSE COMMITTEE REPORT

(9)

Date referred: 5/4/88

FURTHER REFERRALS:

DATE: 5/7/88

The Resources Committee has considered CSSB 475(Res)

"An Act establishing the Tugidak Island Critical Habitat Area; and providing for an effective date."

**RECOMMENDS:**

- replace with HCS (SSB 475(Res))  the same title
- attached amendment(s)  a new title
- do pass
- do not pass
- no recommendation
- individual recommendations
- additional referral to the \_\_\_\_\_ Committee

**ADOPTS:**  \_\_\_\_\_ letter of intent

**ATTACHES NEW FISCAL NOTE(S):**

- fiscal impact  same as previous fiscal note published \_\_\_\_\_
- zero fiscal note  same as previous zero fiscal note published 4/19/88
- zero with analysis

**SIGNING DO PASS:**

Jan Gt  
Mike Harper  
W. P. J.  
W. P. J.  
Adelheid Herrmann

**SIGNING OTHER RECOMMENDATIONS:**

Dick Dunbar Needs Area Plan  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_

Jan Gt  
Chairman's signature

FISCAL NOTE

REQUEST:

Revision Date: 2/16/88 Agency Affected: DNR  
 Title: An Act establishing the Tugidak Island critical habitat area. BRU: Land & Water Management  
 Sponsor: Zharoff Components: \_\_\_\_\_  
 Requestor: Seante Resources

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 88	FY 89	FY 90	FY 91	FY 92	FY 93
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING						
CAPITAL	0	0	0	0	0	0
REVENUE	0	0	0	0	0	0

FUNDING: (Thousands of Dollars)

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

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

The Department of Natural Resources anticipates no fiscal impact with respect to this legislation.

Prepared by: Lawrence Z. Ostrovsky Phone: 465-2400  
 Division: Commissioner Office Date: 4/11/88  
 Approved by Commissioner Judith M. Brady Date: 4/11/88  
 Agency: Department of Natrual Resources

Distribution (by preparer):

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

Original sponsor: Zharoff

1 IN THE SENATE

BY THE RESOURCES COMMITTEE

2 HOUSE CS FOR CS FOR SENATE BILL NO. 475 (Resources)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FIFTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act establishing the Tugidak Island Critical  
7 Habitat Area; and providing for an effective date."

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

9 \* Section 1. PURPOSE. The Tugidak Island Critical Habitat Area is  
10 established to ensure the protection and enhancement of fish and wildlife  
11 habitat and populations, especially marine mammals, birds, fish and shell-  
12 fish; the continuation of fish and wildlife harvest; and public use and  
13 enjoyment of the area in a high quality environment.

14 \* Sec. 2. AS 16.20 is amended by adding a new section to read:

15 Sec. 16.20.610. TUGIDAK ISLAND CRITICAL HABITAT AREA. (a) The  
16 state land within the following described area is established as the  
17 Tugidak Island Critical Habitat Area:

18 (1) Township 41 South, Ranges 33 - 34 West, Seward Meridian

19 (2) Township 42 South, Range 33 West, Seward Meridian

20 Sections 1 - 11

21 Sections 14 - 23

22 Sections 25 - 36

23 (3) Township 42 South, Ranges 34 - 35 West, Seward Meridian

24 (4) Township 43 South, Ranges 34 - 35 West, Seward Meridian

25 (b) In addition to the area described in (a) of this section,  
26 the water and the land below the mean high tide line in the lagoon at  
27 the northeast end of Tugidak Island are included within the Tugidak  
28 Island Critical Habitat Area.

29 (c) The Tugidak Island Critical Habitat Area described in (a)

1 and (b) of this section shall be managed under a management plan  
2 prepared by the department.

3 (d) The department shall permit existing cabins to remain,  
4 subsistence and recreational uses to continue, and commercial uses  
5 such as seal hunting and placer mining to continue, if appropriate  
6 under the management plan adopted under (c) of this section to the  
7 extent that the activities are compatible with the establishment of  
8 the Tugidak Island Critical Habitat Area.

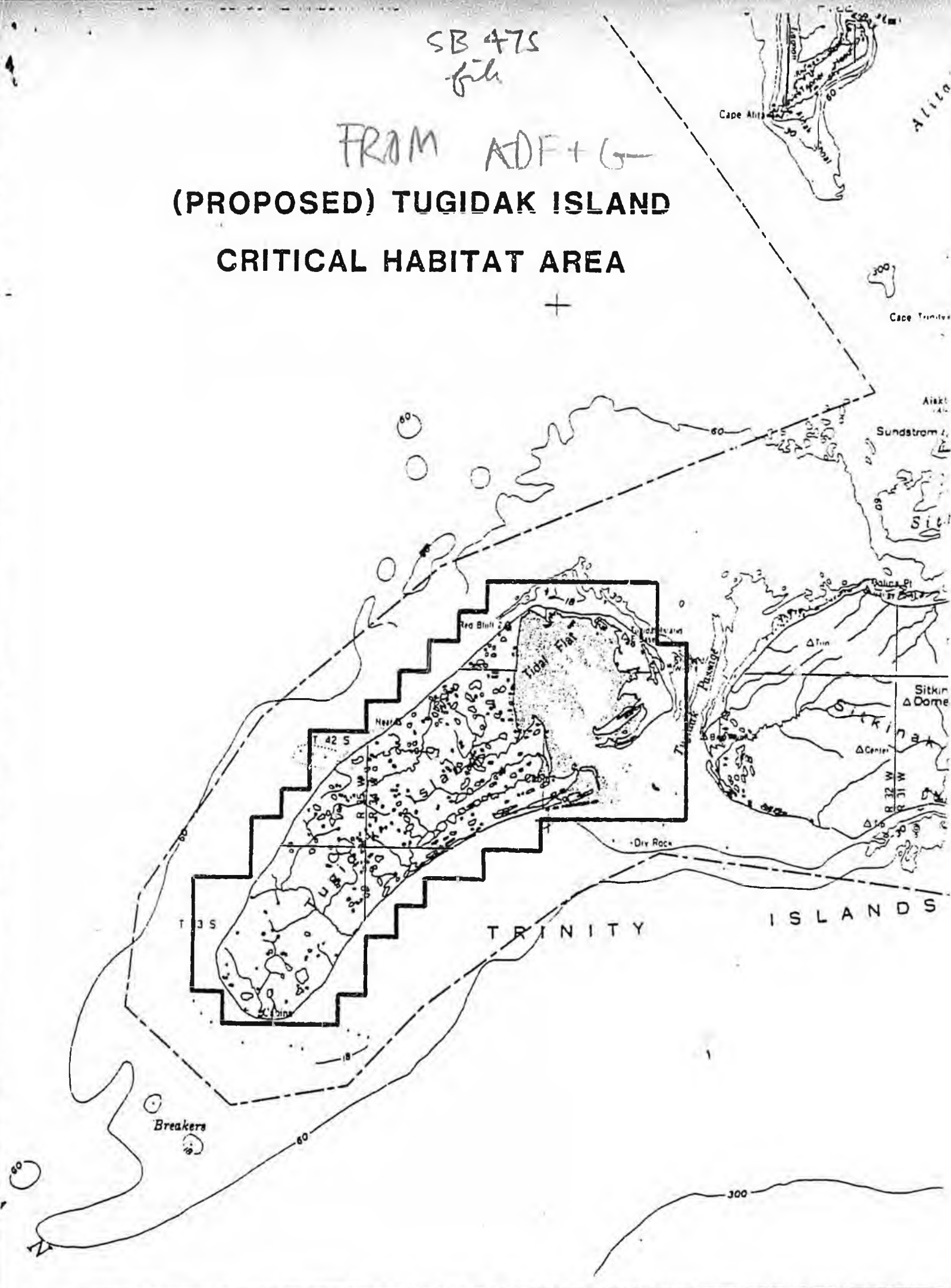
9 (e) The department shall permit entry within the Tugidak Island  
10 Critical Habitat Area for the exploration and development of oil and  
11 gas resources when compatible with the purposes for which the critical  
12 habitat area was established. An oil and gas lease of state land  
13 within the Tugidak Island Critical Habitat Area is valid and continues  
14 in full force according to its terms.

15 \* Sec. 3. After completion of plans for the area including the Tugidak  
16 Island Critical Habitat Area as enacted in sec. 2 of this Act, the commis-  
17 sioners of natural resources and fish and game may recommend an adjustment  
18 in the boundaries of the critical habitat area to the legislature.

19 \* Sec. 4. This Act takes effect immediately under AS 01.10.070(c).

SB 475  
file

FRAM ADF+G  
(PROPOSED) TUGIDAK ISLAND  
CRITICAL HABITAT AREA



For an Act entitled: "An Act establishing Tugidak Island  
Critical Habitat Area and providing  
for an effective date."

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

\*Section 1 AS 16.20 is amended by adding a new section to  
read:

Sec. 16.20.615. TUGIDAK ISLAND CRITICAL HABITAT AREA.  
(a)The land and water contained in the following described  
parcels are designated as the Tugidak Island Critical  
Habitat Area:

- (1) Township 41 South, Range 33 West, Seward  
Meridian  
Sections 19-22  
Sections 27-5
- (2) Township 42 South, Range 33 West, Seward  
Meridian  
Sections 2-11  
Sections 14-23  
Sections 26-30
- (3) Township 41 South, Range 34 West, Seward  
Meridian  
Sections 23-27  
Sections 33-36
- (4) Township 42 South, Range 34 West, Seward  
Meridian  
Sections 1-5  
Sections 7-36
- (5) Township 43 South, Range 34 West, Seward  
Meridian  
Sections 3-8  
Section 15
- (6) Township 42 South, Range 35 West, Seward  
Meridian  
Sections 13-14  
Sections 23-27  
Sections 33-36
- (7) Township 43 South, Range 35 West, Seward  
Meridian  
Sections 1-4  
Sections 7-30  
Sections 32-35

(b) The Tugidak Island Critical Habitat Area is established to ensure the protection and enhancement of fish and wildlife habitat and populations, especially marine mammals, birds, fish and shellfish; the continuation of fish and wildlife harvest; and public use and enjoyment of the area in a high quality environment.

\*Section 2. This Act takes effective immediately under AS 01.10.070(c).



**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: Rep. Adelheid Herrmann  
Co-Chair  
House Resources Committee

FROM: Senator Fred F. Zharoff

DATE: May 3, 1988

RE: CS For Senate Bill 475 - "An Act establishing the Tugidak Island Critical Habitat Area; and providing for an effective date."

I respectfully request that CSSB 475 be scheduled for a hearing before the House Resources Committee at the committee's earliest convenience. The bill passed the Senate on May 3 by a vote of 14-0, and, upon reconsideration, 20-0.

SB 475 creates the Tugidak Island Critical Island Critical Habitat Area. Tugidak Island is an 84,480 acre island approximately 16 miles southwest of Kodiak Island. It is state-owned land within the Kodiak Island Borough. The island features exceptional wildlife and habitat values. Under critical habitat area status, these values would be protected.

I have attached the following backup information for SB 475:

1. Description of the proposed Tugidak Island Critical Habitat Area and map, prepared by the Division of Habitat in the Department of Fish and Game.
2. Department of Fish and Game bill analysis and fiscal note. The fiscal note was zeroed out in the Senate Finance Committee. The committee's intent was that the department should adhere to its existing schedule of one plan per year.
3. Department of Natural Resources position paper and fiscal note. The amendments suggested by the department were adopted.
4. Letters of support.
5. Map showing Tugidak Island in relation to Kodiak Island.
6. Letter from the U.S. Fish and Wildlife Service containing background information on Tugidak Island habitat.
7. Map of mining claims on Tugidak Island.



# STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

STEVE COWPER, GOVERNOR

400 WILLOUGHBY AVE.  
JUNEAU, ALASKA 99801-1796  
PHONE: (907) 465-2400

April 11, 1988

Senator Jack Coghill  
Chairman Senate Resources Committee  
Alaska State Senate  
P.O. Box V  
Juneau Alaska

99811

Re: SB 475 Tugidak Island Critical Habitat Area

Dear Senator Coghill;

Position: The Department of Natural Resources is not opposed to the protection of critical habitat on Tugidak Island, and recognizes that critical habitat values exist there. However, the Department believes that legislative designation should follow from the planning process. Work on the Kodiak Island area plan is scheduled to begin this summer.

Background: The Kodiak Island Area plan will include Tugidak Island. Legislative designation at this time would preclude management prerogatives and boundary descriptions arrived at through the planning process. Planning team members will include representatives from the Department of Fish and Game. Additionally, other concerns such as archaeological and oil and gas and other resource values will be addressed at that time.

If the legislature should decide to pass critical habitat legislation at this time, the Department would recommend language which would allow for boundary amendment as a result of planning process, as well as language which will allow for oil and gas exploration activities.

I appreciate the opportunity to comment on this legislation and am happy to make my staff available to work with the committee as it moves through the legislature.

Sincerely,

*Jennie Jones*

Judith M. Brady

*for* Commissioner of Natural Resources

cc

Committee Members

Sponsor

Governor's office

DRAFT 2/88

PROPOSED TUGIDAK ISLAND CRITICAL HABITAT AREA  
BACKGROUND INFORMATION

LOCATION: The proposed Tugidak Island Critical Habitat Area is located approximately 15 miles south of Kodiak Island and is part of the Trinity Islands group.

AREA DESCRIPTION: The proposed Tugidak Island Critical Habitat Area is a large treeless, low lying island. Among its unique features is a large shallow lagoon and barrier spit complex at its northern end.

LAND STATUS: The proposed critical habitat area encompasses approximately 84,480 acres and is entirely state-owned land and water. It is located within the Kodiak Island Borough.

JUSTIFICATION: Tugidak Island is unique in the Gulf of Alaska not only because of its unusual number of extremely productive and diverse fish and wildlife habitats but also because those habitats have remained in a relatively natural, undisturbed state. To date very little human disturbance has occurred on the island to threaten the vulnerable groundnesting birds, harbor seal pupping areas and rich lagoon environment.

Marine Mammals: Tugidak is most renowned for its harbor seal population. Tugidak Island has historically supported one of the largest harbor seal populations in the world, estimated at 15,000 to 20,000 animals with peak concentrations of hauled out seals reaching 14,000 at a time. Tugidak Island is also a major pupping area for harbor seals in the Gulf of Alaska with annual production once estimated at a high of 5,500 pups. That population is now substantially depressed but remains one of the largest known. Seals haul, pup, and molt on beaches found along the west and northeast side of the island and in the vicinity of the mouth of the lagoon.

Sea otters are common in the nearshore waters around Tugidak Island. Approximately 400 to 700 sea otters are found in the vicinity of Tugidak Island, with medium to high densities along the south side of the island.

Birds: The interspersed of many different habitat types on Tugidak Island associated with cliff and bluff shores; sand and rocky beaches; spits, bars and tideflats; freshwater streams and lakes; saltwater marshes and lagoons; vast eelgrass beds; freshwater wetlands; and uplands attracts some of the greatest diversity of bird life known to nest on and visit any one island in the Gulf of Alaska.

The island serves as a valuable spring and fall resting and feeding area and as a production area for birds migrating from the Pacific coast of North America. Because Tugidak Island is low, treeless, and free of introduced predators, all birds nest on the ground and are particularly susceptible to habitat destruction, predation, and trampling.

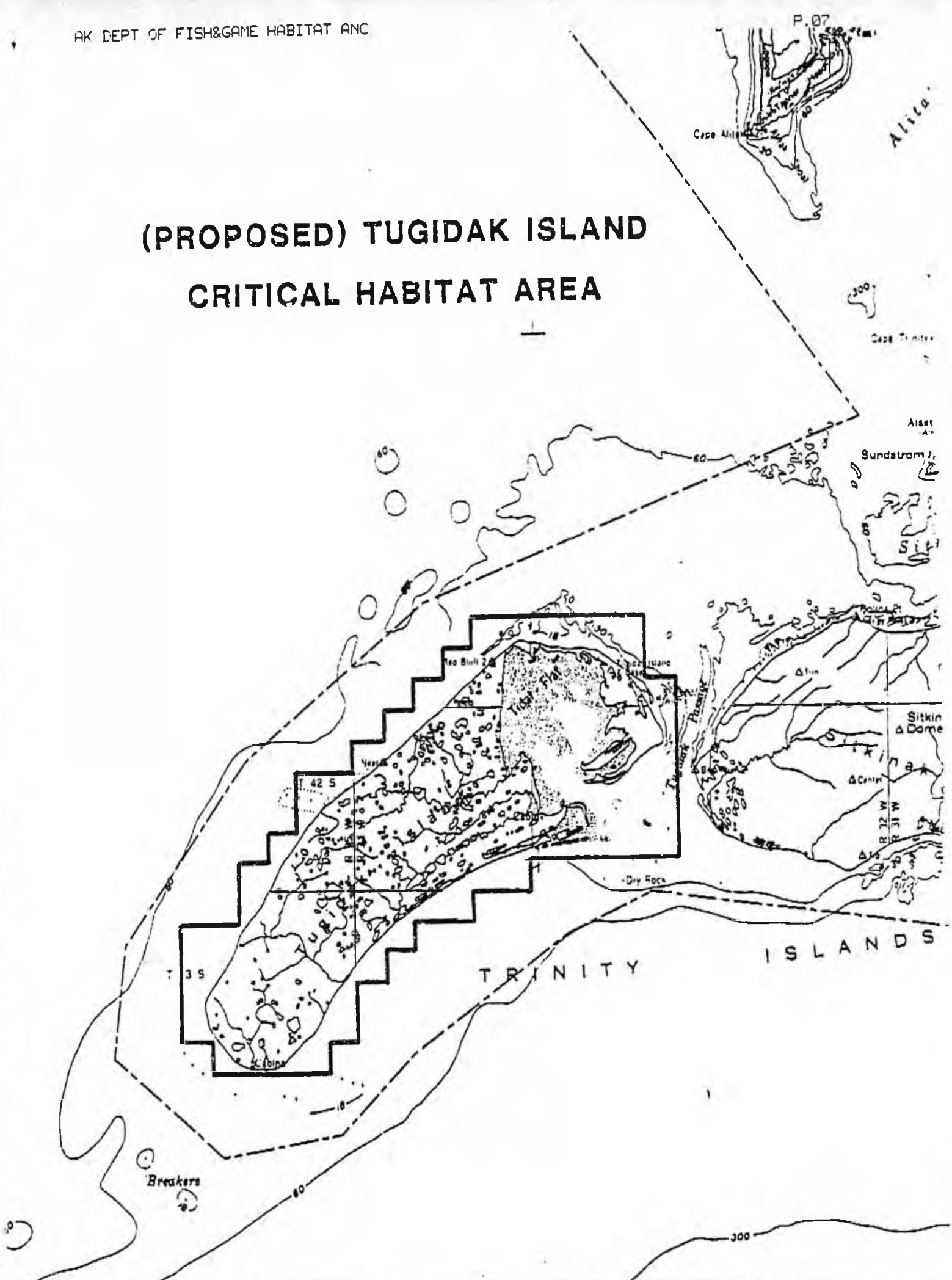
- ° At least 56 species of birds occur on Tugidak Island. Thirty eight species are known to nest there, and 26 of these species are considered common or abundant.
- ° Wetland habitats throughout the island provide nesting habitat for waterfowl, shorebirds, tundra swans and loons, with wetlands habitats along the south shore supporting nesting concentrations of mallards, pintails, gadwalls, green-winged teal and wigeon.
- ° Snow geese concentrate on the island during spring migration to rest and feed.
- ° The lagoon supports spring and fall concentrations of ducks and shorebirds. Black brant and white-fronted geese also concentrate in the lagoon in the fall to rest and feed. The lagoon area provides winter habitat for emperor geese, a species that has recently experienced a serious population decline.
- ° The coastal waters surrounding Tugidak Island are a major overwintering area for waterbirds, primarily seaducks.
- ° Five seabird colonies are documented on Tugidak Island, totally nearly 4,000 nesting birds. Glaucous-winged gulls are the most abundant seabird, followed by arctic terns, mew gulls, and cormorants.
- ° Of particular significance are records of six ground nesting bald eagles. These bald eagle nests are located on bluffs or slight rises in the terrain throughout the island.
- ° Peregrine falcons are also reported to nest on the island's bluffs.
- ° Several thousand ptarmigan nest in upland areas of the island.

Fish and Shellfish: The lagoon and nearshore waters of Tugidak provide a productive marine environment for several species of fish and shellfish. The island's stream systems provide habitat for anadromous fish.

- ° There are three documented salmon stream systems on the island supporting chum and/or coho salmon.
- ° The lagoon is a productive rearing and feeding area for large numbers of Pacific herring.
- ° Known razor clam concentrations occur along the bars at the mouth of the lagoon.
- ° Based upon frequent observations of small Dungeness crab carapaces and exoskeletons washed up along the lagoon's shores and large commercial catches of Dungeness crab directly offshore of the lagoon, the shallow waters and large eelgrass beds found in the lagoon are thought to provide an important nursery rearing area for Dungeness crab.

Archaeological Sites: Eight archaeological sites have been documented on the island. Although largely unexplored, they appear to indicate abundant prehistoric use of the island, with a majority of the sites located along the lagoon.

# (PROPOSED) TUGIDAK ISLAND CRITICAL HABITAT AREA





STATE OF ALASKA  
OFFICE OF THE GOVERNOR

BILL ANALYSIS

DEPARTMENT Fish and Game	DIVISION Habitat	BILL NUMBER SB475	SPONSOR Zharoff
SHORT TITLE OF BILL Tugidak Island Critical Habitat Area			
DEPARTMENT POSITION Support			
PREPARED BY Bruce Baker, Hab. Actg. Dir.	DATE 2/26/88	COMMISSIONER'S SIGNATURE 	DATE

SUMMARY

OTHER AGENCIES AFFECTED BY BILL Department of Natural Resources	CONSTITUENT GROUPS AFFECTED BY BILL Hunting and fishing groups, recreationalists Kodiak area residents
ORGANIZATIONAL SUPPORT FOR BILL Commercial fishing interests Environmental organizations	ORGANIZATIONAL OPPOSITION TO BILL None known

FISCAL IMPACT:  NONE  FISCAL NOTE ATTACHED

BACKGROUND/LEGISLATIVE INTENT  
The purpose of establishing Tugidak Island Critical Habitat Area is to provide:

1. Protection and enhancement for fish and wildlife habitat and populations.
2. Continued opportunity for hunting and fishing.
3. Public use and enjoyment of the area in a high quality environment.

ANALYSIS OF BILL/PROGRAM EFFECTS

1. Establishes Tugidak Island Critical Habitat Area.
2. Identifies the purpose for which the area is established.
3. Provides for the management of Tugidak Island Critical Habitat Area including development of a management plan.
4. Allows existing cabins to remain.
5. Allows present subsistence, recreational and commercial activities to continue in a manner compatible with the establishment of the critical habitat area.

AMENDMENTS PROPOSED

The purpose statement should appear in statute, therefore, it should have a statute number, probably AS 16.20.610(b).

AS 16.20.610(a) should be amended to exclude Sections 12, 13, and 24 of Township 42 South, Range 33 West, Seward Meridian. Portions of these sections include the southern tip of Sitkinak Island.

PLEASE ATTACH A SEPARATE SHEET FOR ADDITIONAL COMMENTS OR ANALYSIS.

FISCAL NOTE

REQUEST:

Revision Date: \_\_\_\_\_  
Title: Tugidak Island Critical  
Habitat Area  
Sponsor: Zharoff  
Requestor: \_\_\_\_\_

Agency Affected: Dept. of Fish and Game  
BRU: Habitat  
Components: \_\_\_\_\_

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 88	FY 89	FY 90	FY 91	FY 92	FY 93
PERSONAL SERVICES			62.8			
TRAVEL			2.0			
CONTRACTUAL			7.7			
SUPPLIES			2.0			
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING			74.5			
CAPITAL						
REVENUE						

FUNDING: (Thousands of Dollars)

GENERAL FUND			74.5			
FEDERAL FUNDS						
OTHER						
TOTAL			74.5			

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

Preparation of the Tugidak Island Critical Habitat Area Management Plan.

Prepared by: Bruce H. Baker, Acting Director Phone: 465-4105  
Division: Habitat Date: 2/26/88

Approved by Commissioner: [Signature] Date: 3/23/88  
Agency: Department of Fish and Game

Distribution (by preparer): \*Amount required only if two plans are prepared con-  
Legislative Finance currently. If the existing schedule of one plan per year  
Legislative Sponsor is adhered to, the operating budget would be adequate  
Requestor and this fiscal note would not be necessary.  
Office of Management and Budget  
Impacted Agency(ies)

## Tugidak Island Critical Habitat Area

-Preparation of the Tugidak Island Critical Habitat Area Management Plan will take one year to complete and require the following expenses (in thousands):

### Personnel

Habitat Biologist	(18c)	10 months	4.5/month	45.0
Game Biologist	(16c)	3 months	4.0/month	12.0
Drafting Tech.	(14d)	1 month	3.5/month	3.5
Clerk/Typist	( 8a)	1 month	2.3/month	2.3
				<u>\$62.8</u>

### Travel

staff travel to Kodiak				2.0
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### Contractual

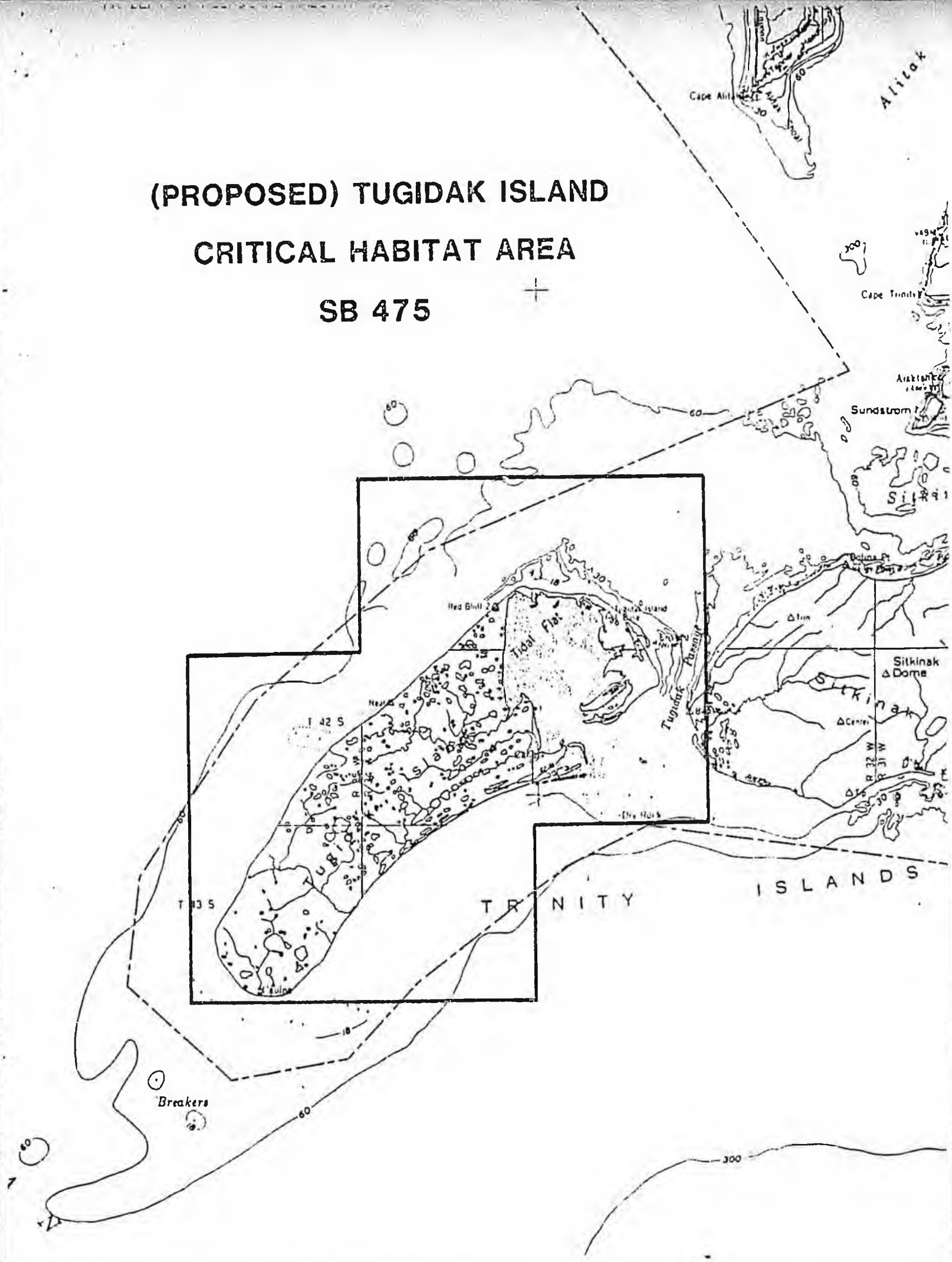
telephone		75/month x 12 months		0.9
photocopy		10/month x 12 months		0.1
advertising /public notices				1.0
aerial photography				0.7
printing/ photographic/ blueprinting				5.0
				<u>\$ 7.7</u>

### Supplies

office supplies				2.0
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TOTAL				\$74.5
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**(PROPOSED) TUGIDAK ISLAND  
CRITICAL HABITAT AREA  
SB 475**



# STATE OF ALASKA

## DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

STEVE COWPER, GOVERNOR

400 WILLOUGHBY AVE.  
JUNEAU, ALASKA 99801-1796  
PHONE: (907) 465-2400

April 11, 1988

Senator Jack Coghill  
Chairman Senate Resources Committee  
Alaska State Senate  
P.O. Box V  
Juneau, Alaska

99811

Re: SB 475 Tugidak Island Critical Habitat Area

Dear Senator Coghill;

Position: The Department of Natural Resources is not opposed to the protection of critical habitat on Tugidak Island, and recognizes that critical habitat values exist there. However, the Department believes that legislative designation should follow from the planning process. Work on the Kodiak Island area plan is scheduled to begin this summer.

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I appreciate the opportunity to comment on this legislation and am happy to make my staff available to work with the committee as it moves through the legislature.

Sincerely,

*Jennie Jones*

Judith M. Brady

*for* Commissioner of Natural Resources

cc

Committee Members

Sponsor

Governor's office

FISCAL NOTE

REQUEST:

Revision Date: 2/15/88  
Title: An Act establishing the Tugidak Island critical habitat area.  
Sponsor: Zharoff  
Requestor: Seante Resources

Agency Affected: DNR  
BRU: Land & Water Management  
Components: \_\_\_\_\_

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 88	FY 89	FY 90	FY 91	FY 92	FY 93
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING						
CAPITAL	0	0	0	0	0	0
REVENUE	0	0	0	0	0	0

FUNDING: (Thousands of Dollars)

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

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS : (Attach a separate page if necessary)

The Department of Natural Resources anticipates no fiscal impact with respect to this legislation.

Prepared by: Lawrence Z. Ostrovsky Phone: 465-2400  
Division: Commissioner Office Date: 4/11/88  
Approved by Commissioner Judith M. Brady Date: 4/11/88  
Agency: Department of Natrual Resources

Distribution (by preparer):

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



**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:** Rep. Adelheid Herrmann  
Co-Chair  
House Resources Committee

**FROM:** Senator Fred F. Zharoff

**DATE:** May 3, 1988

**RE:** CS For Senate Bill 475 - "An Act establishing the Tugidak Island Critical Habitat Area; and providing for an effective date."

I respectfully request that CSSB 475 be scheduled for a hearing before the House Resources Committee at the committee's earliest convenience. The bill passed the Senate on May 3 by a vote of 14-0, and, upon reconsideration, 20-0.

SB 475 creates the Tugidak Island Critical Island Critical Habitat Area. Tugidak Island is an 84,480 acre island approximately 16 miles southwest of Kodiak Island. It is state-owned land within the Kodiak Island Borough. The island features exceptional wildlife and habitat values. Under critical habitat area status, these values would be protected.

I have attached the following background information for SB 475:

1. Description of the proposed Tugidak Island Critical Habitat Area and map, prepared by the Division of Habitat in the Department of Fish and Game.
2. Department of Fish and Game bill analysis and fiscal note. The fiscal note was zeroed out in the Senate Finance Committee. The committee's intent was that the department should adhere to its existing schedule of one plan per year.
3. Department of Natural Resources position paper and fiscal note. The amendments suggested by the department were adopted.
4. Letters of support.
5. Map showing Tugidak Island in relation to Kodiak Island.
6. Letter from the U.S. Fish and Wildlife Service containing background information on Tugidak Island habitat.
7. Map of mining claims on Tugidak Island.

KODIAK AUDUBON SOCIETY  
BOX 1756  
KODIAK, ALASKA 99615

February 29, 1988

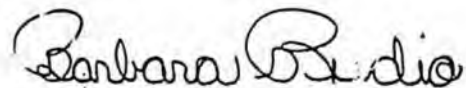
Fred F. Zharoff  
P.O. Box V  
Juneau AK 99811

Dear Senator Zharoff:

The Kodiak Chapter, National Audubon Society, would like reinforce our support for Senate Bill #475, "An Act establishing the Tugidak Island Critical Habitat Area."

Tugidak Island is a unique and special place. Ensuring the protection and enhancement of its fish and wildlife habitat and populations is extremely important to the nearly 100 members of the Audubon Society in Kodiak.

Thank you for introducing the bill. Your continued support of the Tugidak Island Critical Habitat Area will be greatly appreciated.

  
Barbara Rudio  
Conservation Chairman  
Kodiak Audubon Society

April

March 28, 1988

Dear Senator Zharoff,

Thank you for the introduction and support of SB 475 concerning critical habitat status for Igloodak Island.

Being such a lovely unspoiled area of the Kodiak Archipelago, I would be terribly disappointed to see it opened to mass mining or other destructive activities. With critical habitat status, I feel the general integrity of the land would be protected through careful monitoring. I appreciate being able to leave unspoiled land for future generations to enjoy too.

Sincerely,

Susan S. Blott

Susan S. Blott

P.O. Box 1244

Kodiak, AK 99615

KODIAK AUDUBON SOCIETY  
BOX 1756  
KODIAK, ALASKA 99615

February 29, 1988

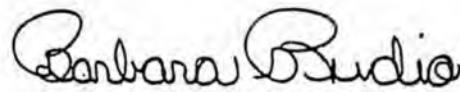
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