

ALASKA

LEGISLATURE

COMMITTEE

FILES

1987-1988

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Statements of Operations

Year Ended December 31,

1984 1983

Interest Income:

Interest on loans	\$ 11,992,708	\$ 13,914,312
Interest on operating reserve	918,081	751,779
	<u>12,910,789</u>	<u>14,666,091</u>
Interest expense	<u>8,386,607</u>	<u>7,234,370</u>
	4,524,182	7,431,721
Provision for loan losses	11,241,619	3,890,135
	<u>(6,717,437)</u>	<u>3,541,586</u>

Other Expenses:

Salaries and benefits	1,785,281	1,707,350
Occupancy expense	260,544	266,825
Office operations	201,133	160,555
Advertising and promotion	197,182	181,911
Travel, lodging and meals	192,661	186,241
Depreciation and amortization	180,127	170,132
Professional fees	148,654	302,822
Telephone and postage	114,774	114,493
Loss on assets held for resale	72,356	
Directors' fees	71,113	88,091
Miscellaneous	30,514	53,693
	<u>3,260,339</u>	<u>3,232,113</u>
Allocated undistributed patronage earnings		
(unallocated undistributed patronage loss)	<u>\$ (9,977,776)</u>	<u>\$ 309,473</u>

See notes to financial statements

Statements of Changes in Capital and Allocated, Unallocated Undistributed Patronage Earnings (Loss)

	Share Capital	Class B Preferred Stock Assessment	Capital In Excess Of Par Value	Contributed Capital	Allocated Undistributed Patronage Earnings	Unallocated Undistributed Patronage Loss	Total
Balance, January 1, 1983	\$31,805,640	\$ -	\$ 49,950	\$ 144,626	\$ 4,570,546	\$ -	\$ 36,570,762
Issuance of stock during the year:							
Class B stock, 27,349 shares, net	2,734,900						2,734,900
Class A stock, 264 shares	2,640		23,760				26,400
Loans receivable on Class B preferred stock issued	(2,734,900)						(2,734,900)
Class B preferred stock assessments		86					86
Less: Assessments receivable		(86)					(86)
Dividends payable					(42,260)		(42,260)
Loan principal charged against allocated undistributed patronage					(72,841)		(72,841)
Unallocated undistributed patronage earnings					309,473		309,473
Balance, December 31, 1983	31,808,280		73,710	144,626	4,764,918		36,791,534
Issuance (redemption) of stock during the year:							
Class B stock, 8,655 shares, net	(865,500)						(865,500)
Class A stock, 60 shares	600		5,400				6,000
Reduction in loans receivable on Class B preferred stock redemption	865,500						865,500
Class B preferred stock assessments		89,507					89,507
Less: Assessments receivable		(79,247)					(79,247)
Loan principal charged against allocated undistributed patronage					(250,681)		(250,681)
Unallocated undistributed patronage loss						(9,977,776)	(9,977,776)
Balance, December 31, 1984	<u>\$31,808,880</u>	<u>\$10,260</u>	<u>\$79,110</u>	<u>\$144,626</u>	<u>\$4,514,237</u>	<u>\$(9,977,776)</u>	<u>\$26,579,337</u>

See notes to financial statements

Statements of Changes in Financial Position

Year Ended December 31,

1984

1983

Source of Funds:

From Operations —		
Allocated undistributed patronage earnings		
(unallocated undistributed patronage loss)	\$ (9,977,776)	\$ 309,473
Items not requiring the use of funds:		
Depreciation and amortization	180,127	170,132
Provision for loan loss	11,241,619	3,890,135
Gain on sale of assets		(8,976)
Funds provided from operations	1,443,970	4,360,764
Net proceeds from sale of assets		256,248
Net proceeds from stock issuance	6,000	2,761,300
Decrease In —		
Cash	568,945	
Loans, net	8,800,349	
Accrued interest receivable	2,634,426	
Increase In —		
Accrued interest payable	244,769	319,806
Notes payable	1,167,917	28,725,892
Class B preferred stock assessments, net	10,260	
	<u>\$ 14,876,636</u>	<u>\$ 36,424,010</u>

Use of Funds:

Loans charged off, net of recoveries	\$ 10,063,534	\$ 1,750,599
Loan principal charged against		
allocated undistributed patronage earnings	250,681	72,841
Patronage dividends paid payable		42,200
Increase In —		
Cash		241,860
Operating reserve	827,865	
Investment in Spokane Bank for Cooperatives	1,030,091	1,328,193
Loans		30,033,366
Accrued interest receivable		1,774,137
Bank premises, furniture and equipment	106,400	236,940
Acquired assets held for resale	2,148,813	
Other assets	275,644	150,501
Decrease In —		
Accounts payable and accrued expenses	2,270	184,193
Spokane Bank for Cooperatives participation payable	129,678	90,509
Patronage dividend payable	42,200	509,611
	<u>\$ 14,876,636</u>	<u>\$ 36,424,010</u>

See notes to financial statements

Note A — Summary of Significant Accounting Policies:

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

CFAB is a cooperative corporation and intends to refund any allocated undistributed patronage earnings at such time as the Board of Directors finds that the financial condition of CFAB will so permit.

Operating Reserves and Income: Board designated operating reserve investments in short-term instruments are stated at cost, which approximates market.

Interest on Loans: The accrual of income on loans is discontinued when interest or principal is contractually past due more than 90 days (See Note L).

Patronage Dividends: Patronage dividends received from Spokane Bank for Cooperatives (SBC), of which CFAB is a member, are shown as a reduction of interest expense to SBC in the year in which those dividends are declared by SBC.

Allowance for Loan Losses: Additions to the allowance for loan losses are provided from charges to income based on management's evaluation of the loan portfolio under existing economic conditions.

Acquired Assets Held for Resale: Acquired assets held for resale are valued at the lower of fair market value or the recorded investment in the related loan. Holding costs are expensed when incurred unless such costs increase the fair market value of the asset.

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

Organization Costs: Certain costs related to the feasibility, capital needs and incorporation phases of CFAB had been

deferred and were being amortized over 60 months. At December 31, 1984 all costs had been amortized. Such costs consisted of legal and advisory fees.

Income Taxes: Amounts provided for income tax expense are based on earnings reported for financial statement purposes, rather than on the taxable income shown on the corporate income tax return. These amounts may differ because certain items are recorded as income or expense in different years for financial statement and tax return purposes.

CFAB uses the flow-through method of accounting for investment tax credits, which results in a reduction of income taxes in the year credits are utilized.

Reclassifications: Certain reclassifications have been made to the 1983 financial statements to conform with the classifications used in 1984.

Note B — Income Taxes:

Income tax expense consists of the following for the year ended December 31, 1985:

Income tax expense calculated	
at statutory rates	\$122,108
Tax effect of:	
Distribution of allocated	
patronage earnings	(100,308)
Investment tax credit	(21,800)
	<u>\$ -</u>

There was no income tax benefit from the unallocated undistributed patronage loss for the year ended December 31, 1984.

Note C — Related Party Transactions:

In the ordinary course of business, CFAB makes loans to members who serve on CFAB's Board of Directors. Loans to members who serve on the Board of Directors must be approved by the SBC. Total loans to these members at December 31, 1984 and 1983 were \$3,182,794 and \$6,234,394, respectively.

Note D — Loans:

The following represents a classification of CFAB's loan portfolio by major category:

	December 31,	
	1984	1983
Vessels	\$46,450,679	\$50,520,974
Fish processors	29,506,571	30,248,447
Agriculture and timber	19,110,057	24,421,884
Gear, entry permits, and other	9,257,056	8,798,907
	<u>104,324,363</u>	<u>113,990,212</u>
Less: Loans receivable on Class B preferred stock	(9,517,700)	(10,383,200)
	94,806,663	103,607,012
Less: Allowance for loan losses	(5,317,621)	(4,139,536)
	<u>\$89,489,042</u>	<u>\$99,467,476</u>

As this is only the fifth year of lending activity for CFAB, loan loss experience has been limited and no similar lending institution exists on which to base an allowance for expected loan losses. Management has established the allowance for loan losses based on a specific provision for loans identified as a potential loss. Additionally, management has included an allowance of 1.5% for loans not specifically identified as a potential loss. A summary of the activity in the allowance for loan losses is as follows:

	December 31,	
	1984	1983
Balance at beginning of year	\$4,139,536	\$2,000,000
Charge to expense	11,241,619	3,890,135
Recoveries on loans previously charged off	470,093	107,539
	15,851,248	5,997,674
Loans charged off	(10,533,627)	(1,858,138)
Balance at end of year	<u>\$ 5,317,621</u>	<u>\$ 4,139,536</u>

The following represents a classification of CFAB's nonaccrual loans by major category:

	December 31,	
	1984	1983
Fish processors	\$15,069,775	\$2,913,520
Timber	8,934,494	
Vessels and other fishing related activity	7,975,177	3,440,990
	<u>\$31,979,446</u>	<u>\$ 6,354,510</u>

If interest on these loans had been accrued, such income would have approximated \$4,380,000 for 1984.

Nonperforming loans, but not in the opinion of management considered to be nonaccrual loans, totaled \$1,487,920.

CFAB serves the financial needs of the commercial fishing and agricultural industries in the State of Alaska. These industries are subject to seasonal and cyclical fluctuations which could effect the borrowers' ability to repay loans on a timely basis.

Note E — Bank Premises, Furniture, and Equipment:

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

	December 31,	
	1984	1983
Furniture, fixtures and equipment	\$ 976,203	\$ 916,083
Leasehold improvements	147,202	125,130
	1,123,405	1,041,213
Less: Accumulated depreciation and amortization	(475,174)	(333,452)
	<u>\$648,231</u>	<u>\$707,761</u>

Note F — Lease Obligations:

CFAB has entered into certain long-term operating lease agreements for buildings and equipment. Rental expense under these leases totaled \$234,076 and \$252,144 for the years ended December 31, 1984 and 1983, respectively. Minimum annual lease payments are as follows:

Year ending December 31,	Amount
1985	\$90,000
1986	35,000
1987	30,000
1988	12,000

Note G — Notes Payable:

Notes payable consisted of the following:

	<u>December 31,</u>	
	1984	1983
Borrowings against lines of credit with Spokane Bank for Cooperatives (SBC); current agreement provides for quarterly interest payments based upon floating rates: Seasonal loan - credit line of \$60,000,000 expiring on March 1, 1985, bearing interest at 11.75% at December 31, 1984	\$ 15,535,000	\$ 49,300,000
SBC matched funds short-term notes with interest rates ranging from 9% to 9.55% maturing at various dates in 1985	35,000,000	
SBC matched funds long-term notes:		
Interest at 10.655%, due July 22, 1985	5,000,000	5,000,000
Interest at 10.544%, due January 20, 1987	5,000,000	5,000,000
Interest at 11.193%, due June 1, 1987	5,000,000	5,000,000
Interest at 10.768%, due September 1, 1987	5,000,000	5,000,000
Interest at 11.28%, due January 20, 1993	5,000,000	5,000,000
Interest at 11.232%, due October 21, 1991	5,000,000	5,000,000
Other notes payable and capitalized equipment leases with various interest rates and maturity dates	39,285	106,368
	<u>\$80,574,285</u>	<u>\$79,406,368</u>

Principal payments required on notes payable are as follows:

<u>Year ending December 31,</u>	<u>Amount</u>
1985	\$55,574,825
1986	
1987	15,000,000
1988	
1989 and beyond	10,000,000

CEAB entered into SBC's matched funding loan program in November, 1982 whereby CEAB may borrow both short-term and long-term funds under its established line of credit at fixed rates of interest, generally providing CEAB with a lower cost of funds.

CEAB must invest in SBC's Class C stock in an amount equal to at least 5% of the cumulative average loan balance maintained with SBC. The amount of CEAB's investment in SBC's Class C stock and equity in allocated surplus was \$4,738,734 and \$3,708,643 at December 31, 1984 and 1983, respectively. The maximum amount due SBC during 1984 was \$94,955,000. These loans are secured by substantially all CEAB assets.

CEAB maintains an unsecured line of credit with a local bank of \$2,000,000. At December 31, 1984 there were no draws outstanding.

Note H — Share Capital:

Shares purchased by the State of Alaska must be repurchased within twenty years by CEAB.

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

Upon issue, the following rights will attach to the three categories of stock:

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

Class B — No voting rights. Class B stock may only be held by members of CEAB, and dividends paid shall not exceed \$10 per share annually. Borrowers must purchase and maintain Class B stock in an amount equal to 10% of their loan proceeds. This amount is added to the loan proceeds in determining the loan balance.

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

Note I — Pension Plans:

CFAB has two pension plans. Benefits for employees were provided through contributions of \$56,881 and \$50,810 in 1984 and 1983, respectively, for the defined contribution plan.

CFAB also has a noncontributory defined benefit plan. Total pension costs for 1984 and 1983 were \$25,855 and \$23,095, respectively. A comparison of accumulated benefits based upon a weighted average rate of return of 8% and plan net assets adjusted for balance sheet accruals as of December 31, 1983 is presented below:

Actuarial present value of	
accumulated plan benefits:	
Vested	\$ 1,617
Nonvested	
	<u>\$ 1,617</u>
Net assets available for benefits	<u>\$12,000</u>

Information with respect to the actuarial computed value of vested benefits and pension fund assets as of December 31, 1984 is not available.

Note J — Class C Stock Repurchase Plan:

In accordance with AS 44.81.010(b), on or before July 18, 2000, CFAB is required to repurchase its Class C stock issued to the State of Alaska. On November 10, 1982 a contract was signed with the State of Alaska outlining the principles of a plan which calls for the repurchase of outstanding Class C stock with CFAB capital funds to be provided by CFAB's member-borrowers over a period of future operations. On December 12, 1983, CFAB implemented its Class C Stock Redemption Program.

Note K — Commitments and Contingent Liabilities:

In the normal course of business, CFAB makes various commitments and incurs certain contingent liabilities. The commitments include obligations to extend credit. At December 31, 1984, outstanding loan commitments aggregated \$12,173,024.

CFAB is a defendant in legal actions arising from normal business activities. Management believes that those actions are without merit or that the ultimate liability, if any, resulting from them will not materially affect CFAB's financial position.

Note L — Accounting Changes:

In 1984 CFAB adopted the policy of reporting loans receivable applicable to Class B preferred stock purchases as a reduction to Class B preferred stock equity. CFAB believes that reporting in this manner more accurately reflects the economic substance of the Class B stock purchases. There is no effect of the change to current or prior years income. The financial statements for the year ended December 31, 1983 have been restated to include the change.

Also, loans contractually past due more than 90 days will no longer be reflected as earning assets. Accrual of interest on non-performing loans in years prior to 1984 was allowed if, in management's opinion, collectibility of such income was assured. The new method of recognizing income was adopted to follow a consistent, conservative approach to accrual of interest income. The effect of the change in 1984 was to decrease interest income by approximately \$2,007,000. There is no material effect on income in the years prior to 1984.

Robert B. Atwood
President and Publisher

Elaine Atwood
Assistant Publisher

William J. Tobin
Vice President, Editor-in-Chief

Missing the benefits

THE MESSAGE is sharp and clear when Jim Campbell, chairman of the North Pacific Fishery Management Council, talks about bottom fishing in Alaska.

He says Alaskans "are doing a good job of promotion but we are falling on our face when it comes to reaping the benefits."

In the past 10 years, bottom fishing has grown from a production of 1,000 tons a year to a projected two million tons in 1987. That reflects the action of the council last December in making the water from three miles to 200 miles offshore an exclusive fishing area for American fishermen.

The growth has been phenomenal, with investments surging as world markets showed a need for more and more bottom fish. American fishermen were skeptical about the new fishery in the beginning, but they have gone all out for it recently.

Under the council's new rules, the Americans will catch 94 per cent of all the fish in that exclusive zone.

THE DISMAYING part of the development is the fact that 53 percent of the individuals in the fish business receive no dividend checks from the state. They are non-residents who come north for the quick buck and head back home as soon as they get it.

Campbell said estimates show that 1986 gross ex-vessel revenue from bottom fishing in 1986 was \$300 million. Of this, only \$40 million went to Alaska fishermen.

It is equally disturbing that the shoreside processors, mostly in Kodiak, Akutan and Dutch Harbor, took

only 3 percent of the total value of landings of groundfish off Alaska. This estimate was exclusive of \$62 million in halibut landings, the majority of which was landed in Alaska.

These figures show anew the fact that Alaska's biggest industry in point of employment is one of the worst offenders in its failure to hire Alaskans and in its patronizing of local processors.

THE REMEDY suggested by the council chairman requires cooperation:

He said the state should take a position of leadership in bringing it about. The combined efforts, concern and talents of state government and private enterprise, along with active participation by the university and the federal government, must plan it together.

The plan must resolve questions involving the factors that limit development efforts, stem from limited entry law and allocations. There is need for diversification to include provisions for pen-reared salmon, improved service support, transportation and marketing.

Probably the most surprising disclosure in Campbell's report, which he made to the Chamber of Commerce, was that Gov. Steve Cowper has told fishing interests that the state has no policy in regard to development, and will not have one for at least a year and a half.

This is a shocking disclosure. Fisheries are too important to too many Alaskans as well as the markets of the world to wait a year and a half for the state to develop a policy.

ALASKA STATE LEGISLATURE · SENATE

SENATOR RICHARD I. ELIASON

RULES COMMITTEE, CHAIRMAN
LABOR & COMMERCE COMMITTEE, VICE-CHAIRMAN
LEGISLATIVE COUNCIL
RESOURCES COMMITTEE
FISHERIES SUBCOMMITTEE, CHAIRMAN



P O BOX 143
SITKA, ALASKA 99835
P O BOX V
JUNEAU, ALASKA 99811
(907) 465-4916

M E M O R A N D U M

TO: Senator Jack Coghill, Chair
Senate Resources Committee

FROM: Senate Resources Fisheries Subcommittee

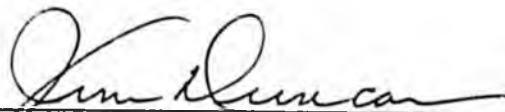
DATE: March 20, 1987

RE: S.B. 8 and S.B. 9 -- legislation relating to the
Commercial Fish and Agriculture Bank (CFAB)

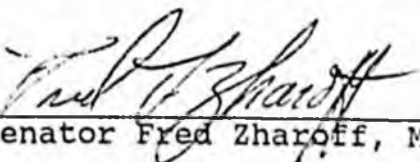
The fisheries subcommittee reports back the above mentioned legislation to the Senate Resources Committee and recommends that S.B. 8 and S.B. 9 be considered by the Committee as soon as possible.



Senator Dick Eliason, Chair



Senator Jim Duncan, Member



Senator Fred Zharoff, Member

SENATE COMMITTEE REPORT

FURTHER:

FINANCE

3/16/87

DATE TURNED INTO OFFICE _____

Mr. President:

RESOURCES _____ Committee considered _____ SB 8

Commercial Fishing and Agricultural Bank.

and recommended:

replace with CS FOR SB 8 Resources) [] same title
[] or adopt _____ CS FOR _____) new title

[] attached amendment(s) and

do pass

[] do not pass

[] no recommendation

[] individual recommendations

[] further referral to _____

[] letter of intent adopted _____

Committee attached or [] adopted fiscal note(s)

[] new [] updated or [] previous

zero [] fiscal impact

MEMBERS SIGNING DO PASS

OTHER RECOMMENDATIONS

Al Glason
Cedric Sturgulinski
James ...
Paul ...
Lloyd ...

[Signature]
Chairman signature and recommendation

[] Committee Backup Attached

A PERFORMANCE REVIEW
OF THE
ALASKA COMMERCIAL FISHING
AND AGRICULTURE BANK

May 22, 1981

Audit Control Number
04-101-1035-S

Board of Directors of the:
ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK

Chairperson
Vice Chairperson
Secretary/Treasurer
Member
Member
Member
Member

Roseleen Moore
Paul Huppert
Bob Waldrop
Dale Pihlman
Harvey Samuelsen
William Sutton
Frank Homan

STATE OF ALASKA

AUDIT DIVISION:
POUCH W—ALASKA OFFICE BUILDING

THE LEGISLATURE

BUDGET AND AUDIT COMMITTEE

JUNEAU, ALASKA 99811

May 22, 1981

Members of the
Legislative Budget and Audit Committee:

In accordance with the provisions of Title 24 of the Alaska Statutes, the attached report is submitted for your review.

A PERFORMANCE REVIEW
OF THE
ALASKA COMMERCIAL FISHING
AND AGRICULTURE BANK

May 22, 1981



Gerald L. Wilkerson, CPA
Legislative Auditor
Division of Legislative Audit

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PURPOSE AND SCOPE OF THE REVIEW

The purpose of our review was to determine if the performance of the Alaska Commercial Fishing and Agriculture Bank (CFAB) is efficient, effective, and economical. Our scope included a review of the Board of Directors' proceedings, operating expenditures, and the loan portfolio. CFAB's financial statements for the year ended December 31, 1980 were audited by a certified public accounting firm.

ORGANIZATION AND FUNCTION

The Alaska Commercial Fishing and Agriculture Bank (CFAB) was created by Chapter 159, SLA 1978 (AS 44.81.010) as a public corporation and government instrumentality of the State, but with a legal existence independent of and separate from the State. Its purpose is to provide financing for the commercial fishing and agricultural industries in Alaska.

In Fiscal Year 1979, the Commissioner of the Department of Revenue purchased \$2,000,000 (200 shares) of special preferred class C stock in accordance with AS 44.81.010(c). Then in March 1980, the Department of Revenue loaned CFAB \$30,000,000 at 9 1/2% per annum. In July 1980, the loan agreements were cancelled through the issuance of an additional 3,000 shares of class C stock to the State and the payment of interest from March 1980, totalling \$480,205. The class C stock receives no voting or dividend rights. CFAB must repurchase the class C stock from the State within 20 years.

CFAB made 136 loans from April 2, 1980 through March 13, 1981. As of March 13, 1981, there were 130 outstanding loans, totalling \$24,287,687 (see Appendix A).

FINDINGS AND RECOMMENDATIONS

Recommendation No. 1

CFAB should require that inventories used as collateral be insured, naming CFAB as the loss payee.

CFAB has developed procedural manuals for the processing and accounting of loans and for collateral control. These manuals are well written and are useful management tools.

We reviewed 67 (49%) of the 136 loans made from April 1980 through March 13, 1981. The loan files, in general, were well organized and contained required information. However, we did note an area of weakness in collateral control that needs to be addressed.

Our test included eight loans for which CFAB has a secured interest in the inventories as collateral for the loan advances. Five of these loans did not have insurance on the inventories, naming CFAB as the loss payee.

CFAB could lose its security on the loan advances through spoilage, accident, fire, etc. Therefore, CFAB should require that insurance be obtained by the borrower, naming it as the loss payee, on inventories in transit and inventories not held in bonded warehouses.

Recommendation No. 2

CFAB should compensate members of the Board of Directors for travel expenses in compliance with Alaska Statutes.

CFAB reimburses members of the Board for actual travel expenses rather than a fixed per diem rate established by the Commissioner of Administration. During Fiscal Year 1980, Board members were reimbursed for \$33,807 in actual travel expenses.

AS 44.81.110 states the Board members are to receive compensation at a rate determined by the Board for each day the Board meets if they attend the meeting. In addition, they are entitled to per diem and travel allowances as provided by law for members of State boards and commissions. AS 39.20.180(2) states the members of boards and commissions are entitled, for expenses other than transportation, to a per diem allowance prescribed by the Commissioner of Administration.

Recommendation No. 3

CFAB should give public notice of its Board and membership meetings in accordance with Alaska Statutes.

CFAB has not given public notice of the dates and places of its Board and membership meetings.

A memorandum dated May 13, 1981 from the office of the Attorney General states the Open Meetings Act (AS 44.62.310 - 44.62.312) is applicable to CFAB. AS 44.62.310(e) requires reasonable public notice be given for all meetings required to be open under the Act. Since action taken at meetings held contrary to the Act may be void, it would be prudent of CFAB to comply with the public notice requirement for future meetings.

Other Information

This section of the report addresses the results of our review of CFAB expenditures from inception through April 30, 1981. We have included this information because a significant number of the expenditures may be inappropriate for an entity subsidized by public funds.

Throughout the audit CFAB management has maintained it is a private cooperative entity. They believe they are responsible only to their members, each of whom has purchased a single share of class A common stock for \$100, and class B common stock in an amount equal to ten percent of the member's loans (the amount necessary to purchase the B stock is added to the loan amount requested, deducted from loan proceeds by CFAB at closing, and capitalized.)

CFAB is primarily capitalized through a purchase of nonvoting class C stock by the State of Alaska. Paid-in capital at April 30, 1981 is shown as follows on CFAB financial statements:

Class A Common Stock	\$ 1,770
Class B Common Stock	2,534,900
Class C Common Stock	32,000,000
Capital in Excess of Par Value	<u>15,300</u>
<u>Total Paid-In Capital</u>	<u>\$34,551,970</u>

Each Alaskan has an interest in the manner in which public funds are spent. CFAB has been given a specific mission by the Legislature; that of enhancing commercial fishing and agricultural activities in Alaska. They have been provided with the authority and the wherewithal to accomplish this mission.

As an entity that receives a large State subsidy, we believe it is incumbent upon CFAB management to exercise a higher degree of prudence with their spending habits than if they were completely privately funded.

The following items represent a sampling of CFAB expenditures from inception through April 30, 1981, some of which are questionable:

A. Furniture, Fixtures, and Leasehold Improvements

The balance of CFAB's furniture and fixtures account as of December 31, 1980, CFAB's fiscal year end, totalled \$313,966. Of this amount, \$246,835 was for expenditures for the Anchorage office. The total expended for leasehold improvements as of the same date was \$65,850, which was for purchases of carpet, wallpaper, etc. The following is an example of the type of furnishings purchased for the Anchorage office.

1. President's Office

Sofa	\$ 3,631
Five swivel upholstered chairs	7,717
Teak bookcase/cabinet units with refrigerator and liquor cabinet	4,232

2. Executive Assistant's Office

Natural oak desk	\$ 2,302
Natural oak credenza	3,150

3. Senior Vice-Presidents' Offices

Two teak executive desks	\$ 2,903
Two teak coffee tables	1,812
Two teak bookcase/cabinet units	5,453

4. Executive Conference Room

Rosewood conference table	\$16,225
Conference chairs (14)	10,470
Soapstone carving of a land otter with a crab	2,000

In addition, CFAB maintains an apartment in Juneau for which \$4,218 in furnishings were purchased, such as two beds, dresser, color television, dinette set, desk, etc. Leasehold improvements were made totalling approximately \$2,254, including new carpet and wallpaper.

B. Art Work

As of December 31, 1980, the balance of the non-depreciable assets account totalled \$13,353. This represents purchases of prints and paintings for the Anchorage office. A sample of the paintings are:

Custom ordered original paintings by Charlen Jeffery

1. "Brown Bear" watercolor	\$ 3,400
2. "Musk Ox" watercolor	1,750
3. "Cows" watercolor	1,850
4. Six additional watercolors on rice paper, subject matters are fishing and agriculture	2,150
5. "Alaska Fisherman and Farmer"	800
6. "Toast of Alaskan Holiday"	800
7. "Alaskan Logger"	950

C. Automobiles

1. 1980 Chevrolet Citation for a branch office	\$ 7,918
2. 1981 Chevrolet Malibu for a branch office	8,874
3. 1980 Subaru 4x4 Station Wagon for the Anchorage office	7,842
4. 1981 Subaru 4x4 Station Wagon for the Senior Vice-President/ Administration	<u>9,350</u>
<u>Total</u>	<u>\$33,984</u>

In addition to the bank owned vehicles, CFAB pays the \$168 per month lease charge for the President's vehicle. Maintenance and repair costs for the leased and bank owned vehicles totalled \$4,543 during Fiscal Years 1980 and 1981, through April 30. Gasoline expense is paid for the leased vehicle, the bank owned vehicles, and the personal vehicle of the Senior Vice-President/Credit, including gasoline consumed for personal use. The staff employees are reimbursed for the business use of their personal vehicles at a rate of 25 cents per mile.

D. Salaries and Benefits

1. Salaries, Bonuses, and State Benefits

Salary and benefit expenditures totalled \$996,692 for Fiscal Year 1980. Included in this amount was \$108,192 for year-end bonuses. In addition, two CFAB employees received a total of \$1,565 in cash bonuses during the year and \$2,390 was paid directly to a travel agency for a bonus trip to Hong Kong for the Senior Vice-President/ Administration and his spouse.

CFAB is presently accruing \$22,000 to \$24,000 per month for bonus expense. The Fiscal Year 1981 total budgeted bonus accrual is \$282,356.

CFAB officers and employees are in the exempt service of the State personnel system. They are covered by the State insurance and retirement programs. They are also exempted from the Social Security Act, as are other State employees, and instead participate in the State Supplemental Benefit Program. Employer contributions for these benefits are paid from CFAB's operating funds. Officers receive four weeks annual leave and employees receive three weeks. In addition, both officers and employees accrue sick leave at a rate of one day per month.

2. Other Benefits, Fiscal Year 1980

Staff room costs (coffee, hot chocolate, tea, sugar, dish soap, etc.)	\$2,943
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Season tickets to the Alaska Repertory Theatre	\$ 376
--	--------

Staff Christmas party at the Anchorage Westward Hilton:

Food	\$2,353	
Liquor	2,197	
Entertainment	600	
Floral centerpieces	<u>211</u>	
		\$5,361

Turkeys for CFAB officers and employees	\$ 415
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Banquet for a staff meeting at the Sheraton Hotel	\$ 773
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The President, Senior Vice-President/ Administration, a prospective employee and their spouses had dinner at the Captain Cook Hotel in Anchorage.	\$ 245
---	--------

A branch manager and his spouse had two dinners with two CFAB employees at the Mecca Lounge in Kodiak.	\$ 320
--	--------

The total charged to the other employee benefit and the other personnel expense accounts in Fiscal Year 1980 was \$6,076 and \$13,810, respectively.

E. Office Space

The Anchorage office is approximately 7,000 square feet which includes two kitchens each equipped with oak cabinets, microwave oven, dishwasher, and refrigerator. Also, one kitchen has a built-in stove top. CFAB purchased a dinette set for \$1,108 and a natural oak conference table and upholstered chairs for \$4,360 for kitchen/staff room furnishings. In addition, the President's office includes a bathroom with a shower stall.

F. Directors' Fees

In Fiscal Year 1980, \$32,479 was paid to members of CFAB's Board of Directors. Originally in March 1979 the Board set its rate of compensation at \$100 per day during Board meetings in addition to per diem and travel expenses set forth by State law. In April 1979 the Board voted to increase the compensation rate to \$250 per day for the Chairperson and \$200 per day for the members. Again, in February 1980 the rate of compensation was increased to \$500 and \$400 per day for the Chairperson and members, respectively. In addition, CFAB has reimbursed Board members for actual expenses rather than paying a per diem rate, see Recommendation No. 2.

In May 1980 the Board voted to compensate members for work concerning CFAB, other than attendance at meetings, at a rate of \$62 per hour for the Chairperson and \$50 per hour for the members. During the period November 1979 through April 1981, a Board member has been paid \$12,438 for organization and consultation services.

G. Travel, Lodging, and Meals

During a review of Board and staff members' monthly expense reports for the period October 1979 through March 1981, we noted the following:

1. President's Foreign Travel

- a. A European tour, from October 24 through November 17, 1980, to Denmark, England, Rome, and Paris: the purpose of the trip was to tour the Danish fishing industry, visit the British banks and the White Fish Authority, examine the British dairy industry, attend the International Fisheries Conference, and the Fisheries Products Exposition. (Cost includes airfare, totalling \$1,881, for the President's spouse, as well as an undetermined amount for her meals and lodging expense.)

\$8,805

- b. An agriculture tour from January 28 through February 12, 1981, to Denmark, Norway, Sweden, and Finland: (Cost includes International Fisheries Conference fees for the President's spouse and the spouse of the Chairperson of the Board, totalling \$376.) \$6,088
- c. At the November 25, 1980 Board meeting, the President apprised the Board of his tentatively scheduled trips for 1981:
- January - Denmark
(Same as b. above)
Spring or Summer - Japan
October - Munich
2. Senior Vice President/Administration - Foreign Travel
- a. A trip to London, England in January, 1981 \$2,681
3. Dinners
- a. The following dinners were reported on the expense reports of the President and Senior Vice-President/Administration:
- 1) A dinner at the Corsair in Anchorage attended by four CFAB employees and their spouses. \$256
- 2) Three CFAB officers and their spouses had dinner at Simon & Seafort's Saloon & Grill in Anchorage. \$191
- 3) The President and Senior Vice-President/Administration and spouses had dinner with a local businessman and spouse at the Corsair in Anchorage. \$210
- 4) The President, Senior Vice-President/Administration, and a prospective employee had dinner. \$164

5)	Two legislators, CFAB's attorney, and a consultant had dinner in Juneau with the President, Senior Vice-President/Administration and a secretary.	\$213
6)	A dinner at Yancey Derringer's in Juneau with four Board members and the Senior Vice-President/Administration.	\$343
7)	Five members of the Board, the three senior executive officers, the Vice-President/Branch Management, and CFAB's attorney had dinner at Josephine's Restaurant in Anchorage.	\$281
8)	Three dinners at Josephine's Restaurant for the five members of the Board and the Senior Vice-President/Administration.	\$534 400 449
9)	The Senior Vice-President/Administration and the Chairman of the Board had dinner at the Captain Cook Hotel in Anchorage.	\$125
10)	The two Senior Vice-Presidents had dinner at Josephine's Restaurant in Anchorage.	\$157

All told, there were 48 dinners on the expense reports of the President and Senior Vice-President/Administration each costing in excess of \$100 during the period October 1979 through March 1981.

b. Cost of dinners or lunches noted on other persons monthly expense reports:

1)	Branch Manager took Branch Assistant to lunch on five occasions.	\$137
2)	The two Seattle branch office employees and six employees from offices in Alaska dined in Seattle.	\$127
3)	The two Seattle branch office employees and seven employees from the offices in Alaska dined in Seattle.	\$448
4)	Staff lunch at Clinkerdagger, Bickerstaff & Petts Public House in Anchorage.	\$172

c. Banquets held in March 1981 at the Sheraton Hotel in Anchorage. Costs include \$398 for liquor.	\$1,331
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4. Miscellaneous Expenditures

a. Alaska Airlines Board Room, United Airlines Red Carpet and University Club (San Francisco) membership dues on the expense reports of the President or Senior Vice-President/Administration.	\$400
b. Tuxedo rental.	\$40
c. Liquor and mixes for the bar in the President's office.	\$243
d. Glassware and cutlery purchased at Design Craft Ltd. in Anchorage.	\$158
e. Towels and accessories for the executive bathroom purchased at Nordstrom in Anchorage.	\$100
f. Two gift certificates for dinner at Josephine's Restaurant in Anchorage.	\$200
g. Gift certificate at Stephan Fine Arts gallery.	\$100

H. Promotional Costs

1. Anchorage Pre-opening Party at the Sheraton Hotel

64 dinners	\$1,325	
19 bottles Chenin Blanc	186	
18 bottles Pinot Noir	124	
Hosted bar - 283 drink tickets	814	
Flowers	180	
		\$2,629

Meals and lodging for: three members of the Board, two CFAB employees, three business associates, and five spouses.	1,153
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Total Anchorage Costs	3,782
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2. Pre-opening Parties at Branch Offices

a. Kodiak:

Party room rental and permit	\$ 160
Food	450
Bar	621
Gratuity	<u>130</u>
Total food and bar costs	1,361
Air charter for CFAB employees	<u>2,711</u>

Total Kodiak Costs 4,072

b. Cordova:

Elks Club 7,610

c. Homer:

Finger food for 200 persons	\$ 900
Bar	934
Tax	<u>18</u>

Total Homer Costs 1,852

d. Air charter for CFAB employees to Cordova and Homer pre-opening parties.

2,541

e. Seattle (costs are based on an estimate prepared by the Branch Manager):

Invitations	\$ 89
Seafood:	
Crab legs	160
Prawns	90
Caterer	1,100
Liquor and mix	<u>600</u>

Total estimated Seattle Costs 2,039

Total Cost of Pre-opening Parties \$21,896

3.	Legislative Cocktail Party at the Baranof Hotel in Juneau (100 guests)		
	Food	\$1,770	
	Liquor	<u>982</u>	
			\$2,752
4.	Sixty-six Eddie Bauer Gortex mountain parkas with CFAB logo purchased for employees and members of the Board.		\$5,064
5.	Gift packs of Blake's Fancy Smoked Salmon for customers.		\$555
6.	5,750 Dot's Tide Table books printed with CFAB logo for customers.		\$4,573
7.	Cookbooks.		\$1,984
8.	1,000 1980 Annual Reports (ccst includes color setups, slides, printing, design work, etc.)		\$27,466

APPENDIXES

APPENDIX A

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK
SUMMARY SCHEDULE OF LOANS

For the period 04/02/80 - 03/13/81

<u>Purpose of Loan</u>	<u>Total Number of Loans Made</u>	<u>Total Original Amounts</u> (See Notes 1 & 2)	<u>Total Outstanding Balance as of 3/13/81</u> (See Note 3)
Entry Permit Purchase	4	\$ 184,800	\$ 176,600
Entry Permit Refinance	7	217,200	217,200
Used Vessel Purchase	34	3,587,155	3,492,258
New Vessel Purchase	20	3,918,596	1,968,703
Vessel Refinance	35	8,708,721	8,427,605
Vessel Repair	2	40,900	40,900
Gear Purchase	8	443,300	408,339
New or Used Vessel Equipment Purchase	8	327,820	311,615
Miscellaneous Debt Refinance	6	409,877	409,859
Fisherman Working Capital	2	10,750	10,750
Fish Processor Working Capital	<u>10</u>	<u>37,757,000</u>	<u>8,823,857</u>
Totals	<u>136</u>	<u>\$55,606,119</u>	<u>\$24,287,686</u>

See Accompanying Notes to the Summary Schedule of Loans

APPENDIX B

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK
NOTES TO THE SUMMARY SCHEDULE OF LOANS
For the period 04/02/80 - 03/13/81

Note 1

Borrowers are required to purchase CFAB class B stock in an amount equal to 10% of the loan proceeds. The original loan amount listed includes the amount loaned for the purchase of the class B stock.

Note 2

Certain portions of the Fish Processor Working Capital loans are guaranteed by the State of Alaska under the authority of SLA 1980, Chapter 32.

Note 3

On May 14, 1980, CFAB signed a loan agreement with the Spokane Bank for Cooperatives (SBC) which established a line of credit to finance CFAB's current lending activity. As amended on June 18, 1980, CFAB may borrow up to \$30,000,000. The agreement is for a one-year term from June 1, 1980, bearing interest at a floating rate prescribed by SBC. Interest is payable the last day of each quarter. The loan is secured by all CFAB notes evidencing loans to members. The loan agreement is to be renegotiated annually. The outstanding loan balance at March 13, 1981 totalled \$1,000,000.

Further, CFAB is required, in accordance with the Farm Credit Act to purchase SBC class C stock in an amount equal to 15% or a lesser amount prescribed by SBC of the quarterly interest payable. The amount of CFAB's investment in SBC class C stock at March 13, 1981 totalled \$47,784.

APPENDIX C

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK
 SCHEDULE OF LOANS BY BRANCH OFFICE (See Note 1)
 for the Period 04/02/80 - 03/13/81
 (UNAUDITED)

Purpose of Loan	Anchorage			Cordova			Kodiak			Homer		
	Number of Loans Made	Original Loan Amount	Outstanding Balance as of 03/13/81	Number of Loans Made	Original Loan Amount	Outstanding Balance as of 03/13/81	Number of Loans Made	Original Loan Amount	Outstanding Balance as of 03/13/81	Number of Loans Made	Original Loan Amount	Outstanding Balance as of 03/13/81
Entry Permit Purchase	-0-	\$ -0-	\$ -0-	-0-	\$ -0-	\$ -0-	1	\$ 39,600	\$ 39,600	3	\$ 145,200	\$ 137,000
Entry Permit Refinance	2	49,500	49,500	3	74,200	74,200	-0-	-0-	-0-	2	93,500	93,500
Used Vessel Purchase	13	1,974,795	1,890,982	9	461,530	450,446	6	397,330	397,330	6	753,500	753,500
New Vessel Purchase	10	1,756,488	1,279,453	5	399,600	231,844	3	1,592,008	286,905	2	170,500	170,500
Vessel Refinance	15	5,686,750	5,516,936	7	346,510	310,426	4	1,519,450	1,444,306	9	1,156,011	1,155,937
Vessel Repair	1	5,000	5,000	-0-	-0-	-0-	-0-	-0-	-0-	1	35,900	35,900
Gear Purchase	4	277,200	260,506	1	33,000	33,000	-0-	-0-	-0-	3	133,100	114,833
New or Used Vessel Equipment Purchase	2	65,070	64,485	3	89,450	73,368	1	24,200	24,200	2	149,100	149,562
Miscellaneous Debt Refinance	2	165,000	165,000	2	192,227	192,209	-0-	-0-	-0-	2	52,650	52,650
Fisherman Working Capital	1	7,950	7,950	1	2,300	2,800	-0-	-0-	-0-	-0-	-0-	-0-
Fish Processor Working Capital	10	37,757,000	8,823,857	-0-	-0-	-0-	-0-	-0-	-0-	-0-	-0-	-0-
Totals	60	\$47,744,753	\$18,063,669	31	\$1,599,317	\$1,368,293	15	\$3,572,588	\$2,192,342	30	\$2,689,461	\$2,663,382

See Accompanying Notes to the Schedule of Loans by Branch Office.

APPENDIX D

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK
NOTES TO THE SCHEDULE OF LOANS BY BRANCH OFFICE
For the period 04/02/80 - 03/13/81

Note 1

CFAB has two additional branch offices; one in Seattle and another located in Ketchikan. The Seattle office does not process loans. The Ketchikan office opened in November 1980 and as of March 13, 1981 had not made any loans.



2550 Denali Street, Suite 1201
P.O. Box 4-2070
Anchorage, Alaska 99509
(907) 276-2007
SRA 90-B
Homer, Alaska 99603
(907) 235-8234

Roseleen "Snooks" Moore
RECEIVED
August 31 1981
**LEGISLATIVE
AUDIT**

August 27, 1981

Mr. Paul V. Harris, CPA
Anchorage Office Manager
State of Alaska
Division of Legislative Audit
P.O. Box 1231
Anchorage, Alaska 99510

Dear Mr. Harris:

The report entitled, A Performance Review of the Commercial Fishing and Agriculture Bank dated May 22, 1981, to which you have requested our reply, is essentially the same as that submitted to us by the auditors themselves. We are, therefore, submitting our reply to that original submission. It remains applicable with the following modifications.

1. The reference to open board meetings is new to this report, and
2. The auditors have removed references to actions taken by the board of directors.

Since the completion of the audit, legislation has been passed clarifying CFAB's status and its relationship to the State. That legislation causes the majority of points covered in the audit, and indeed, the focus of the audit itself, to be currently moot.

The Board of Directors and the Management of CFAB look forward to working with the Committee in the future.

Sincerely,

Roseleen "Snooks" Moore

sd



2550 Denali Street, Suite 1201
P.O. Box 4-2070
Anchorage, Alaska 99509
(907) 276-2007

June 12, 1981

Mr. Paul V. Harris, CPA
Anchorage Office Manager
State of Alaska
Division of Legislative Audit
P. O. Box 1231
Anchorage, Alaska 99510

Dear Mr. Harris:

It is apparent from your letter that the audit has failed to grasp the mandate given to CFAB by the Legislature. It has also been unable to properly evaluate the complexities and intricacies of operation demanded of a private company operating in the private market. These standards are imposed upon CFAB in order to fulfill the mission spelled out in the enabling legislation.

The fundamental concept of the Alaska Commercial Fishing and Agriculture Bank (CFAB) is that it is a private, cooperatively owned and managed financial institution. This design was mandated by the Legislature for the purpose of linking with the national cooperative banking system to bring outside capital to Alaskan fishermen and farmers. The designers of CFAB recognized that it must be a private corporation in order to qualify for participation in the national system. The Banks for Cooperatives are prohibited by law from affiliating with or lending money to a government organization. If CFAB had not been organized to operate as a private organization, it would not have been able to lend, in 16 short months of operation, over \$30,000,000 to its over 225 member stockholders who are Alaska fishermen and farmers, and over \$50,000,000 to its member stockholders who are processors, as required by the Legislature. Nor could we have provided employment opportunities to Alaskan workers who crew the vessels, till the land, or process Alaska's fish and farm products.

Even in CFAB's short history, it has fulfilled the intent of bringing in outside capital to finance our fishermen, farmers and processors. Today, the commitment of the Banks for Cooperatives far exceeds that of the original State commitment. Additionally, we have increased the net worth of the Cooperative by more than \$4 million during that same short period. We have in excess of \$40 million in pending loan applications and fully expect to exceed \$300 million in loans to fishermen, farmers and processors by the year 1985.

Alaska Commercial Fishing and Agriculture Bank

In testimony before the State Legislature on several occasions, the Spokane Bank for Cooperatives has testified that they have an excellent relationship with CFAB and hold its management and operations in high regard. They have remarked that the progress made by the Cooperative during its brief period of operation has exceeded their expectations for us at the end of five years. In that testimony, they plainly stated that they would not be able to lend to CFAB if we were not a private cooperative. If CFAB were not a private cooperative, it would cease to be part of the national cooperative banking system and hundreds of millions of dollars would be lost to Alaskan fishermen and farmers. In their place, the Legislature would have to fund the operations of CFAB in the annual budget document and allocate those millions for the same loans, thus reducing the funds available to the people of the state for other purposes and costing them millions of dollars in subsidies.

Our basic instructions from the Governor, the Legislature, and the consultants at the time of CFAB's creation were to form a private, cooperative financial institution. If that is not the case, as you suggest by your comments and the standards apparently used in formulating your audit, then the intent of the legislation cannot be carried out, outside funds cannot be brought in to benefit farmers and fishermen through CFAB, and the Legislature will be forced to appropriate necessary funds from the General Fund. This will, of course, place the State directly back into the loan business against the wishes of the Legislature and the financial community.

The Legislature also intended that CFAB be audited and required in the original legislation that the board of directors have an annual audit performed by outside, independent auditors, and that the audit report be made available to the Governor, members of the Legislature, and the general public. CFAB has employed the national firm of Price Waterhouse & Co. for that purpose. They have completed audits for the years 1979 and 1980. A copy of the 1980 report is attached. This audit clearly shows CFAB to be following proper practices and procedures.

In determining performance, one must look at achievements toward a stated goal. In its brief history, CFAB's achievements are many. Among them are:

1. Establishment of a well organized, systematically run business which is managed according to generally accepted management practices, including:
 - a. Stated mission, goals, objectives, and action plans;
 - b. Complete and accurate accounting systems;
 - c. Detailed, written policies and procedures covering the whole of our operation;
 - d. Complete budgeting and financial reporting system;
 - e. Employee policies, pay scales, job descriptions, and evaluation systems;

- f. Printed documentation for loans bearing the approval of both general and specialized legal counsels of the Cooperative.
2. Active involvement of the members of the Board of Directors in the policy development and control of the organization, plus a high level of attendance by those members at meetings.
3. Development of a full and professional cadre of accounting, legal, insurance, tax, and management advisors of national stature.
4. Completion of a procedural audit by a national firm of CPAs using both their auditors and management advisory groups to insure the continuity of our procedural and control systems. This form of audit is scheduled to be performed on an annual basis.
5. Development of 32 specialists in various aspects of fisheries finance. These add to an extremely limited, if not almost non-existent, field of expertise.
6. Opening five branch offices, offering the full services of the Cooperative, in key areas throughout the state. Branches are now located in Kodiak, Homer, Cordova, Ketchikan, and Seattle.
7. Maintenance of an active calling program to areas outside of the loactions of our established offices.
8. Attracting and financing nearly 250 member shareholders from geographically dispersed areas within the state.
9. Development of a full range of loan programs to serve the fishing and agriculture industries, adding appreciably to those previously available.
10. Development of credit lines necessary to meet CFAB's financial needs and its commitments to members.
11. Achievement of more rapid turnaround of loan applications.
12. Achievement of profits in each of its accounting periods despite expensing all opening and operating costs. Profits for the first quarter of this fiscal year are \$800,000.
13. Return of patronage dividends equal to $9\frac{1}{2}$ percent of the interest paid by members during 1980.
14. The first installment in the return of the State's initial capital investment was made.

15. Support of agriculture and fisheries development through:
 - a. support of 4-H and FFA;
 - b. creation of the Young Alaska Farmers Financing Cooperative to provide financing for youth agricultural projects;
 - c. development of financial planning manuals for use by fishermen and farmers;
 - d. support and initiation of research projects;
 - e. participation in policy development.

16. Enhancing other financial agencies' abilities and opportunities to finance both fisheries and agriculture. CFAB is currently financing the customers of the Agriculture Revolving Loan fund during a period in which it is out of funds, enabling farmers to plant crops and advance projects in the critical summer months.

We have also provided the necessary additional funds and controls of credit to allow other Alaska banks to safely become involved with or continue their involvement with Alaska processors.

17. Adding a point of financial professionalism to the Alaska fishing and agriculture industries to which foreign and "Lower 48" financial institutions can relate and on which they can rely.

In the formulation of your letter, you have failed to relate to specific key points about CFAB's operation. It is owned and operated by private shareholders who bear the full risk of its operation and whose investments are subordinated to those of the State. It is these shareholders who, by law, have the management and control of the Cooperative. Moneys expended by the Cooperative in the achievement of its business purposes are not those of the State. Unlike a State or other public body, CFAB's expenditures do not represent an irrevocable loss of those funds to the people of the state. Expenses are paid by the income of the Cooperative derived from its operations which, by definition and federal tax law, are the property of the member stockholders. CFAB is governed not only by the specific statute creating it, but also the cooperative laws of the state and the federal tax law specifically dealing with lending cooperatives. CFAB pays full federal taxes, unlike a State agency or department.

We appreciate that performance of an audit of CFAB has posed a difficult problem for you. While somewhat unique to Alaska, organizations such as CFAB are widespread in the lower states. They are certainly the business of the Bank for Cooperatives and are among the clients of our CPA firm, Price Waterhouse & Co. In fact, Price Waterhouse is considered to be among the

best in the practice of cooperative accounting, management and tax practice. It lists among its clients some of larger cooperatives in the United States. Using their experience, and with a number of comparisons to draw from, they have audited CFAB and found everything to be in order and within the context of proper operation.

Being a CPA yourself, you are well aware of the Generally Accepted Auditing Standards imposed upon members of your profession. Among these are the matters of relevance, materiality, and context. It appears that items reported in your letter have been taken out of context and included without review and full understanding of the circumstances surrounding them. There is no stated standard of comparison used in the determination of significance.

Development of your report on the basis of inadequate understanding of CFAB, its purposes, and the requirements of operation imposed upon it causes the Board of Directors of CFAB tremendous concern. Presented in the fashion of your letter, without standards of acceptable comparison, provides the public reader no basis upon which to draw judgment. This may unjustly tarnish the reputation of Management and of the members of the Board, as well as diminish the willingness of some borrowers to do business with the Cooperative. In turn, the private stockholders of CFAB will be injured.

We will comment on each of the items raised in your letter.

Recommendation No. 1 is a good point and one previously raised by our CPA's in the course of completing their procedural audit. That point has been corrected both by requirement of borrower-provided insurance and by CFAB obtaining a blanket policy.

Recommendation No. 2 regards the compensation of Board members for per diem expenses. There is an alternate to fixed per diem provided for in the regulations pursuant to which CFAB has established its policies for board reimbursement. We have asked our attorneys to review that section in the case we have misinterpreted the details of application. If we find that we have, we will, naturally, correct procedures in the future.

In the evaluation of expenses, one must relate them to the mission, goals, objectives, and the business framework in which CFAB operates. While CFAB has initial investment funds from the State, it receives no other support and must repay the State within a specified period of time. Viewed as a benefit on the one side, it is a large financial obligation on the other. CFAB must develop an operation capable of attracting the hundreds of millions of dollars from outside lenders necessary to fulfill its mission and purpose. While the mission of providing loans to fishing and agriculture may appear the same as those given to a State loan program, or to AIDA, the road to their accomplishment is much more complex given the lack of State funding or State guarantees.

In addressing the mission imposed by the Legislature and in creating the organization to meet that mission, the Board of Directors has established policies, philosophies, and procedures which insure the long term viability of the organization. This same organization is established to meet the standards and the expectations of the national and international financial communities upon which we must rely now and into the future. It should be noted that CFAB now has correspondent relationships with Denmark, Danish banks, and Norwegian financial institutions, and is opening negotiations with Japanese and Canadian banks, as well as large commercial banks in the "Lower 48."

To establish its standards of operation, the board has closely examined the standards of other similar institutions. We have determined that CFAB's standards are in all cases within comparable standards, as are its expenses. All expenses are deemed necessary to CFAB's business purpose and are according to budgets established in conjunction with Management.

With regard to the items specified in your letter:

A. Furniture, Fixtures and Leasehold Improvements

The expenses of furnishing the executive offices of the Cooperative are in line with similar expenses at the Spokane Bank for Cooperatives and other financial institutions. Neither the cost nor the decor is inconsistent with the standards of other institutions in Anchorage of comparable size.

They are intended to establish the proper decorum and to relate to the type of visitor frequenting the offices. These include trade missions, ambassadors, presidents of large corporations, and executives from among the international financial community. While Steel Case desks may well serve the necessary business environment of a public agency, they do not serve the demands of this Cooperative. Decor of that nature would only serve to reinforce a "poor country cousin" image. In creating the office environment, CFAB took great care in its design and decoration to meet the needs of its many categories of users. It is designed to be a comfortable place to work for those who spend the majority of their days here; a relaxing, warm place to visit for the borrower who is normally intimidated by banks and bankers; and a tasteful, professional environment for the executive businessman.

A careful watch was made of expenses, and a great deal was achieved by the use of highly qualified decorators with experience in office decor.

The conference area you have mistakenly inferred to be restricted to executive personnel is a general conference area decorated to fit the general office decor and serve the purposes previously described, while accommodating the larger meetings regularly held at the office.

The Juneau apartment is widely used by the Board and staff of the Bank. It was originally rented during the formation stages of the Cooperative during which time the Board and the staff were spending large amount of time on a continuing basis in Juneau. It provided a meeting place and proved cost beneficial against the use of hotels. Retention of the apartment has been reviewed periodically and will be again in the future. Having decided to open our Southeastern office in Ketchikan, but having need to conduct business in Juneau on a regular basis, it has been determined that CFAB requires some form of permanent location from which to operate and hold meetings while in that town. The combination of apartment and office showed clearly to be the most economical alternative versus renting an office on a per square foot basis and using hotels. The wallpaper itself was hung by staff and various items of sparse decoration have been contributed by the Board and the staff.

B. Artwork

It should be noted that you have listed all, not a sample, of the artwork purchased by CFAB. The use of the word "Sample" is editorially misleading.

The artwork in the Anchorage office was purchased or commissioned from local artists to fit both the decor and the operation of the office. The expenses of the works are consistent with the art and are under the value of the pieces in the present market. The cost of the individual works does not come close to the cost of the works contained in the State collection, some of which adorn the walls of legislative offices, nor in the collections of other private businesses in Alaska. All pieces in our offices depict agriculture or fishing, with Alaska overtones.

C. Automobiles

Transportation is a necessary part of our business, as it is with most. Not being a State agency, CFAB does not have access to State pool vehicles, nor was such access intended.

It will be noted that the cars purchased by the Cooperative are small, economy vehicles which meet the demands of Alaska conditions.

Provision of automobiles to members of the executive staff, both for business and personal use, is a normal business practice and one necessary to CFAB if it is to attract the personnel needed. You will note that the car provided to the President is not the high priced, luxury vehicle customary to presidents of other Anchorage financial institutions, but rather a Chevrolet with a monthly lease payment far below comparable costs. The automobile provided for the use of the Senior Vice President-Administration is also available for general Bank use and is assigned to him in lieu of other compensation. The gasoline provided to the Senior Vice

President-Credit only partially offsets the luxury vehicle provided by his previous employer, another Anchorage bank.

The decision to purchase automobiles was made after considering the life cycle costs and discounted cash outflows of purchased vehicles over locally available leases or reimbursement for personally provided automobiles.

D. Salary and Benefits

The attraction and retention of the best people is deemed to be of vital importance to the business of the Cooperative. It is a highly accepted business principal that people capital is more important than dollar capital. To attract and retain these people requires that the Cooperative provide competitive salaries, benefits, working conditions, and opportunities. In establishing these benefits, the Board annually reviews the market, both in Alaska and in the "Lower 48", to determine levels and trends.

It should be noted that CFAB pays the full cost of the PERS coverage, including an allocation for administration. No cost is borne by the State. CFAB's involvement with PERS and other State benefit programs will be deleted with passage of current legislation supported by the Board.

The bonus program has been widely covered and explained in detail, not only to the Budget and Audit Committee of the Legislature, but also to all Senators and House members. It has proven to be an effective tool resulting in rapid accomplishment of goals and objectives. Bonuses are paid for productivity, not for the mere occupation of space. In widely read coverage of CFAB pay and bonus programs, the Anchorage Times reported that CFAB's remuneration to employees, including bonuses, was not out of line with industry standards.

Staff room expenses for coffee, tea, etc. are common for business and a common courtesy extended to visitors and staff of most businesses and even some State offices. The figures quoted include stocking of cups, plates, and other necessary kitchen items.

Tickets to the Repertory Theatre were erroneously listed under benefits and should have been posted to entertainment. While listed under one employee name, they are used by other members of the staff to entertain customers, consultants, and other vendors, as well as support the theatre. If you will check the list of donors and ticket holders to the Rep and other performing arts, you will find a large portion of patronage comes from businesses.

A Christmas party is also a normal event in the private sector. CFAB also uses the occasion to thank particular vendors, consultants, and suppliers, as well as the spouses of employees

whom we feel contribute to the organization. Facilities available to accommodate groups of any size are limited in Anchorage and never inexpensive. The cost of these Christmas parties is part of the overall employee relations program which has provided the Cooperative with measurable and high levels of achievement. Comparison with other financial institutions would reveal that neither the function nor the per person cost is out of line.

In the last paragraph of this section, you have listed other staff benefits of \$6,076 and other personnel expenses of \$13,810. In the former figure, you have double counted an accrual of \$4,551 for the previously listed Christmas dinner and \$345 for tickets to the Repertory Theatre, also previously mentioned. Of the latter, the majority does not represent dinners with interviewees and staff, but rather the expenses of bringing people to Anchorage for interviews; including hotel, meals, car rentals, etc. Naturally, some of the names appearing in those postings will now appear as employees. Also included are a few dinners including employees and primarily involve our branch staffs while in Anchorage for loan presentations, training, etc. If you would have the opportunity to examine the expenses of other businesses, you would find that it is common to carry on business over lunch if it involves something better discussed away from the office or the press of the day's schedule allows only that time.

E. Rent

Here, too, you have failed completely to draw comparisons or to consider the full costs of an office. In commenting upon the cost of the office space (also mentioned in our annual report) you have not mentioned the cost of comparable space in Anchorage or within the same building. In making that comparison, one must also consider a number of factors. First is the cost of making necessary tenant improvements such as walls and wiring. Second are the inducements offered by the landlord to obtain the lease. Third is the extra cost of occupancy such as escalator clauses, utilities, and services. And of equal importance is the availability of expansion space during the course of the lease.

After looking at a number of buildings in Anchorage and receiving bids from several, the actual cost of our present location was not only cheaper than the alternatives, but also offered many side benefits, such as central location to staff; adequate, free parking for staff and members; close proximity to our CPAs, attorneys, and insurance brokers who are contacted on a frequent basis; and ease of finding the location for our members and other visitors. Even some State agencies, such as Fish and Game, pay much higher rent. The forecasted cost of a State office building is considerably higher than the figure quoted. One should caution that the disclosure of this rent figure is a violation of our agreement with the landlord, as rents in the building are not the same for all tenants.

In describing the quarters and appointments, particularly in our kitchenettes, you have forgotten to ask questions that would have put many points into perspective. For example, we have doubled the office space since opening and, in so doing, took over the office space previously occupied next to us. That tenant had a kitchenette also, which we have converted into a much needed second conference room. The cost to remove the previously installed appliances exceeded the cost of retaining them. Due to the cost benefit and the convenience of the facility to the staff and clients on that side of the building, they were left. Additionally, the table in that conference room is not natural oak, but rather formica in an oak pattern, as are all of the desks in the area.

If you had surveyed the building, you would have found the kitchenettes to be common in the building and equipped similarly to ours. As can be seen from the one taken over and now used as a conference room, many are larger than the one mistakenly listed as the executive kitchen. Furthermore, if you had observed other floors of the building during the last three and one half months, it would have been noticed, even casually, that oak is the standard material used in all trim, elevators, cabinetry, and other wood surfaces in the building. It is a standard established architecturally.

The kitchenette is used often for preparation of lunches for luncheon meetings, saving not only the expense of eating out, but also time during busy days.

F. Directors Fees

Directors fees are, by law, left to the discretion of the Board of Directors. CFAB's Board compared compensation paid for other private boards and even some State boards, such as the Permanent Fund. Also, in the consideration was the amount of time necessary to complete the Board function (two days each month for regular meetings) and the lost travel time of one day each way for the majority of members. You should have also found that the Board spends considerable time outside the regular board meetings on behalf of the Cooperative. Rates for this time were compared to consultant time rates and the daily meeting rate. Closer questioning would have revealed that individual Board members bill only a fraction of the time they spend.

You have listed as significant the fact that one member received \$12,438 in consulting and organization fees during an 18 month period. You are referring to the previous Chairman of the Board. During the early organization period of the Cooperative, the Bank had limited staff and those it did have were unfamiliar with much of the workings of the Alaska business system. This individual, at the request of the Board, devoted countless hours to the organizational efforts and brought to the task knowledge and experience not elsewhere available in the organization. His regular business is that of a consultant, together with other

partners, and his income dependent upon hourly billings. He could not afford to devote the time required without proper billing nor would his business partners have allowed it. The time billed was substantially below that applied and the rates below those charged by other consultants and professionals employed by the organization.

G. Travel, Lodging and Meals

Foreign travel is a necessary part of CFAB's business. We deal with internationally traded commodities, both in fisheries and agriculture. Likewise, our members have internationally related financial transactions. Markets and practices in other parts of the world have direct impact upon the financial well being of our stockholders.

CFAB has correspondent relationships in Scandanavia, has purchased equipment to aid Alaska's farming community from Denmark, and is beginning negotiations with other foreign banks. These relationships are used not only to provide necessary credit information on receivables financed, but are expected to result in lines of credit enhancing our lending abilities. Provision of knowledgeable and complete lending services to Alaskan fishermen and farmers cannot be accomplished without development of a wide range of international contacts.

You will find that others on the trips listed included representatives of State government and private enterprise. You should also note that the agriculture trip to Denmark was at Denmark's invitation and most were expenses for their account. Further examination of other private and government departments will reveal a wide range of foreign travel. The significance of international markets to Alaska is evidenced, in part, by the fact that the State itself keeps two fully staffed offices overseas, and is considering a third.

It is the policy of the Cooperative to allow travel expenses for spouses if the functions attended normally include spouses as a part of the activities. You will find this to be a similar practice among most Anchorage banks, other businesses, and the Bank for Cooperatives.

You have mistakenly listed a minor amount of \$376 as an expense of a former trip. It is a prepayment of the Munich International Fisheries Conference to be held this October. That conference will be attended by various of our processing members, as well as the Alaska Seafood Marketing Institute. You might also be interested to know that the Alaskans attending the previous conference were highly appreciative of our attendance and remarked that CFAB was the first Alaska financial institution to show sufficient interest in becoming fully involved in learning the industry.

The Senior Vice President-Administration made only one trip to England. He was accompanied by the Vice President of Branch

Administration who is also a vessel surveyor. They were in London to visit the various departments of Lloyds of London, which is the major insurer of vessels in Alaska. In addition to learning about the intricacies of vessel insurance, they also investigated possible criteria for certifying vessel surveyors, as well as ways in which the risk of Alaska fisheries as perceived by Lloyds might be diminished. This would result in substantial savings to our fisheries members. Competence in both insurance and vessel valuation is a vital part of our business.

Dinners

In listing 48 dinners over \$100, you have not considered the number of people involved, the purposes of the dinners, or the relationship of those entertained to the business. You also seem to miss the prices charged by the average dinner house in Anchorage that is conducive to a business discussion. In fact, it is one of the items that ranks among the more substantial cost of living differences between Anchorage and elsewhere.

All dinners you have listed were in the normal course of business and involved a defined business purpose. Most of the ten dinners you have listed should be self explanatory given the people attending. Without more detailed reference to dates, it is impossible to describe each one. However, since such dinners are not that common an occurrence, I can clarify specific occasions to help you further understand our business. I will refer to them by the number you have ascribed.

1. This was a dinner that involved the Vice President-Branch Administration who had been offered the job in Anchorage, but had not yet accepted. He was in Anchorage to look over the area with his spouse and look for available housing. Raised in Cordova, both he and his wife were unsure of the move and wanted to become more comfortable with the business climate of the Anchorage office. The dinner was to allow his spouse to become acquainted with other spouses and gain assurances of help and availability of necessary family services. It is common for businesses to have such dinners. They are a selling function necessary to have the right people in the right positions.
6. This bill also included cocktails and dessert for an assortment of legislators, UFA representatives, and CFAB consultants.
8. These dinners also included other members of the staff and possibly their spouses. They were held in conjunction with the normal board meetings. It has been the practice of the Board to continue business through the dinner hours and to use this time to obtain more general and informal information about the operation. They often invite staff members and their wives to learn

about particular jobs within the Cooperative and to give the staff members wider exposure to the business.

10. This dinner included the Senior Vice President-Administration and the prospective Senior Vice President-Credit and their wives. The occasion gave these two people, who are key officers of the Cooperative and who must interface directly on almost every matter, a chance to become better acquainted and form the grounds for needed communication. Again, this is a necessary part of a business operation and normal to private business.

Members of the Board and the Executive staff are professionals in upper income brackets and educational backgrounds. The level of entertainment done is consistent with industry standards.

You have further listed four occasions of other staff dinners. We fail to understand their inclusion. Of the first, you mention several lunches totaling \$137. It is difficult to draw any conclusions from that statement since the context, purpose, and applicability elements are missing from your statement.

The dinners listed for the staff in Seattle were most likely for our participation in the Fish Exposition in Seattle during which we had several employees in Seattle to man our booth. The dinners and their prices are normal.

The lunch costing \$172 was a going away luncheon for one of the staff and quite insignificant when compared to the contribution to the Cooperative of the departing member.

The items included in the \$1,331 listed as "Banquets" include the annual meeting of shareholders, a board meeting, the Agriculture Symposium, and a trade delegation.

Miscellaneous expenses listed are for stocking of the office facilities in most cases. Tuxedo rental was for an affair requiring both attendance of the employee and formal wear.

The use of the Alaska Airline Board room is also a necessary part of the business and is used for meetings at the airport with clients and others passing through. It provides private accommodations for such meetings at insignificant annual cost.

H. Promotional Costs

Opening parties are a normal part of business and provide a significant show of interest in both the community and the members of the markets served. The opening Anchorage party was attended by close to 100 people, not all of whom had dinner. Both the cost of the affair and the attendance was reasonable by Anchorage business standards. Reference should be made to the recent opening of the Anchorage office of Alaska Pacific Bank, as well as several professional firms entering the Anchorage market. That comparison will show the cost of CFAB's opening dinner to be normal and the affairs to be equally frequent among those

companies.

Similar receptions were deemed essential to each branch office location listed and were structured to fit the norm for such affairs in each area. It is difficult to envision an opening reception in an area to introduce a new company and new services without representatives of the company present. It would be particularly insulting to CFAB members and potential members for the members of the Board and senior officers not to be present. Additionally, the occasions provide opportunity to the Board and Management to become quickly familiar with the people in the communities they will be serving. Use of charter aircraft when transporting a larger number of people offers a large cost benefit.

As a private company with legislative needs, good governmental relations is a normal and necessary function. The legislative reception, which was well attended, provided the staff and the Board the opportunity to discuss CFAB's needs and operation with legislators who would be unavailable in another form. Such receptions and dinners are also normal to the legislative process and Juneau experiences them on a regular basis.

Gortex jackets were given to the staff as both a traveling uniform providing quick and easy identification and as a functional garment for the conditions in which they travel. Provision of garments is not at all uncommon in the fishing industry. The price you have quoted included 1000 patches costing \$1,200 to be used on hats and other promotions. Your attention is drawn to a feature story in a recent edition of the Fishermens Journal specifying the importance of these hats and logos within the fishing and agriculture industries, both in Alaska and the "Lower 48."

Tide books are an essential item to all fishermen and are used by all our members and potential member stockholders. Constantly referred to by the fishermen, they are an extremely effective media through which to provide facts about CFAB and its available services.

The cookbooks are a part of a visual program on the use of the microwave in cooking fish. It is part of a national promotional campaign produced by the National Fisheries Institute of which CFAB is a member. The campaign has been participated in by numerous processors and marketers. CFAB makes its slide presentation and cookbooks available to home economics groups, businessmen selling microwaves, and cooking classes. It was recently prominently used by the Alaska Seafood Marketing Institute in a show promoting Alaska fisheries products in the Mid-West and will be used again by the same group in Germany. Development of these types of programs falls clearly within the legislative mandate.

The annual reports ordered by the Cooperative were 1000, not 500. The cost of producing that report was above that planned

because of a number of reasons, including the original photographer leaving the state with the pictures, requiring them to be reshot by another photographer; special, quick turnaround time by the printer and separator due to the time constraint of legislatively imposed March membership meeting which left only two weeks between completion of the audit and the meeting. These unusual costs associated with our first annual report should not occur again with future reports. However, the expense of an annual report is an absolutely necessary expense of our business. It is the primary publication supplied by us to our members, legislators, the Governor, the public, as well as our creditors and vendors, and is considered by members of the financial community as an essential communications tool. Put together as CFAB's was, the vehicle provides not only the opportunity to present a company's financial picture, but the entire framework of the business.

I. Review of Board Minutes

Your remarks in this section are truly out of context and without precedent. We can find no reason or justification for their inclusion in your report. Even given the consideration of the inappropriate standards used in your audit of CFAB, it is particularly unique to include two items on which the Board of Directors has taken negative action.

The items presented include no reference to the decision making process involved, the cost to benefit relationships derived, or the purpose of the discussions. Foreign travel for education in the fisheries -- the predominant market we serve -- is a viable item to review. The availability of an extremely low airfare opened an otherwise costly opportunity for discussion. An aircraft in a state dependent upon air travel and for an organization traveling to all parts of the state is also an item one would expect a board to discuss.

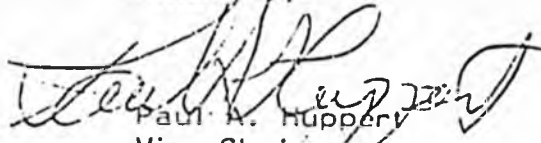
Are you suggesting that there are items forbidden to the Board for discussion and review in the interest of the corporation they are responsible for? Are you further implying that a board should stand in criticism for reviewing all the alternatives open to their business? Or are you suggesting that the board minutes reflect only those items which you, a staff employee of the State, consider to be proper, palatable and in keeping with your particular personal standards? I am sure you are aware that foreign travel is extensive among Alaskans and is a subject reflected in the minutes of many boards. Additionally, the State of Alaska itself has considered purchase or lease of a State plane on several occasions.

Mr. Harris, we appreciate the efforts that you and your staff put into the audit. Danna worked hard and fit in well with the office staff. We are sorry that your understanding was not more complete, enabling your audit to be of a more meaningful nature. Your report only proves that a private business operating

Paul V. Harris
June 12, 1981
Page 16

under the standards required by the private market cannot be audited against standards commonly used by the Legislative Auditor.

Sincerely,



Paul A. Huppert
Vice Chairman

sd

Alaska State Legislature



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SENATOR
ARLISS STURGULEWSKI

COMMITTEES
CHAIRMAN
Legislative Budget & Audit

Community & Regional Affairs
Finance
Resources

*W.P. [unclear]
[unclear]*

Senate RECEIVED

02 SEP 1981

LEGISLATIVE
AUDIT

MEMORANDUM

02 September 1981

TO: Glen Svendsen
Special Assistant

FROM: Senator Arliss Sturgulewski *AS*
Chairman, Legislative Budget & Audit Committee

RE: Commercial Fishing & Agriculture Bank

Enclosed please find the letter sent by Roseleen Moore in response to my earlier question regarding issues raised by individual Legislative Budget & Audit Committee members. Will you have Betty send out a copy of my original letter plus this response to all committee members?

I am sending a copy of Roseleen Moore's response as well as a copy of this memo to Jerry Wilkerson.



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Roseleen "Snooks" Moore
Chairman

August 27, 1981

The Honorable Arliss Sturgulewski
2957 Sheldon Jackson Street
Anchorage, Alaska 99504

Dear Senator Sturgulewski:

We appreciate the findings on management expenditures and the Board has taken steps to reevaluate and correct our current budget and will definitely take these findings into account in the budget preparation for the coming year.

As you can well appreciate, the repayment of the State is a multi-faceted problem that must be approached carefully. The impact upon CFAB and its ability to meet its mission, its goals, and the expectations of the communities it serves will be significantly affected by the course taken. There should be no doubt in the minds of the legislators that CFAB takes the responsibility of meeting its obligation seriously. Repayment of the State is of paramount importance to the Board and Management of CFAB and is of significance in established policies, budgets, and plans.

We are in the process of examining all the alternative means to accomplish the legislative imperative that the Class C stock be repaid by the end of 20 years. Our decision will be reached as part of the planning process at the December board meeting. You can be assured that our direction will be based upon our judgment and will best serve the two industries we serve as well as the original intent of the legislation.

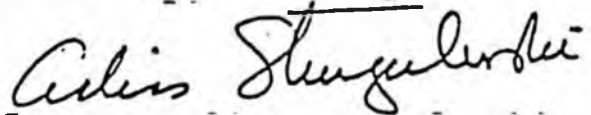
Sincerely,

Roseleen "Snooks" Moore

sd

Your timely response to these two requests will be appreciated by the Committee. Any questions or clarification of these requests can be directed to me.

Sincerely,

A handwritten signature in cursive script that reads "Arliss Sturgulewski". The signature is written in dark ink and is positioned above the typed name.

Senator Arliss Sturgulewski
Chairman, Legislative Budget &
Audit Committee

cc: All members - Legislative
Budget & Audit Committee



State fishing loan bank makes recovery

By JIM ERICKSON
Daily News reporter

The Alaska Commercial Fishing and Agriculture Bank, its decks awash in red ink and in danger of being scuttled two years ago, has manned the pumps.

Rebounding from a near-fatal \$10 million loss in 1984, the lending cooperative posted a \$535,780 profit last year, according to figures released Wednesday. The organization's financial picture had brightened enough to justify the April 1 mailing of dividend checks to CFAB's 577 members, most of them Alaska fishermen.

The company made \$114,187 in 1985.

Ed Crane, president of CFAB, attributed the recovery to several factors. The most significant was a 31 percent reduction in overhead compared to the previous year. Operating expenses totaled \$1.9 million last year, the lowest annual outlay in the cooperative's six-year history.

Crane said much of the savings resulted from the closing of four regional offices in late 1985.

Larger fish harvests and higher prices in the Alaska fishing industry had little ef-

fect on CFAB's bottom line last year, Crane said. Interest income from loans, CFAB's main source of income, declined to \$6.1 million in 1986 from \$10.1 million in 1985. Total loans dropped to \$41.1 million last year from \$62.4 million.

"We've shrunk in (loan) volume really more than we're comfortable with," Crane said. Industry growth has been centered in areas that CFAB cannot participate in, such as joint ventures between Alaska fishermen and Outside companies, he said.

The cooperative, which the Alaska Legislature established with a \$32 million capital infusion in 1981, can make loans only to Alaskans or Alaska companies.

"We've had numerous deals, particularly recently, where people have approached us for a loan to refurbish a processing plant, and we had to say no" because the company was not Alaska-based, Crane said. Despite efforts last year and this year to get law changed to allow CFAB to make out-of-state loans, lawmakers have shown little interest, he said.

CFAB is owned by members and by the state.

"The biggest frustration I feel personally is the lack of

flexibility and the orphan-like existence we live."

Commercial banks, which in the past have shown little interest in lending money to fishermen, now are competing on a small scale with CFAB, he said.

Crane said CFAB has "turned around" runaway loan losses and delinquencies that threatened to ruin the organization two years ago.

CFAB's non-earning loans increased slightly last year to \$17 million. But that amount was still far less than the \$32 million in delinquent loans CFAB carried in 1984.

Ten delinquent borrowers accounted for more than \$13 million of CFAB's current delinquencies.

Continuing problems with bad loans mean the organization must charge higher interest rates on new loans, Crane said.

Partly to provide a "rate rebate," CFAB's board of directors decided to pay members a 1986 dividend. The total amount paid was \$214,309, or 40 percent of CFAB's net income last year. The average check was for \$371, although the amounts varied from \$1.18 to \$29,282.

Despite CFAB's return to modest profitability, it remains unclear whether the

cooperative will be able to repay all of the state's \$32 million investment when it comes due at the turn of the century, Crane said.

"Somehow, we've got to get \$32 million in liquidity built in there" in the next 13 years, he said. "I'm skeptical we can do that."

CFAB now has \$17 million in "solid assets," Crane said. Two years ago, if CFAB had been liquidated, "the state would have lost the whole \$32 million."

The cooperative also faces another at CFAB borrows money to lend to members from the Spokane Bank for Cooperatives, and has \$5.4 million invested in that organization. The Spokane bank is one of 37 banks in the troubled Farm Credit System, which holds nearly one-third of the nation's farm debt.

If the condition of the system worsens or if proposed federal help does not come, CFAB could have trouble borrowing what it needs for members, and borrowing costs could remain "at a relatively high level," CFAB's annual report states.

CFAB ultimately could suffer a paper loss of \$5.4 million if the system collapses, Crane said.

Capital-reared bank is having hard time standing on its own

An auditor's note in the State of Alaska Financial Report announces that the state may lose all or part of \$31.8 million invested in the Alaska Commercial Fishing and Agriculture Bank.

Those who are scrambling to get a few thousand dollars from the state this year are entitled to ask the government how \$30 million was cast to the winds without even the minor formality of a legislative appropriation.

Among the many strange creatures to evolve from Juneau's mad-cap hatchery, the Alaska Commercial Fishing and Agriculture Bank (CFAB) is one of the most curious. It's not a bank and it's not even a state agency, yet it's a creation of the Legislature, financed with state money. It's a sort of bureaucratic platypus.

The CFAB was created by the 1978 Legislature as a public corporation within the Department of Commerce and Economic Development. The original intent was to raise lending capital from the tax-exempt bond market, but the Internal Revenue Service declined to endorse the scheme.

Instead of letting this miscreant die, the Hammond administration devised a roundabout plan to establish the CFAB as a private cooperative bank financed by \$32 million in government money.

In Fiscal Year 1979 the Department of Revenue bought 200 shares of CFAB stock for \$2 million. The stock was special preferred Class C,



Fred Pratt

having no voting or dividend rights. A 1979 act of the Legislature authorized the stock purchase and appropriated \$2 million for stock purchases to finance the bank's start-up costs.

In March 1980 the Department of Revenue loaned CFAB another \$30 million at 9 1/2 percent interest. The bank opened its doors for business April 2, 1980. In July 1980 the loan was canceled by an agreement in which the bank issued the state another 3,000 shares of Class C stock at 1 paid \$480,205 in interest.

I'm unable to find anywhere in the Legislature's records where this \$30 million was appropriated. I checked with Deputy Commissioner of Revenue Mill Barker and he confirmed this after a short search of the department's records and consulting a former Revenue official.

The bank's only obligation to the state for the \$32 million is to buy back the stock at the same price within 20 years. The governor also gets to appoint two members of the seven person board of directors.

The bank's major source of operating capital is the Spokane Bank

for Cooperatives, a member of the federal government's Farm Credit System. The stockholders of CFAB are the borrowers themselves. If you get a loan you must buy one share of Class A stock for \$10, giving you one vote but no dividends, and enough shares of \$100 Class B stock to make up five or 10 percent of your loan amount.

The bank loans you the money to buy the Class B stock by tacking it onto your loan request. If the bank should ever pay dividends, it would be paid out on the Class B stock.

Since it doesn't take deposits, the bank is not chartered by the state and it's specifically exempted by law from the Alaska Banking Code.

The CFAB went right to work, with a panache that quickly caught the eye of the Legislature's financial watchdogs. An audit of the bank's books in May 1981 focused public attention on how the state's "investment" in CFAB was spent.

The legislative auditor noted that the bank president's office in Anchorage was furnished with a \$3,631 sofa, a teak bookcase and cabinet that included a refrigerator and liquor cabinet (\$4,232), and five swivel upholstered chairs (\$7,717). The two senior vice presidents had teak desks, teak coffee tables and teak bookcases. The executive conference room boasted a rosewood conference table (\$16,225), 14 chairs (\$10,470) and a \$2,000 soapstone carving.

They decorated the office with (See PRATT, Page C-5)

Fairbanks Daily News-Miner, Fairbanks, Alaska, Sunday, February 15, 1987—C-5

PRATT

(Continued from Page C-1)

\$13,353 in artwork, the auditors reported. The 7,000 square feet of leased office space in Anchorage included two kitchens, each equipped with oak cabinets, microwave oven, dishwasher and refrigerator. The employee lunch room had an oak conference table and upholstered chairs (\$4,360).

Oddly enough, the staff seems to prefer other places to eat. The bank records included 48 dinners of more than \$100 each on the expense report of its two top officials for an 18-month period. The bank paid \$215 for dinner for two bank officers, a prospective employee and their spouses at the Captain Cook. It cost \$256 for a dinner at the Corsair in Anchorage for four bank employees and their spouses, and the president ran up a \$210 tab taking his wife, a senior vice president, a local businessman and their spouses out to dinner at the Corsair.

The bank's 1980 Christmas party at the Anchorage Westward Hilton cost \$2,353 for food, \$2,197 for liquor and \$600 for entertainment. The bank also spent \$415 for holiday turkeys for its employees.

A pre-opening party at the Sheraton Hotel cost \$1,325 for 64 dinners, \$186 for 19 bottles of Chenin Blanc wine, \$124 for 18 bottles of Pinot Noir and \$814 to pay the tab for 283 drink tickets at the hosted bar. The bank said about 100 people attended this affair, and the total cost came to \$3,782 when travel and hotel expenses were added in.

The bank also held pre-opening parties at the branch offices in Kodiak (\$4,072), Cordova (\$7,610), Homer (\$1,852) and Seattle (\$2,039).

Another \$5,064 was paid for 66 Eddie Bauer Gortex mountain parkas with CFAB logos, given to employees and board members.

The bank responded by saying it wanted to avoid giving a "poor country cousin" image and its spending was in line with that of private sector banks. It claimed the furniture described as "natural oak" was Formica in an oak pattern.

The president was quite a jet-setter. In the fall of 1980 he and his wife toured Denmark, England, Rome and Paris at a cost of \$8,805, and they returned to visit Denmark, Norway, Sweden and Finland the following spring (\$6,068).

The audit reported that in 1981 he anticipated a spring or summer trip to Japan and an October trip to Munich.

The auditor also found the bank was not requiring insurance of inventories used as collateral, which is odd when your collateral might include sensitive inventories like frozen fish. In a sample of eight loans the auditor found five were unsecured, and the bank was listed as the loss payee.

Most of the bank's operations seemed aimed toward commercial fishing, with a major portion going to operating financing for fish processors. Farmers could find much cheaper money with the state's special agriculture loan programs.

I reviewed the bank's annual reports for 1983, 1984 and 1985. In the first of those years, the bank had 828 shares of Class A membership stock outstanding and slightly more than \$100 million in loans. Its interest and investment income was \$14,624,765, but it faced \$7.2 million in interest payments for the capital it borrowed, \$3.9 million in loan loss provisions and its other operating expenses reduced its "profit" to \$309,473.

A note on related party transactions revealed that \$6.2 million of

the bank's loans were to members of the board or directors or bank employees.

The bank reported a ten-fold increase in loans charged off that year, from \$176,121 in 1982 to \$1,858,138 in 1983.

The 1984 report showed a dramatic reversal. The bank lost \$10 million, mostly because it had to add \$11.2 million to loan loss reserves.

"Clearly, the exuberance associated with building, or patronizing, a new entity created a climate conducive to speculative lending relationships," the new bank president reported. The loan interest income dropped to below \$12 million while the interest expense for capital was up to \$8.4 million. The CFAB essentially had a negative net worth.

That year the bank notified the state that it might not be able to buy back the \$31.8 million in stock by the year 2000. There was some fear then that the CFAB might have to be taken over by the Spokane Bank for Cooperatives, Barker told me.

Things improved in 1985, the latest year for which a financial report is available. Loans were trimmed to \$62.5 million, the obligations

to the Spokane bank were cut by \$32.3 million through a reduction in the line of credit extended to CFAB. The year showed a small profit of \$114,187.

The offices in Cordova, Homer, Ketchikan and Kodiak were closed. The bank adopted a policy of recognizing non-performing loans if they were more than 90 days overdue, instead of letting the decision go by a manager's judgement. It also recognized that the Class B stock can't be simultaneously an asset and a loan receivable.

The bank management has done an excellent job in adjusting to its problems, but it's easy to see that the much smaller asset base is unlikely to produce the \$2 million a year in net profits needed to pay back the state by 2000, especially when the bank still shows a loss of \$6.8 million in operations over its seven-year life.

That's the price we'll pay for just one more lesson in how government schemes to promote business turn out to be more promotion than business.

Fred Pratt is a free lance journalist who covers Alaska business and politics.

ALASKA COMMERCIAL FISHING
AND AGRICULTURE BANK

- - -

REPORT ON EXAMINATION OF
FINANCIAL STATEMENTS

- - -

YEARS ENDED DECEMBER 31, 1986 AND 1985

Touche Ross & Co.
550 West Seventh Avenue
Suite 1500
Anchorage, AK 99501-3567
Telephone: 907 272-8462



Board of Directors
Alaska Commercial Fishing and
Agriculture Bank
Anchorage, Alaska

We have examined the balance sheets of Alaska Commercial Fishing and Agriculture Bank as of December 31, 1986 and 1985, and the related statements of earnings, changes in capital and allocated/unallocated undistributed patronage earnings (loss), and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Alaska Commercial Fishing and Agriculture Bank as of December 31, 1986 and 1985, and the results of its operations and the changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Touche Ross & Co.

Certified Public Accountants
January 23, 1987
(March 2, 1987 as to Note I)

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK

BALANCE SHEETS

ASSETS

	<u>December 31,</u>	
	<u>1986</u>	<u>1985</u>
CASH	\$ 147,410	\$ 106,773
TEMPORARY INVESTMENTS	4,150,000	3,200,000
LOANS AND OTHER RECEIVABLES, net of allowance for loan losses of \$3,291,026 and \$3,441,130	41,130,799	62,495,806
ACCRUED INTEREST RECEIVABLE:		
Temporary investments	4,700	44,144
Loans and other receivables	<u>1,302,252</u>	<u>2,071,202</u>
	1,306,952	2,115,346
INVESTMENT IN SPOKANE BANK FOR COOPERATIVES	5,390,548	5,252,423
BANK PREMISES, FURNITURE AND EQUIPMENT, net	351,874	471,503
ACQUIRED ASSETS HELD FOR SALE	83,007	1,606,164
OTHER ASSETS	28,997	90,563
	<u>\$52,589,587</u>	<u>\$75,338,578</u>

See notes to financial statements.

LIABILITIES, CAPITAL AND PATRONAGE EARNINGS

	December 31,	
	1986	1985
LIABILITIES:		
Accounts payable and accrued expenses	\$ 191,979	\$ 308,016
Accrued interest payable	233,634	416,780
Class B preferred stock subscriptions	60,163	
Notes payable	25,002,539	48,268,294
	25,488,315	48,993,090
COMMITMENTS AND CONTINGENT LIABILITIES (Note H)		
CAPITAL AND PATRONAGE EARNINGS:		
Share capital -		
Class C special preferred stock, \$10,000 par value, authorized 4,000 shares, outstanding 3,180 shares	31,800,000	31,800,000
Class B preferred stock, \$100 par value, authorized 400,000 shares, outstanding 40,410 and 65,845 shares	4,041,000	6,584,500
Loans receivable on Class B preferred stock	(3,698,500)	(6,584,500)
Class A membership stock, \$10 par value, authorized 10,000 shares, outstanding 975 and 931 shares	9,750	9,310
	32,152,250	31,809,310
C stock retirement pool	184,930	92,152
Capital in excess of par value	86,940	82,980
Contributed capital	144,626	144,626
	32,568,746	32,129,068
Allocated undistributed patronage earnings	825,691	1,045,365
Unallocated undistributed patronage earnings	535,780	
Unallocated undistributed patronage loss	(6,828,945)	(6,828,945)
	27,101,272	26,345,488
	\$52,589,587	\$75,338,578

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK

STATEMENTS OF EARNINGS

	<u>Year ended December 31,</u>	
	<u>1986</u>	<u>1985</u>
INTEREST INCOME:		
Interest on loans and other receivables	\$6,119,445	\$10,141,090
Interest on temporary investments	<u>165,143</u>	<u>362,767</u>
	6,284,588	10,503,857
INTEREST EXPENSE	3,765,900	6,267,003
LOSS ON ASSETS HELD FOR SALE	1,347	91,127
PROVISION FOR LOAN LOSSES	<u>50,470</u>	<u>1,234,930</u>
	<u>3,817,717</u>	<u>7,593,060</u>
	2,466,871	2,910,797
OTHER EXPENSES:		
Salaries and benefits	1,184,760	1,705,780
Occupancy expense	203,379	252,300
Depreciation and amortization	131,789	160,279
Professional fees	110,181	150,191
Advertising and promotion	67,861	79,922
Travel, lodging and meals	66,219	136,675
Office operations	62,722	126,717
Telephone and postage	40,484	87,238
Miscellaneous	36,522	50,554
Director's fees	<u>27,174</u>	<u>46,954</u>
	<u>1,931,091</u>	<u>2,796,610</u>
UNALLOCATED UNDISTRIBUTED PATRONAGE EARNINGS BEFORE INCOME TAX EXPENSE AND EXTRAORDINARY CREDIT	535,780	114,187
INCOME TAX EXPENSE	<u>226,300</u>	<u>32,200</u>
UNALLOCATED UNDISTRIBUTED PATRONAGE EARNINGS BEFORE EXTRAORDINARY CREDIT	309,480	81,987
EXTRAORDINARY CREDIT - UTILIZATION OF NET OPERATING LOSS CARRYFORWARD	<u>226,300</u>	<u>32,200</u>
UNALLOCATED UNDISTRIBUTED PATRONAGE EARNINGS	<u>\$ 535,780</u>	<u>\$ 114,187</u>

See notes to financial statements.

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK

STATEMENTS OF CHANGES IN CAPITAL
AND ALLOCATED/UNALLOCATED
UNDISTRIBUTED PATRONAGE EARNINGS (LOSS)

	<u>Share capital</u>	<u>C stock retirement pool</u>
Balance, January 1, 1985	\$31,808,880	\$ 10,260
Issuance (redemption) of stock during the year:		
Class B preferred stock, 29,332 shares, net	(2,933,200)	
Class A stock, 43 shares	430	
C stock retirement pool:		
Class B preferred stock assessments		171,398
Assessments receivable		(89,506)
Reduction in loan receivable on Class B preferred stock redemption	2,933,200	
Loan principal charged against allocated undistributed patronage earnings		
Unallocated undistributed patronage earnings		
Allocation to unallocated undistributed patronage loss		
	<hr/>	<hr/>
Balance, December 31, 1985	31,809,310	92,152
Issuance (redemption) of stock during the year:		
Class B preferred stock, 25,435 shares, net	(2,543,500)	
Class A stock, 44 shares	440	
Reduction in loans receivable on Class B preferred stock redemption	2,886,000	
C stock retirement pool:		
Class B preferred stock assessments		70,966
Assessments receivable		21,812
Loan principal charged against allocated undistributed patronage earnings		
Unallocated undistributed patronage earnings		
	<hr/>	<hr/>
Balance, December 31, 1986	<u>\$32,152,250</u>	<u>\$184,930</u>

See notes to financial statements.

<u>Capital in excess of par value</u>	<u>Contributed capital</u>	<u>Allocated undistributed patronage earnings</u>	<u>Unallocated undistributed patronage earnings</u>	<u>Unallocated undistributed patronage loss</u>	<u>Total</u>
\$79,110	\$144,626	\$4,514,237	\$ -	\$(9,977,776)	\$26,579,337
					(2,933,200)
3,870					4,300
					171,398
					(89,506)
					2,933,200
		(434,228)			(434,228)
			114,187		114,187
		<u>(3,034,644)</u>	<u>(114,187)</u>	<u>3,148,831</u>	
82,980	144,626	1,045,365		(6,828,945)	26,345,488
					(2,543,500)
3,960					4,400
					2,886,000
					70,966
					21,812
		(219,674)			(219,674)
			535,780		535,780
<u>\$86,940</u>	<u>\$144,626</u>	<u>\$ 825,691</u>	<u>\$535,780</u>	<u>\$(6,828,945)</u>	<u>\$27,101,272</u>

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK

STATEMENTS OF CHANGES IN FINANCIAL POSITION

	<u>Year ended December 31,</u>	
	<u>1986</u>	<u>1985</u>
SOURCE OF FUNDS:		
From operations -		
Unallocated undistributed patronage earnings	\$ 535,780	\$ 114,187
Items not requiring the use of funds:		
Depreciation and amortization	131,789	160,279
Provision for loan loss	50,470	1,234,930
Loss (gain) on sale of assets	683	(839)
	<hr/>	<hr/>
Funds provided from operations	718,722	1,508,557
Net proceeds from sale of assets	2,032	20,924
Net proceeds from stock issuance	4,400	4,300
Decrease in cash		16,558
Decrease in temporary investments		5,627,865
Decrease in acquired assets held for sale	1,523,157	755,141
Decrease in loans	21,515,111	28,869,727
Decrease in other assets	61,566	411,485
Decrease in accrued interest receivable	808,394	1,089,589
Increase in stock subscription payable	60,163	
Increase in Class B preferred stock assessments, net	92,778	81,892
Increase in Class B preferred stock	342,500	
	<hr/>	<hr/>
	<u>\$25,128,823</u>	<u>\$38,386,038</u>

See notes to financial statements.

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK

STATEMENTS OF CHANGES IN FINANCIAL POSITION
(continued)

	<u>Year ended December 31,</u>	
	<u>1986</u>	<u>1985</u>
USE OF FUNDS:		
Loans charged off, net of recoveries	\$ 200,574	\$ 3,111,420
Loan principal charged against allocated undistributed patronage earnings	219,674	434,228
Increase in cash	40,637	
Increase in temporary investments	950,000	
Increase in investment in Spokane Bank for Cooperatives	138,125	513,689
Increase in bank premises, furniture and equipment	14,874	3,637
Decrease in accounts payable and accrued expenses	116,038	64,000
Decrease in accrued interest payable	183,146	1,953,073
Decrease in notes payable	23,265,755	32,305,991
	<u>\$25,128,823</u>	<u>\$38,386,038</u>

See notes to financial statements.

ALASKA COMMERCIAL FISHING AND AGRICULTURE BANK

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 1986 AND 1985

NOTE A - SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES:

Operations -

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

CFAB is a cooperative corporation and intends to refund any allocated undistributed patronage earnings at such time as the Board of Directors finds that the financial condition of CFAB will so permit.

Interest on loans -

The accrual of income on loans is discontinued when interest or principal is contractually past due more than 90 days.

Patronage dividends -

Patronage dividends received from Spokane Bank for Cooperatives (SBC), of which CFAB is a member, reduce interest expense to SBC in the year declared.

Allowance for loan losses -

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

Acquired assets held for sale -

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

Bank premises, furniture and equipment -

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

Income taxes -

Amounts provided for income tax expense are based on earnings reported for financial statement purposes, rather than on the taxable income shown on the corporate income tax return. These amounts may differ because certain items are recorded as income or expense in different years for financial statement and tax return purposes.

NOTE B - LOANS:

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

	<u>December 31,</u>	
	<u>1986</u>	<u>1985</u>
Vessels	\$25,623,250	\$34,135,387
Fish processors	8,702,504	14,172,810
Agriculture and timber	7,596,991	16,221,453
Gear, entry permits and other	4,371,442	7,697,386
Other receivables	<u>1,826,138</u>	<u>294,400</u>
	48,120,325	72,521,436
Less loans receivable on Class B preferred stock	<u>(3,698,500)</u>	<u>(6,584,500)</u>
	44,421,825	65,936,936
Less allowance for loan losses	<u>(3,291,026)</u>	<u>(3,441,130)</u>
	<u>\$41,130,799</u>	<u>\$62,495,806</u>

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

	<u>December 31,</u>	
	<u>1986</u>	<u>1985</u>
Fish processors	\$ 4,441,655	\$ 5,246,914
Vessels	3,025,085	4,480,381
Agriculture and timber	7,569,743	3,740,558
Gear, entry permits and other	<u>2,286,902</u>	<u>2,185,492</u>
	<u>\$17,323,385</u>	<u>\$15,653,345</u>

Activity in the allowance for loan losses is as follows -

	<u>December 31,</u>	
	<u>1986</u>	<u>1985</u>
Balance at beginning of year	\$3,441,130	\$5,317,621
Charged to expense	50,470	1,234,929
Recoveries on loans previously charged off	<u>688,266</u>	<u>374,889</u>
	4,179,866	6,927,439
Loans charged off	<u>(888,840)</u>	<u>(3,486,309)</u>
Balance at end of year	<u>\$3,291,026</u>	<u>\$3,441,130</u>

CFAB serves the financial needs of the commercial fishing and agricultural industries in the State of Alaska. These industries are subject to seasonal and cyclical fluctuations which could affect the borrowers' ability to repay loans on a timely basis.

Loans to directors -

To qualify for election to the CFAB Board of Directors, an individual must be a borrowing member. Loans to members who serve on the Board of Directors must be approved by the SBC. Total loans to these members were \$141,247 and \$1,613,378 in 1986 and 1985, respectively.

NOTE C - TEMPORARY INVESTMENTS:

Temporary investments consisted of \$4,150,000 of farm credit bonds maturing at various dates in 1987, with interest rates ranging from 5.99% to 8.50% and certificates of deposit of \$3,200,000 with interest rates ranging from 8.45% to 8.52% at December 31, 1986 and 1985, respectively.

NOTE D - BANK PREMISES, FURNITURE
AND EQUIPMENT:

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

	<u>December 31,</u>	
	<u>1986</u>	<u>1985</u>
Furniture, fixtures and equipment	\$ 893,365	\$ 889,432
Leasehold improvements	<u>147,202</u>	<u>147,202</u>
	1,040,567	1,036,634
Less accumulated depreciation and amortization	<u>(688,693)</u>	<u>(565,131)</u>
	<u>\$ 351,874</u>	<u>\$ 471,503</u>

NOTE E - NOTES PAYABLE:

Notes payable consisted of -

	<u>December 31,</u>	
	<u>1986</u>	<u>1985</u>
SBC long-term notes with interest rates ranging from 10.54% to 11.75% maturing at various dates to January, 1993	\$25,000,000	\$28,000,000
SBC short-term notes and seasonal loan with interest rates ranging from 8.7% to 10.25% maturing at various dates in 1986		20,220,081
Other notes payable and capitalized equipment leases with various interest rates and maturity dates	<u>2,539</u>	<u>48,213</u>
	<u>\$25,002,539</u>	<u>\$48,268,294</u>

The loans are secured by substantially all CFAB assets.

Principal payments required on notes payable are as follows -

<u>Year ending December 31,</u>	<u>Amount</u>
1987	\$ -
1988	10,000,000
1989	10,000,000
1990	5,000,000

CFAB must invest in SBC's Class C stock in an amount equal to at least 5% of the cumulative average loan balance maintained with SBC. The amount of CFAB's investment in SBC's Class C stock and equity in allocated surplus was \$5,390,548 and \$5,252,423 at December 31, 1986 and 1985, respectively.

NOTE F - PENSION PLANS:

CFAB has pension plans covering substantially all employees. The total cost charged to operations for 1986 and 1985 was \$57,422 and \$58,372, respectively. The Board of Directors voted to terminate the floor retirement pension plan during 1986. The floor retirement plan provided for payments in the event the remaining pension plan was not sufficiently funded to meet actuarially computed retirement funding. As of December 31, 1985, the net assets available for benefits under the floor retirement plan was \$28,244. This amount will be refunded to CFAB upon the approval of termination by regulatory agencies. In accordance with generally accepted accounting principles, no gain will be recorded until the regulatory approval of the termination is obtained.

NOTE G - CAPITAL AND PATRONAGE EARNINGS:

Share capital -

Shares purchased by the State of Alaska must be repurchased by CFAB on or before July 20, 2000.

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

The following rights apply to the three categories of stock -

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

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

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

Unallocated undistributed patronage loss -

In accordance with Alaska Commercial Fishing and Agriculture Bank bylaws, the Board of Directors acted to reduce an unallocated undistributed patronage loss in the amount of \$9,977,776 as follows: 1) by allocating \$3,034,644 to allocated undistributed patronage earnings of prior years in 1985; and 2) by charging \$114,187 to 1985 unallocated undistributed patronage earnings. At December 31, 1986, the remaining unallocated undistributed patronage loss amount was \$6,828,945 (see Note I).

Class C stock repurchase plan -

In accordance with AS 44.81.010(b), on or before July 20, 2000, CFAB is required to repurchase its Class C stock issued to the State of Alaska. CFAB implemented a program requiring borrowers originating loans after December 12, 1983 to make an additional purchase of Class B stock for the assumed purpose of ultimately funding the repurchase of Class C stock. This plan was in effect until December 31, 1985. Notes originated after December 31, 1985, are not subject to this program but, are subject to new Class B stock requirements.

NOTE H - CONTINGENCIES AND COMMITMENTS:

Contingencies -

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

Commitments -

CFAB has entered into certain noncancelable long-term operating lease agreements for buildings. Rental expense under these leases totaled \$192,450 and \$231,549 for the years ended December 31, 1986 and 1985, respectively. Minimum annual lease payments are as follows -

<u>Year ending December 31,</u>	<u>Amount</u>
1987	\$201,000
1988	182,000
1989	174,000
1990	43,000

NOTE I - SUBSEQUENT EVENT:

On March 2, 1987, in accordance with Alaska Commercial Fishing and Agriculture Bank bylaws, the Board of Directors acted to reduce the unallocated undistributed patronage loss by charging \$321,468 to 1986 unallocated undistributed patronage earnings. The remaining unallocated undistributed patronage loss is \$6,507,477.

In addition, the Board of Directors approved an allocation of 1986 patronage earnings totaling \$214,312 to 1986 patrons. This allocation is to be distributed in cash on or before April 1, 1987.

APR 13 1987

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As we review the developments and results of CFAB's 1986 operations, and prepare to discuss them with members, we are reminded of the question, "Is the glass half-empty or is it half-full?"

For CFAB, the question must be, "Was 1986 a partial success or was it a partial failure?" Many objectives were attained or exceeded in 1986, and there is no doubt that by any conventional measurement CFAB is financially stronger today than a year ago. However, some goals were not met, and the effort to provide financing and services to members at a currently reasonable cost remains a difficult challenge. In these next few pages, we will share with you the major events and developments of the past year.

PMS 561
"The Board of Directors has concluded to return 40 percent of the 1986 margins to its 1986 patrons in the form of a cash patronage refund."

A particular point of satisfaction is the 1986 net operating results — a margin of \$535,780. While that is not a large amount, it compares favorably with the disastrous 1984 loss of \$100 million and the modest \$114,000 margin of 1985. Because CFAB is a cooperative and its net margins are applied to the benefit of the borrower-owners whose patronage produces those margins, we do not operate CFAB toward an objective of large net margins; nevertheless, it is critical that policies established and implemented throughout the entire year be directed toward assuring that there be some net margin, however modest, remaining at December 31.

Consistent with the foregoing and with CFAB's Bylaws, the Board of Directors has concluded to return 40 percent of the 1986 margins to its 1986 patrons in the form of a cash patronage refund. Checks totaling \$214,312 and equal to about 3-1/2 percent of the 1986 interest paid will be mailed to affected borrower-owners by April 1, 1987. The remainder of the 1986 margins has been applied to reduce the unallocated and undistributed patronage loss remaining from 1984 operations.

PMS 561
"Actual operating expenses totaled \$1,931,000, the lowest of any of the six full years of operations."

It is not possible to identify single and specific events or circumstances which created the 1986 margin. It is the result of many interrelated developments. However, it is possible and rational to identify many factors without which the margin would not have been achieved. One such factor is CFAB's operating expenses, or "overhead." A year ago we reported that those expenses for 1985 had been reduced by nearly \$400,000 from CFAB's four-year average of \$3.2 million, and said that for 1986, "...we are striving for a further reduction of \$500,000 to \$600,000..." Our objective was \$2.2 to \$2.3 million — actual operating expenses totaled \$1,931,000, the lowest of any of the six full years of operations. While the Board of Directors and management of CFAB provide basic direction and leadership in pursuit of such objectives, they cannot be achieved or exceeded without the constant and committed efforts of every CFAB staff member. We applaud the performance of CFAB's employees; they are worthy of high regard by all borrower-owners.

PMS 561
"There is no more pervasive and negative influence on CFAB and on the demands it must make of its performing, interest-paying, borrowers than the level of non-performing loans."

A major 1986 disappointment was CFAB's inability to significantly reduce the dollar level of non-earning loans. (A non-earning loan is one on which a contractual payment is delinquent by 90 days or more and/or which CFAB's management has reason to believe represents a continuing and serious problem.) Non-earning loans totaled \$15,653,345 at December 31, 1985, and \$17,321,385 a year later. The relative closeness of those numbers suggests inactivity and is somewhat misleading. The actual changes which occurred are better illustrated by the following reconciliation:

\$15,653,345	Non-earning loans at December 31, 1985
6,909,019	Balances which became non-earning during 1986
(594,663)	Balances charged off during 1986
(4,644,316)	Balances collected or restructured during 1986
<u>\$17,321,385</u>	Non-earning loans at December 31, 1986

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There is no more pervasive and negative influence on CFAB and on the demands it must make of its performing, interest-paying, borrowers than the level of non-performing loans. That aggregate balance effectively represents funds which CFAB has borrowed and on which it must pay monthly interest in cash — since CFAB's only source of cash income is interest on performing loans, there is no alternative but to maintain interest rates at a level which is perceived by many borrowers as excessive. Whether or not that perception is realistic, it is a cause for many difficult discussions between CFAB and its members.

PNIS 561

"The single greatest concern of CFAB's borrower-owners is its interest requirement."

We characterize those discussions as "difficult" because first, we understand and are totally sympathetic to members' points of view. On the other hand, we are unable to offer a response other than to say that CFAB is totally committed to correcting the problems which impose the current burdens on its operations. There are no external sources of relief to which CFAB can turn, or which it can share with its members. Rehabilitation of CFAB can only be achieved through the liquidation or restructuring of its non-earning assets. While that purpose receives constant attention, a frustrating reality is that, in general, results cannot be obtained through CFAB's efforts alone; other parties or processes hold a great deal of control. The \$17.3 million of non-performing balances involves a total of 67 loans, but over \$13.1 million of it is in 23 loans to only ten individual borrowers! In most of the cases, the borrowers are currently under the protection of a Bankruptcy Court or are otherwise embroiled in complex litigation. CFAB's attention to these accounts is both necessary and costly; but that attention by itself cannot force the resolution of the matters involved.

This aspect of CFAB's circumstances is addressed at some length because it is clear that the single greatest concern of CFAB's borrower-owners is its interest requirement. That interest requirement is directly related to the amount and status of non-earning loans. For example, if only half of the \$13.1 million in the 23 loans mentioned above were restored to an earning status, CFAB's interest requirement on an annualized basis could be translated into an overall rate reduction of as much as 2-1/2 percent! There is no mystery or complexity involved, and there is no other response we can offer to borrower-owners' concerns.

"At December 31, 1986, CFAB's investment in SBC totaled nearly \$5.4 million dollars."

Another serious and unforeseen threat to CFAB's recovery efforts appeared during 1986, related to circumstances far from Alaska and not at all associated with CFAB's own markets. It relates to the trends and developments in U.S. agriculture generally and, in particular, within the Federal Farm Credit System which has provided credit to agriculture for 70 years. CFAB was established and structured specifically to seek its financing from that System. Since 1980, CFAB has obtained a major part of its loanable funds through borrowings from the Spokane Bank for Cooperatives (SBC), one of 37 banks of the System. SBC is itself a cooperative, and CFAB has been required to invest capital in SBC in the same manner as borrowing members invest in CFAB.

At December 31, 1986, CFAB's investment in SBC totaled nearly \$5.4 million dollars. Under the circumstances which have prevailed in the past, CFAB would expect that amount to be returned to it in cash in the years subsequent to 1988. However, the dramatic and rapid deterioration of the Farm Credit System as a whole during 1984 to 1986, coupled with the effects of legislation passed by the U.S. Congress in December 1985, suggests that the liquidity of the Spokane Bank for Cooperatives has been or soon will be drastically affected. This will not only affect SBC's ability to retire capital as in the past, but will also tend to force it to maintain interest rates — and therefore CFAB's costs — at a relatively high level.

"...The first investment of true equity by members."

1986 also brought more satisfying and promising developments to discuss with members. Effective January 1, 1986, CFAB's revised Class B Preferred Stock program was established and has been well received. Borrower-owners actually purchased \$342,500 of Class B Preferred Stock during 1986. That is perhaps a modest amount in total, but it is the first investment of true equity by members; and the amount will increase substantially as CFAB grows over the next few years.

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Another new program for 1986 which has proven especially useful and attractive is that which involves a modified level payment plan for term loans. In the past, repayment of term loans was usually structured to involve equal annual increments of principal plus an interest payment. It was difficult for the borrower to project an annual payment amount more than a year ahead, and it also resulted in the highest payments required in the earliest years of what was often a new venture. Under the modified level payment plan, payments are fixed in three-year increments throughout the life of the loan. The resulting ease of budgeting for the borrower has made this program even more successful than was contemplated at its introduction.

CFAB also in 1986 introduced and refined a differential interest rate program. This program incorporates a careful and objective analysis of each individual applicant's creditworthiness within the context of his specific loan request. Every applicant is evaluated against identical standards: to the extent that an applicant's history and circumstances clearly represent a better-than-average credit risk, he is offered an interest rate somewhat lower than CFAB's normal rate. This program is available to, and has been applied to, existing loan accounts as well as to new applicants.

Effective June 1, 1986, CFAB's base interest rate — and therefore the interest rate on most CFAB loans — was reduced by 1/2 percent. Coupled with the cash patronage refund mentioned earlier, 1986 patrons' net costs of borrowing were reduced in a meaningful way from those of 1985.

PMS 561
"The 1987 Annual Meeting will be held in three sessions, also, in October — at Sitka, Anchorage, and Kodiak. We urge your attendance!"

CFAB's 1986 Annual Meeting was held in three sessions — one each in Ketchikan, Anchorage, and Cordova. The basic purpose of that format was to permit and encour-

age attendance by a broader range of members than is possible with a single meeting date and location. The meeting sessions themselves were relatively informal and the members in attendance were able to participate with constructive and challenging questions and observations to the Board of Directors and CFAB's management. Although it was clear that many members (relative to CFAB's total membership) are not yet inclined to take advantage of this unique opportunity to exercise the rights and privileges of their ownership of CFAB, we were encouraged by the participation. The 1987 Annual Meeting will be held in three sessions, also, in October — at Sitka, Anchorage, and Kodiak. We urge your attendance!

One of the important items of business transacted in the 1986 Annual Meeting was the adoption of amendments to CFAB's Articles of Incorporation. The most significant part of that was a re-expression of the powers and authorities of CFAB. The original language of that section was essentially a repetition of the provisions of CFAB's statute (AS44.811); this created, or had the potential for creating, inconsistencies if and as that statute is amended. The revised language now provides for CFAB to engage in essentially "whatever businesses and activities the law permits."

"In terms of numbers, there was also a significant change to CFAB's Board of Directors in 1986:"

In terms of numbers, there was also a significant change to CFAB's Board of Directors in 1986. In February, Governor Sheffield appointed Anchorage businessman Henry Klin to fill the longstanding vacancy in one of the two appointed seats. In April, the Governor also appointed Gil Cunderson of Juneau to replace Bob Waldrop of Ketchikan, whose term had expired. Also in April, Founding Director and former Chairperson Roseleen Moore of Homer resigned from her elected seat. The Board appointed Mr. Waldrop to serve in Mrs. Moore's position until the Annual Meeting. Due to coincidental circumstances, all five of the elected Director positions were subject to contest at the 1986 Annual Meeting: Director Tommy Thompson, Sitka, and Founding Director

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Dale Pihlman of Ketchikan had declined nomination for re-election to their seats. At the Annual Meeting, Mr. Waldrop and Harvey Samuelsen, Dillingham, were elected to three-year terms; Dean Paddock of Juneau and Paul Huppert, Palmer, were elected to two-year terms; and Alan Olness of Petersburg was elected to a one-year term. The stature and total number of candidates were gratifying. The net effect is the loss to members of the experience and commitment of Mrs. Moore, Mr. Pihlman, and Mr. Thompson, with the gain of the dedication and new perspectives of Messrs. Kim, Gunderson, Paddock, and Olness. In its own annual organizational process, the Board elected Mr. Gunderson Secretary-Treasurer of CFAB, Mr. Waldrop to the position of Vice Chairman, and Mr. Huppert to once again serve as Chairman.

PMS 561 "One of its critical needs is for...the philosophies and attitudes of 'owners of a business'..."

CFAB is a cooperative. Its owners are its customers, and only its customers can become owners. That structure lends itself to pronouncements and philosophical expressions which are often dismissed as trite. Moreover, because CFAB is a credit cooperative, its relationship with each customer is pervasive, highly subjective, and precise — measured to the last penny! The rights, privileges, and responsibilities of ownership are much more difficult to define and to pursue. There are no immediate and measurable benefits or other results to the exercise of ownership rights. Nevertheless, unless there is a viable and active ownership base in place able and willing to express its directions and expectations to CFAB's Board of Direc-

tors and management with regard to the total operations of the institution, the only guidance available to us is the language of a statute written nine years ago.

CFAB is in a period of change and of accommodating the realities which have become apparent during its brief life; a period of recovering from adversity while attempting to generate from within the resources to build for the future. One of its critical needs is for a body of members with the philosophies and attitudes of "owners of a business" rather than of "customers with a vote." Again, we urge you to participate in the election of a director later in 1987, to attend an Annual Meeting session in Sitka, Anchorage, or Kodiak, and to seek and take advantage of opportunities to communicate with your directors and management about CFAB as a business. Whether or not you are personally acquainted with one or more of CFAB's Directors, please do not hesitate to contact any of them to discuss your concerns, questions, or observations about CFAB.

Paul A. Huppert

Paul A. Huppert - PMS 561

Chairman, Board of Directors

Edward E. Crane

Edward E. Crane - 561

President

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CFAB's only significant business activity is the extension and administration of loans to Alaska's fishing, farming, and timber industries. Each of CFAB's resources is committed to support that primary activity.

Over the past two years, the liquidation, restructuring, or other resolution of non-performing loans have absorbed a great deal of CFAB energy. Also, the very existence of such loans has created and imposed unusual requirements on performing borrowers. Those requirements have in turn resulted in the loss of loan accounts and opportunities in those instances in which the borrowers or applicants have alternative financing available. Those circumstances are discussed more comprehensively in the Executive Message of this Annual Report. The principal effect has been a sharp decline in CFAB's gross loan volume from \$94.8 million at December 31, 1984, to \$65.9 million a year later, and to \$44.4 million at the end of 1986.

That net reduction is only part of the story, however. CFAB's new loan actions continued in 1986 at a pace much like that of 1985. There were 105 new loans made, totaling \$11,508,000. Of that amount, \$7,825,000 was "new" money, with the remainder being refinancing of loan balances already outstanding on CFAB's books. Slightly less than half, or 46, of the new loans were to new CFAB members; the other 59 new loans were to borrowers who already were, or had been, active CFAB members.

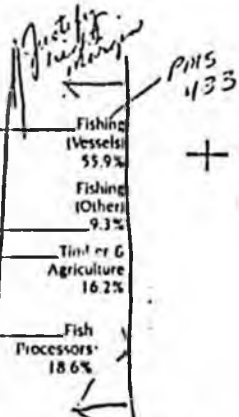
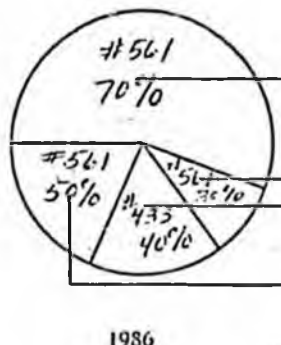
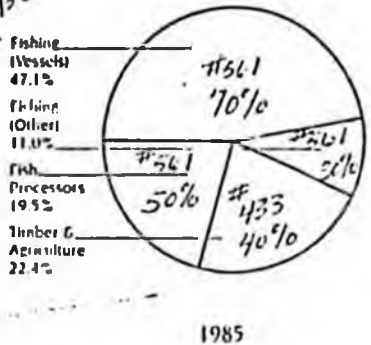
The graphics below show the relative composition of CFAB's loan portfolio at the two most recent year-ends. It continues to be clear that CFAB is an important source of

vessel financing for Alaska fishermen. There is also a noticeable increase in demand for the financing of Limited Entry Permit purchases, particularly for diversification into new fisheries. CFAB is the only private institution which has the legal authority to make such a loan and to accept the permit itself as security. Unfortunately certain restrictions expressed in CFAB's statute and not related to credit considerations have severely limited the range of commercial fishermen to whom CFAB may make such loans.

As discussed in the 1985 Annual Report, CFAB cannot assert that its lending activities have broad effects on the industries it is mandated to serve. The effects tend to be localized and, more specifically, focused on individual borrowers. The most generalized implications of CFAB's presence and ability to offer financing are felt by all fishermen as a result of the competitive pressures imposed on alternative loan sources.

The charts below are somewhat distorted by the consolidation of "Timber & Agriculture" for the sake of simplicity. CFAB has had no new farm loan activity for the past two years. This appears to be the result of two primary factors: (a) The State's own agricultural loan program which offers subsidized financing, particularly for developmental activities; and (b) the relatively strong and stable circumstances of long-established farm operators, whose needs for short-term production financing are also served by the State's programs. The State's posture and capacities appear to be changing, and it seems possible that 1987 will present new agricultural financing opportunities and requirements for CFAB.

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See last year



Board of Directors
Alaska Commercial Fishing and
Agriculture Bank
Anchorage, Alaska

We have examined the balance sheets of Alaska Commercial Fishing and Agriculture Bank as of December 31, 1986 and 1985, and the related statements of earnings, changes in capital and allocated/unallocated undistributed patronage earnings (loss), and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Alaska Commercial Fishing and Agriculture Bank as of December 31, 1986 and 1985, and the results of its operations and the changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Touche Ross & Co.

Certified Public Accountants
January 23, 1987
(March 2, 1987 as to Note 1)

^{PMS 561}

ALASKA COMMERCIAL FISHING & AGRICULTURE BANK *fm 5/33*
Balance Sheets *561*

Exhibit 1133

	December 31,	
	1986	1985
Assets		
Cash	\$ 147,410	\$ 106,773
Temporary investments	4,150,000	3,200,000
Loans and other receivables, net of allowance for loan losses of \$3,291,026 and \$1,441,130	41,130,799	62,495,806
Accrued interest receivable:		
Temporary investments	4,700	44,144
Loans and other receivables	1,302,252	2,071,202
	<u>1,306,952</u>	<u>2,115,346</u>
Investment in Spokane Bank for Cooperatives	5,390,548	5,252,423
Bank premises, furniture and equipment, net	351,874	471,503
Acquired assets held for sale	83,007	1,606,164
Other assets	28,797	90,563
	<u>\$52,589,587</u>	<u>\$75,338,578</u>
Liabilities		
Accounts payable and accrued expenses	\$ 191,979	\$ 308,016
Accrued interest payable	233,634	416,780
Class B preferred stock subscriptions	60,163	
Notes payable	25,002,539	48,268,294
	<u>25,488,315</u>	<u>48,993,090</u>
Commitments and Contingent Liabilities (Note H)		
Capital and Patronage Earnings:		
Share capital—		
Class C special preferred stock, \$10,000 par value, authorized 4,000 shares, outstanding 3,180 shares	31,800,000	31,800,000
Class B preferred stock, \$100 par value, authorized 400,000 shares, outstanding 40,410 and 65,845 shares	4,041,000	6,584,500
Loans receivable on Class B preferred stock	(3,698,500)	(6,584,500)
Class A membership stock, \$10 par value, authorized 10,000 shares, outstanding 975 and 931 shares	9,750	9,310
	<u>32,152,250</u>	<u>31,809,310</u>
C Stock retirement pool	184,930	92,152
Capital in excess of par value	86,940	82,980
Contributed capital	144,626	144,626
	<u>32,568,746</u>	<u>32,129,068</u>
Allocated undistributed patronage earnings	825,691	1,045,365
Unallocated undistributed patronage earnings	535,780	
Unallocated undistributed patronage loss	(6,828,945)	(6,828,945)
	<u>27,101,272</u>	<u>26,345,488</u>
	<u>\$52,589,587</u>	<u>\$75,338,578</u>

See notes to financial statements

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ALASKA COMMERCIAL FISHING & AGRICULTURE BANK ^{7/13/83}
Statements of Earnings ^{Net}

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	Year Ended December 31,	
	1986	1985
Interest Income:		
Interest on loans and other receivables	\$ 6,119,445	\$10,141,090
Interest on temporary investments	165,143	362,767
	<u>6,284,588</u>	<u>10,503,857</u>
Interest expense	3,763,900	6,267,003
Loss on assets held for sale	1,347	91,127
Provision for loan losses	50,470	1,234,930
	<u>3,817,717</u>	<u>7,593,060</u>
	<u>2,466,871</u>	<u>2,910,797</u>
Other Expenses:		
Salaries and benefits	1,184,760	1,705,780
Occupancy expense	203,379	252,300
Depreciation and amortization	131,789	160,279
Professional fees	110,181	150,191
Advertising and promotion	67,861	79,922
Travel, lodging and meals	66,219	136,675
Office operations	62,722	126,717
Telephone and postage	40,484	87,238
Miscellaneous	36,522	50,554
Directors' fees	27,174	46,954
	<u>1,931,091</u>	<u>2,796,610</u>
Unallocated undistributed patronage earnings before income tax expense and extraordinary credit	533,780	114,187
Income tax expense	226,300	32,200
Unallocated undistributed patronage earnings before extraordinary credit	309,480	81,987
Extraordinary credit - utilization of net operating loss carry forward	226,300	32,200
Unallocated undistributed patronage earnings	<u>\$ 533,780</u>	<u>\$ 114,187</u>

See notes to financial statements

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7-133
Statements of Changes in Capital and Allocated / Unallocated Undistributed

541 Patronage Earnings (Loss)

Part 1
 1133

	Share Capital	C Stock Retirement Pool	Capital In Excess Of Par Value	Contributed Capital	Allocated Undistributed Patronage Earnings	Unallocated Undistributed Patronage Earnings	Unallocated Undistributed Patronage Loss	Total
Balance, January 1, 1985	\$31,808,880	\$ 10,260	\$79,110	\$144,626	\$4,514,237	\$ -	\$ (9,977,776)	\$26,579,337
Issuance (redemption) of stock during the year:								
Class B preferred stock, 29,332 shares, net	(2,933,200)							(2,933,200)
Class A stock, 43 shares	430		3,870					4,300
C stock retirement pool:								
Class B preferred stock assessments		171,398						171,398
Assessments receivable		(89,506)						(89,506)
Reduction in loan receivable on Class B preferred stock redemption	2,933,200							2,933,200
Loan principal charged against allocated undistributed patronage earnings					(434,228)			(434,228)
Unallocated undistributed patronage earnings						114,187		114,187
Allocation to unallocated undistributed patronage loss								
Balance, December 31, 1985	31,809,310	92,152	82,980	144,626	13,034,644	(114,187)	3,148,831	26,345,488
Issuance (redemption) of stock during the year:								
Class B preferred stock, 25,435 shares, net	(2,543,500)							(2,543,500)
Class A stock, 44 shares	440		3,960					4,400
Reduction in loans receivable on Class B preferred stock redemption	2,886,000							2,886,000
C stock retirement pool:								
Class B preferred stock assessments		70,966						70,966
Assessments receivable		21,812						21,812
Loan principal charged against allocated undistributed patronage earnings					(219,674)			(219,674)
Unallocated undistributed patronage earnings						535,780		535,780
Balance, December 31, 1986	\$32,152,250	\$184,930	\$86,940	\$144,626	\$ 825,691	\$535,780	\$ (6,828,945)	\$27,101,272

Change in share capital

See notes to financial statements

Statements of Changes in Financial Position ^{>133} _{>541 ✓}

	Year Ended December 31.	
	1986	1985
Source of Funds:		
From Operations:		
Unallocated undistributed patronage earnings	\$ 535,780	\$ 114,187
Items not requiring the use of funds:		
Depreciation and amortization	131,789	160,279
Provision for loan loss	50,470	1,224,930
Loss (gain) on sale of assets	683	(839)
Funds provided from operations	718,722	1,508,557
Net proceeds from sale of assets	2,032	20,924
Net proceeds from stock issuance	4,400	4,300
Decrease in cash		16,558
Decrease in temporary investments		5,627,865
Decrease in acquired assets held for sale	1,523,157	755,141
Decrease in loans	21,515,111	28,869,727
Decrease in other assets	61,566	411,485
Decrease in accrued interest receivable	808,394	1,089,589
Increase in stock subscription payable	60,163	
Increase in Class B preferred stock assessments, net	92,778	81,892
Increase in Class B preferred stock	342,500	
	<u>\$25,128,823</u>	<u>\$38,386,038</u>
Use of Funds:		
Loans charged off, net of recoveries	\$ 200,574	\$ 3,111,420
Loan principal charged against allocated undistributed patronage earnings	219,674	434,228
Increase in cash	40,637	
Increase in temporary investments	950,000	
Increase in investment in Spokane Bank for Cooperatives	138,125	513,689
Increase in bank premises, furniture and equipment	14,874	3,637
Decrease in accounts payable and accrued expenses	116,038	64,000
Decrease in accrued interest payable	183,146	1,953,073
Decrease in notes payable	23,265,755	32,305,991
	<u>\$25,128,823</u>	<u>\$38,386,038</u>

See notes to financial statements

Years Ended December 31, 1986 and 1985

Note A - Summary of Significant Accounting Policies:

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

CFAB is a cooperative corporation and intends to refund any allocated undistributed patronage earnings at such time as the Board of Directors finds that the financial condition of CFAB will so permit.

Interest on loans: The accrual of income on loans is discontinued when interest or principal is contractually past due more than 90 days.

Patronage dividends: Patronage dividends received from Spokane Bank for Cooperatives (SBC), of which CFAB is a member, reduce interest expense to SBC in the year declared.

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

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

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

property, the cost and accumulated depreciation are removed from the respective accounts and the resulting gain or loss recorded.

Income taxes: Amounts provided for income tax expense are based on earnings reported for financial statement purposes, rather than on the taxable income shown on the corporate income tax return. These amounts may differ because certain items are recorded as income or expense in different years for financial statement and tax return purposes.

Note B - Loans:

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

	December 31,	
	1986	1985
Vessels	\$25,623,250	\$34,135,387
Fish processors	8,702,504	14,172,810
Agriculture and timber	7,596,991	16,221,453
Gear, entry permits, and other	4,371,442	7,697,386
Other receivables	1,826,138	294,400
	<u>48,120,325</u>	<u>72,521,436</u>
Less loans receivable on Class B preferred stock	(3,698,500)	(6,584,500)
	<u>44,421,825</u>	<u>65,936,936</u>
Less allowance for loan losses	(3,291,026)	(3,441,130)
	<u>\$41,130,799</u>	<u>\$62,495,806</u>

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

	December 31,	
	1986	1985
Fish processors	\$ 4,441,655	\$ 5,246,914
Vessels	3,025,085	4,480,781
Agriculture and timber	7,569,743	3,740,558
Gear, entry permits and other	2,286,902	2,185,492
	<u>\$17,323,385</u>	<u>\$15,653,345</u>

Activity in the allowance for loan losses is as follows:

	December 31,	
	1986	1985
Balance at beginning of year	\$ 3,441,130	\$ 5,317,621
Charged to expense	50,470	1,234,929
Recoveries on loans previously charged off ..	688,266	374,859
	<u>4,179,866</u>	<u>6,927,439</u>
Loans charged off	(888,840)	(3,486,309)
Balance at end of year ...	<u>\$ 3,291,026</u>	<u>\$ 3,441,130</u>

CFAB serves the financial needs of the commercial fishing and agricultural industries in the State of Alaska. These industries are subject to seasonal and cyclical fluctuations which could affect the borrowers' ability to repay loans on a timely basis.

Loans to directors: To qualify for election to the CFAB Board of Directors, an individual must be a borrowing member. Loans to members who serve on the Board of Directors must be approved by the SBC. Total loans to these members were \$141,247 and \$1,613,378 in 1986 and 1985, respectively.

Note E — Notes Payable:

Notes payable consisted of the following:

	December 31,	
	1986	1985
Spokane Bank for Cooperatives (SBC) long-term notes with interest rates ranging from 10.544% to 11.75% maturing at various dates to January, 1993	\$25,000,000	\$28,000,000
SBC short-term notes and seasonal loan with interest rates ranging from 8.7% to 10.25% maturing at various dates in 1986		20,220,081
Other notes payable and capitalized equipment leases with various interest rates and maturity dates	<u>2,539</u>	<u>48,213</u>
	<u>\$25,002,539</u>	<u>\$48,268,294</u>

The loans are secured by substantially all CFAB assets

Note C — Temporary Investments:

Temporary investments consisted of \$4,150,000 of Farm Credit Bonds maturing at various dates in 1987, with interest rates ranging from 5.99% to 8.50% and certificates of deposit of \$3,200,000 with interest rates ranging from 8.45% to 8.52% at December 31, 1986 and 1985, respectively.

Note D — Bank Premises, Furniture and Equipment:

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

	December 31,	
	1986	1985
Furniture, fixtures and equipment	\$ 893,365	\$ 889,432
Leasehold improvements ..	<u>147,202</u>	<u>147,202</u>
	1,040,567	1,036,634
Less accumulated depreciation and amortization ..	<u>(688,693)</u>	<u>(565,131)</u>
	<u>\$ 351,874</u>	<u>\$ 471,503</u>

Principal payments required on notes payable are as follows:

Year Ending December 31,	Amount
1987	\$ -
1988	10,000,000
1989	10,000,000
1990	5,000,000

CFAB must invest in SBC's Class C stock in an amount equal to at least 5% of the cumulative average loan balance maintained with SBC. The amount of CFAB's investment in SBC's Class C stock and equity in allocated surplus was \$5,390,548 and \$5,252,423 at December 31, 1986 and 1985, respectively.

Note F — Pension Plans:

CFAB has pension plans covering substantially all employees. The total cost charged to operations for 1986 and 1985 was \$57,422 and \$58,372, respectively. The Board of Directors voted to terminate the floor retirement pension plan during 1986. The floor retirement pension plan provided for payments in the event the remaining pension plan was not sufficiently funded to meet actuarially computed retirement funding. As of December 31, 1985, the net assets available for benefits under the floor retirement plan was \$28,244. This amount will be refunded to CFAB upon the approval of termination by regulatory agencies. In accordance with generally accepted accounting principles, no gain will be recorded until the regulatory approval of the termination is obtained.

Note G — Capital and Patronage Earnings:

State Capital: Shares purchased by the State of Alaska must be repurchased by CFAB on or before July 20, 2000.

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

The following rights apply to the three categories of stock:

- Class C - No voting or dividend rights. May only be issued to the State of Alaska.
- Class B - No voting rights. Class B stock may only be held by members of CFAB. Prior to December 31, 1985, all loans required a purchase of Class B stock in an amount equal to 10% of the loan balance; however, this purchase was not funded but was evidenced by notes. On loans made subsequent to December 31, 1985, each borrower is required to make a cash purchase of Class B stock in an amount equal to 5% of the total loan. This investment will remain in place until retired by the Board of Directors.
- Class A - No dividend rights. Each member of CFAB must own one share of Class A stock. Each share of stock carries one vote. To vote a member must be engaged in commercial fishing or agriculture and must be a current borrower or have borrowed from CFAB during the preceding two years or have a minimum retained patronage earnings with CFAB of \$2,500.

*Part 4
4/3/83*

Unallocated Undistributed Patronage Loss: In accordance with Alaska Commercial Fishing and Agriculture Bank bylaws, the Board of Directors acted to reduce an unallocated undistributed patronage loss in the amount of \$9,977,776 as follows: 1) by allocating \$3,034,644 to allocated undistributed patronage earnings of prior years in 1985; and 2) by charging \$114,187 to 1985 unallocated undistributed patronage earnings. At December 31, 1986, the remaining unallocated undistributed patronage loss amount was \$6,828,945 (see Note I).

Class C Stock Repurchase Plan: In accordance with AS 44.81.010(b), on or before July 20, 2000, CFAB is required to repurchase its Class C stock issued to the State of Alaska. CFAB implemented a program requiring borrowers originating loans after December 12, 1983 to make an additional purchase of Class B stock for the assumed purpose of ultimately funding the repurchase of Class C stock. This plan was in effect until December 31, 1985. Notes originated after December 31, 1985, are not subject to this program but are subject to new Class B stock requirements.

Note H — Contingencies and Commitments:

Contingencies: CFAB is a defendant in several legal actions arising from normal business activities including actions related to delinquent loans and foreclosures. CFAB reserves for potential losses on delinquent loans as described in Note A. As to litigation outside of delinquencies and foreclosures, management believes that those

actions are without merit or that the ultimate liability, if any, resulting from them will not materially affect CFAB's financial position or its results of operations.

Commitments: CFAB has entered into certain noncancelable long-term operating lease agreements for buildings. Rental expense under these leases totaled \$192,150 and \$231,549 for the years ended December 31, 1986 and 1985, respectively. Minimum annual lease payments are as follows:

<u>Year Ending December 31,</u>	<u>Amount</u>
1987	\$201,000
1988	182,000
1989	174,000
1990	43,000

Note I - Subsequent Event:

On March 2, 1987, in accordance with Alaska Commercial Fishing and Agriculture Bank bylaws, the Board of Directors acted to reduce the unallocated undistributed patronage loss by charging \$321,468 to 1986 unallocated undistributed patronage earnings. The remaining unallocated undistributed patronage loss is \$6,507,477.

In addition, the Board of Directors approved an allocation of 1986 patronage earnings totaling \$214,312 to 1986 patrons. This allocation is to be distributed in cash on or before April 1, 1987.

Board of Directors and Staff

W. L. ...

Board of Directors

- Paul A. Huppert
Chairman
- Robert Waldrop
Vice Chairman
- Gilbert Gunderson
Secretary/Treasurer
- Hyoung "Henry" Kim
Director
- Alan D. Otness
Director
- Dean Padlock
Director
- Harvey Samuelson
Director

Staff

- Iver H. Amundsen
Assistant Vice President
- ~~Karol A. Askerman~~
~~Assistant Vice President~~
- Karl D. Barnard
Vice President
- Dan A. Berkshire
Assistant Vice President
- Cynthia D. Blush
Senior Bookkeeper
- Darleen S. Church
Vice President
- Robert H. Clark
Assistant Vice President
- Edward E. Crane
President
- John W. Enge
Fisheries Analyst
- A. W. Hall
Business Development Officer
- Lela F. Hart
Assistant Vice President
- Sharon A. Morgan
Administrative Support Secretary
- Deanne L. Osha
Documentation & Information Specialist
- Dayra R. Presley
Communications Manager
- Judy A. Ouling
Administrative Support Clerk
- David G. Rogers
Senior Vice President
- Chianne G. Sanchez
Executive Secretary
- Douglas W. Sindt
Data Processing Supervisor
- Lora C. Smith
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- Deborah A. Tosch
Documentation Paralegal
- Godelieve C. Van Lint
Administrative Support Clerk
- DeLories M. vonGemmingen
Executive Secretary

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