Alaska Industrial Development and Export Authority
BOARD MEETING MINUTES
February 23, 2011
Anchorage, Alaska

1. CALL TO ORDER

Chairman Felix called the meeting of the Alaska Industrial Development and Export Authority to order on February 23, 2011, at 10:05 a.m. A quorum was established.

2. ROLL CALL: BOARD

Members present in Anchorage: Acting Chair Michael T. Felix (Public Member); Susan K. Bell (Commissioner, Department of Commerce, Community, and Economic Development); Bryan Butcher (Commissioner, Department of Revenue); Ronald G. Arvin (Public Member); Robert D. Sheldon (Public Member); Hugh S. Short (Public Member); Gary R. Wilken (Public Member).

3. AGENDA APPROVAL

The agenda was approved as presented.

MOTION: Mr. Wilken moved to approve the agenda. Seconded by Commissioner Bell. There being no objections, the motion passed.

4. ROLL CALL: STAFF, PUBLIC

Staff present in Anchorage: Ted Leonard (AIDEA Executive Director); Chris Anderson (Deputy Director-Commercial Finance); Brian Bjorkquist (Department of Law); Sara Fisher-Goad (AEA Executive Director); Jim Hemsath (Deputy Director-Development Finance); Valorie Walker (Deputy Director-Finance); Judy Bradshaw (Clerk AEA); Sandy Burrows (Administrative Assistant AIDEA); Shauna Howell (Executive Assistant AEA); Shelby Weems (Accountant V AIDEA); Teri Webster (Administrative Assistant AIDEA); Sherri Siverson (Executive Assistant AIDEA).

Others present: Pat Clancy, Gordon Davis and Mark Gardiner (Western Financial Group); Kelly Cliff (Callan Associates); Paul D. Kendall (Public).

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5. PUBLIC COMMENTS

There were no public comments.

6. WORK SESSION FOR NEW BOARD MEMBERS

Mr. Leonard gave an overview of the work session: The Legislature and the Governor expressed a need for more private sector involvement in managing the state's economic development. As a result, the board has been increased to seven members and the composition changed to five private sector members and two commissioners. Mr. Leonard reviewed the history of the Strategic Planning Initiative. Mr. Leonard stated that when he was first hired, he was charged with three goals: to increase AIDEA's profile, to make AIDEA's loan programs more effective and utilized, and to start building and owning projects. Mr. Leonard indicated that as staff analyzed the situation, it was found that AIDEA had a talented workforce and the financial capacity to implement the structures and programs needed. However, AIDEA did not have a comprehensive roadmap, and needed to change some internal structures and add more tools to accomplish goals. The steps taken since 2009 to implement the Strategic Planning Initiative were reviewed. Mr. Leonard stated that funding for an internal financial analyst is being requested, and that the aggressive legislative packages submitted in the last few years will be discussed later in the meeting. The items to be covered in the workshop include AIDEA's mission, goals and objectives; programs, portfolio, balance sheet/financial capacity; investment policy; organization/ and presentation of the preliminary dashboard.

- **AIDEA Mission, Goals, Objectives**

Mr. Leonard gave a PowerPoint presentation on AIDEA's mission, goals, and objectives. The new mission, "To promote, develop, and advance economic growth and diversification in Alaska by providing various means of financing and investment" was discussed. Investment was added to the new mission statement, because an essential part of what AIDEA does is investing in projects. The new vision, "To be an active partner with Alaskans and a dynamic resource in statewide economic development," goes back to the goal of trying to raise AIDEA's profile, its ability to support commerce, and the Governor's and Legislature's initiatives. Consultants from across the country, as well as new staff members, who can raise AIDEA skill sets, have been brought in to help with economic development.

Chairman Felix felt the board should review and agree on the new mission statement, which should be clear enough to drive all of AIDEA's activities. Commissioner Bell felt it was consistent with the Governor's expectations and the organization. Mr. Sheldon felt the mission statement was more momentum based, which he liked. Mr. Wilken said he approved of the new mission statement, but felt it should be reworded for clarity.

Mr. Leonard continued his presentation, indicating that AIDEA is a development finance authority designed to support, encourage and be a catalyst for the financing of economic growth through investments in infrastructure, business and industry. The Department of Commerce, in conjunction with the Governor's office, sets economic policies. AIDEA enables and supports implementation of the State of Alaska economic development strategies and priorities set by the Governor and the Legislature.

Mr. Leonard gave a brief overview of AIDEA's history. Mr. Leonard stated that AIDEA was created in 1967 and funded in the early 1980s with about $190 million, which provided the initial funding for what is now known as the Loan Participation Program. In the mid-1990s, AIDEA was given $143.5 million to finance its first development project, the Red Dog Mine. AIDEA has issued more than $1.1 billion in conduit revenue bonds and purchased more than $800 million in loans since its inception. AIDEA assists in financing large and small projects in urban and rural areas throughout all major industry sectors.

The board discussed how projects were chosen for funding. Mr. Leonard explained that House Bill 119 hopes to expand AIDEA's ability to invest in areas identified as being important to the Alaskan economy such as communications, health care, and new technologies. In the past, a project sponsor would request funding, but now staff is proactively reaching out to other sectors. By statute, AIDEA is confined to natural resources, industrial manufacturing, tourism, and energy projects, which can limit which sectors receive funding. Mr. Bjorkquist explained that the definition of a project, which is something tangible, allows AIDEA to focus on general areas, as opposed to AIDEA having authority in general areas. The statutes give AIDEA the authority to develop a project, but the board must exercise its discretion as to whether or not a project should be funded. The board further discussed the intent of the statutes. Research and development is not funded, but an infrastructure project that supports research and development can be financed. The board continued to discuss the wording of the statutes.

In response to Mr. Arvin's question about the movie theater being built in the Mat-Su Valley, Mr. Leonard explained that the project fell under the commercial/retail code. The project was not funded by AIDEA, but AIDEA was the conduit to them receiving a tax-exempt loan. When bonds are a certain size, they have to be approved by the area in which the project will be funded.

Mr. Leonard continued his presentation. AIDEA does not compete with the private sector. AIDEA does not provide grants. AIDEA funds both small and large projects in both rural and urban areas. The board discussed the differences between small and large projects. There is no true definition of a small or large project. The Legislature allows AIDEA to bond for projects under $10 million. Anything over that amount must be approved by the Legislature. As a rule of thumb, AIDEA can fund up to $20 million in its Loan Participation Program. Limitations, which are based on AIDEA's financial capacity, will be further discussed later in the meeting. As with any corporation, AIDEA has to manage shareholders' expectations. AIDEA's fiscal year goes from July 1 to June 30. For FY12, AIDEA's dividend to the state general fund will be $29.4 million. To date, AIDEA has returned about $304 million in dividends to the state, which is almost the state's entire initial investment in the program.

In response to Mr. Sheldon's question about retaining money in the program, Mr. Leonard talked about establishing a range for future dividends, rather than having it depend on the year's success. Mr. Arvin suggested that the board ask the Legislature to re-appropriate the dividend back to the organization instead of putting it into the general fund. Mr. Leonard explained that the dividend program was created as a compromise with the Legislature to ensure the fund would not be raided, which also provided security for bond holders and rating agencies. Mr. Leonard stated that the Legislature can change the laws and utilize any funds they deem necessary.

Mr. Sheldon said when a business pays a dividend it is under the assumption that the shareholder can do more with the money than the business can. Mr. Sheldon stated that the State of Alaska cannot reinvest the money, once it is spent, and that it is important to know that the dividend can be zero with the new initiatives we are taking on with project development. Mr. Sheldon said there needs to be a discussion at another meeting regarding long-term projects and legislation to develop a structure that guarantees funds are available to complete the projects. Mr. Bjorkquist clarified that the board has to declare a 25 to 50 percent dividend, but there are times when the Legislature could choose not to appropriate a dividend or the Governor could veto an appropriation of a dividend.

Mr. Sheldon said it would be difficult to obtain high ratings for long-term projects if AIDEA's funding could be raided. The board discussed the funding statutes. Mr. Bjorkquist explained that the dividend statute, which was a political promise that gave comfort to the bond market, was the protection against the fund being raided. Ms. Walker read the non-impairment statute, which says the state pledges and agrees not to limit the Authority's powers to fulfill the terms of a bond resolution nor impair the rights of existing bond holders. Mr. Sheldon said that meant the larger projects needed a more heavily rated debt component so they could be defended longer term. Mr. Leonard noted that staff was working on an updated board manual that would include the newest statutes. Mr. Leonard indicated that the dividend portion of the program needs to be managed and discussed with the Legislature, and that before dividends are established, staff does a long-term needs analysis, as well as review working cash flow needs.

Ms. Fisher-Goad discussed a $1 million dividend over-appropriation that occurred several years ago, which the Governor line item vetoed down to the correct amount. Ms. Fisher-Goad stated that this demonstrates the checks and balances between what the Legislature can do and the Executive Branch's ability to place limits on what they do.

The board further discussed the dividends. Mr. Felix said that if a smaller dividend were paid, then the rest of the money should be invested and leveraged to protect it from being raided. AIDEA's ability to finance and leverage its assets would be increased if less were paid to the shareholder. As with any corporation, AIDEA's mission is to increase shareholder value. However, a better shareholder value could be enhancing the economy rather than paying a larger dividend. Mr. Leonard said this item would be expanded on later in the meeting.

- **Programs, Portfolio, Balance Sheet/Financial Capacity**

Ms. Walker gave a PowerPoint presentation on AIDEA's financial strength. AIDEA's balance sheet has three income-producing components: development projects, investment portfolio, and the Loan Program. AIDEA's Loan Participations and Project Development Programs are financed by internal funding or by issuing bonds. With good access to the credit market, AIDEA enjoys an AA rating by both rating agencies based on strong financial and statutory foundations. AIDEA needs to be proactive and maintain these favorable rating agency perceptions.

Mr. Clancy explained that AIDEA was among the highest rated development authority. Rating agencies typically consider development authority projects to be riskier than general municipal revenue sources. There have been discussions with the rating agencies about the likelihood of the Legislature doing something to reduce income by taking investment securities or making investments that would make income producing investments less likely. The dividend policy was developed as a direct guard and to create a more predictable relationship between the Legislature and AIDEA. The board further discussed ratings. The State of Alaska enjoys robust oil revenue and has a higher rating than AIDEA. A state's rating impacts that of a development authority. AIDEA is currently rated three steps below the state. Alaska Housing's rating was recently upgraded due to the fact that the state was upgraded. Mr. Burnett said the state enjoyed a good credit rating because it has a large pool of money and a good income, but Alaska Housing, AIDEA, and local governments all have an effect on its credit rating. Mr. Sheldon expressed concern about promising to fund projects when there were so many competing interests. Mr. Leonard said that when considering which projects to invest in, even with the broader sectors available, AIDEA needed to consider which ones would provide the state and AIDEA with the best returns.

Alaska has a strong economy. The Authority has good credit strength and there are strong bondholder protections. AIDEA has solid debt projections using conservative assumptions. To issue bonds, AIDEA needs to generate 1.5 times the debt service coverage. AIDEA has to generate $1.50 in projected cash for every dollar of debt service. Ms. Walker explained how the debt service was calculated. Mr. Clancy, after reviewing the FY11 financial statement, said the current debt service was $12.7 million, resulting in coverage of 7.4 times. The board further discussed debt service, loan maturities, interest rates and other items pertaining to cash flow. On average, AIDEA gets about $50 million back on its portfolio for cash flow. AIDEA's debt service projection, as of June 30, 2010, is 6 times in all years. The current year was 7.4 times, the projection for the next year goes as low as 6.5 times and then begins to climb back up as more of the debt is amortized.

Ms. Walker discussed legal authority limitations. AIDEA has a statutory limitation of $400 million in bonds that can be issued in a rolling 12-month period, which includes conduit revenue bonds but excludes refunding bonds. AIDEA can finance development projects under $10 million without specific Legislative approval. By regulation, if AIDEA receives an application for tax-exempt loan participation over $1 million, AIDEA is required to sell bonds to set the loan rate. This protection ensures that a tax-exempt rate is not funded by taxable assets. Each year, no less than 25 percent and no more than 50 percent of the base yearly net income is required to be paid each year in a dividend approved by the board, appropriated by the Legislature, and signed into law by the Governor.

The revolving fund bond indenture is for general obligation debt. The bondholder protections include a liquidity requirement of having cash or U.S. Treasuries maturing in one year or less in an amount less than either $50 million or 25 percent of the outstanding principal amount of bonds, which is currently $27.4 million. The debt service coverage test on a projection basis has to equal 150 percent or 1.5 times. The unrestricted surplus test requires a range between $100 million to $200 million. The current outstanding bond total is $110 million.

Ms. Walker said to continue having access to the bond markets without a significant rating change, we would need no less than 1-to-1 cash to debt coverage, cash investments would be approximately $300 million, AIDEA's projected debt service coverage should not be below 3.0 times, and AIDEA should continue and/or do projects that make sense. The board discussed AIDEA's ratings. Mr. Clancy said Western Financial Group did not believe AIDEA needed the AAA-3 rating, because an A-1 level provides more head room and capital market access. Mr. Leonard said AIDEA needed to keep a good rating, but balance that with being able to do projects going forward. The board discussed the possible benefits of establishing an LLC or subsidiary corporation.

Mr. Wilken requested that the PowerPoint presentation be e-mailed to the board members. The following information was also requested: the relevant statutes, the amount and percentage of the dividends since inception, and where does the dividend fall in the 25 to 50 percent bracket. The "Break Even Chart" used by the Alaska Permanent Fund, which was discussed, is a great visual and something that should also be distributed to the board.

Mr. Davis gave a PowerPoint presentation on the Strategic Plan. The process was started in 2009 with three initiatives: outreach throughout the state, an extensive analysis of the State of Alaska and AIDEA, and a best practices assessment around the country and internationally. From this emerged some key factors to consider for the Strategic Plan. AIDEA had become passive and reactive, but should have a more proactive role. AIDEA's financial reserves and access to capital would allow it to be more proactive in supporting economic development. With the organization and highly skilled staff, there is a potential of having a more significant role in the state's economic development. AIDEA had statutory limitations that restricted their ability to do what was commonly done in other states. What emerged from those key factors were three fundamental initiatives: diversify and grow AIDEA's assets to support economic development; improve existing programs and add targeted new economic development financing tools; and expand the development and impact of AIDEA's economic development financing. Within the three initiatives, there was a series of goals set. Diversify and grow AIDEA's assets to support economic development: update the policies for updating and managing the balance sheet, utilize $150-200 million of additional portfolio capacity over the next three years; allocate portions of the balance sheet for risk development; and expand balance sheet capacity. Status of work on initiatives: expand perception and reality of commercial lending program from credit to commercial finance; regain historic levels of loan participation for real estate and development; match rates to economic development objectives; provide terms that would otherwise not be available in the commercial financing market; and link commercial finance programs to financial and economic development metrics. Expand deployment of AIDEA's economic development financing: establish strategies for sector targets meeting economic development criteria; outreach to private and public participants in Alaska economic development; establish systems for outreach, analysis and sponsorship of economic development financing alternatives; establish AIDEA's role in state economic development efforts; develop a single point of contact financing capability for targeted projects - leverage state, federal, private capital into multi-source project funding packages; develop internal means to rapidly intake and assign economic development opportunities; re-engineer AIDEA organization, systems, decision-making around mission, vision and objectives; and aggressively manage projects for maximum economic development benefit while maintaining financial prudence.

Recess from 12:05 p.m. to 12:26 p.m.

Mr. Felix called the meeting back to order. Last year there were five bills passed that dealt with AIDEA. HB-90 allowed AIDEA to remove the sunset from its ability to bond for development projects under $10 million and gave AIDEA back the authority to issue general obligation bonds without going to the Legislature. It removed refunding bonds from the $400 million cap. We asked for modifications to the confidentiality statutes that we believed would help when working with private sector companies or other entities. HB-363 changed the composition of the AIDEA/AEA board and enlarged the board. SB-269 related to Recovery Zone Facility Bonds, allowing AIDEA to take the cap for facility bonds. It was not as successful as we hoped, but it was in line with other states and taught us important lessons that will benefit AIDEA in the future. SB-300 allows more flexibility in setting rates in loan participations. There were a few changes requested on the Rural Development Initiative Fund Program that were tied to this bill. SB-301 allowed AIDEA to purchase Power Project Fund loans from AEA as an investment to recapitalize the fund. Mr. Leonard reviewed pending legislation. HB-119 has three sections. It empowers AIDEA to setup regulations to self-manage its procurement system; allows AIDEA to investment in a portion of a project through an LLC or a corporation; and expands the definitions of a development project. HB-120 allows AIDEA to participate in new market tax credit assistance guarantee and loan programs. In the program, the federal government encourages investment in low income census areas through a tax credit program, which involves a tax credit investor and a leveraged lender. AIDEA would be able to provide a guarantee for the leveraged lender side of the formula. If the board felt strongly enough about a project for economic reasons, AIDEA could actually be the leveraged lender. HB-103 relates to AEA and its programs. A portion of the bill will transfer eight AIDEA employees who are directly working on AEA programs and projects to AEA, providing a clear definition of AIDEA and AEA employees. SB-25 relates to participation by AIDEA in energy programs. HB-121 is the Department of Commerce's bill dealing with micro loan programs. Future legislation includes setting up an AIDEA program that would assist in funding large projects, mirroring the State Infrastructure Bank Program; improvements to the Conduit Bond Program; and potential new tools for development finance such as direct loans for economic development infrastructure projects.

The board further discussed the State Infrastructure Bank Program. Other states with similar programs that have been successful are Vermont, California, and South Dakota. In response to Mr. Sheldon's question of whether the Mongolian or Canadian models had been considered, Mr. Leonard said any information provided would be forwarded to the Department of Commerce and the Governor's office for consideration. The board further discussed the Mongolian and Canadian models. Mr. Sheldon questioned if the board or staff felt comfortable trying to organize various entities. Mr. Felix discussed AIDEA's charter as it relates to the administration and the Legislature. He felt the board should work through the Legislature, being careful not to overreach their charter. Mr. Sheldon pointed out that although AIDEA was often a passive organization, the Strategic Plan indicated a move toward the proactive side, and said he liked the idea of a State Infrastructure Bank Program, as long as it was very focused. The board discussed what other countries did for their infrastructure development. Part of AIDEA's function is talking to potential investors in the state, looking at those funding mechanisms and projects, and then bringing them forward to the Economic Development Subcabinet and the Governor's office.

Mr. Arvin briefly described Taiwan-Alaska Trade & Investment Cooperation Council (TATICC), a government-to-government, and subsequently business-to-business, platform. Mr. Arvin stated the program opened many doors for his company as a private sector participant in minerals and timber. Mr. Arvin indicated a platform such as TATICC would be very beneficial to the state of Alaska and may be a good model to consider. The board continued to discuss TATICC and several people described how the program had benefitted them. It was noted that such a program should exist within the administration, not AIDEA.

Mr. Leonard continued his presentation on current, pending and future legislation. Mr. Leonard stated AIDEA believes there are improvements that could be made to the Conduit Bond Program to allow smaller businesses to utilize the infrastructure, tax-exemption that can be used for industrial projects under $10 million. Mr. Leonard stated that a problem with the Conduit Bond Program is the cost of issuing a bond for a project less than $10 million eats up the savings that are derived from being tax-exempt. Several states have programs that issue conduit bonds down to $2 to $3 million. AIDEA will research how they do it, what legislation allows it, and how they partner with commercial and investments banks to do smaller volumes, but still have access to the lower cost, tax-exempt financing. An RFP is being issued to obtain the rates and areas of expertise of economic development consultants and advisors from around the country so AIDEA has a stable of advisors and experts that we can utilize. The

Council of Development Financial Agencies will be holding their yearly conference on May 8-12 in Boston to review their programs and share new ideas. Board members are encouraged to attend. Other educational conference opportunities are also included in the board packet.

In response to Mr. Sheldon, Mr. Leonard said the full 2010 legislative package was passed, with the exception of HB-363 that was initiated by the Legislature. The board further discussed whether they thought the pending legislation would be passed. Mr. Wilken talked about a 2007 Alaska Permanent Fund report, which would be good background material. In the report, a consultant looked at all of the sovereign wealth accounts across the world, five in the United States and 45 across the world.

Mr. Davis and Ms. Anderson gave a PowerPoint presentation on key AIDEA programs. The Authority has three key programs: Loan Participation, Development Finance, and Conduit Revenue Bond. The lesser programs include Loan Guarantee and Export Assistance, Rural Development Initiative Fund, and Small Business Economic Development Loan Fund.

The Loan Participation Program includes a three-pronged role for AIDEA's mission: direct economic development funding, liquidity for Alaska businesses/support for Alaskan lenders, and AIDEA balance sheet for income statement support. Mr. Gardiner explained that after reviewing Alaska's commercial lending market, it was determined that the role AIDEA played in providing liquidity for the lending community was a factor in keeping the funds flowing from Alaskan banks to businesses over the last few years. There was also an emphasis put on providing capacity to relatively small institutions, such as community banks, so lending could occur in locations that it otherwise might not have. The terms and conditions offered by AIDEA, combined with the support of local institutions, are different in Alaska than in most other states. The board discussed the type and size of loans AIDEA provided in the Loan Participation Program. In response to Mr. Short, Mr. Leonard said there were projects that would not have been feasible without AIDEA's participation. Extending the maturity of the loan can make a big difference on the feasibility of a project in cash flow and debt service basis.

Ms. Anderson continued to review the Loan Participation Program. The objective of the program is to provide long-term financing to Alaskan businesses. AIDEA does up to 90 percent participations of the loans by eligible lending organizations with a cap at $20 million. The terms for personal property such as equipment and other tangible items are up to 15 years, depending on the type of collateral; 25 years for real property, with up to 75 percent loan-to-value with either fixed or variable interest rates. There is a $1,000 application fee, which is eventually credited toward the 1 percent commitment fee on AIDEA's participating portion. The guiding principles of the program are encouraging economic growth and diversification, encouraging new activity by providing financing for commercial facilities, complementing the private sector rather than competing with them, providing capital at a reasonable cost, and expanding Alaskan capital by providing market liquidity and market share for Alaskan lenders. The types of financing include buy/sell transactions, term out of construction loans and refinancing.

In response to Mr. Felix, Ms. Anderson said that in 2010 refinancing loans were less than 50 percent of the total dollar volume. Generally, there are now fewer acquisitions due to the lack of confidence in the marketplace. Construction loans are also down, because it is not cost effective to build new properties when the rental rates are lower. Mr. Felix questioned how refinancing loans moved them closer to the mission statement, which the board discussed. Mr. Leonard explained how refinancing a company's debt allows them to fund inventory and working capital, thus retaining jobs. Mr. Sheldon discussed another example where a $20 million loan retained one job, and indicated that the board needs to delineate a process by which it qualifies these programs so the money is used in the best way possible. Mr. Leonard felt there were ways to do refinancing that would help the market and create more income for the authority, which was further discussed. The board talked about inflation rates, indexes and the interest rates banks were charging for loans. Mr. Short said significant refinancing has been done the last three years, because people are trying to bring some certainty to their businesses. That may not create jobs today, but it may create jobs in the future. As interest rates start to rise the number of loans being refinanced will start to decrease. It goes directly to the mission statement when AIDEA plays a role in strengthening businesses. Mr. Felix felt it was not economic development to refinance a loan so someone could go out and buy more real estate. It is economic development if that person is going to reinvest the money in their business and create more jobs. Often it is difficult to tell the difference, but better evaluation tools could be developed. The big concern is incrementally using AIDEA's equity for others and then having a compelling project come forward that AIDEA cannot afford to finance. Mr. Short cautioned against holding off on projects because there may be a better project in the future, because it may never materialize. Mr. Felix said AIDEA's risk profile was long-term. For all practical purposes, once money is committed then it is off the Balance Sheet's Liquid Assets line for 15 to 20 years. Mr. Sheldon felt the board needed to consider what would happen if the capital market shut down. Regardless of the interest coverage, you would not be able to leverage up at any price. AIDEA needs to consider liquidity and the capital necessary to move projects forward, as well as consider the worst case scenario of how AIDEA would move projects forward if it was the sole funding source and the capital market seized up. Commissioner Bell asked staff to present ideas on things like prioritizing for new jobs or certain geographic areas or where terms could be changed that would help preserve the option of having loan participation.

Ms. Anderson resumed the presentation by describing the Loan Participation Program process. A borrower comes into a bank with a proposal. The bank fills out a form which we review and decide if the project fits our requirements. The bank underwrites and approves the loan. It then comes to AIDEA to undergo our underwriting process. It then goes to the Credit Committee for approval. Loans that are more than $3 million go to the board for approval. In 2007, about 47 percent of the deals that were approved went to the board. Several statistics were reviewed. The average weighted maturity is 18.7 years. The percent of the loan portfolio prepaid each year historically is 6.5 percent. AIDEA's average loan balance has been $1.5 million. AIDEA has the potential to sell loans or a percentage of its loan portfolio. In 2010, AIDEA's loans were current at 99.4 percent, as compared to the average for Alaskan commercial banks of 96.39 percent. AIDEA's annual charge-offs from 2006 to 2010 was 0.06 percent.

The board discussed default rates. Banks that bring too many bad loans to AIDEA are dropped from the program so they strive to bring only the best loans forward. The value of refinanced loans, AIDEA's underwriting process, and the composition of the Credit Committee was discussed. There is not currently a board member on the Credit Committee, but the original Strategic Plan calls for a board member on both the Credit Committee and the Loan Committee. Mr. Bjorkquist discussed a recent Alaska Supreme Court case that dealt with state employees reviewing RFPs and potentially be held personally liable for that participation. AIDEA statutes provide immunity against personal liability for AIDEA employees acting within the scope of employment, but that protection does not extend to board members. Personal liability issues also include the expense of defending yourself in case a lawsuit is filed. In response to Mr. Felix, Mr. Bjorkquist did not believe there was any E&O insurance for the board. Another issue is loans in excess of $3 million have to come before the board for approval, and it would be awkward to review a decision already made by a board member sitting on the committee. The board further discussed having a member on the Credit Committee and decided they needed clarification on whether board members were covered for personal liability issues before making a decision.

MOTION: Mr. Sheldon moved to table the decision to place a board member on the Credit Committee.

Mr. Wilken did not think it was a good idea to have a board member on the Credit Committee for three reasons: the logistics would require that the member be on-call, the member would be put under a great deal of pressure, and the board would rely on the member and not do its homework. Mr. Leonard agreed with Mr. Wilken and felt that if a board member were to be placed on the committee, there should be a term limit. The board decided that the personal liability issue would be researched and then the issue further discussed at the next meeting.

Mr. Sheldon withdrew the motion.

Ms. Anderson resumed the presentation by reviewing the Loan Participation Program portfolio. The portfolio is divided by sector, geographic region and type. Under program metrics, business liquidity refers to the money that flows through the economy. The board discussed how the liquidity could be measured. Mr. Felix said there were two ways to look at priorities: measure them after the fact or get aggressive and set goals for sectors that can provide real economic opportunities for the state. If the board is serious about achieving the economic development as outlined in the mission statement, this concept needs to be further explored at another meeting.

Mr. Felix directed staff to provide a five-year view of the sectors identified in the Strategic Plan and the projected trends for potential growth or declines in jobs. Then provide suggestions as to how AIDEA can support the industries that will generate jobs and provide economic development for the state.

Mr. Wilkin asked for three to five examples of things AIDEA does in relation to the Loan Participation Program that the private sector cannot do that would justify AIDEA's existence. Ms. Anderson explained that AIDEA provided businesses with long-term financing at reasonable rates and a predictable fixed debt service, which provides stability and encourages those businesses to expand. Mr. Sheldon noted that AIDEA was also created as a firewall to protect the Permanent Fund.

Ms. Anderson continued by reviewing the chart of the Loan Participation Program's portfolio, which the board then discussed. Mr. Gardiner talked about an analysis that said the program was addressing sectors that a commercial lending product should address in the Alaskan economy. Mr. Leonard noted that the chart also indicates that a large portion of AIDEA's portfolio goes to state financial institutions, which was discussed earlier in the meeting. After further reviewing the portfolio, Mr. Gardiner noted that the program did not finance infrastructure, but it financed revenue-producing enterprise real estate. Mr. Leonard said that went to AIDEA's purpose of supporting small business expansion.

Ms. Anderson reviewed the results from the Loan Program. From FY2002 through FY2010, 3,331 construction jobs and 4,897 permanent jobs have been created or retained through

AIDEA's Loan Participation Program. The program provided Alaskan commercial banks liquidity, which assisted in differentiating Alaskan businesses from commercial bank restrictions in the Lower 48. Mr. Felix said it would be helpful to know how many of the 4,897 permanent jobs were actually created versus retained. Mr. Leonard said staff would be separating those figures in the future.

Break from 2:32 p.m. to 2:48 p.m.

Mr. Felix called the meeting back to order.

Mr. Hemsath said after a meeting with Partnerships BC, which is the Canadian arm of economic through public/private partnerships, they offered to give a presentation on what they do, how it might apply to AIDEA, and the templates they use in creating roads to resources. TATICC, which was discussed earlier, co-financed a relatively detailed study on coal to liquid resources in Cook Inlet.

The Development Finance Program was reviewed. Its objective is to acquire, manage and operate projects in Alaska. AIDEA owns the project, or a portion of the project, and is repaid through user fees, lease payments or other revenue sources. AIDEA-owned projects provide more than 735 direct jobs in Alaska, with the majority being at the Red Dog mine and Ketchikan shipyard. The board discussed specific projects and why they were financed by AIDEA rather than another entity such as the Department of Transportation. Development Finance is designed to promote, develop and advance the general prosperity and economic welfare of Alaska, to relieve problems of unemployment, and to create employment by owning and operating enterprises and other facilities. A project must be endorsed by the local government, economically advantageous to the state and the general public, and contribute to the economic growth of the state. The applicant must be financially responsible and the project must be feasible and able to produce revenue adequate to repay the bonds or loans with which it is financed. AIDEA provides businesses with incentives to come to Alaska through lower cost financing or by changing the structure of a business to make it competitive.

Mr. Leonard pointed out that this was another example of what AIDEA does. A majority of AIDEA's statutes address bonding and financing. Businesses and Alaskan projects have access to the capital market based on AIDEA's financial strength, which allows for expanded access and better rates.

Mr. Felix said he was confused about AIDEA's responsibility to develop versus the state's responsibility through its agencies. Mr. Short said the Department of Transportation's role is typically to fund and build transportation links that have a general use and benefit. They do not do project financing for infrastructure that supports a specific facility or region that has the ability to pay for itself. The projects on the list are infrastructure projects that serve specific facilities or narrow areas and have the ability to generate revenues to be self-financed. There are also mixed projects that involve some level of contributions from the Department of Transportation, to the extent that they are able to justify it as a general use facility. AIDEA does the project finance component. The board further discussed the type of projects that should be financed through AIDEA, which must adhere to the constraints discussed earlier. A project must be able to produce revenue. AIDEA does not build roads or infrastructure for the general good of the state. We focus on specific economic development to create jobs and projects that will eventually pay for themselves.

Mr. Hemsath continued his presentation and stated that AIDEA will not do a project unless it can pay for itself. However, AIDEA is more flexible than straight loans, which was further explained with examples. AIDEA has five active development projects: DeLong Mountain Transportation System, Healy Clean Coal Project, FedEx Facility, Ketchikan Shipyard, and Skagway Ore Terminal. All of the projects can generate revenue and will be long-term strategic assets as well.

Mr. Short asked staff to provide a short presentation on the Cook Inlet project, including the issues, timeline, where the decision points are, and what will be asked of board members regarding the potential controversy. Mr. Leonard said staff would schedule a presentation to review the Cook Inlet project with the board members.

Mr. Hemsath resumed his presentation. Mr. Hemsath indicated that the program, designed in 1967, leaned toward heavy industrial and manufacturing type projects. The expansion of the definition of a project allows AIDEA to look at projects that fit today's environment. For example, a project can be a pilot plan as it relates to energy facilities. The five active development projects have a net value of about $326 million. The process for reviewing projects includes several components. AIDEA considers whether the project fits the program and strategy; if there is a demonstrated need for AIDEA's involvement; another entity's ability to finance the project; financing structure; and security.

The board talked about why AIDEA was involved in certain projects such as the FedEx Facility. Mr. Hemsath explained that FedEx is not in the business of building hangars and their capital is invested in aircraft. They could just as well have gone to Vancouver. With AIDEA buying and building the hangar, FedEx was encouraged to remain here and establish a cargo hub in Anchorage. Strategically, if FedEx leaves, AIDEA would still own the hangar and it can be utilized by someone else.

Mr. Sheldon expressed concern about the lack of clarity regarding the definitions between Loan Participation and Development Finance in relation to a decision that was made by the board about a month ago. Mr. Bjorkquist explained that both programs dealt with financing projects, although the definitions of a project were different for each program. The Loan Participation Program has a statutory requirement that the loan participation has to meet certain criteria, but if AIDEA intends to own the project then those conditions can be waived. Development Finance has no specific criteria for what needs to be in the agreement. The statute only requires that there be a finance plan that estimates all the costs, including the operating costs. The authority gives preference to projects that do not require financial assistance from the state. However, if a project does require financial assistance that assistance has to be in place before the project goes forward.

Mr. Hemsath resumed his presentation. The metrics for the Development Finance Program include sector targets, number of projects and locations in the pipeline, number of jobs created or maintained, dollar value of AIDEA of projects and project phase, and private investment leveraged.

Mr. Felix asked for an overview of projects currently in the pipeline. Mr. Bjorkquist noted that any confidential material discussed should be done in executive session. Mr. Felix said he was more interested in the type of projects in the pipeline rather than who they were for. Mr. Hemsath said staff could produce a list of the number and types of projects, Mr. Felix felt stabilizing and lowering the cost of energy was one of the highest priorities in the state, because economic development is difficult to create if stable energy costs are not available. For example, if there are no energy projects in the pipeline then staff needs to look for those types of projects. Mr. Hemsath reviewed some of the projects currently in the pipeline including a fisheries project in Sitka, the Cook Inlet resource extraction project, roads, mines, internet server farm, fuel storage, and others. The board discussed natural gas storage. Mr. Short said he was uncomfortable with some of the projects, such as the internet server farm. An existing company has been trying to get into that game for years. Mr. Short indicated that if AIDEA uses its balance sheet to help a different company get into the game, AIDEA would be interfering with market forces. Mr. Felix pointed out that care should be taken not to disincentive private investment. The board further discussed AIDEA's potential interference in the free market. Mr. Felix asked the board to review the upcoming projects and provide staff with a clear direction in terms of where they wanted the focus of economic development to go.

It was noted that the Investment Policy would be discussed before continuing with the Balance Sheet/Financial Capacity.

- **Investment Policy**

Ms. Walker reviewed the investment policy. AIDEA has inside portfolio management, as well as two outside managers. The primary goals are safety; liquidity for the internally managed portfolio; and return for the external managers. AIDEA's funds are public funds with a goal of preservation of capital. The investment police was adopted in 2001, and then amended and restated in 2006. There are different parameters for internal and external funds. Allowable investments have a goal of preserving capital, and for a debt - to be able to support the debt. However, there has been some discussion of whether that statement is still true considering the changes in the credit market over the last two years.

Mr. Sheldon expressed his discomfort with mortgage backed securities (MBS) and other types of loans, which do not pass the safety and soundness test. MBSs, GSEs and Treasuries as investment options were discussed.

Mr. Cliff, of Callan Associates, said Mr. Leary, who was not available for the meeting, is the investment consultant assigned to AIDEA's account. Mr. Cliff stated that AIDEA's investment objective is safety, liquidity, and return. The investment policy makes sense and is what we often see for conservatively run programs. Investment grade, which is considered very safe, and non-investment grade portfolios were discussed. The Enterprise Fund, having a one-fifth allocation, seems to meet AIDEA's liquidity and safety needs. The remainder of the portfolio, which is managed with longer term investments in the investment grade universe, provides the safety and return but with somewhat diminished liquidity. When combined, these resonate with the investment objectives of the plan. AIDEA's performance results have been good. The MBS issue was further discussed. Since the initiation of the GSEs, the Ginnie Mae entities were explicitly backed by the U.S. government and the follow-on entities were implicitly backed. If you adjust similar coupon and maturity dates of GSE mortgage backed securities versus Ginnie Mae's, there is only a slight spread. Depending on which coupon stack you look at, there is a spread of about 10 to 20 basis points versus the explicitly guarantee mortgage backed securities. In general, investing in securities is not seen as a major threat. U.S. Treasury Secretary Geitner has reaffirmed the government's committee to the GSEs.

In response to Mr. Sheldon's question about why the U.S. government failed to put GSEs on the balance sheet, Mr. Cliff said Callan looks at how the government has historically supported these types of entities and what they are saying they will do. GSEs control almost 80 percent of the mortgage market. Mr. Sheldon said Fannie Mae and Freddie Mack would not be put on the balance sheet even with the expansion of the debt limit, because the government does not have the capacity to do it. If they do not have the capacity then 10 basis points is not worth the risk. Mr. Cliff said institutional investors and the public market were currently the heaviest buyers of the mortgaged backed market. Mr. Cliff said he cannot say that these concerns will not come to fruition, but AIDEA's portfolio is benchmarked to the Barclay's Aggregate Index, which is the broadest sweep of investment grade liquid bonds that trade in the marketplace. There is another index called the Barclay's Government Credit Index, which excludes the MBS piece of the aggregate. If the board is uncomfortable with MBS, the benchmark for the portfolio could be changed to exclude mortgage backed securities and the investment policies be rewritten to exclude purchasing MBSs. While there would be little in earning penalties for switching to the Government Credit Index, there might be more volatility. Historically, the risk factors that drive the mortgage backed market are unique enough that when you add them to a government and credit portfolio, it dilutes the total portfolio volatility down.

After extensively discussing mortgage back securities, the government's involvement, what other Callan clients were doing in relation to GSEs, and a possible approach of not purchasing GSEs until the issues were resolved, Mr. Cliff was asked for his advice on the investment policy. Mr. Cliff said the least egregious change would be to move the mandates of the managers and the benchmark for the investment portfolio to the Barclay's Government Credit Index. A powerful rule of thumb is the less liquidity desired the more expected return you can get. The current construct of the investment program resonates well with AIDEA's investment objectives, as it would under the Barclay's Government Credit Index. Mr. Leonard noted that liquidity has always been important to public fund management. Mr. Short suggested making a recommendation, based on this conversation, which would then become an agenda item for the Wednesday meeting. After discussing the fact that the resolution would need to be amended and the policy rewritten, the board discussed the timeline to accomplish these tasks. The board decided to have Callan Associates provide the discussed investment policy changes in writing, talk about this issue with the investment managers, and schedule a meeting in two weeks to further discuss the issue.

Mr. Felix said the remainder of the agenda would be covered tomorrow and/or at the next board meeting.

Mr. Wilken discussed the volume of paperwork for new board members, which is a voluntary position, and questioned if there was a way to be paid without all the paperwork. Ms. Walker explained that 1099 forms used to be issued, but the IRS now requires the paperwork that was provided.

- **Organization**
- **Presentation of Preliminary Dashboard**

7. DIRECTOR'S COMMENTS

- Next regularly scheduled board meeting is Wednesday, March 2, 2011

8. BOARD COMMENTS

There were no board comments.

9. ADJOURNMENT

There being no objection, the meeting was adjourned at 4:32 p.m.

Ted Leonard, Executive Director/Secretary
Alaska Industrial Development and Export Authority