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STATE INVESTMENT ADVISORY COMMITTEE

MEETING

NOVEMBER 5 AND 6, 1976

Anchorage, Alaska

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STATE INVESTMENT ADVISORY COMMITTEE

November 5 and 6, 1976

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Chairman Eric Wohlforth called the meeting to order at 9:00 a.m. on Friday, November 5, 1976, in Room 406, State Courthouse, Anchorage, Alaska.

Members present were:

Dr. Logsdon, Associate Director, Agricultural Experiment Station, University of Alaska, Palmer
Mr. Eric Wohlsforth, Attorney at Law, Anchorage
Robert Barnes, President, Alaska State Bank, Anchorage
Mr. Dennis Waldock, Foster & Marshall, Anchorage
Mr. Jamie Love, Alaska Public Interest Research Group
Mrs. Lanie Fleischer, Anchorage
Mr. James Crawford, Coordinator Alaska Offices, Ted Stevens/ U. S. Senator, Anchorage
Senator Frank Ferguson, Kotzebue
Commissioner Motley, Department of Commerce & Economic Development, Juneau
Commissioner Gallagher, Department of Revenue, Juneau
Deputy Commissioner Edenso, Department of Revenue, Juneau
Senator Kerttula, Palmer
Representative Gruening, Anchorage
Mr. Freer for Commissioner Allen, Department of Administration, Juneau
Mr. James Rhode, Anchorage
Mr. Robert LeResche, Director Development Planning & Research, Juneau (present on November 6)

Absent Members:

Mr. Emil Nottis, President Alaska Native Foundation, Anchorage
Mr. Pihl, Comptroller Ketchikan Pulp Company, Ketchikan
Mr. Robert Thorstenson, Petersburg
Mr. Robert McFarland, Anchorage
Senator Butrovich, Fairbanks
Representative Malone, Kenai
Representative Urion, Anchorage

MR. WOHLFORTH: We are calling the meeting of the State Investment Advisory Committee to order. I am acting as temporary chairman in the absence of Bob McFarland, who is on vacation right now and is unable to attend.

You all know of the passage of the Permanent Fund Amendment last Tuesday, which has been the subject of study by this Committee of two intensive meetings and this is the third meeting where the subject matter of the structure of the Permanent Fund and testimony has been taken at prior meetings from consultants, really in a learning process, in aid of a learning process to advise the Legislature, if you will, the appropriate legislative committees of some Permanent Fund operations in other states and provinces and development loan bank operations elsewhere throughout the world.

This morning we have time set forth for public hearings the subject being, now the Permanent Fund has passed, with its limitation that monies placed therein be used for income producing investments. What kind of structure of operation, what kind of organization, what sort of use of monies for income producing investments is appropriate to recommend to the Legislature and to the legislative committees when they convene and start their work in January. Fortunately, we have legislative members on this Committee and, therefore, we hope that the continuity of information which is started will flow more evenly as the legislators carry their information back to the

committees when the Legislature convenes.

The agenda is formated over a 2-day time frame and I will just briefly go through the agenda. This morning is set aside for a public hearing. This afternoon at 2:00 o'clock Mr. Butler of White Weld will give a report on possible uses of the Permanent Fund to leverage investment. In other words, the concept of non-direct investment of the monies but use of the Fund to create other investment vehicles or investment instruments for those general purposes. At 3:00 o'clock, Mr. Bob Richards will speak in general on the Alaska banking system and presumably in his capacity for investments of various kinds which might be contemplated for the Permanent Fund. At 4:00 o'clock, the Committee will have open discussion, presumably to digest and to comment on some of the items which they have heard this morning and will hear this afternoon. At 9:00 o'clock tomorrow, and presumably at the same place, Price Waterhouse Company will report on management governing boards and problems encountered in both the operation of other permanent funds and in the operation of development loan situations, development loan bank situations elsewhere in the world, the question of What Went Wrong. In other words, how can we avoid some of the mistakes that have been made elsewhere in this area. At 10:00 o'clock tomorrow there is scheduled a work session under the general topic of Structural and Organizational Considerations. At 1:30 tomorrow, a continuation of work sessions on the question

of structure of the vehicle, which will make the investments, if you will, which are permitted under the Constitutional Amendment which just passed on Tuesday.

As you speak this morning, if you would proceed to this little card table, the microphone will be placed on the card table, and simply identify yourself and spell your name for the purposes of the transcription. All of these hearings are being transcribed verbatim. And here is the transcript of the last meeting. Again, with the notion that the legislative committees will have a complete record of the information and comments that have been submitted at these meetings. I would like to get an indication now of the number of members in the audience who do wish to be heard this morning. Seven members. Given that, I don't think we need to impose any time stricture because there seems to be plenty of time to accommodate all those who wish to be heard. I do have one request to speak initially and that request comes from Mr. Phil Daniels who is here and apparently has a pressing time problem. If any of the others have absolute time committments and there is any reason they can't stay beyond the next hour, we would be glad to hear them in a preferential order.

Again, just to alert you to our interest, this is an information gathering, educational type of effort, speaking on the structure and organization of the vehicle which will "administer" the Permanent Fund as well as intentional investments as they

relate to what is happening in Alaska and what we estimate what will happen later. So we would begin the public hearing then and Mr. Phil Daniel will be first.

MR. PHIL DANIEL: Mr. Chairman and members of the Committee, my name if Philip Daniel and I am with United Fishermen of Alaska. That is a rather dubious gathering of commercial fishing organizations representing about 24 groups that are spread through the coastal regions of the State.

I would like to speak in rather general terms about the present situation in the fisheries as it might relate to the Permanent Fund. The first observation would be that the Alaska fisheries at this point in time is rather archaic in structure and in its scope. I don't want to say by that that we are not reasonably efficient in the things that we do. I am really trying to get at the problem that the fishery is rather narrow in its viewpoint. We are presently harvesting about four stocks. They are gourmet items as most of you probably know if you have gone close to any of those items on the grocery shelf. And we are neglecting things that could be done. Certainly, that might pertain to the subject at hand. By that I mean that two years ago, 5.6 billion pounds of fish were harvested in Alaskan waters and of those 5.6 billion pounds that were harvested the Japanese and Russians took 5.1 billion which is about 89 percent of the poundage produced. That by no means represents poundage of salmon or the various traditional fish that we are primarily

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concentrating on, but primarily bottom fish that American fishermen are not presently trying to harvest. I don't know what the economic value of those bottom fish would be, but I would assume that, if a market were developed, it would be substantial.

The first problem is simply that the market has not been developed. And the present burden, of course, is upon the processor as far as developing the market. It's a substantial burden and it may be that the State could play a role there. I don't know whether, for example, the State might want to think along the lines of standardizing a brand for the State of Alaska, something in the direction of Florida orange juice or Florida oranges. I know there has been discussion of this in Juneau. That certainly could help. Any marketing operation, getting the message out to the general public could help substantially.

Additionally, and I don't want to go too deeply into what might be possible except to kind of outline the problem. But there is just no question in my mind, in the future we are going to have to rely more and more on the renewable resources. There is going to be a terminal point, at this point in time, we don't know when that will be as far as the very substantial oil production that is going to take place in the near future. And, at that point, I would assume we will be dropping back on the traditional renewable resources, tourism, fisheries, timber and things of this type. So it might well be worth considering what the Permanent Fund by way of investment could do to stimulate

the fisheries, and certainly the movement into the bottom fish.

Under the present 200-mile regime, we have an ability to displace the foreign vessels that are presently harvesting our fish stocks. I don't think that is going to happen initially at a very, very high rate. Mainly because there is going to be a temptation to trade off Alaskan interests against other national interests and there is only 350,000 of us and you have about 200 million people sitting down in the Lower 48 and I think there will be a continued temptation for the State Department to trade off Alaskan interests and perhaps make concession on our bottom fish stocks that probably shouldn't be made. But over a period of time, under the present bill, we can displace the foreign fisher. And that is going to require, of course, a gearing up on the part of American fishermen, but even more so the development of those markets. So I think that should be the main thrust of the thinking.

Additionally, as many of you may have heard to the point where you don't want to hear it again, our salmon fisheries are in very great difficulties. We only have about a third of our salmon stock remaining at this point in time. We feel that that situation need not exist in the future, primarily of the success of the Japanese efforts in hatchery production. Last year Japan produced 16 million chum salmon which is four times the annual average production for the State of Alaska. And they have done that at a very substantial cost benefit ratio. Their better

hatcheries are achieving a cost benefit ratio of 24 to 1. I would not want to say then that we can expect that kind of achievement here, but it certainly should be able to operate at a profit. And this will be the crucial test in any hatchery system, whether it is a State hatchery system relating to the presently passed bond issue, or whether we are looking at it from the standpoint of private non-profit hatcheries that presently exist. The crucial test would be whether they could the fish and afford to catch them. Traditionally, of course, the hatcheries that are producing fish in the Northwest are often questionable in that respect. They very often had a fish return that was more expensive that you could afford to produce. You perhaps could justify it from a sports fish point of view and from a tourism point of view because those fish are individually worth more to the State in those areas than they are in a commercial fishery. But from a commercial point of view, there have been some very significant breakthroughs in the last few years in hatchery production that has brought the price down very substantially. The present price tag that is being talked about is somewhere between one and four million dollars for a 40 million fish capacity gravel incubation system. I don't want to go into detail on gravel incubators except to say they produce a very healthy smolt and they product it at a very much lesser cost than the so-called conventional hatcheries that have been employed for years in the northwestern part of the United States.

The crucial test, again, is whether or not in Alaska we can build these hatcheries, turn the fish loose, and get them back to us at a profit. I think that is a distinct possibility. We very strongly urge a loan program that was passed by the last Legislature creating a 200 million dollar loan program which works in this fashion: The fishermen would assess themselves and the value of their catch in a particular region, the money derived from that assessment would be used for security to approach that loan. And, of course, the idea is to put part of the burden of replenishing the fishery on the fishermen themselves. And I believe there is almost an universal willingness among fishermen to help absorb the cost. This doesn't, of course, say that we should not have State-owned hatcheries. I have some criticism of the State program at this point in time. It is obviously new and it is perhaps a little bit premature to be terribly critical of them. But I can certainly see a role for State hatcheries and especially in areas where there is intense concentration of sport fishermen. On the other hand, if the commercial fishermen themselves are willing to help pick up the tab for rehabilitating the commercial species, it is probably a very desirable situation. And I think that willingness does exist.

I could see the Permanent Fund acting as a stimulant to the industry moving into the bottom fishery. I can see it acting perhaps as a stimulant to the hatchery production situation. The

bills that are presently passed are not perfect. We may want to revise them extensively. There is certainly going to be a considerable monetary requirement so far as rehabilitating the salmon fishery. If that were done solely with State money, we might be talking of a sum of around 300 million dollars. That is a substantial amount of money. It is not, of course, unthinkable if you look at what is happened in the rest of the Pacific realm. Washington just initiated last year a 200 million dollar expansion of their presently existing program. British Columbia initiated a 300 million dollar expansion of theirs. Japan is expanding her hatchery system at a very significant rate. Last year they released a billion smolt. And within ten years, they will be releasing 2 billion smolt from their hatcheries. Last year we released 6 million smolt from all of our official sources. So it is rather pertinent that we look in these directions. I don't want to try to convince anyone who is sitting at the table that I have a good grasp of the economics of the situation. I am really rather naive and am speaking to you as a commercial fisherman. But I can certainly see a very significant role that could be played by the Permanent Fund to stimulate the industry and hopefully provide an economic base that we can turn to when other avenues have exhausted themselves. Thank you.

MR. MOTLEY: Mr. Chairman, could I ask a couple of questions? Mr. Daniel, you talked about -- you said that no

market was established for the 5.1 billion pounds. What you really mean is that there has been no domestic market.

MR. DANIEL: That is correct.

MR. MOTLEY: Wouldn't you think it is a logical assumption that given a 200-mile limit that the people who have been used to eating that 5.1 billion pounds of fish aren't going to stop eating them. So what we are really talking about is a change in the relationship of the process in which they're caught and processed within the 200-mile limit, i.e., the exclusion of foreign fishing rather than necessarily disrupting the total market. Is that a fair statement?

MR. DANIEL: I would say it is. Certainly, if the American fishermen were to catch those fish, I think the American fishermen would like to see the reserve in the present balance of trade deficit. We had a 1.5 billion dollar balance of trade deficit last year, the Federal Government did on fisheries products. Well, if you could turn that around so so that we were harvesting and selling to the Japanese, that would be fine.

MR. MOTLEY: So what we are talking about, you would envision the Permanent Fund to be a vehicle to possibly replace the Japanese mother ships with American mother ships or on-shore processing facilities?

MR. DANIEL: Well, I think that. But I would like to go beyond that. We have done so little in the Lower 48 to convince people that fish is a good product. In France, the

average Frenchman eats about 33 pounds of fish a year, and in Japan it is almost twice that. The average American eats about 11 pounds. We are primarily beef eaters, I suppose, in the United States. And I have heard many people make the observation, first, that you can't buy fish here in Alaska, which obviously is not the greatest market in the world by virtue of the lack of population. But if we could do something to get fresh fish or good products down into the Midwest, for example, or the East Coast. I've seen fish products that we harvested here that you could sell on the East Coast for 40 to 50 cents a pound, bottom fish, that you can't give away here. You use them for bait. And it is really not desirable and I think -- and I really agree with you, you want to continue to go to those markets. At the same time, if there is anything you can do to broaden that market, especially broaden it into the Lower 48, I think that would be desirable.

MR. MOTLEY: With regard to the fish hatcheries program, would you envision, given the Constitutional Amendment states that it is a return on its investment, that the private nonprofit hatchery program as envisioned in the current 200 million dollar program -- we've got one going in Cordova and we're looking at a couple of others -- would they under the ground rules of the Constitutional change, do you think that they would be a more apt vehicle for this investment as opposed to a State-operated hatchery program?

MR. DANIEL: I really think that they can do it more cheaply and I think as far as the capital investment, the initial investment. There are going to be two things in those private hatcheries, one, they have to have good biologists and, two, they've got to have a good business manager.

MR. GALLAGHER: Those mother ships, or a like vehicle, how much would they run in American dollars? A million and a half?

MR. DANIEL: I think it would be very, very much more than that. 80 foot, 100 foot crabbers now run better than a million dollars. The mother ship, a floating factory ship is what we're talking about would probably run millions of dollars. To displace the Japanese does not necessarily require a mother ship fleet. The only they've got that mother ship there is because it's a distant water fishery, which is the most inefficient method moneywise to produce protein that exists. And with shortage on fuel and various things of this type will really limit their operations in the future. In some cases, we'd need a floater, it wouldn't have to be an extensive operation necessarily as far as size. Again, land-based processing is very often appropriate. The only time it would not be would be in cases where weather conditions or harbor facilities were not available. I don't know what the economics of that is, the cost of a floater as compared to a land-based processing operation.

MR. LOVE: What effect do you think all this off-shore

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operation would have?

MR. DANIEL: Well, there is real nervousness among the fishermen. I said one time in a public testimony on this type of question that perhaps it was the case and I heavily emphasized the perhaps, that fishermen were simply paranoid about some of these issues. It came out in the press a little bit later that I had said they were, in fact, paranoid. The problem with most of the fishermen is they can read and they read things -- for example, there have been some reports by the National Fishery Service that indicate vulnerability of crab and shrimp loss one part per million of oil actually dissolved into the water. Well, this makes fishermen nervous. They don't really know what that means but it doesn't sound good. So there is real apprehension about OCS. My only solution to it is not a very sophisticated one. I have suggested repeatedly to the oil companies what needs to be done is take a group of fishermen and go to the Gulf of Mexico and allow those fishermen to talk to their counterparts. You might want to allow them to talk to some experts too, some professorial types and perhaps people who are experts on pollution problems. But the main thing is the fishermen themselves have more credibility with Alaskan fishermen than anyone else will have. And if you can get these guys to sit down and talk to their counterparts in the Gulf and the guys down there, in fact, say, as some of my lobbyist friends from the oil companies indicate, that they can live with OCS

development, I think that will go further to solve the problem than anything else. I think the fishermen would be -- I would be enormously grateful not to feel apprehensive about OCS.

MR. LOVE: How much investment capital do you think would be advisable?

MR. DANIEL: I really couldn't answer that with any sophistication at all. I would get into figures on what it would cost to rehabilitate the fisheries. I think that figure would probably obtained if the State did the entire job. I believe if we get private industry into it, we can do it somewhat cheaper. As far as developing markets and as far stimulating the harvest of bottom fish, I really don't have figures on that. I just haven't heard any, I don't know that any exist, although they probably do.

MR. LOVE: I just wanted to point out in the interest of future deliberations, it would be useful to have some figures given to us. Also if you see the need for an investment in the area of hatcheries and also in building boats or in processing facilities.

MR. DANIEL: Well, I can see it in the boat building if you're moving into different fisheries. We are obviously in the salmon industry too efficient at this point in time. If you're using a boat for other purposes besides salmon, perhaps it is justifiable. If you're looking at the standpoint of moving into these bottom fisheries, very definitely we could use State

money in that respect. Because the burden right now for the fisherman who wants to develop a new technique or move into something is entirely upon that fisherman. I don't know of any experimental monies that are available except perhaps a very small amount. I could see it there. I see it certainly in the hatchery situation but, again, I want to emphasis that what we are really interested in is the loan program where the State gets its money back. Simply a loan that is repaid out of the sale of surplus fish at the hatchery racks and repaying these assessments on the fishermen.

MR. LOVE: You think the big part of it is hatcheries.

MR. DANIEL: Well, the bottom fish thing could be tremendously valuable. Right now we have had a tendency to be rather narrow in our viewpoint and look only at the hatcheries because salmon is a glamour fish. And we're in trouble on salmon and I think people recognize that. But I think we also ought to look at those bottom fish stocks very, very definitely. And I can't be as specific there about what the State can and can't do. But 5.1 billion pounds of fish should be worth a considerable amount of money, so if we could move into that area, it would seem to me to be very desirable.

MS. FLEISCHER: I want to ask you, for instance, on bottom fish. I don't know anything about them. How renewable are bottom fish? You are not talking about hatcheries when you are talking about bottom fish.

MR. DANIEL: No. Hatcheries would only apply to the salmon.

MS. FLEISCHER: How do ---

MR. DANIEL: Well, it is a more frustrating situation. For instance, our halibut stocks are in big trouble now. There was a time previously when they got so depressed that we simply quit fishing for them for a number of years and they did recuperate. We've got additional problems now because the Japanese -- the halibut are not the target species for the Japanese, but they catch about a 1 percent incidental catch while they're chasing pollack and various things of that type. That just devastates those halibut stocks because these are primarily juvenile fish, you know, immature. They are renewable but it's not the same thing as being able to put a hatchery in and let them go and let them come back to you. The main method of renewal is simply to quit fishing for them. The Japanese and Russians at this point in time have absolutely devastated some of the stocks. We're down on pollack to where we're supposedly harvesting primarily juveniles. We have already gone through ocean perch to the point where they are in grave jeopardy and the Japanese use what is called the pulse fishing technique. They go in and harvest the fish where it is down to the point where they are no longer economically feasible. Then they leave them alone and theoretically allow them to recuperate. However, our biologists don't think they necessarily give them enough time.

MS. FLEISCHER: Is there anything that can be done, as far as you know, for renewing bottom fish?

MR. DANIEL: We need a better and more careful regulatory regime. Under the new bill, we have the ability to tell the Japanese and Russions who can fish and where they can fish and when they can fish.

MS. FLEISCHER: In other words, there will be cooperation maybe.

MR. DANIEL: We can insist upon it. There is always the question whether our State Department is going to show any courage.

MS. FLEISCHER: I wanted to ask you also about -- some of the other things you have mentioned like tourism and timber and other industries in this State can be a threat, I imagine, to fisheries and I was wondering if the fishermen are part of that decision-making process and whether you are able to cooperate with the timber industry or the timber industry is able to cooperate with you to protect like salmon stock.

MR. DANIEL: We have tried to adopt a very cautious attitude toward timber and oil. And certainly do not want to get into the stance of trying to say these two industries which are very, very vital industries in the State should not exist. There is a real apprehension in Southeast Alaska among fishermen as to what is happening on those salmon streams. And we have tried and tried, again, to get as much protection in the salmon

streams as possible with prohibiting timber harvest. I certainly think that there is a possibility of mutual existence there. The thing that encourages me too, I don't want to see us just simply throw open the door and say we're not going to worry about stocks because that's the least expensive way to produce fish. With hatchery production, it is interesting that today in Washington and Oregon and B.C., as well as in Japan, their production on salmon is as great as it ever was. In fact, in Japan, far greater than it has been historically. And the Japanese are producing their fish on the island of Hokkaido and Northern Honshu Province and the population pressure there is just unconscionable. There are 6 million people living on the island of Hokkaido.

MS. FLEISCHER: So, in other words, they create salmon streams, in effect, so you aren't dependent on the natural streams. That was one of my questions plus the fact that I was reading about a salmon fishery in Washington and apparently part of what happened there was the dams on the rivers. And I know that there are some plans and probably will be more for hydroelectric development here in Alaska. And I am wondering if that can be planned in a way not to interfere with the salmon industry or whether you are part of that decision-making process as to where dams should be.

MR. DANIEL: Well, I think there are certainly bad things you can do. We have so many streams to choose from and

there are some where it would be very, very distressing -- if we went out and tried to dam up Iliamna Lake, for example. Not that that is going to happen but that is a major spawning area and terribly valuable from that viewpoint. Certainly there are alternatives in most cases where they are not necessarily interfering with salmon. And we would be concerned about that. Hydroelectric projects, without a doubt, are a major feature that caused a decline in the Northwest.

MS. FLEISCHER: My question was, are you part of that decision-making process?

MR. DANIEL: In a very, very small way. It's partially our own fault. We obviously can become more a part in these decision-making processes. Our organization is a bit new and we have been somewhat preoccupied with limited entry, especially in the last few weeks. But I think the opportunity certainly exists, it's just a matter of our taking advantage of it.

MR. FREER: What sort of research effort aimed at better utilization of the fish that were caught in Alaska. I wonder if you saw any need for a continuing type of research program such as that for use of monies from this Fund?

MR. DANIEL: Well, we really need to do those things, I think. One of the things that I hadn't really thought about is how desirable -- we've got so many stocks, sea urchin, for example, that are highly valuable in Europe that we are not even touching. We have some abalone down in Southeast. There's

probably a long, long list of fish and fishery products that we are not utilizing. Research in those areas would be highly desirable. The National Fishery Service does some of that, probably not an adequate amount. By the way, I did mean to mention earlier in my testimony that with the 200-mile limit bill on the books you may see some Federal money coming into these areas. But whether or not it will be a substantial amount or whether or not it will work to our best interest is still a matter of question. I would certainly say, yes, we could use additional research.

DR. LOGSDON: What is the existing capability of Alaska fishermen to take bottom fish?

MR. DANIEL: Well, the guys in crab fishing, boats that are quite substantial in their size. And I would say that many of them could be converted. It seems I remember a cost of 45,000 dollars conversion, to convert some of these boats over to where they would have a capability on bottom fish.

MR. EDENSO: There would be a limitation on the size of the boat.

MR. DANIEL: Yes, there are lots of factors.

MR. EDENSO: If you're just talking conversion in gear, it is going to be in excess of 50,000 dollars.

MR. DANIEL: Okay. Well, I had seen the figures but it's been several months ago, I saw them and they slipped away from me. Some of the guys in Kodiak and on the Chain would tell

this story a bit braver than perhaps they should about their ability to move immediately there. I know that the desire exists, but the practicality of the matter, it means gearing up and gearing up not only so far as the boats but processing capability and marketing ability. And considering those factors, no, not close. The boats themselves are much closer than anything else so far as being able to get into the business.

MR. WOHLFORTH: This subject is obviously one that would take us weeks of testimony and we want to bear in mind we're just getting an introduction. Hopefully, people like Mr. Daniel will work closely with this Committee and the legislative committees on a continuing and more detailed basis on what he has just been able to give us a brief introduction to this morning. I think I would say you, unless you have a burning question, that we suspend questioning in deference to the others who are here and who may have a time scheduled that they really need to meet.

MR. WALDOCK: Mr. Chairman, I would like to ask just one question. Mr. Daniel, I would like to know if there is any research underway at this particular time to see whether or not, if we funded the Fishery Department, whether it is going to be a profitable operation because part of the criteria of the Permanent Fund money has to have a return for the investors.

MR. DANIEL: Well, no, I would say that there is probably not much being done there. Not as much as should be,

and probably should be very carefully looked at as far as whether you let the money go in the direction of private industry or whether you let it go into any department, whether or not you are going to get an attractive cost benefit ratio. I doubt that very much is being done in that direction.

MR. GALLAGHER: We attempted to do some but it is pretty sketchy.

MR. DICKEY: I am Don Dickey, president of the Alaska State Chamber of Commerce. I have with me two well-known Alaska businessmen, Mr. Bill Scott, an accountant from Anchorage and Mr. Frank Murkowski, a banker from Fairbanks.

I want to first say we can all take pride in the voter response to the Permanent Fund, a two to one overwhelming support I think is an indication that people are interested in seeing the benefits of such a program. I would commend the Legislature for their efforts, Mr. Malone and Mr. Miller and any others I may not have seen, so that the record will indicate they did put the package before the public and gave them a chance to vote on it and this Committee has also. In fact, at noon Tuesday when people were voting on this issue, I had Mr. Edenso as a speaker. So we were confident that the public was going to accept it and we are delighted that you have met so promptly to get public input on the program.

Our purpose today, basically, is not to much to offer specific suggestions as to where the funds might be invested but

we will, in the future, be specific on that. But perhaps more to speak to the point of the goals, the objectives and the structure that we see might be helpful.

I think the Permanent Fund is an exciting concept, properly used can bring untold benefits to the widest cross-section of Alaskans. I think it has also the ability or the possibilities of abuse and, if abused, will create a boondoggle second to none that we've had and of unprecedented consequence. Hopefully, in our testimony I hope to bring that out. Our purpose is to suggest ways that it can avoid the rocks and shoals and that it can be a success.

About two years ago the State Business organization had a conference -- convention -- the theme, Can Alaska Afford Prosperity. And it wasn't a facetious question. We were asking ourselves -- most of us that had lived here for a number of years that we seem to thrive best in poverty, perhaps have had more experience with it and when we get prosperous, as we did once, and appear to be threatened again, we seem to have little problems of getting along together or just how that should be utilized, like a family does sometimes when they divide up the pot. So our suggestion today to you -- it is not a new subject to us, asking what we would do with our funds. We've been down this path before and we'll tell you something about that and offer some suggestions on how constructively we think this might be structured.

I am going to ask first from Bill Scott. He is past president of the Alaska State Chamber of Commerce. He is Alaska managing partner of the accounting firm of Peat, Marwick & Mitchell.

MR. SCOTT: Thank you, Don. There are a couple of things that seem to me important. They are more structural than the on-going things that Frank will mention.

Again, in the interest of being very brief, it seemed to me that in the structure of the Fund itself, in the management of it, it needs strong leadership. We have discussed this back and forth and I don't think that facet is disagreed with by many. But it seems to me that it needs to be in perhaps a separate State-created corporation or entity, it doesn't have to be a corporation, that would be answerable to the Legislature. Because it will, in fact, it seems to me to be the Legislature that will set many of the guidelines. That entity then should be headed by an able and strong leader who can implement policy as the Legislature dictates.

I believe that the Fund should have constant and on-going review, not only from the financial transaction standpoint but also from an operational analysis standpoint so that programs can be continually evaluated. And, third, it seems to me that what has been referred to in the national press as a sunset provision be part of the enabling legislation. So that, if three, four, five years down the track it is obvious

to everyone that the Fund is going awry, that the intitial purpose, while apparently valid at the beginning, no longer seems to be serving the wishes, that there can be automatic provisions for change in the structure without going through a complicated political process to arrive at that ability to change.

With that, I would like very much for Frank Murkowski to continue our presentation with some comments he has on more specific investment areas.

MR. DICKEY: Before Mr. Murkowski speaks, he has many titles. He is president of the Alaska Bank of the North, Fairbanks. He is chairman of the board of the Alaska State Chamber of Commerce. And probably of equal importance for your purpose today, he is former Commissioner of Economic Development and in that capacity had some involvement with loan funds so I think he can add something to your deliberation.

MR. MURKOWSKI: Thank you, Don. I would like to call your attention to one of the basis premises of the Permanent Fund in its concept, the statement that the fund is to be used for income producing investment. That really opens up a Pandora's Box. Not only to your Committee, but to the Legislature and the administration, the labor, business community and just the populace of the State as a whole. Because it implies all the grandiose benefits from such a substantial reserve, savings account, or whatever you want to

call it.

I would like to express some concerns I have directly in this area. And obviously being a banker I am automatically suspect from the standpoint that what I am going to say is basically that I don't want the State to compete with me in the loan business. The reason I say that is I don't feel the State can realistically involve itself in very, very broad loan programs for the benefit, theoretically, of the public as a whole in a very general way because of the politics that enters into these programs once they are established and the lack of independence that a State agency has in loaning funds. I am speaking very general and across the board in this respect. I've been there, I've handled State loan programs and I am very much aware of the political pressure that is brought to bear. It is all well meaning but it results in bad loans and severe losses. This is not necessarily the rule by any means, but there is enough of it to make for a great deal of concern. I think there are some specific programs, loan programs that can be handled and utilized. There are some very successful loan programs within the State. I would point out the Veterans loan program as one. But when you get into these very broad areas of providing loans that are, in effect, high risk. The individual who is living in a community will go to a legislator and say, "I've got a tremendous program here and I would appreciate your help" and he prevails without getting into

the credit worthiness of what the application is to the director who is responsible for the function and the pressures begin. And it results in some very, very difficult situations that can be avoided if it is properly structured.

I would suggest that the area that you look into initially are some the broad guarantee concepts. There is on the books at the present time, I believe it is called the Alaska State Industrial Corporation which allows the State ot use its tax exempt status. The concept I think came into effect, oh, about nine or ten years ago and it has never been used because there has been a reluctancy in the administration to allow the State's credit to be on the line in the concept of a guarantee. It has an application from the standpoint of providing the development of industries that are of high potential but yet high risk from the standpoint of other adequate markets in the State. I would use as an example one, the cement business in Alaska today. We certainly have all the resources to develop a cement manufacturing process but it is questionable whether the markets are here. But a guarantee program where the Permanent Fund could guarantee the bonds has an application. That type of program would result, in my opinion, in substantial new industry. It would not be a tax incentive per se, but it could have a very substantial assistance to the development of the industry.

I would suggest too that when thought is given to the

concept of participation in loans that you require high participation from the lending institutions, if you get into programs of that nature. I don't think 10 percent is adequate. I think 25 percent is more realistic. Because then the policing is done by the lending institution that is directly involved in the credit.

There are some applications in the area of renewable resources that you are going to get a great deal of testimony on. And I think one of the most paramount at this time that this Fund could really get involved in in the form of a guarantee concept would be in the area of agriculture. You are going to hear a lot about fish, mining, tourism, oil and gas, timber and whatnot. But the concept of making large tracts of land available by theoretically using a portion of the Permanent Fund, say, to clear the land. Then get into a lease-back, it's got to be a large corporation, total utilization development concepts, then they would pay it back off of the development of the land, you are creating some basic, new indusry within the State. You are creating jobs in a new area. And you're creating obviously substantial markets overseas for the products.

So, in conclusion, I would just leave you with the dire warning, if the program does get into an area where it is a broad loaning function, then politics is going to enter into it. And I would hate to see what is going to happen five or

ten years down the line because no administrator can hold up under that kind of pressure. I would be happy to answer any questions.

MR. GRUENING: Did you say the Veterans loan program was an example of one that ---

MR. MURKOWSKI: No, I specifically stated in my testimony that the Veterans program was an excellent program. There are many excellent programs. The Veterans program is not a broad loan program where somebody can come in with anything. It is secured by real estate, the safest kind of program there is.

MR. GRUENING: Is that because it's a housing loan?

MR. MURKOWSKI: That is one of the reasons, sure. It has specific guidelines and you have got to, in effect, have the collateral value. Specific guidelines. So it takes reasonable discretion out of it because you've got specifics. But you get into areas where you're projecting what the cash flow of a new business is going to be and you've got to be realistic with it and, if it's marginal, that means it is marginal and you've got to look at it that way. You can't kid yourself by saying, "Well, we hope this will happen and this will happen and, therefore, it will work".

MR. GRUENING: The fact that it is a home loan as opposed to say participating by the bank. Which factor is important?

MR. MURKOWSKI: There is no relationship. The real estate loan stands on its own. You've got guidelines and you loan a percentage to the value, you know what the value is and you look to the credit worthiness of the borrower. If he's got the income to pay for the loan, why, theoretically, he gets the loan.

MR. GRUENING: Why couldn't the same kind of criteria apply to any business loan.

MR. MURKOWSKI: Well, first of all, any kind of business loan doesn't fall into value. Usually the individual wants to start a business. He's an unknown entity. He has no operating experience. These are the usual type of loans that come into the State. He wants to borrow for the collateral, he has no equity. He might have a great idea.

MR. GALLAGHER: I'd like to throw a little light on this subject. When I was in the banking system, we reviewed our reserve for bad debts and 89 percent of our charge offs were commercial loans, 2 percent in real estate, and 9 percent were in installment loans.

MR. SCOTT: That says it all.

MR. GALLAGHER: We took all of our losses in commercial loans..

MR. MURKOWSKI: There is no politics in the Veterans program.

MR. SCOTT: I agree.

MR. GRUENING: I am interested in why you cannot insulate some of the politics from the business loan situation? You say there are no politics in the banks ---

MR. MURKOWSKI: Well, it's a different type of politics. The banker is going to go broke or he is going to eat his bad loans, but with the government it doesn't work that way.

MR. GRUENING: My question is, can't we make the people that are administering it responsible?

MR. MURKOWSKI: I think the people are responsible, it's the pressures they get. I think that the individuals, the Commissioners that are here would agree with me up to a point. There are several State loan programs in various departments. There has been a coordination in the last few years to get them together and they are getting together. Loaning money is just that, you need some real expertise. And, if you're making a secured type loan, there is a certain application of rules and regulations, that's one thing. But when you get out in the area of making a credit judgment where you don't have those sound rules to utilize, you've got, say, a new business, you've got to have somebody who has had some experience. And that's fine, you can get that theoretically but then you've got the legislator and I've seen it happen time and time again where you've got the constituent working on him. He's got a million things to do and one of them is not to evaluate that guy's loan. So he says,

"Well, you ought to talk to Joe Blow who is the director of that program" and he goes down and he says, "If there is anything you can do for Joe Blow" -- that's when the pressure starts and it really can develop. And, if you can figure out how to insulate it from politics, more power to you.

MR. GRUENING: I am asking for your suggestions.

MR. MURKOWSKI: I have no suggestions. I don't think it will work.

MR. MOTLEY: As administrator of 9 of the 11 programs you are talking about, I would like to discuss the matter with you.

The Veterans Loan program as of the first of this year had a delinquency of less than 2 percent. The average for all the State banks, including your bank, is 3.25 percent, 31 days or more. So I think that stands on itself there. In regard to the business loans, I don't think you are entirely correct when you say there is no collateral. I think all of the statutes affecting all of the business loan programs except one which is the new one of child care centers, requires collateral. What you say is correct, it can happen in the way you have talked. We inherited two loan programs from your old department, long after you left. One of them was the Alaska State Development Corporation. Those loans were loans that were made, you may recall, that were bought from banks. They had 16 out of 21 loans delinquent. The Small Business Development Corporation had 18

out of 21. Today there are 3. I submit to you that it can be run. You use the same test that banks use and that is a good underwriting procedure. You can insulate them from the political system. I think the record is there for it. I agree with you that the risk is there, the political risk of legislators and administration, but I think it can be overcome.

MR. MURKOWSKI: The Alaska Development Corporation hasn't functioned other than in a cleanup capacity.

MR. MOTLEY: That is a fulltime job, that cleanup.

MR. MURKOWSKI: So that has been the basic utilization of that office, it hasn't been functioning so far as taking on new loans.

MR. MOTLEY: That's right, just cleaning up the bad ones that were bought from the banks.

MR. MURKOWSKI: That is absolutely correct, there's no question about it. It was a bail-out for the banks.

MR. WOHLFORTH: Mr. Waldock.

MR. WALDOCK: I would like to direct my question to Mr. Dickey here. Rather than to reinvent a new wheel as far as a vehicle to handle out Permanent Fund, I would like to know if you would give your comments or the comments of the Chamber of Commerce in regard to the use of the vehicle that Frank Murkowski was talking about and that is the Alaska State Development Corporation. Realizing there are a few pitfalls with it, could you also comment about any safeguards that might be put in there

to beef that thing up?

MR. MURKOWSKI: Mr. Motley, I think that is under your department now.

MR. MOTLEY: The suggestion you had I think is an excellent one. I think if you had the banks in there with you then everybody has something at stake and you have two underwriting criteria.

MR. MURKOWSKI: If you keep the banks in enough and don't let them off with 5 or 10 percent. That program that Dennis is referring to, Tony, I think you will agree has a real application. It just hasn't been used because its been of real concern. Eric, I think you were involved.

MR. WOHLFORTH: I am aware of the Alaska State Development Corporation experience, which I don't think is as bad, frankly, that a lot of people, maybe the public has in mind. Back in '63 when it was started it did finance tourist facilities and other things that were needed and might not have gone forth. There was no question they took out some bad paper. And I think the point of a higher degree of private participation is absolutely the key to any reinstitution of that kind of vehicle.

MR. DICKEY: I might mention we worked about two years to get that first program through. Its intent was perfect, its performance was not. To respond to Mr. Murkowski's suggestion, I think one of the reasons there was too small involvement with

the private banking institutions. A greater partnership, I think they wouldn't walk away from it, they would be quite interested in how the thing turned out.

MR. LOVE: Mr. Murkowski, you said one of the benefits of having banks make the loans rather than having government make the loans is the bank has to take the loss.

MR. MURKOWSKI: Rather than the public.

MR. LOVE: But if the State gets into the business of guaranteeing loans that the banks make, doesn't, in fact, the bank make loans that the public takes a loss?

MR. MURKOWSKI: Well, as Mr. Motley indicated, if the bank has a substantial participation percentage, why, obviously the bank is going to spend a great deal more time analyzing the risk than if it had a 100 percent guarantee.

MR. LOVE: Say a 80 percent guarantee. My point is, the more the government gets involved in these loan programs, the less the bank has a stake in it. It seems to me --- You would normally have just a free market situation and I am just, you know ---

MR. MURKOWSKI: What I am suggesting to you is the question -- just on specific program -- loan programs, is it the best interest of all concerned that the State go into the direct lending programs or utilize the expertise that exist in the private sector by putting certain stipulations on the percentage of participation required by the banks, and then does the State

come in and utilize its principal put into this or does it guarantee a specific portion. You get the best of both worlds under the guarantee concept because you haven't used the principal.

MR. LOVE: So you think the primary benefit of channeling loans through banks is because banks are -- the primary benefits is because banks can better assess risks. That would be the primary goal.

MR. SCOTT: You are utilizing existing expertise.

MR. GALLAGHER: It seems like there are a whole lot of goals for the Permanent Fund. I know that the banks may be the best people to assess risks, but it seems like there are other goals we are going to have -- social goals. The point is, the strength of dealing with the banks is evaluating the area of risk by requiring bank participation. And you develop some integrity in the process.

MR. MURKOWSKI: I agree with you. But I would say that the area that banks generally fall into, which is the small, or short term loan, they have the expertise to continue in that area. If you are talking about providing some of the resource development that we need, I think this is where the State steps in. As the example I have given, a cement plant, the State has a vehicle through its guaranteed program, the agricultural ---

MR. MOTLEY: Large single loans.

MR. MURKOWSKI: Large single. The tremendous impacts on the State is where I see the Permanent Fund having a tremendous

application.. I don't think the State would have to use the principal in the Permanent Fund, the State could use the guaranteed concept of the Permanent Fund.

MR. MOTLEY: For large loans.

MR. SCOTT: As an aside, while it is almost certain, if not extremely probable, that any loan that is made within the State will have social impact. And the extent that it creates a better economy and new jobs, that social impact will be good under all the other guidelines that we go by. I don't believe that the social impact should be the prime consideration on a loan made from the Permanent Fund, or anybody else.

MR. LOVE: Do you think (inaudible) should be the principal goal of the Permanent Fund of do you think that we should look as principal goals as standards of the quality of life and whether or not certain types of development are necessarily good. I just wondered which direction we should work for?

MR. SCOTT: Why can't we have both?

MR. LOVE: Will you agree that our goals are going to be quality of life first and then we're going to look towards ---

MR. SCOTT: Every goal I ever had in my life was toward the bettering of the quality of my life and in the process of everybody else's that I dealt with.

MR. LOVE: The reason I bring this up, it seems to me there are going to be times when these can be best achieved

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through increased economic growth and times when it would adversely affect these.

MR. SCOTT: That to me has to be the Legislature's decision and not the administrators of a loan program. Separate the two. I think the two are separable and don't directly affect one another except incidentally. You're talking about different policies. We're talking about policies of investing and loaning and regenerating from the existing Permanent Fund. I don't think we're talking about trying to mix that in with social legislation or social goals of the State. They deserve attention but ---

MR. LOVE: I certainly agree that the legislators should be the people who provide the basic framework. Should we take a look at how the investment policies affect concentration of wealth and this sort of thing?

MR. SCOTT: I don't understand your question.

MR. LOVE: My question is, should we look in terms of who benefits the most economically by the investment, how is the wealth concentrated, who approves of the actual benefits, whether it is sub groups of society and that sort of thing.

MR. MURKOWSKI: Motherhood, everybody is in favor of that. I'm in favor of a cement plant because it's going to lower the cost of living in the State of Alaska ultimately.

MR. FREER: You made several remarks about I guess you call it an anti fail-safe mechanism. In case the Permanent Fund

started to get off track there would be some mechanism for calling a halt. This may be looking down the road quite a few years, but there might come a time when the Fund doesn't need any more. It might be drawing off revenue from the State which would be better used for something else than going into a Permanent Fund. Is that something that you might have had in mind?

MR. SCOTT: That is inherent in -- when I'm speaking of the sunset situation. We know of funds, of course, in other States where there was no provision for some ultimate termination and the fund continued to grow and nobody wanted it any more.

MR. FREER: That is inherent in what you were saying.

MR. SCOTT: I think you have to have the ability to stop it or modify it at a given point.

MR. WOHLFORD: Any more questions?

MR. EDENSO: I think this is directed at Mr. Murkowski. You were talking about loans and such, like business loans, any different kind of loan program the State may have. We are aware, at least I am, I have had some experience with State loan programs. We do have fixed interest rates an allowable range of interest rates and allowable terms. I wonder if you could address yourself to what you think might be reasonable terms, for example, a small loan program, whether it should have 10 years or 20 years, or 5 years, or whether or not it should have a fixed

interest rate, which we do now, 8 percent; or should the interest rate be tied to some kind of market rate of interest or that kind of thing? Terms, years, dollar amounts, ceilings, 100,000, 200,000, and interest rates, whether it should be tied to a market rate of interest.

MR. MURKOWSKI: Well, I can't necessarily come up with a blanket suggestion. I would comment with the application that obviously the borrower needs 10 years instead of 5. If he can't make it on 5, well, then realistically he's got to have 10. It is different in each particular case. The longer you put it out the more risk you have in subsidizing interest rates. I think there was a time when the Veterans Loan Fund was 7 percent when the price of money was greatly in excess of that. The State was effectively subsidizing the cost of money. Is that in the best interest of the State? I don't think it is.

MR. EDENSO: Probably what I am asking is, how much of a subsidy do you think would be reasonable in your small business loan program?

MR. MURKOWSKI: Well, obviously, from the private sector, I don't like the word subsidy because of what it implies. I don't think that the State loan programs per se should be subsidy programs from the standpoint of the application of the word subsidy.

MR. EDENSO: Mr. Murkowski, there is a hidden question in there and it is, if we tie it to a market rate of interest

which is what the banks very nearly do in this State, and we are, in fact, in danger of competing with the banks, commercial banks, in their area of activity, which is to provide the business community with business loans and with market money. If you get into that, and, again, we're talking about a potential competitive stance that a portion of a Permanent Fund may or may not have with the banking community. I believe you, as a banker, may have some specific ideas on that.

MR. MURKOWSKI: I think you have got to establish the priority that the Permanent Fund is going to apply itself to. How broad you want to get, if and when, or, if you get into a loan program on an expanded basis. And then, realistically, how you evaluate the services of the private sector as it serves the public in its loan needs. And should you only come into those areas that the private sector can't serve adequately. And who makes the decision whether the private sector is serving the public adequately. Obviously, if the individual comes to the private sector and is rejected because of the risk, he's going to go to the public sector and say, "We need more service from the public sector because the private sector isn't servicing our needs". And the public sector is going to respond because its obligation is to respond to the public. But then if the public sector theoretically makes that loan that is high risk and it goes sour, the taxpayer pays for it. So you get into evaluations here and judgments that you're going to working at for a long

time.

MR. EDENSO: I don't wish to argue with you but you also mentioned credit worthiness in your testimony, and credit worthiness, I am sure we all know, is one of the things taken into consideration in looking at a potential loan. Mr. Motley, I am sure, has had some experience with the State business loan program, credit worthiness. And we know that these, in the public sector, are designed for receiving high capital risk types of services. However, under the proposed Permanent Fund we have no designated area there the thing would be housed right now. Is that something that you have in the back of your mind or, as a banker, do you see the Permanent Fund providing high capital risk venture capital money to businessmen in this State, or through the banks to businessmen in this State?

MR. MURKOWSKI: I would have to decline to comment directly on that. How do you evaluate when something passes from high risk to reasonable credit. High risk, you're pretty darn'd sure you're going to take a loss.

MR. EDENSO: I am sure there are standards for comparison. At looking at other loan programs in the Lower 48, you do have venture capital firms that do this all the time.

MR. MURKOWSKI: But the rates they take are excessive.

MR. EDENSO: Exactly. You do have a high capital cost involved with venture capital. Those who are willing to loan in the venture capital area are also looking for a high return on

their investment.

MR. MURKOWSKI: Some of them take an equity position too.

MR. EDENSO: On the opposite side of the coin, or on the other side of the coin, you do have stable businesses that go belly up. Part of it we know has to do with management. However, again, we do look at venture capital type loans in the Permanent Fund -- will this be in direct competition with, or do you see it co-venturing with banks as well. In other words, are banks going to step into a venture capital on a partnership basis with the Permanent Fund?

MR. MURKOWSKI: I don't know. I can't give you a definitive answer.

MR. EDENSO: I have one other question. Would it be a consideration for the Permanent Fund on a loan policy to loan directly to a borrower, bypassing the banks entirely? How do you view that. Again, that is leaning more toward a competitive attitude with the banks. For example, in a very large size loan, such as 10 million dollars or, say, 5 million dollars, for 20 or 15 years, something of that nature, you know, whatever interest rate you might want to select. Do you see a problem with that?

MR. MURKOWSKI: Yes, I do, very definitely. I see a problem in the concept of the State developing a huge, gigantic overall, total-encompassing series of loan programs. If they get into that, they might as well buy out the banks. Theoretically, at least, they have the capital in the Permanent Fund to do so

and run a gigantic State bank. The we're just one step away from a welfare state then. You'd never be able to control the politics in it. I would suggest that you look hard and long at your loan programs because the problem is administrations change. State loan programs change with administrations. I think this particular administration has done an outstanding job with the loan programs they have.

MR. EDENSO: One of the purposes of my question is that we do have a very rapidly growing influence or segment in the business community in Alaska with 12 Native regional corporations, who have potentially a very high need or desire for capital. And they want to, in fact, use the credit, or somebody else's money, to the maximum extent possible to substantially influence their income opportunities. Suppose they do express a strong desire to participate in a Permanent Fund, would you see the banks as well participating in this kind of a development activity or lending activity?

MR. MURKOWSKI: The experience, I think, that most of the banks have had with the Native regional corporations is their effort to acquire whatever their particular interest is. They are in a position to put in an equity contribution that makes the long-term financing available for whatever they have in mind. So I don't think they really, at least at this point, have a problem as far as securing the private sector long-term funds.

MR. EDENSO: I am not referring to a problem. I am just

wondering if there is an existing vehicle, or there may be a problem at some point in time with that.

MR. WOHLFORTH: Part of the work session this afternoon deals with the structure of the Board or whatever it is that administers the Fund. I am wondering if any of the three of you would care to comment, at least tentatively, on how you would like to see such a Board structured. I am thinking, if you want appointments subject to the approval of a governor?

MR. KERTTULA: I wonder if I could interject something. This is more of a comment, Frank. If you are going to use a banking mechanism for screening short term or intermediate loans, you have to have a number of fail-safes. And the State has had a very bad, unfortunate relationship over the years with you fellows. Three come to mird. The hundred million wasn't much invested in the State to begin with and we got some pretty substantial "too bad, little boy" comments from fellows of such substance as the president of the First National. Two, we were foolishly using you fellows as a mechanism for investment on Wall Street in the equities, you lost millions for us and showed no great interest in getting yourselves up at 3:00 or 4:00 in the morning and getting on that Street early. And, three, you destroyed the State Development Bank, which was an interesting mechanism, which we would have put a hundred or two hundred million dollars into when we have the nine hundred million, if you hadn't mishandled that. Bailed out some bad loans. And the

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banks did finally come and pick up, some of you didn't, because of political and other pressures. We haven't had a good relationship with the banking community for these reasons. We're going to have to build some fail-safes into any programs we use. One, that you can't use existing loans on your books that aren't going good. Two, that as of the date of your request for any facility for the loans, none of those have been before you before. We've had a lot of bad relationships with the banking community where they're going to have to roll a peanut with their nose for a long time to overcome. Now, I favor ---

MR. SCOTT: We are not here representing the banks.

MR. KERTTULA: Now, I made a position, and I think these should be remade. You're going to have to develop some substantive method of showing us that we're not going to get screwed a fourth time by dealing with you fellows. There's a happy possibility of your using your screening expertise, of your willing to put up substantial amounts of money to correspond with the State's investments. All those things will help. We've had some pretty bitter experiences with you guys.

MR. MURKOWSKI: I think those of you who are familiar with the times of sale of the stocks that the State had acquired, the market was at an all-time low. If we had sold those stock within the last three months, we would have made a handsome profit. You go into the market and you take your chances. I obviously take issue with the generalization that the banks

lost the State money under the table or above the table or whatever. It was a matter of when they sold.

MR. KERTTULA: But we couldn't get them to actively participate on the Street on the method that had been suggested. We couldn't get them to get in there early in the morning. They were late on the Street. Those little suggestions found no adherence to.

MR. MURKOWSKI: I assure you they were working. It was a matter that the market went down. Maybe there was some poor advice on some of the stocks that were purchased. By the same token, those same stocks did come back. Be it as it may, the decision was made to sell, and they sold, and they sold at the bottom of the market and there was a loss.

MR. KERTTULA: That was a political decision, I suppose.

MR. MURKOWSKI: If it had been hung out for another six months or another year, it would have worked. Anyway, I agree with you. We've got a situation now where we've got a Permanent Fund, the question is, how do we work together to make it work. And a fail-safe system has got to be in there. It wasn't obviously in the Alaska State Development program. That did some good things but there was provisions where banks came in and got bailed out of bad loans and it is my testimony that that is wrong and shouldn't happen again.

MR. MOTLEY: I think I see some common ground between the Senator and Mr. Murkowski, and that is in the area of

participation in loans. If everybody has enough into the game, everybody scrutinizing the underwriter, I think there is merit in pursuing the guarantee. Candidly, I don't like guarantees because I think you have the lower end of the level of your underwritering criteria. But, if structured right, I think you can keep the underwriter criteria up there.

MR. WOHLFORTH: I really wonder at the productivity of reliving some of these things. If one looks at them, maybe there is a whole range of judgments and institutional factors that weren't what they should be. But we are trying to go forward and look forward. What sort of structure do you see as appropriate for the institution, corporation, whatever it is called now. The range of structures are as many as one can think of. Directly voted by the people is one. Secondly, appointed by the governor and confirmed by the Legislature for a fixed term, nonremovable except for gross dereliction of duty. No. 3, appointed to serve at the pleasure of the governor, which is the composition of most of our State boards and agencies, I think with the sole exception of the Board of Regents and maybe the Utility Commission. Have you given any thought to this? Do you want to comment on it. It is also, I might say, the subject of discussion this afternoon.

MR. DICKEY: It was, of course, passed on Tuesday. We have spent two days discussing that and arriving at the same philosophy that you have that, yes, it is a problem and it is

very important. We would like to reserve the right to come back and specifically address that. I think it is a key to this thing. We don't want to duck it at all. We want to come back in more detail. We appreciate the opportunity to be here and I would say at least the majority of the Committee was friendly -- all. We hope some of the suggestions will be of value. I am sure groups such as the Native corporations, the banking, and savings and loans groups, conservation groups, other consumer groups will come before you, as they should. I think that was one of the commendable things on the capital relocation, regardless of what you voted, at least the public was heard. And I think this Committee is starting out on that step and I commend you.

MR. WOHLFORTH: Thank you. I wonder how many more in the room this morning desire to testify. Three more.

MS. FLEISCHER: I am really looking for some information. I don't really understand the dividing line on subsidy. Isn't guaranteeing loans, say for a high risk cement industry with public money a form of subsidy? Or, if we use public money or bonds to build roads or hydroelectric plants, to help the mining, manufacturing industry, isn't that a form of subsidy? Or do you see that as a different kind of subsidy?

MR. MURKOWSKI: It's an interpretation obviously. If the mine can't be developed without it and then the road is built theoretically to open the mine, it provides jobs, it provides a tax base for the State and so forth. So it is returned,

theoretically.

MS. FLEISCHER: Theoretically, wouldn't there also be a return, say, on other forms of subsidies?

MR. MURKOWSKI: Yes.

MR. SCOTT: You can build a return into any program. A guaranteed program could provide a percentage rate in exchange for the guarantee. It doesn't have to be a loan of money to justify a rate of return.

DR. LOGSDON: I don't know how many high risk loans the banks make, but do the banks participate in equity in high risk loans?

MR. MURKOWSKI: No. Prohibited by law. In Canada banks can do it and in most foreign countries.

DR. LOGSDON: Do you see this as a possiblity for a loan fund on long term high risk?

MR. MURKOWSKI: With the State taking an equity? Not in the overall application. A road to a mine, that is an equity in that the State put the road in, it's for the public benefit.

I would like to just clarify for the record, in case anybody misunderstood my intent. I am harping to some extent on the pitfalls of broad, general loan programs. I think this administration particularly has done more to funnel, coordinate and get control of them. I think Tony agrees. Spent a lot of time cleaning up the debris from other administrations and has done an outstanding job of it. As far as the Alaska State

Development Corporation, I am not here to defend it or condemn it but the point that it didn't work in the concept that it was designed to do but it did do some good things. I wasn't in politics at that particular time.

MR. WOHLFORTH: Gentlemen, we certainly appreciate yo participation. Mr. Smith, Central Alaska Utilities.

MR. SMITH: Mr. Chairman and members of the Committee. I would like to represent, in effect, a program that we took to the Legislature in 1974 and again in 1975, in support of a fund to create a source of long term financing for public utilities operating in the State of Alaska. It might be somewhat redundant but the argument is still entirely valid. In the presentation that we made before Senator Kerttula's Commerce Committee supporting Senate Bill 116, the testimony was given in April of 1975. The bill was well received, it did not go forward, however, in the press of other business. In fact, I presume that there was inadequate funding available to do much with it.

I represent two entities. My name is Robert Smith, I am president and general manager of Central Alaska Utilities, a water utility supplying the suburban area in Anchorage. We have roughly 9,000 customers, we are serving a population in excess of 30,000 people in the Anchorage area. I am also president of the Alaska Utilities Association, which is an association of regulated utilities throughout Alaska consisting

not only of water utilities but gas, telephone, electric, refuse and various other utilities that are regulated by the Alaska Public Utilities Commission, of which there are some 143 different utilities. Now, of those 143, 33 are public or government owned such as municipal utilities. 95 are investor-owned utilities. And 15 are quasi-public or co-ops. All of which then represent and serve people entirely within the State of Alaska.

In the interest of saving time, I will just highlight the presentation that I gave before Senator Kerttula's committee and would certainly be happy to answer any questions. The Alaska Utilities Association, as such, does not represent or have membership of all of the regulated utilities, many of which are quite small, some of them fairly substantial. But of the 18 member utilities, some 55 to 65,000 people are actually being served or are represented by those utilities.

One primary difficulty that we all have faced characteristically over the years, and this is a national problem, not just in the State of Alaska, but the utilities have a great deal of difficulty in obtaining long range financing for the development of their facilities. Primarily, facilities such as reservoirs, transmission lines, extensions to serve new areas and source facilities such as wells and treatment plants. It is not apparently to the banking community or the financing community an attractive investment. However, the utilities are

one of the most stable operations anywhere in the country. Our product is absolutely essential to the maintenance of life and health. A community cannot grow, expand, or really even exist without the use of those utilities. Our customers are not subject to the vagrancies of inflation, particularly in a transient economy. Once the people are being served, if the community, unless it is abandoned, continues to use our service on pretty much of a level. And the great difficulty that we find is we build an installation that has a life from anywhere from 10 to 50 years, the 10 year would be a mechanical portion of the system. 30 to 50 years is the normal life of pipelines, reservoirs and the type of installations that we need to distribute our product.

Our problem has been we are virtually unable on the public financing market to obtain financing in excess of 7 to 10 years. The lending agencies just are not interested in that type of an institution or business. I think possibly because it is a low risk, low return type of operation, this has had some effect on obtaining long range financing. But generally we have had to operate on a long range improvement with very short range financing which puts an extremely severe burden on the utility. And the customers, in turn, either have to pay the higher cost or do without the service. We are in the process now of constructing two reservoirs in our own system, without which the area that we serve would have substandard fire protection, as an

example. We can provide the water necessary just to keep the system going without those reservoirs. But by providing the reservoirs, we offer a substantial benefit to the areas plus a degree of fire protection that we feel the customers are entitled to. If we can't finance them, we can't build them, it's just as simple as that.

We are also anxious that a program be established to set up a fund whereby those utilities that are regulated, or are designated as public utilities, all of which are regulated by the Alaska Public Utilities Commission, would have a source of financing available to them at a long range reasonable rate of interest. We are not asking for a grant program. I don't believe in it. I have operated both in the private sector and the public sector for many years professionally in this capacity. I don't believe in a grant program per se in this particular situation where there is a possibility of return. We feel that such a fund, if established, would be self-sustaining, it would have an earning power. And we are willing to provide that earning power on the base of our business operation. Now, our suggestion is, and it is not a critical or a magic figure, that a revolving fund maintained in the order of 10 million dollars would probably be adequate, at least for the time being, with the sounding that we got through various utilities. There could be a restriction as to the amount of funding provided to any given utility in any given year. This is no problem. It should,

however, have the basic criteria that, provided it is a proposition of reasonable risk, that long term financing be available, in excess desirably of 15 years, hopefully, in the order of 20, 25 or even 30-year financing.

The problem is, if we go out to build an improvement that has a 30 to 50 year life, it's depreciated on that basis. We depreciate our system essentially on a 33 year life. If we have to fund it and pay the funding off, pay the loan off in a 5 to 7 year period, it is a severe burden on the utility. The cash flow has to be generated and the only place that that can be generated is from the customers. This is set up in the rates and the customers obviously have to pay the bill and it puts a burden on them, or they don't get the service.

I do have copies of the testimony that was given before the Committee, which I believe explains the situation and I would be happy to leave those with the Committee. We have several letters that we received from members of the Association regarding their feelings concerning such a Permanent Fund and their anticipated use of such a fund. We have letters from the Light & Power Company, Kenai Utility Service Corporation, immediately available. All of whom have expressed sincere interest in the funding. We have had verbal expression from many of the members of the Association along this same line. I also have a copy of the bill that was introduced, Senate Bill 116 together with letters that we have sent to legislators outlining

the problem, expressing our feelings as to the need for this kind of program. And a letter of information also that was sent to the Alaska Utilities Association membership detailing what we are trying to do and soliciting their support.

I have just touched on why that fund is necessary. We feel it is necessary. We feel it is a good risk. Money that will be spent entirely within the State of Alaska and the benefits would be entirely for Alaskans. We are asking for a program in which monies would be borrowed and they would be repaid with interest. The key to the whole situation is that we need a vehicle whereby funding is made available to utilities which are vital to the existence economy, health and happiness to the people of the State of Alaska and which are essentially not now available. That is essentially our pitch for this program.

MR. GALLAGHER: Is it not true, Mr. Smith, that with the existence of the public utility any subsidy, I am thinking in terms of interest rate, does get passed onto the consumer through the rate making process?

MR. SMITH: That's correct.

MR. GALLAGHER: Both for the private and the public utility.

MR. SMITH: Absolutely correct. The cost of doing business is paid for by the customer whether it is in a department store or a utility company.

MR. LOVE: As I understand, you want long term loans.

MR. SMITH: Long term loans with a reasonable rate of interest is what we are suggesting.

MR. LOVE: What is easonable rate of interest?

MR. SMITH: 3 percent, 9 percent I believe is the ceiling on the existing funds now.

MR. LOVE: As I understand it, the basic problem in financing utilities isn't the problem of the interest rates, it's the problem, it is securing a long term loan.

MR. SMITH: The key problem is the term, not the interest rate. Obviously, the higher the interest, the more the customer has to pay for the money and the service. However, that is not as big a problem, it can be overcome and still operate within a reasonable area provided we can get the term.

MR. LOVE: If the State gets in the area of making loans to utilities, do you think that would raise the question of whether or not the Permanent Fund be used to promote public ownership of utilities?

MR. SMITH: I think they are two and completely distinct areas. I really don't think that one has any bearing on the other. I have spent about 12 years operating public utilities, City Engineer, and Public Works Director, and I have during the entire period of time always felt that private industries supply whatever services they can feasibly and government only then should supply those that cannot be done privately. In answer

to your question, I think they are two separate areas. I think it should stand on its own merits as a good business investment.

MR. WALDOCK: Mr. Smith, if the Permanent Fund should find that investing in the utilities is a prudent investment, what kind of return could we expect on our money?

MR. SMITH: In terms of an interest rate?

MR. WALDOCK: Yes.

MR. SMITH: Well, that obviously is going to be up to the Legislature to decide. I believe interest rates on the existing funds are in the order of 8 to 9 percent.

MR. WALDOCK: 8 to 9 percent.

MR. SMITH: Those exist now, I understand.

MR. GALLAGHER: If we go back over a period of time, we will see that in 1951 long term low interest was in terms of 3 to 4 percent. And if you look at the inflation rate in that period of time, it would be maybe 1 percent. Then go back to the late middle '50's you will find that long term low interest was in the terms of 5 to 6 percent. In that period of time, inflation was 3 percent. Today inflation may be 7 percent long term. And that is why rates of 8 and 9 percent -- again, it's really an adjustment on the rate of inflation and not -- economics haven't changed since then.

MR. SMITH: Yes, I agree.

MR. WOHLFORTH: Is there a question of whether or not it should be market rate, is that what you are essentially saying?

MR. SMITH: Well, that isn't really our question. Yes, I feel it should be somewhere related to market rate, yes, absolutely. I don't feel that it is our position to attempt to set the rate, however. And this is why I phrased it a reasonable rate of interest, because I think it should be. I honestly do.

DR. LOGSDON: If I understand you correctly, are you suggesting that the Permanent Fund should be subdivided into categories? I notice that you have talked in terms of 10 million dollars as a separate fund within the Permanent Fund.

MR. SMITH: I would for the particular reason that -- possibly it is somewhat selfish, but I think it was also mentioned by Mr. Murkowski in his testimony, it does designate a particular area with a particular level of financing so that the utilities have some means of planning and programming and also the State does too. They know what areas they are working in and with what amounts and are not in a position jockeying, say for example, the fisheries over the same funding to see who gets there first. So I would like to see it designated at a particular level or a particular fund for that specific use, and that is the use of utilities. I am not trying to relegate this to just water utilities or just investor owned water utilities or whatever. Although I think that would be the heavier use since municipal utilities do have the availability of bond funds that we don't have. But I would like to see it designated as a particular fund, yes.

MR. MOTLEY: Just a recap. Is the main resistance in the private sector in raising money coming from the term, the length of the term as opposed to the interest rate?

MR. SMITH: Basically, that's true. That's absolutely correct.

MR. MOTLEY: Mr. Chairman, I must tell you I find it most refreshing that Mr. Smith thinks 8 or 9 percent is a reasonable interest rate. Other groups that we deal with on occasion believe 2 or 3 to be reasonable.

MR. SMITH: I would certainly accept a rate of 2 or 3 percent. But that it not really why I am here because I don't think it is realistic.

MR. LOVE: How would utilities look at loans from the Permanent Fund with an interest rate that would be readjusted every five years?

MR. SMITH: I don't think that would be really unreasonable, although I think it would be somewhat unusual.

MR. LOVE: I know they are doing that with home mortgages.

MR. SMITH: Yes, and we have considered it on that basis. Again, our primary difficulty is the term rather than the interest. Because the interest rate is an element that is easy to identify and it is an ongoing expense and one that can be readily incorporated in the rate base. I don't think that is entirely unreasonable, if it can be set up on a workable basis.

MR. LOVE: The problem of financing utilities, is it a rural problem, an urban problem, or a Statewide problem?

MR. SMITH: I think it is a national problem. I belong to a national association of investor-owned water utilities and that seems to be the trend of it regardless of the size of the utility. American Water Company, General Water Company, Central Alaska Utilities, Eagle River Utilities, they all seem to have that common problem of lack of available funding.

MR. LOVE: Are most of the investor utilities in urban areas in Alaska?

MR. SMITH: In Alaska? I can't really speak for that entirely. I presume largely that is true although there is probably a large scattering of small utilities that are serving suburban or rural areas simply because there is nobody else there to do it. I would say we are probably far and away the largest investor-owned water utility in the State and probably the third largest water utility as such that operate in a suburban area.

MR. GALLAGHER: What is you own capital need?

MR. SMITH: Roughly a million dollars a year. It goes out very easily and very fast. The water comes free, we've been accused of selling a commodity we get for nothing and we have offered as a counter to that that anybody who wants to come to the well with their own bucket, we'll supply them free water. Two

reservoirs that we are just completing now are roughly on the order of 750,000 dollars. We are spending presently about 1-1/2 to 2 million dollars a year on capital improvements on our own system. Those are funds that are derived from our cash flow, but largely, probably two-thirds to three-fourths of those funds are coming from developers as a cost of development of a subdivision and that has certain benefits. They are providing the financing in those particular areas, however, they are only interested and capable of providing the facilities directly within their subdivisions. It does not accomplish such things as building reservoirs. It also puts quite a burden on the developer. As you all know, the cost of lots in the Anchorage area is at a ridiculous level at the present time. 20 to 23,000 dollars for a subdivision lot. Largely because of the cost of development. We also have individual home owners or people within a neighborhood that are existent but need the service but flat can't afford it and we can't afford to finance it for them. We have had to establish, since we are not in the lending business, for those few cases that absolutely had to have it and could not come up with the money, provided a 3-year financing program at an extremely high rate of interest, about 14.5, 5 percent. Simply because we had to be in the position of enabling them to get the service and there was no other way to do it. We would rather not be in the financing business. The same, conversely, if we have the long term financing available and it

can be established that an extension, for example into a new area will accomplish a great deal of good and a return over a period of time, I think it is a good investment. It would also then enable you gentlemen to finance that improvement and let the people take advantage of the long term financing as opposed to a two and three year program as we have now. It is an extreme hardship in many cases.

MR. WOHLFORTH: That was a very eloquent presentation, sir, and we appreciate your coming forward.

MR. SMITH: We appreciate the opportunity to be heard. I would like just to part on one final shot. The money is, again, to be spent entirely within Alaskan industry and the service that we provide is entirely to Alaska.

MR. CRAWFORD: What is the breakdown as far as water utilities and electrical utilities as compared to REA?

MR. SMITH: I can't honestly say. I believe we only have one REA in the group. All of the regulated utilities are not members of the Association. We have opened the membership and invited membership of all the regulated utilities. Of the 143 that are regulated, I believe 18 are actual operating members. Many of them are extremely small. Some of them are REA's and they haven't expressed any particular interest nor have the municipals. I believe we have two municipals. It is also a new organization. We are just putting it together. Essentially, we started this thing with the idea of generating

support for this loan program. So, primarily, those utilities that were interested in the loan program itself immediately joined and have been active in it.

MR. CRAWFORD: This is primarily electricity.

MR. SMITH: We have extended membership to everybody that is a regulated utility. Our membership even includes a couple of TV operators.

DR. LOGSDON: Did I understand you to say there were 143 utilities?

MR. SMITH: By our count from the PUC list there are 143 regulated utilities.

DR. LOGSDON: Did I understand you to say 10 million dollars?

MR. SMITH: Well, we picked a figure that we felt was reasonable based on our queries of the various utilities and what they felt their needs might be. We picked a figure of 10 million dollars. A level of 10 million dollars to be available during any given year with no utility receiving more than a million dollars at a throw.

MR. EDENSO: One question I have is, what is the average or the normal turnover rate for long term debt in Alaska utilities? In other words, how long is the average long term debt kept on the books?

MR. SMITH: Do you mean the term of the various programs? There are some that have been reported to us -- I

don't have a real reading on it. Just the few reports that we have had. We did get a response from one utility that had a 30-year loan. We, ourselves, happen to have an SBA loan, it was a disaster loan, which was a 30-year loan. The balance of our funding has been 5 to 7 years that we have been able to get on the open market.

MR. EDENSO: I understand that. But on the average for the utilities in Alaska, you don't have long term debt.

MR. SMITH: Except in extreme or unusual cases, long term debt has not been available for the utilities.

MR. EDENSO: What I am getting at is, would 10 million dollars be adequate if you have an average life of your long term debt of 30 years?

MR. SMITH: Well, there are a number of factors that are going to govern this. One is the rate of expansion of a given utility for a particular area. In our specific case, we're going 10 to 15 percent a year so our needs are greater. A million dollars a year essentially would satisfy our need. So trying to use that as a criteria, we're trying to make a projection without having all the facts available and maybe 10 million dollars would be light. I don't know. I honestly don't know. Chances are, if the fund was once established and put into use, and the utilities aware of its use and methods of operation, then 10 million wouldn't be sufficient. But we are trying to start -- to put a parameter on the thing, we are trying to start

with a figure.

MR. EDENSO: Do you know what the total asset dollar value is for the utilities in the State?

MR. SMITH: No, I honestly don't.

MR. EDENSO: In excess of 300 million dollars?

MR. SMITH: Yes, I would say that is very easily true. In our case, we're roughly a 20 million dollar operation and this is water only.

MR. EDENSO: Do you have a feeling that the demand for expansion and demand for utilities in the State, has there been any kind of information of that nature available to you?

MR. SMITH: No, there hasn't.

MR. EDENSO: 10 to 15 percent is your growth rate.

MR. SMITH: That has been our pattern of growth, that is correct.

MR. LOVE: Could we receive some of that information from the Public Utilities Commission?

MR. WOHLFORTH: That occurred to me that is where all the figures are.

MR. SMITH: That is the one clearing house source of information. Every utility is required to file an annual report to the Commission. The Commission is aware, incidentally, our our presentation and did support us in this presentation to the Commerce Committee.

MR. WOHLFORTH: Thank you again, sir. Any more

questions?

MS. FLEISCHER: Are you talking about two different kinds of financing programs, one for the utilities. But also a separate financing for individuals who may need ---

MR. SMITH: No. I feel that, if such long term financing was available to the utilities themselves, then they would be able to provide that service to their customers. Thank you very much.

MR. WOHLFORTH: Two gentlemen from the Home Federal Savings & Loan have been sitting very patiently. The chairman of the board and the president.

MR. BOWDEN: I am Dwight Bowden, chairman of the board of the Home Federal Savings & Loan Association. I am also a real estate broker and primarily interested in residential housing.

Our interest here this morning as members of the savings & loan community, having known about this for a very short time, we have had a limited amount of time to discuss the Permanent Fund with the other members of the savings and loan community. However, we feel that our views will only differ by degree with the other savings and loans.

Paul Kapansky is here as president of Home Federal Savings & Loan.

We feel one of the excellent uses of the Permanent Fund would be as a secondary market for

residential home loans or possibly as multi family housing loans in the State of Alaska.

Alaska has always been a capital-short state and the banks and the savings and loans have traditionally only been able to make loans if they were able to sell them to some Outside investors. Outside investors always look at Alaska and considered Alaska as a capital-short state and automatically our rates go up a point or two over if they were buying a loan in their own neighborhood. We feel that the Permanent Fund could well be used as a competitive market and possibly at rates that would allow Alaskans to own their own home, or keep housing costs down.

Of course, another big factor in the cost of housing in Alaska is all the fees that are charged to the developer at the time that he takes out a loan because of high risk and the fact that Alaska is a capital-short state. In order to compensate for that risk, the Outside investor wants very substantial fees. But we do feel this is an area the Permanent Fund could get into at fairly low risk and provide much needed housing for Alaskans who can't afford it.

MR. KAPANSKY: I think that we also feel that not only to compete with some of the existing secondary markets but perhaps create a secondary market where there is none, primarily residential lending. There does not seem to be any problem in finding a secondary market for some of our housing with a loan up

to 68.750. Anything above that with the exception of the state gets more difficult. As you are probably aware, many of our homes up here sell for considerably more than 68,750. And this have a tendency to put a crimp on some of the sales of these homes. Our primary secondary markets and I speak specifically for Home Federal on that and not necessarily for the S & L industry up here, the Federal Home Loan Mortgage Company. Although they do purchase mortgages, if they follow within certain criteria up to 68,750, they also have criteria for certain areas which they will not purchase the mortgages in. It doesn't necessarily mean that these areas are a more risky area, it's just that they have come up with certain criteria that says we will not purchase these. They do not live in the area and are not all that familiar with it. I don't think the loans are any riskier, and perhaps the Permanent Fund could be used to supplement that also.

When we get involved in commercial projects, it has been my experience, as I think Mr. Bowden has indicated, it is an extremely capital-short state. The S & L's, the financial institutions Outside realize this. When you attempt to put together a project or a package, and although it may be a very strong package, when you go to peddle it down there and deal with them, they realize you don't have too many alternatives and perhaps in order to put the package together you have to pay their points and you perhaps have to pay a higher rate as opposed

to if we had something within the State of Alaska which perhaps we would not have to charge the buyer or the builder as much.

MR. MOTLEY: Do you sell any of your loans to the Alaska Housing Finance Corporation?

MR. KAPANSKY: Yes, we do.

MR. MOTLEY: Is their rate more competitive than the Freddie Mack?

MR. KAPANSKY: I think their rate is -- they are normally lower because it is for a qualified buyer. I think it allows people who would not ordinarily be able to purchase a house to purchase one.

MR. MOTLEY: Are their geographical restrictions a lot more liberal? You talked about restraints that Freddie Mack had and you meant geographical?

MR. KAPANSKY: That is right.

MR. MOTLEY: Those don't appear in the Alaska Housing Finance Corporation, is that correct? In other words, there are no geographical restrictions.

MR. KAPANSKY: I don't believe there are.

MR. MOTLEY: So that settles that aspect of what you are talking about.

MR. KAPANSKY: Not necessarily. Alaska Housing Finance, to my understanding, is set up on a per family per income basis. In other words, if you make over "X" dollar amount and only have two children.

MR. MOTLEY: We are talking about geographical now. Not income limitations. I would assume that you don't sell more to them because there isn't that much Alaska Housing Finance Corporation money available. Is that a fair statement or not?

MR. KAPANSKY: The reason we don't sell more to them is you once again get into the income limitations.

MR. MOTLEY: Income limitation is the problem.

MR. KAPANSKY: Yes.

MR. MOTLEY: The reason I bring it out is because I think what you are saying is a very valid point in regard to the difficulty of finding a secondary market. Alaska Housing Finance Corporation has attempted to fill that to a certain extent, but there is such a big market. I think it might be a useful thing to explore. The vehicle is there if it had more dough, would you agree to that?

MR. LOVE: I believe you were talking about redlining when you were talking about certain areas. I mean there are certain areas of the state ---

MR. KAPANSKY: Certain areas of the state secondary markets do not care to invest in.

MS. FLEISCHER: Such as?

MR.KAPANSKY: I couldn't tell you specifically off the top of my head.

MR. LOVE: Are there any areas in Anchorage that are redlined?

MR. KAPANSKY: Probably areas in Mountain View, and they call that a transitionary area, going from single family to multi family.

MR. LOVE: We are not just talking about Dillingham and Barrow?

MR. KAPANSKY: No, we're talking about here in Anchorage.

MR. BOWDEN: For instance, they won't normally purchase a loan on a single family home zoned for a higher use. Anything that is in a transition area. Possibly an older residential area that is in transition to a commercial use.

MS. FLEISCHER: Who makes the decision as to whether it is in transition?

MR. KAPANSKY: The secondary -- they have representatives who come up here on occasion and they also have their own appraiser who checks out the areas also.

MR. LOVE: You are suggesting we start government loan programs for homes over the 70,000 dollar bracket to 80,000, 90,000. It seems odd to me that the government would want to provide government loan programs for people who can afford to buy an 80,000 dollar home.

MR. WOHLFORTH: We are talking about the secondary market.

MR. KAPANSKY: The secondary market. Because that is extremely limited. As you are aware, this is a capital-short

state so you can only make so many home loan mortgages.

MR. LOVE: My question is whether or not that should be a priority ---

MR. KAPANSKY: I think essentially what you are saying is because a person can afford a 70,000 or 80,000 dollar house and many banks up here cannot afford to portfolio those, so therefore that person should not be afforded the opportunity to purchase one of those homes.

MR. LOVE: It seems odd to me, a government effort at a social loan program ---

MR. KAPANSKY: You are saying he should purchase it but where is he going to get the financing.

MR. LOVE: That's his problem.

MR. BOWDEN: He's saying there aren't funds available and you're saying that's tough.

MR. MOTLEY: I think you have missed the whole point of the secondary mortgage.

MR. LOVE: I don't think I did. I think I understood exactly what he is saying. I have a couple of other questions here.

MR. WOHLFORTH: Are they questions?

MR. LOVE: Yes, they are questions. Do you think we look more towards being involved in the house market whether it is multi or single family homes because of the increasing cost of the single family home. How realistic do you think it

is over the long run to really think in terms of providing single family homes?

MR. BOWDEN: I would say multi family housing is going to be priced in the range that more people can afford than a single family home on its own lot because of the high cost of land and the high cost of developing that land. I would say any developer or builder in the Anchorage area would be quite happy if he could develop and build a home to sell for 60,000 dollars or less. But it is a virtual impossibility because the economics just aren't there.

MR. KAPANSKY: We haven't gotten that involved.

MR. BOWDEN: We're very small.

MR. LOVE: Rehabilitation loans for houses. Is that an area where the current money markets aren't serving those needs?

MR. KAPANSKY: You're talking about home improvement loans? I can't speak for all the S & L's but I know we are quite active in it. And once again, something because of our size, which we have to look at, we can only tie so much in portfolio because in our business -- once again, because we are young and haven't established a good servicing market, what I mean by that is selling houses on the secondary market, most of the mortgages which we look at as a matter of survival have to be salable markets and that is dictated by the secondary market.

MR. LOVE: There is going to be, I think, a big move

to have the Permanent Fund get involved in housing. A number of the legislators made that part of their campaign. Housing is a real tough item here and I think it important that we get comments from the banks and savings and loan industry. In just exactly what areas are needs in terms of financing. The secondary market is not buying these second deeds or not buying home improvement loans. I would be interested in the future in hearing more.

What would you think if the Permanent Fund Committee or whatever said, we won't put dough into the savings and loans that utilize the proxies? Would that be objectionable to your institution?

MR. BOWDEN: What would be the objective of such a regulation?

MR. LOVE: Well, just to give the people that put the money in the bank a more democratic control over the system, like the system was supposed to be when it was originally set up. In most banks there is not very much respect for control by depositors ---

MR. KAPANSKY: Once again, I think you're dealing with the nature of the animal, if they chose to have a voice which I am not assuming they want. And then from a practical standpoint, as you are aware now, perhaps a municipality, on occasion they put funds up for bid. One of the restrictions is that we cannot collateralize deposits. So, therefore, we, in most instances,

can only bid on 100,000 dollars in increments. So if you are talking about putting funds into permanent funds which come from one source. But if you chose not to have it collateralized, yes, it might be helpful.

MR. LOVE: I'm talking about the secondary money market.

MR. KAPANSKY: What you are saying is that because we are controlled by proxy, therefore, you shouldn't purchase our --- We contribute to the economy and we put 15 million in loans into the economy.

MR. LOVE: What do you think of that idea?

MR. KAPANSKY: To me it doesn't make sense.

MR. GALLAGHER: As you are aware, the Department of Revenue put out of the pension fund large quantities of money into housing. Is that program a successful program?

MR. KAPANSKY: I can't speak for the whole industry. But at Home Federal we have utilized every nickel that we have been able to get our hands on.

MR. GALLAGHER: Has it satisfied that market, or is that market quite a bit bigger than ---

MR. KAPANSKY: It's quite a lot bigger than you have funds to utilize. As a matter of volume, I can't put it into -- whether it's 68.750 or whatever. The S & L industry approximately made about 199 loans last year. So we do contribute quite a bit to the economy. For instance teachers retirement, I think there is more in need that you have funds.

MS. FLEISCHER: I just wondered what the income limitation is. For Alaska housing the problem was, you said, income limitation.

MR. KAPANSKY: I couldn't say specifically but I think the formula they use is it varies on the size of your family. A person may make 24,000 dollars a year and have no dependents and are not qualified. But a person making 24,000 dollars a year and having three dependents would qualify. So it goes in various increments and stages.

MS. FLEISCHER: So, basically, it is for low income people.

MR. KAPANSKY: Essentially.

MS. FLEISCHER: My question was, knowing the housing market here, are there houses available for people if they are really low income?

MR. KAPANSKY: The average home up here is about between 60 and 70,000 dollars. When you look at it in mortgage payments of existing rates of 9 or 9-1/2, you're looking at a monthly payment of 650 or 750 dollars. And generally the rule of thumb that we use and the secondary market uses, because we have to sell our loans through the secondary market, we're tied into that. They look to an income ratio of about, their monthly payment to their gross monthly income of about 25 percent. So at a 650 dollar monthly payment, you're looking at an income of 30,000 dollars a year.

MS. FLEISCHER: But you're saying that if there were, if the State would provide that secondary market, then possibly the State could meet its own needs.

MR. BOWDEN: Set your own criteria.

MR. KAPANKY: Set your own criteria and I think you would open up the housing market a little bit more to people which now can't afford it.

MR. WOHLFORTH: Are there any other questions? If not, we thank you very much, gentlemen.

MR. FLEETWOOD: I'm Al Fleetwood, and I am appearing here today in my capacity of Secretary-Treasurer of the Alaska Bankers Association. My presentation is in behalf of the Alaska Bankers Association.

In particular, the Alaska Banks Association is pleased to support the creation of a Permanent Fund, and congratulates the Legislature on its foresight in giving the voters of Alaska the opportunity to approve this concept.

You have invited us to submit suggestions concerning the use and policies governing the Permanent Fund. We appreciate this opportunity to participate and certainly pledge our fullest support and cooperation and assistance in your efforts to establish the policies for the best possible use of the fund.

The fund can be used as an economic stabilizer. It is our position that it should be structred and maintained as a Trust for the lasting benefit of the citizens of the State of

Alaska.

As such, all objectives, investment policies and guidelines should be established within the context of the "reasonable or prudent-man" investment principle.

So managed, we feel that the Permanent Fund can be a tremendous asset for our State in terms of both a capital source for future development and a cushion for a possible period of inadequate State revenues. It should be treated as a trust fund for the Alaskans of the future.

At this time, we are actually not prepared to make definitive suggestions as to how to best achieve what we are sure would be our mutual goals. We are hopeful that we may have sufficient time to develop specific suggestions for your consideration, believing that a little more time at this time will be worthwhile for such a far-reaching function. It is hoped that we can have meaningful recommendations in your hands in about 45 days.

Again, I thank you for this opportunity and look forward to our next meeting. That's about it.

MR. WOHLFORTH: Any questions to Mr. Fleetwood?

MR KERTTULA: That is a good presentation.

MR. FLEETWOOD: Well, we mean to establish an eager foot in the door.

MR. LOVE: One suggestion, will the Association try and come back with some specific suggestions for how to deal with

some of the problems which have been brought up, some of the ways or protecting the interest of the State from political maniuplation and also bank participation. We're not going to be stuck with bad loans. I would like it if I could just see some specific proposals presented to us from the Association that we can look at in terms of amounts of bank participation.

MR. FLEETWOOD: Let me give you a little bit of background of our meeting. I wish the Permanent Fund could be invested in something in the Post Office to make its system more efficient, but we got out our mailing list and most of them had just one day in order to come to the meeting and all but one bank in the whole area was represented at that meeting. It's difficult to get all the banks together, but they are committed to come up with some composite position. And I think you're going to get this. I am interested to see what will come out of it also but I think it will be very, very meaningful to your Committee.

MR. KERTTULA: You think you can stretch across the State banking and mutuals and the whole works.

MR. FLEETWOOD: Yes. They are all members with the exception of the S & L's. But if we can't come up with a composite position on all points, we just don't address those points.

MR. KERTTULA: The medical fraternity did that and their composite position put the public right straight in the

middle. I hope yours doesn't.

MR. FLEETWOOD: I hope it doesn't too.

MS. FLEISCHER: I just wanted to ask, when you're saying a composite position, on the goals of the Fund as well as well as the structure?

MR. FLEETWOOD: Yes.

MR. KERTTULA: The only thing you could ever get together on before, Al, was raising the interest rates.

MR. WOHLFORTH: Any questions? If not, we thank you very much.

(RECESS AT 12:00 NOON AND RECONVENED AT 2:00 O'CLOCK)

MR. WOHLFORTH: The afternoon session of the Investment Advisory Committee considering the Permanent Fund. We do have scheduled a report from Mr. Ken Butler of White Weld on leverage financing, however, I was told that he is not here, is that correct?

MR. FUHRMANN: Yes.

MR. WOHLFORTH: We are fortunate to have two other representatives of that firm and, if they will introduce themselves to the audience, they can proceed with their comments.

MR. FUHRMANN: I am Charles Fuhrmann and with me is Ted Swick. We are from our New York office.

We were asked to comment in an introductory fashion today on the use of leverage in the Permanent Fund, or the

possibilities of such use. It is our feeling that it is premature for a detailed discussion of leverage because the goals and objectives of the fund, which are an integral part to any decisions about the use of leverage and its appropriatness have not been established. Nor has there been a decision taken as to whether or not leverage is appropriate for the Fund. We agree that it is appropriate for Committee members to be aware of the possibilities of leverage so that they can focus on those decisions.

The Fund itself is going to have a pool of funds and a future cash flow. The cash flow being by statute at least 25 percent of various revenues which can be projected by analyists government officials and the financial community. And leverage should be a means magnifying the influence and maximizing the economic impact of the Fund. And there are various ways of doing that. One is by direct borrowing of the Fund, either tax exempt borrowings, if the funds to be borrowed are going to be used in certain fashions. That possibility exists and Ted will discuss that in greater detail in a moment. Or straight debt issues in either the public or private capital markets where the Fund was the borrower.

Among the various development banks and other funds in the world, many have used borrowings on their own assets either from their governments or from the public or private market. Some of the other funds are actually the borrowing

entities for their public agencies and for other purposes, and so there are all kinds of possibilities with respect to borrowing. You can borrow long, you can borrow longer, you can borrow longest. And, as I say, they are either the public or private market and you can be issuing either tax exempt or straight securities.

Another means of leverage and one that has been discussed briefly here this morning is the use of guarantees, which allow you to have a multiple effect in the use of your assets rather than being limited to the assets themselves, you could extend guarantees of other people's securities to an extent much greater than the assets you have. And the value of the guarantee would be based on the amount of leverage you created and the form of the collateral behind the guarantee. Whether you have created a pool of cash or a pool of investments against which the guarantees are issued, or whether you were guaranteeing strictly against the future cash flows anticipated by the Fund. Some people have used guarantee limits of 10 times assets, 5 times assets, 20 times assets. And the value of that guarantee is dependent upon the amount of assets or earning power or future cash flow behind the entity issuing the guarantee. These guarantees could be extended to public -- other public financings, from Alaska authorities, or to private credits.

In addition, there are several forms of Federal borrowing entities or programs that provide guarantees which

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depend upon and given to people on the basis of the equity behind the issue. I refer, for example, to Title 11 financing, which is available at the Federal level for the building of a merchant marine operation, ships, or vessels or any kind. And the U. S. Government extends guarantees up to 87-1/2 percent, vessels built using the Title 11 program. And they expect those vessels to have a 12-1/2 percent equity interest in them. And their willingness to give those guarantees is often dependent upon the strength of that equity. And there are also possibilities there for guaranteeing the equity and not just the debt of other entities in order to get them to qualify for programs that already exist on the Federal level. Sometimes guarantees can take the form of guarantee of performance beyond the principal and interest payments on debt then. They can also be related to equity performance.

A third means of leveraging the Fund or at least maximizing the economic impact, is the form of the participation or financial participation you take in a project's financial structure. As opposed to being the lender on a senior basis to a project, any consideration on the part of the Fund to take subordinate positions, either equity or subordinated debt securities. Encourage and facilitate the participation of private capital, because they come from behind that capital and create a sense of security and minimize the risk to that capital. And, in this way, you have the means of expanding the size of the

projects you can participate in without having to be the total lender.

Discussed this morning was participation -- participating only with private capital and that may be an attractive alternative but oftentimes you will find with some of the projects you may wish to consider, that private capital will not be available unless somebody is going to step in with subordinated capital to give some security to it.

Again, in the area of participation loans, by being a central force of a principal lender to a transaction, you can often encourage money from the banks and other lending institutions, many of which deal in longer term financing than banks do. So your means of creating leverage are borrowing yourselves to create a larger pool of funds readily available to you through the future cash flow generated by the resource revenues. Guaranteeing loans or equity. Providing subordinate capital, either debt or equity to transactions. Or being only willing to participate in loans which would encourage external capital to also be participating with you. Those are the four principal ones.

An unusual element here is the ability to use tax exempt market to borrow some of the funds, should you wish to do so, and I think that Ted is better informed in that area than I am and can better deal with it.

MR. SWICK: I think we ought to take a few minutes to

talk about tax exemption. In discussions, sometimes it isn't clear exactly what it means. It certainly means something in the capital market but what it means in terms of government and that side of the thing. As far as the ability of Alaska through its Permanent Fund to participate in tax exempt activities is inherent in its very existence as a local government. The assets of the Fund itself and the source from which they come has no bearing at all on whether or not your activities can be tax exempt. The only restriction that I see, and our experience shows and the law says, based on Federal statutes, that if you were using the proceeds of a bond issue issued by the Fund or an appropriate underlying entity that might be created, that those bond proceeds from that specific tax exempt issue could not be used for the benefit of a private person. I think is the language they use, which would include either individuals or corporations.

Those funds that come directly from the principal source of your money in the Fund are not a deterent to being -- having access to the tax exempt field at all. There is no restriction on that whatsoever.

The various financing alternatives that relate to leverage have been used and are available in the tax exempt market. You wouldn't be breaking any new ground. Demonstrations and exhibits of these activities can be easily brought to you. The general existence of the people who have used them are

already in your files in regard to some of the funds that exist in the Lower 48 that you are already familiar with and have background material on. The material you have, I don't believe up to this time shows you the details and the mechanics of exactly the way it works. It is certainly implied in the summary of those entities.

I don't know whether there has been any decision on this tax exempt subject. Perhaps I could clear it up a little bit. The financing possibilities and the use of the Fund, whether to commit principal in some way or commit earnings only. As Charles has already said there are things that can be examined at that point in your life when you decide really what do you want to do and then the financing mechanisms are either copied, if you will, or developed for your needs. Or, in certain circumstances it is not beyond possibility that new configurations can be created with some work and some thought. And, hopefully, at that stage is where we would make a more specific recommendation. It is our judgment that the possibilities of extent to which the assets of the Fund can be expanded, if you will, into a fairly sizable activity. Your alternatives and your choices are very broad. And I think the economic impact can be very pleasing to what you are trying to accomplish.

Charles and I would be glad to elaborate, if you have any questions. We believe that it is too early to get into these

things, you know, who pays what, and how does this dollar get to there, and all that until we collectively have a feeling of what about this or what about that, and which way should we go.

MR. FUHRMANN: I might add that I have suitcase that is lost between here and New York and it is probably sitting in Seattle with Ken Butler in a fogged-in airport. In that suitcase is a study of how some of these other funds have used leverage. And the requirements of the lending agencies in terms of covenants and extent of leverage in order to maintain AAA credit rating for either the guarantee or the borrowing. That will ultimately get here. If not in the next 24 hours, I will see that the bag gets delivered to somebody on the Committee before it gets returned to me in New York. So you can look at that. I think that will be helpful to you.

Also, off the subject for a second, in the same bag is a bibliography that was requested at the last meeting on what people might be reading about development funds and various programs around the world and how people have used them and it lists books on the subject and articles on the subject. And to the extent that those are not available to you, we will be happy to get copies of anything on that bibliography for you. In addition, there are two additional studies to go with our original study on international and domestic development funds, to include the industrial estates in Newfoundland and Quebec development banks. Those will be available to you.

MR. SWICK: We have here -- just a 2-page introduction to the subject. I might even describe it as superficial perhaps. I will leave copies here with you.

MR. GALLAGHER: Could you elaborate on whether the limits -- when you talk about public purpose in tax exempt financing, just what are the limits of public purpose? It seems to be the industrial development authorities are just about the limit of where a public purpose might be and sometimes they reach over what public purpose might be. Could you elaborate on just what the current thinking is on limits of what public purpose is in the United States?

MR. SWICK: Well, sir, as you implied and Eric is probably closer to some of this. But the definition, I guess has been stretched in some people's minds beyond reason, particularly when you talk about industrial aid and lending of credit to private persons. There is still a very broad body of opinion and the United States Congress may act to restrict it even further. They may adjust it so that it presumably has some impact on smaller businesses or smaller activities where the restrictions are now directed pretty much. As far as pollution control is concerned, it created a volume in the tax exempt market which has been dealt with, I think, well, the market has performed well. There is some fear in the minds of the Federal Congress that it is overburdening the market but I'm not sure that can be really measured accurately.

I think every state, in effect, rolled over and have industrial aid and industrial development and economic development, with the exception of the State of Washington. I don't have an answer to your question other than as I remarked earlier, the place they go and the place they come down in local government for financing economic development is when you use bond proceeds. The clearest demonstration of the other technique is what has been done in Pennsylvania where they've used other assets for industrial loans. One recent development which is maybe only two years old shows that on the other hand the IRS will take a view of what a public purpose is when they declared the handling of garbage or refuse as now a public purpose. Subparagraph 3 in the 1968 Act relates to industrial development. I would think though that the attitude generally in the Federal Congress would be that the public purpose is stretched about as far as it should be and it should be brought back a little to the more traditional activities of government.

I think it is possible for this Fund and the source of its assets, as I have already said, to be not restricted in the activities you can engage in with that money. If they do go into the borrowing market on an entity of their own and expand their capital base in that manner, the Fund does, I think it is very easily done with legal documents to have that money segregated and just trace it through so it doesn't end up in an industrial private person's hands.

MR. FUHRMANN: It needn't be fundable in the sense it contaminates the whole fund.

MR. LOVE: Would you say that housing and public utilities, even investor-owned utilities, are those the more traditional areas?

MR. SWICK: Investor-owned utilities, the answer is no. They have entered into the tax exempt field as I am sure you are well aware in the area of pollution control in very significant amounts. It has been a much more reasonable source of their raising capital for non-productive expenses that they have to do to comply with our environmental protection laws. Traditionally, really the services you come to expect from your town, county, borough, or State, schools, roads, sewers, water.

MR. LOVE: Housing is.

MR. SWICK: Housing is.

MR. LOVE: Let me see if I understand this. You've got a million dollars in principal and you either commit that into safe securities and use the principal as your reserve fund basically, or you use, say, the earnings off your million dollars which might be, say, 60,000 dollars a year or something like that as a committee of one. And after you've got this amount that's committed, how much bonds can you sell and maintain a AAA rating, how much reserve to get a AAA rating?

MR. SWICK: You go to the credit matter which is important because it has a direct relationship on the cost of

money. Levels of credit by our traditional ratings, AAA is the best credit and on down to AA, BAA and then it begins to drop out of what is called investment quality. The cost of money directly relates to those investments. If you want to have a AAA bond issue, we would want to make something up, say a new high school ---

MR. LOVE: Let's just say housing.

MR. SWICK: Then to insure yourself of a AAA rating on the securities that were sold in the tax market to build the house units ---

MR. LOVE: Buy the mortgage.

MR. SWICK: You would probably have to take an equal amount of the Fund's assets.

MR. LOVE: 100 percent.

MR. SWICK: One to one. What the investor in the tax exempt bond issue then sees is that he has a government security. And the market for that bond is probably going to be maybe 5 percent and pledged assets invested in U. S. government are earning 7.

MR. GALLAGHER: You might enlighten further that it is only because of the State's credit rating itself that the State agencies don't have a higher rating. It is traditional in the market that the agencies don't have a higher rating, I don't care how strong you make the credit, it's not going to be higher than the State itself.

MR. FURHMANN: This isn't completely true.

MR. GALLAGHER: It's substantially true.

MR. SWICK: A housing bond issue -- I'm making all this up -- and pledged to it were assets of the Fund invested in a like amount of U. S. government, you really don't get into that problem of it being an agency of the State and having to have the same rate. They'll go right to the ---

MR. WOHLFORTH: That would be of such a high quality that it would be unique almost. I am wondering, would it have to be quite such a tough pledge. This was suggested back in '69 by some of the investment bankers who came up and they said what about a State public improvement corporation which would be a bond issuing autonomous public authority. The pledge that they envisioned was a pledge of income from the Fund up to 1.3, 1.4 times debt service annually. To the extent that interest was met, those funds were then free for expenditure at the end of the year. Since it was a test kind of thing, during the year the pledge is effective in favor of bondholders' debt service. At the end of the year, it fell over and became free and things started up again. That was one of the thoughts they gave us.

MR. SWICK: You're right, I was starting at the top.

MR. FUHRMANN: Guaranteeing the AAA.

MR. SWICK: Bring it down. Any choice as to what you would actually put toward that particular indebtedness. Whatever you do will determine what it costs in the market.

MR. FUHRMANN: A lot of this, you should also be aware that the rate agencies are prepared to negotiate and discuss with you in advance of any issue what they really require. You participate, you don't just send it in and pray. And you also go with some pretty good advice. But there is nothing to say that you have to be invested in Treasury. You could be invested in fisheries, public utilities, vessels, timber lands, food packaging and all the rest with various invested securities. You have as your assets a series of investments, bonds and certificates. And those may have just horrible credit, or they may have very good credit, or a mixed bag of credit behind them. That could be set aside too or the earning power and future principal could be set aside but then the demands would obviously be greater than they would be in terms -- if you wanted to preserve the credit and they would be if your investment was solely in U. S. government. But this is not to restrict what you do with your Fund to maintain credit and value in the credit that you put into the market.

MR. LOVE: I guess you could go down quite a bit though from 100 percent. You could down to about 20 percent reserve and, if so, what type of interest rate? Can you give me some ballpark figures?

MR. FUHRMANN: The credit agency is concerned about the last dollar as they are the first dollar. It would not be correct to tell you that, if you only guaranteed 80 percent of

the issue ---

MR. LOVE: How about 20?

MR. FUHRMANN: You just wouldn't work that way. You would have to guarantee the whole issue.

MR. GALLAGHER: He is asking the size of the reserve fund necessary to get there.

MR. FUHRMANN: It depends on what you've got in the fund. That is what we are trying to say. If it's all governments there probably is a break, and it depends on how the Permanent Fund is structured. The credit agency may be able to look to the future cash flow of the fund as well as security here.

MR. LOVE: It seems a couple of weeks ago somebody was taking about 10 to 1 leverage in the Fund. Are you saying you're not going to leverage 10 to 1 in the tax exempt market, that you have to go to different markets?

MR. GALLAGHER: What he is saying that you go to 10 to 20 and you may not gain that much.

MR. FUHRMANN: You may not be AAA when you're finished, but you can probably go that far as some people have indicated. We haven't. Some funds have gone as high as 20 to 1 but most of those have the taxing power behind them of the nation. The Permanent Fund doesn't.

MR. LOVE: Say we were to get some estimates on, you know, hypothetical situation, you might be able to get this type

of a rating for this type of -- let's say bonds for mortgage or something like that. If you were leveraging say 6 to 1 or 5 to 1 or something like that --- To make the whole thing more tangible, I would like to see -- this may not be appropriate right now but it is just really too early to do this type of thing, but ---

MR. SWICK: It could be done but I would warn you that it would probably be such an academic discussion, how it would ever relate to the market place would be anybody's guess. A credit analysis on the municipal side, there are really only two things that you get down to. What is the willingness of the issuer to make the thing work piled on top of the need for it in the first place as a governmental service. Not to get too far afield, you are talking about housing on several occasions. You may be familiar with Section 8 deal setup in the Housing Act and what a basic disaster it has been. The problem simply is that the lender of money doesn't find any comfort in any bonds that are based on the Section 8 program. Housing units of that part of the Act which have been created have been a failure.

MR. FUHRMANN: Jamie, if I were to tell you that the interest rate you pay for a loan is based on the terms of the loan, the structure of it, whether it is 1 year, 2 years, 10 years, 15 years, and the credit behind the loan, whether it's AAA of AA or A, or whatever. And if I told you the credit rating somewhat depended upon the extent of the leverage, you can go as

you want but at some point the market will tell you that they won't accept you as a credit at all. But the Fund itself, to simplify the whole thing and ignore tax exempt from it, the Fund has a pool of funds, some of which may be invested as assets, cash, it will be investments in debt and equity securities perhaps, it has the potential to earn money on its investments. And has a dedication by statute of future cash flows coming from oil revenues. So the credit institution -- if the Fund itself were to issue straight bonds, not tax exempt, and they are the issuer and they are not creating any pool or anything else, they are not setting it aside to be issued against anything, it is not a collateralized bond of any kind, the credit agency and the market place would be looking at what their perception of what the oil revenues will be in the future, earning power of the assets you have already invested in other things, how good an asset those are, to determine what you are going to pay for that and what maturity they are prepared to let you have. Now, if you take away credit from me, if you stick over something in a pool, if you just put the worst loans over there, I can tell you you're going to have trouble getting a long maturity, you're going to have trouble getting a low interest rate, you're going to have trouble selling it at all.

MR. LOVE: I'm not talking about the worst loans.

MR. FUHRMANN: If you put the best ones over there, you're going to have to get a longer maturity rate -- maturity,

you're going to get a lower interest rate. It will be a breeze selling the loan. And you will be able to have greater leverage on it. Because the earning power will be better and it will be perceived better without damaging your credit standing.

MR. LOVE: I think I understand the process.

MR. WOHLFORTH: Other questions?

MR. WALDOCK: Jim,when these studies on the leverage that White Weld comes up, would you see that we all get a copy of that. I would appreciate that.

MR. WOHLFORTH: We've had some limited experience with the leverage concept, although very limited experience, in terms of loans from the General Fund to support a Capital Reserve Fund. One new agency which is starting up, the Alaska Municipal Bond Bank Authority. And we have seen some credit recognition to it. Certainly not what we had hoped for but it never is what we hope for. The Bond Bank Authority has an actual hard dollar legislative appropriation. As a reserve fund it happens to be put on a 10 to 1 basis. And I think it has achieved, in part at least, a rating based on that. I am sure some of the Committee will want to be thinking about the same kind of leveraging principle in terms of municipal loans. Some way of translating the State's credit, which I feel will improve dramatically probably within the next year and certainly within the next two years, ways of translating that credit to the local government who will have continuing borrowing needs. We have a small

example of how that can be done. The Legislature has taken a step in that direction and we are seeing some signs of success. I am certain the local governments will feel that very keenly if the State is able to borrow at a AA or AAA rating, and they are barely able to achieve an investment grade rating and they can see interest rates that they are paying substantially more than the State itself. So it is something that has to be thought about as this whole process develops, from my point of view.

MR. FUHRMANN: I might point out in that line an experience we had. We represent Nationale Prinensierra (phonetic) which is the Mexican development bank, for all intents and purposes. No. 1, politics in Mexico is rather intense between the people that run the Treasury Department and the people that run Nationale Prinensierra, is just one example. But the Nationale Prinensierra has essentially been used as a vehicle for which everything goes to the market in Mexico, except the Mexican government itself. All the agencies go through it and everything else. And the Mexican government issues bonds. Nothing in Mexico is really rated because they don't want to be rated anything less than single A and, therefore, they have chosen not to be rated at all and run the risk of being rated less than that. But we were in a position to offer Nationale Prinensierra a security that was going to sell better and be perceived in the market places as better credit than the Federal government's direct paper. And, in that case, the Federal

government was fearful that this would influence their sinking fund retirement programs and their ability to issue direct paper in the future and everything else and people would be insisting that -- Nationale Prinensierra not only represented the agency but also represented the government itself in the market place. So they rewrote the charter of Nationale Prinensierra to remove the advantage that Nationale Prinensierrra was going to be able to have, that was going to help them in the market place. So, if there is a sense of competition, you may find that happening here too. There is certainly within this Fund the ability to create a AAA security. So keep that in mind.

MR. WALDOCK: I wonder if you would address the possibility of using an insurance program on some of our loans, i.e., the Alaska State Housing Development people just put out some bonds here within the last month, and it is a fully insured program. Would there be any possibility of using this type of an insurance on various types of loans that we might be able to utilize through the Permanent Fund?

MR. SWICK: Well, when you're talking loan insurance you are talking about bond issues of local communities?

MR. WALDOCK: Yes.

MR. SWICK: Yes, I think very quickly to answer you the technique that is used in the Housing Finance Agency, State Bond Bank that Eric referred to, are techniques that can be applied right to this corporation money.

MR. FUHRMANN: I am not sure there is much difference between a guarantee and an insurance program. You understand with a guarantee program the Fund could look to -- could get a fee for providing the guarantee. And to the extent that they are putting assets aside to collateralize the guarantee, those assets will not be idle, will be invested. And the combination of the guarantee fee and the earnings on the put-aside assets may be considered an attractive investment alternative for you.

MR. WOHLFORTH: The insurance program Dennis referred to -- the current program of this corporation is to purchase conventional mortgages which are either 80 percent loan to value or insured through PMI, Private Mortgage Insurance. A 2 percent fund has been created, essentially take care of the uninsured portion, or the perceived portion which needs coverage. It is, again, just another financial device that may well be proven.

MR. GALLAGHER: It also has an additional reserve fund that insures the whole bond issue and not the credits themselves.

MR. WOHLFORTH: Yes.

MR. SWICK: I think the point is the assets of the Fund would be positioned in the same way that the corporations have done.

MR. WALDOCK: Does any development corporation use this principle?

MR. SWICK: I can't come up with one. South Carolina

was gatting at it and the legislation failed on the floor and it never got to a test. The private mortgages were interviewed and had meetings and had associations meet to get themselves into this th ng, but it never got together.

DR. LOGSDON: What was that, we couldr' near that down here.

MR. FUHRMANN: Were there any other funds using the insurance concept.

MR. LOVE: Are you prepared now to give us more tangible ideas if we went into the tax exempt market the traditional type of loans we might make other than housing?

MR. FUHRMANN: We indicated, Jamie, we have talked about things like power transmission and distribution, housing, schools, roads and highways, recreational facilities, airports, ports, hospitals, water and sewer systems, transportation facilities and so forth.

MR. LOVE: These development corporations they are basically in developing structures and facilities, they are not like research development or something like that?

MR. WOHLFORTH: He may be asking about the IBB test, what is the test for an industrial development bond with security interest ---

MR. FUHRMANN: It's the ratio in dollar amounts and they you start qualifying for all kinds of things.

MR. LOVE: How about if it was like for a public

resource development company or something like that, a public insurance company. Say the State went into the medical malpractice field or the workmen's comp. field or auto insurance, the State got involved in resource development, would that become eligible for tax exempt borrowing? If it was actually publicly owned.

MR. SWICK: I don't know why not.

MR. LOVE: It is not the nature of the activity, it is who the ultimate borrower is, right? But home owners would qualify ---

MR. FUHRMANN: Someone is going to track the dollars that you have raised to make sure that you have not abused the privilege of tax exempt financing.

MR. LOVE: But a homeowner would probably qualify. But a guy with a 100 or 200 apartment complex, he probably wouldn't qualify.

MR. WOHLFORTH: It is all very meticulously set out Section 103 of the Code.

MR. SWICK: You understand that those restrictions -- those restrictions only exist to the extent that you use the proceeds of the tax exempt bond issue. Don't confuse that with the fund.

MR. CRAWFORD: What is the point spread between tax exempt and non-tax exempt bonds?

MR. SWICK: It would be easier for me to say it

fluctuates. I guess traditionally we're talking about 1-3/4's, 2 percent over a period of years. You get disruptions in the market based on technical things that are of a temporary nature. The tax exempt market is the full product of the money market and the whole interest rate structure. The demands for capital on the public and private side change that. It's substantial.

MR. FUHRMANN: Changes with maturity.

MR. WOHLFORTH: Some commentators in talking about the Permanent Fund and opposing it specifically, this was printed in the Lt.-Governor's material submitted to the voters, said that instead we should retire our general obligation debt and finance all our improvements directly from recurring revenues in the future. What would be your reaction to that?

MR. SWICK: My quick reaction is, why do that, just keep doing -- you've got your governmental function and your regular sources of income for your governmental services. Those activities continue and I'm sure you don't want to lose sight of the fact that there is going to be additional income from the General Fund, this 25 percent or whatever that is going into the Permanent Fund, which would be used for these special things that go beyond the everyday expectations of your General Fund creditors.

I don't envision the existence of the Permanent Fund making it unnecessary for the State of Alaska to go into the General Obligation bond. The same idea that has been inherent

in all your discussions, there is no sense in paying cash for a facility or an activity that is going to benefit Alaska now and down the road. That is the whole theory behind municipal finance, to build a facility that has a 25, 30 or 40 year life, you, in effect, have the fellow who is going to use it 30 years from now also paying.

MR. LOVE: I think some of that was coming from fiscal conservatives who want to see the State budget limited and expenditures cut back.

MR. SWICK: There is nothing criminal about being in debt, is there?

MR. FUHRMANN: You are doing a lending by taking this money out of the General Fund and putting it into a Permanent Fund.

MR. WOHLFORTH: Are there other questions? Before you leave, there is a point that I think maybe we need to have some expert advice on, later on, from perhaps the Attorney General's office as we look at some of these questions. The phrase, income-producing investments which is virtually the only qualification in the amendment, what can they invest it in. As we consider intrastructure investments, I'd say, if they are to be direct. And we talk about schools, roads. Obviously some public investments fall into the income producing category and others do not. We talk about the concept of leveraging. It may be that the Legislature considers that we will continue to borrow

for public improvements and have the Fund, indeed, provide a substantial reserve against the amount that is borrowed.

I think we ought to consider early whether or not, if we use a reserve fund concept for public borrowing, if we can do other than a borrowing for so-called income producing investments, which a school, obviously, doesn't qualify for. Does the fact that ultimately that the monies may be paid back to the reserve fund as a loan, does that qualify it as an income producing investment. I am not clear at all in my own mind whether that is the case.

MR. SWICK: You have already said that this idea of providing what we loosely call front-end money, having it returned and it will begin to return at a later date and still qualify.

MR. FUHRMANN: We talked about that at lunchtime after some of the comments that were made this morning by the bankers, Chamber of Commerce people, I believe.

Ted asked me, he said, "What happens if the Fund wants to get into research and development or front-end money to something that would lead to an income producing situation" and my answer was that if the Fund is, indeed, income producing that another form of leverage that we really haven't talked about here, it's not really leverage but it is in a sense of multiplying your economic impact and your ability to pledge future funds that will be coming into the Fund as opposed to current funds, was

that you can provide a long-term takeout to a bank so the bank is actually putting up the start-out or front-end money and is assured of a takeout from you when the project becomes operational. So, in that sense, you have the ability right away to encourage R & D and projects getting off the ground that are not initially income producing. The other alternative, of course, is having interest holidays until the project gets going. But that may not be consistent with the income producing concept.

One way you can work with banks is being there to provide the long-term takeout and let banks do what banks do and you do what most development funds do which is long term financing and not short term financing or working capital.

Take that concept. No one has decided yet whether you're going to be development oriented or capital preservation oriented, or to what extent you want to be both or either. Back to Lanie's goals and objectives.

MR. SWICK: You can do other things.

MR. FUHRMANN: You let us know what it is, and we'll tell you what kind of leverage.

MR. WOHLFORTH: Next on the program is Bob Richards from the Alaska Banking System

MR. RICHARDS: The comment on the discussion that we were just having that the insurance that is available to municipalities in Alaska, the Housing Finance Corporation, that

is limited to to 20 million dollars, may or may not have some application to the Permanent Fund, but one thing that is interesting, one of the positive elements of the Permanent Fund is your judgment that there is an opportunity for a AAA rating. That is pretty exciting and, of course, that would preclude any real need for additional insurance.

The specific inquiry that you made at our last session is being researched and that activity was preempted by the request that we go in the direction that we are going into today. At any rate, those questions will be answered and will be submitted to you in writing.

Mr. Rhode and Mr. Edenso requested that I prepare some observations on the interface of the Alaska Permanent Fund with the Alaska Banking System. And I have done that, and about all I have is just that, observation as distinguished from comprehensive analysis of this matter.

The discussion today will really have two parts. The first part will be kind of institutional in nature, that is, comments on describing the Alaska Banking System. And the other part, and the longer part, the more significant part, is the relationship -- inititial observations on the relationship between the Permanent Fund and the Alaska Banking System. I have some tables here that underlie some comments I will be making. If you don't mind, I'll use the same format I used last time. I will lay this out and then we can discuss it.

I think that relative to consumers in other states, Alaskans enjoy access to a broad banking system. Now, we all know that on any per capita contest, Alaska wins hands down. Just by the mathematics of the issue. But, be ng that what it may, the statistical fact remains that on a per capita basis there are more separate banking institutions -- this is not number of offices -- there are more separate banking institutions in Alaska than in all of the other western states. By the way, I don't know relative to the rest of the country. This is an analysis I have performed -- I arbitrarily compared Alaska to the other western states, which reduced the research effort. Further, as exhibited in Exhibit B, for communities of 10,000 and over, people in Alaska have twice as many banks as the U. S. average. Exhibit C is just coming at this item in a little different way. That the Alaska commercial banks service some pretty darn'd small entities, by any measure --- By the way, as an aside, I have shown this Exhibit C to various of our correspondent banks from Outside who are utterly aghast at the proposition of building a bank to service such small population. Finally, Exhibit D is a map, which I think indicates a fairly broad geographical dispersion of Alaska's commercial banking system. But, as you can see, quite clearly the Alaska banking system falls right in line with the Alaska economy is related directly to the present day economic complexion of the State. And, finally, Exhibit E is just for your files, your background,

it is simply a list of all of the Alaska -- I indicated Alaska financial institutions. Included are commercial banks, savings banks and savings and loan associations. I will have to confess to you a typographical error in here and that is Behrends, that is Hoonah not Hootnah. And another quite surprising -- when you put this together -- I was informed that the total was 110 commercial banking offices in the State, I found out it was a somewhat surprising total, clearly in excess of what I had intuitively imagined. So I think the information on these exhibits -- although, again, like the statistics I presented to you before, an intrinsic nature of the statistics that I will always present to you, and I think an intrinsic nature of any statistics anywhere at any time, they are imperfect But perhaps some sort of general conclusion that might be drawn here is that the Alaska consumer, in terms of convenience, has access to -- is not hurting in terms of access to financial institutions. I will put that, the Alaskan consumer functioning within the cash economy.

Now, the information that I have presented to you is primarily just for your background. The main element that we wanted to get to today was some comments on the Alaska banking system and the Permanent Fund. I think the most important element of the Alaska banking system, in terms of the Permanent Fund, is the role which Alaska banks -- and I am going to use the term banks and you can broaden that term as appropriate. The

role which Alaska banks have played as a conduit for channeling funds from large, long-term investors to Alaska's families and businesses. I'll repeat that, I think the most important element of the Alaska banking system in terms of the Permanent Fund is the role which Alaska banks have played and are playing as conduits for channeling funds from large, long term investors to Alaska's families and businesses. I will give you some examples. Over 80 percent of the money which finances the purchase of homes in Alaska does not come from Alaska bank deposits. It comes from large institutional purchasers of mortgages. And these institutional investors are comprised, at the present time, basically of one Federal agency, Fannie Mae and Freddie Mack. (2) Outside savings institutions. (3) Union pension plans. The local banks originate the mortgages, that is, they take the application from the borrower and do all the paperwork, et cetera. Then the banks sell the mortgages to these large investors and service the mortgages for a fee. By that I mean collecting the payments, making the tax and insurance payments. And, in fact, the borrower deals solely with the bank and is not even aware of the institutional investor who purchased his mortgage.

Now, another way in which the Alaska banks serve as the conduits for the flow of funds into the Alaska economy is through loan participation with Outside banks. This situation normally arises when a customer comes into his bank in Alaska and requests a loan that exceeds the lending authority of the particular

Alaska bank, or which has a characteristic such that, for some reason or another, the Alaska bank wants the participation by a large Outside bank. The Alaska bank then presents the loan to an Outside bank with which it has a correspondent relationship for consideration by the Outside bank to lend the amount of money which exceeds the Alaska bank's authority. This is a very, very common practice and it goes on every day. And Exhibit G --- I'm sorry, I meant to give Exhibit F to you earlier. Exhibit F is still descriptive institutional material and it simply -- note that I entitled this the partial list. This list simply came forth by my checking the yellow pages of the telephone book and my sitting back and using -- inquiring of other people, and this is just to give you some sort of a representation of the variety and magnitude of the financial institutions which are channeling funds into the Alaska economy. Well, at any rate, back to Exhibit G now. As I indicated to you, another way in which Alaska banks channel funds, serve as a conduit for channeling funds into the economy is through loan participation with Outside banks. And Exhibit G is just -- and financial institutions. And Exhibit G, again, is just a representative list of financial institutions that I know of which have purchased or which participate in Alaska loans.

Probably the most significant investor which injects funds into the Alaska economy through the Alaska banks is the State of Alaska. The State General Fund, the public employees

retirement fund and the teachers retirement fund currently hold over 100 million dollars in loans and mortgages which were purchased from Alaska banks. Additionally, at the Federal level, the Small Business Administration has been a substantial purchaser of Alaska loans.

So the relevancy of all of this, everything I have talked about so far has led to one point and that is: The Alaska banking system is structured and has operating procedures established for serving as an effective conduit for the flow of funds from large investing agencies to Alaska's families and businesses. The Alaska banking system has a considerable amount of experience in this procedure and the bankers of Alaska perceive this, I think, as one of their important roles. The investing agency benefits from this system by receiving the knowledge, the skill, the manpower, indeed, the entire mechanism of, I think, an extremely efficient group of institutions set up to perform this very function. The large institutional investor pays a fee for this service, which, obviously, the institutional investors, to date, have felt was more economical than setting up their own organizations to take loan applications and process the paperwork and et cetera. Or else they are making irrational decisions, one of the two.

The conclusion then, it seems to me, is that if a portion of the Permanent Fund is allocated toward loans to consumers, families and Alaska businesses and organizations -- and

I don't mean to imply that it should be -- I don't mean to imply that it should be. I don't mean to imply that it shouldn't be. But, if it is, if a portion of the Permanent Fund is allocated toward loans to consumers, families or Alaska businesses and organizations, it appears to me to make sense to do this through an efficient system of financial institutions already set up to perform this function. As I say, this is the conclusion that a number of large institutional investors have already come to themselves.

Further, however, I think that, if the managers of the Permanent Fund, whoever they may be, should give consideration toward allowing Alaska banks to participate in the large economic development type loan. Now, some Alaska banks already participate in major financing in the State which was actually originated between the corporate headquarters of a national firm and a large lender , a large bank in the Lower 48, who then bring in, so to speak, the Alaska bank. The advantage of having the participation of the Alaska bank is two-fold. One, often the Alaska bank brings an understanding of the environment within which the loan is being made. And, No. 2, the Alaska bank provides a certain amount of local supervision of the loan by maintaining surveillance over the activity which the loan is financed.

Now, I think that most bankers in Alaska are quite enthusiastic over the Permanent Fund. This was evidenced in the

statement which they made to you this morning. Because, frankly, they are aware of the tremendous good that can be forthcoming from this vehicle. And they certainly do not perceive it as a threat, at least the bankers with whom I have discussed it. It should be kept in mind that commercial banks are in business to make short term commercial loans. Hence, their name. The Permanent Fund, on the other hand, as indicated in my very first working paper I presented to you, should have long range orientation. It's very name implies this. And it is my opinion that the Alaska voters had this in mind when they approved it. So, operated as I think they ought to, the Permanent Fund and the Alaska Banking System are certainly not in a competitive posture and are certainly in a complimentary posture. As an added service to the Permanent Fund, however, the Alaska Banking System does offer an efficient conduit through which the Permanent Fund could channel certain of its investments.

Those are my observations at this point on the Permanent Fund and the Alaska Banking System. Again, to summarize, I think they are complimentary systems.

MR. WOHLFORTH: I would be my suggestion we all take a little break and a leg stretch before we launch into Mr. Richards with questions. Let's try and hold it down to about five minutes.

OFF THE RECORD

ON THE RECORD

MR. WOHLFORTH: We are back into session now, if you will take your seats. Bob Richards has concluded his prepared remarks and now it is questioning time. Who would like to be first?

MR. GALLAGHER: I want to make one institutional observations and then I want to talk about institutional problems. I see a need for an institutional change. These numbers on banks in the size of towns are good numbers. There are even a number of smaller communities in Alaska. I see the need for us to change the Banking Code to make mobile branches or branches that don't have to be open five days a week and 8 hours a day, which is under the current law. It could make the banking system even more responsive than it presently is for rural Alaska.

MR. RICHARDS: I share the same feeling.

MR. GALLAGHER: The institutional problem that I would like to get at and it really relates to rural Alaska is that it is the tendency of the commercial banks in the State to send out the relatively young and inexperienced managers out to these small rural branches. Since they are young and inexperienced, they seem to be unwilling to take risks or do any new sort of program. I was wondering just what sort of institutional change or what sort of emphasis could be accomplished in order to make them more responsive to that problem.

MR. RICHARDS: Two reactions. No. 1, I don't necessarily concur with your thesis. No. 2, it would be helpful to me to know what sort of tack we're going to take over the questioning period. Are we just going to discuss the Alaska Banking System? Are we going to discuss the Permanent Fund and the structuring of the Permanent Fund? Are we going to be discussing the relationship between the two?

MR. WOHLFORTH: Unfortunately, Mr. Richards, I have been able to exercise very little control over the questioning and the direct relevancy of the questions to the Permanent Fund. So I would just have to say that it is going to have to be fielder's choice to some extent. I guess the agenda item, Alaska Banking System, has probably an indirect relationship because any State loan program that is conceived to come from the Permanent Fund must interface with the system as you have already indicated. So I would hope that we would try and keep our questions in that general context, but certainly I can't insist that they be. Did you have any more response to Commissioner Gallagher's comment or question?

MR. RICHARDS: Well, as I say, I don't think there is sufficient -- I haven't seen a sufficient amount of data to lead me to that conclusion. There are young inexperienced people in all enterprises in Alaska. And, as you know, I was once an employee of the National Bank of Alaska and I could perceive no -- either policy or behavior on their part that substantiated the

thesis expressed.

MR. GALLAGHER: I happened to have to go to visit several rural towns and I just happened to go visit the branch manager in each town and quizzed them on what State loan program monies were getting down to their level and were they aware of certain State loan programs. And the answer was universally no, they were not aware and, no, they had not participated.

MR. RICHARDS: Have you visited branch managers in Anchorage?

MR. GALLAGHER: No, I haven't. But under the State loan programs -- that work through the banking system, we are getting substantial loans our of Anchorage banks and Fairbanks. But it is in the rural areas that we are not getting that sort of applications.

MR. RICHARDS: I respect your raising the thesis. It is one that I do not necessarily concur with its validity. No. 2, I don't feel qualified to respond to it.

MR. WOHLFORTH: Maybe we are talking in general the whole communications problem which has been such a problem in Alaska. We are challenged all the time to figure out ways of getting the message across, even what is happening at these meetings. And media devices, I don't think there is a state -- I don't think any of us have really fulfilled our responsibility of how to get events that are happening across. We are doing a lot now with task forces and groups and committees, but there are

a whole lot of people who aren't clued in yet. It's a universal problem.

MS. FLEISCHER: It's just that I don't really know anything about this. For one thing, this is kind of a small point in a way but I note the census data here is 1970. I know that the towns aren't this small.

MR. RICHARDS: I agree with you. I think you are raising a trivial point.

MS. FLEISCHER: Well, what I was wondering was, are you saying that towns as small as 150 people can have a bank now. Did they have a bank when there were only 163 people there?

MR. RICHARDS: That is a very important question or point that you raise, Lanie. And I don't think you can draw that conclusion necessarily. It depends upon the role of that town in the region in which it is located. It depends upon the relationship of that town to the other towns served by the branch system of which that branch is a part.

MS. FLEISCHER: In other words, the town itself may be small but they may be serving ---

MR. RICHARDS: Right.

MS. FLEISCHER: What I was wondering, what is the need for banks in smaller villages, unless there is a need, if people need to be served.

MR. GALLAGHER: One of the institutional problems I was referring to, FDIC requires them to be open five days a week

and I think six hours a day if they're open. And so there is an institutional problem. If the State allows a State bank to do it, then automatically the Federal banks are also allowed to do it under Federal regulations. So it is a matter of changing the State banking code to be more responsive in that area.

MS. FLEISCHER: That is something that could be done regardless of what happens to the Permanent Fund.

MR. RICHARDS: I think most bankers, or at least I would concur with some sort of mobile system or parttime system, or some sort of device to make remote banking efficient.

MR. LOVE: The Permanent Fund, a lot of people think it is to provide loans to Alaska residents. I think what would be helpful to the Committee is some indication of the areas where the Permanent Fund might fill gaps that are not otherwise met, either by the bank's own portfolios or secondary money market. And I feel like right now I don't feel we are working with very objective data. We've never really had the banks tell us where those unmet needs are.

MR. RICHARDS: We would be happy to.

MR. LOVE: Secondly, I think at some point and you may or may not be the proper person to draw on for information, I would like to know a little bit better how we can interface with S & L's credit unions. I know there are some that say, S & L, we're going to have different types of problems -- the impact of the Permanent Fund on savings and loans some people say is going

to be different than the impact on commercial banks. I would like to know how the difference. And also a little bit more about the credit unions. You may prefer to defer to other consultants on this matter, I'm not sure.

Also, Senator Kerttula earlier got into a dialogue with Frank Murkowski about some of the problems in the past, the Development Loan Corporation or something like that, and some of the areas where he thought the banks had taken advantage of the State. The State had made money available to the banks to make loans. And we told him, Frank Murkowski, that we would like some specific proposals submitted to us that would outline how they think that we ought to balance -- safeguarding the public's interest. This is obviously public funds being invested by the bank. That in itself would present a problem if the bank didn't have to take the loss. What I am saying, the members of the Committee, we're going to come up with some recommendation. The State's interests have to be safeguarded in these types of investments, and I have a vague notion that has to be done somehow. I am not sure of the best system and I would like you to provide us with a recommendation.

Also, another area and this has to do with just some dollar figures. We sort of know that the banks are not providing money in the secondary market. I would like some figures at some time over what the total dollar amount is made annually in mortgages. Roughly, how much of this is by Federal

agencies, how much by Unions. So we kind of know the dollar amounts currently we are dealing with so we can understand a little bit more about how the Permanent Fund relative to its size fits into all these overall pictures. Secondly, besides mortgages and things like that, the amount of consumer loans that are being made, the different kinds of Alaskan loans so we've got of a detailed picture of just how all these investments -- how these markets are being served. We are asking each person to give us some figures, the utilities, the fisheries said they didn't know yet how much they wanted. But before we start making a lot of grandiose plans for the Permanent Fund, we have to know what the needs are in the State to what we're looking at in terms of this money. Then we can look at decisions about whether or not we want to get into leverage and make direct loans and things like that. These are the types of things I would like to see provided relative to how the banks fit in with the Permanent Fund.

MR. RICHARDS: I feel confident that I can respond adequately to the first three. To your fourth there is a data problem in terms of -- we can estimate, we can come up with some sort of rough estimate I think, but ---

MR. GALLAGHER: That information may be available in the semi-annual report we send to FDIC. You tell them in one of those reports just what loans you make and which ones you sell.

MR. RICHARDS: That's true, but whether or not FDIC is going to ---

MR. GALLAGHER: Or are you going to go to the State Banking Commission.

MR. LOVE: You say you think the State should move into the long term money market -- just overall ideas about the total amount of money to commit to the long term investments or that we could commit -- that the market probably wouldn't be over saturated with, whether it's mortgages, take out loans on various resources or something else.

MR. WOHLFORTH: Are there other questions.

MR. WALDOCK: Bob, would you mind exploring a little bit more in depth in regard to your -- second to your last paragraph in your presentation today in regard to the competition of the Permanent Fund and the banking system. I understand from what I read here that you are implying that you think we ought to concentrate as Committee members toward larger sums of money and longer term structure for these monies rather than to participate in the shorter term type vehicles.

MR. RICHARDS: For two reasons. One, I'm no political scientist, I'm just another guy off the street when it comes to this observation. But it seems to me that the Alaska, the very nature of this thing that Alaska voters approved, the Permanent Fund, and all the talk that I have ever heard about this subject has some sort of connotation of long range permanency. It's my

guess as just another guy off the street that was what the Alaska voters intended.

The second reason is all the other paragraphs that led up to the last paragraph, there is, in my opinion, existing a very efficient mechanism for handling the short term credits. And I think it is more efficient than any other mechanism that could be established. This is not to preclude the Permanent Fund from investing in some short term credits, but I think they should do it more in the way of purchasing, participation with local financial institutions. It's more efficient.

MR. GALLAGHER: One comment I have made here from time to time, I see the banking structure in Alaska resembles a rural economy with small short term deposits, or very little long term deposits and quite a bit of short term deposits. Is there any data available to show the legion of financial institutions that go together in a mature economy, let's say like in California you'll have insurance companies. Is there financial data available that shows all those assets per state and how they make up?

MR. RICHARDS: I am not aware of any in a meaningful way because, you see, those -- the State data is a reflection of the headquarters of those various firms and they could be investing in loans all ---

MR. GALLAGHER: The reality of the matter is quite often they use the investment within 50 miles of headquarters

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though. Loan officers intend to loan to things that they are familiar with. If the home office is in San Francisco, they tend to lend in the San Francisco area.

MR. RICHARDS: Yes, but I just don't know what portion the Bank of America -- maybe they're a bad choice but certainly others, Security and UCB and Union bank. I may be able to draw some inferences from this but that would be --- I concur with your original thesis that the deposit mix in the Alaska bank tends to reflect a rural economy and there is not the mature deposit, so to speak.

MR. GALLAGHER: Is there any data that you might be aware of that could prove my thesis?

MR. RICHARDS: No, but I'll look for it.

MR. WALDOCK: Bob, would you mind clarifying for me what is the length of a short term loan and what is the length of your long term loans? What I am trying to say is, I would like to know what you mean by a short term loan, i.e., what the commercial banks are doing versus what you think the Permanent Fund should be doing in regards to length of time.

MR. RICHARDS: I think more than maturity is -- I could give you a textbook answer to that question but it would be meaningless in terms of Alaska. I think rather than the maturity is the implied market. I think that Alaska banks are well set up to take care of credits that originate from Alaska families and businesses. I am not asserting that there are not some gaps, as

suggested by Jamie. I think there are some gaps. How large they are, how significant they are, I don't know. But I think the Alaska banking system, at least is set up to take care of credits generated by local Alaska businesses and families.

But to give you another kind of response to your question. They make consumer loans that are as long as ten years. The textbook answer is a commercial bank makes loans to businesses for less than a year and they are paid off within that period. That's a nonsensical definition in terms of Alaska and many other areas as well. It's kind of more the market perceived by the enterprise. The Permanent Fund, as I have suggested really from the outset, should be oriented more toward the larger -- oh, for lack of a better word, economic development types of loans. In terms of what its organization does, I'm not saying they should just invest in those kinds of loans. If they invest in local loans or loans of families and locally owned businesses, so to speak, I think that can best be done through the Alaska banking system on simply the basis of efficiency.

MR. WOHLFORTH: I can remember, if I may, the time of the lease sale in '69 the banks were anxious and properly so to be considered for State deposits and, indeed, substantial amounts were deposited with the banking system and some money, I think 25 million was put up on a 10 to 14 year basis. The colloquy of the bankers at that time reflected an underlying fear that even

though the deposits were made on a long term basis that, in fact, they might not be. And at least one had a perception, one couldn't prove it, that their ability to really use these deposits in a meaningful short term commercial loan was inhibited by the perception that the deposits were vulnerable. Do you think that deposits from a Permanent Fund, in quotes, would carry that same kind of banking apprehension or not. Do you think that deposits would be more meaningful did they come from a fund of this nature rather than the General Fund?

MR. RICHARDS: Yes, I definitely think so. I definitely think so. I'm glad you raised that because there are way in which the Fund can influence indirectly the type of lending activity of Alaska banks. And if you place long term -- except for this apprehension -- if you place long term funds with bankers that don't have that apprehension, the bankers will feel more inclined to make longer term loans. Getting back to perhaps some assertions that Senator Kerttula made this morning -- I wasn't here. But just because I'm saying -- suggesting one thing you might do is buy the loans from commercial banks. I am not implying this be done willy-nilly, but you can tie all sorts constraints around this or criteria. If the manager of the Permanent Fund concludes that certain loans, certain types of loans ought to be made in certain places, they can say, we will buy these types of loans made in these types of places.

But to repeat my answer to your inquiry, I think the

attitude on the part of Alaska bankers is such that long term CD's, let's say for example, purchased by the Permanent Fund would be perceived as stable long term deposits and, therefore, would find their way into those kinds of loans.

MR. GALLAGHER: In talking about vis a vis making a loan direct and putting deposits, when FDIC looks at its financial institutions they usually require certain asset mixes and capital structure bases. By putting in deposits are you not creating a cost to the bank to have a certain capital structure that may not be reflected in its natural capital asset structure?

MR. RICHARDS: You are absolutely right. The response is inquiry, it implies within the bounds of prudent asset management, you bet, or liability management.

MR. GALLAGHER: I think Alaska banks are more in the liability management than the asset management.

MR. LOVE: All these things you are saying about banks could be equally applied to credit unions.

MR. RICHARDS: I don't think I am particularly qualified to respond to the matter of credit unions. They are under a whole different set of laws with which I am not familiar.

MR. LOVE: My suggestion to the Committee would be, if we are going to pursue this idea of having banks making a certain number of loans, we also ought to analyze equally the possibilities of doing the same thing with savings and loans and

credit unions.

MR. GALLAGHER: The credit unions aren't in that business. There's no institutional thing that is against it but they have never been in that business. S & L's are very much in that business.

There is one difference between S & L's, credit unions and banks under their financial charters. S & L's and credits unions cannot collateralize deposits. That has been a thorn in the Department of Revenue's side when we put out deposits. One has to collateralize it 100 percent, and the other ones by the FDIC regulations, or FLIC, and those other institutions cannot pledge assets. Public trust and having some connotation of public trust and security. Those two institutions because of their nature and because of those restrictions do not have as much security.

MR. LOVE: Would that be the same thing on mutual savings banks?

MR. GALLAGHER: No. Under FDIC regulations.

MR. CRAWFORD: Bob, is there a substantial demand that is not being satisfied? Is that true?

MR. RICHARDS: Well, I have to respond to that question as an economist. As you know supply and demand always clear at the market price. And I don't know whether the demand for toothpaste in Alaska is being satisfied or the demand for -- pick any product you want. In economics, demand is always

-- supply and demand always equal. So the implication that demand is not being satisfied definitely implies some sort of value judgment being made on the part of the asserter.

I don't mean to be begging the question at all. But too often this assertion -- frankly, I think it is a naive assertion and to give a naive assertion a sophisticated response, it just cannot --- Naive in the rigors of economic analysis, not naive necessarily in the understanding of the world, this sort of thing. I know that from time to time comments are made on the street by people that the banks aren't loaning enough money. That is like somebody saying on the street John Stepp isn't selling enough Fords or Larry Carr isn't selling enough groceries. The banks are in business to loan money. And banks want to loan money. And every bank that I know of in Alaska is loaning just as much money as it can consistent with its judgment regarding the credit worthiness of applicants and liquidity considerations.

MR. CRAWFORD: Is money tight now?

MR. RICHARDS: Well, putting on my economist's hat, no.

MR. GALLAGHER: You earlier though spoke of institutional sort of problems. You referred to commercial banks lending short. If the need in the State is long lending then there may be an unfilled need.

MR. RICHARDS: That could very well be. You're right,

there very well may be a demand for more Jeeps, but that is no criticism of John Stepp. I assume -- are commercial banks doing enough of what they are supposed to do.

MR. LOVE: Can you get a home improvement loan for 5,000 dollars from most banks?

MR. RICHARDS: Sure.

MR. LOVE: That is not what I've been told by people that work in mortgage banks. They say they can't make enough money on them, they don't like to process the paperwork. They tell me opposite. This gets back to, are there areas that aren't being serviced. Maybe that is an area for the Permanent Fund to look at.

MR. CRAWFORD: That wasn't the basis of the question. With the documentation we have been presented and the analysis for the western states. The purpose of the question, I guess is there are substantial demands now which are not being met, which I think you answered.

MR. WOHLFORTH: I think that in any what we call -- have to really call an offshore problems like Alaska with a relatively young banking system, a young and volatile economy, there's going to be a lot of basic dissatisfaction with the banking services, real or perceived, it's the nature of the thing. The banks represent to a lot of people, you know, a kind of money center which they don't like.

I would like the discussion, if we can, to get off a

little bit of examination of the adequacy of the banking system because I don't think we can hope to resolve that in an objective sense, but into a little more of the details. Some of the observations that Bob Richards has made. He stated, and I don't think you have to be taxed with it as having been stated as an absolute certainty, that the larger loan, the longer term loan, and Murkowski said the same thing this morning, were probably a thing that the Permanent Fund should be looking at and not disrupt the credit mechanism of the banking system which is to some extent satisfying and servicing the shorter term smaller amount of loan catagory. I think, however, that is something we are just beginning to approach in this Committee. That assumption needs a very rigorous testing. The consultants from White Weld and others are aware of development corporations in some of the Canadian provinces that have made some very serious mistakes in large loan situations.

MR. FLEETWOOD: A short term loan is 5 years or less. (inaudible) Their policies, what they do with their funds is based on where their capital comes from. Principally, they are involved in making loans and investments and their loans are of the short intermediate variety and their investments usually cover securities. They are prohibited by law from making equity investments. I don't know the local policy with respect to banks and whether they do reach out for longer loans. Funds in development banks have a completely different capital structure.

80 or 90 percent of their capital is either equities and long term and the other 10 to 20 percent is perhaps short term in nature. So these funds in development banks. (All the rest of this inaudible)

MR. WOHLFORTH: To me your comments are helpful, maybe bringing us back on the track a little bit. Is there a demand for long term credit? Is there a real demand for long term credit? What does real mean? Does that mean there are projects which should be financed now and which are not because of lack of long term capital.

MS. FLEISCHER: Do we have the answer to that question?

MR. WOHLFORTH: I said two meetings ago I think it is probably one of the central questions to the whole concept of a development loan bank in the State. We don't want to set up a credit mechanism which is inappropriate to the economic scene and climate of the State. Everyone in his own mind's eye has perceived the capital needs for Alaska but nobody, it seems to me, has a real grasp on what they are, are they being unmet now for lack of capital.

MR. BARNES: I think Bob alluded to the difference in the Alaska banking system to the United States banking system and is very substantially different. And I think it illustrates that the Alaska banking system a mortgage banking system plus we are filling a gap and that gap is real estate monies. That's where the real need is. We have to now write our mortgages to the

underwriting standards of Outside lenders. Someone sitting down in Washington tells us the criteria we have to use if we're going to sell them loans. And those, in many cases, are not realistic Alaska criteria. They will say we won't take anything that doesn't have streets, gutters and sewers. That eliminates half of Anchorage and certainly the rural areas. So, why don't banks make more mortgage loans on the Kenai Peninsula, we can't sell them. They don't meet lenders' criteria. If the State had a program in which these criteria were eliminated, that I think would serve a real purpose.

MR. CRAWFORD: I notice on the agenda tomorrow we get into the structure. We still haven't decided what our goals are. I think we continue to put the cart before the horse. I think we should decide what the objectives of the Fund and in what direction we want to go.

MR. WOHLFORTH: Do the members feel we are making any progress in our thinking? In the discussions we have had, are the areas sharpened in your minds, the issues that the Legislature has to face and I see them facing it this year and perhaps next year in determining the goals and the areas where this Fund can be effective.

MR. LOVE: I think some of the most important things we can do now, I don't think this Committee can commit the State towards goals in different directions. I think the best thing that we can do is that, if you embark on certain goals, these

might be some of the structures which you might want to look at, if we want to get into development banking. I'm not so sure that it is going to be too fruitful for us to presume that we can set goals, social goals for the Fund. I think what we can do is getting some good background in terms of types of vehicles and the structure that is necessary. I think we should get some facts before us. So when the public begins to deal with these decisions about goals, that they have better information and understanding of the program and they also have before them a bunch of different alternatives and choices so that they are making their decisions based upon the best educated and most sophisticated understanding of the whole thing.

MR. CRAWFORD: We have heard comments from various people about public utilities, secondary mortgages, and fisheries and several others. One of the bases for decisions is how big a pie there is to split up, which we don't have. Can we get projections as to what is going to be in the Fund.

MR. GALLAGHER: I think Bob Barnes' point was well taken. I think under that context is what tomorrow's session is about.

MR. WOHLFORTH: I think it is frustrating for any group to be thrust with any job of finding the goals. And it is possible you can only get to it through a process of discussion, if you will, of segments of lending activities or capital needs in the State. Then the goals could conceivably begin to emerge

as the understanding of what we are dealing with is developed. I, for one, like the question, What Went Wrong. That is to say at least we can be aware of some of the positive things that have happened elsewhere that we want to avoid and we can transmit that to the Legislature. That seems like a valuable effort. I honestly think it is completely unrealistic to say we'll sit down at 9:00 o'clock tomorrow and determine our goals. That is my own private view.

MR. EDENSO: Mr. Chairman, I don't think anyone intends tomorrow to try to identify the goals or objectives, or for that matter, what you will do with the income once you have earned it. I think that will take a public process, public participation process that will include several months and a great deal of effort by a legislative body plus a whole number of dollars which we don't have. However, we do have a task before us and one of the easier portions of that task is to address what kind of structure and organization we may have. I think if you take it in the context that we do want to provide some kind of social service or social good or if you do want to provide some economic development activity or if you do want to provide some community development activity than you can begin to talk about structure and organization and management. I think that we are very seriously remiss in our thinking if we can assume that we can go along between now and January, meeting every month, every two or three weeks at the company's expense without coming up with a

product.

I fully intend to see that this Committee has some kind of product before the legislative body in January. That may mean taking each one of us out behind the barn and settling our differences, or it may not mean that. I am hopeful we will get a lot of cooperation. This is a constructive effort, we are trying to construct something. We are trying to construct a Permanent Fund. We have hired some very expensive, very talented consultants to do that for us. We've got them here, we've had them here several times. We have spent a considerable amount of money. You have listened for literally hours on end to them describe different kinds of organizations, different kinds of funds and I think it is about time we started taking a cut at it. You know, at least a significant portion of our task. To divide the task up into three major catagories, one is what are the goals and objectives. I don't believe we can answer that. I don't believe we have either the time or the money available to us between now and January to do that. A second is, what kind of organization, what kind of structure, how does that relate to the general public, how does it relate to the legislative body and how does it relate to the administration. I think we can address that. I think we can take some real significant cuts at it and come up with very sound, very well based ideas. And, finally, you do have a problem of what do you do with the income of the Permanent Fund. How you distribute

that, how you directly benefit Alaska. I think, again, we are talking about a large amount of time and a very large effort on the part of this committee and on the part of a number of other people. We don't have that time. We do have a committee and we may be able to talk about it. There have been ideas kicked around such as Alaska, Incorporated, such as tax benefits or tax rebates. The only thing that is lacking in that is our imagination and how to address the problem. So, again, I think we do have a task. I'll really put it before the Committee. I think the Committee ought to begin to sit down and look at it. One of the reasonable things we can do is talk about structure and organization. And I think one start at that is what went wrong with other efforts. What kind of mistakes have been made. And then from there just get into a general working session and say, "Look, maybe we want a dual board system or maybe we don't". There are all kinds of questions that that could raise. With that I would ---

MR. GALLAGHER: With the basic assumption that you do want to look at this sort of management structure given this sort of goals and objectives.

(MEETING RECESSED AT 4:50 P.M. AND TO RESUME AT 9:00 O"CLOCK, NOVEMBER 6, 1976)

(CHAIRMAN WOHLFORTH CALLED THE MEETING TO ORDER AT 9:00 A.M., NOVEMBER 6, 1976)

MR. REGIS: This is the second report of Price, Waterhouse. If you recall, the former report was given by Pete McDowell. That first report was a comprehensive look at matters affecting the security and protection of any prospective fund to be established with the proceeds associated with the Alaska Permanent Fund issue. By contrast, this is a specific issue oriented question which was given to us through Jim Edenso and Jim Rhode.

We were presented with three specific questions which this report attempts to address. The first was, what development banks had gotten into trouble and why. Secondly, from our experience with development banks, what are our preliminary views as to an appropriate policy level and operating structure for the Permanent Fund. And, lastly, and this was primarily in response to a question which was posed in the prior presentation, what are some of the specific criteria by which the success of development banks -- development bank efforts are measured.

First, let's take a look at the problems associated with development banks. The only notorious and widely-known case of a development bank failure or what can be called very close to a development bank failure, occurred with the development bank of Ethiopia. This also happened to be the very first

development finance company which was funded by the World Bank. A development finance company, you may recall from McDowell's prior presentation, is in reality just a smaller version of an international developmert company. And the primary distinction is that its concentration is in one geographic area and tends to concentrate on smaller dollarsize issues as opposed to the large things associated with an international finance company.

In this particular instance -- let me step back for a minute, I said that this is the only widely-known case of a close to failure. There are some specific reasons for that which I will go into a little bit later. But for the moment, concentrating on the Ethiopian bank. The problems probably began as a result of a split between the agricultural and industrial sections of their charter. Originally, it was a multi-faceted institution. And subsequently the agriculture was retained and the industrial section was put off in a separate development bank. Now, from what we have been able to determine the causes for the problems subsequent thereto were essentially four. First of all, the only thing left with this bank was the agricultural area. There was too much concentration in that particular sector of the economy. Crop failure or whatever, there was not adequate diversification to protect that portfolio as a whole. Secondly, the key issue, the loans were much too small. Too small to be adequately supervised, to small to be processed efficiently. And, in turn, by their size alone, as one

would guess, they were to mostly unsophisticated borrowers who did not properly use the proceeds to expand production and as a result were unable to repay many of them. Management, and this again is a key issue, management was simply not adequate to the task. And, finally, the control systems which were devised for a multi-faceted bank and which were set up to handle a larger volume, or larger single value portfolio, were not probably revised when they went to a small organization.

These problems were recognized with the Ethiopian bank and it was remerged into the industrial bank and, at the present time, it appears to be operating successfully.

At the outset, I said that there were no known failures and very few notorious examples of problem banks. That requires a bit of comment. For the most part, development finance companies, which are the most risky of all ventures, can be shored up by the local government so they are understandably reluctant to wash their dirty laundry in public, and it is very difficult to find case by case information. Our discussions with World Bank and other associated with them on a no-name basis and trying to concentrate on issues as opposed to specifics gave us a laundry list, if you will, of common reasons why some of the other banks had gotten into unpublicized trouble. And the reasons, again, are pretty much the same as the Ethiopian bank with some diversification but essentially they are: Incompetent management, unusual or undue political influence, and lack of a

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clear operating mandate. And in some cases, there is also one final one and that was too ambitious a program.

A summary of lessons which could be learned from these experiences would be first of all that the operating management must be very capable as must the Board. The appointment power must be removed generally from the political influence so that operating management can and does indeed exercise prudent decisions. The charter of the institution must clearly define the objectives. Impossible objectives should not be set. If you wish to loan a certain dollar value of money, it isn't any trouble to throw it away. And, finally, government influence must be reasonably controlled so as not to dilute the independence of the institution.

The second issue had to deal with organizational structure. Perhaps I will save that for the last in order because it probably will elicit the greatest comments and questions.

Perhaps we will move on to page 6 of this report about measurement techniques. This question primarily arose from a -- one of the Committee members asked, what criteria other than simple ability to repay were used in determining whether or not a program was successful for a development bank. First of all, most of the organizations we presented to you in the prior report were World Bank or World Bank-affiliated, or somehow associated with receiving funds or whatever. The World Bank has

a section called Operations Evaluating Department, or some words very equivalent to that. The function of that particular organization is solely to evaluate the results of particular programs which are undertaken. At the completion of every project, there is a very detailed project completion report submitted by the various sections involved in making the loan. And this is reviewed by the OER Department. From time to time, the OER Department also specifically audits some of these programs and looks to the report to see that it is indeed factual. The thrust of the evaluation process in the World Bank and its affiliates is that it is both inward and external. I use the word inward intentionally as opposed to internal-external. Inward meaning that they use both the borrower, borrower's consultants, other third parties, to measure the success of the project as well as their own internal staff. The purpose obviously being to avoid the prospect of the bank considering its own beauty in the mirror.

Evaluation is really a 3-fold process. The primary thrust is a comparison of actual to plan as it was originally proposed when the project was brought to World Bank or World Bank actually sought it out.

There are a whole series of specific things which are compared in this actual plan which include implementation, just how quickly it was done, if it was done in the same time as proposed, has a serious impact of a host of the benefits

intended. Compliance, did the borrower and the government associated meet the loan covenants and so forth. Did the consumer perform as expected. Questions relating to that. What is the financial performance of the borrower. That is the obvious one. What is the economic impact to the extent that it can be measured. Regretably this is probably the most nebulous area and perhaps one of the prime objectives. Unfortunately, it would take a number of years to really assess it in many cases. And, finally, a question of efficiency. Efficiency on the part, primarily, of the lending institution. Could or should other projects of this like be offered and can it be done in a more expeditious manner.

The second thrust is a macro view of the impact on the economy of the country or the area, whatever was intended and this would be cumulative as opposed to individual. Annually within World Bank there is a report by the Evaluation Section which measures the cumulative impact of all the projects. And this macro view is designed to see whether you help employment, income redistribution, whatever else was intended in that particular country, has the standard of living increased, whatever.

And, finally, is the suggestion at the outset that the thrust is inward. Can we do a better job? Was the performance of the bank actually appropriate to the circumstances presented to it? Was the diagnosis of the borrower's needs appropriate?

Was the definition of the objectives of the project correct at the outset, understood, whatever. Were there unintended effects, either good or bad? Poor or good environmental impacts? Was the bank participation effective or was it detrimental. The purpose of all this is to restructure activities in the future -- future efforts.

Let's move back to page 3. It starts on the end of page 3, Organizational Structure. This is the first, I guess, question for the most part asked of us in terms entirely judgmental call. So far, I think most of our input has been in terms of comparison with other associations with the possible Permanent Fund. For input only this would probably be the first conclusion. This is a very tentative one and there are a number of factors yet to be decided.

The question essentially is, what is the appropriate organizational structure at the policy level for the Permanent Fund institution assuming that development financing is a significant part of the activities. The objectives that we were trying to achieve when we set up this -- our conclusion is essentially it should be a dual board structure. I'll get into that in more detail. The objectives that we were trying to achieve with this dual board structure. First, we wanted to avoid undue political influence while being yet responsive to the political system. We wanted to provide for public input. We wanted to make sure that the organization allowed the

selection of the most capable people. And, finally, we wanted to make sure that the organization preserve the operating management's prerogatives ordinarily associated with management exercise.

The dual board structure is composed -- our suggested dual board structure would be composed of first a board of citizens and secondly a board of directors. The board of citizens, the primary purpose, in our view, in this board of citizens is to react and to act and suggest changes in the charter. Secondarily, it's purpose would be to represent, if you will, the citizens of the State of Alaska and voice their views with respect to the operation of the Fund. I should not say secondarily, it is equally primarily. But that second objective would be accomplished through an annual meeting very comparable to that which is held for normal corporations. This board of citizens could be composed of two -- and that is only a suggestion -- two members from each Senatorial District. We used that since that would be the easiest in terms of trying to preserve one man, one vote at this point. It is suggested the board be composed of two members, elected by popular vote from each Senatorial District, to a term of either two to four years. But to coincide with the election of the State representatives, or the election of the governor or members of the Legislature. The purpose, of course, to get the maximum amount of input into these races.

The board of citizens would meet annually only unless there were some other special purpose. They would not be compensated except to the extent of expenses. And essentially they would be representatives in what might be termed Alaska, Inc.

We were also asked if we felt that a popular election of some portion of the board was appropriate, why we might feel so. I think there are three reasons. The first would be that it allows the public input in the sense that the wishes of the majority of the State can be expressed. The views and concerns of minorities in geographic areas. Finally, it does in reality give life to the concept of Alaska, Inc. There is a very close analogy with the representatives elected here being very comparable to the board of directors or the board of governors being elected by shareholders.

Now, the board of directors. Our view of the board of directors is that initially it be composed of a group of, say 7, it could be as high as 11, that is a matter of choice. But we said for the moment 7 members who would be appointed by the governor, staggered terms, so no one gubernatorial candidate or elected official can control it. And to be confirmed by the Legislature so the Legislature has its input. The board of directors essentially, and the key here is that in our view it is a policy making board. It receives and acts on the issues presented to it by management but does not intervene in management in the sense that it does not present specific loans,

it does not suggest geographic redistribution emphasis, whatever. Its purpose is to set policy and to react to input provided by the staff.

The president of Alaska Permanent Fund, in our view, should be appointed by the board of directors. The key issue here would be the strength of this individual. He should have the power to conduct all the ordinary business of the corporation, hire, fire, be responsible only to the board in the sense of what is normal prerogatives of management. He would serve also ex-officio as chairman of the board of directors but would have no vote.

Those are our views on the three questions presented to us. Are there any questions you might have?

MR. GALLAGHER: How could that large board and the board of citizens be more responsive than a body that is already elected every two years called the Legislature? Why would that be more responsive to the Permanent Fund?

MR. REGIS: I would think it would be more responsive because it has only one issue to deal with. It has only one function, hence the viewpoint of the individual or the use of that function is clearly well established and is not intermingled with a host of other issues.

MR. WOHLFORth: I am not sure the split between the -- you state the board shall be empowered to recommend changes and to receive, consider, and vote on statements of policy for the

Fund submitted to it by the president of the board of directors. The board is delegated all powers, the board of directors is delegated all powers except those reserved to the board of citizens. Have you thought out how far down in policy the board of citizens goes and where the split is between that board and the board of directors? Do you have any comments on that?

MR. REGIS: I believe our view is that the split would be very narrow in the sense that it would be issues that would effect, i.e., for example, an ordinary corporation under the Articles of Incorporation or the bylaws associated therewith.

MR. WOHLFORTH: You also state that the board of directors would be explicitly prohibited from suggesting or recommending any particular financing operation to be considered or made by the board. But it would have power to decide on -- let's say loans or equity investments proposed to it by the staff. What do you mean by particular financing operation? Are you talking there of the actual industry to which a loan would be made or the borrower? Is that what that means?

MR. REGIS: In our view, the board would decide on issues presented to it and would indeed query very closely the staff on all of the factors that into recommending either for or against a particular loan. But it should not enter into the question of seeking out particular areas of loans other than to say by policy. Now, let's say that our policy with respect

to the State is to fund heavily in the agricultural area. That would be the prerogative of the board to suggest to management that these are the kinds of things we are interested in doing as a policy matter. Not to say, put this particular farm on the ballot for us to vote on.

MR. WOHLFORTH: You don't want the board members to come in to meetings and say, " this is a great prospect", you want that to be all staff generated.

MR. REGIS: Yes, precisely. But it would be the board's prerogative to set the sectors in which the Fund should be operating as a matter of policy.

MR. FERGUSON: You are recommending that we have a board of citizens of approximately 40 members.

MR. REGIS: Are there 16 Senatorial Districts?

MR. FERGUSON: The reason I ask this is because on a few of our boards and commissions we have Judicial Districts. Five Judicial Districts. A board of citizens with 40 members would be unwieldy. It takes the Legislature over 90 days just to consider some of these matters. You can imagine how long it would take 40 people to deal with the Permanent Fund.

MR. REGIS: I am a little indifferent exactly how you carve up the geographic areas. I suggested Senatorial. Maybe yours is better. I would not quarrel with that at all. With respect to the unwieldiness, the World Bank has something like 140 governors and it works very effectively. And this particular

board would meet only once a year with basicallyl, 2, or 3 major issues to confront it. It's a very simple function. So I doubt that 40 members would be unwieldy. That is my personal feeling. But, if it is, then you just cut the number back. My reaction is if you can get around 40, 50 whatever it broadens the representation, which is an important feature.

MR. EDENSO: Could a board of citizens board member also be a legislator?

MR. REGIS: That is a question I hadn't addressed.

MR. EDENSO: It seems to me if somebody is running for the State Legislature and there is another board he could run for and be very influential in both areas, it would be a tremendous incentive for him to be on the board of citizens as well as a legislator.

MR. REGIS: I hadn't given that a lot of thought. My visceral reaction would be negative. I would like to think about that.

MR. LOVE: I guess I missed part of this, but why not just make the Senators a board, have them on the citizens board?

MR. REGIS: The reason we suggested that is one of the key objectives, Jamie, that we were trying to accomplish was to allow for positive input from all sectors yet make sure it was not unduly influenced by any one. The Senate is already involved in confirming the board of directors. So if the Senate was involved in confirming the board of directors and was also

serving as a board of citizens, it would have disproportionate weight and influence on the Permanent Fund.

MR. CRAWFORD: If the board of citizens is a group that is only going to meet once a year, why do we need it? Why would any citizen spend time and money to run for a position that according to your presentation is, No. 1, a nonpaying position and, No. 2, has no -- if they meet once a year, what do they do?

MR. REGIS: The purpose of the meeting once a year is to receive the report and the accountability of the operating personnel and board of directors. So you make the Permanent Fund accountable to the board of citizens or, in effect, the electorate itself. And, secondarily, perhaps even more importantly, you want to be able to change the direction of the Permanent Fund if circumstances themselves change. There is no proviso without some kind of public input for the citizens to do that. This way, at least once a year there is a meeting that says, "Yes, are in agreement and the Permanent Fund is proceeding in the right direction", or, "we wish to change it. And we are going to change the direction of the Permanent Fund, here's what we want to do to it".

MR. LOVE: One of the fears I have would be the whole issue of how much money they could spend to get elected, who they could get contributions from. It seems obvious to me you would at least have to think about the problem. Say the canned salmon

contributed 100,000 or whatever to various candidates. I can see basically the recipients of a potential loan being very heavy contributors to the people who are running for office to decide where these loans are allocated.

MR. REGIS: Again, I would go back to the prior comment of making sure there is not undue influence from any one sector. To make unusual contributions to a member of the board of citizens, your prospects of achieving a loan under the protection built into this organization is not great.

MR. LOVE: I'm not saying that if I gave you 500 dollars -- to a candidate that I'd want a loan for a million dollars. I'm saying a particular industry as a whole deciding that they wanted to make a pitch for investment and that they wanted to support various candidates. Let's say the mining industry decided they wanted to put 200,000 dollars in the campaigns and they weren't saying that you had to loan the money to three corporations or this corporation, just basically we want to set aside 200 million dollars for us to develop -- I'm sure they would have a good argument to develop mining resources, and maybe contributions could be raised through corporations, maybe contributions could be raised through executives or other people connected with the industry. I can show you examples on the last poll control on how money has been raised for various industries. What I am saying, is I am not so sure that the members elected to these so-called citizens boards -- if you

make it people that are going to receive major financing from those groups that are looking to get the investments.

MR. RIGIS: You would have to work your way through the, both the operating management which is relatively autonomous and the board of directors who are responsible to the Legislature and the governor, I would think that short of a majority being elected that way, which I think would also surface in terms of a political backlash, it would be very difficult to accomplish. To accomplish loans to a particular segment of industry through the citizens board. I don't think that is a great danger, but I do recognize the validity of what you are saying. They could gang up on a particular issue.

MR. LOVE: What you are saying is it's not going to be a big problem because they are not going to be that powerful. But I assume the first impact is how the money goes and how it is managed.

MR. FREER: I would see the citizens board acting in really a legislative capacity that relates to the Permanent Fund, in meeting once a year and how it has been managed and if it is staying on the track. My comment might be, why couldn't the Legislature sit once a year as a citizens board? They are duly elected by the citizens of Alaska, why couldn't they sit as a board once a year and fulfill the normal functions of a Legislature anyway in reviewing the operation of the fund. That is mofe of an observation than a question.

DR. LOGSDON: One observation might be that the citizens board might be an awfully expensive group to bribe. One thing we are trying to achieve here, as I understand it, is insulation from political processes as it relates to other things other than the Permanent Fund, which might be an argument against the Legislature sitting as a citizens group.

MR. REGIS: That is right. That is our viewpoint in suggesting this as entirely separate from the Legislature.

MR. BARNES: The function of a citizens board is like stockholders, like having the annual meeting and doing stockholder like type thing and would certainly not pass on day to day operations.

MR. REGIS: That's right. Like in an ordinary corporation, it would receive a report from the board of directors and operating management on what the fund is doing and where it is going. And what policy is to be passed upon by them.

MR. BARNES: Couldn't the Legislature do that just as easily?

MR. REGIS: They could indeed. My thought is I would prefer to see something removed from the Legislature so the Legislature has its input through the board of directors instead of -- as control, as it would be under that method.

MR. WOHLSFORTH: There is an analogy too of the Legislature which is supposed to sit as an assembly for the unorganized borough and never has exercised that function. So

one would wonder how close attention they would give to this thing.

MR. EDENSO: I think an observation is a good many of the residents of Alaska perceived the Permanent Fund as a means of insulating government from the legislative body. I think if we assume that the legislative body will have the functions of a board of citizens or a direct board over the Fund, then what the hell is the whole purpose of trying to insulate the Permanent Fund from the legislators.

MR. GALLAGHER: The purpose was to insulate it from undue political influence, not necessarily from the legislators. What you have a dual board structure is to do that. You need the proper political input.

MR. EDENSO: I think what I am saying is that the Permanent Fund is viewed as a savings account, whereas a separate fund which the legislative body can in no way influence for budgetary purposes or government expenditures is one of the most often voiced viewpoints in the public media. And if you turn around and set the legislative body as the policy making body on top of the Fund, then you may have, in fact, defeated the purpose of the Permanent Fund.

MR. GALLAGHER: I don't see it ---

MR. CRAWFORD: An observation is, they can't defeat the purpose, not that they would, of a Permanent Fund if they can't spend the money. As I understand it, that was in the proposal

that passed.

MR. REGIS: But if they were to function as both a board of citizens and to pass on the board of directors that would give them a chief proporation of the influence. I think that is Jim's point, this insulates the Fund from any influence by the Legislature but still allows very positive influence.

MR. WOHLSFORTH: I think we must distinguish between policy and influence, otherwise we are going to be getting off the track very rapidly.

MR. LeRESCHE: I am still unclear as to what you are suggesting as to where the line between policy and operations is. Let's focus on your two boards for a minute. You used the example of concentrating on agricultural investment. And the way you described it the second board of directors would be the deciding body. Did I hear you say that?

MR. REGIS: The board of directors will overall decide the policy of the Fund subject to review by the citizens board.

MR. LeRESCHE: Then you have the citizens board voting on that policy.

MR. REGIS: The citizens board votes on the Articles of Incorporation and the Bylaws and, in fact, passes on the annual report made to it by the board of directors. If the citizens board disagree with the direction of the Fund, they can change that, in effect, through the Bylaws, if they so wish. I think that would also require review by the Legislature at that point.

Because basically the Bylaws and Articles are going to be part of the -- so that goes back to the Legislature and so forth as well.

MR. LeRESCHE: I understand that. But then in your text you also say the board of citizens shall consider and vote on statements of policy submitted by the president of the board of directors. And that is what is confusing me.

MR. REGIS: It is also the reason I stopped because you have taken it out of context with the preceding which says "Charter ...and the receive, consider and". If you change the charter you are going to automatically change all the rest of the direction.

MR. LeRESCHE: But if the board of directors comes out with a statement of policy and says we'll stress agricultural investment and the board of citizens has nothing to say about that short of changing the whole charter?

MR. REGIS: Short of reviewing a change of the charter.

MR. LeRESCHE: So they don't actually vote on that policy.

MR. REGIS: Not prospectively, retrospectively it would apply, either endorsing or suggesting a change.

MR. LeRESCHE: So they can have a positive role, they don't have to sit there.

MR. REGIS: They always have the advisory capacity by meeting once a year even if they don't suggest a change in the charter.

MR. LeRESCHE: So the actual policy sits with the board of directors and the oversight policy is with the board of citizens.

MR. REGIS: That is correct.

DR. LOGSDON: Let me see if I have this concept clear. What you are talking about is essentially establishing a separate corporation to handle the Permanent Fund. The stockholders of that corporation are all the citizens of the State of Alaska. In order to have a stockholders meeting and you can't find a room that is large enough to put everybody into, so you essentially select a certain number of citizens and put them in there to represent the stockholders and they perform the same function as stockholders of any corporation.

MR. REGIS: Very comparable, yes.

DR. LOGSDON: And the reason this is separated in this sense from the Legislature is because you've got a separate corporation. There is no question but that the Legislature represents the people. It's really two separate functions,but because it is a separate organization ---

MR. REGIS: That is right. It is a State instrumentality so consequently you do have to put State input in it.

MR. MOTLEY: Who are the president and this board of directors directly answerable to? Who could fire the president and the board of directors?

MR. REGIS: The president can be fired by the board.

The board can be fired by -- either their term expires or they can be fired by the Legislature and the governor.

MR. LeRESCHE: Which?

MR. REGIS: I hadn't given that that much thought. They way that they are put in, course, is that they are put in by -- the governor recommends and the Legislature agrees. I would think they would have to come out the same way.

MR. LeRESCHE: Do you mean to say they would both have to agree to fire them to get rid of them. The governor appointed somebody and he was confirmed by the Legislature.

MR. REGIS: I would think that either the governor or the Legislature could act to remove them. But it would take both to agree just as it does with any kind of legislative matter.

MR. LeRESCHE: To get them on. But to get them off, that is the question. If either one would refuse to impeach him, then the person could stay on.

MR. REGIS: If either one refused, that's right. But I would think that would also have the override protection. Let's say the Legislature wanted to removed him and votes to do so and the governor says no, there still could be an overriding feature that allows the Legislature by a sufficient majority to kick that particular rascal out.

MR. LeRESCHE: On the Public Utilities Commission, the Legislature voted to knock the guy off and if the governor doesn't like it, it's too bad. It rarely happens, I don't think it has

ever happened on the Public Utilities Commission but that accountability is in the law.

MR. EDENSO: I am not sure I understand what you are getting at, but it seems to me if the person doesn't know who the hell he's working for, who is he going to take his orders from, the governor or the legislative body or who? Who is his boss?

MR. MOTLEY: The line of authority.

MR. WOHLSFORTH: We all know the pattern in Alaska is people appointed by the governor and confirmed by the Legislature are dischargeable, serving at the pleasure of the governor with two exceptions, the PUC and the Board of Regents. Previous to about four or five years ago we did pass some laws where people were removable for cause, which meant in effect their terms are absolute. I think that is the context of the way it is now and anything other that is a deviation, which may be proper.

MR. FREER: Mr. Chairman, are we working in such virgin ground that there is no background or history of how another somewhat comparable Fund might have been structured and worked successfully? Or are we in something brand-new?

MR. REGIS: There is no directly parallel fund from which to draw on.

MR. FREER: We're breaking new ground.

MR. LOVE: The Alberta fund, how about that?

MR. REGIS: The fund is analagous but the function of the fund is entirely different. If you say no to development banking, then Alberta becomes analagous.

MR. LOVE: What is Alberta doing? Can you explain that to us?

MR. GALLAGHER: I don't understand how Alberta is that much different. Take the word development out of it and then talk about what is different about it.

MR. REGIS: Isn't Alberta more concerned with investing as opposed to development and financing activities?

MR. GALLAGHER: What is the difference?

MR. FLEETWOOD: The Alberta situation is not necessarily dissimilar. The only things that are different are that they have taken a definite stand that they are a fund and, of course, a trust fund in that concept and have removed the option of leverage and I think equity as well. I can't remember. But they have indicated that up to a certain percentage of their fund may be invested in development of some project, income producing project, and have various criteria for those. If this were to end up being a smorgasbord, I think it would be easy to say that Alberta is also a smorgasbord.

MR. WOHLSFORTH: Alberta is reasonably new, it hasn't much of a track record.

MR. FLEETWOOD: Alberta is very new in terms of having its own capital in the Alberta Heritage Trust Fund. However, it

has been making investments all along. And within the original capital, which I believe was a billion and a half dollars, some of that came in the form of previously made investments as opposed to cash. They have invested in capital projects, money market instruments, employment-oriented projects, among other things that they are already invested in.

MR. GRUENING: In the Alberta situation, isn't there an assembly, or committe, or its management position more or less the board of directors analagous? I read kind of an overview of it.

MR. FLEETWOOD: I don't know the proper terms for Canadian government officials, but to simply it, it appears that their Cabinet members act as the board of directors. And then there is an administrative group below that, which is essentially the Treasury Department. With respect to the socially-oriented projects, their responsibility comes from the Legislature. And with respect to the profit-oriented or preservation profit oriented projects, the responsibility is with the administrators of the operation.

MR. GRUENING: You have an executive officer who oversees the whole thing. How is he selected?

MR. FLEETWOOD: By the board, the Cabinet members of the board. To be honest, at the present moment the thing is very comingled with the Treasury Department.

MR. REGIS: Isn't it true that at the moment it has not

done an awful lot of development financing. It has the ability to do these things but it has not yet functioned.

MR. FLEETWOOD: As the Alberta Heritage Trust Fund that may be the case.

MR. REGIS: But it is not functioning in the development financing area at this moment.

MR. FLEETWOOD: No. To really go into it requires -- they can go up to 15 or 25 percent in do-good loans..

MR. WOHLSFORTH: Why don't we take a break now.

OFF THE RECORD

ON THE RECORD

MR. WOHLSFORTH: Let's get back together if we can. Just before the break we were getting some comments on the structure of the Alberta Heritage Func and we might resume with those.

MR. FLEETWOOD: Prior to that, we were discussing what they had done so far. They have invested in something called SinCrude Development Canada, Canada Cities Services, the Alberta Energy Company, telephone and municipal finance corporations, and liquid money market instruments.

They can leverage their assets although they can only borrow from the Treasurer. And while by statute or by legislation they can borrow long or short term, the real thing and definitely what they plan to do is not only borrow short term to cover cash flow -- anticipated cash flow at the end of a month

or something, they get 30 percent of the non resource oil revenues and know what it is coming.

With respect to structure, they do have a 24-man Heritage Trust Fund investment committee which is all the members of the executive council in my terminology. It was explained to me in terms of Cabinet members. And it is also my understanding, as someone here pointed out, these are also members of the Legislature. I don't understand their political system so ---

MR. WOHLSFORTH: It is a parlimentary system, is it not.

MR. FLEETWOOD: But this is the provinces and not the nation.

As I stated earlier, when they set the fund up, I believe it was in May, they took investments that had been made with the fund in mind, as well as cash, and had established a procedure on which they would evaluate that. They can continue to receive investments and securities made by other areas of the government in lieu of cash, but these investments must stand pretty strict criteria and there are established means of evaluating even the social benefit non-income producing investments for that purpose. They established some up to guidelines with respect to how their funds could be used. If people here determine to have guidelines, which is the only way to do it, if you have specific guidelines of, say, for example, 30 percent of the Fund's assets must be in something and 20

percent must be in something else, it can only cause problems of operation and may lead even to bad loans at times when you would want to make very good loans, by doing so you may distort the ratios, therefore, you must quickly look for one in another category in order to make the loan that you want to make. Some up to procedures. In any case, they are allowed to invest 20 percent of their assets in projects which provide long term economic and social benefits for people that will not necessarily yield a return to the fund.

MR. FEGLS: A prior question was posed to me, did I see this organization as appropriate if the primary function was to be a development bank. I wouldn't consider 20 percent to be the primary function. And my response is tempered to the kind of organization which would have as one of its primary functions development bank. I think if the smallest point were 20 percent then I might come up with a different answer, but that wasn't the way the question was posed to me.

MR. WOHLSFORTH: 20 percent, what about the balance of the 100?

MR. FLEETWOOD: 15 percent may be invested in the Canadian or provincial government type securities. Up to 100 percent could be invested in income producing social economic diversification and development type projects as long as they were income producing and yielded a return to the fund. And that is in potential development. And up to 100 percent of the fund

can be invested in temporary money market securities at the discretion of the Provincial Treasurer. The major purpose there is idle funds are funds waiting to be used in one of the other catagories.

MR. EDENSO: You said Provincial Treasurer, is that the treasurer of the government of treasurer of the fund?

MR. FLEETWOOD: I am responding to the question are there similarities in the goals and objectives. I am not recommending structure. This is very integrated into the system. The Provincial Treasurer is the guy that operates and administrates the fund to all intents and purposes.

MR. EDENSO: Is he an employee of the government, or is he an employee of the fund?

MR. FLEETWOOD: He is an employee of the government. There is a Gary Beatty who is manager of the Heritage Trust Fund.

MS. FLEISCHER: Who is he employed by?

MR. EDENSO: I think that answers my question, thank you.

MR. FLEETWOOD: The officials in the Treasurer's Office, I have a list here. The officials in the Treasurer's Office are five people. One of them is the manager of the Heritage Fund. But if one were to deal with them, you would deal with any one of the five people. And the five are the Provincial Treasurer, the Deputy Provincial Treasurer, the Assistant Deputy Provincial Treasurer and the Director of Investments, Financial Management.

MR. EDENSO: Mr. Chairman, I think what we are talking about is the similarity of the fund, the proposed fund and its activities in Alaska not of the Alberta Heritage Fund. And I think the discussion up to that point of having to do with the dual board system proposed by Price Waterhouse.

MR. WOHLSFORTH: I think it was asked if there were any situations which were analagous and I think that led to the Alberta structure. Do we have any more questions on the Alberta structure?

MR. LeRESCHE: Who hires the executive director?

MR. FLEETWOOD: I am not that familiar with it. Our Canadian people are very close to it, I don't know about the appropriateness of the structure, the similarity and purpose are definite. They do report as Dan has been suggested, they have annual reports and a committee of the legislature reviews them on the performance of the fund.

MR. LOVE: This is a parlimentary form of government.

MR. GALLAGHER: I think I might have a broader definition of a development bank. I think your definition is more narrow than mine. I would see a broader definition and that is why I would see some difference.

MR. FEGIS: Are you trying the definition out on me?

MR. GALLAGHER: Well, as I perceive your definition of a development bank, it is only for economic diversification.

MR. FEGIS: No, I wouldn't say that. Do you mean

economic diversification would be the sole criteria?

MR. GALLAGHER: Yes, of a development bank. That is what I perceived when you described it.

MR. FEGIS: My perception of a development bank -- we are using the word bank, but it's really an institution. My definition would be the fund of resources to be used to accomplish basically social objectives which are primarily economic in impact through the private enterprise system.

(REPORTER PLAYED BACK LAST ANSWER AT MR. FEGIS' REQUEST)

MR. WOHLSFORTH: Now, that you have heard your definition, do you wish to amend it? I think it is a tall order to define the purpose, the structure and the goals. So I am sure people will bear that in mind when they start to tear it apart.

MR. LeRESCHE: Would you include in your definition a cooperative, say, for example, as a feed into the free enterprise system?

MR. FEGIS: I don't think I understand your question.

MR. LeRESCHE: Would you include things like co-ops and stuff like that as utilized into the free enterprise system?

MR. FEGIS: Yes.

MR. LeRESCHE: Is free enterprise anything that is not part of the government? I want to make sure I understand your definition of free enterprise.

MR. FEGIS: In this context, yes. To primarily use the private sector of the economy.

MR. LeRESCHE: That could include private nonprofit corporations?

MR. FEGIS: I would say yes. The criteria would remain the same whether or not the funds were granted to that enterprise.

MR. LeRESCHE: They are at least equal.

MR. WOHLSFORTH: Let's see, where were we. Do you want to pursue this definition of a development bank or turn your attention back to structure? What is your pleasure? Are there any other comments?

MS. FLEISCHER: I wanted to ask about several things. You said the question you were answering is, how is he fund to be structured if this is a development bank?

MR. FEGIS: If a significant activity were development banking.

MS. FLEISCHER: I had a thought on the board of citizens. I don't really see a use for that board of citizens. I think it would be sort of a useless board if they met but once a year and had no real power. In fact, I'm afraid that you could see this as an attempt to tell the citizens that they did have power and they didn't have power and they might be cynical about the board of citizens. I'm not sure whether they should or shouldn't have power but I see that particular setup as a sop to the citizens by saying you would have control over the Permanent

Fund through your board of directors. I don't think it is realistic to think that they can change the bylaws, especially if it has to go through the Legislature. And if they did change the bylaws, it would take them a long time.

I was wondering if, for instance, the Fund were a savings account fund or even initially a savings account fund, if a decision were made to invest money and then put the income into a general fund, for instance, it would be set up entirely differently.

MR. FEGIS: It certainly would, yes.

MS. FLEISCHER: Then the Legislature would make the decisions about the money would be spent out of the general fund. So if they decide to invest in fisheries or decided to invest in agriculture, whatever they decide to do, they would make the decision because they would be spending out of the General Fund.

MR. FEGIS: I don't think this particular suggested organization would fit those circumstances by any means at all. If you were going to a savings fund concept, the relative risk becomes measurably less. So I am not even trying to address that question. Just as a pure commentary on that, if you are going to go to solely a savings account concept, if that were the primary function, then a whole lot less complicated organization would be drawn up, there is no question about it.

MS. FLEISCHER: Maybe we should be doing this, laying out the alternatives. It could be a pure savings acount, it

could be a pure economic development fund, or it could be a broader economic development fund. Or, it could be a combination of those three things. If it were any one of those, or a combination, the structure would be different. Or, maybe it wouldn't. What I am saying is, maybe we should start saying, if we want it to be purely this kind of fund, then it would be set up this way. Then we would ask, how would you set it up as a savings account fund? How would you set it up if it were going to be a purely economic diversification fund. How would you set it up if it were a broader development fund. How would we set it up if it were going to be a combination of those? What would be a good combination? What percent would make the most sense. Maybe what we should be asking you is, if you would give us the structure of at least those four alternatives. Then we could give it back to the Legislature and say, "Okay, if you want to make this decision, then this is the structure.". And other decisions could be made according to how it is set up. Then we could lay out the choices so it would be really clear to the Legislature as well as to the people of the state.

MR. GALLAGHER: I agree. That's one of the things we take up in the last hour, just sitting down and discussing whether the likely management --- If your goals and objections are savings account, you're going to have a different one. And I thought we would take the last hour in just discussing that very thing because there are certain implications. Quite

obviously, if you only do what is called a savings account, the need for broad input on policy decisions as to what to invest in is a lot -- you don't need that large of a board.

MS. FLEISCHER: Because the Legislature will, in effect, be making the decisions.

DR. LOGSDON: There is a question that comes up in my mind here as to this citizens board as being any kind of board that can function. On the basis the amendment was stated, I am not certain myself that the Legislature can abrogate their authority through the board to do anything besides what this board here is and that is just to advise in more or less a general sense. I think there will really be a legal decision.

MR. GRUENING: I think your point was and it is well taken, that ultimately the goals will have to be established by the Legislature and only the Legislature. That would just clarify some of the problems we had initially -- in which people were alarmed that this group was somehow going to decide the goals. I am bothered somewhat too that we are thinking that whatever the structure is is going to administer the whole fund. I have been thinking that maybe we want to be very modest of that portion of its administering so that we have maybe a track record of -- maybe as much as 10 years before we decide we're going to do something with the other half of the fund. The savings concept, I think -- we were stating yesterday, you heard Mr. Richards state that he thought the voters didn't intend anything

but long term investments. I think that is probably farther from the mark than saying they probably intended a savings portion of that. So maybe what we're talking about is a structure that is going to administer a small portion of that fund, at least for the first decade. I am just tossing that out for thought. We may not get too worried about whether this is going to be the structure for the Permanent Fund. And I think Lanie has a good point, we might consider also if it is going to be a savings acount administration for a number of years.

MR. FERGUSON: I think that is right. I think we can embrace the concept of economic objectives. It is going to take several years of front end investigation and accumulation of capital before you are going to have the ability to do it. You're probably right, for several years probably into some kind of a savings account program and to a lesser extent development.

MR. LOVE: I think that one thing we need to start addressing pretty soon before we make any decisions about structure, is a better overall picture of what I think are three important areas. One is a better idea of how capital markets are currently served in Alaska. I think some more actual data as to what markets are being served to what extent by what institutions, what gaps there are, what our perceived needs are. Secondly, I think we have to have a better overview in terms of current loan programs that the State is already managing so we have a complete inventory of what already exists, what the

experience of each one of those programs has been, what the successes and failures of our own programs have been. And how much money is involved relative to the amount of money we are talking about being in the Permanent Fund in the next five years. And I think the third thing, we have to have a much better idea as to how the size of the Permanent Fund relates to the overall revenue situation in the State over the next 10 to 20 years. In other words, how big is the Permanent Fund going to be when the State runs out of revenue from Prudhoe Bay. When is that going to happen? And what size is the State's budget going to be ---

MR. GALLAGHER: We showed you that at the first meeting.

MR. LOVE: Part of what we got was, how big is the Fund going to be. How big is the State budget going to be relative to the amount of money ---

DR. LOGSDON: The size of the budget will be that money that is available plus a certain percentage.

MR. LOVE: I think maybe if we think we're going to have an incredible bust in 20 years, that a savings account may, in fact, be all of a sudden much more important purpose for the Fund that the development aspect. It may be then that the development aspect becomes more important as we need to develop a broader tax base. I think these are three different areas where we need a lot more data than we presently have. We can realistically make real solid choices in terms of either the

goals or the structure.

MR. WOHLSFORTH: There is a lot of insight into what Jamie just said. We can approach this thing from the point of view, does there have to be an economic study of just where we are, and a long term economic study of how effective our capital markets are and what sort of projects are ready to be financed. What has been the effectiveness of our existing loan programs. And then even this broader one, how large is the State budget going to be in relation to the Permanent Fund in 10 years. This has implications obviously for the savings account concept. I think these are things that really are worthy of consideration.

MR. EDENSO: I think it is really nice to raise those kinds of questions and to seeks answers to them. However, in reality, we are really faced with the question, do we or don't we want to address something called the structure of the Permanent Fund. We could spend the next 10 years studying the nature of the capital market in Alaska and we would find on an annual basis as the price of oil fluctuates the capital market in Alaska so fluctuates. I think what we've got is a question before us, we could consider a number of ways to approach it. And I think, again, that looking into the future, we would be a little remiss in waiting for some period of time. I've heard as much as 10 years structured out there to try to establish the structure of a Permanent Fund. I think in 10 years we'll have a fund that is in excess of at least a billion and a half dollars

and it could well be even more than that. We are doing ourselves an injustice if we don't start kicking off at some point in time. In approximately 120 days we are going to start getting money in the Permanent Fund. For example, what are we going to do with that money? Who is going to manage it? If we don't have a structure at least established by then, we are not going to be able to answer that question. Are we by default going to let the Division of Treasury manage it in the money markets? Are we going, by default, allow some bankers in Alaska to manage it? Are we going to allow the State Legislature to meet once every Friday and decide whether or not to buy or sell some fixed income security and whether or not to buy or sell some mortgages in the State? Are we going to have to sell some money or buy some, you know, as a result of our lack of decision. I submit to you that gets to be a fairly costly undertaking. We have got to address structural organization. It would be desirable to answer every question you could ever think of but it gets costly the further down you go.

MR. LeRESCHE: I just want to repeat something that we said before but we don't seem to follow up on. Jim is right, some suggestions have been made that the Legislature certainly has to deal with this. But even our expert witnesses and consultants say the structure will vary according to the objectives we set forth. This group hasn't set specific objectives for the Permanent Fund yet and, therefore, it is

premature to discuss specifics about the structure. That's about as simple as I can say it.

MR. GALLAGHER: I would like, Mr. LeResche, to take that question on. We've been selling that Permanent Fund now for two years and we've been talking about goals and objectives. In fact, what we have sold to the people quite often might be called a smorgasbord. We've talked about savings accounts, we've talked about these other things. At this point in time, to go back and say, "People, what we have in mind now is either only economic development". At this point in time say to a certain constituency, "We lied to you. We're only going to do this sort of thing".

MR. LeRESCHE: Let's just say what it is we want. Four alternatives, like Mrs. Fleischer says. Let's write them down and say, this structure fits this objective. We just don't seem to be able to grab hold of that although we all seem to agree that it is necessary.

MR. RHODE: Mr. Chairman, in discussions at the staff level with Mr. Edenso, the Deputy Commissioner, and others, just exactly what Mrs. Fleischer urges is what we hope to do in the next step of assignments but that is subject to the sense of the Committee. It is quite clear to me that the Legislature is not going to recommend that the Fund be turned over entirely to construct buildings at the University of Alaska. We're not going to have a Texas permanent fund. There are three major

areas of activity for the Fund, or as were demarcated in a publication by the Department of Revenue and given here at the last meeting. Given those broad goals, we expect this Committee to state its recommendations and preferences, but also offer alternatives to the Legislature. I hope this would be the feeling here that we don't know exactly that we are going to favor aluminum plants as opposed to apartment co-operatives in order to proceed.

MR. LeRESCHE: I am talking at the level of savings account, direct social objectives, maximum return on investment, industrial diversification. You choose a different mix or those or you choose one or the other, you have a different management structure. So let's lay them out.

MR. RHODE: It can be done so let's ---

MR. LeRESCHE: This gentleman is in the unfortunate position of saying what structure fits a certain type of objective.

MR. RHODE: As a special background, Price Waterhouse was in the area of development loans. You're bringing up exclusively savings account. They have expert advice on money markets and things like that. But it can be laid out and I am just suggesting that it be. Maybe I'm not quick enough to realize the things that are implicit.

MR. EDENSO: We do have a problem and that problem is, without a goal, without an objective, we can't in fact look at

some reasonable approaches to management and structure. We are faced with a very critical time factor. In 120 days or less, 115 days approximately we are going to start receiving funds into the Permanent Fund. We need to have something before the legislative body for their consideration. I do not believe it is possible, given the current level of resources, both monetary and human, to establish the goals and objectives of the Permanent Fund. I just don't believe that is possible.

Another major question is, what do we do with the income. It's not that we haven't thought of it, we have. We have tried to take the most reasonable approach possible in looking at the major problem areas we are confronted with. And I am sure that as we go along we are going to find that different structures are going to fit very neatly with different kinds of objectives, but we can't afford to ignore what is in front of us.

MR. LOVE: In response to Jim's question, frankly I'm at the point where I feel -- in a position to just make a motion that we recommend the money just be placed in the financial markets initially until we can do the work necessary to develop actual goals and objectives for social programs, and I think it is premature for us to get involved ---

MR. GALLAGHER: You are talking about strategy, not goals and objectives ---

MR. LOVE: Without getting into too much controversy, I mean in terms of semantics and stuff, let me just say that I

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think we are going to end up putting the money in conventional money markets for a period of time until a lot of the planning and work with the public and with the Legislature, until we begin to have some of this data that I talked about earlier and it becomes available. I think that is what we are going to initially start with.

MR. GALLAGHER: Except the basic goals and objectives, economic, maybe diversifications, community development and savings account. Then you're talking about strategies, as to how to do those things. Strategies are things that will change from time to time as the economy changes.

MR. LOVE: I don't want to get into a big argument about goals and objectives because I think there is confusion about what those words mean. I can agree with you and still say that, in my opinion, I think what we are really coming down to --- We're just going to take the total amount of money in the Permanent Fund, the first half year is not going to be all that significant, as I understand, particularly in comparison with all the other State's revenue.

MR. GALLAGHER: 90 million isn't significant.

MR. LOVE: That's about the size, isn't it, of the VA loan program? What I am wondering, isn't that what we are really talking about, at least initially when the money first comes on. Realistically, we're not going to have any other choice other than to put that money in conventional money markets.

MR. GALLAGHER: Yes, you do. You have a choice, you can keep up with the Veterans Loan Program ---

MR. WOHLSFORTH: If you please, stop the colloquy. Mr. Gruening is next.

MR. GRUENING: I appreciate Jim's comment that he wants a work product out but I think the reason we need it out isn't something horrendous is going to happen if elaborate structure isn't established the first part of the next Legislature. I think the Legislature might address itself to some kind of temporary administration of it. What Sterling is suggesting that maybe you just buy current investments, but that is something the Legislature would have to consider and may not think that is such a great idea. They may wish to have that money as it is accumulating, before they establish an elaborate structure or any kind of structure on a permanent basis, authorize some kind of temporary administration, maybe, as any other surplus fund. Of course, that would give you the authority probably to buy those loans. But that is something you might consider whether you might give the Legislature a recommendation on a temporary basis. I don't think we have to come up with the structure that is going to exist for the next 10 years.

MR. GALLAGHER: I really can't conceive of us, Clark, going back to the voters and saying we are not going to do any community development, we're not going to do any housing ---

MR. GRUENING: I agree with you on that. But I think

Lanie is absolutely right, we do have to outline some goals and say these are the structures that will probably be more appropriate for those goals. If you have a combination, you might amalgamate some kind of thing. I think there is time for that. If we come up with a structure that we are not exactly happy with, it doesn't necessarily have to be the one that is going to exist for the next 10 years.

MR. GALLAGHER: I don't see, if you make the decision you are going to invest in housing, how the structure is going to change.

MR. GRUENING: Let's say that then, but let's get into it.

MR. WOHLSFORTH: If we do nave these back and forth colloquys, we have just got to keep them short. It isn't fair to the other members. Everyone is itching to say something. I am not blaming anybody, but please don't make my job any harder. Who had their hand up next to speak?

MR. EDENSO: Thank you, Mr. Chairman. I don't believe that this meeting was intended to come out with something that would be our recommendation to the Legislature for a structure and organization. I think it is a first effort at considering various structures that are available and really getting down and having some meaningful dialogue in trying to tear them apart and put them back together, are the circumstances we are confronted with. And I really think that, although this may not seem

constructive, this is constructive. What we are all attempting to do is put something together. And for all practical purposes, I think talking about goals and objectives is really a good thing and should happen. The question in front of us is, are we going to have some kind of structural organization at least identified. The various ones that have been put before us, from what I could see, none of us are really all that familiar with to be able to look at them and talk about it. White Weld had to come here and explain the Heritage Fund, which you all had at the second meeting.

MR. GRUENING: I am not suggesting we debate the merits of the savings account aspect as opposed to another thing, that is not what I am saying. I'm saying let's take that and see if there are any differences that should exist in the structure to administer that kind of policy.

MR. GALLAGHER: That is what I want to do in this hour, talk about -- if you have a savings account objective, what are the differences in management structure that you might desire. Or if you want to have a smorgasbord, what -- or if you want to do all three of them -- what are the institutional things that you want to have in it.

MR. GRUENING: And along with that, what structure might you consider as an interim structure until we think we've really got a handle on it.

MR. FERGUSON: I'd go along with the board of trustees

7 members appointed by the governor and confirmed by the Legislature to take care of the administration of the investments in the Permanent Fund for "X" amount of years. I feel right now, without knowing all the alternatives available whether we have diversification or whatever. We're not going to be able to do that here or in the next six months or a year. I think what we are going to do is make recommendations to the Legislature and the Legislature will have its ideas. I think the first thing we have to do is at least recommend that we have a structure set up to administer the investments of the funds as they come in until we actually see how much money we have. It's easy to say we're going to have a billion dollars in there in three years, but until we see that it is awfully hard to determine how to utilize the funds.

MR. GALLAGHER: Let me talk for a second about what I would like to accomplish by this session and what I would like, maybe, a group to accomplish by the next session or the following session.

I can see what I would like to accomplish by this session is come up with a management structure. If we agree that the three goals are savings account, community development and economic diversification, come up with a management structure at the next session. That we spend the interim between that session and the following thinking about the strategies as to how you accomplish those things. In those areas we need a

whole lot of sector analysis on, let's say the housing. What are some of the institutional things that we have got to go through the housing, where are the housing needs in the State. If you want to talk about fisheries, during the interim, the Legislature has hearings on how you affect a sector called fisheries. In the following session, when we have 200 million dollars probably in the Permanent Fund, then we have those policies established. The Legislature has then had two years to work on the problem and at that point in time, you can start accomplishing something.

MR. FERGUSON: If I may respond to that, regardless of what structure you set up, you're not going to be able to reach all the people. You take ---

MR. GALLAGHER: It will help the Legislature in doing the sector analysis that will be necessary for the following year.

MR. FERGUSON: You take the debt on bonds, general revenue bonds, I think that is one way. Although it still doesn't reach the maximum amount of good for the whole State. You take the airport bond that just passed, is basically for the rural areas. You take the University of Alaska basically for the urban centers. So you can't reach all the people. You take tax rebates, that's only going to reach the taxpayers.

MR. GALLAGHER: I'm saying that what reaches the people is what you do with the Fund. It's the strategy once

you have the structure. Once you have the structure, the Legislature then spends the next in-term years developing strategy as to how do you help the people.

MR. FERGUSON: May I make one final comment. I think the Committee is wandering away from the subject I presented, but I think there was a purpose in having asked us to present a proposed structure for this type of -- strictly development banking fund. This probably represents the most complex of all the things you might do. I think this was part of the dialogue with which you attempted to begin. But let's start with the most complex and then we can work back to something less.

MR. RHODE: Representative Malone will be here later but he always expected that a temporary statute would be necessary to provide for the routine investment of whatever revenues are reaching the Fund. What he is hoping for from this Committee are recommendations and alternatives on structuring the fund given a set of goals, exactly as you have been discussing here. And that does not have to be done under a crisis footing. As Representative Gruening said, this may well be a process that involves the session of 1978 or beyond that.

MR. GALLAGHER: Jim, are you contemplating not even addressing the management structure until you've got two or three hundred million dollars in size?

MR. RHODE: No.

MR. GALLAGHER: Because it's the sector analysis, the

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strategy, where all the analysis has to go in.

MR. RHODE: This Committee ought to be able by session time or in the early months of the session to be able to assess or make some recommendations along the lines, if there is to be any development activity, for instance, you ought, or ought not, to have a governing board insulated from those who make loan appraisals and so forth. Or, if this Fund is to make any kind of community loans, then you ought to consider the following: 1, 2, 3. And offer its assessment together with its professional advice. And also there is considerable experience here in the banking -- experience, I will have to say, more considerable than in the Legislature. That is why Representative Malone, particularly, wants to hear from this Committee. But it is not to prejudge it for the Committee or not to prejudge it from the Legislature. The Legislature may well be able to resolve a lot of these organizational matters by the first session, but hold that until the goals and so forth have been settled and combined with the enabling act. I wouldn't begin to predict that.

MR. GALLAGHER: Do you mean goals or strategies?

MR. RHODE: As you like.

MR. LOVE: I would like to address this to Price Waterhouse. If we are really talking about not embarking on -- just accept this as hypothetical and not the concensus of the group -- what we are really talking about in the first year would be a conservative approach on how to invest these funds.

Probably just putting the money in a conventional money market. Looking at perhaps a more diversified approach in the second year after a lot more information has been brought in and more people have had more time to examine all these things. It probably would make sense then to recommend a 7-member board of directors and a 32-member citizens board right off the bat.

MR. FEGIS: No, it wouldn't make sense to provide for that.

MR. LOVE: I am looking for you to think in terms of making a recommendation to us. One of the alternative structures would be to simply perform a function of very conservative investments the first year. And, secondly, maybe provide some information and advice, either for the Legislature or this Committee, or the administration during that first period of time, planning for the second year. And I would like to know how that structure would differ from the structure that is in this paper right here.

MR. FEGIS: I have not given that question a lot of thought. But my reaction is that probably the citizens board would not be required at all although you might want to have it provided for at a future point. I think you specifically would want to provide for it at least in this concept, you want the citizens to be able to input and say we do not want it to be a savings account. That may be one thing you would get out of the citizens board one year hence. So I think you would want to

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provide that it could meet within a given period of time, probably on an interim basis.

MR. LOVE: I'm not quite sure -- what structure did you say we should have if it is to undertake this job that I have outlined for the first year?

MR. FEGIS: I think I would like to think about that question a little further. I would say that at the outset, at least, there wouldn't be a necessity for it.

MR. LOVE: I certainly think it is among the range of alternatives we're going to have to present to the Legislature.

MR. GALLAGHER: I think there is a need to come at the next session with something to start working on strategies.

MR. LOVE: I included that in the ---

MR. GALLAGHER: I am not necessarily disagreeing with you. I think there has got to be some sort of structure in order to do strategy analysis -- planning, on how you help the various structures. So when you come back to the next session, at least you can start to accomplish something.

MR. LOVE: I think the definite planning ought to start now and be in high gear for the next few years. I think by the time you get going ---

MR. GALLAGHER: The strategy will take the longest time to put together.

MR. LOVE: Maybe that is one the major recommendations we can make. The initial management structure for the Permanent

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Fund have a very large mandate toward doing certain types of planning jobs, certain types of economic planning jobs. The types of analysis that we think are very important. Maybe that is more important a job in the first year than making loans.

MR. GALLAGHER: I agree. I think the sector analysis of each sector is how to help it along with public funds by the Legislature would be very necessary. In order to get anything accomplished in the second year Legislature.

MR. CRAWFORD: There was a suggestion about an hour ago that we look at the options and maybe thrash those out and I, for once, would kind of like to get on with that.

MR. BARNES: I think I would agree with Mr. Love's earlier suggestion that it is almost time for a motion to promote some kind of progress in this Committee. And I would suggest that I don't feel any sense of urgency that some members do to come out with particularly anything except to recommend that the Legislature enact temporary legislation to invest the funds, which are not going to be very significant in conventional money market investments to give us the time. Then, if they want to -- for us to flush out all the options, which they can do themselves, then let's do it. I think we should decide that there should be a suggestion for them to make temporary legislation and then, if they want to give us their goals and objectives, then we can certainly work out the alternatives for them.

MR. GRUENING: I think that is a good suggestion, but

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I think we could go farther. If we make a motion that we all go home -- I would concur with that motion but we might suggest to the Legislature something they could consider in terms of structure on a more permanent basis. I think that is what Jim would like to see us do.

MR. EDENSO: Again, this is a first cut at looking at a structure and organizational basis.

MR. GALLAGHER: Let's do what I want to do in this hour. One of the things I would like to accomplish in this hour is, if we want to talk about savings account objectives, what sort of management structure the Committee would see. To me, there are two obvious things. One, you can either leave it in the Department of Revenue -- and, if your goal is only savings account, then leave it in the Department of Revenue and have them manage it just like any other fund. That's the most inexpensive. Or, the other alternative is to have some sort of small board overview that activity but still have it accountable to one manager. If that is your goal, the savings account, what does the Committee think of those two alternatives?

MR. WOHLSFORTH: I can give my view. I don't think it makes any sense at all to have a board, an operational board, and it has been proven state after state that it is a pain in the neck. You need one manager who should be the State Treasurer, or in this case, the Department of Revenue. Also, bear in mind the State lost a lot of money in 1970. And, again, I am agreeing

with what someone said here. By not getting into the investment act for the General Fund until June 15, the money came in, as you know, the prior September. In the meantime, the State could only invest in direct U. S. Government obligations, it couldn't even invest in agencies. So we had over 900 million dollars at that time at which we were losing an increment of anywhere from 1-1/2 percent to whatever the differential was because the Legislature had it in mind that they had to deal with the whole problem rather than simply segments to get us a reasonable money market instrument statute. I would hope that would be avoided this time, that there could be an investment statute on the books by the time money is in the fund to permit a proper rate of money market instruments.

MR. LOVE: I would like to offer a motion that we recommend to the Legislature that in the first year that the Permanent Fund be managed by the Commissioner of Revenue under existing statutes ---

MR. GALLAGHER: That is not what I want accomplished this hour.

MR. FREER: Maybe we've reached that same point that Abraham Lincoln did when he came to this little group of soldiers at the fence and he couldn't figure out what command to give them to get them on the other side of the fence. Maybe it's time we fall out and reassemble on the other side of the fence.

MR. WOHLSFORTH: Are you suggesting a break?

OFF THE RECORD

ON THE RECORD

MR. WOHLSFORTH: Take your seats, please. Yes, Mr. Gruening.

MR. GRUENING: I have a motion to make. I move that the Committee direct Commissioner Gallagher to draft for consideration at the next scheduled meeting of this Committee a temporary statute which authorizes management of the Permanent Fund monies in a manner similar to the Department of Revenue's present administration of surplus funds.

MR. WOHLSFORTH: Is there a second to the motion?

MR. LOVE: I'll second it.

MR. LOGSDON: May I make an amendment that it be a statute and not a temporary statute?

MR. GRUENING: I concur.

MR. GALLAGHER: I have a question. Does that mean some sort of sunset provision in it like this one will self-destruct after one year?

MR. GRUENING: Make this discussion on the motion. Presently there exists a set of statutes which deal with the Commissioner's authority to invest surplus funds. Now, the Permanent Fund will have to have that kind of statutory authorization from its establish forever. Because there always be funds that are not immediately invested in one of the goals,

whatever they will be. They are funds that are coming in. They are funds that haven't been administered for purposes of the goal. So you always have to have that kind of statutory authority. So, in a sense, maybe this could be a statute that exists for the life of the Permanent Fund. On the other hand, I like the suggestion of a sunset provision. It may be in the structure. You might consider that, but I think that maybe right now what we are concerned with is strictly how are we going to administer this fund until we really get the structure for the goals more firmly established.

MR. GALLAGH: Let me say what I see. I see the Department of Revenue under this and see if we agree. Investing, during next fall, monies and meanwhile the Legislature will pass a statute creating the structure. During next fall they will start creating the management structure that starts doing some of the strategy work as to how to help various sectors. And then at the end of the following session you will have implementary legislation as to how you implement various strategies. Am I clear?

MR. GRUENING: I'm not entirely sure what you're saying. I'm saying that this particular recommendation, the draft would not create any instruction that doesn't exist now. It's just authorizing the administration of funds that come in under some kind of arrangement. We may not agree as to how similar it should be to the present statutes dealing with surplus funds, but

we would like to look at a draft, that's all.

MR. GALLAGHER: I don't want this to be the end-all of things that we do.

MR. GRUENING: No.

DR. LOGSDON: I might suggest that this be a clause in the statute permitting the Commissioner to invest these funds, with a structure that was established in the future. To provide funds to this as established by the Legislature.

MR. GALLAGHER: I think when you revise in the following session under a strategy bill, that will be part of it. And at that time the Commissioner of Revenue will phase out of it, which I think he will more than likely do.

MS. FLEISCHER: What I wanted to say about the sunset clause, which I understand gives the people a chance to reaffirm things on a periodic basis. So perhaps what we could do is see that the sunset clause is in the enabling legislation itself but it doesn't have to be in this first statute.

MR. GRUENING: Is that an amendment?

MS. FLEISCHER: No.

MR. GRUENING: The constitutional amendment itself establishes the fund. There is nothing we have to do further to establish the fund, it is established. Money is going to accumulate as of an effective date of 120 days. Actually, the money doesn't start to accumular until the effective date which is 120 days.

MR. GALLAGHER: Certification date.

MR. GRUENING: Certification. So the money isn't accumulating now, it won't be accumulating until another 120 days, whenever they certify this last election. What we are talking about is a recommendation from this Committee, after Sterling drafts a suggested piece of legislation which would authorize somebody to handle those funds in some manner, a very conservative manner. They're not going to make any long term investments, that is the sense of my motion.

MR. MOTLEY: Mr. Gruening, what do you visualize as far as the objectives of the Commissioner of Revenue? Can he invest this thing in equities and can he invest this thing in just savings accounts, can he invest it to deposits to banks? Can he do all these things?

MR. GALLAGHER: What he is saying is for me to come back with a recommendation.

MR. GRUENING: I am not suggesting any of that. Obviously, not in dams or a lot of things that have been discussed here, but something to conserve the principal. You can't just put it in a cache or put it in a piggy bank. Probably in CD's. My intention would be something -- CD's, something very modest like that, in Veterans loans. But I want to see what he comes back with and we can discuss it at that point.

MR. LOVE: I am speaking for the motion so we can get

a motion on record so we can progress fast. This is a comment to the Commissioner, I would be hopeful that it would be a structure that would provide a somewhat liquid investment of the fund.

MR. GALLAGHER: If there is something -- and things don't come on stream and I'd bet into some sort of box. Of course, there isn't that much money in the fund.

MR. WOHLSFORTH: Is there any more discussion on the motion? The question has been called. The motion, as I took it, is that it is the direction of the Commissioner of Revenue to draw up a statute for presentation to the next meeting, which would authorize him to invest the Permanent Fund in a manner similar to other State funds. And included in the motion was some provision, some time limitation on that authority. Is that correct or not?

MR. GRUENING: I would use the language, authorizes management, although it means investment. I think the public needs to know the distinction between the kind of investments the Fund will get into in the future and the need to manage the Fund on a surplus fund. I don't want them to think we're drafting a statute dealing with, authorizing him to make investments at this point. It is an investment but not the kind of investment people are envisioning.

MR. WOHLSFORTH: Money market investments.

MR. GALLAGHER: I want it very obvious that it is a

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temporary thing.

MR. GRUENING: Right. In order to manage, you've got to invest but I think the language "authorizing management" of the Permanent Fund.

MR. LeRESCHE: I thought your original motion said interim management.

MR. GRUENING: Somebody objected to that, but if you want to make another amendment. I don't really care, one way or the other. Every statute is temporary in the sense that it can be repealed. You could put a self-destruct date on it which would make the Legislature consider whether -- if it does adopt it, whether it wants to continue it.

MR. GALLAGHER: The other assumption that underlies the whole thing is we are going to work on having a structure next year. I want that clear to everyone out there in the world too. We can't put that in the bill, but we are just talking about general understandings.

MS. FLEISCHER: Could we have a reading on the motion?

MR. GRUENING: The motion is the Committee direct Sterling Gallagher to draft for consideration at the next scheduled meeting of this Committee the statute which authorizes management of Permanent Fund monies in a manner similar to the Department of Revenue's present administration of surplus funds.

MR. WOHLSFORTH: Are you ready for the question? All in favor say aye. Opposed? Motion carries.

MR. WOHLSFORTH: We have accomplished only a small part of the task.

MR. GALLAGHER: Let's talk about the time with the Committee. I have to have a report to the governor on Monday having to do with a totally unrelated subject and that is going to take me about three hours to write. I need some time, that report has to be typed all day Sunday and I have to hire a Kelly Girl and things like that to be ready for a Monday morning meeting. My time limits are getting short. I would like to go through maybe some sort of a drill -- not a drill, something like you suggested, Bob LeResche, and put up maybe a savings account or maybe the four objectives up on the board and talk about just management structures overall and see how the Committee reacts to them.

MS. FLEISCHER: You mean right now.

MR. GALLAGHER: Yes, or do we have time to do that.

MR. WOHLSFORTH: How long can you meet with us?

MR. GALLAGHER: I can probably meet for another hour and a half.

MR. WOHLSFORTH: That would be then basically our agenda for the rest of the day so far as your involvement is concerned.

MR. LOVE: I would like to hear if there are alternative ideas on the ways to do management. Part of my inquiry is to find out if other members of the Committee have other ideas.

MR. GALLAGHER: I would like to do some freelancing. Mainly what I want to do is have a freelance, if we talk about these goals -- structures.

MR. LOVE: One idea that I think we are going to have to deal with sometime and that is -- if there is going to be a movement to regionalize decision making or something like that -- I'm not convinced that is best idea but I think we should at least look at different models -- maybe not having a centralized board, maybe having different communities or different segments of the State being able to make different choices. Just like the Regional Corporations are taking a much different direction in terms of funds and maybe splitting the thing up may be an alternative we ought to look at as opposed to a centralized fund.

MR. GALLAGHER: Before we go jumping off into community development, why don't put put the four different things that we have been talking about: Savings account. Economic diversification. Community Development. And then maybe title a third one, Smorgasbord.

Let's talk about the savings account area. The Commissioner of Revenue can invest it under some sort of surplus, or you could have a separate institution do it. Let me give you a run at this one, just my personal feelings on this one. Doing savings account investments is a very technical thing. You don't need a whole lot of board input. That is what we have presently -- the State Investment Advisory over the year -- kind

of a trophy, it didn't have any real function because the only thing the Commission of Revenue could invest in were money market instruments. When we got the 900 million everyone thought about doing development and community loans but the crush of the budget prevented that happening. So the original purpose of the State Investment Advisory, it just kind of withered away for two or three years there because there was just nothing really to do. That's why, if you're going to have a goal of savings account, at the most you have -- maybe you could set up a separate fund and have a small board and that's the extent of it. Does anyone see any difference in the management structure? You can either do it through the Treasury and have an Advisory Board or have a full board with a director and two or three people to do accounting.

MR. LOVE: I think you can really decide the purpose of the Fund is a saving account purpose but you can still get involved in quite a bit of social loans in the State that are income producing. You may make a decision, for example, that the money markets, which are not perfect or not adequate, are serving some very profitable and sound investments within the State of Alaska. Mortgage loans and areas outside of conventional neighborhoods.

MR. GALLAGHER: Are you suggesting something like they do in the retirement fund, invest in the highest and best return. I do invest in mortgages.

MR. LOVE: You may have fairly elaborate social types of loans being made that still gain, you know, right up there in highest and best returns. In markets that are not the conventional money market, simply because the money markets aren't perfect. What I am saying is it may be necessary in a savings account approach to have some type of fairly active input in terms of social goals.

MS. FLEISCHER: You mean socially oriented decisions about where to invest the money.

MR. LOVE: Another thing, if you look at savings accounts, you may decide for a savings account to be super effective, you may decide for a savings account to have an impact on future generations that you may want to slow down the rate of growth by not putting the earnings back of the general fund back into the Permanent Fund because you may decide that the savings account may not be very effective if it is very small related to overall State expenditures and revenue maybe 20 years from now when the Permanent Fund disappears. To me the savings account is a real objective goal and it may have broader policy implications in terms of investment strategy, and for that reason you may not want to invest it in the State, you may want to invest it out of State.

MR. WOHLSFORTH: I think the income must go to the General Fund.

MR. GALLAGHER: No.

MR. LOVE: If it's a true savings account, then the income should not go to today's citizens, the income should definitely go to future generations. So I think it would have to be, if it is a true savings account, reinvested.

MR. WOHLSFORTH: I don't know about that. You've said an awful lot in the last couple of minutes. You said a savings account might have social objectives and then you sort of transitioned into such things as mortgage investment. Mortgage investment which has been done through the retirement fund has a perfectly legitimate nonsocial context. There is nothing socially oriented about buying a 10-1/2 percent good Alaska mortgage.

MR. LOVE: It is serving markets that haven't otherwise been served.

MR. WOHLSFORTH: Every investment has a social content, if you're talking about even investing in General Motors stock or whatever, U. S. Treasury. I think you get to a pretty attenuated use of the word social there. I don't necessarily accept the proposition that any savings account has to have its interest reinvested. Equally, you can have the income and the principal is there for future generations. I do accept the basic proposition though that may make some sense that even with a savings account it is good to have a board to ping-pong your work against at least twice a year. That is always good for a manager.

MR. CRAWFORD: A couple of the options that have been suggested here such as proceeds of the savings account concept going into the General Fund or proceeds going back to the Permanent Fund for a specified period of time for growth fund.

DR. LOGSDON: What do you consider a savings account?

MR. GALLAGHER: In my mind we mean government corporates and fixed income. You can also buy private placements. You can also make CD's.

MR. EDENSO: Are we considering the different ways you earn income in the savings account approach, or are we considering some kind of a structure and organization for managing the savings account approach?

MR. WOHLSFORTH: I think we're off on a mixture.

MR. EDENSO: Well, regardless, you have a pool of money there and you have agreed to manage it somehow, you've got to have some kind of management decision making process which tells you investment A is better than investment B verus C, or what have you. And if it's going to be into some kind of developmental activity or some social goal, then you're going to have a board or management structure that somewhat varies from a pure investment banking function where you're making decisions on money market instruments, whether fixed income, equity or mortgage loans. It's a different kind of activity, a different kind of decision making process. To try to get a board to agree on one instrument over a specific period of time when you know

the money market is changing daily, you might never gain any income opportunities. Under savings account then, we're talking about a straight money market activity.

MR. LOVE: This is something I don't think has been discussed. Let's say that your policy for the savings account was partially to buy mortgages in Alaska because they are considered good investments. So you went into the secondary money market and you're buying notes from savings and loans with commercial banks, is this the area where the Permanent Fund should get involved like making decisions, here's a chance to use the economic power of the State of Alaska to use these social funds to reform institutions within the State. For instance, say we will not buy mortgages from savings and loans if they use the proxies because we don't think that's a democratic way for that institution to function. I'm just using that as an example. At some point if we decide, you know, whether or not it would be the purpose of the Permanent Fund even if it was managed as a savings account to get involved in using its economic power to get other types of objectives out of different institutions within the State. I don't know if you guys want to talk about that at any point or rot.

MR. GALLAGHER: The financial objectives you get out of U. S. Government, when you invest in U. S. Government, are you going to say, you know, get -- on your deficits?

MR. LOVE: You might not get anything out of there but

you might very well be able to affect the savings and loan industry.

MR. GALLAGHER: When we're talking about savings account, we're mainly talking about investment decisions that arise outside -- it's a trust account and you look for the highest rate of return. And that quite likely may not be in Alaska.

MR. WOHLSFORTH: Let's accept the proposition that it is possible the Legislature could indeed decide that they wanted to reform financial institution practices in Alaska through the use of the monies in the savings account. All right, we've said it now let's go on to something else. I don't think it's a realistic use of a savings trust account personally. Others may think so.

MS FLEISCHER: Would that include mortgage investments, secondary markets. As we heard yesterday, the savings and loan sell their mortgages to these outside investors and whether that is the kind of investment we would be making with this Fund in the State. If it is, then could you also tie that to some decision, for instance, to invest in home mortgages in the villages.

MR. GALLAGHER: No, then that would become some sort of developmental.

MS. FLEISCHER: If a decision is made that it does not produce income, but experience shows that it is sometimes income producing. That has been shown in Chicago in areas that

were redlined because the banks decided they were not income producing but, in fact, when they went in there and did make loans to those neighborhoods, they were very high income producing loans, in fact higher than citywide. So my question is, who is making the decisions as to whether ---

MR. GALLAGHER: That is an important structural question.

MR. LOVE: It is an important one I think, who is going to make the decision.

MR. GALLAGHER: The thing that is analagous to it the pension fund. And we do try to fill the unfilled need in the State. One of the things we try to fill is the 68 to 100,000 dollar market where there is no Outside investor for, and on which we get outrageous rates of return. The major market that we are filling with the pension fund is the 68,000 to 100,000 dollar market.

MS. FLEISCHER: There is a person staying at the house now from Bethel and you can't get loans on houses in Bethel. Or if you get the loan, you can't get insurance. Is that need being met?

MR. EDENSO: Well, Lanie, you have to understand the nature of the way land is sold and deeds in rural Alaska. Sometimes you just can't get any kind of indication as to who owns title to what. And you have the consideration of whether or not you have adequate fire protection and whether or not you

can get insurance on your mortgage.

MS. FLEISCHER: Well, apparently they can't.

MR. GRUENING: Maybe what we are trying to get at through the trust account if we do want to reform the practices of banks, maybe it can be more directly done through a statute which says you can't redline, or identifies redlining. Maybe we're trying to do indirectly what we can better do through another means, another vehicle. The other points, let's say housing loans to Bethel, if the bank isn't making it -- maybe that's what we're going to do under community loans. Have the Permanent Fund make it directly out there. But I think we are going to end up having everything under one category again.

MS. FLEISCHER: My question was, is this a good place for it and your answer was probably not.

MR. GRUENING: Probably not, but we could list it.

MR. WOHLSFORTH: Is there any more discussion under savings account.

MR. LeRESCHE: Could we pretty much establish the principle that the savings account objective would require the simplest of all the management structures? Is the board agreed on that?

MR. WOHLSFORTH: Yes.

MR. CRAWFORD: Possibly under options there, we should list the trust concept of managing for the highest return.

MR. GALLAGHER: That is one of the goals you have to

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write up there, Jim.

MR. LOVE: I would like to at least look at the structure of the Regional Native Corporations as an alternative to that of a centralized system. We've got sort of an analagous situation. If the Natives are managing for the purposes of providing revenue and profits and mostly making investments within the State of Alaska -- this is at least something that I think should be analyzed in terms of alternatives.

MR. LeRESCHE: I don't understand which characteristics of the Native Corporations he is talking about.

MR. LOVE: There are separate corporations representing geographic areas of the State. Maybe the same thing could be done with the Permanent Fund. I may not advocate that but I certainly think we ought to at least consider that, particularly since there is such an obvious model to study, you know, the implementation of the land claims.

MR. EDENSO: I don't see the similarities between the Permanent Fund and the Native Land Claims Settlement Act at all. I don't think there is any degree of comparison. The one has a completely different objective than the other. The Native Land Claims Settlement Act was to satisfy what Congress recognized as a just claim upon the State of Alaska and the U. S. Government. The other is the Permanent Fund which distributes benefits from a resource owned by all the residents of the State of Alaska.

MR. LOVE: What's the difference?

MR. EDENSO: The difference is the Native Land Claims Settlement Act is mandated by law to provide in fee simple title, mainly land distribution to the 12 Regional Corporations and to provide monetary distribution to the 12 Regional Corporations. It also identifies specifically who the beneficiaries are under the Act.

MR. LOVE: The beneficiaries are the people of Alaska, I think that is pretty clear.

MR. EDENSO: Who are the people of the State of Alaska ten years from now.

DR. LOGSDON: There is one point that I think he is trying to make here. Should the Fund be in the whole or should it be subdivided in parts based on one thing or another. For instance, we heard yesterday the possibility of subdividing the Fund by specifying a certain percentage of it should go in utilities, a special fund for utilities. I think what he is saying is, should we subdivide or ---

MR. GALLAGHER: The question is, should it be sectoral or regional.

MR. GRUENING: Maybe one of the points Jamie was getting at is maybe democratizing the economic decisions by region. If we're talking about development, shouldn't the people within a given region decide what kind of development they want as opposed to, let's say a central board which may be represented -- let's say Anchorage interest -- developing our Anchorage economy

is built on development on the outside. Maybe it might be determined the region in which people would like to live should have a say in the structure as to how they want it developed.

MR. GALLAGHER: The other way, of course, is sectoral. You have to do power development, you have one to do utility development and one to do agricultural development.

MR. GRUENING: Decentralization of management is maybe a better term. I think that is a basic question, whether we're going to have a one management structure for development or whether you decentralize.

MR. EDENSO: Decentralization decision making.

MR. LOVE: These are all various alternatives. It could be completely an autonomous corporation. It could be central management with regional decision making, development for a particular area. It could be combinations of the two. It could be completely autonomous Statewide thing that just did everything at a State level. Maybe that's the most efficient way to do everything.

MR. WOHLSFORTH: Does this all presuppose a central governing board which interfaces with a regional development corporation. Let's get back to a little logic there. There is a Permanent Fund, not 12 or 14 permanent funds established by the voters. Almost certainly, it seems to me, there has to be a central -- some central governing body

MR. LOVE: That could be a very simple function. An executive director, divides up based on population, 13 or 16 or 10 ways.

MR. WOHLSFORTH: I don't think myself that is what is in contemplation.

MR. EDENSO: It seems to me, Mr. Chairman, we're not talking about structure of organization, we're talking about functions, developmental function, and trust savings account function, community development loans. These are all different kinds of investment policies and investment functions.

MR. LOVE: To give you an example, let's say Kachemak Bay where the Statewide organization said we want to develop this area, offshore oil development, that's really the best thing to do, more jobs. The people of Kachemak Bay said we want to develop the fisheries, we want to have hatcheries and we want to have this and we want to have that. I see there could be a conflict in terms of --- I'm just saying this as a possibility, this may be a lousy example, but there could be different ideas about what development is best for the area.

MR. LeRESCHE: I think you're talking about different objectives for different areas rather than about different management structures.

MR. LOVE: I think we should be openminded about all possibilities. It may be that you would want maybe 6 or 12 different management structures competing against each other and

some maybe would do very good and some maybe very bad, but maybe out of that -- maybe as a development approach, you'd learn more about it maybe than having a central organization with nothing to compare its success or failure against.

MR. WOHLSFORTH: Just one more time and then I'll quit. There may be real merit in having regional authorities and they may be closer to people and they will be competing, but nevertheless it seems to me contemplated, unless I am absolutely crazy, that we have some central agency of some kind that has to allocate between agencies. Unless there is to be a 12-party division of the fund right from the start among those agencies. Would you accept that?

MR. LOVE: No, I wouldn't. I'm not saying I'm against it ---

MR. WOHLSFORTH: I am not talking about what you like, I'm talking about what the thing says.

MR. LOVE: I think that you could conceive that there would be a very simple administrative function at the central level that really was hardly anything ---

MR. GRUENING: What I had in mind -- I think you're right, I think there has to be some central administration to determine which region gets it. But the idea would originate and be administered by a regional authority which may or may not be part of the Permanent Fund. They won't have to be. They could spring up on their own. But the concept would be the

Permanent Fund wouldn't take, say Outside investors who want to move into a region, or develop, or promote -- they would be dealing as say the World Bank is dealing with other authorities. That was just one thought I threw out. I can't anticipate that you would divide the Fund into 12 -- say if you were going to go as a model the Regional Corporations -- say we'll have 12 funds. I don't know how you could divide the money in any way that would meet the constitutional mandate.

MR. EDENSO: Mr. Chairman, I really have some difficulty in understanding what Jamie is talking about, but it seem to me what he is trying to do is -- an organizational idea or a pure structural idea, what normally happens very efficiently in a market. If somebody has an idea that maybe is going to make money, they go to a bank, they find out if that idea has got some merit, the bank either says yea or nay, and you go with it. It sounds to me what Jamie is trying to do is create a whole bunch of little things that you are going to have in a central location anyway to satisfy some kind of structure. Is that my understanding of what you are saying?

MR. GALLAGHER: Let's look at a management structure of -- it's only a new development, what a management structure is quite likely to be is a small highly technical staff.

MR. LOVE: Centralized, either regionalized or centralized.

MR. GALLAGHER: Either way. You can have a small

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technical staff. A staff that goes out and makes a whole lot of little tiny loans or a staff that makes a series of very large loans.

MR. LOVE: How do the Native corporations do it. As I understand it, they are autonomous -- the money is divided up among them and then they do out and do their thing. The make their own investments, they make joint ventures when they want to. Some of them invest in their own communities, some of them invest in Anchorage.

MR. GRUENING: The money is divided according to the Bill. It is complex -- based on population within the region. I don't know where you would draw the line -- you might be able to do it by statute, say so much money would go in this region ---

MR. GALLAGHER: You mean make it on a per capita basis of revenue sharing or something like that. Well, when you talk about development loans -- let's say divide up a region -- a development loan in the Aleutians, it might be a whole lot more risky than a development loan in Anchorage.

MR. WOHLSFORTH: Certainly, the idea of a local development corporation is a good one. I support that, it might be a good intermediary for this kind of thing. But I can't see that the amendment contemplates a division of the money by regional sector so to that extent I don't think you can go much farther than simply recognizing that we may interface with local corporations.

MR. LOVE: The only reason I bring this up and I hope in the future we can have some presentations on this. I would like to learn from the Native Corporation's experience how they manage their funds, what kind of investments have they made, with what success or failure have they invested. I would hope at some point we would have some info on that.

MR. EDENSO: Mr. Chairman, there is information on that. It is published annually in each annual report from the Native Corporations. And for all practical purposes they have made their investments into construction activities and into money market instruments.

MR. WOHLSFORTH: I think it is a good point and certainly they are a model of somebody who has a lot of money to invest in the last four or five years.

MR. LOVE: I don't want to be on the record as an advocate for a decentralized system but I think it would be wrong for us not to consider this in our options and to take a look at some of the advantages of doing it this way and also the experience of how it has already been done. If it has been a bad experience, I would like to know why it was a bad experience and in what areas does it feel it has had a good experience. So that we can know that as we develop our own structure.

MR. GRUENING: I have great difficulty in envisioning how you could apportion as they have done in the Lands Claim

bill money by either region or population. If it were by population, it would all go to Anchorage. I am trying to cope with that. I don't even think we can talk about it in terms of dividing it -- the money by region, but dividing the decision making as to how the money is used within a region. I think we are addressing a political question here. Maybe we don't want to have one agency saying we're going to make a loan in the Bethel area for this, no matter what you think. I think that's what we are getting at.

MR. EDENSO: I think one of the things that was addressed by centralization, decentralization concepts was the idea submitted by Price Waterhouse and the recommendation for a board that would be composed from all the various election districts in the State. That would very definitely give you input on a regionalized basis as to how you would structure and possibly make decisions concerning either savings, development or community development types of activity.

MR. WOHLSFORTH: Don't we have something we can put up here?

MR. EDENSO: So far we haven't had anything to do with structural organization.

MR. WOHLSFORTH: As Clark just said, divide the decision making by regions and this raises the issue would there be some sort of subsidiary governing board by regions or does representation on the citizens board meet that problem?

Central and regional boards might be better than funds.

MR. LOVE: I like Clark's suggestion of saying that we consider recommending that people in a given geographic area have some say over the types of development investments in their own communities. I think that sounds like something we should really ---

MR. EDENSO: One of the problems I have is the way Jim has been writing these up here, one thing versus another thing. I think what we are doing that way is excluding one over the other. We should just say centralized boards, decentralized boards, etc.

MR. CRAWFORD: Under development, I think it would also be appropriate to get into the management of it on an administrative rule basis, whether or not the funds would go to development of any of these at the highest return to the fund.

MR. GALLAGHER: Development doesn't necessarily mean that. Maybe the highest economic return but not the highest ---

MR. LOVE: I think that's true, we've got to resolve whether or not the development loans are going to be prudent or best return, or what is the alternative criteria ---

MR. EDENSO: We can give it away. The point on that it seems to me you at least have to earn some kind of income whether it is 1 percent or 2 percent or 100 percent.

MR. GALLAGHER: You may be looking at the highest economic returns, or you may -- but then you stray away from that

and decide to make it social -- tie in a social one. Say in a rural area an economic diversification that doesn't really make all that much sense. It employes lots of people ---

MR. LOVE: I think there is a difference between high return to a return and a lower interest rate. And a third category is marginal chance of return. That is a decision we are going to have to decide whether or not we want to include in the types of investments that won't pay off at all. That could make the Permanent Fund less than permanent. If it does pay off -- but if it doesn't pay off, at some point we are going to have to develop some philosophy along that line.

MR. WOHLSFORTH: I would say that income producing, you're not only going to get the income but you're going to get the principal back too.

MR. LOVE: I think it's a threshhold question.

MR. EDENSO: Mr. Chairman, under the decentralized concept, would the decentralized board or organization , would that be making decisions concerning an investment or a series of investments or something of that nature. And, if so, how would they indicate that to some kind of a centralized organization which establishes a Permanent Fund. You obviously don't have a dozen Permanent Funds, you only have one.

MR. GALLAGHER: Jim, there is one other third sort of board that we did talk about. It wasn't regional, it was sectoral.

MR. LOVE: Instead of boards for geographical areas, boards for various types of development. You may want an advisory board for petroleum development, mining. And you bring in people with unique expertise versed in these various areas of development that are more qualified to give advice in those particular areas. I think that has a lot of merit.

DR. LOGSDON: The thing that scares me about that is the only example I am able to put my finger on is the failure of the development bank.

MR. LOVE: We are just showing alternatives here. He is not saying that the loans would be diversified, he is just saying an advisory board for something like that of particular industries so that they could have a broad background.

MR. WOHLSFORTH: Sectoral advisory boards? I don't know what that means but it sounds good.

MS. FLEISCHER: Another consideration if we did that, we'd still have to have some way to protect the neighborhood, even if the decision were made by an expert, it still could be a bad decision for that village, that region, that area.

MR. GALLAGHER: It's a combination. It's a central board with a combination of sectoral advisers. And under the central board you go out and talk to the people and see if they want it in that area.

MS. FLEISCHER: There could be a project developed which would be absolutely devastating to that particular village

or region.

MR. GALLAGHER: There are two ways to do it, you can put the decision making out there or do the hearing process out there.

MR. MOTLEY: I would like to ask the board for a comment. If you decentralized this and went into various regions, let's assume, for example, a genuine need for electricity and a particular individual in that particular region where the dam is going to be constructed says I like to fish in that stream and therefore I think this is really a disastrous thing so henceforth let's say no to this particular area. Wouldn't this cause a lot of problems in some of these larger development programs that may be necessary for Alaska.

MS. FLEISCHER: Maybe the need is for energy, maybe thermal energy is a better answer than a hydroelectric dam.

MR. EDENSO: I think, again, central boards is descriptive of possibly more than one board.

MR. LOVE: We have the Price Waterhouse model which is one model for development. Another approach I think might be to just turn the development completely over to the Department of Economic Development and just make it a cabinet position -- say that that function of the Permanent Fund be managed by somebody in the Cabinet. I think that is an alternative you might want to consider.

MR. MOTLEY: Wouldn't that come under a great deal of

political pressure?

MR. LOVE: In terms of development loans I think that might be good.

MR. MOTLEY: That means that the present governor or whoever designs that Cabinet then can pretty much select in which direction that the Permanent Fund's monies are going to go.

MR. LOVE: This may or may not be all the funds that are in the Permanent Fund. It may be that a certain percentage is in savings account, a certain percentage in development.

MS. FLEISCHER: The question then is, do you want it subject to the pressure of the population, maybe you do want politics to have something to say about it.

MR. LOVE: Maybe you just want a commissioner who is a member of the governor's cabinet subject to confirmation or rejection by the Legislature.

MR. GALLAGHER: There is also one other thing, you could make it all in CD's and put it all in banks and let them make all the decisions.

MR. LOVE: Let them make all the decisions, that is something they have expressed a willingness to do.

MR. GALLAGHER: I didn't hear them say that.

OFF THE RECORD

ON THE RECORD

MR. LOVE: Mr. Meekins approached me yesterday about the Legislature making up the board of the Permanent Fund. I

know that there are many legislators who think that is a good idea. I guess that is not too surprising.

MR. GALLAGHER: They don't have the power under the Constitution to be able to do it though.

MR. LOVE: Maybe they were given that power by the Constitutional amendment.

MR. GALLAGHER: They weren't given any executive power, all they were given was policy making power.

MR. EDENSO: The question then comes, can a legislator also be on the board. Then you've got a board that is 60 members strong, not 40.

MR. RHODE: I have had discussions with legislators on that point. And I said it awaits legal advice by the Legislative Council or the Attorney General as to whether in fact the Legislature could, in fact, or further as one legislator has suggested that they be able to approve each and every loan over a certain size. I have been advised that possibly because the amendment was a separate part of the Constitution the normal doctrine of separation of powers might not apply.

MR. GALLAGHER: We have a pretty clear case on the Royalty Board on which the people just voiced their opinion.

MR. WOHLSFORTH: I think there are some real legal questions here that I hope are being addressed at the outset. I have at least four that I have heard. A. How much latitude is there in the Legislature to divide the Fund up into regions.

B. How much delegation is permissible by the Legislature to aid the board. C. What does income producing mean. And D. Can the Legislature appoint members of the board directly, or sit as members of the board.

MR. GALLAGHER: That's a question whether the Legislature considers it executive.

MR. WOHLSFORTH: I think they are all interrelated. I think they are major questions that have to be addressed very early.

MR. CRAWFORD: Is the Attorney General addressing those questions?

MR. GALLAGHER: We have to know what the questions are before we can answer them. We will try to get them answered, yes.

MS. FLEISCHER: I move that we ask Sterling to ask the Attorney General for answers to those questions before the next meeting.

MR. CRAWFORD: Can I make a suggestion on your motion. And I will second it. I would like to amend the motion to read either the Attorney General or a private attorney, whichever has the time prior to the next ---

MR. GALLAGHER: The Attorney General has a staff of 35 attorneys.

MR. CRAWFORD: I just want to make sure we are going to get it back so we can do something on it.

? : Would you repeat the questions?

MR. WOHLSFORTH: A. How much latitude is there in the Legislature to divide the Fund up into regions of the State. B. How much delegation of powers is permissible by the Legislature to aid the board. C. What does income producing mean. D. Can the Legislature directly appoint members of a board. These are broad questions and I wouldn't have the vaguest notion that a young Attorney General spending all his time from now to the next meeting could give us clear-cut definitive answers. But at least he can get started on it.

MR. CRAWFORD: I think it would be helpful to give some type of deadline, either we can get an answer or we can't.

MR. EDENSO: What are you going to do if he doesn't.

MR. CRAWFORD: It is sometimes helpful to give people deadlines.

MR. WOHLSFORTH: We agree. Let's move on to community loans.

MR. GALLAGHER: Community loans. I can see in this area direct lending, I can see indirect lending -- I am just going 1, 2, and 3, Jim. You can see community development corporations. You can see different sort of boards, different agencies for different sort of things like housing, utilities. Again, we're going over the range of possibilities.

MR. LOVE: I think Sterling earlier brought this up the idea, I don't think it should be community loans but rather

community development. I think the earlier concept was that you just go to highest and best use and maybe go to a trust approach in terms of income producing, and you just give people money and let them make their own choices. I mean if people have more money then they can afford to pay more local taxes, they can afford to buy houses easier.

MR. GALLAGHER: You can't do that as an investment loan, you can only do that with income producing investments.

MR. LOVE: We're talking about three goals, trust account, economic development and community development. I'm saying that you might achieve community development better by distributing money ---

MR. GALLAGHER: They've got to produce income and have to have an asset.

MR. LOVE: I'm just saying that the way you might develop a community is by having a trust account, instead of reinvesting the money in a trust account, distribute the money to people and that they use their money in the market place to develop their own communities. I would feel better if you put down community development as a goal because I don't think the goal is to make loans, the goal is to develop -- development type of stuff.

MS. FLEISCHER: Community development loans.

MR. LOVE: Giving away money might be -- from the income, distribute the income.

MR. GALLAGHER: That isn't in this management structure.

MR. EDENSO: You've got something written up there, fund, and I didn't hear anybody say fund, and you've got CDC's and I didn't hear anyone say CDC's. And you've something called differential. We're talking about structure.

MR. LOVE: I think Jim's point is he may want to deal exclusively with CDC's for community development. That is a potential way of doing it and it also addresses some of the things we talked about earlier -- development loans, you know, sort of decentralizing them.

MR. EDENSO: Why don't we say what CDC's are first.

MR. GALLAGHER: Let's say in fact what they do, they do a lot of small business loans, they are not much into the housing business.

MR. LOVE: I think there is a lot of emphasis on CDC's. In depressed areas where they have tried to develop local economy, big emphasis on jobs. However, I think as Sterling has mentioned in earlier meetings, they could just as well be involved in construction of houses as well as anything else.

MR. EDENSO: Bob, do you have any ideas on structural organization?

MR. BARNES: My idea on this type of thing is, if you're going to have a central board to handle this thing, then what does the central board look like. I think the model that Price

Waterhouse came out with is basically the model that everyone seems to be happy with, but we haven't addressed that citizens board type thing. I don't think we should get into whether we're doing direct loans or indirect loans. I'm talking about the structure -- who is going to manage this, and we're philosophizing on how you do these things but not the structure of this entity that does it. I think that is what we should concentrate on.

MR. LOVE: I think it should be decentralized as much as possible.

MR. EDENSO: Do you have any ideas pertaining to the structure itself or the organization of the structure, possibly a board or not a board?

MR. BARNES: I sort of do think that the citizen board approach for the political sensitivity is important. That could be a small board appointed by the governor who actually operates the entity and let them choose the management. I don't think we should get into the board will have to have so many managers. We can give that to them as their responsibility delegated to them. And I think that is the basic structure. We all seem to come back to that. And the Legislature will tell us the philosophy, the goals that that board is supposed to meet. No matter what you're going to do, basically that structure is going to serve if you have a developmental type approach. If you have the savings approach, you have a small board and a small

staff. And I think those two alternatives are the only things we are talking about.

MR. LOVE: I think we are going to have to deal with the same issue here that we did on development loans and that is -- we may come to different conclusions on the two programs -- and that is whether or not you want to have decentralized decision making about what the priorities are in different communities as far as development in those communities. You still will be able to have centralized management of the actual development but you may want the decisions made about what they want developed decentralized.

MR. BARNES: Mr. Chairman, I would say the citizen board concept answers that question. You do have the input, that's what they're there for. If you keep putting this decision points out all over the State, you're going to get nothing done. Someone will say no or veto it or something like that. So it doesn't serve a purpose to say you have to completely put it out there. You have the input on a general broad basis and that's the only way it's going to work. They can't say yes and no to every project, you'll get nothing done. Ten years from now you'll just have money piling up.

MR. MOTLEY: Might I take a few minutes of the Committee's time. I've spent quite a bit of time with a number of other people, managerial people throughout the business community on the kind of a structure that I would like to

basically put out to have the Committee review and have discussion on. And, if it would be acceptable with you, I would like to turn the board over and put it down in black and white so everybody could see.

MR. GALLAGHER: That's what we are trying to accomplish here, finish up community development. Has it been already discussed in the development aspect or is it a combination which we come to next?

MR. MOTLEY: It's basically just a structure to manage the Permanent Fund, period. It does not have any objective goals or anything else, but at least establishes a centralized managerial group, such as Bob Barnes is talking about and also Frank Fergusion was talking about it.

MR. GALLAGHER: What is its objectives?

MR. MOTLEY: The objectives will have to be settled by what the Legislature says.

MR. GALLAGHER: Then what you are trying to do is nonresponsive to what we are trying to accomplish.

MR. MOTLEY: Well, basically, I thought we were trying to accomplish a structure, a managerial structure, to handle these Permanent Funds. There has been a comment made that we have to have a different kind of managerial structure if we have a savings account or if we have a development corporation or a community loan project. I don't think so.

MR. GALLAGHER: We still have one category left called

combination. If you want all three of those goals or an additional one, maybe what you want to do is bring it up when we get to combination.

MR. MOTLEY: All right, I'll wait -- I'll hold off until after we finish the combination.

MS. FLEISCHER: I still don't understand how you'll get regional decisions reflected under community development. I think that people will have some priorities in their own communities that somehow have to be reflected and I don't understand how that ---

MR. GALLAGHER: You don't think it can be accomplished with some sort of sectoral -- say the Natives want teachers housing, and then you do that through Alaska Housing Finance, you don't think that can be accomplished.

MS. FLEISCHER: Do you want to put -- repeat what we've said under development under community development.

MR. GALLAGHER: I think we have it up there.

MS. FLEISCHER: Okay, then spell it out for me. The board made up of representatives from different agencies?

MR. GALLAGHER: No, let's say you have one agency handling housing and another one small business loans.

MS. FLEISCHER: Then how does a particular village get their priorities ---

MR. RHODE: They would approach that existing State agency to put a loan together and offer it to the Permanent

Fund.

MR. LOVE: In response to Mr. Barnes' comment that he thinks the citizens board would be able to perform the function of giving the input of what a particular community wants out of it since we've got these guys elected from the Senatorial Districts, I think the problem with that the citizens advisory board is given two jobs. One is to decide their priorities as to whether or not the Fund should -- let's use these existing things, trust, development and community development. Now, let's say you're a community and the guy that got elected ran on a real strong platform of development and that was it. He was opposed, let's say, to putting a lot of dough into community development or the trust account. Let's say he was successful to a degree that they're still going to put some money into development, that may not be the person who is best equipped to represent the wishes of that particular community. He may have done a pretty good job in saying this is our priority in terms of how we want the Permanent Fund invested, but he may not be the most sensitive person as far as that community is concerned in terms of community development. I'm not thrilled with Price Waterhouse's idea of a 32-member citizen committee meeting once a year. I would like written down on the board, regional advisory committees to the central management of the Permanent Fund about the types of community development they want as part of the structure.

MR. LOVE: Also, I think we should also ---

MR. WOHLSFORTH: Jamie wait a minute. Others may have some thoughts now and the time is short. You have really had ample time. Does anyone have any other comments on this subject before we turn the board over?

MS. FLEISCHER: Can we add veto to that because of what Mr. Barnes said, and I do think the people should have the right to veto a particular project if it isn't right for that particular region.

MR. EDENSO: Should we have a general election to get some kind of development done?

MS. FLEISCHER: I don't think we should ram something through because it is good for the State if it is not good for the region.

MR. GALLAGHER: A community development loan is a pretty small loan and it only affects --- If you are talking about a bigger development project, then it would fall over here. But if you are talking about a housing loan in Bethel, I don't want them to vote on every housing loan. The very fact that you do a development loan, you've got to go out and get input from the community. That is the only way you can do it. If you're going to have a utility system, the city council has got to decide they want a utility loan.

MS. FLEISCHER: In other words, you are saying it is already ---

MR. GALLAGHER: It is implicit when you talk about community development.

MR. EDENSO: Why don't we add to a 5th one under community development loan, why don't we say city councils and managers and boroughs and combined assemblies. Those are structures that we could conceivably deal with.

MR. WOHLSFORTH: I think you get to a point where you really don't like the philosophy of a development loan and you get to this point. Admit it if you don't like it.

MS FLEISCHER: If you're talking about me, I do like the idea but I want to make sure that somehow the structure is set up so people have a real say as to what happenes to them.

MR. GALLAGHER: We all agree with that.

MR. CRAWFORD: Mr. Chairman, I would like to ask Dennis a question. Do you feel that this recommendation you have come up with is applicable to the four alternatives that we've had? Is it a management system that can be accepted ---

MR. MOTLEY: If you are asking my opinion, yes.

MR. WOHLSFORTH: Maybe we can get on with that. Is that the board's decision?

MR. MOTLEY: What we tried to do in the approach was to approach it as a businessman's decision if each one of us was given a million dollars or a billion dollars or whatever and try to work out managerial decisions on how you're going to structure this thing. You can go on for an eternity talking

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about various structures. You could have them decentralized where you would have everybody in the whole State of Alaska working on this thing, the bureaurocacy involved would be so great you'd never get anything done. Starting off here at the top, using the Department of Revenue for openers. Commissioner of Revenue. Over here in this block will be the Deputy Commissioner and we have Deputy Commissioners of the Treasury. I'm taking a line off of that because of the fact the Department of Revenue has already got short term vehicles, people working down there in governmental investments in Treasuries and CD's or deposits in the bank, we thought that working off of this particular Department of Revenue which is in charge of handling money for the State of Alaska. Over here a totally separate group of people, i.e., a president -- or start from the top, Chairman of the Board, president, vice president and so on. The same structure as the banks. When a bank such as Bob Barnes, or the NB of A or the First National -- have a working staff and the Chairman of the Board and the president and these various officers, depending on the amount of work to be developed and this will depend on whether or not we are just going to go to savings or whether we are going to development or community loan and whatnot. The larger it is the more staff you're going to have. Over here and totally separate from any other entity -- we have this box, and we have a staff of people. For example, you decide to go just into a savings account, you

might get one person, i.e., a money manager from Outside which will invest in CD's or governments or whatever we have. We think that they should have a board of directors. We selected, and this is something open for discussion, 12 people. The 12 people are broken down into groups of 3. The top group would be in power for 4 years. The next group is 3 years, 2 years and 1 year. By structuring it like this you are going to alleviate potential possibilities of turning this thing into a political football because of the fact this particular individual up here will be in office, either elected or appointed, for 4 years, Governor Hammond is going to be there for 2 years, or maybe another 6 years. But each one of these individuals will keep moving on so there will be no direct conflict by the board of directors who, in fact, will be the people -- the board of directors will be responsible to these people here. These people can hire or fire these individuals depending on the performance of what they are doing with the Fund.

We suggested that these 12 people be selected, 6 from the administrative group, the governor's group, and 6 from the legislative group. Those particular individuals would be chosen such as the way the commission board or the board of realtors is chosen. Divide the State into five different sections and a particular individual comes out of each one of those areas to make up the board of realtors, to make all the decisions in the real estate area. Now, this particular group

up here is expanded to whatever the demands are going to be. If you decide every step is going to go into development, general development of the State of Alaska, needless to say this particular board is going to have to be much more large in size. If you elect just to put it in savings, probably one small business manager and one-quarter of one percent in the Lower 48 to invest in various savings accounts, Treasuries, or whatever. Just an individual, maybe out of the Revenue Department. But this way, you have totally alleviated the thing from the political atmosphere. This particular board could treat just as a business assignment. Take the money and make it go.

Now, as far as the structure of these people are concerned, this has to go on to a later date because the people of the State of Alaska or the legislature will have to decide what kind of vehicle they are going to want. If they want a combination of savings account, general development or community. That could be called maybe Alaska General Development Corporation or it could be called something else that the Price Waterhouse people and the White Weld people come up with. That is something the legislature itself is going to have to decide and that will be the proportionate or amount of money for each area that you are going to want to go into. At least by keeping this concept, working management, they can immediately take over the responsibility.

MR. BARNES: I think you need a tie-breaker on your

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board, either 11 or 13.

MR. MOTLEY: 13 we'll say, or some odd number. The question was asked, how is the policy decision made up here. The policy decision would come -- let's assume that after this Committee and the legislature have come to an agreement, 1/3 into development, 1/3 into local community areas and 1/3 into savings. This policy would be handed to this group of people by the legislature, these people would be responsible -- if they didn't they'd get fired and put in new people. By putting in the kind of staff, you can go out and hire the best in the United States to be the president of the board and so on, so you have the best banking expertise.

These particular individuals will be six from the legislature, six from the administrative department.

MR. FREER: The six from the administrative side, do you contemplate they would be existing employees of the State or would they be from the public sector.

MR. MOTLEY: From the public sector.

MR. FREER: Would they be fulltime paid employees?

MR. MOTLEY: Our suggestion was that the governor would select six people, again using the real estate's board concept, divided into 5 different sections. Try to pick people out of each one of the sections so each one of the sections in the State of Alaska has representation. The same with the legislative people over here, they would choose their people

from the various areas of Alaska so that the whole State is represented to help make these decisions.

MR. FREER: Are they voluntary, or are they paid?

MR. MOTLEY: We believe that they should be on a voluntary basis. These people up here, this board of directors, working board of directors are going to be paid very handsome amounts of money. These people over here will be supervising to make sure that your policies, whatever the legislature chooses, is carried out. And if it isn't carried out, you remove the board of directors and put in a new board of directors.

MR. WOHLSFORTH: Mr. Gallagher has to leave but we might as well continued with any questions on this.

MR. BARNES: It is very similar to the Price Waterhouse model. You are using the legislature as the citizens board. And you are setting up an operating board and it sets up management which is pretty much what Price Waterhouse has said. Doesn't it strike you that it is fairly similar?

MR. MOTLEY: We felt that it was a little bit more workable from the standpoint that it is more clear cut and less bureaurocacy involved so far as getting those decisions out. And it also gives more attention to these particular individuals who are up here. If they don't carry out these policies that have been selected, these 12 people are going to elect to fire them. It's just like over at your shop, if you don't carry out

the policies of your board, the decision of the board, you aren't going to be there any more.

MR. WOHLSFORTH: Any other discussion before Sterling has to take off?

MR. LOVE: Two comments. First I am wondering when we're going to address different ways of things to do with the earnings. As we have community development, development and trust funds, I think we ought to have -- that the goal is to redistribute the wealth.

MR. GALLAGHER: If your goal is to redistribute the wealth, how ---

MR. LOVE: I would like us to take a look at possible ways of distributing it. There will be prosperity in the State brought about by the revenues, who is going to get the most of it? Who is going to become wealthy and who is going to remain poor? I'm not saying we should discuss it right now, but I think those are some things we are going to have to discuss.

MR. GALLAGHER: The third week in December is the next meeting.

MR. MOTLEY: Is there a possibility to move it forward just one week?

MR. EDENSO: Jim Rhodes and I have talked at some length about the next meeting. Due to travel schedules and time of the day, time of the year, holidays and everything, it looks as though the third week of December is probably the best.

And probably if we could have another 2-day meeting. I think we pretty well filled up two days this time, so December 17 and 18th. But that is only open to the Committee. If the Committee decides that is a bad time, then let's hear some other suggestions.

MR. MOTLEY: Would it conflict very much with the Department of Revenue if we had it sometime between the 6th and the 10th, which is the second week in December?

MR. LOVE: I would like to see us meeting again in the month of November, even if we don't have a -- because I think this has been very fruitful.

MR. [illegible]: If we could have some work committees in November and come back and look at organization and structure.

MR. LOVE: This has been very helpful to me in getting a clearer picture. I would like to the committee as a whole meet sometime in November and pursue the discussion we started today. Maybe just for a day.

MR. WOHLSFORTH: I wonder if it came to a vote how we would feel about some subcommittee work. I think you resisted it very strongly at the last meeting.

MS. FLEISCHER: No, we didn't, we asked for it.

MR. EDENSO: If we are going to hold a meeting that soon, I would like some ideas, or at least a better idea of what we are going to attack or address at that meeting.

MR. LOVE: I would like us to talk about the two things I mentioned previously. Distribution of earnings from the Fund and the effect of the investment policies on either concentration of wealth --- Secondly, I think we should have some additional presentations, if we could, by the consultants giving us a background on present State loan programs and maybe something relative to the activities of the Native Corporations.

MR. RHODE: I think to take each one of these areas we have discussed today, the three different separate goals and start looking at how an organization under that would be structured.

MR. : You might break down into subcomittees on the basis of the three sets of structures, and in each case focusing on what kind of governing board. What any of them be elected or not. Would you have professional managers that are appointed by an executive officer.

MR. WOHLSFORTH: The idea of subcommittees makes worlds of sense. These are expensive meetings when you consider the number of people who are being brought in from throughout the State.

MR. LOVE: What kind of subcommittees do you want?

MR. WOHLSFORTH: I think Jim had a suggestion on that.

MR. RHODE: According to the three things.

MR. LOVE: I don't think one on the savings account.

MR. RHODE: Probably not, but on the other two.

MR. LOVE: Community development and development.

MR. RHODE: I think that allows people who have strong ideas in one area or the other to concentrate on them.

MR. LOVE: Just work sessions and whoever shows up becomes the subcommittee.

MR. RHODE: Have a work session and then at the next formal meeting in December.

MR. LOVE: Let's have a couple of work sessions on those two subcategories that you mentioned sometime in November, and just those who are interested in those particular areas make up the subcommittees

MS. FLEISCHER: Could you ask the consultants to come up with some ideas on the structure based on these alternatives.

MR. RHODE: You have the structure in front of you. I think it is a relatively simple one. In my judgment, every issue that you have to face is laid out in the paper by Price Waterhouse or White Weld.

MS. FLEISCHER: I don't think it is very workable.

MR. : One is simple and one is complex. If the complex one or the goals demand complexity, then it is variations on a theme that Price Waterhouse has suggested. The questions are, should the citizens board be elected or appointed, should it be -- should the citizens and the governors board be merged into a single board. Should the governor be given guidelines as to how he designates his people. Then the next

level is operation as opposed to management and a control.

MS. FLEISCHER: I guess what I wanted to know is whether we could have some help on the implications of the variations on the theme.

MR. CRAWFORD: I think it is going to be very difficult for us to come up with any kind of concensus on a structural entity until we get the answers from the AG so far as the constitutional questions.

MR. WOHLSFORTH: It might be helpful if we do have an interim meeting and the young AG's assigned to the problem could advise us at least -- give some preliminary views and that would lead us a little bit farther down the line. I doubt very much if we could get a definitive yes, no answer very quickly,if at all. On the 17th and 18th, is that agreeable for the next full board meeting.

MR. EDENSO: There is some difficulty with that whole week.

MR. MOTLEY: How about the 3d and the 4th of December.

MR. WOHLSFORTH: Will somebody move that? If no objection, so ordered.

MR. EDENSO: A subcommittee meeting on the 19th and 20th has been suggested.

MR. RHODE: Does the Committee available at this work session or not?_

MR. WOHLSFORTH: 19th and 20th for a workshop, December

3 and 4th for the regular meeting. May I have a motion to adjourn?

MS. FLEISCHER: So moved.

(MEETING ADJOURNED AT 1:50 P.M. NOVEMBER 6)