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STATE INVESTMENT ADVISORY COMMITTEE

MEETING

October 13, 1976

Anchorage, Alaska

Reported By
TAKU REPORTERS

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1 STATE INVESTMENT ADVISORY COMMITTEE

2 October 13, 1976

3 Anchorage, Alaska

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5 Chairman Eric Wohlforth called the meeting to order
6 at approximately 9:45 a.m. on Wednesday, October 13, 1976,
7 in the Conference Room, Department of Revenue, 509 West
8 Third, Anchorage, Alaska.

9 Members present were:

10 Dr. Logsdon, Associate Director, Agricultural Experi-
11 ment Station, University of Alaska, Palmer.
12 Mr. Eric Wohlforth, Attorney at Law, Anchorage
13 Robert Barnes, President, Alaska State Bank, Anchorage
14 Mr. Dennis Waldock, Foster & Marshall, Anchorage
15 Mr. Martin Pihl, Vice President and Comptroller,
16 Ketchikan Pulp Company, Ketchikan
17 Mr. Robert Thorstensen, Petersburg Fisheries, Inc.,
18 Petersburg
19 Jim Edenso, Deputy Commissioner, Department of Revenue
20 Mr. Jamie Love, Alaska Public Interest Research
21 Group, Anchorage
22 Mrs. Lanie Fleischer, Anchorage
23 Representative Hugh Malone, Kenai
24 Representative Richard Urion, Anchorage
25 Representative Clark Gruening, Anchorage
Langhorne Motley, Commissioner, Department of Commerce
R. LeResche, Office of Governor, Juneau

Absent Members:

Mr. Emil Notti, President, Alaska Native Foundation,
Anchorage
Mr. Robert McFarland, First Federal Savings & Loan,
Anchorage
Senator John Burtrovich, Fairbanks
Senator Jalmar Kerttula, Palmer
Senator John Sacket, Fairbanks
Andrew S. Warwick

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Others present were:

- Peter B. McDowell, Price Waterhouse
- Paul Dodson, Alaska Dept. of Revenue
- Vincent Wright, Alaska Dept. of Revenue
- Carol A. Greil, Area Realtors, Inc.
- Dona K. Lehr, Policy Development & Planning
- Kenneth Jensen, Arthur D. Little, Inc., San Francisco
- Ken Butler, White, Weld & Co., San Francisco
- Gary Larson, Price Waterhouse & Co.
- L. Patrick Oden, White, Weld & Co.
- Charles J. Fuhrmann, White, Weld & Co.
- Jack O'Quinn, Alaska Oil & Gas Assn.
- William Batko, Institute for Local Self-Reliance
- Lisa Jorgenson, AKPIRG
- Dan Regis, Price Waterhouse & Co.
- Bradford Tuck, Fed/State Land Use Planning Commission
- Susan Andrews, Anchorage Times
- Paul Engelman, Fed/State Land Use Planning Commission
- Thomas R. Packer, Alaska National Bank
- Dave Rose, Bond Bank Authority
- Jim Weber, BLM - State Office
- Jim Rhode, Staff, House Finance Comm.
- Frank Reed, Jr., Dean Witter & Co.

Advisee:

Sterling Gallagher, Commissioner, Department of Revenue

1 MR. WOHLFORTH: We're calling the meeting to order.
2 My name is Eric Wohlforth, I'm pinch-hitting for Bob McFarland,
3 the Chairman, who is embarking on a round-the-world cruise
4 for some seven weeks and left yesterday. The first item of
5 business on the agenda is opening comments by Commissioner
6 Gallagher.

7 There is a sheet being passed around the room for
8 convenience. If you can simply sign your name when it reaches
9 you, or print your name, your firm, unless you're a member
10 of the Committee, and your address, it will be helpful.

11 So we'll now hear Commissioner Gallagher's opening
12 comments.

13 MR. GALLAGHER: I would like to welcome you all to the
14 second meeting of the State Investment Advisory Committee con-
15 cerning the establishment of the proposed Permanent Fund.
16 The last meeting served to introduce the new members of the
17 Committee and to initiate the process of establishing the
18 Permanent Fund. This meeting will allow the Committee the
19 opportunity to begin evaluating the work currently being under-
20 taken by the Consultants for the Permanent Fund.

21 Bob Richards will further describe the State's economy
22 by providing a sectional analysis of each segment. His input
23 will allow the Committee to begin focusing on the potential
24 investment opportunities available in Alaska. Information
25 of this nature will be useful for considering investment

1 policy.

2 Price Waterhouse will present their report on the
3 organizational structure, management and control of existing
4 funds which currently undertake the administration, management,
5 and investment of large development projects. Their report
6 compares the characteristics of funds which are similar in
7 nature to the proposed Permanent Fund, e.g., the limitation
8 which permits only income earning investments.

9 White, Weld and Company will present their report on
10 existing permanent funds. Characteristics of these funds
11 will be reviewed and outlined for the Committee.

12 The Governor has asked the State Investment Advisory
13 Committee to actively pursue the establishment of the Perma-
14 nent Fund. This Committee was expanded to include a broader
15 base of Alaskans to provide a greater breadth of ideas and
16 input for establishing the Permanent Fund.

17 There has been some concern expressed in the news
18 media that the State Investment Advisory Committee has become
19 a "powerful board." This is a basic misunderstanding of the
20 State Investment Advisory Committee. The State Investment
21 Advisory Committee is mandated by statute to advise the Com-
22 missioner of Revenue on investment policy for the State's
23 funds. The use of the State Investment Advisory Committee
24 for the Permanent Fund is an exception and its expansion is
25 intended to be temporary. Upon the event that the Permanent

1 Fund is established, it is anticipated that the State Invest-
2 ment Advisory Committee will return to its previous status.

3 There has been much concern expressed concerning the
4 goals of the Permanent Fund. Let me share with you at this
5 time my view on the potential goals of the Permanent Fund.
6 Briefly, I see three major goals of the Permanent Fund.

7 The Permanent Fund could have as one of its goals the
8 strengthening of the State's economic base. This could be
9 accomplished by adopting policies for the investments which
10 tend to stabilize the economy, a flattening out of the so-
11 called peaks and troughs in the economy. Investments into
12 renewable resources using non-renewable resource funds will
13 help future economic conditions. Policies which tend to
14 reduce the seasonality of employment would provide greater
15 employment opportunities for more Alaskans. The benefits of
16 the Permanent Fund should reach a broad population base of
17 the State.

18 A second goal could be to provide assistance in the area
19 of community development. This idea falls within the broad
20 population based concept. Assistance in communication develop-
21 ment, housing assistance and other socially related programs
22 could be the goals for the permanent fund.

23 Finally, a third goal could be to support the "savings
24 account" concept. This would affect the economic growth of
25 the State and allow for greater selectivity and participation

1 in future development. Additional benefits could be derived
2 from direct earnings received on the funds. Finally, this
3 could provide a "cookie jar" for the occasional rainy day.

4 Many people have expressed concern for safeguarding
5 the funds. There are many ways of developing safeguards, and
6 some of these have been traditionally used by other organi-
7 zations with similar responsibilities. Safeguards are generally
8 provided procedurally through the management and control of the
9 organization.

10 Management provides safeguards by building checks and
11 balances into the decision-making process, e.g., a loan com-
12 mittee in a bank; limited lending authority; banking and
13 cash handling procedures, etc. A further control is the use
14 of generally accepted accounting reporting and auditing pro-
15 cedures. Annual audits are a very effective check on manage-
16 ment activities which enhance greater control procedures.
17 Further, public reporting requirements on a regular basis
18 greatly inhibit the misuse of funds.

19 A brief review of our activity will establish that
20 there is a major effort by the State to establish the Per-
21 manent Fund: the cooperation between the administration and
22 the legislature in establishing the Permanent Fund; the use
23 and expansion of the State Investment Advisory Committee as a
24 human resource pool to develop the Permanent Fund; the hiring
25 of consultants to provide research and data relevant to the

1 development of the Permanent Fund; and the use of the public
2 forum, the Alaska Growth Policy Board, to carry the dialogue
3 of the Permanent Fund to the general public.

4 MR. WOHLFORTH: Thank you, Commissioner. Before we
5 get to the next item, I think Mr. Edenso wants to make a few
6 remarks to the members of the Committee about the materials
7 which are here today.

8 MR. EDENSO: Before we start the meeting formally
9 beyond this point, I'd like to find out if the members of the
10 Committee, all of you have received copies of the Price
11 Waterhouse report and the White, Weld report as well as a
12 copy of the agenda.

13 MR. LOVE: I just got mine this morning and I didn't
14 have a chance to really review it.

15 MR. EDENSO: The reason we're concerned, I'd like to
16 point out that Alaska Airlines has posed some problems for
17 delivering the reports and delivering the mail through South-
18 eastern and through Anchorage actually. The White, Weld
19 report took six days to get here, and that was by special
20 messenger. So we did have some difficulties in distributing
21 and obtaining the report. However, if you are missing the
22 agenda and a copy of the reports, I do have a couple extra
23 reports with me and if I run out I'd be happy to provide
24 those to you at a later point.

25 MR. WOHLFORTH: Thank you. We will appropriately now

1 formally convene the meeting of the State Investment Advisory
2 Committee, and the Chair does note the presence of a quorum
3 (the Acting Chair).

4 The item of business next before you is adoption of
5 the minutes of the August 26 meeting which have been in your
6 hands for some time, and I'll entertain a motion for their
7 adoption.

8 MR. LOGSDON: I so move.

9 MR. WALDOCK: I'll second that.

10 MR. WOHLFORTH: Is there any discussion? If not, all
11 those in favor of adoption signify by saying "aye."
12 Contrary? They are adopted.

13 The next item of business is slightly out of order
14 on the agenda, but I've been advised it would be convenient
15 to turn to Mr. Vince Wright, who I believe is Director of
16 Research for the Department of Revenue, to give an update on
17 revenue projections -- if he's ready to go.

18 MR. WRIGHT: Yes. Each quarter the Department of
19 Revenue publishes what we call a Revenue Journal. In that
20 Journal we feature what we consider to be the results of
21 vital research efforts. This particular Journal is devoted
22 to Permanent Funds. Now, in presenting this thing we are
23 not advocating any ideas whatsoever. We're simply presenting
24 a series of thoughts, concepts and ideas that council members,
25 administration and the legislature have developed over a

1 period of time in relation to the Permanent Fund concept. .
2 The idea is just to get thoughts out to the voters, such
3 that he or she can comment on them, scrutinize them, perhaps
4 develop them a little further.

5 The numbers on the back of the Journal here are an
6 update of the charts that I presented last time. Now, in
7 these projections what we have done is listed those items
8 that Joint Resolution No. 39 has specified as being quali-
9 fiable for the Permanent Fund monies. Right now the amend-
10 ment reads at least twenty-five percent, and I stress that --
11 at least twenty-five percent of State oil royalties, State
12 gas royalties, Federal royalties, mineral lease rentals and
13 bonus sales will be set aside for Permanent Fund purposes.

14 Now, on page nine we have listed these items in
15 numerical amounts that are attributable to each one of these
16 categories by year commencing in FY 77 and going out through
17 fiscal year '85.

18 On the second page over, immediately on the back, page
19 ten, which is titled "Permanent Fund Analysis at 25% Contri-
20 bution Rate" we have calculated what the actual contribution
21 rate would be on a per year basis in the third column there.
22 The last column, we have simply accumulated those figures,
23 so that you see by fiscal year '85, based on 25% contribution
24 rate you're now calculating to roughly 1.8 Million Dollars
25 with the accumulated permanent fund.

1 Now, in developing these projections there are many
2 assumptions that go into them such as pricing of oil, thrupt
3 assumptions, tariff rates, etc., and due to the changing
4 conditions out there in the real world we constantly have
5 to update these figures. I would like to, in conception
6 terms, indicate how we derived wellhead value. I don't want
7 to get into the numbers. I think the numbers are going to
8 be constantly changing. For those of you who are not familiar
9 with wellhead value and its importance, I would like to go
10 into it.

11 It's on the basis of wellhead value that we determine
12 our royalties; it's 12-1/2 percent. You start out first of
13 all with what we call refinery products. In this case we're
14 assuming what we call OPEC prices, world-wide prices. We're
15 adopting Saudi, Arabian crude prices, and from that we sub-
16 tract what we call a series of tariff rates. There are
17 various tariffs. For example, you have the tax tariff, which
18 represents the line itself, you have the tanker tariffs.
19 The tanker tariffs, in this case one set coincides with
20 shipment from Valdez to Long Beach. The third set of tariffs
21 in this particular instance, for a six-month period we have
22 assumed to be connected with the Panama Canal route. We're
23 assuming that for a six-month period we're going to ship oil
24 through the Panama Canal.

25 The fourth set of tariffs we've identified with what

1 we call the SOHIO line project. In other words, assuming
2 that everything is approved, there will be a line running from
3 Long Beach to Midland, Texas. Now, what that line consists
4 of is partially an El Paso gas line which El Paso has agreed
5 to convert to an oil line should the FPC approve it, and it
6 also consists of two hundred miles of new line that have to be
7 built across Southern California.

8 Now, all those items in the tariffs, we crank those
9 out and you've got refinery prices and we derive what we
10 call wellhead value. From that wellhead value you then take
11 your royalties, which amount to 12-1/2 percent.

12 If you have questions in regard to anything in the
13 Journal at this time around you can call us down there at
14 the Department of Revenue. It might take some time to digest
15 what is in the Journal today. Are there any questions right
16 now?

17 MR. MOTLEY: What was the allocation for going
18 around the Panama Canal, how much did that add to the bill?
19 I didn't see that.

20 MR. GALLAGHER: It's Seventy-Five Cents, Tony, to
21 Long Beach, and it's probably about a Dollar, another Dollar
22 to the East Coast, about a Dollar Sixty, Dollar Seventy-Five.
23 Other tariff is Two Dollars and Twenty, so that's about
24 Forty-Five, Fifty Cents.

25 MR. MOTLEY: Just for the Panama Canal?

1 MR. LAGHER: It adds about Forty-Five or Fifty
2 Cents by taking it through the Panama Canal.

3 MR. MOTLEY: Past Long Beach?

4 MR. GALLAGHER: Past Long Beach and going by water.

5 MR. REED: So you end up with, you're saying, about
6 a Dollar Fifteen to a Dollar Twenty by the time you get to the
7 East Coast; is that it?

8 MR. GALLAGHER: No, I'm saying a Dollar Sixty to
9 Two Twenty.

10 MR. REED: I thought it was Seventy-Five Cents to
11 Long Beach.

12 MR. GALLAGHER: That's right, then there's another
13 tariff, an additional tariff, if you're taking the surplus
14 oil to ---

15 MR. MOTLEY: In other words, let's say Fifty Cents
16 roughly through the Panama Canal.

17 MR. GALLAGHER: Added to that. I said it totals a
18 Dollar Seventy-Five for surplus oil going to Pad 3. It would
19 be Seventy-Five Cents to Long Beach, and if you go by sea
20 to Pad 3, Two Dollars and Twenty Cents.

21 MR. REED: What's Pad 3?

22 MR. WRIGHT: Petroleum District Number 3, which is
23 Midland, Texas.

24 MR. MOTLEY: It's the Gulf area.

25 MR. GALLAGHER: Most of the Saudi crude is based on

1 shore. It's the closest market, Two Twenty, where you can
2 displace Saudi crude.

3 MR. LOGSDON: I'd like to commend the Department of
4 Revenue for the picture on the front of your Journal, of the
5 oat and pea silage in the shadow of Byers Peak. I think
6 that's very nice, especially with "Permanent Fund" written
7 across the front of it.

8 MR. WRIGHT: We had Senator Kerttula in mind here.

9 MR. WOHLFORTH: Thank you. If you would identify
10 yourself before you speak, it would be helpful to the secretary.
11 There is a verbatim transcript of these minutes taken.
12 It was Dr. Logsdon that just spoke and made the comments about
13 the picture on the Revenue Journal.

14 MR. WRIGHT: Are there any other questions about the
15 Journal?

16 MR. LOVE: What would happen -- I mean, have you got
17 really any projections on this, what would happen if the tax
18 rate was changed drastically? I guess there's an area that
19 taxes will go into this, or something, the net effect.

20 MR. WRIGHT: That is correct, taxes do not go into
21 this, only percentages of royalties.

22 MR. LOVE: Would that affect the royalties or anything?

23 MR. WRIGHT: Let's put it this way, depending on which
24 route the oil goes, the tariff rates can be affected. There-
25 fore, wellhead value can be affected, therefore, royalties.

1 MR. LOVE: I'm talking just about the question of
2 Alaska State taxes.

3 MR. WRIGHT: The tax doesn't.

4 MR. WALDOCK: Dennis Waldock. Sterling, have you taken
5 any consideration into shipping any of this excess oil, rather
6 than through the Panama Canal, until this new line is built
7 over to Midland, Texas -- have you taken into consideration
8 of shipping it over to Japan and what the savings would be
9 by exchanging of shipping oil to Japan by going ahead and
10 exchanging oil with the Middle East coming to the East Coast?

11 MR. GALLAGHER: We have done projections on that.
12 There is a considerable savings to the State. The advantage
13 to the United States is very minimal because, of course, you
14 just displace the Saudi crude. You know, there may be a great
15 savings to the United States, but there is no very large net
16 savings to the U. S. because the oil is shipped. Just
17 different people get it, the income. In one case shippers
18 seem to get the money, or pipeline companies, and in the
19 other case it would go to the owners of the property. We,
20 being an owner, would receive quite an income differential,
21 but the nation as a whole would not get that much difference.

22 MR. WALDOCK: Do you know any statistics on how much
23 it would save us, the Alaskan people?

24 MR. GALLAGHER: The tariff roster in our office, which
25 is the Saudi, Arabian report for oil to Japan versus this

1 world tanker rate from Valdez to Yokohama, there's about a
2 Nine Cent differential per barrel. I'm saying the advantage
3 to the Japanese is somewhere around Nine Cents. I'm saying
4 that the advantage to the Japanese of trade is about Nine
5 Cents a barrel, us versus Saudi, Arabia.

6 MR. LOVE: These are preliminary figures, aren't they?

7 MR. GALLAGHER: You know, the whole tariff to Long
8 Beach is only Seventy-Five Cents under the American flag. If
9 you're talking other flags, you're talking about lower rates,
10 but Japan isn't that far away.

11 UNIDENTIFIED: When you're talking about Seventy-Five
12 Cents, that's the tanker tariff, that's not including the
13 TAPS tariff?

14 MR. GALLAGHER: That is correct.

15 UNIDENTIFIED: What is an estimate for the TAPS tariff?

16 MR. GALLAGHER: TAPS tariff is Five Twenty-Five down
17 to Three Fifty, depending on the thruput -- in the Five
18 Twenty-Five range.

19 MR. WOHLFORTH: If there are no further questions,
20 questions may occur to members or others during the course
21 of the meeting, there will be time later as you've had a
22 chance to further digest the report and some of the statements
23 from Commissioner Gallagher and Mr. Wright. If there are
24 no further specific questions, or if neither of them have
25 anything further to say at this point we turn to Mr. Bob

1 Richards, who will give us a status report on the Alaska
2 economy. Mr. Bob Richards, you all know, is Senior Officer,
3 Alaska Pacific Bank, as well as our leading economist.

4 By the way, if the sheet with names on it is still
5 circulating, keep it circulating so we will know who all is
6 here.

7 MR. RICHARDS: Thank you, Mr. Chairman, I appreciate
8 the invitation to be here and, out of a sense of awareness
9 and of a sensitivity to the Alaska Transportation System at
10 the present time, my outline was hand carried this morning.

11 The discussion will take three parts -- well, four
12 parts, as I understood kind of our directive to you. One,
13 a discussion of kind of what the Alaska economy looks like to-
14 day, particularly as related to some sort of a Permanent Fund
15 activity, what the Alaska economy looks like today. The second
16 part will include a discussion of where the Alaska economy
17 seems to be headed. The third part will include a brief
18 examination of what sort of policy implications seem to
19 naturally flow from the first two, and the fourth is simply
20 a little bit of regional observations, we might say.

21 I think I inadvertently sent around my copy, and I apologize
22 that I didn't prepare a sufficient number of copies. I'll do
23 that next time. If anybody would like any further copies
24 I'd be happy to supply them if you'll just give me your
25 business card or address.

1 There's really not too many surprises at all in this
2 first look-see at the structure of the Alaska economy, but
3 perhaps it does serve a purpose to verify what we kind of
4 felt intuitively anyway. The first couple of charts are to
5 take a look at the cyclical behavior of Alaska's economy,
6 and particularly the first one, civilian employment. The
7 first chart is just charting historical development of
8 employment. The second one is charting the historical develop-
9 ment of population.

10 I think that subsequent to the bust following the
11 gold rush Alaska has lived with an image which is really not
12 an accurate description of its economic history. Alaska's
13 economic history has not been plagued with booms and busts,
14 at least in the sense what the term "bust" implies to me.
15 Certainly following the gold rush there was a bust of mammoth
16 proportions, but other than that Alaska has not had a series
17 of booms and busts. Alaska has had cyclical fluctuations
18 and from time to time rather disruptive cyclical fluctuations.
19 But I would submit that most states in the nation, indeed
20 the nation, has had cyclical fluctuations. We'll come back
21 to this.

22 But at any rate, I don't see anything on the charts
23 on Tables 3 and 4 that describe to me, at least over the
24 period for which they were charted, any sort of boom and
25 bust behavior. We'll come back to the significance of this

1 later on. All we're really doing right now is going through
2 some descriptive material.

3 Turning to the chart on page 5, what we did here was
4 to take the average annual employment in the State of Alaska,
5 the average level of employment at any given day, the average
6 level of employment in the State of Alaska, and that we just
7 arbitrarily stated was 100%. In other words, this chart here
8 is an index. Then we simply took every other month as a per-
9 centage of the average. It's not indicated on this chart.
10 It should have been, but it's not. This is based on 1972 and
11 1973 data purposely to omit the distortion of the pipeline
12 activity. Granted, any future years will never again resemble
13 what '72 and '73 were, but I have a strong intuitive feeling
14 that the seasonality of future years will probably resemble
15 '72 and '73 more than they're going to resemble '74 and '75.
16 I thought that was more valid.

17 Frankly, this chart was surprising to me, because
18 although I understood that we have a seasonal economy, I'll
19 have to confess to you this is rather dramatic in my opinion,
20 this degree of seasonality. As you see, we peak in August and
21 we trough in January. Okay.

22 The other tables, Table 6, on pages 6, 7 and 8 and 9,
23 take a look at the diversification of Alaska's economy, and
24 the diversification in two dimensions. One, the industry
25 diversification, and the other is the geographic diversifica-
tion.

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1 Again, there is not anything surprising on here at all.
2 But I think there are some highlights that should be noted.
3 As you can see, we have a pretty small basic sector relative
4 to the United States, the U. S. average of these things on
5 the right. I'm looking on page 6 now. I put the U. S. average
6 there just to put Alaska's mix more in perspective and make
7 it more meaningful to you. As we all know, we have a large
8 government sector. By the way, this excludes military.

9 MR. MOTLEY: I'm looking across the chart, government
10 and then it's manufacturing; were those words swapped there?

11 MR. RICHARDS: No, that's because each is listed in
12 descending order of magnitude.

13 MR. RHODE: Since this is 1975, doesn't it tend to
14 over-state construction relative to government?

15 MR. RICHARDS: Yes, it tends to over-state construc-
16 tion.

17 MR. RHODE: Usually for government it's crowding 40.

18 MR. RICHARDS: Jim, it's at 40 because that's what
19 occurs when you add in military.

20 MR. RHODE: Oh, I see.

21 MR. RICHARDS: This excludes military, and the reason
22 I excluded military is the U. S. data that I had. I could
23 find no U. S. data that included military at all.

24 MR. RHODE: This is also '75 data.

25 MR. RICHARDS: That's right.

1 MR. GALLAGHER: And '72 data would show government,
2 including military, right up on 50 percent.

3 MR. RICHARDS: That's right. It's been decreasing
4 though.

5 MR. EDENSO: What are the industries most affected
6 by seasonality?

7 MR. RICHARDS: Well, that's interesting that you
8 raised that question. You can turn to page eleven and then
9 we'll come back. Excuse me, this was getting at the labor
10 intensity rather than the seasonality. These are our major --
11 our major sectors are listed here and, of course, the industries
12 most affected by seasonality are tourism and fishing, secondly
13 would be forest products and construction, and third would be
14 trade and services only because they play off the first four
15 and, therefore, would be affected somewhat by it.

16 MR. GRUENING: What does the hundred percent line
17 on seasonality represent, one hundred percent of what?

18 MR. RICHARDS: Well, that's a term, when you refer
19 to this as an index. Another word for that line is the
20 average.

21 MR. GRUENING: How is it derived? What does that
22 represent?

23 MR. RICHARDS: I took the average employment for each
24 month of the year. The employment in January was this, in
25 February it was this, in March it was this, in April it was

1 this. I added them all up, divided by twelve, and that's
2 the average month. In other words, it just so happens that
3 March, as you can see here, March and November turn out to be
4 average months of employment.

5 MR. GRUENING: What is the average month of employment?
6 How many people unemployed and how many people employed of
7 the total work force?

8 MR. RICHARDS: I don't have the absolute numbers here
9 with me. But what this tells you is that there are fourteen
10 percent more people employed in August than there are in
11 November, and there are about twelve percent less employed
12 in January than there are in March.

13 MR. GALLAGHER: The reason that January doesn't
14 reach down there, or December doesn't meet the January dog
15 is because you're going to have a higher base, you see, by
16 January; is that not right?

17 MR. RICHARDS: No. I understand the point you made,
18 but that doesn't emerge in this graph here. If you charted
19 this, then January just happens to be a -- I mean December
20 happens to be a higher employment month.

21 MR. GALLAGHER: The line goes down?

22 MR. RICHARDS: Pardon me?

23 MR. GALLAGHER: The line goes straight down?

24 MR. RICHARDS: Yes, it would. You're still having
25 the outflow, you're still having the holiday season impact.

1 MR. GALLAGHER: Are you sure it isn't a statistical
2 aberration and that if you've got a higher base ---

3 MR. RICHARDS: No, it isn't because your base is the
4 same. For every month your base is the same, and that is the
5 average month.

6 MR. GALLAGHER: That's pretty dramatic between January
7 and December.

8 MR. RICHARDS: Yes, it is. This was the most surprising
9 of all the graphs. This one was the most surprising to me.

10 MR. LOGSDON: That doesn't surprise me. After
11 Christmas everything shuts down. This has been typical in
12 Alaska, and it shuts down ---

13 MR. RICHARDS: I knew the pattern would exist, I
14 knew this pattern would exist, but the magnitude, you know!

15 MR. EDENSO: What you're saying is that there is more
16 stability and seasonality in employment in trades, services
17 and finances, government, possibly transportation, communi-
18 cations and utilities than there is in construction,
19 manufacturing and mining; in other words, your productive
20 industries plus your limited service industry of tourism
21 is largely seasonality affected.

22 MR. RICHARDS: That's right.

23 MR. EDENSO: Your mainstay for employment in the State
24 is not affected by seasonality.

25 MR. RICHARDS: Well, government is the mainstay, and

1 it is not. Keep in mind distributive is a function of, over
2 the long run. Now, certainly not in some short run cases, but
3 over the long run distributive is a function of government
4 and basic. Government and basic is the only thing that
5 causes, you know -- they result from autonomous investment
6 decisions.

7 Distributive is an induced investment decision. Some-
8 body constructs a service station on a corner up here because
9 he thinks there is going to be population, or there is, or
10 there is going to be population to support the service station.
11 Somebody invests in an oil well up here because he feels
12 there is oil in the ground. It has nothing whatsoever to do
13 with any internal characteristics of the Alaska economy.
14 Distributives are a function of what's going on in Alaska
15 economy, and government partially is, and the basic is not
16 at all, and government is partially not.

17 I sense we're not on the same wave length yet.

18 MR. EDENSO: I'm not sure I really understand what
19 your breakdown here is and basic and distributive; I'm not
20 sure I understand what basic is.

21 MR. RICHARDS: Basic is mining, manufacturing, now
22 in Alaska tourism, forest products, fishing, petroleum,
23 hardrock mining, and we also toss some construction -- we
24 toss construction in there. That could be argued.

25 MR. EDENSO: Those aren't really affected by

1 seasonality then.

2 MR. RICHARDS: No, we're talking about two different
3 things here, peaches and pears. Some of them are seasonal,
4 some of them are not. I'm not suggesting that all basics
5 are seasonal. Basics are basic. They're autonomously
6 induced. Distributive is internally induced. Now, to the
7 extent of whether or not some basics are seasonal and some
8 basics are non-seasonal, that's another dimension.

9 MR. EDENSO: That's what I'm trying to get at. What
10 are those basics that are in fact seasonal, and what percentage
11 or proportion of the economy, and what is the importance of
12 their role in the economy?

13 MR. RICHARDS: Well, you can see. You can see how
14 they affect the total severe unemployment on the previous
15 chart. Tourism, the most seasonal, or tourism and fishing;
16 the second ---

17 MR. EDENSO: From your previous chart I can't tell,
18 by looking at it.

19 MR. RICHARDS: Well, I'm giving you the answer.

20 MR. EDENSO: I'm looking at employment numbers. You
21 give us an average per month but you don't give us breaking
22 down employment-wise, labor intensive-wise, what each one
23 of these industries represents.

24 MR. RICHARDS: Representative in what respect, the
25 seasonality of each industry?

1 MR. GALLAGHER: I think he wants another chart like this
2 for each industry.

3 MR. RICHARDS: For each industry. Good, we'll do it.

4 MR. EDENSO: I think it's important in considering
5 what industries are seasonality, what percentage of the work
6 force they represent.

7 MR. RICHARDS: You bet it is, Jim.

8 MR. PIHL: Bob, do you have any data on resident and
9 non-resident employment, and I would judge that the peak is
10 greatly increased by non-resident employment?

11 MR. RICHARDS: Yes, we do have data on that and I
12 can develop that for you, if you'd like, as well.

13 MR. WOHLFORTH: It was Mr. Pihl that spoke, for the
14 benefit of the stenographer, and I ask you again to identify
15 yourselves before you speak. There is a lot of money going
16 into a written transcript of this meeting, and it just doesn't
17 make sense to have all the names spelled wrong or missed
18 altogether. Mr. Love.

19 MR. LOVE: Mr. Richards, as I go through these charts
20 I notice some of them have dates and some of them don't have
21 dates insofar as the source. Are we to assume that the data
22 is for 1975 unless otherwise indicated?

23 MR. RICHARDS: No, I'll tell you. I fully intended
24 to walk through this with you.

25 MR. LOVE: I'll just hold off then.

1 MR. RICHARDS: Okay. We were on page six. When you
2 take a look at construction, again although it's officially
3 classified as a basic industry, you must recognize the
4 nature of it, and that is it's mostly internally induced as
5 well. There are some exceptions, Federal highway funds, etc.
6 But it's mostly internally induced. So, when you separate
7 out what is external and autonomous from what is internally
8 induced, you see that Alaska's economy is highly a function
9 of what is external and autonomous.

10 Also another element that comes out of this, as indi-
11 cated, the disproportionate role played by the public sector
12 in Alaska relative to the national average.

13 On page seven I give you the employment mix by
14 state, and the two largest population centers, and they follow
15 the same general pattern as the state, varying just slightly
16 and, as one would imagine, Anchorage, the commercial and
17 financial center, and the population center, has a lower
18 basic sector and a higher distributive sector, and I think
19 this is something you would find in every state in the nation.
20 I'm sure this situation exists in Seattle relative to the
21 State of Washington, Portland relative to Oregon, etc.
22 There's nothing here that is cause for any sort of undue
23 concern in that regard.

24 MR. LOVE: 1975?

25 MR. RICHARDS: Yes, this is 1975, thank you. Jamie,

1 I'm sorry, you're going to end up being right. These three
2 are 1975, seven, eight and nine, 1975.

3 The next graph, however, I think is cause for some
4 concern, and it definitely has some investment implications,
5 it seems to me, in terms of a Permanent Fund, and that is
6 the disproportionately great amount of the source of the
7 gross state product. Excuse me, this is 1973 data -- I'm
8 sorry, 1973 data. Excuse me.

9 Almost two-thirds of our gross state product comes
10 from the South Central region, and the table on page nine
11 indicates the South Central region has 54.5 percent of the
12 population, so the gross state product per capita is con-
13 siderably higher in South Central than elsewhere. Again,
14 intuitively, what this says is the non South Central is
15 poorer than South Central in terms of productive wealth
16 you might say. Southeastern also has a higher than propor-
17 tionate share of gross state product relative to population.
18 So, again, all this is verifying things we already knew
19 anyway, and that is Southeastern and South Central are
20 relatively wealthy, the rest of the state is relatively
21 less wealthy in terms of output of goods and services, in
22 the economic sense of wealth, not in the income sense.

23 However, an editorial aside, I would imagine that
24 would be true for income as well. But you just don't impute
25 something from the data here that doesn't exist.

1 As we know, Alaska is a highly labor intensive state.
2 Labor costs have been of concern to all of us. The table on
3 page ten shows per capita personal income by states for 1974.
4 As one would be willing to bet anywhere, Alaska heads the
5 list, and it so happens that Alaska is 30 percent -- it's
6 29.6 percent to be exact -- higher than the U. S. average.
7 Now, the major source, 90 percent of personal income in
8 Alaska is from wages and salaries as distinguished from other
9 sources of personal income being proprietors' income, Social
10 Security payments, retirement benefits and so forth.

11 MR. MOTLEY: What was that, 90?

12 MR. RICHARDS: Over 90 percent comes from wages and
13 salaries. So this 30 percent differential would reflect
14 somewhat the wage and salary differentials.

15 MR. GALLAGHER: Has there ever been one of these
16 charts done correlating it back to inflation or real dollars?

17 MR. RICHARDS: The change in real over time?

18 MR. GALLAGHER: No. Take inflation.

19 MR. RICHARDS: Yes.

20 MR. GALLAGHER: In this state in comparison to the
21 national economy.

22 MR. RICHARDS: Yes.

23 MR. GALLAGHER: And I would like to see this chart
24 reposed over the real, discounted, for instance.

25 MR. RICHARDS: Okay, what do you want to use as the

1 base period? This is a balance sheet, if you will, and
2 inflation is an income state. Inflation is a function that
3 occurs over time. What would you like me to use as the
4 base year? 1960 or ---

5 MR. GALLAGHER: I would like you to use -- can you
6 somehow get the cost of living index for each state and then
7 repose it on here?

8 MR. RICHARDS: Yes, I can, Sterling. But as I indicated,
9 that is a function of time. This is a function of a moment,
10 of an instant. The cost of living is a function of changes
11 over time, so you'd want to take a look at these also as
12 changes over time.

13 MR. LOVE: He's just saying that if the cost of living
14 in Alaska is 50 percent higher than the cost of living in
15 the District of Columbia it wouldn't make sense to say that,
16 you know, in real dollars our income is higher than that
17 of a person living in the District. Our standard may be, in
18 fact, lower in some instances.

19 MR. RICHARDS: So it's not inflation you want to take
20 a look at. You want to take a look at cost of living dif-
21 ferential at a moment in time.

22 MR. REED: Sterling, Frank Reed. Bob, I was wondering
23 if you have done anywhere in the study, and I don't have a
24 copy of it -- but have done a study in there of the disposable
25 income because I think that is, of course, a critical factor

1 involved which integrates in the cost of living and how much
2 of a percentage of our income we spend for housing, etc.,
3 and it would be a very interesting figure; has our disposable
4 income percentage-wise increased. That's something that
5 I've always believed to be true up here, but I've never really
6 seen it, you know, in a proven fact.

7 MR. RICHARDS: Okay. Back on the point that you
8 brought up, Commissioner Gallagher, I can give you some
9 general reflection of the situation right now, that in terms
10 of based on 1974 data the cost of living between Anchorage,
11 and Anchorage is the only place in Alaska for which the cost
12 of living is measured, the cost of living differential between
13 Anchorage and the U. S. average was 25 percent. So, dis-
14 counting this, it would bring it down to close to the U. S.
15 average.

16 MR. GALLAGHER: Right, but I think it will also show
17 us slightly ahead of the U. S. average. One was 30 percent
18 ahead and the other was only 25.

19 MR. RICHARDS: That's right, we'd be slightly ahead,
20 but pretty darn close to, and I'll do that, I'll correlate --
21 I'll adjust all of these for cost of living differentials.

22 The next chart is one we looked at a few minutes
23 ago, but this kind of arrays the sectors of our economy on
24 the basis of the extent of their labor intensity, and as you
25 can see here, we're a highly labor intensive economy.

1 MR. GALLAGHER: One of those things that shows, if you
2 want to raise that basis, take out the seasonality, you invest
3 more in government?

4 MR. MALONE: Sterling, looking at the breakdown on
5 per capita incomes across the United States and relating Alaska
6 to Washington, D.C., it looks like government might be the
7 best investment if we just made a simple assumption.

8 MR. RICHARDS: Apropos to that, I've got an article
9 in here I'm going to pass out to you people. It appears in
10 the last Business Week, October 18, 1976. Everybody in this
11 room should read this article. October 18, 1976 Business
12 Week, page 138, and it talks about the effect of an imbalance
13 between growth in the public sector and the private sector.
14 It's an absolutely fascinating article and it's the result of
15 a study by the European arm of the Hudson Institute. I'll
16 pass out copies when it's over. It's interesting nighttime
17 reading.

18 This chart on page 12 really kind of results from an
19 interest, I don't know, an avocation of mine of always taking
20 a look at conventional wisdoms that seem to exist, and one
21 interesting notion here is that in terms of although the
22 two terms, union and Alaska seem to be synonymous in some
23 circles, I think this data is kind of interesting.

24 MR. LOVE: Except we just got one union.

25 MR. RICHARDS: Notice, this is based on 1972 data,

1 which this proportion would be considerably higher today
2 because of the distortion of the pipeline.

3 MS. FLEISCHER: Why is that?

4 MR. RICHARDS: This I had to get out of the national
5 publications.

6 MS. FLEISCHER: There must be a drastic change between
7 '72 and '76.

8 MR. RICHARDS: Oh, yes, there has been. Yes.

9 MR. LOVE: On this we're about the lowest of all the
10 states that don't have right to work laws. That's interesting.

11 MR. RICHARDS: Yeah. Well, it's also a function --
12 it goes back -- it's a function of the complexion of our
13 industry mix.

14 MR. URION: Bob, this wouldn't have included state
15 employees as union members?

16 MR. RICHARDS: No, not in '72.

17 MS. FLEISCHER: So it's really not right on the chart.

18 MR. RICHARDS: I'll consider my hand slapped on that
19 one and come up with more current data. I don't like to do
20 that.

21 The last two charts reflect the disproportionate role
22 played by the petroleum industry in terms of the public
23 sector and, indeed, the eggs of the public sector, or an awful
24 lot of the eggs are in that petroleum industry basket and,
25 of course, as we all well know, this problem is going to

1 become more intense.

2 MR. GALLAGHER: This problem?

3 MR. RICHARDS: Well, the potential problem is going
4 to become more intense.

5 MR. GALLAGHER: Your data on this page doesn't cor-
6 relate with my data, and I'm the keeper of the books.

7 MR. RICHARDS: Okay, you're right. I was very, very
8 conservative, super-conservative. Even when you get super-
9 conservative you come up with rather startling conclusions.

10 MR. GALLAGHER: That's right. Every one of the
11 numbers are higher.

12 MR. RICHARDS: Yeah.

13 MR. LOVE: I'd just like to make a point on this.
14 You said it's a problem and a large percentage of our revenue
15 comes from petroleum related industries, but one of the
16 advantages of that is that you have to raise less revenue
17 through things like personal income taxes and state application
18 of sales taxes and things like this. So I think you've got
19 to look at this in terms of, you know, what you may perceive
20 as a problem because it's a centralization of our revenue
21 source in a single industry, it may be interpreted by others
22 as an overall benefit because it allows us a tax relief off
23 other groups that otherwise would be carrying the burden.

24 MR. URION: It doesn't work out that way.

25 MR. RICHARDS: I think the point you made is a valid

1 one, but nevertheless I still hold the notion that severe
2 lack of diversification in any regard is ipso facto a problem.

3 MR. LOVE: I'm accepting that.

4 MR. RICHARDS: Okay. And the final discussion is a
5 further elaboration of the role of the public sector in
6 Alaska, which in this elaboration results simply from the fact
7 of the major role that it does play in the state. It has,
8 in fact, been by far -- there's not even a close second --
9 it's been by far the major cause of population growth in the
10 State of Alaska.

11 MS. FLEISCHER: Bob, could I ask you again, you do
12 not include the military?

13 MR. RICHARDS: No, and furthermore this discussion,
14 this simply is an examination of state and local government.
15 Federal is left out of here, and military is left out.

16 MS. FLEISCHER: Oh, it doesn't include federal
17 government employees?

18 MR. RICHARDS: No.

19 MS. FLEISCHER: That must be a rather large ---

20 MR. RICHARDS: Federal is larger than state and local.

21 MS. FLEISCHER: I was going to say.

22 MR. RICHARDS: Federal is larger than state and
23 local. Federal ---

24 MR. MOTLEY: But it's been stable.

25 MR. RICHARDS: As a proportion it's been diminishing

1 over time. It's stable.

2 MS. FLEISCHER: You don't include it because it's
3 not relevant?

4 MR. RICHARDS: No, I did not include it because it's
5 not relevant. It's relevant but the area of expansion, as
6 Commissioner Motley just pointed out, it's been stable,
7 essentially stable, over the past decade.

8 MS. FLEISCHER: You're looking at growth?

9 MR. RICHARDS: Yes.

10 MR. WOHLFORTH: I think probably it would be best now,
11 just to keep in orderly discussion, if we went around the
12 table with the members and had a chance to ask questions.
13 I know this is probably the most fascinating part of the whole
14 presentation today, and we do have some time if the schedule
15 here is right.

16 And if you could, the members who have a question
17 could just go around, starting with Representative Malone,
18 and we could just come right around back again and there's
19 probably time for questions from the audience. I think it
20 would be useful if we try not to get into third party colloquy
21 when somebody is addressing Mr. Richards. Let's leave it at
22 that and then when your turn comes you can bring up your own
23 points. So, if you have anything ---

24 MR. RICHARDS: Mr. Chairman, do you want me to finish?

25 MR. WOHLFORTH: I thought you had, excuse me, sir.

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MR. RICHARDS: That's all right, I've finished. The others were very, very brief. I don't mean to imply I'm going to belabor this. In fact, I'll hold these here so you don't fall into the normal human trait of pawing through them as I summarize. These two have to do with the ---

MR. EDENSO: Before you get into that I have some questions.

MR. RICHARDS: Okay.

MR. EDENSO: Your last page, 15, shows an increase in state and local government employees as nearly 15,000. For a specific period of time within that time frame have you had a larger increase than at some other time?

MR. RICHARDS: Yes, the latter years the increase was greater than the former years.

MR. EDENSO: Is that something that you assume is just going to appear as a bump on an overall average line?

MR. RICHARDS: The answer to that, Mr. Edenso, lies not with me and thee.

MR. EDENSO: Right, this is my point. We don't know, looking at this, where we see a tremendous amount of growth taking place. I assume it occurred after 1971 or 1972. Maybe that's an erroneous assumption.

MR. RICHARDS: I'll get you the specific pattern on that.

MR. MALONE: Mr. Chairman.

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MR. WOHLFORTH: Yes.

MR. MALONE: I had one question which I don't know if it's fair to ask Bob, but maybe the data could be obtained somewhere, and that is the increase in employment, particularly in the government sector in Alaska is very large; are there any statistics available or information available that might indicate to us where these people came from who went to work for state government, whether they came from the state itself, or whether they came from outside the state. Maybe we could sort of round that up.

MR. WOHLFORTH: Mr. Rhode says he has something on that.

MR. RHODE: Yes, I checked with Kent Dawson, who gets budget matters from the Governor's office, and was formerly the head of Budget and Management. They did one quick survey and found about 55 percent of those hired as state employees had been physically resident in the state less than one year at the time of their hire.

MS. FLEISCHER: Does that include students who had been outside and were coming back?

MR. RHODE: Sorry.

MS. FLEISCHER: Does that include students who had been living outside in college for four years and were coming back?

MR. RHODE: No, those would count as full bona fide

1 residents. This was done for the year 1975.

2 MR. WOHLFORTH: Do you have any reply to that?

3 MR. RICHARDS: No, I don't. Okay, to capsulize in
4 not more than seven minutes where the Alaska economy seems
5 to be headed, the next two or three years will be periods of
6 rather severe slowdown in growth, and then commencing three
7 or four years out we will enter a period of reacceleration.
8 The reasons for the forthcoming slowdown in the rate of growth
9 are threefold: (1) the decrease of employment on the pipeline
10 project, (2) more modest state spending increases, which seems
11 to be reasonable to assume based on the posture the legislature
12 seems to be taking and (3) a holding back in the private
13 sector, because I think the private sector anticipates the
14 slowdown and just like in any business cycle anywhere, they
15 help to contribute to the very thing they anticipate.

16 The slowdown is not going to be a bust for three
17 reasons: (1) this huge stable underlayment of government
18 providing 40 percent of total jobs, 30 percent of civilian
19 jobs, (2) the fact that the pipeline is not contributing as
20 much of the boom as is normally believed and, therefore, the
21 absence of it is not going to contribute as much to the bust
22 as normally believed. My study showed that 40 percent of those
23 workers send their payroll checks directly outside. Frank
24 Murkowski's study showed that 60 percent of the workers send
25 their payroll checks directly outside. And the third factor

1 is that although I just asserted that businessmen are going
2 to kind of start to play it close to the vest, they're not
3 going to squelch their expansion plans and investment plans
4 completely because they're too much aware of what is coming
5 in the 1980's, and so investment in the private sector will
6 continue, there's no doubt about that; I'm just saying at a
7 slower rate than it has in the past two or three years.
8 That's the short run outlook.

9 The long run outlook -- again, I don't want to belabor
10 points that we all are already aware of, but just to summarize,
11 in my opinion the three most rapidly growing sectors of
12 Alaska's economy over the next ten years will be petroleum
13 (this is in the private sector, by the way) -- petroleum,
14 construction and the visitor industry. I think by the end
15 of the next decade these three industries will surpass fishing
16 in their importance as sources of employment. I think the
17 fishing industry will grow moderately, kind of like it has
18 in the past. The hardrock mining and forest products industries
19 are impossible to predict and, hopefully, they'll experience
20 some growth, but probably at slightly more erratic patterns
21 and uncertain rates. And finally, I think agriculture con-
22 tinues to remain a long shot, though a tremendous potential;
23 there's no doubt about that.

24 In the public sector, state and local government in
25 ten years will replace the federal government as the dominant

1 employer in the State of Alaska. Anchorage, I think, will
2 continue to serve as the state's commercial and financial
3 center -- and that is that.

4 Now, what sort of policy implications seem to flow
5 from all of this, and there is nothing particularly astute
6 or insightful in these policy implications. They just seem
7 to kind of naturally come up out of this material that's gone
8 before. The first is, I don't think we have to get hung up
9 on doing something drastic to counteract the booms and
10 busts that have plagued Alaska's history. As I've asserted,
11 I don't think that's a true statement. However, if we had
12 the rest of the week to examine the events that are likely
13 to occur over the next decade and kind of get the investment
14 function (if you will) for Alaska over the next decade, we would
15 find, I would think, that this function is discreet as dis-
16 tinguished from continuous. It seems to me that Alaska's
17 economic growth over the next decade is going to come from a
18 series of relatively major additions to our economy as dis-
19 tinguished from just normal expansions of what is already
20 here. Therefore, I think we can look forward to periods of
21 hyper-inflation, periods of unemployment, on the down side,
22 etc.

23 The dams, the gas pipelines, the major oil discoveries,
24 etc. So it seems to me that one policy implication of this
25 notion of cyclicity, I've indicated here -- one is an effort

1 to go after the relatively less cyclical industries. But
2 another one would be, and I didn't mention it here, but I
3 think it's really more relevant in terms of the actual manage-
4 ment of the Fund, and that is to utilize the investments by
5 the funds somewhat as a counter-cyclical device, i.e., to
6 dramatize the point, if we're building a second oil pipeline,
7 if private industry is building a second oil pipeline,
8 maybe the time for the State Permanent Fund to invest in a
9 dam is not coinciding with the construction of the second
10 pipeline but, indeed, following it.

11 And it's interesting to observe that state spending
12 policy was doing a beautiful counter-cyclical job in the
13 early '70's, i.e., it did pump money into the economy in the
14 early '70's and kept things better than they otherwise would
15 have been. But they didn't turn off the spicket. This is
16 not a state phenomenon, this also happens to be a national
17 phenomenon. They didn't reduce the spicket so the state, in
18 fact, has contributed to the intensity of the upswing
19 cycle and all the problems related thereto that we're
20 experiencing.

21 But at any rate, this notion refers not so much to
22 the type of investments that the Permanent Fund would be
23 making, but it would be the timing of the investments, and
24 perhaps the location as well, the geographic location as well.

25 The next one, seasonality, is very easy to say and

1 very difficult to do. Obviously we need more jobs in the
2 wintertime, but coming up with something is a horse of a
3 different color.

4 Diversification, again we're going to have an awful
5 lot of our eggs in that petroleum industry basket, and it
6 seems to me that -- and also the geographical diversification
7 concern is equal to the industry -- and that is a heck of a
8 lot of the chickens that hatch from that egg are found here
9 in the Anchorage area, South Central area. You know, one
10 could argue for the case that perhaps the entire state would
11 be better off, the whole would be better off if the parts,
12 if the geographical parts had a more equal share in the
13 generation of the whole.

14 Again, as I've pointed out, our economy is highly
15 labor intensive. This is one blessing of the petroleum
16 industry, it's extreme capital intensity. There's another
17 thing about labor intensive -- the most critical element of
18 labor intensive industries is really they tend to be low
19 wage industries. Although bank tellers and hotel clerks
20 are paid more in Anchorage than they are in the Lower '48, yes,
21 that's true, but bank tellers and hotel clerks are paid
22 considerably less than roustabouts on drilling rigs and
23 bookkeepers for petroleum firms, and there's only one thing
24 that explains that, one and only one thing. That is the
25 differing degree of labor intensity and capital intensity.

1 In terms of the policy implications of the outlook,
2 I don't think that there's any reason for the state to panic
3 about going into a bust and, therefore, to go into some major
4 explicit counter-cyclical spending spree. It seems to me
5 that the normal increases that simply flow from social con-
6 cerns will be enough to keep a sufficient amount of spending
7 injected into the economy, and the implication of the long-
8 range outlook is that the fund -- that because of the type of
9 growth we're going to have, is going to be principally capital
10 intensive, and it's likely that public revenues will increase
11 to a considerably greater degree than the demand for public
12 services. Therefore, it seems to me that the managers of
13 the fund are going to have more latitude for investment
14 decisions because, even of that 75 percent, I'm asserting that
15 a heck of a lot of it is going to be available for going into
16 public works projects and this sort of thing as distinguished
17 from simply hiring more automobile license clerks and that
18 sort of thing.

19 As I indicated, this is just a rough pass, and I've
20 got a little item here that I won't even talk so much about.
21 This is simply a current statement of how the Alaskan economy
22 seems to be doing today on a regional basis, and I'll pass it
23 out to you. I'd just like to give you a -- we can discuss
24 the regional element in depth at some time later. And, just
25 for the fun of it, I was so intrigued by this article that

1 I'll pass it out to you and you can do with it what you'd
2 like to.

3 MR. WOHLFORTH: Thank you. We'll go around the table
4 with questions as we started to. Representative Malone has
5 one. You can lead off, and then Mr. Waldock and so on.
6 There's an awful lot to digest here, and we can digest some
7 of it.

8 MR. MALONE: Thank you, Mr. Chairman. This isn't
9 actually a question; maybe it's a comment, Bob. The concept
10 of using the fund balance or the fund investment as a counter-
11 cyclical device, as you described it in the Alaska economy,
12 poses a very difficult political question in that when you
13 have a great amount of activity in the economy, when you have
14 something going on, say, like the Trans-Alaska Pipeline,
15 there's considerable demand for capital at that time, and
16 when the business community perceives things may be slacking
17 off, then they're not going to go on the hook for the debt.
18 So then probably those types of investments or expenditures,
19 whatever it would be, an injection of money, may it not more
20 normally come from the state budget in terms of, say, a public
21 works project rather than an investment that is in the
22 private sector per se, construction of a new plant, a new
23 service industry?

24 MR. RICHARDS: Hugh, I think that's a very valid
25 observation in terms of looking at the Alaska economy by itself.

1 It's true that in periods of down-turn counter-cyclical
2 either fiscal or monetary policy is kind of like trying to
3 push a boat out in the water by pushing on the rope. You
4 can make it available but the extent to which -- I agree
5 with your observation. Perhaps the fund, however, could be
6 utilized to enter into this kind of autonomous investment.
7 Perhaps this is the time for the fund to construct its
8 methanol plant or -- I mean to buy the bonds to permit some-
9 body to construct a methanol plant, or somebody from outside
10 relative to the resource development. But I concur with your
11 observation.

12 MR. MALONE: Then that implies a very active regressive
13 management policy on the fund itself. In other words, we're
14 going to find these projects and identify them and to some
15 extent promote them in order to accomplish them.

16 MR. RICHARDS: Yes. I think rather than really
17 utilize the fund as a counter-cyclical device; I think you're
18 opening up a can of worms and you're probably getting the
19 focus of the management of the fund in the wrong direction.
20 Rather than using it as a counter-cyclical device in an
21 active sense, in an aggressive sense, more look at it on the
22 negative side and just in terms of those investments you're
23 going to do, just be sensitive to the cyclical implications
24 of them and, you know, say, "Hey, maybe we should wait a year
25 before we do this."

1 MR. MALONE: I follow what you're saying.

2 MR. RICHARDS: That sort of orientation rather than
3 the other.

4 MR. MALONE: Thank you.

5 MR. WOHLFORTH: I just have to interject, under my
6 prerogative to interject, a point here. I think that it's
7 the public sector's experience in the last six years -- it
8 seems to be intensely interesting when you mention, of course,
9 that after the oil lease sale in 1969 and '70 we expedientially
10 expanded state spending, not only for current expenses but
11 for capital improvements. Then with the pipeline finally on
12 the horizon and a real burst in potential economic growth
13 for the state, we again expanded our state's spending and
14 in a capital improvement sector of it which, of course, means
15 anywhere from 80 to 90 Million Dollars in bonds per year.

16 Now, why did that happen? I feel because there was
17 a perceived requirement in construction of necessities in the
18 state. We wanted schools, rural schools, we wanted roads and
19 all these things that were, you know, necessary, and really
20 continued to be necessary, notwithstanding there was a tremen-
21 dous burst in economic growth related to the pipeline.

22 I come to no conclusions on the subject matter, except
23 to say that it is a very difficult mix of public, private,
24 perception of what is needed in the state and at the same time
25 observing what's happening to your economy, and observing the

1 possible inflationary effect of the two sectors going along
2 at the same time at their almost hyper-level they did in the
3 mid 1970's. I would love to see some studies. Maybe ISEGAR
4 (sic) has done some on just that phenomena, and whether we've
5 learned any lessons from it, whether we can learn any lessons,
6 it's just a comment.

7 MR. WOHLFORTH: Thank you. Jim, you've got something
8 to say, I think.

9 MR. RHODE: Mr. Chairman, I was just going to observe
10 that sometimes the various agencies and those who are reviewing
11 capital works proposals will argue that since we had 18 to
12 25 percent inflation last year in the construction sector
13 we had better get moving on this because the longer you wait
14 the worse it's going to be when, in fact, you're causing
15 that very rate of inflation.

16 MR. WOHLFORTH: Dennis, I guess it's your turn. Go
17 ahead.

18 MR. WALDOCK: Mr. Chairman, Dennis Waldock. Bob,
19 speaking from an economist's point of view and not an individual
20 resident of Alaska, have you begun to develop charts on what
21 ratio of monies should be applied towards the economic invest-
22 ments rather than social investments? At the last Investment
23 Advisory meeting I was left with the feeling that you had
24 strongly felt that the majority of the money should be directed
25 towards economic investments rather than social investments,

1 and I was wondering if you had the opportunity to work up
2 charts on the ratio that you might suggest.

3 MR. RICHARDS: No, I haven't, because I don't think
4 that -- I just don't think you can avoid the value judgment
5 at least implicit in that exercise. You even used the word
6 "should" and you said to separate my economist side from my
7 personal resident side. My economist side is only concerned
8 with what will or what is likely to, as distinguished from
9 what should. However, an interesting first step in that
10 exercise is included in this report from the Hudson Institute
11 that correlates public investment and private investment, and
12 it gets at the point that I was making last time, and that is
13 when public investment and private investment get out of
14 balance the public investment tends to become counter produc-
15 tive to its social objectives and there are some numbers in
16 there. They've got some numbers in there and, Dennis, in
17 response to what you just stated, I will give some thought
18 to this matter and see how we might come up with some numbers
19 on it.

20 MR. WOHLFORTH: Thank you. Dr. Logsdon.

21 MR. LOGSDON: Yes, in relation to Mr. Reed's comment
22 a while ago on spendable income, Alaska with over 90 percent
23 income from wage and salaries, how does this compare with the
24 U. S. average? Do you have that figure?

25 MR. RICHARDS: I don't have it, but I think it's

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1 somewhere in the high 70's, 76, 78.

2 MR. LOGSDON: It just happens, you know, of course,
3 the wage and salaries, you can't hide those from taxes.
4 I think this could be a significant figure, about 70 percent?

5 MR. RICHARDS: 76, 78 percent. We just have a fewer
6 proportion of retired people, of welfare recipients ---

7 MR. WOHLFORTH: Representative Gruening.

8 MR. GRUENING: Clark Gruening. Bob, in this first
9 paper you're talking about the population growth related to
10 state spending. It seems to me that money was generated by
11 the bonus lease sale. So, in a sense, what other alternative ---
12 let's put it this way: the money was there. Now, could it
13 be that the Permanent Fund was an alternative as a savings
14 to prevent the spending that generated the population growth?
15 If you were to conclude that that is not a worthy goal or
16 that was not good to have that growth in government at the
17 time, what's the alternative? I mean, the money itself was
18 generated by the lease sale, not by the government. Maybe
19 this comes later, but what is the policy implication?

20 MR. RICHARDS: Clark, I don't think it's my role to
21 make any sort of political observation or political recom-
22 mendation. As an economist, I can look you in the eye and
23 state to you that what 90 percent of Alaskans two years ago
24 believed to be the case, i.e., oil has brought people to
25 Alaska, is not the case. That's all I'm stating. I'm not

1 saying whether it's right or wrong. I'm just laying the facts
2 out there for you and, of course, you, God bless you and Hugh
3 and Rick, have the challenge of coming to grips with what's
4 right and what's wrong. I have the luxury of just sitting
5 back and taking a look at what is. That's all I'm saying,
6 is what is. And I kind of make a point of editorializing
7 here a bit. I kind of make a point out of it because public
8 impression has been so much the opposite. That's why I've
9 kind of made a point out of this.

10 MR. GRUENING: I know you thoroughly objected, Bob.
11 What I'm getting at, let's say the government decided not to
12 hire any new state employees, instead they injected into the
13 private sector. It seems to me you encourage the same popu-
14 lation growth. It's the function of spending to generate
15 that, not the fact that it was spent in government, per se,
16 that brought the people here; isn't that right?

17 MR. RICHARDS: Well, it depends whether you invest
18 it in a highly labor intensive sector, which government is,
19 or a highly capital intensive sector. You know, granted
20 if you spend it -- you're right, a job will be created.
21 A job will be created, but you can spend it in ways so that
22 more jobs or fewer jobs, fewer people come, more people or
23 fewer people; you can affect that.

24 MR. GRUENING: I have one other question, Mr. Chairman.
25 Your graph shows an unequal distribution of economic wealth,

1 and as it relates to, say, the Permanent Fund, would you say
2 that that would be relevant to the structure of the Fund as
3 far as looking to the future. Let's say if that were one
4 of the goals of the fund, to somehow even out the economic
5 distribution to the state; in other words, bolster regional
6 economies so that you don't have this uneven high cut.

7 MR. RICHARDS: I think so, very much, but we have to
8 be sure to distinguish here between what is form and what is
9 substance, and it should be invested regionally on the basis
10 of something that will be sustainable and activity that will
11 be sustainable in that industry, in that region, and that will
12 in fact contribute to a real long run sustainable change in
13 these proportions, as distinguished from simply -- and by
14 that I mean a basic alteration of the geographic mix of
15 Alaska's economy as distinguished from some kind of window
16 dressing injection of funds to the present people who happen
17 to reside there. There is a very real distinction there.
18 Otherwise we'd just end up with this same pie chart ten years
19 from now.

20 MR. GRUENING: Along that line I'd kind of like some
21 information -- maybe Tony can provide it -- on where state
22 loans have generally gone geographically.

23 MR. RICHARDS: I don't think the state is involved in
24 any kind of a loan program now that would do the job that I
25 just asserted ought to be done.

1 MR. GRUENING: Yeah, I think that will be borne out
2 by the ---

3 MR. RICHARDS: No, not because of where they're
4 placing the funds, because of the type of loan program.
5 I don't think it exists.

6 MR. GRUENING: Right, what I'd like to see is a
7 matter -- I'm relating to structure now -- I'd like to see
8 where the loans have gone.

9 MR. MOTLEY: Mr. Chairman.

10 MR. WOHLFORTH: Mr. Motley.

11 MR. MOTLEY: I'd be happy to provide that, Mr.
12 Gruening. We happen to keep it by election districts.

13 MR. EDENSO: Mr. Chairman, I'd like to ask Mr. Motley
14 to present it to the Committee, not just to Mr. Gruening.

15 MR. MOTLEY: I'm sorry, it's in the public domain.

16 MR. WOHLFORTH: Next is Robert Barnes, the President
17 of Alaska State Bank.

18 MR. BARNES: I notice in Alaska everyone is really
19 enamored at the cost of living today, and use it as a juncture
20 for higher salaries, and wonder why it's so high. I think
21 the request of you was to make that chart to show the cost
22 of living index ranking. Do you think that would show Alaska
23 at the top and Mississippi at the bottom of all the states?

24 MR. RICHARDS: Yes, it will.

25 MR. MOTLEY: Where will it put Georgia?

1 MR. RICHARDS: Maybe we'd better get this out right
2 now, and I think one of the things you're getting at, Bob, is
3 something with which I concur, and in a certain respect the
4 Bureau of Labor Statistics measurement of cost of living
5 gives as much misinformation as information. It does not
6 sufficiently take into consideration life style differentials.
7 We all know that a gallon of gasoline costs more in Anchorage
8 than it does in Seattle, and we all know that people in
9 Anchorage spend less on gasoline than people in Seattle.
10 So there is a very important -- but I don't think it should
11 be thrown out. It's as good a -- it's the only thing we've
12 got and I think it's a good rough estimate. But users of it
13 have to respect it and accept it for nothing more than what
14 it is, and that is kind of a rough guesstimate.

15 MR. BARNES: A second question, Bob: do you think
16 that our situation is similar to Venezuela in that if we
17 take these funds that have been projected, put them into the
18 economy as Representative Gruening said, the money was there,
19 what alternative was there to spending it? I would think
20 the alternative is what Venezuela did, put it in a fund that
21 is not used in the economy on a short term basis and only
22 brought back into the economy diversified over a much longer
23 period of time, until our situation is similar to that.
24 In other words, can we absorb these funds into our economy,
25 can we build dams and other projects?

1 MR. RICHARDS: You know, that's a fascinating question,
2 the whole question of absorption, and it's the key question.
3 It's a key type question, and one to which I'll have to admit
4 I've not addressed any attention; but it's a key question.
5 Yes, I agree with you.

6 MR. McNEIL: Art McNeil of Ketchikan Pulp. I'd like
7 to compliment Bob Richards on all of this data and report.
8 I think, as usual, he has taken a mass of data and drawn out
9 the report, practical aspects of it. I think it's very
10 helpful and has identified a number of things that the
11 investment policy should be directed at, such as seasonality.
12 I think the aspect of resident versus non-resident employment
13 is an important one to the state. I do notice the projection
14 of growth and other income of the state that Bob has of
15 285 million for fiscal year '77, growing to 800 million in
16 '85; it's a pretty substantial rate of growth. I don't have
17 a calculator here, but I guess that's up around a 20 percent
18 rate of growth per year to get there. I think all this is
19 very, very helpful.

20 MR. WOHLFORTH: Thank you. Jim Edenso.

21 MR. EDENSO: On this aspect of the point of the
22 growth in other income, Bob, could you elaborate on that a
23 little of that, 285 going to 800?

24 MR. RICHARDS: Almost all of that is induced by the
25 growth of the petroleum industry and the growth of state

1 government, and almost all of it is personal income -- I
2 mean not almost all of it, but the majority of it is personal
3 and corporate income taxes. Maybe Commissioner Gallagher
4 wants to make some observations.

5 MR. GALLAGHER: I have a chart that will be of interest
6 to you that I have on a speech on Saturday. One of the things
7 it shows is that government spending made a huge climb in
8 1970, and since that time all we've bought with government
9 is inflation, the bigger population base. All those big
10 leaps in numbers are just inflation and population base.
11 This is boiling government spending down to a real per capita
12 dollar, and the times when we were going through 20 percent
13 population gains we were also going through 10 percent infla-
14 tion. So when the budget went up by 30 percent it shouldn't
15 be that much of a surprise. When we go back and look at a lot
16 of government programs like the School Foundation Program,
17 they're really a function of per capita spending.

18 MR. RICHARDS: But you realize that's somewhat
19 dangerous because you have a circular effect here, that is,
20 the major factor causing the per capita to expand has been
21 the government spending and the multiplier effect thereof.

22 MR. GALLAGER: I agree. It was the year 1970 when
23 we built the base and we've been building the same base.

24 MR. RICHARDS: To dramatize the point, if you only
25 had government employees and you had 50 of them, and you

1 doubled spending and hired 50 more, your spending per capita
2 would not have increased at all, and there's definitely that
3 phenomena to work in there.

4 MR. GALLAGHER: Of course, in defense of next year's
5 budget ---

6 MR. RICHARDS: Excuse me.

7 MR. GALLAGHER: We have a little pudding bandaided
8 on the federal government which will increase per capita
9 spending by 10 percent which is called the Native Claims
10 Settlement Act, and that will be an increase of 58 Million
11 Dollars in just that category.

12 MR. MCNEIL: Mr. Chairman, I do think there should
13 be a thing known as efficiency in numbers, however.

14 MR. GALLAGHER: Everyone has got to prove his own case.

15 MR. WOHLFORTH: Jim, do you have anything?

16 MR. EDENSO: Yes, I do, Mr. Chairman. Bob, on your
17 first working paper number two, on page eight, you give us
18 "Gross State Product by Region." I can speculate on why
19 you made your comments concerning the disproportionate
20 distribution of that product by the South Central and
21 Southeastern. I wonder if you might be able to elaborate
22 a little more on why we do have a concentration of gross
23 state product in the South Central region and the Southeastern
24 region disproportionately on population versus the Interior
25 and other areas.

1 MR. RICHARDS: Well, the reason why is precisely the
2 reason why this is going to change dramatically over the next
3 few years, and that is that's where, in terms of Southeastern,
4 that's where the resource has been, the fishing and the forest
5 products have been, you know. That's where our industry has
6 been. The primary factor underlying South Central has been
7 that this is the hub of the largest sector, the distributive
8 sector, and it's the hub of the second largest sector, the
9 public sector, and it's also the financial sector, but that's
10 included in the distributive sector.

11 MR. EDENSO: So where there are different types of
12 development or potential investment opportunities, a very
13 prime consideration will be the ability of that particular
14 region to support an industry of any kind.

15 MR. RICHARDS: I think it's a very good point.

16 MR. EDENSO: So you're talking on the front end on
17 large capital outlays for in construction development.

18 MR. RICHARDS: Yes. Excuse me, I didn't understand
19 the point you were getting to, but I do now and I concur with
20 it, yes.

21 MR. WCNLFORTH: Thank you. Mr. Love, do you have
22 anything?

23 MR. LOVE: Yes. First I would select to say that
24 I share some of the concerns that Mr. Waldock has expressed
25 in terms of wanting to have something more objective in front

1 of us in terms of evaluating, I think, your basic orientation
2 in terms of where you think the direction of the Permanent
3 Fund is. In your first, Number One paper, you gave what I
4 considered a very short and subjective paper on what you con-
5 sidered to be the different investment possibilities and in
6 terms of how we would maximize benefits to the Alaskan public.
7 There's very strong indications for a development banking
8 type approach and, as I expressed to you, there's a lot of
9 questions that I have on some of the basic assumptions you
10 made. I tend to agree with a lot of your assumptions but
11 I'm reluctant to see this Commission submit itself to that
12 course unless some more objective data comes out, that we
13 can have other people look at, so the bait will not just be
14 the fact that Bob Richards authoritatively says that this
15 is the route to go. I want to be able to quantify this as
16 much as possible in the future. I think there's a lot of
17 support for that position on this board, and I would suggest
18 that we try to develop something so I can feel responsible
19 in my job, to be more quantifiable, more objective.

20 MR. RICHARDS: I concur with everything you've just
21 stated and I will endeavor to do that task for Alaska. We
22 face a practical problem of simply data.

23 MR. LOVE: Yours is the problem. We're unanimous, that
24 is that the discussion has been reduced to a level of, "Do
25 you believe Bob Richards," or something like that, and it

1 really shouldn't be.

2 MR. RICHARDS: I hope the Commission hasn't degenerated
3 to that point. At any rate, I would strongly urge you to --
4 I think you should get a copy of this Hudson Institute report
5 that's outlined. I didn't just frivolously pass that out.

6 MR. LOVE: I understand that. Frankly, the Hudson
7 Report, there's a lot of other things involved in potential
8 choices for investment, Bob, and I'm not talking about comparing
9 any of these investment and development banks in Alaska
10 of the private sector versus adding on more government
11 employees in "X" agencies. I'm sure you would agree there's
12 many other choices to be considered.

13 MR. RICHARDS: I think I outlined about eight or
14 nine of them.

15 MR. LOVE: Right. To compare them all I think we're
16 going to need some more stuff.

17 MR. RICHARDS: Are you suggesting I'm supposed to be
18 the staff to the Commissioner?

19 MR. LOVE: No, I'm just saying in the absence of this
20 position, as a Committee member I'm just pointing out some
21 of my reactions. Secondly, Mr. Wohlforth brought up earlier
22 the point that there are times when there is a relationship
23 between government spending and providing intra-structures
24 to development industries, and I'm wondering if we can get
25 into this a little more in the future so we better understand.

1 You made some bold and sweeping assertions that government
2 spending is the main fuel to inflation and we're all ---

3 MR. RICHARDS: Wait a minute, hold it! Hold it!
4 Did anybody hear me say that? I have stated that government,
5 the State of Alaska, the state and local government in Alaska
6 have been by far the major contributors to the population
7 growth of the state. I've said all of that and I've said
8 only that. Now go ahead.

9 MR. LOVE: Okay. I think what I'm interested in as a
10 member of this Committee and as concerns anyone about the
11 increase in government spending and the increase in the amount
12 and size of the bureaucracy, I want to know more about the
13 cause and effect relationship between the development of a
14 capital against other industry and the needs that creates
15 in terms of more intra-structure. So I think there may be
16 cases when you might point to government and say government
17 spending is actually what is adding the fuel to the economy
18 but you may also be able to point to a situation where a
19 particular kind of development created that need. Would you
20 agree that there are situations where development creates
21 needs for government spending, government services?

22 MR. RICHARDS: Absolutely! I think what we're talking
23 about here, I think we share the very same concern, and I hope
24 the Commission shares the same concern, is that you want to
25 conduct this enterprise known as implementation of the

1 Permanent Fund so as to maximize social benefits in the long
2 run. I happen to be a great follower of Adam Smith, and
3 there is only one sector of the economy that's sacred, and
4 that is the consumer. To say it in economical terms, in
5 political terms, the individual, and the benefits, the total
6 way of real and psychic benefits that he achieves; that's
7 what we're going after.

8 MR. LOVE: So you would agree then that it's important
9 for us to not just look at what might be a symptom in some
10 cases may be the real cause of some of this increase may be,
11 in fact, there's needs for government created by certain
12 kinds of development. I think that's something that at least
13 I would like to have more information on in terms of under-
14 standing how those two factors inter-relate because I'm
15 sure that it's not fair to just assume government just
16 grows out of nowhere. I'm sure there is some cause for
17 the relationship that ---

18 MR. RICHARDS: I think if you imputed that inference
19 on my part you're being unfair to me.

20 MR. LOVE: I'm not. You know, I'm just saying that
21 we agree that there's a relationship. But what that relation-
22 ship is I don't know and I'm not clear. So if you're talking
23 about a concern for more government employees and yet you're
24 also advocating a real development banking approach which
25 may, in fact, create the need for additional state employees,

1 something that I may be definitely opposed to -- so to really
2 put the lid on this state spending and increasing the
3 bureaucracy, you may be advocating us to go in the wrong
4 direction. That's why I say I'm interested in seeing some
5 more information before making a choice.

6 A third point I want to make is, and it's interesting
7 to me, you know, you say, yourself, that you're a follower of
8 Adam Smith, and it strikes me that your approach to this
9 whole investment strategy of the state is not that of a
10 marked economist, but I see you advocating that we make a
11 very definite -- I think the point is as we go through the
12 first paper we see a number of things. We're talking about
13 subsidies concerning the quality of life, or subsidies to
14 income, subsidies to low income families, investment policies,
15 and then we get into the area of diversifying the economy,
16 and I assume the only reason for the state to get involved
17 in those type of loans is because the private market, itself,
18 is not servicing those areas. In other words, if there is
19 something that's a sub-market, marketability involved in those
20 loans, then it imputes to me that there's some type of sub-
21 sidy. My concern is, if that's what we're getting into, that
22 all those subsidies be on the table so that the public
23 understands exactly what the difference between the income
24 we can gain through development loans versus highest return
25 on whatever the market would provide.

1 Now, I tend to actually probably favor your position
2 more, which is opposed to a straight market approach because
3 I believe that there's a lot of cases where the market
4 doesn't properly serve the needs of the state. But I just
5 find it interesting that you find yourself describing your-
6 self as an avid follower of Adam Smith who idolizes -- you
7 know, I don't understand economics as much, but it has always
8 been my impression that he has always advocated a rather
9 classic market approach instead of this social orientation
10 towards development banking that you've been discussing.

11 MR. RICHARDS: Well, I don't think you completely
12 understand Adam Smith, but I don't think anybody is advocating
13 laissez-faire or that sort of thing. That went by the
14 boards a long time ago. We got into a discussion of sub-
15 sidies at the last session, which was a very good discussion,
16 and many of us contributed to presenting various definitions
17 of it. My definition of a subsidy happens to be when the
18 social cost is less than the social benefit of any enterprise.

19 MR. LOVE: I tend to agree with you, and that's why
20 I say I align myself more with your point of view than that
21 of a classic, what I would consider a market approach.

22 MR. RICHARDS: I don't know of anybody, even Milton
23 Freedman, that you can say is an advocate of laissez-faire, and
24 I think the way you're using this term market approach, which
25 I really don't quite understand, implies that.

1 MR. LOVE: I use the term market approach to describe
2 the philosophy that the state's funds should apply to the
3 highest and best return and should not necessarily be
4 investments in development banking.

5 The second point you made about, you know, you think
6 that a good development bank would be, along with the net
7 benefit would be in excess of the net cost.

8 MR. RICHARDS: The net social benefit would be in
9 excess of the net social cost.

10 MR. LOVE: Well, I think this is a very good approach
11 and one thing I'd like us to explore as we go into this further
12 is some way to see who receives the benefit, who pays the
13 costs, so we can identify which income groups, broken down
14 maybe by minority groups, in which communities, geographical
15 locations, skills levels, resident, non-resident, who
16 actually benefits by these particular projects and who bears
17 the cost, to see if they're the same people. I wonder if
18 you advocate, not maybe by yourself but by some of the
19 other consultants, by more of a micro-analysis or a dis-
20 aggregation of these items for us.

21 MR. RICHARDS: Well, Jamie, the way I would summarize
22 the discussion you just held is that we've got to have facts
23 before we make an investment decision, and I concur with that
24 completely. You bet you do.

25 MR. LOVE: That concludes my remarks.

1 MR. WOHLFORTH: Thank you very much. Lanie Fleischer.

2 MS. FLEISCHER: A lot of my questions have been answered
3 by the time you've gotten this far. I had a couple smaller
4 questions such as, on the assumption you've made on
5 seasonality, for instance, I was just wondering if you have
6 data or if we need some data that would show us whether we
7 know that we want to provide jobs in the wintertime. For
8 instance, in Alaska a lot of the jobs are seasonal, and a
9 lot of those are by choice because of the fishing being the
10 way it is, and a lot of people do make their income for the
11 whole year in one short season and then they lay off the rest
12 of the year and do other things by choice.

13 MR. RICHARDS: Lanie, I think it's a very valid
14 observation, I really do. I agree with you. You know, that
15 ipso facto is not necessarily bad.

16 MS. FLEISCHER: That's what I was wondering, if we
17 made the determination or if we can make the determination.
18 Seasonality by itself, in other words, may not be a crime.

19 MR. RICHARDS: Mr. Edenso asked me to do it by
20 industry and by region, and maybe that will help to get toward
21 it, and I'll give some more thought to the matter.

22 MS. FLEISCHER: Okay, I had another question which
23 isn't exactly your place to answer because I think this is
24 for the Committee, but in the cyclical of our economy
25 I also wonder, as did Hugh Malone, I wonder if we'd want to

1 sustain a high population here or to continue doing things
2 that attract people from outside. Obviously we want to
3 employ people who live here and probably on a continuing,
4 steady rate, but do we want to attract large numbers of
5 people from the outside and do we necessarily want to sustain
6 them.

7 MR. RICHARDS: Do you want my value judgment response
8 to that?

9 MS. FLEISCHER: Yes, you can give your value judgment
10 on that, but I realize it's not necessarily your responsibility.

11 MR. RICHARDS: I'll give you my value judgment response
12 to that, and it may surprise you. We are going to get a
13 certain amount of economic growth in Alaska whether you, I
14 or anybody else in the state wants it or not; it's beyond
15 our control. I have a strong intuitive feeling that that is
16 going to be a pretty darn healthy rate of growth. So my own
17 personal value judgment is, given that, let's do things that
18 minimize the population growth of the state -- for what it's
19 worth.

20 MS. FLEISCHER: That was all.

21 MR. GALLAGHER: Minimize the population growth, change
22 the pattern.

23 MS. FLEISCHER: Okay, I also had questions about
24 whether or not the rest of the state outside of Southeast
25 is really out of balance, per se.

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MR. RICHARDS: Whether they're out of balance in a sense?

MS. FLEISCHER: Yes.

MR. RICHARDS: The gross state product per capita?

MS. FLEISCHER: But there is a lot of movement in the state. People tend to live in two places, a lot of them.

MR. RICHARDS: Yes. Furthermore, these whole estimates of gross state product, I suspect, as well.

MR. WOHLFORTH: Thank you. Mr. Thorstenson.

MR. THORSTENSON: Bob Thorstenson. Being from Southeast, while I was interested in your long term opinion or outlook on minerals, forest and fisheries -- the first two were almost pessimistic, a rather slower growth. Fisheries you seemed to have a little more optimism on. I'm wondering if you can back that a little bit more. We in the industry have had a recent bit of optimism with our extended jurisdiction, with higher prices for fish and world consumption of protein and higher standard of living. So I feel quite a bit more optimism than you do, apparently, in the immediate growth ---

MR. RICHARDS: Well, I'm speaking in relative terms now. You know, when you compare it with the petroleum industry -- go ahead.

MR. THORSTENSON: Yes, I realize the relative position. I think though my question was, do you see any immediate

1 injection of capital that will change this term of growth,
2 either domestic or foreign?

3 MR. RICHARDS: In the fishing industry?

4 MR. THORSTENSON: Production of capital in the fishing
5 industry.

6 MR. RICHARDS: Bob, I don't mean to hedge or not
7 arise to a responsibility, but you have a considerable -- I
8 put a heck of a lot more weight on your opinion on that matter
9 than on mine, and I would like to know what your opinion on
10 the matter is.

11 MR. THORSTENSON: Well, I think that I was fishing a
12 bit. I know there's a lot more investment coming into the
13 industry, and this recent crisis created in the foreign
14 countries by our extended jurisdiction, we see a lot more
15 injection of capital into the industry. I think that this
16 group will have to weigh that situation, whether that's
17 something we want to see or we should see it or attempt to
18 encourage the capital from domestic sources such as this one.

19 MR. RICHARDS: I certainly concur with your line of
20 reasoning.

21 MR. THORSTENSON: That's all.

22 MR. WOHLFORTH: Thank you. Representative Urion.

23 MR. URION: Bob, earlier in your presentation (I
24 haven't been able to find it) you said something about at
25 some point in time the state and local government employment

1 was going to overtake the federal government. Do you have a
2 point in time?

3 MR. RICHARDS: Yes, I said within ten years.

4 MR. URION: Within ten years. You're assuming that we
5 continue the rate of growth that we have set in the growth
6 pattern?

7 MR. RICHARDS: That's right, I assumed that the state
8 government would grow over the next ten years as it has over
9 the past ten years, which is probably not even a reasonable
10 assumption. But the other sector, which Commissioner Motley
11 has pointed out, and it should be underlined here, is really
12 the more intense participant in this deal than state govern-
13 ment is the local government. I'm just pointing that out
14 to say that we're not just making assumptions regarding
15 one sector, but what's Fairbanks going to do or Anchorage.

16 MR. URION: But your statistics here show that if we
17 want to discourage population growth we should discourage
18 public employment growth; is that right?

19 MR. RICHARDS: Well, yes. Certainly, yes.

20 MR. URION: If you use this mu'tiplier here, or whatever
21 you used.

22 MR. RICHARDS: Yes.

23 MR. WOHLFORTH: Commissioner Motley.

24 MR. MOTLEY: In the interest of time, Mr. Chairman,
25 I know you have a real heavy gavel over there, I just want to

1 thank Mr. Richards. In his usual manner I think he has been
2 able to take some very dull figures and numbers and make
3 them meaningful to us.

4 The only one other comment I would like to make, and
5 I think, Jamie, when you think back when you started on the
6 Medical Malpractice Commission -- what we've done here this
7 morning is, we've gone all the way around the barn with a
8 lot of things other than just the Permanent Fund, and I'm
9 not suggesting that you isolate it as such, because one of
10 the problems I think we're going to face as we discuss the
11 Permanent Fund, what is the object of this exercise. These
12 other things do inject into it, but I, for one, am going to
13 finish out my thirty seconds with an attempt to put some self-
14 discipline to keep the prime objective in mind in regards to
15 creation of the Permanent Fund. I think a lot of the other
16 things we've talked about happen in different governmental
17 circles all the time anyway, be it in legislative committees
18 or others. Thank you.

19 MR. WOHLFORTH: If I may say, we're creating a
20 unique environment a sociopolitical economic environment
21 if, indeed, the voters pass the Permanent Fund. Mr. LeResche.

22 MR. LERESCHE: I have two or three, Bob. One is not
23 directly relevant to the subject at hand, but you made a big
24 point at the beginning of saying we're not going to have a
25 bust, we've never had a boom/bust economy. You said that very

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strongly. Then you went on to say ---

MR. RICHARDS: Well, I didn't quite exactly put it that way. We did have a bust after the gold rush.

MR. LeRESCHE: Did you say that you don't expect a bust any time soon?

MR. RICHARDS: Yes.

Mr. LeRESCHE: Okay. I'm confused. Then you said our growth will be discreet rather than continuous, that we'll go through periods of unemployment and inflation, that we should perhaps use the Permanent Fund at least passively as a counter-cyclical device. How do you define this bust that we're not going to have?

MR. RICHARDS: Okay, to a certain extent there's a semantic issue here, yes, which I've created, and maybe I've reacted too much to the term "bust". But I'll have to confess I've been -- my attitude toward the term "bust" has been influenced substantially by outsiders coming to Alaska and inquiring about this post pipeline bust, and it's bankers, it's journalists, it's a whole array of people who traipse through here with whom I've come in contact, and the way they ask this question, the way they bring up the question and then talk about it, using the term "bust" implies that when the oil pipeline is going to be over that's all she wrote and we might as well all pack it in and there's going to be an economic collapse, something that approaches the depression,

1 the great depression. I'm asserting that that's what we're
2 not going to have, and I apologize for that if I've kind
3 of over-reacted to this notion which I've sensed in certain
4 circles.

5 MR. MOTLEY: That's a very valid point, you're right.
6 There are enough people talking about it. I think it has
7 to be quantified.

8 MR. LeRESCHE: It's a matter of degree.

9 MR. RICHARDS: That's right, exactly. Yes, we are
10 going to have cyclical fluctuations and probably rather
11 severe from time to time.

12 MR. LeRESCHE: Okay, that clarifies it. Secondly,
13 you said a lot of things about the petroleum industry and
14 related industries, that they hold a disproportionate number
15 of our eggs right now. They're certainly highly capital
16 intensive, they're destined to grow probably fastest of all
17 the industries in the next ten years and various other things.
18 This implies to me in kind of a simplistic sense that because
19 of these reasons we shouldn't use the Permanent Fund to
20 invest in petroleum related industries because it's going
21 to take care of itself and we already have too much in it.
22 Is that a fair conclusion to draw from what you said?

23 MR. RICHARDS: Or unless you invested it in such a
24 way that the cyclical behavior of that industry is mitigated,
25 and by that I mean perhaps some vertical or horizontal

1 diversification. But I haven't really thought through the
2 matter that much myself.

3 MR. LeRESCHE: It's interesting to me that the
4 relationship between the fact that we have so much of our
5 income coming from that industry, that would seem, per se,
6 to argue against getting any more of our income tied into
7 that industry or its ancillary industries. But I see why
8 there is another reason we might want to do it.

9 Finally, this is just kind of a basic question of an
10 assumption -- you've said that regionally our economy is
11 very unbalanced. Just as an economist, what are the virtues
12 of having our economy balanced regionally?

13 MR. RICHARDS: I'm glad you raised that, because an
14 awful lot of people have really imputed some value judgments
15 here and, of course, I have to accept responsibility for that
16 in tones of voice and so forth. You're right, I don't know
17 of any state in the Union that is regionally balanced,
18 California certainly not, Washington, Oregon, Utah, Colorado.
19 So, no, I don't mean to imply that if all those sectors were
20 equal that would be better than what it is now. I don't
21 mean to imply that at all.

22 MR. LeRESCHE: And there's no basic economic reason
23 that would imply that then that you know of?

24 MR. RICHARDS: No, other than I just have an intuitive
25 feeling that this is a bit startling. Furthermore, this data

1 tends to coincide (more important) with something we kind of
2 intuitively feel anyway, and that is in the Interior and the
3 Western region and the North, there are not sufficiently
4 sustainable economy so as to enable the people residing there
5 to do some of the things they apparently want to do in terms
6 of their standard of living.

7 MR. MOTLEY: Bob, isn't there one further distortion
8 in there, one further distortion in there that distorts that
9 regional because the bean counting that goes on as the gross
10 state product doesn't necessarily apply to the Northwest
11 region?

12 MR. RICHARDS: Very, very good.

13 MR. MOTLEY: Isn't that one of the things that
14 distorts it?

15 MR. RICHARDS: Yes, absolutely.

16 MR. MOTLEY: It's not cash oriented.

17 MR. RICHARDS: Right.

18 MR. LeRESCHÉ: I'd like to make one more comment.
19 This morning we've talked a lot about growth and I think
20 several of us have fallen without trying to into the trap of
21 lying with statistics. The best way to structure your
22 statistics is to pick a base year that's going to end up
23 proving what you want to prove and assume that somehow
24 magically things were perfect in that base year, and then
25 we'll change up or down from that and it's either good or bad.

1 Now, that's just an observation. A lot of our discussion of
2 changes over time has been based on implicit and perhaps poor
3 assumptions of the fact that 1960 was just perfect in terms
4 of wages, state employment, per capita and things like that.
5 I make no value judgment, but we ought to think in terms of
6 the fact that maybe that wasn't necessarily perfect.

7 MR. RICHARDS: This data -- you know, you're free to
8 draw your own value judgments from this data.

9 MR. LeRESCHÉ: That wasn't directed at you, Bob.

10 MR. RICHARDS: It could be.

11 MR. WOHLFORTH: There is about ten minutes left before
12 the noon break, and if any of you members of the audience have
13 any particular questions that they want to just give Mr.
14 Richards, if he doesn't mind, it might be valuable (non-
15 governmental types) maybe. If not, we can go back and ask
16 some more. I know that Mr. Edenso has one last point he wants
17 to fire off here.

18 MR. EDENSO: Thank you. Bob, your first paper, first
19 part of your presentation this morning, you're talking about
20 distribution of labor between the various sectors of the
21 economy. You didn't describe the labor as skilled or unskilled
22 and such, or how that was distributed, or how that was
23 affected generally by the fact of seasonality which influences
24 Alaska's employment. I was wondering if we do have any numbers
25 which do reflect that or if you do have any statistics like

1 that or any comments concerning it.

2 MR. RICHARDS: The skill level of the labor?

3 MR. EDENSO: Yes.

4 MR. RICHARDS: The State Department of Labor does and
5 we can get them.

6 MR. EDENSO: We know that there is a distribution of
7 skilled and unskilled and that also has a major effect
8 within the economy.

9 MR. RICHARDS: Okay.

10 MR. WOHLFORTH: How about questions from the audience
11 that may have been sparked by any of the comments that were
12 made or the presentation here? I'm inviting any questions
13 from the audience to Mr. Richards in the few moments we have
14 before the lunch break. If there are none, any more questions
15 from the members?

16 MR. MOTLEY: I have just one comment. It appears
17 to me that the quest of the search for data is in evidence
18 here, and I think it's a valid one. Probably, by its nature,
19 it determines our first investment, and that appears to be the
20 Full Employment Act for Consultants.

21 MR. WOHLFORTH: On that subject, this afternoon, for
22 those of you who don't have the agenda, at 1:30 there will be
23 a report on current Permanent Funds, characteristics of
24 management, legal structure, etc. by Mr. Ken Butler of
25 White, Weld and Company; 2:30, report on the organization

1 management and control of development banks by Peter McDowell
2 of Price, Waterhouse; 3:30 is new business. That's just
3 what's on the agenda this afternoon.

4 Without objection then we'll adjourn till 1:30.

5 (Whereupon the meeting recessed at 11:55 a.m.
6 and reconvened at 1:30 p.m.)

7 MR. WOHLFORTH: Although we're missing a few members,
8 some people have a time schedule they want to keep, so we'll
9 resume the session now. I have had a request for a very
10 brief opportunity to present observations by Mrs. Fleischer.
11 If the Committee has no objection I would propose putting
12 her on the agenda at this time and then go immediately to
13 the White, Weld report which is scheduled for 1:30.
14 Go ahead, Mrs. Fleischer.

15 MS. FLEISCHER: Thank you I made some notes on what
16 I wanted to say so I could confine myself to the subject and
17 keep it brief, but I do have a lot to say. But I find myself
18 sitting here thinking we are putting too many carts before
19 the horse and that all of the information being presented here
20 may or may not be relevant to what we really need to do, and
21 that's why I wanted to make a remark now and say to the
22 Committee that what I would like to see us, after these
23 reports have been finished, is to focus on the thing we have
24 to do first, and that is establish the goals and objectives
25 for this Committee or for this Permanent Fund. We need to have

1 a discussion, an open discussion on what we see the Fund, the
2 purpose of the Fund and what we think it should be for
3 before we really know what questions to ask our consultants.
4 I know they can give us some information that's useful, but
5 the whole world is full of information and we don't know what
6 charts we want, what information we want, until we've
7 established our goals.

8 I think we need to include the people in the state
9 in the decision making process in regard to the goals and
10 objectives. I know that that's probably an unpopular thought
11 because of our time constraints, but I think it is a necessary
12 thing to be done, and I do believe that if the voters of the
13 state are shown that this is the way it's devised they won't
14 oppose it. I don't think they'll defeat the amendment on
15 the Permanent Fund because I believe that whatever Permanent
16 Fund means to the people, it does mean something positive, and
17 I think it's up to the Committee to see that the goals and
18 objectives set do reflect what the people of the state want
19 to do with the Permanent Fund, that they are established, and
20 I think we have to do that.

21 You know, I'm a little bit concerned that maybe some
22 goals have already been established, or maybe some people
23 somewhere have established goals. But as a committee we
24 haven't done that, and I see that as one of our first jobs,
25 and I want to see that we do that. That's not something we can

1 ask our consultants to do; that's something we have to
2 decide as people of this state, what goals we have for the
3 state and, therefore, for the Permanent Fund itself. I
4 would request that we do that job before we do anything else.

5 MR. WOHLFORTH: Thank you very much. I think, for
6 however it fits in with your request, that we should have
7 some enlightening information on at least what others have
8 done this afternoon and that is, of course, the purpose for the
9 two firms who are about to make a presentation. The first
10 firm, as I understand, is the investment banking firm of
11 White, Weld and Company of New York City. Mr. Ken Butler
12 is indicated as making the presentation, but there are other
13 gentlemen there. If you will introduce yourselves and after
14 you do so, if you'd go right into your presentation.

15 MR. BUTLER: Thank you, Mr. Chairman. I am Ken
16 Butler from the San Francisco office of White, Weld and
17 Company. On my left is Mr. Pat Oden of the Public Finance
18 Department of the firm in New York, and on my right is
19 Mr. Charles Fuhrmann of the corporate finance department
20 of the firm in New York.

21 In accordance with the request of the Committee, we
22 have provided you with a survey of domestic, foreign and
23 international development banks, funds and development pro-
24 grams for your use in determining the future structure and
25 objectives of the Alaska Permanent Fund. In performing our

1 survey we have selected those banks, funds or development
2 programs which are of major importance, as well as those
3 which are particularly relevant to Alaska's situation in that
4 they are either based upon natural resource revenues or
5 confined to a limited geographic area.

6 Mr. Fuhmann and Mr. Oden are here as representatives
7 of a larger group of White, Weld people who are involved in
8 advising you on the Permanent Fund within the state. Our
9 analysis of domestic permanent and development type funds
10 was headed by Mr. Pat Oden.

11 MR. ODEN: Basically, in analyzing the domestic
12 permanent funds we took a look at two categories which are
13 represented in Exhibit "1" and Exhibit "2". Exhibit "1"
14 focused on those states which receive income from a finite
15 natural resource and the manner that they use that income.
16 The majority of the states receiving income from finite
17 natural resources spend that income on a current basis.
18 Those states and the application of the income that put those
19 incomes in trust are set forth in Exhibit "1" of the report
20 you have.

21 Exhibit "2" is a little more amorphous. That is two
22 states -- well, not two states, one commonwealth and one state,
23 which have economic development programs, formal economic
24 development programs. We've requested from every state their
25 particular assistance programs and aid programs to industry,

1 and they vary from property tax forgiveness to income tax
2 foregiveness to outright guarantees.

3 We are in the process of accumulating a substantial
4 file on complete information from each state on their economic
5 development program. Therefore, seen in this report today
6 is not the entire spectrum of economic development programs
7 in the United States; it's only two, and the additional
8 information will be coming. I think it will provide a tremen-
9 dous data source for the Permanent Fund, to give them an
10 excellent handle on what approaches every other state has taken.

11 That's essentially the sum.

12 MR. BUTLER: Because, as Jim mentioned earlier, Mr.
13 Chairman, I might check. Do all members of the Committee have
14 a copy of the report presently, since we're referring to it
15 heavily? Good.

16 With respect to the international and foreign develop-
17 ment banks, funds, and development programs, Charles Fuhrmann
18 headed the firm's effort in that area, and he would like to
19 make comments concerning that aspect.

20 MR. FUHRMANN: Substantially all of the less developed
21 nations of the world, and a certain number of the more developed
22 nations, have government owned or controlled entities whose
23 purpose is to participate in the financing of local economic
24 development projects. In most of the small nations, these
25 entities function principally as the vehicle through which

1 the major world-wide institutions provide funds, i.e., the
2 World Bank, through them, etc. These are also the vehicles
3 through which the nations' development funds are dispersed
4 into the economy by the government, and they are very heavily
5 involved with political process. These entities also act
6 as the conduit, as I said, for World Bank funds and other
7 development funds provided by the larger international
8 institutions, and are invested in smaller projects in the
9 country concerned through these development banks, the
10 World Bank considered not being interested in smaller projects
11 themselves, so they make larger loans to these development
12 banks who, in turn, make smaller loans for smaller projects
13 in their area.

14 One of the advantages of the latter process is that
15 the use of a local bank as a vehicle permits the larger
16 institution's loan to receive a government guarantee, which
17 is commonly a prerequisite for the extension, or the initial
18 extension, of credit to that country. In most countries the
19 development banks and funds that perform these functions also
20 serve as the means through which internal economic growth is
21 directed and channeled in accordance with national economic
22 policies and are, in effect, extensions of the local economic
23 ministry.

24 Our report covers three of these, the Swedish Invest-
25 ment Bank, Japanese Development Bank and National Financiera,

1 which is the Mexican Development Bank. You will not have
2 page two of the National Financiera summary, but I brought
3 adequate numbers with us for everyone to have one. For some
4 reason they got left out in assemblation. In each case these
5 institutions are responsible for carrying out the national
6 economic policy through their activities and they enjoy
7 various degrees of autonomy from the national political pro-
8 cess. The most independent is the Swedish Investment Bank
9 and the least is National Financiera. National Financiera
10 and the Japan Development Bank are heavily involved in the
11 political process in their respective countries. National
12 Financiera is also the conduit for World Bank lending in
13 Mexico, both for corporate borrowings and public agency
14 borrowings.

15 That summarizes the group that is in Exhibit "3".

16 Exhibit "4" is the larger development banks and funds
17 which are international institutions whose memberships consist
18 of several countries and whose purpose is to foster the
19 economic growth and development of a particular region or
20 its members. In general, these entities represent potent
21 world-scale economic forces and tend to be both non-political
22 and commercial in their operations. The financial strength
23 of these entities is typically based on the uncalled capital
24 subscriptions of their members, and virtually all of them
25 borrow heavily, both locally and in the international capital

1 markets. Substantially all of the activities of these
2 institutions consist of direct lending for specific projects
3 in the various countries, and lending policies appear to be
4 determined on social benefits as well as economic grounds.
5 As a result, and to the extent that many major industrial
6 nations are commonly among the larger contributing members
7 of these institutions and receive no benefits, they can be
8 viewed as quasi foreign aid banks.

9 Among such international and regional development
10 institutions covered by our survey (and Price, Waterhouse
11 has taken a much further step into the management and
12 organization structure of most of these entities) the most
13 significant is the International Bank for Reconstruction and
14 Development, the World Bank, both in terms of its world-wide
15 membership and the international scope and significance of
16 its lending activities. Importantly, all of the other
17 international institutions included in our survey, whether the
18 Inter-American Development Bank, Asian Development Bank, the
19 African Development Bank, these have been created with the
20 assistance of and modeled after the World Bank, both opera-
21 tionally and in financial structure.

22 Of these three derivative institutions, only the
23 African Development Bank is not a significant international
24 borrower and depends heavily on loans from other institutions,
25 such as the World Bank. This characteristic results from the

1 fact that there is no local capital market in Africa large
2 enough to support the program of that bank, and neither are
3 the countries involved in the credit of that bank substantial
4 enough to merit good credit ratings in the international
5 markets. So they are dependent upon, almost completely,
6 borrowing from the World Bank, etc.

7 Two other institutions which fall somewhat into this
8 category of large international institutions in that their
9 activities are regionalized rather than localized are the
10 European Investment Bank and the European Coal and Steel
11 Community, both of which are related to the Common Market.
12 Significantly, both of these borrow in various capital
13 markets and relend for projects consistent with their purpose.
14 The credit strength of the European Coal and Steel Community
15 is based fundamentally on the strength of the private steel
16 industry in Europe, while the European Investment Bank is
17 modeled along the lines of the World Bank and depends on the
18 credit of the Common Market member states.

19 The remaining type of institution is one which functions
20 in a limited geographic area or within a particular industry
21 to promote economic growth and development, or to achieve a
22 social objective, and is based on local or regional resources.
23 This is Exhibit "5" groups of companies, of institutions.

24 Of the three basic groups of international development
25 institutions, this group contains the smallest number of

1 entities and is, perhaps, the most analagous to the situation
2 in Alaska. These development institutions or funds are new
3 and, to a large degree, based on natural resource revenues.
4 Significantly, only two are international in scope; others are
5 modeled after the World Bank but limited in their activities
6 to a defined geographic region, ethnic grouping or social
7 purpose. The remainder are national investment funds.

8 The majority of these funds are based in the Middle
9 East and dependent upon oil related revenues. Those that have
10 an international scope are the Saudi Development Fund and the
11 Arab Bank for Economic Development in Africa, both of which
12 were created after the increase in world oil prices in recog-
13 nition of the balance of payments and development problems
14 created in the developing states by such increase. The
15 remaining funds, the Arab Fund for Economic and Social
16 Development, the Abu Dhabi Fund for Arab Economic Development,
17 the Islamic Development Bank, and the Kuwait Fund for Arab
18 Economic Development, although created at approximately the
19 same time as the others, reflect in both the source of their
20 capital, which is member states' subscriptions or allocation
21 of national revenues, and their purpose, the Arab nationalism
22 which emerged after the Mid-East wars. Importantly, most of
23 these funds have yet to become fully operational, and it is
24 too early to judge their potential significance. The two
25 national investment funds, the two which you may find are the

1 most directly related to the proposed Alaska Permanent Fund,
2 are the Fondo de Inversiones de Venezuela and the Alberta
3 Heritage Savings Trust Fund. The similarities here extend
4 both to the source, which is non-resource revenues or non-
5 recurring resource revenues (I should say) and the purposes
6 which can be seen in our summary studies.

7 We have not undertaken, nor have we been asked by
8 this Committee, to recommend to the Committee certain key
9 features of any one of these bank's funds or development
10 programs of the others. What we have done in the study is
11 try to provide you with information regarding the various
12 alternative purposes, alternative income policies, investment
13 criteria, etc., so that you could have a feel for what the
14 world-wide scope, or environment, or whatever, what the
15 alternatives are, and be able to focus on them and just
16 from among them, and also create those of your own more
17 particular to your situation.

18 The purposes in these 30 odd studies cover a pretty
19 wide range. Some are developed to encourage economic nationali-
20 zation and structural adaptation and development, some are
21 to create employment, improve personal income, expand
22 regional development, centralize industry, promote exports,
23 stimulate capital formation, foster economic independence,
24 urban redevelopment programs, supplement private investment,
25 not be the sole investor, improve land use and settlement,

1 subsidize low income housing; some deal only with the intra-
2 structure projects, roads, utilities, water, sanitation.
3 Education is the main emphasis of many of the programs.
4 Some are to develop conversion areas, replacing judicial
5 activities with new industries; some are geared strictly
6 toward better living and working standards; many of the funds
7 are involved not only in providing monies but also in pro-
8 viding technical and financial services. Some of them are
9 policemen and police the operations in which they invest,
10 and others take a back seat position. There are those that
11 are a reservoir only at the present time for public funds
12 to keep them out of the current economy and avoid inflation,
13 waiting for the time when the monies are needed. Some are
14 geared for redistributing income, encouraging technical
15 independence, and some are meant to assure rational and
16 diversified internal investment which may not be taken care
17 of in the normal course of general programs.

18 These are a variety of the purposes, and there are
19 many more, and they will come rather obvious to you as you
20 look through those pages, and we've structured them in a way
21 to try to be most useful. They're each in the same format
22 so that you can look in the same spot and see what their
23 purposes are or income policy is.

24 With respect to income policy, many of them have
25 the income of the fund retained by the fund. Others have it

1 put into a statutory reserve, representing a percentage of
2 their investments or as a reserve against bad investments,
3 or some of them have it limited to a percentage of their
4 equity investments to protect against those going sour, or
5 a percentage of their soft loans, or a percentage of their
6 total portfolio. Various kinds of reserve have been estab-
7 lished by some, by others none at all. In almost every case
8 the fund is involved in covering its own operating costs.
9 Some are taxed by their national authorities, others are
10 untaxed. Some, the income goes direct to the state or
11 national treasury, the general funds, but the capital is
12 left untouched. Others, there's access to the capital. Some
13 dividend their income to the stockholders, if you will.
14 Some have structures with common and preferred stockholders,
15 which brings in additional capital. Some have the income
16 transferred to related funds. In other words, they may set
17 aside certain more risky ventures, or whatever, and have
18 those funds available for that be limited to the income of
19 the Permanent Fund or Permanent Capital, you know, whether
20 it's a fund or a development bank. And some have the funds,
21 the national ones, some of the ones involving member states,
22 as subscribers to the capital, have the funds allocated to
23 the members' capital accounts which, in some cases, has a
24 tendency to increase that nation's participation or voice
25 in the management decisions of the fund. Others have them

1 transferred to specific purposes, the income transferred to
2 university funds, public schools, or ilio-mosinary (sic)
3 institutions or the enhancement or care of the environment,
4 or some special cause the income goes to which is divorced
5 from the investment policy of the fund.

6 Criteria that are used in making investment decisions
7 range all over the lot as well. A large number of these funds
8 have, among their criteria, that the funds not be generally
9 available from other sources so that the fund is not competing
10 with local sources. Some don't have that at all. Some demand
11 that the projects that are invested in are commerically
12 viable, that they have an impact on the economy, that the
13 terms reflect a satisfactory return on investment, that the
14 terms are consistent with the risk and actually apply tradi-
15 tional credit standards to the project they are considering
16 investing in. Some demand that they only participate in
17 loans as a participant, not be the sole lender. Many have
18 floating rates, some have fixed rates. Those that have these,
19 some have limitations on what the interest rate can be, that
20 it can be no higher than is available in the private market
21 or it can be no lower than "blank" percent. Some have criteria,
22 they can only lend to government agencies or other governments.
23 Some say they can only be for productive purposes, they must
24 be prudent investments, that they can only be used to supple-
25 ment private capital, or to make private capital available

1 by putting in subordinated monies. Some structure their
2 investments in a fashion that is appropriate to the project
3 or the project will even pay, both in terms of interest rates
4 and amortization schedules. Others say that they will only
5 structure them in good business terms and if the project can't
6 stand it the project doesn't get the money.

7 Some only support projects that are for the local use.
8 Others invest both in their own environment or geographical
9 environment, others invest all over the world and their pur-
10 pose is to make money, build credit behind something. For
11 example, it could be considered a potential objective here to
12 purely maintain capital in this fund, build it to provide
13 a credit standing for the state as it puts its own issues
14 out. Some of these funds exist for that purpose, or the funds
15 are kept in house and only guarantees are used, and they're
16 able to leverage the funds by putting out more guarantees
17 against the capital that is in the fund.

18 Some insist that the projects being financed encourage
19 savings in their community or are constructed to the balance
20 of payments of the nation involved. Employment is a big issue
21 in many of these funds to stimulate employment or to diversify
22 geographically employment, or industrially employment, or
23 develop skills, talents or technical expertise that they
24 don't have. Many of them are only interested in larger
25 projects, they do not want to have a widespread dispersal

1 of their funds and limit themselves only to major, huge
2 projects that take place.

3 Some insist on security on all loans and others take
4 the social good and social benefit route and don't really care
5 whether they're going to lose all their money in terms of
6 investments but, to quote from this morning, the social
7 benefit is determined to outweigh the social cost. Many
8 of the funds have limitations on the percentage that they
9 will have go to risky loans or government oriented loans,
10 or certain industry kinds of loans, or various levels that
11 control that are shown by the funds, guidelines of investments,
12 how much can go here, there, etc. Many have limits on how
13 much can go to any given project; they will only put up five
14 percent, or 50 percent of the capital, the balance must come
15 from private sources, other sources.

16 Some have requirements regarding diversification of
17 equity; that they're going to participate in equity at all
18 or whether it must be diversified by industry and they can't
19 become the sole owner of the oil industry or whatever comes
20 to my mind -- but that particular group that have that as
21 one of their criteria happen to own the oil industry.

22 So, there are a variety of criteria, and we hope that
23 as you review these that you will have available to you a
24 wide variety of things other people have done and be able
25 to judge on your own the merits or demerits of any of these

1 alternatives in putting together your own.

2 We have, as Pat suggested, in addition to providing
3 these summaries, have begun to compile a file of source
4 materials which are essentially background materials on each
5 of these funds, and our work here is no way complete. We
6 are continuing to collect information on additional funds,
7 both domestic and international. There are a few more
8 Canadian entities that we are in contact with in discussing
9 their programs with, who for some reason or other we are not
10 at the present moment completely complete on the information
11 we would need to either provide a summary or provide the
12 information on. But we are preparing for you, and have
13 brought with us, the initial version of what we would call
14 a resource file so that members of the Committee and members
15 ultimately of the Permanent Fund management, etc. will have
16 the beginnings of a resource file on what other people are
17 doing around the world. This file includes annual reports,
18 prospectuses for those that leverage themselves, copies of
19 their charters, and the legislation that was necessary to
20 implement them originally, and just about anything else we can
21 get our hands on. So we will be leaving that with you today.

22 At this point we feel, as we have indicated in our
23 cover letter to this report, that it would be most helpful
24 to have certain representatives of the Fund meet with the
25 Alberta Heritage Fund people and the State of New Mexico

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1 people to assess their programs and to better understand the
2 philosophy of their decisions. We have discussed this
3 internally and with the Alberta and New Mexico people, and they
4 are interested in such discussions.

5 We would also suggest that it could be helpful to
6 have certain representatives of the Committee visit with
7 us in New York to discuss first-hand with various members
8 of our firm their experiences with the various international
9 foreign and domestic funds and development programs. I think
10 we've indicated that we are advisors to Abu Dhabi, we are
11 administrators of the Saudi Arabian Monetary Association and
12 have worked closely with the Fondo de Inversiones de Venezuela
13 and many other programs.

14 A lot of the information that we would normally put
15 out on those we would prefer not to necessarily in writing
16 because of our relationships with them, and we feel that also
17 the opportunity to discuss face-to-face with the people that
18 have been involved directly in those could be most helpful
19 and also save trips to various spots in remote corners of
20 the earth. We would also suggest that a visit to the credit
21 agencies would be most helpful to understand what they look
22 for, because I think it's hard to divorce this project com-
23 pletely from the whole financibility of the State of Alaska
24 and its many programs.

25 But also to understand what they would be looking at

1 with respect to the fund should you decide that leverage
2 or raising debt against your equity here was an objective
3 or goal, we think that could be most useful.

4 MR. BUTLER: That's a brief overview of the domestic
5 and international techniques we've used and ground we've
6 covered and all. Maybe at this time it would be appropriate,
7 Mr. Chairman, to answer questions or anything else that's
8 of concern. We do have the data that Mr. Furhrmann referred
9 to sitting over there that we'll be happy to leave with Mr.
10 Edenso or whoever would be the appropriate person, for
11 further evaluation.

12 MR. WOHLFORTH: Thank you very much. There's about
13 25 minutes available for questions on the agenda, and I
14 suggest that we start with this side of the table now to be
15 fair, and remember many people want to have an opportunity
16 to talk, and that this report is basically on permanent
17 funds and the like; development bank structure and organization
18 is dealt with in the next report. So with that, I would turn
19 it over to Mr. LeResche.

20 MR. LERESCHE: Okay, I just have one fairly simple
21 question, but which is basic to my use of the report. The
22 first page of the letter in your report which you read to
23 us, you allege that certain funds are more relevant to Alaska
24 than others for two reasons, first because the source of funds
25 is natural resources and secondly, because they're confined

1 to a limited geographic area. I don't understand that.
2 Two questions: why is the source a matter at all and,
3 secondly, how is our fund limited to a geographic area?
4 We're not obliged to invest it only in the state.

5 MR. BUTLER: That wasn't the implication. One, the
6 first meeting of this group whenever it was, some six weeks
7 ago, it was mentioned by several members that they thought
8 it would be most fruitful to concentrate on places north
9 of 60 degrees latitude and with non-renewable natural resources
10 as the main source of funds and this sort of thing, and we're
11 taking predominantly our direction from comments of that type.
12 Secondly, we didn't think it was as applicable where somebody,
13 like Development Bank of Puerto Rico or the World Bank, where
14 their sole source of funds is borrowing in the international
15 capital markets -- not that there's nothing particularly in
16 there, but it's not as applicable as if you have the resource
17 picture. So those two. Mainly we took our lead from members
18 of the Committee that expressed this.

19 MR. LERESCHE: Maybe you could help me by telling me
20 whether that makes any more sense than I think it does.

21 MR. FUHRMANN: I don't think it makes any sense at all
22 when it comes to what the objectives are, and the opportunity
23 to see what other people have done, like in structure.
24 In structure it makes some difference because the member
25 states are not going to be represented here. They're not a

1 series of names who are involved in this environment or in
2 this fund as contributors, but with respect to what they do
3 with their income and what their objectives are and the kinds
4 of projects they necessarily invest in, I don't think it's
5 fair to say they're irrelevant.

6 MR. LeRESCHÉ: Then one other related question,
7 an important thing to me as I read through this is going to be
8 to look at each fund's objectives, and then at their manage-
9 ment structures, and it's hard for me to make a general
10 statement I'm sure, but generally speaking, do the management
11 structures follow logically from the objectives in all cases
12 here?

13 MR. BUTLER: Maybe Mr. Oden could speak briefly
14 from the domestic funds we've looked at and Mr. Fuhrmann a
15 little bit from the international aspect.

16 MR. LeRESCHÉ: And if the answer is no, maybe which
17 ones make more sense to you.

18 MR. ODEN: In most of the states, the states that
19 we've reviewed with respect to permanent funds, they fall
20 into a couple of broad categories. One is one of the grand-
21 daddies of permanent funds, which is Texas. Those monies are
22 all applied by the University of Texas system. They're on
23 state-owned lands. The second is New Mexico, the same
24 sort of situation. Those were set up the previous decade,
25 and the rationale on where those should fit within the

1 governmental structure would certainly not be, I think,
2 relevant today. The objectives of the currently, the newly
3 developed permanent funds, I think they're set up as far
4 as their populace is concerned to serve those objectives.

5 MR. FURHMANN: On the international ones, obviously
6 the ones that involve member nations are going to be structured
7 on an organization, and management and policy level to
8 reflect the membership of international bodies. The national
9 ones, or the ones that relate to a particular area often
10 reflect either the political environment from which they've
11 come, whether it's more democratic or less democratic. Some
12 of them have recognized for their own purposes the advantages
13 of independence, and others have felt the advantages were having
14 it be less independent. So I don't believe that you will find
15 the correlation you're looking for, that the objectives of the
16 fund are directly reflected in the management, how it's
17 organized. Perhaps it should be, but I don't think that
18 you'll find that.

19 MR. LERESCHE: Okay, that's helpful, thank you.

20 MR. WOHLFORTH: Thank you. Commissioner Motley.

21 MR. MOTLEY: In going through this report, I was looking
22 for the common thread that we have here, that is, a restriction
23 according to the big income producing investments, and I
24 haven't found it. Is that true or not?

25 MR. FUHRMANN: No, you missed some, because there are

1 a lot that have, as I stated, in the criteria -- some of them
2 insist upon the commercial viability of the project, yes.
3 Some of them insist, as I said earlier, upon a satisfactory
4 return on their investment, and coupling that with the
5 ability of the project to meet those terms. An enormous
6 number of them, almost the bulk, other than the foreign aid
7 banks, which are dependent upon the taxing authority, etc.
8 of the nations involved, they're not worried. Almost all
9 of them are involved, more involved in income producing and
10 less socially good loans than the opposite.

11 MR. MOTLEY: Are they as restrictive as just the one
12 liner that the people decide on; that's my question.

13 MR. FUHRMANN: I think that one liner has got a lot
14 of flexibility.

15 MR. WORHLFORTH: Has anyone used that terminology in
16 the charter?

17 MR. FUHRMANN: You will find in the charter, I
18 believe -- I'm sorry, I can't in my mind figure out which
19 ones there are. You've got the charters of the Islamic Bank
20 and the Kuwait Fund, and I think in both of them it's insisted
21 they be income producing, and the words themselves are used.

22 MR. MOTLEY: The reason I raised that question is
23 because it appears to me that the Permanent Fund is attractive
24 to some people because, in essence, it will be a negation
25 of use for public building and so on. You know, be that

1 valid judgment or not.

2 MR. FUHRMANN: Who knows?

3 MR. MOTLEY: That's right, but I'm just wondering
4 whether there are any as restrictive as that, because to say
5 it has a lot of latitude, I think there are a lot of people
6 out there that would say they've been had if they thought
7 that latitude was written into it -- they may not have voted.
8 And that's just a value judgment on my part.

9 MR. FUHRMANN: I don't think it's my position to make
10 an enormous number of comments on your question because I'm
11 not involved in the political decisions of Alaska, and I'm
12 not voting on this, nor have we been asked to recommend.
13 But if I were to view the language that you're voting on
14 on November 2, 3, whatever day it is, that language leaves
15 a lot of flexibility for people between now and the legis-
16 lation that we would anticipate you're working toward early
17 in 1977 to more greatly define what income producing means,
18 and I think at the last meeting there were discussions about
19 the fact that income producing can be one-tenth of one percent
20 or twenty percent.

21 MR. MOTLEY: My basic question was, how many speci-
22 fically restricted to income producing.

23 MR. FUHRMANN: I don't know how many, but I think if
24 you read through there you will find that it is specific
25 about about that.

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MR. MOTLEY: I tried to read through the purposes and I didn't see any that just said that.

MR. FUHRMANN: Don't look in the purposes, look in the section called portfolio.

MR. MOTLEY: It appears that one needs a road map, if you'd now give it to me.

MR. BUTLER: Some of the foreign funds, sadly enough, don't have a detailed written description on them, some of those subjects, to give them this flexibility I think that Charles mentioned, and sadly on short notice or just by reading what's available in writing it doesn't always point that up clearly.

MR. MOTLEY: Thank you, Mr. Chairman.

MR. WOHLFORTH: Representative Urion.

MR. URION: Well, if I haven't had a chance to read this I don't know if I'm ready to ask any intelligent questions. One thing I can't see here, did you make any judgment on how these funds have fared? I can read the portfolio, but I don't know in the monies they put in, the type of loans they made, and good and bad loans, or what.

MR. FUHRMANN: Most of them have done very well.

MR. URION: I can't read that in there.

MR. MOTLEY: Obviously the one you managed did better than most.

MR. FUHRMANN: No, we don't manage any of them, nor

1 desire to. Most of them that are dealt with in the inter-
2 national section are involved in loans and have government
3 guarantees. Some of them specifically state they will not
4 participate in restructuring bad loans, which is to say they
5 won't call upon the guarantee of the government behind the loan.

6 Others, National Financiera, the Mexican Development
7 Bank, has as a policy that they will participate in restruc-
8 turing bad loans, and they have had hundreds of them. What
9 they do is, they restructure the debt service, give interest
10 moratoriums -- there are all variety of things being used.

11 There are some Canadian funds now that are involved
12 in having made some investments which we are investigating
13 now exactly what they are doing with respect to them, and
14 they're somewhat sensitive about talking about what they're
15 doing. But we are in the process of discovering what they do.
16 But most of those funds have very good success, mainly because
17 they have the guarantees behind their investments. You know,
18 it depends.

19 You can survive on a performance basis forever as
20 long as you're willing to restructure the loan.

21 MR. MOTLEY: In other words, you have no delinquencies,
22 you just rewrite the deeds.

23 MR. FUHRMANN: Right.

24 MR. URION: Do we have in amongst the papers here
25 something that would tell us that?

1 MR. FUHRMANN: The annual reports of some of these
2 will have information.

3 MR. URION: The annual reports?

4 MR. FUHRMANN: Yes.

5 MR. URION: And what will be the statutes that sets
6 up the management structure and how the funds will be used?
7 Do we have any of those available?

8 MR. BUTLER: Yes, we have it specifically for the
9 Alberta Heritage Trust Fund and others.

10 MR. FUHRMANN: The Kuwait Bank.

11 MR. ODEN: And domestically we have them available
12 but there's numerous cross references, etc., etc. We've
13 endeavored to underwrite the pertinent sections. But we do
14 have those.

15 MR. URION: Do we have those?

16 MR. EDENSO: Mr. Chairman, if I might. Mr. Urion,
17 your Price Waterhouse report also describes the structure and
18 organization, and management control features of nine funds
19 that are involved in this, and some of the very ones that
20 they've talked about.

21 MR. URION: That's all.

22 MR. WOHLFORTH: Thank you. Mr. Thorstenson.

23 MR. THORSTENSON: Chuck, I'm missing page three of
24 your introduction to this as well -- I got page two mixed in.
25 My question, I guess, would be to Chuck. I felt when I heard

1 you say that politics becomes a problem in management of
2 these funds, particularly on a national level, more or less;
3 you mentioned some were very political and some were less
4 political. Would you recommend a way that this could become
5 less of a problem, particularly in our case?

6 MR. FUHRMANN: Right now I would rather not. I'd
7 rather not. I don't know whether you want to have it be part
8 of your political process or whether you want it to be separate.

9 MS. FLEISCHER: We haven't decided.

10 MR. FUHRMANN: No, you haven't decided.

11 MR. EDENSO: I'm getting out of line. Maybe you
12 could explain some of the political processes that have
13 occurred which have resulted in a structuring of some kind
14 of management entities.

15 MR. BUTLER: We can speak to that both domestically
16 and internationally, in that there is some parallel between
17 the United States and others.

18 MR. ODEN: With finite natural resources, a lot of
19 states had a severance tax or some other sort of royalty
20 that was coming in that up until 1973 was not that significant.
21 All of a sudden they find themselves with a tremendous source
22 of revenue. So states such as Montana, Wyoming and New
23 Mexico have created new programs, primarily under the auspices
24 of the Governor and the State Treasurer, and the management
25 of the funds in these are usually left to a certain degree on

1 a discretionary basis with broad guidelines produced by the
2 finance arm of the executive branch of these states. That is
3 the typical structure.

4 MR. BUTLER: For example, in New Mexico, and correct
5 me if I'm wrong, Pat, the fund is managed by the Governor, the
6 State Treasurer and four or five members appointed by the
7 Governor but approved by the State Legislature, but within
8 the very broad guidelines of the charter. Then they're
9 free within that to invest in any manner, and obviously that
10 could be quite political because the Governor is on the board
11 as is his appointee, the Treasurer, as are his other appointees,
12 and that's where the sole decisions lie. Monetarily it's
13 been a successful program to date as far as they have had
14 no losses.

15 MR. ODEN: It might be noteworthy that insofar as
16 the investments of the funds, the Texas Permanent Fund and the
17 New Mexico Permanent Fund are really the only two I came up
18 with a definite policy to invest in common stocks. The
19 others have sort of not learned their lesson, but have become
20 much more wary about investment in common stocks and have
21 by internal regulation limited themselves to income producing,
22 fixed income securities, primarily federal government securities.

23 MR. FUHRMANN: Most of them attempt or express that
24 they are above politics. They express that they are.

25 MR. WOHLFORTH: I would suggest that when we use the

1 term "political" or "politics", you know we run into a big
2 semantics problem. Do we mean politics - invidious, or
3 politics - of the political process? So why don't we try
4 and say which way we are using it? It might help save a
5 little time.

6 MR. FUHRMANN: Let's talk about where the people come
7 from that manage these things. Are they coming from the
8 political arena, are they politicians, are they involved in
9 representing the people either by election or by dictatorial
10 power, or wherever they got there, or are they out of the
11 business community or the investment community, are they
12 financial people, or are they agricultural types or engineers?
13 And to answer that question is to say that you will find funds
14 that had any or all of those or a combination of the above.

15 But the majority of them do reflect people from the
16 political community. They have either been there or they
17 are still there. But they will argue that their decisions
18 are taken irrespective of their political inclinations, whether
19 it's partisan or whether it's political philosophy, what we've
20 so quickly come to call liberal or conservative, or whatever,
21 but their decisions are taken objectively, and that they run
22 these things all on a businesslike basis.

23 What is most important, we feel, is that whoever
24 runs it must be answerable and responsible to the public and
25 easily identifiable and accountable. Otherwise the opportunities

1 for graft, mismanagement, etc. are enormous. I keep thinking
2 in my mind about the Venezuelan situation, where the manage-
3 ment changes about every three months. At first the reason
4 was because they were making decisions that were not
5 necessarily agreeable to the powers that be in the political
6 process, and later it was because the people themselves that
7 were put in those positions couldn't live with the bureaucratic
8 environment in which they were placed. Now it's because the
9 image of working there is considered so unattractive that
10 nobody wants to be involved. But they are working hard to
11 straighten themselves out.

12 I think we have very strong feelings that the group
13 or individuals involved should be people that are able to
14 judge and evaluate situations that structure, and must either
15 be in a position to monitor and evaluate their investments
16 or get people that can do it for them. We think that
17 this is a long run situation. That, I believe, is definitely
18 established here, that we're not talking about a temporary
19 fund, you're talking about a permanent fund and, therefore,
20 it is important that the people be "above" politics, Mr.
21 Chairman, because politics or political parties in power
22 would ever change and the fund is meant to be permanent and
23 to go over time. So we think the people should be people
24 of stature and run for all and on a businesslike basis.

25 But again, the most important thing, we think, is

1 accountability, and being able to answer to the people.
2 I think this is really what Price Waterhouse and we discussed
3 at length right after this.

4 MR. GRUENING: Mr. Chairman.

5 MR. WOHLFORTH: Yes.

6 MR. GRUENING: While we're on the subject, I'm curious
7 How do you reconcile being above politics as a goal and then
8 trying to be accountable? I don't think they're mutually
9 exclusive.

10 MR. FUHRMANN: Well, performance must be able to
11 be judged, and the person responsible for the performance
12 must be able to be evaluated. That's what I'm talking about.

13 MR. GRUENING: Politics doesn't -- decided by whom
14 though?

15 MR. FUHRMANN: What I mean is they shouldn't be
16 necessarily -- well, I don't know what I mean.

17 MR. LOVE: Sort of like what Eric was saying.

18 MR. FUHRMANN: Shouldn't be used as a favor to get
19 votes. The guidelines and objectives should be clearly
20 established so the person has an operating map from which
21 to work, and then the person identified, and then let alone,
22 subject to evaluation of performance. I don't know -- you're
23 asking us for recommendations which we're prepared to do at
24 some point in the future if we're asked to. But we haven't
25 been so far and really prefer not to. I think that there is

1 a responsibility here on the part of the Committee members
2 to give us some guidelines of where you want us to go.

3 MR. WOHLFORTH: We have time (probably in order not to
4 short-cut the next presentation) for one or two more questions,
5 and then we'll resume after the next presentation.

6 MS. FLEISCHER: I just can't resist pointing out that
7 it sort of bears out my point, the discussion we've had.
8 Mr. LeResche asked a question of applicability, and you don't
9 know which funds are going to be applicable, if any of them
10 are going to be applicable or if all of them are going to be
11 applicable, or which ones we look at until we know what the
12 purpose of our own fund is going to be. That's still, I think,
13 our number one task, we have to decide that before we know
14 how to evaluate anything. I think it is useful to look at
15 what other people are doing ahead of time to give us some idea
16 of the alternatives that are available, but ---

17 MR. FUHRMANN: Well, that is the purpose of this.

18 MS. FLEISCHER: Right, but we still can't really
19 discuss things until we know which direction we want to go,
20 and I do hope that management and structure would reflect the
21 goals and objectives and that is that we still have to know
22 that so we know how we want it structured.

23 MR. WOHLFORTH: Yes.

24 MR. LOVE: I'd like to know, based upon your experience
25 of studying all these different funds, foreign and domestic --

1 I'd like to know, when these funds were created in the first
2 place, the same task that we're going through right now, if
3 you could tell us a little bit about the processes by which
4 the different communities went through in developing the
5 funds, the amount of time it took them to come up with their
6 plans, the public processes they went through. I think that
7 might be very helpful to us in seeing some of the steps maybe
8 we have to go through here.

9 MR. BUTLER: In general, we haven't done that at
10 this point in that, as has been mentioned a couple times, we
11 don't have a lot of very specific guidelines to go on. This
12 was an overview and, Jamie, we frankly just have not gone to
13 that depth, especially as far as time and the exact discussions.
14 In some cases we do have in the source data here, for example,
15 some of the actual Congressional testimony or Legislative
16 testimony that went into creating some of these, in Alberta
17 and places like that. Some of this may be difficult, if not
18 impossible, to get from, say, the Middle Eastern countries
19 and things, as an example.

20 MR. FUHRMANN: Where they obviously grew out of sinful ban
21 types of arrangements, some of the different structures. But
22 we do have it in some cases, yes.

23 MR. LOVE: I would be interested at some point though
24 in some observations or information on that.

25 MR. WOHLFORTH: Proceed.

1 MS. FLEISCHER: Eric, could I? I forgot one of the
2 questions I wanted to ask. When we read the data from these
3 various funds are we to read purpose here as both objectives
4 or do some of these funds have other sets of goals and
5 objectives from which they've extracted the purpose, and I
6 do notice under "Portfolio", for instance, there is a lot
7 of talk and most of these are about objectives. It doesn't
8 say exactly what the objectives are.

9 MR. FUHRMANN: I think that you can remember that
10 these are summaries.

11 MS. FLEISCHER: Right.

12 MR. FUHRMANN: And there is more extensive information.

13 But I think you're going to find that those summaries
14 are pretty all inclusive with respect to objectives. So you
15 will see the flexibility that is built into the language of
16 the law or charter, but not necessarily in the operating
17 policies that actually govern. Most of them are subject to
18 policies that have been set on a continual basis by a board
19 that meets regularly, which board is either made up of people
20 from the political process or representatives of the various
21 nations that are involved as investors, or a group of some
22 from people within the fund themselves who are managing it
23 and people from outside who may be citizens and/or part of
24 the political community or the business environment.

25 MR. WOHLFORTH: Commissioner.

1 MR. GALLAGHER: One of the things you said was that
2 you didn't see the relevancy, in answering a question over
3 here, the relevancy of some of the international boards, and
4 maybe you should rethink the question and ask what is the
5 constituency of the board. I think that a lot of them are
6 very relevant in that if you examine what their constituency
7 of the management is, it was a very broadly based constituency.

8 MR. FUHRMANN: Maybe one man from Switzerland, one
9 man from England, one man from France, because England, France
10 and Switzerland were contributors of the equity of the fund.

11 MR. GALLAGHER: Right and, in fact, we in this case
12 have got a broad political support, and the support comes
13 from all sectors of the state. Now, if you go back and
14 examine that, your management structure ---

15 MR. FUHRMANN: I see your point, but I think that
16 you will find that there are funds that are more similar that
17 have done what you're saying, where they have pulled people
18 from representative groups, be it knocking it down from the
19 level of nation, to the level of state and the level of county.
20 Your point is the broad base representation.

21 MR. BUTLER: We'll be happy to pursue that in more
22 depth, and at this point are looking for this kind of sug-
23 gestions and guidance to home in from here.

24 MR. FUHRMANN: But it's obviously a natural board
25 that is created when you have twelve countries participating.

1 It's obvious who the twelve board members are going to be,
2 one from each nation.

3 MR. GALLAGHER: It's obvious but, you know, that comes
4 back from their constituency, namely, those countries that
5 are involved.

6 MR. WOHLFORTH: Jim.

7 MR. EDENSO: I think I would like to defer asking
8 any questions until after other members of the board have had
9 an opportunity to explore with you what you've explained to
10 them concerning the other funds, and also in the interest of
11 moving on until we get to the point of the next report.
12 So, Mr. Chairman, with your permission ---

13 MR. WOHLFORTH: I think it might be well, unless the
14 other people here would object seriously, that we go on to
15 hear the Price Waterhouse and then resume questioning on the
16 other side of the table. You'll have the benefit then of two
17 things to respond to. We will recess you gentlemen subject
18 to call.

19 MR. BUTLER: Thank you. Could I ask a question?
20 There could be a problem of how do we gain access to some of
21 the background material?

22 MR. WOHLFORTH: I presume it will be in your office,
23 Jim.

24 MR. RHODE: Yes, it will. Sir, I was going to suggest
25 that if we could have one set here in Anchorage then people

1 could reach me and I'll be glad to supply copies.

2 UNIDENTIFIED: Where can we reach you?

3 MR. RHODE: Our office is in the Dawson Building at
4 Sixth and K, number 30, and the phone number is 277-2423.

5 MR. WOHLFORTH: This is the point in the agenda where
6 we're going to hear from Mr. Peter McDowell of Price Waterhouse
7 and Company accompanied by Mr. Dan Regis, who is the resident
8 Anchorage partner, to report on the organization, management
9 and control of development banks and you have, I think, in
10 hand his report. Go ahead, Mr. McDowell.

11 MR. McDOWELL: Thank you, Mr. Chairman. It has been
12 brought to my attention that there may be a few of our guests
13 in the audience who don't have the full background on our firm.
14 If I could just take 30 seconds I'll explain it.

15 Briefly, Price Waterhouse is an international C.P.A.
16 firm with departments for taxation and management consulting
17 as well as our normal auditing functions. Our background
18 for this particular study is that we are the auditors of
19 all of the development institutions that we've discussed in
20 our report, plus a number of others around the world, and
21 in addition I have been personally involved with the manage-
22 ment and the lending programs of the development institutions
23 for the last two and a half years. So we were asked, in effect,
24 to transfer some of this knowledge, based on these two sets
25 of client activities, to the Committee and to the state.

1 If I may, I'll report on what is in the hands of all
2 members of the Committee.

3 MR. LOVE: Not everyone is familiar with it but we've
4 all got it in hand.

5 MR. McDOWELL: Fine. If it would be all right, I'd
6 like to go through it from two directions, one the report
7 itself, the other I'd like to after that address some of
8 the questions which I've extracted from the minutes of the
9 last meeting.

10 The report is a report of five case studies, four of
11 which are specific institutions based in Washington, D.C.
12 We selected these four, the International Finance Corporation,
13 the World Bank, the Inter-American Development Bank and the
14 finance program of the U. S. Government's Overseas Private
15 Investment Corporation for detailed review, partially because
16 we know a great deal about the institutions and have a long-
17 standing client relationship with each of them and partly
18 because they are prominent, well managed and diverse and
19 generally are representative of the types of institutions
20 active in the development banking field.

21 The fifth case study concerns a class of institutions
22 which are normally organized in each developing country and
23 go by the term commonly of development finance corporations.

24 I have summarized our findings, particularly the
25 similarities among the five case studies. First, however, I

1 might define a development bank. Simply, it's a bank which is
2 like other banks that we're familiar with, with two or three
3 exceptions: (1) it does not accept deposits, (2) it is very
4 aggressive in the promotion of the projects to which it makes
5 loans or provides equity financing, it is active as opposed
6 to being relatively passive. The development banks then form
7 sort of a community in the financial area or markets of the
8 world with these differences, two differences, to normal banks
9 that we consider. But other than that the bulk of them are
10 managed and operated and established as commercial institutions,
11 as Mr. Fuhrmann and his associates explained earlier.

12 The report, and again I won't try to go through every
13 page, but I would like to highlight some of these points
14 and certain of these case studies -- if we could, start at the
15 last. This is attachment "V" titled "World Bank/IFC - Spon-
16 sored Development Finance Companies". I won't go through the
17 general statements of purpose and the philosophy sections,
18 but I would like in this case study to turn to the section on
19 relationships with governmental units. These DFC's are
20 normally national institutions, they are concerned with only
21 nation/state now rather than a group. Some of the problems
22 normally encountered by DFC's are those which I've indicated
23 on page four and five.

24 The relationships with their governments, which
25 normally are their owners, are (1) they cooperate closely

1 in order to represent private sectors during the development
2 of economic policies and plans by the government. They,
3 however, have an initial objective that they are expected to
4 maintain adequate profits and sustain their credit worthiness,
5 or in other words to sustain their integrity as financial
6 institutions, and make an important contribution to develop-
7 ment. That's the public policy goal that often causes them
8 to engage in compromises that an ordinary businessman wouldn't
9 countenance.

10 The governments apply pressures because they normally
11 own all or most of the stock and, therefore, are the stock-
12 holders. As with any corporation, they can dilute the
13 independence of these institutions in many ways, and I've
14 listed three of these; pressure to hold interest rates below
15 market and, again, most of these institutions survive on some
16 capital and from funds borrowed from other sources; pressure
17 to consider projects which are too small for economic invest-
18 ment and, perhaps, are too risky; and pressure to fund
19 projects in least developed regions.

20 Now, I think as our discussions took place this
21 morning all or some of these items, you can see, could be
22 situations faced within the State of Alaska.

23 The influence, which is political influence, govern-
24 mental influence, can easily become interference with manage-
25 ment decisions, and this is where you have a problem. Most

1 of the DFC's organize to be independent as far as management
2 decisions on investments, staffing and internal administration
3 are concerned. These are the three keys to having a well
4 managed institution.

5 So, pointing out in terms of relationships with
6 governmental agencies, the DFC's probably have the most
7 direct of these five case studies. Even OPIC doesn't have
8 such direct influence, although it is a creature of the United
9 States Government, as far as the chance or the probability
10 of interferring with its day-to-day operating decisions.

11 The fourth case study, which is the Overseas Private
12 Investment Corporation Finance Program, is also interesting
13 in terms of some of the exceptions that it encompasses to the
14 normal structure and control of a development bank. Its
15 sources of funds are U. S. Congressional appropriations and
16 proceeds from its own operations. In addition, it has
17 authority to guarantee loans to a far greater amount than it
18 has authority to make direct loans. So it's a guarantor of
19 other people's loans in many more instances than it actually
20 makes loans itself. That's a difference. The others tend
21 to strictly make their own loans; although most have their
22 guarnatee power, they don't care to exercise it.

23 The relationships with government are, I think,
24 interesting as well. OPIC is a corporation of the United
25 States Government. It's subject to review about every four

1 years through the Congressional authorization processes.
2 Congressional oversight is, in effect, directed toward it.
3 It has its own Sunset Law. Every four years it comes up and
4 the question is asked, "Should OPIC continue," by the Congress
5 and so far it's been answered positively the one time they've
6 been through the cycle. It comes up again in 1978.

7 Selection of its board, senior management and staff
8 is a very closely related governmental function. There are
9 six members of the board of directors from the private sector
10 and OPIC's president, directly appointed by the President
11 of the United States and confirmed by the U. S. Senate.
12 The four other government directors hold specific posts in
13 the current administration. The private sector director can
14 serve a three-year term, and they have rules about expiration
15 so that the appointments and expirations of directors' terms
16 occur on a staggered basis.

17 The first three case studies, I think, will probably
18 reflect similarities than exceptions. The World Bank, the
19 International Bank for Reconstruction and Development, is
20 really the first of the species. It was founded for two
21 purposes (1) to assist in reconstruction after World War II,
22 which that job has been over quite some time, and (2) to assist
23 in the development of economic development of under-developed
24 countries, which is the role it's been carrying on for most
25 of its life. The Inter-American Development Bank was formed

1 at a later date to, in effect, in response to the need felt
2 by countries in Latin American that the World Bank was fine
3 and they liked the loans and they liked the projects but
4 they weren't getting enough and, therefore, they preferred
5 to have in addition to the World Bank their own bank. We
6 in the United States agreed and provided a substantial portion
7 of the initial capital for that.

8 The International Finance Corporation is again a
9 later development. If was found that the World Bank could
10 not and did not wish to deal in the private sector directly
11 and its member countries, and the International Finance Cor-
12 poration was established as a related institution, in some
13 ways a subsidiary, but a related institution to deal solely
14 in that sector. It's quite small, it's a very small institu-
15 tion compared to the main bank itself.

16 The summary of our findings, if I may, I would like
17 to go through and just point out a few things. Of the five
18 case studies, some of the similarities include (1) they all
19 have a common purpose to provide loan financing for high
20 priority economic development projects in developing countries.
21 The IFC and OPIC -- IFC also provides equity and OPIC also
22 provides loan guarantees. None of them make small loans.
23 All of them make loans that are relatively large and, as
24 stated earlier, they pass on funds to specialized intermediaries,
25 generally the DFC's in individual countries and they, in turn,

1 because they're a smaller scale operations, are able to make
2 loans to small businesses and small government projects, and
3 do it on a reasonably economic manner. The problem with it
4 is that the operating costs of an institution like one of
5 the larger development banks is relatively high because they
6 have extremely competent people who are well paid in order
7 to retain them, and it could very well be that you could spend
8 a minimum of a Hundred Thousand Dollars in staff time putting
9 a loan together. If the loan is a Hundred Thousand Dollars
10 the cost benefit ratio just doesn't work out to make any
11 sense.

12 The operating philosophies are similar, they're all
13 aggressive in project promotion, preparation and design
14 activities to far greater extent than normal commercial
15 banking institutions. They are also all run on a prudent
16 and businesslike basis, and most frequently the word "prudent"
17 is that which is included in their charters to indicate that
18 they should be run on a commercial businesslike basis. The
19 charters are relatively general, but "prudence" has been
20 interpreted by the institutions to mean just that. They're
21 expected to generate revenues adequate to fund their operating
22 expenses, including the costs of borrowed money, and to
23 provide some profits to insure security and growth as con-
24 tinuing institutions.

25 The institutions tend to be independent from their

1 governments, with the exception of some of the development
2 finance companies. But the general range is that they are
3 independent to a fairly great extent as far as day-to-day
4 management and operations are concerned. Each institution
5 is organized with boards, boards of governors and/or boards
6 of directors, and a strong chief executive officer. Again,
7 this is a crucial factor in the success of these institutions.
8 They universally have strong chief executive officers who are
9 delegated substantial powers to manage the institutions.

10 Related to one of the questions that came up earlier,
11 the stockholders -- each of the institutions is effectively
12 a corporation. As with any of our corporations in this
13 country, the stockholders have the ultimate power. Now, in
14 their case you often see two boards, the first board being
15 the board of governors. Well, the board of governors, in
16 effect, votes on those same issues that our stockholders of
17 a normal U. S. financial or commercial corporation would vote
18 on. They are the stockholders, as persons. They represent
19 the governments which own the shares, but they are in effect
20 the stockholders. If you send out a prospectus to the
21 shareholders of the corporation that you're involved in and
22 ask them to vote on something, the boards of governors would
23 in fact vote on those matters. They delegate their powers,
24 with a few exceptions, to operating management which begins
25 with another board, a board of executive directors. That

1 board is part of a line management and they are approximately
2 the equivalent of our normal corporate board of directors
3 as we might have in this country, plus some of the functions
4 that are normally ascribed only to our individual management
5 executives. They're kind of a quasi-combination. They look
6 much more like a British board of directors than a United
7 States board of directors.

8 The British have a system where their boards are
9 made up mostly of the internal management with a few outside
10 directors. But that board is an executive board that meets
11 daily, weekly, whatever is necessary to run the organization.
12 That's in effect what the board of executive directors does
13 in a development bank.

14 The chief executive officer is chosen by one or the
15 other of the boards; there's no consistency; he's chosen by
16 one of the boards, normally the board of executive directors
17 or the equivalent; in one case by the board of governors.
18 In all cases key senior management, starting with the chief
19 executive officer and the professional staff personnel, are
20 selected by the board or chief executive officer or his
21 delegated executives. The only exception is that in OPIC
22 the portion of the staff below the professional level is hired
23 and paid, and remunerated, and dismissed and so forth under
24 U. S. Government Civil Service Regulations. The key posts
25 are exempt; in other words, there are no exceptions to that

1 rule.

2 The institutions share common control structure.
3 I think this is a crucial area, and as I go through another
4 set of rhetorical questions that I hope to be able to answer,
5 I'll go through the controls in more detail. But each of
6 the institutions is organized to provide an adequate separation
7 of duties and numerous levels of loan and investment review
8 and approval, and I'll go back to why in a moment.

9 Final responsibility and accountability clearly rests
10 with the board and the senior management in every case, and
11 their accountability extends to public accountability in all
12 instances in the specified institutions and in many instances
13 in the DFC's. To a minimum, audited annual reports are issued
14 to their stockholders and to the public. In addition, all
15 major institutions carry on very comprehensive voluntary
16 public information programs.

17 The World Bank and the World Bank group, I think,
18 publishes a thousand, two thousand documents a year concerning
19 themselves, and there's very little that you can't find out
20 about these institutions in terms of their goals, objectives, and
21 their lending programs that isn't published by them in one
22 form or another.

23 Now, if I may go back, I reviewed the minutes and
24 I said, "Now, what directly, what were some of the concerns
25 that the Committee appeared to express at its August meeting?"

1 If I can be so presumptuous as to outline some questions and
2 the answers as defined for this kind of institution, I will.

3 The first question is, how do you insure political
4 influence is minimized in the loan or investment operating
5 process. I'm not stating and I don't think you're stating
6 that political influence should not exist. This is a state
7 corporation, or a state creation; but how do you keep it out
8 of the loan and investment operating process. Well, all of
9 them have done this partly by creating an independent corporate
10 entity with all of its operating functions, with the exception
11 of the International Finance Corporation which, as I said,
12 is a subsidiary of the World Bank to some extent. The others
13 have all their functions, they have all the functions of a
14 bank. They have their lending operations, they have their cash
15 management operations, they in effect control their own liquid
16 assets, they make their own borrowings as independent insti-
17 tutions. But the crucial thing is that they have all of
18 their operating functions self-contained as to the day-to-day
19 management decision making. That's the key. In other words,
20 if you put into a charter that a certain item that's crucial
21 in the management of one of these institutions and it's not
22 granted to that institution, you probably are going to create --
23 you would create problems, or at least these institutions tend
24 to be successful, I believe, partly because they are independent
25 corporate entities.

1 Another thing is to delegate all operating respon-
2 sibilities from the stockholders to a board of directors
3 which represents enough diverse interests so that no single
4 outside agency or group can control decisions of the board.
5 I think OPIC is probably the best example of board selection
6 to do this. The majority on the board of sic is from the
7 private sector. There are four Presidential appointees
8 who are also on the board, there's the president of the
9 institution itself, and then there are the five (shall we
10 call them) outside directors. Half the board is outside
11 directors.

12 The U. S. Government cannot make a board decision.
13 Essentially they do not have a majority on the board. They
14 have a strong input, they've got 40 percent plus the president,
15 but they cannot make a final loan decision or investment
16 decision without the concurrence of at least one member
17 from the private sector. So there is a situation where your
18 board is diverse enough that no one has the controlling interest
19 in the vote, controlling power over the vote.

20 The international banks, as we've pointed out in each
21 of these case studies where we have the information, the
22 largest single stockholder, in other words the largest amount
23 of voting power, is about a quarter. It happens to be the
24 U. S. in each case or the World Bank and IFC and Inter-American
25 Development Bank. The United States government cannot

1 control the lending decisions, the operating decisions of
2 any of those institutions, unless it gets another 25 percent,
3 26 percent of the vote to go along with it, and that's quite
4 a number of countries.

5 Now, there are many other factors involved in insuring
6 this kind of thing to insure any political influence is kept
7 out of the operating process. Then the alternate side of
8 the question is, how do you insure that adequate political
9 influence is exerted in the policy making process; because
10 again we come back to the fact that these are all government
11 created institutions.

12 The first thing they tend to do is lay out objectives
13 in the charter for the institution, objectives and an operating
14 philosophy. Simply said, the bank will make loans for
15 development projects in less developed countries and it will
16 do so on a prudent basis. That's a simple statement of the way
17 most of their charters are written, just about that general.

18 But second, only ultimate powers are reserved to
19 stockholders, but the fact is ultimate powers are reserved
20 to the stockholders. The stockholders have the power to change
21 the articles of incorporation, they have the power to liquidate
22 the institution, and they have the power to elect the directors,
23 select and elect the directors, two in effect staggered and
24 partially insulated terms but yet they still have all of
25 these ultimate powers.

1 In accordance with the way the Constitutional
2 Amendment is written regarding the Permanent Fund, the
3 Legislature of the State of Alaska appears to have the first
4 of these two powers, the power to change the articles of
5 incorporation (because this thing is established by legislation)
6 and to liquidate the institution. The third power, the
7 election and selection of the directors can certainly be
8 shared among -- well, in the first two powers subject to veto
9 by the Governor. The third power, that of appointment of
10 the directors, can certainly be shared subject to guidelines
11 provided by the articles of incorporation and, in fact, in
12 all these cases it is.

13 You have, obviously, in these very general but final
14 powers, you've got a lot of opportunity for insuring that
15 adequate political influence is exerted. But you also have
16 the opportunity by structuring an independent corporation
17 with certain other features to make sure that that political
18 influence stops at the policy making level and is not exerted
19 at the operations level.

20 Another question which I extracted is, what can be done
21 to insure that high standards of credit worthiness of borrowers
22 and project viability are maintained. The first requirement
23 along this line, again a general one, is all of these insti-
24 tutions are required to be prudent, and that's interpreted
25 as making enough income in total, not necessarily from any one

1 project, to pay their operating expenses to provide for
2 reserves against bad debts and losses, and normally to put
3 the rest of it (if there is any left over) into capital so
4 that their borrowing and lending power can be increased.

5 The second major area that they observed is that they
6 have competent management and staff, and they insure that
7 they have competent management and staff. How is it done?
8 Primarily they structure a strong chief executive officer,
9 as I've stated before, and give him, subject to the approval
10 by the directors, the power to hire, dismiss, organize, and
11 pay the staff of the institution. That's a crucial factor,
12 that you have the people of high quality.

13 Now, what will these people of high quality do? Well,
14 I think, if I may, I'd like to direct your attention to
15 Attachment II, which deals with the World Bank and move to
16 page eight. This is probably the ultimate in what a develop-
17 ment bank can and does do to insure credit worthiness and
18 project viability. This is an institution, incidentally,
19 which has a requirement that all of its loans are guaranteed
20 by the government of the country in which the loan is made.
21 So they don't need to do any of this. Yet they feel that
22 to do their job, to be active, development of an active
23 development force, that they must go through this standard
24 of activity which, again, is the highest standard that you
25 will find.

1 Page eight, we discuss the control that the board
2 of executive directors provides. They must approve all pro-
3 posals for loans, borrowings, budgets, reports and policy
4 issues before they are implemented. They also have standing
5 committees and, again, we mention the audit committee, and
6 three different audit agencies report to that audit committee
7 of the board of directors rather than to the management of
8 the bank. So the board of executive directors is final
9 approval. It also has reporting to it several of the outside
10 checks on the activities of the management and staff.

11 Let me go on to operating controls, starting on page
12 eleven. What are the operating controls built into this
13 bank? Again we've described these on the basis of our interest
14 as auditors and our information as auditors, as well as our
15 review of documents and discussions with key executives.
16 They use budgets and they use long range plans. Three dif-
17 ferent departments review credit worthiness of borrowers.
18 Project loan preparation follow-up is extensive. I go through
19 some of the phases that they're involved with. Again this
20 is the activism in development that is characteristic of a
21 development bank. They separate again duties of all sorts.

22 Another question, and this really falls into the
23 last one; how do you determine priorities. How are priorities
24 established for industries and among projects? This is a
25 crucial thing. They have limited resources, and I assume that

1 eventually the Alaska Permanent Fund will find that its
2 resources are probably limited relative to the total needs
3 it could be serving. The institutions go through extensive
4 economic analysis themselves. They are a key force in
5 economic analysis for the economies of their countries in
6 which they are investing or loaning money.

7 The DFC's, the case study five, are closely involved
8 with government economic planning in most of the countries.
9 Most have planned economies to a significant extent and they
10 have then priorities established by the government for which
11 sectors are to be emphasized and then later on which projects.
12 The other means of establishing project priorities, particu-
13 larly among projects, if you only have one project it's
14 obviously the highest priority. You must have a variety
15 of projects to look at to be able to rank them in order of
16 priority. The aggressive, the active promotion of projects
17 with extensive participation in their design and implementation
18 is the other source of priorities.

19 How are projects identified? This is a related
20 question. Well, two ways. They're brought to the attention
21 of the institution by the prospective borrowers and they
22 are also brought to the attention of prospective borrowers
23 by the institution itself. So there is a two-way communications
24 flow.

25 Again, these are just three questions that appeared

1 out of the minutes and, if I may, I'd like to stop at this
2 point and entertain any questions that the group may have,
3 and I'd be glad to refer to any section of the report or
4 try to answer any questions related to it.

5 MR. WOHLFORTH: Do you want to lead off, Jim, or
6 do you want to wind up afterward?

7 MR. EDENSO: I'd like to defer to other members of
8 the Committee.

9 MR. WOHLFORTH: Martin.

10 MR. PIHL: I made a note of a couple of question
11 areas. I'm not sure whether you want to answer one of these
12 or whether Ken Butler might, or his group might. One has
13 to do with foreign investment and whether these funds are
14 used to, you might say, control your own destiny, touching
15 on a matter that Bob Thorstenson brought up about foreign
16 investment coming into the country and whether you see in
17 these cases whether there is any play or role in the control
18 of investment, in capital, that is made.

19 MR. McDOWELL: I think if I can respond in two ways --
20 if you look at the flow of capital to developing countries
21 on a world-wide scale, I don't believe that the development
22 banks themselves create new capital. I think they divert
23 capital. The World Bank again being the best example, the
24 World Bank goes to the U. S. capital market or to the URAL
25 currency market, or to the Japanese Financial Market, and it

1 borrows money. I don't think it creates any new capital
2 because it doesn't have the functions of a regular bank in
3 that sense. It takes capital which probably would have gone
4 to an alternative use in the U. S. or Europe or Japan and
5 diverts it through development projects to the developing
6 countries. So they are, in effect, quite instrumental in,
7 as you say, controlling the destiny of what happens in any
8 one of those individual constituent countries.

9 MR. PIHL: In this case we're starting with the
10 capital.

11 MR. McDOWELL: Then you're not even removed. They're
12 removed by one institution from the capital itself. The
13 big institution marshals the capital and then spreads it out
14 through the governments in essence. In the case here you
15 don't need anyone else to marshal the capital for you. You
16 have the resources and you have the credit as a state to do
17 that, and given that, again I don't believe in a world-wide
18 scale they actually create new capital, I think they just
19 divert capital. Perhaps there's an analogy in the Alaska
20 situation. Perhaps you have the opportunity to divert capital
21 into Alaska that may not come here otherwise.

22 MR. PIHL: The second question or area, you mentioned
23 security and growth of the fund. Do the funds try to maintain
24 a growth that's equivalent to a long-term inflation rate,
25 for example, or when you speak of maintaining the integrity

1 of your fund, Two Billion Dollars by 1985, it's got to grow
2 by a certain percentage to remain permanent. Do the funds
3 try to do this?

4 MR. McDOWELL: They try to. They're not all successful.
5 They all make enough money to pay their operating expenses,
6 including the costs of borrowings, and to set aside, in the
7 cases of those that don't have the government guarantees, to
8 set aside reserves for bad debts so that you don't shrink
9 your capital by losing it. They haven't been necessarily
10 completely successful in countering inflation. They do make
11 some contribution toward the erosion of capital by inflation,
12 but in most cases they don't necessarily overcome that com-
13 pletely, and it isn't considered to be one of their over-
14 riding objectives.

15 So they maintain their integrity as best they can.
16 You look at them over a 40 or 50 year period, their capital
17 has been eroded by inflation, you know, there's no two ways
18 about it. But their social purpose -- in other words, the
19 definition of "prudence" only goes to a point and then it
20 becomes more important -- that you're prudent up to a stage,
21 that stage being not to let the capital deteriorate very fast,
22 although it's probably going to a little bit. Then beyond
23 that their objective is to get the money out there, to get
24 as much money out there as they can, at rates that the
25 countries can afford.

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MR. PIHL: Thank you.

MR. WOHLFORTH: Bob Barnes.

MR. BARNES: A brief question on the organization and controls. You went through quite a description of that, and it seems that they're very elaborate, which creates a large bureaucracy, which creates a lot of overhead and makes it uneconomic for the small loans. That's the natural progression?

MR. McDOWELL: Well, it's not necessarily the size of the staffs that makes it uneconomic to do small loans. It's a combination of the operating philosophies, that is to be active in all stages of the project, definition, development and implementation, which runs your operating costs up. The other is the fact that their staffs are very highly qualified and, by virtue of that, to retain them they're well paid. They don't have that many employees per dollar, but they do have high paid employees, and they do spend a lot of man hours on any given project.

MR. REGIS: Peter, is it not also a fact that they're after this role in order to search and ferret out the market opportunities that this becomes a more costly endeavor, if it's to be anything except a passive role?

MR. McDOWELL: It's always a two-way -- projects come both ways, from them out and from others to them, and they prefer to have them coming from both directions. If you look

1 back at the way they operate, if you go back far enough into
2 the origins of the lending program for any particular country,
3 it's probably the majority of the projects probably have come
4 out of their institution rather than the other way around.

5 MR. BARNES: Has there been a problem in any of these
6 organizations with the so-called strong executive concept
7 such as McNamara at this point is too strong to be accountable
8 to anybody?

9 MR. McDOWELL: No, he's accountable because the
10 ultimate power in these institutions is -- because there is
11 some erosion of capital, unavoidably, in the way they
12 operate and the way they're set up, and because a strong
13 chief executive would normally like to see his institution
14 expand profitably, but to see it expand. The member govern-
15 ments can put the check on him, which they've just done, as
16 a matter of fact, by saying, "We won't increase the capital.
17 Your leverage ratio is set, we won't raise that either. We
18 don't think it would be prudent, and you'll be held to your
19 proper size," and this just occurred in the last three months.
20 It was primarily, interestingly enough, the United States
21 Government that took the lead. But again, even we don't have
22 the power by ourselves. We had to persuade a number of
23 other countries to join us on that issue.

24 MR. BARNES: I have one last question but I think
25 it's really on New Mexico and I think maybe the White, Weld
group could answer that. I notice that there are two funds

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1 that are handled within the state treasury operation. Do you
2 know if they have a large staff or if they have a relatively
3 small staff?

4 MR. FURHMANN: They have a very large staff.

5 MR. GALLAGHER: The State Treasurer there is a doddering
6 old man.

7 MR. FUHRMANN: I believe by a very large -- it's
8 like about thirteen hundred people or something, in round
9 numbers, if I'm not mistaken.

10 MR. McDOWELL: This is interesting, I think. Back
11 in Attachment V on DFC's I gave the upper limits of size of
12 the DFC's as a group, and I said they go up to three thousand
13 employees and they go up to Three Billion Dollars in lending.
14 Well, the one with three thousand employees is not the one
15 that lends Three Billion Dollars. So they vary all over
16 the map, but then there are totally different employment
17 objectives in the developing countries than we would even
18 consider reasonable here.

19 MR. FUHRMANN: The Mexican one actually acts in many
20 cases as the finance department for the corporations they're
21 involved with, so they have enormous responsibility to the
22 companies that ultimately get the funds. At the same time,
23 the National Financiera, itself, cannot do anything without
24 going to the Minister of Finance for approval in a sense of
25 its raising its own monies, etc., because they don't want

1 to be competing with the government's financing in the market-
2 place. So they have a cue all the time as to who is going
3 to be raising the money.

4 MR. McDOWELL: Just one more point, Bob. The crucial
5 control is that these institutions are expected to earn a
6 profit. Again, it may not be adequate to offset all infla-
7 tionary impacts, but that chief executive has got to make
8 money, and normally there's a lid on the interest rate they
9 can charge. So his only flexibility is in his operating
10 costs. He's got to manage his organization so that there is
11 a spread adequate to at least pay expenses and to provide
12 a return that is prudent, shall we say; so you do have a
13 control.

14 MR. BUTLER: I'd just like to point out I brought an
15 article on this recently from the Wall Street Journal called
16 "Man with a Mission" and it's about Mr. McNamara and the
17 World Bank, about a week ago, and the recent meeting of the
18 INF in Manila and all. In one little paragraph here, apparently
19 there's some question about whether they are earning a profit
20 or how this is measured. This is a little bit out of context,
21 but it says, "The U. S., Britain, West Germany, Japan and
22 France, the bank's largest shareholders, there's a question
23 of whether or not the McNamara management, preoccupied with
24 pumping out ever larger loans, has paid sufficient attention
25 to the bank's financial soundness. It was this concern that

1 prompted the U. S. to lead a quiet but successful campaign
2 this year for internal changes to slow the pace of lending
3 and insure that the interest rate the bank charges on its
4 loans is higher than its cost of borrowing." I think that's
5 what Peter was alluding to earlier. But obviously some
6 people in the some of the nations with money at stake here
7 are somewhat concerned about the recent trends.

8 MR. McDOWELL: Yes, the shareholders have just made
9 Mr. McNamara accountable in a very direct way. That's
10 probably the best description of it.

11 MR. WOHLFORTH: Representative Gruening.

12 MR. GRUENING: The last time I saw McNamara he was
13 pointing at a map of Vietnam. I have a question on what
14 Bob LeResche raised earlier about whether the source of the
15 funds really was relevant, and I've been thinking on that
16 for the last hour. In the Alaska situation the funds will
17 be the natural resources, and as I understand the World Bank
18 it's borrowed money by and large, and it seems to me that
19 responsibility to the shareholders in the Permanent Fund case
20 is somewhat different in that the shareholders in Alaska would
21 be all of the citizens who have a right to that resource.
22 So I'm wondering whether the political control aspect, does
23 that change your thoughts on the management, how far down
24 policy decisions should go in terms of political control?
25 I mean, if the Legislature is, in fact, and the Governor,

1 ultimate policy makers, would that change your thoughts at
2 all as to how far down in terms of policy? To me it's a
3 fine line, where policy and management breaks off. Would it
4 influence your thinking any as to where that line would be,
5 given the fact -- and I think that the source of income is
6 important.

7 MR. McDOWELL: I think ownership is important.

8 MR. GRUENING: Okay, maybe that's better.

9 MR. McDOWELL: I think that in each of these cases,
10 with the exception of the DFC's -- the DFC's has stockholders
11 more like any corporation does. Unless they're a hundred
12 percent government owned they've got 5, 10, 20 stockholders.
13 They might have the IFC, they might have First National City
14 Bank, each, say, with a seat on the board or the right to a
15 seat on the board. At least they've got some votes as far as
16 their shares are concerned. In the other cases there's not
17 quite the direct analogy. Not only do we have the direct
18 analogy here. The stockholders of the Alaska Permanent
19 Fund, I agree with you, are the citizens of the State of
20 Alaska.

21 Now, just as the World Bank has a board of governors
22 appointed by the stockholders, I would suspect that some device
23 of this kind is going to be necessary because you can't have
24 all 450,000 people on the board of directors. You've got to
25 narrow it down. Now, who do you choose? You, the Legislators

1 and the Governor and some of the other executive officers are
2 elected by the people to represent them in most matters,
3 perhaps including this one. If you do, then you've got a
4 logical structure you can just grab right away at this top
5 policy level. Or perhaps you'd like to spread it out through
6 some other channel and say, "Well, if we get 12 or 15 people
7 who are representative of the population of the state, then
8 they can represent the stockholders, they can be our board
9 of governors," in the analogous situation.

10 MR. GRUENING: Do we need a second board of directors?
11 In other words, the Legislature in itself is a board of
12 directors. But just thinking out loud here, do we need that
13 second peer board? In other words, if I understand you,
14 the Legislature would be involved but through a board, they
15 would have some kind of control over a board.

16 MR. McDOWELL: Through the appointment and perhaps
17 process, but I think that the line stops at who decides
18 whether or not to grant a loan. That process should not be
19 directly impacted by -- I don't believe it should be directly
20 impacted by the stockholders. Again, let me use the general
21 phrase, because I'm not sure which body you will eventually
22 decide to pick to be called the stockholders, or represent
23 the stockholders. You've got to go one more step down, and
24 then that next group should have that power.

25 MR. GRUENING: Just one more question. I was thinking

1 that it appears in the Alberta Fund that the Assembly there
2 has some kind of committee that has something to do with
3 the loans. I don't know whether they actually approve the
4 loans or not, but would it be going too far down to have a
5 system where the Legislature approved loans over a certain
6 amount or certain special loans? For example, we could
7 set goals here, but then you have the problem of which goals
8 over a period of time take priority. I see that five years
9 from now one goal would be more important than another, and
10 the Legislature may disagree with that certain policy and,
11 being elected by the people, may decide, "We want to emphasize
12 this goal." Could you see a situation where the Legislature
13 would say, "Okay, we don't want to see a loan of this amount
14 in this policy area"?

15 MR. McDOWELL: I think you'd be into operations at that
16 point, but if you -- perhaps if you -- you have left the
17 power with the Legislature, in effect, to create and then
18 to change the articles of incorporation. Now, taking just
19 a look at the general statement of purpose for the International
20 Finance Corporation, for example -- no, that's not sufficiently
21 restrictive. Let me pick one that is.

22 The purpose of the Overseas Private Investment
23 Corporation is to encourage economic and social development
24 in approximately 80 lesser developed countries considered
25 friendly to the United States. That's a major restriction on

1 their lending because there are 120 developing countries, and
2 only two-thirds of them are eligible for OPIC financing.
3 Now, that statement was created by the United States Govern-
4 ment, and they can change it tomorrow, and they can change
5 it during the next session if they wish, to include the other
6 40 who aren't friendly or to cut it down to 40 who are the
7 most friendly. Just this one example, that's a tight
8 restriction compared to what most of these institutions have.
9 But, again, it's a direct creature of the United States Govern-
10 ment, and the U. S. Government has the power and the right
11 to set that kind of restriction any time it wants, as the
12 Legislature of the State of Alaska has with the Alaska
13 Permanent Fund.

14 The other problem is because, if you take an opera-
15 tional decision and transfer it up too far, then you cannot
16 hold the management of that institution accountable; you've
17 just destroyed their accountability by assuming it at another
18 level. You know, you can't hold them accountable. I mean,
19 I would assume that if you did create a fairly strong chief
20 executive officer type organization, and he and the board of
21 directors, which is the operating board of directors,
22 which is representative of the various groups, should be
23 representative of the various groups in the state, decide to
24 make a loan and then that's called back at some later date,
25 he would probably resign because you can't hold him accountable

1 for his results anymore.

2 MR. FUHRMANN: Can I comment on Clark's question
3 with respect to Alberta? The Alberta has, if you remember,
4 percentages of their fund that limits the amount that can go
5 into what we have been terming here in the last two meetings
6 as soft loans or loans that don't really have a strong
7 economic return, and that's 20 percent of their fund. That
8 is standing, that rule sticks. That does not mean that 20
9 percent of the funds can be invested in soft loans by the
10 executive committee. The Legislature has to appropriate those
11 funds that go into soft loans. The Legislature can also
12 recommend loans of a more general nature and then the fund
13 will put monies into those loans, so the Legislature does
14 participate as a recommender and a recommender with full
15 authority. Once they recommend, that loan will be made,
16 but it will be structured by the executive committee and the
17 operating people. So they do in Alberta, the Legislature
18 does maintain some participation in how loans get paid.

19 MR. McDOWELL: Which is really -- it's completely
20 similar to the normal governmental budget making and approval
21 process. It's really no different than having in the state
22 the Executive propose a budget to the Legislature, which
23 reviews it, modifies it and eventually approves it. So you
24 haven't really done anything different probably in a like
25 situation.

1 MR. WOHLFORTH: Doctor Logsdon, do you have a question?

2 DR. LOGSDON: Yes, I would like to get something
3 clear here now. Do these development banks borrow private
4 money?

5 MR. McDOWELL: Some do, yes.

6 DR. LOGSDON: Do they participate in equity?

7 MR. McDOWELL: In the case studies here, the Inter-
8 National Finance Corporation does, and normally, depending
9 on what they're supposed to do with the developing finance
10 companies, some of them will participate in equity. There's
11 no universal rule.

12 DR. LOGSDON: I wondered about this term, Development
13 Banking. I see an ad for a commercial bank that says, "We
14 are a Development Bank."

15 MR. McDOWELL: That's interesting.

16 DR. LOGSDON: What do you think they're saying? Are
17 they trying to identify those features of the Development
18 Bank?

19 MR. McDOWELL: I suspect not. I suspect they have
20 another concept of the term "development". I don't know;
21 is that your bank?

22 MR. BARNS: Yes. I don't suppose it's illegal, is it?

23 DR. LOGSDON: Well, I have an ad that I copied out
24 of a magazine that talks about, "We are Development Bankers,"
25 and they do participate in equity and take a very active part,

1 apparently, in the companies in which they invest.

2 MR. BARNES: This is not a United States Commercial
3 Bank?

4 DR. LOGSDON: It's a United States Bank.

5 MR. BARNES: It would have to be a private bank then.

6 DR. LOGSDON: And apparently a private bank.

7 MR. REGIS: Peter, the one bank in which equity
8 participates, that is as a vehicle for loans primarily is
9 it not?

10 MR. McDOWELL: Yes, the IFC's -- well, let me just
11 give you the numbers. Last fiscal year they made 225 Million
12 Dollars in loan commitments and equity financing of 20 Million
13 Dollars. So the one that does equity, it's still ten to one
14 on loans over equity.

15 DR. LOGSDON: We haven't heard anything about the North
16 Dakota Bank. Is there any relationship here between the North
17 Dakota Bank and this Permanent Fund?

18 MR. MOTLEY: North Dakota is no state bank.

19 DR. LOGSDON: Yeah, it's a state bank.

20 MR. GALLAGHER: It's the general fund of the state
21 treasury. It's a liquidity portion of the general fund and,
22 you know, they operate on liquidity purposes.

23 MR. LOVE: They make regular commercial loans though.

24 MR. GALLAGHER: Yes, but they're all federally
25 guaranteed and they're sellable, and that's a big difference.

1 MR. LOVE: It has a high rate of return, it's higher
2 than the top one hundred banks -- a higher rate of equity
3 last year, I think, than the one hundred largest banks in
4 the country.

5 MR. McDOWELL: There's no provision for loan processes.

6 MR. GALLAGHER: It's all demand deposits, that's one
7 of the reasons, and the demand deposit is the State General
8 Fund.

9 MR. LOVE: It's also very -- you know, we talked about
10 the employee thing, and I think it employs less than 90 people.
11 It's small in employees. It's a relatively popular proposal
12 in the bank, even among their really conservative Republican
13 dominants, who control the state.

14 MR. ODEN: Excuse me. I might add that we've been
15 in touch with the bank and they're sending a whole packet
16 of information, and you should have a summary sheet similar to
17 those you have within two weeks.

18 MR. WOHLFORTH: Dennis, you're next.

19 MR. WALDOCK: Yes, Mr. Chairman. First off I would
20 like to state that as soon as we all have finished asking the
21 questions of these various financial consultants that we
22 have here today, I have four questions that I would like to
23 direct to the Investment Advisory Committee itself. But
24 in regard to my question to whatever group would like to
25 respond to it, since you both have been involved with the

1 structure of a lot of the development corporations that you
2 have in your pamphlets that you gave us, and given Alaska
3 with its small population and great infusion of money,
4 projected possibly to be Two and a Half Billion Dollars by
5 1985 -- in other countries which had that large influx of
6 money with a small populace like we have, has there been any
7 cases where you've thrown into disarray the banking systems,
8 the regular, ordinary banking systems of those countries?
9 Let me go a little bit further. What I'm trying to say is,
10 let's assume, for example, the Permanent Fund Executive Branch
11 elected to get into mortgage loans -- well, this would throw
12 the rest of the banking systems into total chaos.

13 MR. LOVE: That's not necessarily true.

14 MR. GALLAGHER: We're already in the mortgage loan
15 business.

16 MR. WALDOCK: You are to a certain extent.

17 MR. LOVE: We already own forty percent of the market.

18 MR. WALDOCK: But you're trying to tell me that you
19 can take Two and a Half Billion Dollars and put it into
20 mortgage loans in Alaska?

21 MR. WOHLFORTH: The question is really, is there an
22 example throughout the world where a huge infusion of money
23 (maybe it's the Saudi countries) has disrupted the banking
24 system, and do any of the advisors have anything they would
25 like to put to that.

1 MR. FUHRMANN: The answer with respect to both Middle
2 East and Venezuela, which are really the areas that are most
3 similar to what you're talking about, is that they had among
4 their objectives and purposes initially getting the money out,
5 and they have invested in external investments, money market
6 instruments, government borrowings, they've put money into
7 the World Bank, or into subsidiary banks of the World Bank,
8 things like this. They've taken the money out of their
9 own economy to avoid that conflict, as well as the resulting
10 inflationary impact if they had allowed that money to go
11 into their own economy.

12 MR. MOTLEY: So they upset somebody else's apple cart?

13 MR. FUHRMANN: Yeah, right, or made it available in
14 places where the apple cart -- there's nobody there.

15 MR. ODEN: In addition, in New Mexico there is a
16 severance and a Severance Tax Permanent Fund. Investments
17 of that fund are in CD's of state banks. So rather than harm
18 the state banks, it's really been a great advantage to the
19 state banks to have a ready market for their CD's, and as the
20 CD market can approve of a loan at the going rate for CD's
21 now anyway.

22 MR. WALDOCK: What is the length to share those CD's?

23 MR. ODEN: They vary from one to five years. With
24 those monies the banks turn around and make loans on capital
25 projects. They do all the research and they do all the

1 evaluation on the validity of the loans rather than being
2 done by the state.

3 MR. WALDOCK: Well, with a five-year limit there, it
4 really isn't restricted to short term loans.

5 MR. ODEN: Yes, it is to a large extent. Those can't
6 be rolled over.

7 MR. FUHRMANN: The purpose of almost all these funds,
8 in one way or another, is to help build capital formation
9 internally and make private financing available. This often
10 is the reason why they get into equity, is to provide the
11 credit upon which the entity can finance itself, leverage
12 itself off the equity or anything, in the case of encouraging
13 other institutional investment through participation loans
14 only, or buying the CD's of the banks, of the private -- you
15 know, you can make the funding available -- all these concepts.

16 MR. GALLAGHER: Mr. Waldock.

17 MR. WALDOCK: Yes.

18 MR. GALLAGHER: I believe at the last meeting I spoke
19 to that very question, and I said if you go back and look
20 at the deposit structure of the State of Alaska in comparison
21 with other states in the Union, you would find that we resemble
22 the deposit structure of more rural states in that we have
23 high demand deposits and low in savings deposits. If you
24 orient the Permanent Fund toward long-term investments, i.e.,
25 those longer than five years, then you're not competing with

1 the commercial banking system. The commercial banking system
2 here in the state doesn't put all those mortgage loans on the
3 books. In fact, they sell them to Fannie Mae and several of
4 the state agencies. We would not, in fact -- even if you go
5 into the mortgage loan business you're not competing with the
6 commercial banking system, especially if they're the ones
7 that make the loans.

8 MR. MOTLEY: Providing an outlet for them.

9 MR. GALLAGHER: Yes.

10 MR. WALDOCK: Sterling and Tony, mortgages was a quick
11 example and it was a poor example, but the point I'm concerned
12 about is that the terrific influx in money could, if not con-
13 trolled properly, throw the whole banking society off kilter,
14 and I was curious to see if that had taken place any other
15 place with this large infusion of money with the low amount of
16 populace that we have. That was basically the question.

17 MR. GALLAGHER: There's probably adequate funds for
18 the short term lending. Commercial banks are oriented
19 toward short term lending with the shortness of money. And
20 this state is not in the short term market, but it's in
21 the long term market. So if we orient ourselves in that
22 manner we're not going to be disruptive at all. We'll be,
23 in fact, supplementing.

24 MR. WOHLFORTH: Do you have another questions?

25 MR. WALDOCK: No. Well, I have four other questions,

1 but I would like to wait until after the rest of the Committee
2 members have finished speaking to the consultants.

3 MR. WOHLFORTH: Representative Malone.

4 MR. MALONE: Thank you, Mr. Chairman. Mr. McDowell,
5 one thing you mentioned in discussion of the World Bank, I
6 believe, was that you didn't really believe it was in the
7 process of diverting capital. Will you describe that process
8 to the Committee and whether that might hold any implications
9 for the Permanent Fund?

10 MR. McDOWELL: We were saying from a world-wide
11 standpoint such institutions, I think, do divert capital
12 because they take capital out of developed country capital
13 markets which again probably would have been loaned to some-
14 one else if it hadn't been loaned to the World Bank, and
15 channel it into specific projects in specific developing
16 countries. Maybe there's an analogy here. Back to your
17 question, the one country that I am familiar with that's got
18 a similar situation was Kuwait. What happened in Kuwait was
19 that they filled up their commercial banking coffers with
20 kind of a wash in cash, everything else just flowed right
21 out into the international financial markets in other countries.
22 In effect, it was just passed out of their banks into other
23 banks and invested in securities elsewhere in the world.

24 Let's say that could happen here and probably will
25 happen here in the early stages at least. The revenues to the

1 Permanent Fund will probably flow through the treasury out
2 into the capital markets of the United States initially, I
3 would guess, although some of it would stop over in banks
4 in the states and create mendable assets, but most of it will
5 probably flow right on out there. So you won't see a terrific
6 disruption of your banking system before it's had a chance
7 to grow a little bit more and to absorb some more of this.

8 Then, if that's all you do with it, then that capital
9 will be out there, it will be earning a certain return for the
10 State of Alaska, but it probably will be loaned then to some
11 other project. It may be loaned to U. S. Steel for expansion
12 in Pennsylvania, it may be loaned in the European market for
13 expansion in Europe, or Africa or somewhere else. If you
14 create an institution that can call those funds then back
15 to you at a later time, channel them into the Alaskan economy,
16 then you in effect have gained a measure of control over your
17 own destiny, and you've been able to divert a capital flow
18 that may have gone somewhere else instead. But I think
19 without an institution for diversion or without some rules
20 for diversion, in effect, goals for diversion let's say, it
21 probably won't occur.

22 MR. GALLAGHER: Mr. McDowell, maybe you're not familiar
23 with the assets in the State Treasury. There is what you
24 might almost call a Permanent Fund already in the State
25 Treasury, and it's Two Hundred Million Dollars and growing.

1 You know, it could be a goal of the Permanent Fund to return
2 the General Fund, which is the State's operating column,
3 back to its original purpose and not leave that Permanent
4 Fund in there.

5 MR. WOHLFORTH: Mr. LeReche.

6 MR. LERECHE: You've been really helpful to me in
7 kind of helping us, helping me at least, think about where
8 the line between policy control and operational control is,
9 but I'm still not clear and, obviously, you can't be clear
10 today. But let me ask you a couple more questions that,
11 hopefully, will illuminate this a little bit more. The
12 institutions you described have two measures of success (this
13 I gathered implicitly in what you said) credit worthiness and
14 project viability. Does that pretty much summarize the
15 measures that you're using to tell us those are successful
16 institutions?

17 MR. McDOWELL: No, those are really for the projects
18 and the countries that they lend money to. For the institution
19 itself their measures of success are continuation; in other
20 words, just survival. Do they survive intact as financial
21 entities? In other words, are they permanent or continuing?
22 That's partly measured by whether they make a profit every
23 year. So they're very much like any other commercial insti-
24 tution, you know, there's a bottom line. It's a number, and
25 that's one of the measures of their success. The other measure

1 of their success is the changes in the countries that they
2 deal with. Does per capita income go up? Does income
3 distribution improve? In other words, within a given country
4 is the quality of life for the people of that country better?

5 MR. LeRESCHÉ: It's measured on achieving their other
6 objectives also.

7 MR. McDOWELL: Essentially, and those are the more
8 important objectives. The bottom line, you know, on the
9 income statement is just the one that measures whether or not
10 they're achieving prudence. That's just one of their objec-
11 tives; they have to be prudent.

12 MR. LeRESCHÉ: It was hard for me to hear in your
13 statement.

14 MR. McDOWELL: Yes. The other is, again, in these
15 general statements of purpose you read these more qualitative
16 goals. But they do their best to measure whether they're
17 achieving these qualitative goals, and those are some of
18 the measures which they use.

19 MR. LeRESCHÉ: I think your strong message was that
20 these have been successful institutions because of their
21 executive autonomy of the operation or operations. Tell us
22 a little bit more about why you assume that? Did you take some
23 examples that didn't have autonomous operation or was this,
24 in effect, because of that?

25 MR. McDOWELL: Some of the banks in the countries

1 themselves, the DFC's, the National Development Banks, have
2 failed, gone out of existence, and they haven't done even
3 the basic thing, that that is to survive. In most instances
4 when you read reports of why it happened or what happened,
5 they were susceptible to the pressures from the fact that
6 their major or only stockholders was the government of the
7 country, and the government of the country imposed restric-
8 tions on them or pushed them in different directions that
9 they just couldn't survive economically on. So, generally
10 speaking, that's what happens.

11 Some go down because of poor management, no question
12 about it. Some are poorly managed and they just collapse
13 because they made bad loans and the government didn't do a
14 thing, they were left completely alone. But in many of the
15 instances the fact was that this inevitable pressure became
16 interference in the day-to-day operating procedures.

17 MR. LeRESCHÉ: So the line of policy interference
18 was drawn a little too high or too low?

19 MR. McDOWELL: Too low, yes.

20 MR. LeRESCHÉ: I'm just trying to understand exactly
21 where you would want it drawn. You said that it's proper to
22 lay out the objectives of the Fund or the institution in
23 the charter. Then you said the charters of most of these
24 are very general, one or two sentences.

25 MR. McDOWELL: Well, or maybe several paragraphs,

1 but they're still general wording. The wording is still
2 general.

3 MR. LeRESCHÉ: But also in the case, I think, of
4 the World Bank you said the leverage ratio was set by
5 limitation on interest or ---

6 MR. McDOWELL: It's right in the articles.

7 MR. LeRESCHÉ: That seems fairly specific as opposed
8 to general. Isn't that an operational control?

9 MR. McDOWELL: Not really. It's a description of the
10 size of the institution. The stockholders in effect stated
11 that they did not want the institution to exceed a certain
12 size without calling for a new vote to subscribe more capital.
13 I should point out that the stockholders of the World Bank
14 and the other institutions can increase the size of their
15 institution not by -- well, they can do it by changing the
16 leverage ratio, but it's quite difficult to change the
17 articles of incorporation even though it can be done.
18 In these cases it requires a significant vote, which is not
19 the situation here. But they can accept or reject management's
20 requests for an increase in capital. The World Bank can
21 leverage it at, is it nine to one, whatever capital they've
22 got.

23 MR. REGIS: It's not interference in the management
24 prerogative.

25 MR. McDOWELL: It just says you have so many funds to

1 work with.

2 MR. LeRESCHÉ: Okay, one step further then. The
3 Alberta Fund goes one step further. It sets proportions of
4 loans that can be made for various purposes. In this con-
5 text, if we were proposing to you the Alberta setup and asking
6 you, as our consultant, if that was a good one or a bad one
7 because of executive autonomy, what would your evaluation be?
8 Would you recommend our getting into something that specific?

9 MR. McDOWELL: Let me just answer -- I'm not trying
10 to avoid the question -- if you decide that the objectives
11 of the Development Fund shall be several: that is, it would be
12 perhaps a "Development Bank" similar to these, and it will
13 also, let's say, get involved in very small loan programs,
14 which you can do this, you know. I'm saying that the other
15 institutions don't because they've found it's not really
16 economic, but you can certainly possibly do it -- and it
17 shall be involved in "social programs" where the interest
18 rate can be zero or slightly over, then sure, you might
19 as well strike the percentages because you've got three quite
20 different programs. If you make the thing just one program,
21 then I would say no, you're hamstringing management and the
22 board's ability out in the future to adapt to the changing
23 conditions of the state.

24 MR. LeRESCHÉ: Okay, but a strong executive officer
25 working under the Alberta rules would still feel accountable.

1 MR. FUHRMANN: He doesn't feel accountable with respect
2 to the loans that are in the soft category because it's been
3 removed from the fund by being put on the Legislature. He is
4 accountable with respect to those things he does have
5 authority over. So they have maintained the autonomy within
6 the normal business environment with respect to soft loans
7 but the responsibility really rests back with the Legislature.

8 MR. McDOWELL: Where it normally is in a government
9 program anyway. So you're almost saying perhaps that in the
10 State of Alaska we have a variety of governmental institutions
11 and programs doing a lot of things in the social intra-structure
12 areas. I'm not sure that I would say -- I mean, I wouldn't
13 say that it was necessarily advisable to create another
14 institution to do the same thing. I think what you have is
15 an opportunity to create an institution that's going to do
16 something else that you're not doing already. I think Alberta
17 has, in effect, taken (I don't know what the percentage is
18 but) 20 percent of their "Permanent Fund" and it's not part
19 of their Permanent Fund. It's just part of their regular
20 government programs. It's subject to the same processes as
21 their normal budget requires. So I don't think they've done
22 anything different with that section, that soft loan section.

23 MR. LeRESCHÉ: Just a final comment. I guess what's
24 concerning me is who controls the secondary effects, the
25 good income producing it has? Will the executive officer

1 have to choose between two or three of these things, all
2 things being equal, but this will have different effects on
3 different parts of our state's economy. Who controls that
4 and I assume you're arguing that the executive officer
5 controls it himself.

6 MR. McDOWELL: Well, the board does.

7 MR. LERESCHE: The second board?

8 MR. McDOWELL: The operating board.

9 MR. LERESCHE: Thank you.

10 MR. WOHLFORTH: I wonder if we might take about a
11 two-minute at ease. We've been sitting here for two hours
12 and twenty minutes, and then resume. Let's keep it short.

13 (Whereupon the meeting recessed at 3:50 p.m.
14 and reconvened at 4:05 p.m.)

15 MR. WOHLFORTH: Please take your seats and we'll
16 resume. Unless there is a serious objection I propose another
17 fifteen minutes of questions for the consultants and then,
18 since we are running out of time on the agenda, try and wind
19 up by between a quarter of 5:00 and 5:00 o'clock in terms of
20 general discussion of where we do we go from here. I realize
21 that cuts short. Who was the questioner? Were you through,
22 Bob? Okay.

23 MR. MOTLEY: Mr. Chairman. I would like to address
24 the remarks you made with regard to guarantees. Have you seen
25 any quality of the investment of the loans, a difference in

1 programs that had guarantees as opposed to programs that had
2 direct loans?

3 MR. McDOWELL: Guarantees depending on the sense that
4 the agency or the institution is acting as the guarantor for
5 them, not that it gets somebody else to guarantee them?

6 MR. MOTLEY: No, that it acts as a guarantor.

7 MR. McDOWELL: Yeah, the one case of that -- well,
8 where they actually do it is OPIC, and their loan guarantees
9 far exceed their actual loans. Their experience on the pro-
10 jects is that they tend to be slightly less involved with the
11 development of the project when they're doing a guarantee
12 operation than they do when they're making a direct loan.

13 MR. MOTLEY: What about the profit between the two
14 as far as the of the quality of investments go?

15 MR. McDOWELL: Well, their losses don't seem to be --
16 from what I understand their losses don't seem to vary that
17 much between the two. They do have losses. They do lose
18 money on the loans, they've got work-out projects, and they're
19 doing work-outs all the time on losers because they do get
20 into very, very high risk areas by design. But nothing was
21 indicated to me that they found the experience to be sub-
22 stantially different. This is more the nature of the businesses
23 they're investing in that causes the losses, whether they're
24 guaranteeing the loans or not because they do almost the same
25 amount of preliminary work prior to giving a guarantee as

1 they do if they give a direct loan. It's just a difference
2 in scale. Their guarantees they use for projects that are
3 for the larger amount involved. They save their limited
4 amount of loan capital for small loans. But again, they're
5 heavily involved in each kind.

6 MR. MOTLEY: Thank you, Mr. Chairman.

7 MR. WOHLFORTH: Representative Urion.

8 MR. URION: I'll pass, Mr. Chairman.

9 MR. THORSTENSON: Bob Thorstenson. Pete, do you
10 anticipate a DFC type of an institution involved with the
11 Permanent Fund in Alaska?

12 MR. McDOWELL: Well, I've been asking some questions
13 about whether there -- at the last meeting there was quite
14 a bit of discussion about what do we do when we need small
15 loans. Does an institution created by the Permanent Fund
16 make them or does someone else make them? It looked to me
17 like the Permanent Fund will have a lot of money, it will be
18 relatively large and, therefore, it will probably not be
19 too well equipped to deal in the very small areas. I was
20 trying to draw the analogy to the development banks we've
21 discussed in here, most of which finance intermediaries.
22 It appears that there are two sets of intermediaries already
23 in existence in this state, i.e., the Native Regional Corpora-
24 tions as a potential level of intermediary, and the Local
25 Development Corporations as another level of this organization.

1 and the commercial banks, not to exclude them, which are
2 already set up, perhaps to deal in smaller loans using funds
3 that they may be loaned in turn from this institution.
4 So I can see the parallels, and you may very well want a two
5 tier system in the state in the future.

6 MR. WOHLFORTH: Thank you. Any questions?

7 MS. FLEISCHER: I don't have any questions.

8 MR. WOHLFORTH: Mr. Love.

9 MR. LOVE: Peter, as I understand a lot of these
10 development banks we're talking about, one of the reasons
11 for them is to help under developed capital formations,
12 divert monies from markets where capital is more readily
13 available to areas where it's not easily obtainable, from
14 the various industrial nations, etc. I'm wondering, you know,
15 just how applicable that is to the State of Alaska which seems
16 to have a radically different situation. Instead of a country
17 that has to divert capital from other markets because we're a
18 capital poor area, we seem to be an area where there is not
19 really a shortage of capital and, in fact, we have dangers
20 (like Mr. Richards talked about), a problem of how much capital
21 we can absorb. Do you see that as something that should make
22 us think very carefully about whether or not a development
23 bank approach, as you've described it and used the World Bank
24 and these other things for that, per se, is that the best
25 vehicle for us in the investment of the Permanent Fund?

1 MR. McDOWELL: I think I would like to ask the people
2 from White, Weld to come in also, but I'll just lead off. I
3 think, yes, there are a number of differences between the
4 situation in Alaska and the situation in most developing
5 countries. The opportunity probably exists in Alaska to use
6 "development money" not to try to have to raise the level of
7 literacy and the level of the income of the individual citizens
8 of the state from zero or almost zero up to some acceptable
9 level where you avoid starvation, etc. Those problems really
10 don't exist, at least in the same magnitude, as they do in
11 the developing countries.

12 But the other issues that are addressed by the develop-
13 ment banks include such things as the -- investment decisions
14 aren't made on economics alone, they're made on income distri-
15 bution effects, they're made on employment effects, they're
16 made on environmental considerations, health considerations
17 and social considerations, plus the economics of the situation,
18 the project situation. So, perhaps even though those are
19 relatively less important when what you're really trying to
20 do is create a way for people to get enough to eat.

21 I don't think the models -- you know, they vary
22 wildly -- I think you could adapt it to the Alaska situation
23 with some significant structural emphasis differences.

24 MR. LOVE: I'm not saying that I think that's a bad
25 idea. I'm just -- I think that was an obvious thing to talk

1 about since the ones you described seemed to be, from a
2 logical situation, pertinent. Do you think if we identify
3 goals as addressing the issues like employment problems,
4 distribution of wealth, and other social considerations,
5 the one vehicle we can do that is through the development
6 bank? Do you think in Alaska, with our present situation,
7 this might be a real good way to address those?

8 MR. McDOWELL: Yes, they could certainly be required
9 as conditions for consideration of a project, to at least
10 say these things should and will be considered.

11 MR. LOVE: And these are common objectives in those
12 areas where they do this development bank, is that right?

13 MR. McDOWELL: You've got different layers of developing
14 countries, some are quite developed and still get this money
15 and develop these projects. You'll see, for example, that
16 in the analysis of a project in Singapore, which still gets
17 a couple of these loans, one or two of these loans a year,
18 environmental considerations are very important compared to,
19 for example, a very poor country in Africa.

20 MR. LOVE: I think it's good to hear this because I
21 think there are so many misconceptions of just why people
22 got this, what the term "development bank" means. I think
23 that the things you described are the exact opposite of
24 objectives that some people might attach to it, but they might
25 seem frequently at odds with those; the idea that those two

1 can work together is something that the public probably needs
2 to think about more.

3 The other is the -- well, first of all, you said that
4 these types of -- you mentioned before that in some of these
5 countries that these are the real important objectives of
6 capital that have to be measured not just in terms of whether
7 the loans are being paid back at a good rate of return or
8 not, or whether or not in addition to being paid back that
9 they positively affect things like the standard of living,
10 quality of life, literacy and things like this. I wondered
11 if your firm can provide us, or I guess it's staff members,
12 can provide us with some of the mechanisms by which these
13 objectives are evaluated, whether they succeed or not, because
14 I think that's something that very soon we're going to have
15 to start developing is, what are the mechanisms for evaluating
16 whether or not the loan programs that the state enters into
17 are actually achieving the specific objectives being outlined.
18 Now, the other thing is -- well, first, do you think that's
19 something that your firm will be able to provide us with?

20 MR. McDOWELL: There's examples of the reporting of
21 the accomplishment toward this sort of objective in the
22 annual reports of the institutions. Sure, they have their
23 income statements, but mainly what they're doing is addressing
24 what effect they've had on the countries and these other
25 areas of concern. So those are examples of the public

1 reporting of it. In other words, they know that they must
2 report to their public, not only that they made, you know,
3 Ten Cents a share or whatever it was, but they also have to
4 report what was the measurable progress (if you can measure
5 it) toward the other more social type objectives.

6 MR. LOVE: You see, I'm just saying that when we talk
7 about this it's going to be, I think, better for us as we
8 can start to develop if we can see conceptional models
9 (cookbooks maybe) as to how we can actually compute these,
0 you know, easier ways of evaluating loans prior to when they're
11 made as to what the objectives might be, or evaluate them after
12 a period of time. I know that we're starting from ground zero
13 right now, or from scratch, and I haven't been able to get
14 a handle on how that process can be taking place. So if you
15 have any more information about that, I think it would be
16 very helpful.

17 MR. REGIS: I think we can. I don't see any reason
18 why we can't develop more detailed information in that area.

19 MR. McDOWELL: No, that's no problem.

20 MR. LOVE: That concludes my questions.

21 MR. WOHLFORTH: Thank you. I just have one comment.
22 There is quite an abundance of literature on the subject
23 matter. The Brookings Institute did about three or four
24 years ago an exhaustive study on the World Bank, and I would
25 hope that we might have at least a beginning bibliography

1 available. It seems to me it's going to be necessary for the
2 Legislative Committee that considers what we're doing here,
3 hopefully, to acquaint themselves with the published material,
4 and I would hope that one of the consultant groups would take
5 that task in hand and give us a bibliography early so that
6 we can begin to see to what extent the sources are available
7 here in Alaska where we have (I'm embarrassed to say) an
8 extremely poor library system for anything in the nature of
9 business materials or stuff of this kind. It seems to me
10 while there are a few months left before the Legislature
11 attacks this, it would be well to start getting material here
12 in some supply. Anything else on this side of the table,
13 any questions?

14 MR. LOVE: I'd just like to suggest that maybe in
15 some of these larger studies that they could be made available
16 in Jim Rhodes' office, who has an office here in Anchorage
17 and does work with this Investment Advisory Committee, then
18 maybe members of the Committee could make use of the material
19 that way instead of having to distribute a lot of stuff to
20 everyone.

21 MR. WOHLFORTH: We're more or less through with the
22 direct questions of the consultants and we'll simply open
23 it up for general comments and discussion, as the agenda
24 indicates it's time for new business, and we'll go around
25 the table starting on this side again. I think you're up.

1 Any observations on the meeting today or any insights that
2 you would like to share with us?

3 MR. MALONE: Insights? No. Thank you, Mr. Chairman,
4 I don't have any general comments right now. I am concerned
5 about what the future course of the Committee would be, but
6 would be glad to listen to the insights others may have.

7 MR. WOHLFORTH: Dennis.

8 MR. WALDOCK: Mr. Chairman, I indicated earlier I have
9 four particular questions I'd like to direct to the Committee,
10 and that is in regards to the course of where we're going,
11 and I'd like to start off with the first question. It's
12 mainly because of myself and a few of the other Committee
13 members who have noticed, for example, all these new financial
14 consultants that we've got here for the Permanent Fund, i.e.,
15 the Arthur D. Little, Price Waterhouse, White, Weld., etc.,
16 I've been wondering exactly what kind of criteria was used
17 for the selection of these financial consultants.

18 MR. WOHLFORTH: I guess that would be a question of
19 the Commissioner's Deputy in terms of the process that they
20 went through in the selection, if they care to respond.

21 MR. GALLAGHER: I point out that only two are under
22 contract at the present time, Arthur D. Little being the one
23 that isn't under contract. The process that we went through
24 was to search out with the Legislative branch who were some
25 of the people who were knowledgeable in the areas, and several

1 names were brought forward. We called from that list and
2 talked to several different groups, ones that we thought
3 appeared to have the most to bear on the subject.

4 MR. WALDOCK: The second question I'd like to address
5 to the Committee ---

6 MR. MOTLEY: Dennis, could I just amplify? I think
7 he's brought up a very good point, Sterling, and I think it's
8 something, maybe for the edification of some of the newer
9 members. This Investment Advisory Committee, as an entity
10 of the state, is subject to the procurement and purchasing
11 rules and laws of the state, and I think we have to keep that
12 in mind as we go down the pike because it could conceivably
13 put Mr. Malone in a rather interesting position of Legislative
14 Budget and Audit hat on one hand and a Member of the Committee
15 on the other hand, and I say that with tongue in cheek but
16 you know what I'm talking about. We are subject to certain
17 procurement purchasing requirements.

18 MR. WALDOCK: The second question that I'd like to
19 bring up is, what are exactly the fees paid to these various
20 consultants and what is the length of their contract.

21 MR. EDENSO: I think I can respond to that. The terms
22 of the contract are general, they are intended to expire at
23 the presentation or the completion of our task, which one of
24 them, and I think Mr. Rhode and I both agree on, is to have
25 the Committee itself return to its original condition after

1 we have responded or prepared some product or some output for
2 the 1977 Legislature. Whether that be in the form of recom-
3 mendations for content of a statute or whether that be a
4 statute I'm not sure, but we anticipate completing the closed
5 contracts sometime in January of 1977.

6 MR. WOHLFORTH: Jim.

7 MR. RHODE: Mr. Waldock, in fact, I believe all the
8 contracts are identical in that they expire with the convening
9 of the Tenth Alaska Legislature, and generally the compensation
10 is based at their customary fees with a ceiling not to exceed.

11 MR. WALDOCK: Which is?

12 MR. RHODE: Well, it depends on the contract. For
13 example, White, Weld's is set at the amount of Twenty Thousand
14 Dollars ceiling for their professional time, and allowances
15 have been put aside for expenses. It's customary in all
16 consulting work of the State of Alaska to pay actual expenses
17 in addition to professional time, and we've estimated those
18 as best we can.

19 In part, I prepared some estimates based on the con-
20 sulting work that was done in connection with the Alaska
21 Power Study, which was my own experience, but Mr. Edenso had
22 other studies from which to make further estimates.

23 MR. EDENSO: In answer to how much they're costing,
24 the Legislature passed an appropriation of \$185,000 during
25 the last session, and in a fit of conservatism and desiring

1 to save some money for the state, the Governor slashed that to
2 \$135,000. I would commend the Governor for his philosophy.
3 The Governor really had no idea what the magnitude of this
4 project was and what the related costs were, especially in
5 developing the kind of data base that is necessary to proceed
6 with developing the establishment of a Permanent Fund or the
7 effort it would take to gather all this data.

8 However, getting down to the actual costs, we have on
9 contract Mr. Bob Richards from the Alaska Pacific Bank.
10 His contractual services are a ceiling of \$15,000, not to
11 exceed that. We have budgeted for him for travel and expense
12 purposes \$2,000. His total then is \$17,000 that he is limited
13 to.

14 The other contractors are White, Weld and Company,
15 Incorporated of New York. Their contractual service fee is
16 \$20,000 (that's the ceiling), travel and expenses, since
17 they are from New York, since they have been visiting with
18 other funds and are anticipated to continue those visitations,
19 it's \$10,000, for a total of contractual services plus expenses
20 of \$30,000.

21 We have on contract, but we have not utilized, Pro-
22 fessor Edward Solomon from Stanford University, contractual
23 services of \$5,000, travel and expenses of \$2,500, for a total
24 of \$7,500.

25 We have an unsigned contract, but an agreement should

1 we wish the information, of Dr. Richard Neve from the
2 University of Alaska in Seward, to provide us specific informa-
3 tion on fisheries and fisheries related subjects. We have
4 budgeted for this contract \$5,000 and travel and expenses
5 \$1,000, for a total of \$6,000.

6 We have budgeted for the Legislators involved with
7 the Permanent Fund and for their discretionary use a total
8 of \$30,000. We have budgeted for legal research purposes
9 \$5,000. We have budgeted for travel contractual services
10 for the State Investment Advisory Committee \$3,000 in
11 contractual services, an additional travel and expenses of
12 \$5,000, for a total of \$8,000.

13 MR. WALDOCK: I didn't get the figures on Price
14 Waterhouse.

15 MR. EDENSO: Price Waterhouse, excuse me, they were
16 not on my list. Price Waterhouse has the identical features
17 to the consultants White, Weld and Company, Incorporated.
18 They are contractual services not to exceed \$20,000, travel
19 and expenses not to exceed \$10,000.

20 We have a contingency fund of \$16,500. We had pro-
21 grammed, prior to our full realization of what the costs
22 would be for the information we were asking from Arthur D.
23 Little, we had programed \$10,000, for the travel and expenses
24 budget not to exceed \$5,000. However, I should point out
25 to you that the information we are asking from Arthur D. Little

1 is very complex and very difficult to gather. It requires some
2 very talented people in the area of the national economy,
3 interpretation of that with the state economy, and some
4 econometric modeling, not techniques but the results of a
5 developed econometric model. We have not signed this contract
6 yet. We're currently contemplating asking for a supplemental
7 appropriation to allow us to proceed with this.

8 I think that generally gives us a total of \$135,000.
9 Contractual services total amount, \$109,500, travel and
10 expenses is \$25,500.

11 I left out one other contractor. He has not signed
12 but I've got his contract here, and that's Mr. Bill Batko.
13 He would come under the budget item of State Investment
14 Advisory Committee. Mr. Batko was recommended to us by Mr.
15 Love. His contract -- I am not familiar with the exact
16 dollar number, but his total contractual services is \$500 and
17 his travel and expenses we have budgeted for \$1,500.

18 MR. WALDOCK: My next question is something that's
19 concerned me here. After taking the time to consult with
20 attorneys on the exact responsibilities of the Investment
21 Advisory Committee, my question stems as such. Since it is
22 one of the responsibilities of the Investment Advisory
23 Committee to advise the Commissioner of Revenue and the State
24 of Alaska on their selections of financial consultants, and
25 since these financial consultants primarily for the help

1 on the Permanent Fund have already been selected, can it be
2 assumed that the Investment Advisory Committee is not going
3 to be held responsible for any incorrect advice given by
4 these consultants.

5 MR. WOHLFORTH: I would say yes, it can be assumed.
6 That's my answer, for what it's worth.

7 MR. GALLAGHER: It was an executive prerogative.

8 MR. EDENSO: For the information of the Committee,
9 I'd like to attempt to respond to that. Alaska Statutes
10 Chapter 37.10.070 Paragraph F, "The investment policy shall be
11 formulated by the Commissioner of Revenue, who shall be
12 advised by a committee appointed by the Governor but shall
13 contain representation from the Legislature. In formulating
14 investment policy they shall consider maximum income and
15 safety as governed by the prudent man rule and the benefit
16 to the private and public sectors of the economy in terms of
17 increased housing and commercial credit, stimulated business
18 activity, increased employment, support of the market for
19 state and local bonds, increased public revenue, together
20 with the possible inflationary effect of the investment and
21 (h) and (i) of this section. The Commissioner of Revenue,
22 with the consent of the Committee, may enter into contracts
23 for services providing investment advice, custody of securities
24 and execution of transactions in or out of Alaska."

25 MR. WOHLFORTH: Is there any more?

1 MR. EDENSO: That pretty much spells out what the
2 previous role of the Investment Advisory Committee was.
3 However, in the expansion of the Committee to undertake
4 the task of establishing the Permanent Fund, the Governor
5 asked that the Committee address itself only to the Permanent
6 Fund at this point in time in its expanded state. Now, were
7 you to begin to provide advice to the Commissioner as an
8 expanded Committee, and I would suggest that with the new
9 members of the Committee, that may be inappropriate at
10 this time.

11 MR. MOTLEY: Mr. Chairman.

12 MR. WOHLFORTH: Yes, Commissioner.

13 MR. MOTLEY: Mr. Waldock and I have not discussed this
14 subject before, but I think I can understand the thrust of
15 his questions. I think, as a long-time member of this Com-
16 mittee, he would like to continue to participate in some of
17 the decision making processes with regard to the selection
18 of criteria, of consultants, et al., and I, as a fellow member
19 of his Committee, I think I can understand what he's saying.

20 I don't have any problem with the selections that
21 were made, and I may be reading something into it, Dennis,
22 that you haven't said, but I have no problems with the
23 selections made. But I have taken note of his scrutiny of
24 the process.

25 MR. WALDOCK: I'd like to say the same thing, and it's

1 not just myself; I think that everybody on this Committee
2 should have that opportunity to have that choice, and we
3 might as well get the course of this Investment Advisory
4 Committee aimed in the right direction. I saw this as a
5 particular area of conflict and problems and decided to
6 address myself to the Committee in regards to it.

7 MR. MOTLEY: I think one of the things, Dennis, you
8 have to keep in mind is, as we meet on them -- and I've
9 fallen into this spot under other circumstances so I think
10 I can address it -- and that is, in the interest of getting
11 on and trying to get things done, sometimes we find ourselves
12 way out in the front end of the Board, and maybe that may or
13 may not have been the case in this case. But I've certainly
14 heard what you said and I've taken note of it.

15 MR. WALFORTH: The final question here is, I think,
16 the real crux of what I was trying to drive at here. There
17 is a law in effect that came in effect after the Investment
18 Advisory Committee had actually been in operation, and I
19 believe that law came in effect in 1972, (I wasn't able to
20 get the exact date) and that is that anybody working in an
21 advisory or a consultant capacity may not act as a contra-
22 capacity as an investment banker, or dealer, or accountant
23 capacity due to the possibility of conflict of interest.
24 This generally held in the Permanent Fund. My question is,
25 will this also hold true for the Permanent Fund?

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MR. MOTLEY: What is the statutory reference?

MR. WALDOCK: 1972, Tony.

MR. WOHLFORTH: Yes, but what chapter?

MR. WALDOCK: Unfortunately I Xeroxed enough copies to bring along for the members and left it in my office, and I'll have to get it back

MR. WOHLFORTH: The only one I'm aware of is that prohibition which applies to the state and local governments of having a financial advisor bid on bonds. Is there another one that I'm not aware of?

MR. RHODE: No. That's what you're talking about, isn't it?

MR. WALFORTH: Yes.

MR. RHODE: It doesn't apply in this situation because they're giving advice on general public issues. They're not structuring debt, preparing a prospectus, advising us on any specific type of investment, nor are there any investments for them to deal in.

MR. WALFORTH: Mr. Rhode, couldn't you possibly see a conflict of interest in investment advice or a consultant in this particular case because it takes in a broader area? Couldn't there be a little bit of conflict of interest if that individual was to structure the way the Permanent Fund is to be run and then, in fact, turned around and be in the other end of the operation?

1 MR. RHODE: This matter was specifically addressed.
2 Every consultant, at least on my motion, was given a copy
3 of the relevant statute, and so in our informal opinion
4 (we could get a written one from Legislative Counsel), the
5 situation didn't cover them. But my immediate reply is this:
6 I'm not aware that Price Waterhouse is even dealing in
7 securities, and in the case of White, Weld, they're in
8 virtually every type of investment that is possible, all the
9 way from tax exempts to taxable debt. So I don't understand
10 how--any way the Fund turned out there would be some kind of
11 business that they might have a part in at some later point.
12 But that would be true of any highly reputed national invest-
13 ment banking house that we might bring before this Committee.

14 MR. WALDOCK: That's the exact point. I think that
15 if they are used as consultants they, in fact, should not
16 be involved in the other end of the operation.

17 MR. RHODE: What other end?

18 MR. WALDOCK: The actual use of the Funds, once
19 it's in operation.

20 MR. WOHLFORTH: In other words, you're proposing that
21 their actions here up to the Legislative Session would bar
22 them from any advisory role in terms of the Permanent Fund
23 later; is that what you're saying?

24 MR. WALDOCK: Not in an advisory role, in actual
25 active role.

1 MR. WOHLFORTH: Well, what do you mean by active role?

2 MR. WALDOCK: I guess I'd have to read the law again,
3 but even probably on an advisory role.

4 MR. RHODE: No, it doesn't say advisory. It says if
5 you're actually dealing in some kind of debt instrument for
6 the state at the same time you're advising them, that's
7 unlawful. But if you're rendering advice and there's no
8 involvement with any kind of financial transaction, then
9 you are not under the conflict of interest laws.

10 MR. GALLAGHER: I'm not aware that White, Weld is
11 involved in any issuance of any debt of any agency of the
12 state government.

13 MR. RHODE: It's not.

14 MR. WALDOCK: Well, that wasn't the point I was striving
15 for. I'm striving for the point of, they are a consultant
16 at this period of time, and I'm not directing it towards
17 White, Weld or any of the other consultants; I am just making
18 a statement and asking for a question here. For example,
19 an investment advisory firm cannot act as a consultant, a
20 financial consultant and then turn around and be an under-
21 writer of an issue, i.e., the bond bank that just was formed
22 here in the last year. Now, that role or law went into
23 effect in 1972.

24 My question here is, now that we've utilized the
25 talents of these consultants that we have selected or have been

1 selected, are they going to be barred with the Permanent Fund
2 monies to participate in the operational end once those funds
3 are in operation.

4 MR. GALLAGHER: If we sell debts out of the Permanent
5 Fund, is that your question?

6 MR. WOHLFORTH: I think it's to some extent hypotheti-
7 cal. Shouldn't it await the event, if we get a Permanent
8 Fund, if the Legislature passes the ---

9 MR. LOVE: Mr. Chairman, I would suggest that what we
10 do in this case is to ask for an Opinion by the Attorney
11 General on this specific question that Dennis has just asked.
12 He's asked a very specific question, I think a legal question,
13 and he's asking about a specific statute, and I can't see any
14 problem with going to the Attorney General and asking him
15 to provide us with an authoritative Opinion.

16 MR. GALLAGHER: I'm not even sure I understand the
17 question.

18 MR. EDENSO: Mr. Chairman.

19 MR. WOHLFORTH: Mr. Edenso.

20 MR. EDENSO: Mr. Chairman, I think that what Mr.
21 Waldock is doing is putting the cart way in front of the horse
22 at this point in time. The structure, the nature of the
23 organization, in fact the control of the Permanent Fund has
24 not been established. We don't know whether or not it's going
25 to be an agency which is directly related to the state, falls

1 under the state regulatory statutes, falls within the statutes
2 which he's referring to, falls within those confin... The
3 Permanent Fund, or the management entity which has direct
4 responsibility for investing or not investing these funds,
5 the decision making process has not been identified or
6 defined. So I think his question might be very pertinent,
7 but at this point in time it is impossible to say, or even
8 to ask a legal Opinion on it.

9 MR. WOHLFORTH: I'll have to rule, as the Chair, that
10 we've exhausted the subject. If someone wants to make a
11 motion we can deal with, otherwise we'll go on to another
12 question. We've got a lot of things to say in here. I don't
13 want to cut anybody off, but just idle conversation on the
14 thing will keep us here until 6:00 o'clock without getting
15 into some of the really important items. If there is a motion
16 it will be recognized.

17 MR. MOTLEY: I would move that I would be happy to
18 work with Mr. Waldock and anybody else whom you appoint to draft
19 the question and ask the Attorney General. There may be
20 ramifications down the stream; maybe White, Weld and the
21 rest of the world would like to know what their ramifications
22 are downstream.

23 MS. FLEISCHER: Second.

24 MR. WOHLFORTH: Second to the motion. Any discussion?
25 All those in favor say, "Aye."

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(Whereupon Committee members said, "Aye.")

MR. WOHLFORTH: Opposed. So ordered.

MR. MOTLEY: Do you want to appoint anybody else, Mr. Chairman, to draft that question?

MR. WOHLFORTH: Well, you and Mr. Waldock work on it.

MR. MOTLEY: Anybody else that would like to work on it ---

MR. URION: Mr. Chairman.

MR. WOHLFORTH: Yes.

MR. URION: Mr. Chairman, before we get completely off of this subject matter here, I'd like someone to explain to me this \$30,000 you had in your budget there for Legislators to use how they see fit. I happen to be a Legislator.

MR. EDENSO: Mr. Chairman, I didn't say they could use it as they saw fit. I merely pointed out that they could use it as they determined they wanted to use it in their efforts in participating in the Permanent Fund.

MR. URION: How is it being used?

MR. EDENSO: To the best of my knowledge, it's being used for expenses incurred by the Legislators for matters relating to the Permanent Fund, for telephone, for some travel, etc., and I think the people who are directly responsible for that, I would ask that they add to what I have said.

MR. MALONE: Mr. Chairman.

MR. WOHLFORTH: Yes, Mr. Malone.

1 MR. MALONE: The appropriation was made in the Execu-
2 tive Branch, so what they have done is actually set aside
3 \$30,000 for the Legislature to basically make proposals
4 against. Now, it's the budget for that \$30,000 which, for
5 the most part, myself and Senator Kerttula have worked up.
6 Jim doesn't have that budget here, but if you ask him he can
7 get you a copy of it. The primary expenses are staff and
8 office expenses.

9 MR. URION: It's kind of unusual to give money for
10 Legislators to the Executive Branch. What are we trying to
11 do, hide it from the taxpayers, that the Legislators spent
12 about another \$30,000?

13 MR. GALLAGHER: The intent behind that was that the
14 Administration and the Legislature are cooperating in this
15 effort. We put the money in one place just like in a tax
16 study. Most of my funds for my study is put in the Legis-
17 lature. I go with proposals to the Legislature; they find
18 them worthy or they don't find them worthy.

19 MR. MALONE: Mr. Chairman.

20 MR. WOHLFORTH: Yes.

21 MR. MALONE: One further comment on that, Rick.
22 Probably, normally those funds would have been transferred
23 and accounted for separately, but because of some legal
24 confusion on the transfer of funds, elected not to ask for
25 transfer right now.

1 MR. RHODE: At one time it was prepared to go to the
2 Budget and Audit Committee to make the formal transfer of
3 the \$30,000, but you're familiar with the legal posture of
4 that Committee in regard to transfers of appropriations.

5 MR. GALLAGHER: Let's say they're prepared to receive
6 the money.

7 MR. URION: I understand I'm the sixth vote too.

8 MR. WOHLFORTH: Mr. Love.

9 MR. LOVE: I don't know if the entire Committee can
10 resolve the dispute between Rick and his colleagues, but there
11 is something that involves the issue of consultants that I
12 wanted to ask Dennis. I have a concern that as we're going
13 along a lot of the presentations today seemed to all point
14 in the direction that we're going to develop this development
15 bank, and that most of the advice in this meeting today I
16 felt was provided and (I hope I'm not of the wrong impression)
17 that we've already committed ourselves to a direction like
18 that without other alternatives and without hearing from the
19 public before we commit ourselves to that choice or any other
20 choice.

21 What I wanted to express, at least, before this meeting
22 is over that it's my hope that one of our very next meetings
23 will be a meeting where the public has an opportunity to
24 appear before us and tell us what their thinking, what their
25 ideas are for the Permanent Fund, and to have some input there,

1 and that we also keep in mind that there are probably many
2 different other approaches to the investment purposes for
3 the development, many different ideas and proposals that
4 we should probably at least hear before we make our mind up
5 about what the proper direction is. I'm expressing this
6 because I'm not sure whether we can commit ourselves in any
7 direction. I certainly am not committed in any direction
8 without hearing more advice from more people and having more
9 information, and also having an opportunity to hear from the
10 public.

11 MR. MOTLEY: Mr. Chairman.

12 MR. WOHLFORTH: Yes.

13 MR. MOTLEY: Jamie, I don't think anybody is committed.
14 There isn't going to be any commitment until November 2nd, or
15 3rd, or whatever. I think what we did today was most
16 enlightening. It's probably the initial intellectual exercise
17 to figure out what may happen if certain things do occur,
18 and I think there were some very visionary questions that
19 were asked here. I think when you take it back to brass
20 tacks they put it very well. I mean, what is the mission.
21 I can tell you that as a voter, just as a voter, and you
22 assume that the voter doesn't have the benefit of these dis-
23 cussions that have gone on today and the benefit of this good
24 work, then as a voter you have to take a very strict con-
25 structionist approach, to coin a phrase, and that is that

1 it says -- in the one thing that changed the Constitution it
2 says income producing investment, and I think that's where
3 you have to start from. There isn't any mention in there,
4 and it won't be on the ballot about it, and that's social
5 benefits versus net social costs. There won't be anything
6 in there about subsidies, there won't be anything in there
7 about soft loans, there won't be any of that stuff in there.
8 I think we have to keep that in mind. That's where it's
9 starting from, and that doesn't come for another two or three
10 weeks. I don't mean to say that what we did today -- I mean,
11 we're ahead of the power curve for once, but I think we have
12 to keep that in mind, exactly what the voters are going to
13 be looking at; that's just that one line that appears on the
14 ballot, and that's it.

15 MR. WOHLFORTH: Do we have any more comments on this
16 matter of goals and objectives, or any other comments?

17 MS. FLEISCHER: Yes.

18 MR. WOHLFORTH: Yes, Mrs. Fleischer.

19 MS. FLEISCHER: Well, I am really reluctant to leave
20 the room without some decision on establishing the goals and
21 objectives of the Committee. I would like for us to decide
22 to decide to do that, and I so move.

23 MR. LOVE: To decide to decide?

24 MS. FLEISCHER: I move that we make the next order
25 of business a discussion of and decision upon, if we can do

1 that, the goals and objectives for the Permanent Fund.

2 MR. MOTLEY: Mr. Chairman, is the motion on the floor
3 and open for discussion?

4 MR. WOHLFORTH: I haven't heard a second yet.

5 MR. LOVE: I'll second.

6 MR. MOTLEY: I'll second just for the sake of putting
7 it open for discussion.

8 MR. WOHLFORTH: It's open for discussion.

9 MR. MOTLEY: I think it's a little premature at this
10 stage of the game.

11 MS. FLEISCHER: Well, when are we going to meet next?

12 MR. MOTLEY: Well, I don't know.

13 MS. FLEISCHER: After the election in November?

14 MR. MOTLEY: Believe me, I really think it would be
15 presumptuous of us to come down with all kinds of goals and
16 objectives when there's just a one liner that's going to be
17 on the ballot.

18 MS. FLEISCHER: Well, by the next time we meet we'll
19 know whether we have a task or not.

20 MR. MALONE: Mr. Chairman.

21 MR. LOVE: That's right. I'd just like to say
22 something else, and that is ---

23 MR. WOHLFORTH: Let the Chair recognize Mr. Malone.

24 MR. MALONE: Thank you, Mr. Chairman. As Commissioner
25 Motley expressed himself there, I really have to agree with

1 him. The very creation of this fund in the first place is on
2 the ballot to be decided November 2 by the people of the state,
3 and while I'm quite hopeful the outcome of the election will
4 be positive, I feel it is presumptuous right now to start
5 laying out goals, and I think that is definitely the charge
6 that the Governor gave to this Committee, but I think it
7 would be precipitous to do it right now.

8 MR. WOHLFORTH: Yes, Jamie, you're next.

9 MR. LOVE: I think that this Committee is going to
10 have to be looking at the question of developing some pretty
11 important goals and objectives relative to investment policies
12 regardless of what happens to the Permanent Fund. Now, we all
13 know that the reason the Permanent Fund is being created
14 is that we're looking at some mechanism to deal with anti-
15 cipated surpluses of revenue; we're going to be having more
16 revenue, that's what our projections are, than the state is
17 going to spend. So there's going to be an amount of money
18 in excess of the amount that we've described as the Permanent
19 Fund, regardless of whether or not the Constitutional Amend-
20 ment passes. I think that the state is going to have to tackle
21 this problem of devising a good investment policy for those
22 funds regardless of the outcome. Also I think also that's
23 something that -- you know, in some of the recent reports
24 like the Times editorials and some of the other news reports,
25 I almost get the impression that some people are talking as if

1 the Permanent Fund is going to create a problem of having
2 to deal with all this revenue and make all these loans and
3 make all these investment decisions. I think it's important
4 for this Committee, as the Governor's Investment Advisory,
5 to realize that the Permanent Fund doesn't have anything to
6 do with whether or not those policies are going to have to
7 be developed. Those policies are going to have to be
8 developed by virtue of the fact that the money is going to
9 be there and somebody is going to be making those decisions.
10 You know, regardless of the outcome of that amendment that's
11 up on the November ballot, this Committee is going to have
12 to start developing some broad policy goals and objectives
13 in terms of how the surplus is going to be invested, and they're
14 also at some point going to have to start involving the public.

15 MR. LOGSDON: Mr. Chairman.

16 MR. WOHLFORTH: Yes.

17 MR. LOGSDON: Am I correct that the purpose of the
18 standing committee is to address only the Permanent Fund?

19 MR. WOHLFORTH: I think that's correct, yes.

20 MR. WOHLFORTH: So that if there's a "no" vote on
21 the ballot, this Committee then automatically reconstitutes
22 itself to what it was.

23 MR. WOHLFORTH: I hadn't understood that until today,
24 but I guess that's right.

25 MR. MOTLEY: I think that the statute is very clear

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as to the membership. It's very broad.

MR. GALLAGHER: You can appoint any amount of members you want.

MR. MOTLEY: It's up to the Governor.

MR. WOHLFORTH: New members have, in fact, been appointed, have they not?

MR. GALLAGHER: Yes.

MR. WOHLFORTH: And they've gotten certificates.

MR. LOGSDON: May I offer an amendment to the motion, that if the voters approve the Permanent Fund before the next meeting that this issue be considered, the issue of objectives of the Permanent Fund be considered at the next meeting?

MS. FLEISCHER: You mean that would be the main order of business, which is what I was interested in.

MR. LOGSDON: Well, that was your motion, wasn't it?

MR. WOHLFORTH: Do you consent to the amendment?

MS. FLEISCHER: In the event that it passes.

MR. LOGSDON: Then we would have a mandate at that point to address this issue, I think.

MS. FLEISCHER: Right, but I do have a question. I guess we're not clear as to whether that's the sole purpose of the expanded committee or not.

MR. WOHLFORTH: I think the question is right now, do you accept the amendment or not to your motion. Would

1 you accept the amendment?

2 MS. FLEISCHER: I understand the question. I'm just
3 wondering, if it fails then what is the Committee going to do,
4 not talk about the goals and objectives.

5 MR. LOGSDON: Then the Committee is not going to
6 look to the objectives of the Permanent Fund because there
7 won't be one.

8 MS. FLEISCHER: Okay, I accept the amendment.

9 MR. WOHLFORTH: You accept the amendment, all right.

10 MR. GALLAGHER: Let's just talk about this whole
11 subject of goals and objectives. You know, this thing didn't
12 get this far down the line without talking about something
13 before the Legislature, and we talked about -- you know, the
14 Fund has a lot of broad base public support, and the public
15 obviously believes in something out there. From what I can
16 tell from the public support for the Permanent Fund, it's
17 coming out of three different sectors. There's those who
18 believe in savings account concept, there's those who believe
19 in community development and there's those who believe in
20 economic diversification. Now, maybe there's a fourth or a
21 fifth goal that I don't perceive of there.

22 MS. FLEISCHER: You mean you're saying that's what
23 the goals are, that's your choice?

24 MR. GALLAGHER: No, that's among the wide range.
25 That's at least those goals that I brought to the public.

1 The choice hasn't been narrowed down to all three.

2 MS. FLEISCHER: No, I know that. I wanted to clarify
3 that. I didn't mean that we should decide what the goals
4 and objectives were going to be within the next meeting. I
5 mean we should make that our next task, and I don't say that
6 it is a short nor an easy task. I do think it has to involve
7 the public and it has to involve the results of the public
8 forum and a public discussion on the whole fund. I'm saying
9 it hasn't been done yet, or if it has been done, if the
10 decision has already been made as to what the goals of the
11 Permanent Fund are going to be, then let's have that on the
12 table.

13 MR. WOHLFORTH: That's been expressed several times
14 today, that this group has decided the goals and objectives.
15 How can one say that we haven't honestly, and have you believe it?
16 I haven't; I don't think anyone else has.

17 MS. FLEISCHER: Okay, then I think that should be
18 the next thing we do.

19 MR. WOHLFORTH: The motion is to consider goals and
20 objectives at the next meeting if the Permanent Fund passes.

21 MR. MOTLEY: Is that your amended motion, Lanie?

22 MS. FLEISCHER: That sounds right.

23 MR. MOTLEY: I'm looking to you because I was the
24 second. Is that right?

25 MS. FLEISCHER: I said that, yes, we should start at

1 the next meeting to make that our main task.

2 MR. WOHLFORTH: All right. Do we have any further
3 discussion on that motion? Are you ready for the question?
4 All those in favor signify by saying, "Aye."

5 (Whereupon the Committee members responded
6 by saying, "Aye.")

7 MR. WOHLFORTH: Opposed. It passes. I may suggest
8 that I think what Commissioner Gallagher has presented in his
9 initial talk outlines some, at least, of three possible goals;
10 indeed, there may be more.

11 MR. LOGSDON: Mr. Richards also had a list of eleven
12 points, I think that could be considered objectives.

13 MR. MOTLEY: Mr. Chairman, could I make one comment?
14 You have to understand that with regards to the public
15 perception of the Permanent Fund, as time goes on it becomes
16 more and more public aware. It's put on a ballot, it's dis-
17 cussed by the Legislature, it's put on a ballot, people speak
18 for it, but prior to that time no decisions have been arrived
19 at, but that doesn't mean that there haven't been some people
20 who were paid by the state to think about this and haven't
21 been thinking about it, and one of the guys is sitting right
22 over there. He's been thinking about this since he went
23 to Juneau, and I think it's proper that he did, and I don't
24 think he's arrived at any conclusions. There haven't been
25 any decisions made as to goals and objectives. He's just doing

1 his job, kind of getting ahead of the game, and that's really
2 where we're at. Nobody has made any decisions.

3 MS. FLEISCHER: Well, some of the presentations imply,
4 at least, a direction.

5 MR. EDENSO: Well, one has to start somewhere.

6 UNIDENTIFIED: You got up here and you throw the rock
7 out in the pond and then you start rowing.

8 MR. GALLAGHER: I'd like to quarrel with that a
9 little bit. These people talked about a development bank.
10 Now, what is a development bank? A development bank does a
11 lot of social sort of things. It's community development and
12 economic development, one of the three things I laid out as
13 the objectives. Another one was savings accounts. If you
14 accomplish social and economic objectives with a development
15 bank and you strip away the word "development" but you look
16 at things that accomplish social objectives and economic
17 objectives, you know, what else is there, things to put
18 money in.

19 MS. FLEISCHER: Are you asking me?

20 MR. GALLAGHER: Yes. If the thing doesn't have a
21 social objective and it doesn't have an economic objective,
22 what else is there to put money into?

23 MS. FLEISCHER: Savings account.

24 MR. GALLAGHER: Yes, the only other third objective
25 could be a savings account.

1 MS. FLEISCHER: Okay, but we've used all the money for
2 consulting, unless we have other questions.

3 MR. WOHLFORTH: I think I have to recognize Mr. Love
4 and cut off the private colloquy.

5 MR. LOVE: I'd like to respond to what Sterling is saying,
6 first of all by making a general comment that I, for one, have
7 really enjoyed the presentations today and I think there was
8 a lot of thoughtful discussion and I appreciate the materials
9 we have received so far, and I do appreciate the necessity
10 for the Administration, who have been doing a lot of planning
11 on an ongoing basis like this, and I think it's really good
12 that they've started involving the public at this point
13 through the expansion of this Committee at a very early
14 point. It's a very positive thing and I have really a lot of
15 confidence in the good will and everything else of the
16 administration in this thing.

17 I do think that, you know, when we get into this talk
18 about goals and objectives -- I think that a lot of Com-
19 missioners feel that there is a lot of -- that generally out
20 there in the public that people's perception of what this
21 Permanent Fund -- it's so different from each person that
22 you talk to, that there's a necessity for this group to
23 sit down and discuss some of the basic assumptions about
24 just exactly what everyone's different idea is, and I think
25 that is what Lanie is getting at with her suggestion that

1 we get into a process where, as a Committee, we start dis-
2 cussions of our goals and objectives. Not every member of
3 the Committee, I think, feels comfortable with saying that
4 their own perception is apt to be shared by either the voters
5 or even by people they've met in the last fifteen minutes.
6 I think it's probably a need that many Commission members
7 themselves feel they have to have a more general discussion
8 about some of these things before we go much further, and I
9 think that's a lot of the stuff that Lanie's getting at.
10 I don't think it's any indication of a lack of appreciation
11 or support for any of the efforts of the administration or
12 the Legislature so far.

13 MR. WOHLFORTH: Any further comments here?

14 MR. MOTLEY: I move for adjournment.

15 MR. GRUENING: I'll make it quick then.

16 MR. MOTLEY: I withdraw the motion, in deference to
17 somebody that sits on my budget, or did, and probably will.

18 MR. GRUENING: This charge of the Governor is pretty
19 ambitious, in looking this over, and perhaps Sterling or
20 somebody could talk to what's the deadline on this thing.
21 It seems to me the Legislature convenes January 12 and they're
22 going to start, I imagine, on this matter too. At this point
23 we wouldn't give much assistance to the Legislature or the
24 Governor. Maybe we might want to narrow some of the -- if
25 we're going to just concentrate on the Permanent Fund, narrow

1 our attention at least if we're going to get something out
2 that is going to be of assistance to the Legislature and the
3 Governor by convening. I'm just suggesting that goals and
4 objectives is a pretty heavy task in itself. Between now and
5 the election I think, as individuals, the best we can do is
6 say, as Tony points out, these are the limits of the fund,
7 this is income producing, and try to describe what the language
8 could mean. But as far as beyond that, I think really
9 limited, and we're probably limited in the amount of time
10 we're going to have to deal with it before the Legislature
11 convenes. Maybe the Governor doesn't intend that to be a
12 deadline, but somebody ought to carry the message to him;
13 these are some real deep issues here.

14 MR. MOTLEY: It will be carried by special messenger.
15 Isn't that how we got things done earlier?

16 MR. GRUENING: Yeah, thanks.

17 MR. WOHLFORTH: Let me try this out on you. Frankly,
18 it's been suggested to me, but I think it's a practical
19 suggestion. One date that was suggested for the next meeting
20 was November 5. We recognize that meeting times will never
21 coincide with everybody's availability and so on, but that
22 is, of course, after the election -- it's several days after --
23 that the next meeting contain time for public input, if you
24 will, with advertisement, obviously, so there can be public
25 input of the kind that was suggested here, that a sub-committee

1 act in the meantime with Mr. Edenso developing questions,
2 pinpointed questions, for the consultants so that we can
3 carry from all the Committee members here today questions
4 that will really put them on their metal and develop more
5 specific information where members feel the need to have
6 gaps filled or more ongoing experiences actually detailed.
7 That is my suggestion and I would entertain a motion, if
8 someone would so move, to at least get it on the floor for
9 discussion, that the meeting date be November 5, that there
10 be time for public discussion and that there be a sub-committee
11 appointed to meet with the Commissioner or his Deputy to
12 pinpoint specific questions we want answered at that meeting
13 from the consultants.

14 MR. GRUENING: Can we divide the question? It's got
15 three things there.

16 MR. WOHLFOPTH: Sure.

17 MR. GRUENING: The meeting date, that sounds like
18 a good time. I'll second the motion.

19 MR. WOHLFORTH: Is that satisfactory? Okay, the
20 next meeting will be ---

21 MR. GRUENING: Possibly 5 and 6.

22 MR. WOHLFORTH: Oh, it's a two-day meeting then?
23 The 6th is Saturday.

24 MR. GALLAGHER: That's fine. I'm in New York and
25 flying backward.

1 MR. WOHLFORTH: All right, a two-day meeting, Friday
2 and Saturday, the 5th and 6th. That's the proposal, it's
3 a motion. Is there any objection to that? All right, the
4 next meeting has been established as November 5 and 6.

5 MR. GRUENING: Then the other one -- I don't happen
6 to remember all of the other one -- the other one was the
7 public participation, and I so move that we advertise ahead
8 of time, perhaps even starting now before the election.

9 MS. FLEISCHER: Would you say that in the form of a
10 public participation in the morning and then we could possibly
11 entertain it that afternoon?

12 MR. WOHLFORTH: Sounds like a good idea.

13 MR. EDENSO: Mr. Chairman, I do have a problem with
14 that. If we advertise now for public participation in a
15 meeting that is somehow never going to happen because the
16 amendment didn't pass on the 11/2 election ---

17 MR. GALLAGHER: You know, I think there might be
18 something to do; what do you do it, with the Permanent Fund
19 that's already in the General Fund. The Committee could
20 sit down and really discuss and see what we'll do with the
21 Permanent Fund.

22 MR. LOVE: I might just say that the purpose of the
23 meeting would be for people to come and address the Committee
24 on the issue of investment policy because that issue is still
25 before us regardless of whether we have a Permanent Fund or not.

1 MR. WOHLFORTH: All right then, is that satisfactory,
2 that the meeting day the morning be devoted to public input
3 and so on? Then finally, a sub-committee, or whatever, to
4 work with the Commissioner of Revenue on pinpointing questions,
5 specific questions, for the consultants to answer at that
6 meeting. Does anyone want to move that or not?

7 MR. LOVE: The problem I've got with that is so far
8 I've had -- both the administrative representative, Mr. Edenso,
9 and administrative representative, Mr. Rhode, and both indicated
10 that if I had any questions to channel to the consultants
11 all I had to do was write them out and send copies to both
12 Mr. Rhode and Mr. Edenso and they would make every attempt to
13 have those questions addressed by the consultants, and I have
14 been very satisfied with the cooperation of both those people.
15 I feel there is a vehicle right now if any member of this
16 Commission wants to do that, they can just provide that
17 information and channel it through these two staff people so
18 that everything is coordinated and there would be somebody
19 that would know what's going on all the time. I don't know
20 if it's necessary really for the Committee to do this.

21 MR. WOHLFORTH: Mr. Rhode.

22 MR. RHODE: Mr. Chairman, one of the terms of the
23 second part of your divided motion -- if there would be
24 room, for example, to have some working sub-committees of
25 members of this Committee, perhaps people that are most

1 concerned about possible social goals for the fund in terms
2 of the long program, or those who are more concerned about
3 long-term development, or those who are more concerned about
4 the fund being used in some sort of savings account, then we
5 could make, I think, far more economical use of the consultants'
6 time. Their fees run -- but, of course, with a large meeting
7 like this it's difficult for them to come to grips with the
8 full list of questions that people have. So, would your
9 motion bar some kind of ---

10 MR. WOHLFORTH: I'm not making the motion. Someone else
11 will have to make it. As Chairman I've suggested it for
12 everyone's consideration.

13 MR. EDENSO: Mr. Chairman, I would like to point out
14 Mr. Rhode and myself have worked at some considerable length
15 by default in getting our consultants activated, on board,
16 and responding to some major areas of concern we feel that
17 we've identified here. The Committee up to this point in
18 time has really given us no direction on this, and what
19 Mr. Rhode is asking, and I really appreciate it, is that
20 unless you do give us some direction I'm going to just charge
21 on like I want to get the job done.

22 MR. LOGSDON: Like you have to get the job done!

23 MR. MALONE: Mr. Chairman.

24 MR. WOHLFORTH: Mr. Malone.

25 MR. MALONE: On the subject, if a general discussion

1 is planned at the next meeting as well as participation
2 by the public, I would think that the concept of sub-committees
3 might be more valuable after some of those things are
4 hammered out, the sub-committees after the charge. I'd hate
5 to set out those tasks without some consideration.

6 MR. MOTLEY: I would support Mr. Malone.

7 MR. WOHLFORTH: What is the pleasure of the group?

8 MR. GALLAGHER: I wonder if there isn't something
9 that I may want. I'm asking the Committee if they have some
10 questions they also want the advisors to address at the
11 next meeting.

12 MR. MALONE: Mr. Chairman.

13 MR. WOHLFORTH: Yes.

14 MR. MALONE: I'm not sure all the members of the
15 Committee are familiar with the procedure Mr. Love described,
16 but I think it's probably an adequate way of getting a
17 specific question.

18 MR. WOHLFORTH: Well, I take it the sense of it --
19 I think the sense of the meaning ---

20 MR. MOTLEY: There never was a motion, was there?
21 I don't recall any motion.

22 MR. WOHLFORTH: Scratch the idea of the sub-committee
23 for now. Let me say by the next meeting I hope you find
24 a Chairman, not me -- not that I haven't enjoyed the
25 experience.

1 MR. MOTLEY: I think you've worn the mantle well, Eric.

2 MR. WOHLFORTH: I'll entertain a motion for adjourn-
3 ment. Oh, we have some other business.

4 MR. LOVE: I would like to introduce Mr. Batko, Bill
5 Batko. I had recommended to the administration and told
6 them that myself and Lanie talked to a couple of the members
7 of this Commission and he's worked with us. He's been doing
8 some work which we submitted to the board in short papers
9 having to do with different types of not such gigantic, but
10 smaller development corporations. I just wanted to introduce
11 him so if anyone wanted to talk with him -- he's only going
12 to be here two more days -- if anybody wanted to talk to him
13 they could. I would like you also to be aware that he's
14 going to be submitting to this Committee a -- this is a \$500
15 for personal services, very small -- he's going to be submitting
16 some papers after he gets back to Vermont and thinks about
17 everything, all the discussions that went on here.

18 MR. WOHLFORTH: Go ahead.

19 MR. EDENSO: Mr. Chairman, I would also like to
20 introduce Mr. Ken Jensen from from Arthur D. Little at
21 San Francisco. We have held conversations and have a tenta-
22 tive contract with Mr. Jensen, and the purpose of the contract
23 is to ask Arthur D. Little to provide us with some national
24 economy questions, given the potential size of the Permanent
25 Fund and the nature of Alaska's economy and what Alaska's

1 economy might look like in the future. The reason for this
2 type of information is to give the Committee, or provide
3 the Committee information which relates directly to potential
4 investment policy. For example, do you want to cut a per-
5 centage of the fund and dedicate it to certain specific kinds
6 of investment in Alaska? Do you want to put a ceiling, a
7 maximum size ceiling on a potential investment or an area
8 of the economy and say, "You shall not invest any more than
9 this amount in this particular area," and we think that with
10 the experience Arthur D. Little has had in doing this kind
11 of analysis in the past that they would provide us some
12 fairly good information. However, as I pointed out earlier,
13 there are considerations for the budget and the budget size.

14 MR. MOTLEY: With that in mind then, you're asking
15 for the Committee's approval. I'd like to review that
16 contract to make sure that we avoid any kind of duplication
17 on the other efforts that are involved in establishing that
18 for the state. I would withhold that until I've had a chance
19 to review that contract.

20 MR. EDENSO: I'm familiar with your potential contract,
21 Tony, since it was let, your contract with the company.
22 What we're asking for is results of the effort of their
23 model, (we're not asking them to resolve the model for us)
24 results of their model, given characteristics of the nature
25 of the economy in Alaska, working in close coordination

