

LEG. FINANCE - BILLS 1979 - 1980 1295

SB 170 cont. 1095

III. Distribution of the federal and State subsidies

A GSOC may be useful as a device for capturing and redirecting federal tax revenues on earning assets. However, the GSOC's own budget, no matter how spartan, can only draw from the subsidy pool. Moreover, even before the subsidies get to the GSOC, a portion will be diverted to asset sellers in the form of inflated market prices. An additional portion of the subsidies will be absorbed by banks and other lenders who earn more money from engaging in leverage-arbitrage of their own than they do by creating those opportunities for others.

This observation explains why the powerful bank lobby did not oppose the "enabling" federal legislation. That lobby would almost certainly have opposed any serious attempt at diffusing stock ownership since it is precisely this issue--disintermediation--that the banks have lobbied against for so many years. However, the GSOC legislation promises to cut banks in on the subsidy (at least those banks who win the favor of the GSOC directors).

Under scrupulous and cold-blooded financial management, it might be possible to hold the subsidy diversions to a minimum. But to do so, the GSOC's directors must turn a deaf ear to the pleas of special interest groups. It is to be expected, however, that the GSOC directors will be besieged with requests for help from particular firms or industries that might be deemed essential to the State or local economy. Moreover, the subsidy diversion would be largely hidden in the sense that the GSOC still would be able to show a "profit" as long as it retains enough of the subsidy. Thus it may be difficult for GSOC directors to defend a decision to "support" some firms and some banks but not others. Such dilemmas always raise the possibility that political or other nonfinancial factors may influence the operating decisions of a GSOC.

In sum, while supporters may yet be able to show that GSOC benefits outweigh the additional costs that a State must bear under the federal "enabling"

legislation, thus far, little evidence has been offered in support of that contention. Instead, the case that has been presented is long on moral posturing, and long on railing against the sorry state of affairs that now exists, but painfully short in terms of sound economic reasoning that would lead one to believe that a GSOC offers any reasonable hope of achieving the expressed objectives. If left unattended, the existing biases in the federal legislation would funnel benefits to existing capitalists, as stockholders in banks and capital intensive firms, and to new GSOC bureaucrats, leaving an as yet undetermined fraction for (excess) distribution to citizen-shareholders. Even this distribution is regressive in the sense that the federal tax savings is greater for those in higher tax brackets. Since the same citizens must pay for the State subsidies (as well as their portion of the federal subsidy) either in the form of increased taxes or in the form of increased inflation (assuming that taxes are not raised), it is far from clear that the benefits outweigh the costs for any group of citizens. It should be clear, however, that the society as a whole loses since new costs are created but no new revenues are created to pay for those costs.

In the absence of "clarifying" analysis, the decision before the Alaska State Legislature appears to be one of whether or not to assist capital intensive firms in recovering part of the taxes they currently pay to the federal and State government. If so, a GSOC might be an appropriate vehicle, one that would also benefit selective banks and would create supporting jobs through its own bureaucracy. If sufficiently subsidized through tax benefits, loan guarantees, etc., a GSOC might even produce a modest excess cash flow to citizen-shareholders. However, if this is the ultimate goal, the State would be far better off to scrap the proposal for a costly administrative structure (the GSOC) and eliminate the subsidy diversions by simply distributing to its citizens the equivalent of the

proposed State subsidies to the GSOC. If it is deemed essential that checks be considered as "dividend" dispersements rather than as transfer payment (which they will be in either case), then the State might adopt a more ennobling title such as "the return on a citizen's share in State Wealth." It is doubtful that many citizens will feel all that different once they have cashed their checks. Only the banks and the capital intensive firms appear to have a strong financial incentive for favoring the more cumbersome and costly GSOC alternative.

Alaska General Stock Ownership Corporation
Effect of Purchase of BP share of TAPS
on Tariff Rate

MEMO from Harry Eppenbach (Senior Policy Analyst)

- 1) It is unlikely that AGSOC would get the Investment Tax Credit. Even if it did, it would be substantially lower than the current \$140 mil.
- 2) AGSOC may not have any federal tax liability but this could reduce the eventual tariff to within the \$4.28 - \$5.09 range.

MEMO from Richard Burnham (Assistant Attorney General)

- 1) The rate base would probably not include the full purchase price as assumed by KELSO because the FERC is leaning toward original cost less depreciation in determining the rate.
- 2) The KELSO report bases projections on a stationary tariff rate, however, if FERC bases initial rates on original cost less depreciation, then the rates will decline.

STATE
of ALASKA

MEMORANDUM

TO: Larry Eppenbach
 Division of Research Services
 Legislative Affairs Agency


DATE: March 22, 1979

FILE NO:

TELEPHONE NO:

FROM: AVRUM M. GROSS
 ATTORNEY GENERAL

SUBJECT: Kelso Report

By: 
 Richard M. Burnham
 Assistant Attorney General

I have briefly reviewed the Kelso Report and would like to pass on to you two of my comments.

First, at page 4 of Chapter 1, and again in Summary Table IV, the report attempts to project the amount of GSOP shareholder distributions given various tariffs and various purchase prices for BP's portion of TAPS. It appears that the assumption underlying the projections is that the full purchase price, whatever it may be, will be included in the rate base. For the following reason, I think that assumption is not only questionable, but probably completely in error.

The inclusion in the rate base of the full purchase price of a pipeline was what led to the Williams Brothers pipeline litigation. Petroleum Products, Williams Brothers Pipeline Company, 355 I.C.C. 102 (1975) (Williams I); 355 I.C.C. 479 (1976) (Williams II). There, Williams Brothers purchased a pipeline from the Great Lakes Pipeline Company for \$287.6 million dollars. Williams then turned around and included the full purchase price in the rate base for purposes of computing the tariffs, resulting in increased tariffs. Shippers objected to this inclusion of the full purchase price as part of the rate base because (1) the price was much higher than the sum of the money actually spent over the years by Great Lakes in putting the pipeline together and (2) Great Lakes had already been compensated, through depreciation, for almost \$100 million. Essentially, the position of the shippers was that through the rates they had paid for transportation of oil through the pipeline, they had already paid for much of the pipeline. For a purchaser to come along and charge a higher tariff based on a high purchase price would be to compel shippers to again pay for the construction of the pipeline. In the shippers' view, the rate base should have been computed on the basis of the original cost less depreciation, which in the Williams' case would have provided a rate base of approximately \$101.1 million, as opposed to Williams' \$287.6 million.

The ICC staff, using a "valuation" rate base, composed partly of original cost and partly of cost of reconstruction, came up with a suggested rate base of \$167.6 million.

Initially, the ICC sided with Williams Brothers and approved the increased tariffs. The shippers appealed, and the U. S. Court of Appeals for the District of Columbia remanded the entire matter to the new Federal Energy Regulatory Commission for purposes of reassessing whether in this day and age the "valuation" rate base is appropriate. Farmers Union Central Exchange v. Federal Energy Regulatory Commission, 584 F.2d 408 (D.C. Cir. 1968).

The whole question of whether a valuation rate base or an "original cost less depreciation" rate base should be used in pipeline regulation is pending before FERC in two cases in addition to Williams Brothers. In one, the Association of Oil Pipe Lines, composed of approximately 50 pipeline companies, has petitioned FERC to stay everything under the sun until the completion of Docket No. RM 78-2, Valuation of Common Carrier Pipelines, formerly Ex parte 308. That proceeding is a general rule-making proceeding addressing the whole question of what methodology should be used in the future to set pipeline tariffs.

The second case which has raised the issue is the Trans-Alaska Pipeline tariff case. There, the State of Alaska, the Department of Justice and the staff of the Federal Energy Regulatory Commission have all strongly argued in favor of the use of an "original cost less depreciation" rate base. My best guess at this point is that FERC will ultimately adopt an original cost less depreciation approach to ratemaking. If it does, Kelso's apparent assumption that purchase price will be directly related to the tariff which can be charged is erroneous. Even if ferc adheres to a valuation rate base, the full purchase price is not necessarily included in the rate base, as shown by the ICC staff's recommended rate base for Williams Brothers.

Along the same lines, I also noted that Kelso's projections of dividends to GSOP stockholders appear to be based on a tariff which would remain the same throughout the life of the pipeline. They may have taken this approach solely because it is extremely difficult at this juncture to forecast what the tariff will be from year to year when it isn't even known yet what the final tariff will be for the first year of operation. However, I merely note that if "original cost less depreciation" rate base methodology is

March 22, 1979

adopted by FERC, tariffs will necessarily decline over the life of the line as depreciation reduces the rate base. In the unlikely event that FERC adheres to the "valuation" rate base approach, tariffs based thereon will increase over the life of the line as the cost of reconstruction increases because of inflation.

If you have any questions or if I may be of any further assistance to you, please don't hesitate to contact me.

RMB:cb

STATE OF ALASKA
THE LEGISLATURE

POUCH Y - STATE CAPITOL
JUNEAU, ALASKA 99811
937-465-3800

LEGISLATIVE AFFAIRS AGENCY

MEMORANDUM

March 22, 1979

SUBJECT: AGSOC Dividends From Purchase of BP Share of Pipeline
(AKPRIG memo) (W.O. 6934)

TO: The Honorable Hugh Malone

FROM: Larry Eppenbach *LE*
Senior Policy Analyst

In this memo I shall comment on several issues that relate to the dividends AGSOC shareholders may receive from a purchase of BP's share of the TAP's pipeline. The issues include BP's unused Investment Tax Credit and how the tax free status of the AGSOC will affect the pipeline tariff it may file.

First, AGSOC shareholders shouldn't count on receiving BP pipeline's unused investment tax credit -- at least under the proposed transfer plan. For the AGSOC to receive the investment tax credit (ITC) it would have to acquire all of the shares of BP Pipeline Inc. and then liquidate that corporation while preserving the credit. This is a very complicated area of tax law and it is arguable whether or not the AGSOC could emerge with the credits intact. There is little doubt, however, that if the AGSOC attempted to purchase only the pipeline's assets and liabilities and not the corporation itself, then it would not be entitled to the ITC. The Kelso report appears to contemplate only the transfer of pipeline assets and liabilities to the AGSOC.

In addition, although BP Pipeline Inc. now has an estimated \$140 million dollar unused ITC, by the time a purchase by the AGSOC is consummated the ITC may be far smaller. The TAPS pipeline is now operating profitably under original tariff filings causing BP's U.S. tax liabilities to mount rapidly. The investment tax credit is more likely to be drawn down in payment of these liabilities than increased by additional investment in the line. It is impossible to predict how long the investment tax credit may remain, but three to five years appears to be a reasonable estimate.

For all of these reasons it is not likely that shareholders of the AGSOC would ever receive benefits of an investment tax credit when purchasing BP's interest in the pipeline. This is not to argue against any attempt to capture the credit but to suggest that its expected value may be so

small as to eliminate it from consideration in any analysis.

A second major question is the effect of an AGSOC owned pipeline's tax exempt status on its ability to file high pipeline tariffs and issue large cash dividends. This is also a highly technical area of both tax and regulatory law. To begin, the assumption that an AGSOC pipeline would be exempt from state income taxes may be erroneous --particularly the state tax on oil and gas production and transportation income. If the state grants the AGSOC tax exemption then, to the extent the state gives up revenue it would otherwise receive, the state is subsidizing the AGSOC. Since the real incidence of the tax is passed on in the form of a higher tariff to the oil shippers the tax exemption represents a real net revenue loss to the state and an expensive subsidy to the AGSOC.

The assumption that the AGSOC will pay no federal tax liability on income from pipeline ownership appears justified providing it flows through the income to shareholders. The assumption, however, that the AGSOC filed pipeline tariff will be in the same neighborhood of tariffs filed by taxpaying pipeline companies may not be justified. FERC is not likely to look favorably on "in lieu" tax provisions that would keep a tariff higher than it would otherwise be without the taxes. Although no one can forecast eventual FERC action this issue, any view that they may split the difference is not justified.

Further, as outlined in the attached memorandum from Deputy Attorney General Rich Burnham, there is no reason to believe that FERC would allow the rate base to increase if the purchase price of the pipeline should exceed the FERC set valuation. All of these factors suggest that the tariff of a AGSOC owned pipeline may be lower than those of other pipelines and, as Mr. Burnham further points out in his memorandum, they may go lower still should the original cost less depreciation rate base methodology be adopted by FERC.

How much lower? The amount of tariff reduction depends upon the size of the initial tariff. For example, assuming BP Pipeline's original filed tariff of \$6.35 a barrel, then the elimination of the federal tax liability would reduce that tariff \$1.26 to \$5.09 per barrel. At the other extreme, under the conditions imposed by the interim tariff of \$4.68 (now suspended) the elimination of federal tax liability would reduce that tariff only 40¢ to \$4.28. Should FERC move to reduce the eventual tariff by the amount of any federal tax liability then the eventual tariff should fall within the range of \$4.28 to \$5.09. These adjusted tariffs place the line outside the feasible range identified by Kelso and Company unless the AGSOC would be able to purchase the pipeline for \$1.3 billion and borrow those funds at an interest rate of seven per cent. These are not considered to be likely conditions.

The Honorable Hugh Malone

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March 22, 1979

A final question involves how the State of Alaska may benefit from a tariff reduction? Possibly the state could tender its own oil to the AGSOC pipeline and because of the lower tariff and resulting higher wellhead value the state would be able to receive more annual oil revenue.

However, the common carrier status of the TAPS line would tend to mitigate against any substantial revenue increase to the state. All other oil shippers would have to agree not to tender their oil to the AGSOC pipeline for the state to receive the entire benefit. In addition, at the present time, the state is not in the position to exercise its choice since it has a contract with ALPETCO for the sale of its oil at Pump Station 1.

I would be pleased to comment further on these issues should you so desire.

LE:lmk
Enclosure

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LE:lmk
Enclosure

DESIGN OF AN ALASKAN
GENERAL STOCK OWNERSHIP PLAN
VOLUME I

A REPORT TO THE ALASKA STATE LEGISLATURE

PRINCIPAL RESEARCHERS:

LOUIS O. KELSO
JOHN A. MISKIMEN
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KELSO & CO., INCORPORATED
SAN FRANCISCO, CALIFORNIA

FEBRUARY 15, 1979

STATE OF ALASKA

THE LEGISLATURE

BUDGET AND AUDIT COMMITTEE

February 21, 1979

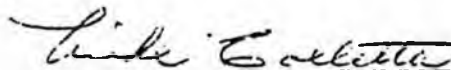
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Pursuant to an appropriation to the Legislative Finance Division contained in Chapter 163, SLA 1978, the Budget and Audit Committee entered into a contract with Kelso & Co., Inc. of San Francisco to provide a legal and financial design of a corporation which would (1) be owned by all Alaskan citizens; (2) invest in the development of Alaska's resources and its economy; and (3) do so with special tax status, in furtherance of the first two goals.

Enclosed is Volume I of Kelso & Co.'s report which provides an analysis of the salient features of such a corporation, now designated as General Stock Ownership Corporations (GSOC's) under Subchapter "U" of the Internal Revenue Code. Volume I contains a summary of the report, proposed Alaska legislation to establish a GSOC, recently enacted amendments to the Internal Revenue Code which provide special tax treatment for such corporations, and proposed articles of incorporation and by-laws.

Volume II of Kelso & Co.'s report is available from the Legislative Finance Division. Volume II is an appendix which contains legal memoranda regarding (1) federal constitutional issues and (2) the application of federal securities laws to GSOC's. Also contained in Volume II are other sections of the Internal Revenue Code referenced in Subchapter "U".



Senator Mike Colletta
Project Director



Representative Jim Duncan
Project Director

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FOREWORD

This volume contains the salient features of the design for an Alaskan General Stock Ownership Plan.

Included are the basic documents needed for legislative review. The separate appendix report (Volume II) covering the subject in greater detail is available from the Legislative Finance Division.

SUMMARY OF REPORT

The Nature of This Report

This report has been prepared by Kelso & Co., Incorporated pursuant to its contract dated September 1, 1978, with the State of Alaska, Legislative Finance Division. That contract provided that Kelso & Co., Incorporated (the "Contractor") will provide to the Legislative Finance Division and the Alaska State Legislature, on or before February 1, 1979, a design study for a General Stock Ownership Plan in the manner described in Contractor's proposal to the State of Alaska dated July 10, 1978, as amended by modifications indicated on an exhibit attached to the contract. The delivery date for the completed report was subsequently extended by Amendment I to February 15, 1979.

Broadly speaking, Contractor's proposal to the State of Alaska contemplated the development of a legal and financial design of a corporation to acquire and finance investments involved in the economic development of Alaska in such manner as to build broad capital ownership into all "residents" or "citizens" of the State of Alaska as these may be, from time to time, defined by the Legislature. Absent correlative legislation at the Congressional level, which did not exist at the time the contract was entered into, it was anticipated that a corporate entity could be designed of such nature that it could, during an initial period of years while major payments on the purchase price or construction price of its assets were being amortized, and prior to its distribution of dividend income to its shareholders, enjoy the character of an agency of the State of Alaska.

Such an agency would be entitled to the immunity of the sovereign State of Alaska from Federal taxation. It would in the most specific way be devoted to promoting the general welfare of the people of Alaska. Nevertheless, it was contemplated that efforts would be made, beginning immediately after the activation of such a corporate entity, to seek appropriate Federal legislation giving it and its shareholders tax exemption under Federal law so long as its income is being used to amortize the acquisition cost of assets, and to thereafter function as a private corporation broadly owned by its Alaskan shareholders.

As it happened, however, Senator Mike Gravel of Alaska, with our cooperation, drew a Federal General Stock Ownership Corporation Bill that would take, if enacted, the long first step towards making GSOCs readily feasible. Against incalculable odds, Senator Gravel managed to get Congress to adopt the law, and on November 6, 1978, the President signed into law the Revenue Act of 1978, Title VI of which authorizes the establishment of General Stock Ownership Corporations, giving immunity from Federal corporate income taxes to corporations specially chartered by a State Legislature and containing the requisite characteristics set forth in the Federal law. Thus the ultimate goal of the contract was in part accomplished: General Stock Ownership Corporations (GSOCs) organized after December 31, 1978, and before January 1, 1984, were granted permanent immunity from Federal corporate income tax. The new Federal law, however, has one shortcoming: The corporate taxes that would otherwise be collectible from the corporation itself are to be borne, pro rata, by its shareholders, even before amortization of the purchase

price it pays for productive assets has been amortized.

In terms of practical meaning, this would suggest that Alaska General Stock Ownership Corporation (AGSOC) should initially invest in income producing assets of such nature that the combined investment tax credit, depreciation and interest costs would eliminate any tax on shareholders in the early years of operation and quite possibly permit the payment of dividends. Such dividends would be taxed as ordinary income in the particular stockholder's tax bracket.

Discussion with the Legislative Finance Division yielded a mutual understanding that Kelso & Co.'s contract should be interpreted as calling for the design of a General Stock Ownership Corporation that would take advantage of the pioneering new Federal law, and this report reflects that accommodation. Implicit in favorable action by the Alaskan Legislature in the adoption of AGSOC as herein proposed, or any variation thereof, is the assumption that efforts would soon thereafter be initiated to persuade Congress to perfect the one shortcoming in Title VI of the Revenue Act of 1978 to ultimately extend the immunity from Federal income taxation to GSOC shareholders to the extent of income applied to purchase productive capital assets for the corporation. If the assets initially purchased by AGSOC are characterized by high depreciation and investment credit deductions, and if Congress is ultimately persuaded to make such alteration, the end result would be better than the design contemplated by the literal terms of the contract because of the permanent immunity to corporate Federal income taxes, the limits on concentration of ownership, and the requirement of a high payout of

earnings as dividends.

Recommendations of the Report Concerning the Operations of AGSOC

The Federal law makes the initially issued stock non-transferable by the shareholders for a period of five years following initial issuance except in the case of death of a shareholder or upon the shareholder's ceasing to be a "qualified resident" of the incorporating state. In addition, legislation proposed in this report restricts transfers of shares until the shareholder reaches the age of majority as provided for by Alaska law and does not permit any assignment, pledge, mortgage or other encumbrance of shares for five years. The Federal law does not require that a shareholder leaving the state sell, transfer or forfeit his stock, and the design proposed in this report permits such emigrating shareholder to take his stock with him in order to continue to enjoy its income in the future. However, he would not be able to sell, or otherwise transfer, his share to any person who is not, at the time of such transfer, a qualified resident of the State of Alaska. The object both of the Federal GSOC law and of the enabling legislation proposed herein is to broaden the ownership of productive capital by individual residents. The whole tenor of both the Federal law and the enabling legislation contemplated herein is to inhibit concentration of the ownership of AGSOC shares.

Marketability and Sale Value of AGSOC Shares

Since AGSOC shares can only be owned by individuals, and no individual may acquire more than ten shares of the corpora-

tion's stock, a public market in the shares in the usual sense of public stock markets in the United States today will presumably never arise. Public stock markets are in essence speculator markets. For the most part, buyers buy to sell at higher prices, and sellers sell with a view to purchasing something else that will rise in value so that it can be sold "for profit". This does not mean, however, that limited selling and buying of AGSOC shares as permitted in the event of death of a shareholder, or emigration of a shareholder from the state, cannot occur during the period of the five year non-transferability restriction imposed by Federal law. Undoubtedly, in the event of a desire to sell such shares, either a direct qualified resident buyer would be found by the seller, or the shares would be temporarily transferred into a general escrow account either in the trust and escrow division of AGSOC, or in any duly appointed outside transfer and escrow agent, until the seller's representatives, or a qualified stock broker, could find a buyer. In such case, the broker would be precisely that, bringing seller and buyer together and charging a fee, with the transfer being made directly from the individual seller to the individual buyer. This proposed design recommends that such sales during the initial five year restriction period, in the case of emigrants from the state, be at the then current book value. During this five year period, the corporation shall have the right of first refusal to purchase such shares if it desires to do so.

After the expiration of the five year period of restricted alienability, or the attaining of majority age by the shareholder, whichever is later, a strictly investor market for AGSOC

shares will undoubtedly arise. The report recommends that during the initial five year period, the price obtainable upon any sale of AGSOC stock, where the reason for the sale is emigration, be pegged at book value, which could significantly discourage such sales. Sales of AGSOC stock by estates of decedents would be determined by negotiations of the buyer and seller. After all, the object of AGSOC is to build the ownership of income producing capital into Alaskan residents. GSOCs, by Federal law, confer a high degree of private property upon their shareholders inasmuch as they will effectively be required to pay out 90% of their net income in dividends each year. This gives the "wages of capital" represented by AGSOC stock something of the character of private property enjoyed by the wages of labor: They are paid periodically and dependably, if earned. Kelso & Co. recommends a far-ranging educational and communications program between AGSOC and its shareholders to encourage them to not sell their AGSOC shares, and to look to them as a source of income.

Kelso & Co. also recommends that quarterly valuations of AGSOC shares be made and that this information be made available, as speedily as possible after each valuation report, to all shareholders. Presumably, therefore, in a free investor market, the expert appraisal of independent professional appraisers will influence the price at which shares of AGSOC stock are traded. The investor interest of buyers should dominate such a market and it should be relatively free of speculator interest.

The Governance of AGSOC

As a private business corporation, AGSOC, it is recommended, would have a management made up of the most highly trained professionals available and a Board of Directors of which a majority would be Alaska residents. Because it would be owned initially by all residents of Alaska, it could properly enjoy financial support of the State or its agencies in a number of ways. It could receive, if authorized by the Legislature, a loan or guaranty of a loan of start-up funds to enable it to organize, hire professional management, pay directors' fees, negotiate for the acquisition or construction of productive assets, and negotiate financing. Such financing might be made, if properly authorized, by the State, or receive State guaranty or guaranty by a State agency.

There is no limit on the number or amount of assets which AGSOC could acquire under the recommendations herein set forth. While, with the passage of time, there will be a growing number of Alaska residents who did not meet the eligibility test at the time of the original issue of AGSOC stock, these could be taken in as shareholders through the issuance of additional stock.

Recommended drafts of Articles, By-Laws, and general recommendations concerning stock issue and transfer procedures, dividend procedures, the applicability of Federal securities laws, and the Federal constitutional provisions affecting Alaska GSOC are also included in the report. The proposed Bill would eliminate regulation under State securities law as unnecessary. State constitutional questions have been referred to the Alaska Attorney General's office for review.

State Partial Guaranty of AGSOC's Project Financing

Project financing for AGSOC, whether for the acquisition or development and construction of productive capital assets, will evolve from a request from AGSOC to the State of Alaska. The AGSOC Bill provides that if the Legislature determines that the partial financing or the guaranty of financing for an AGSOC project is necessary or desirable, a special election (if a general election is not scheduled to be held within sixty days) will be scheduled for voter approval.

The Future of AGSOC

Certainly great care in the establishment of AGSOC is warranted. At the same time, it needs to be recognized that the old techniques of business finance, by which the already rich are constantly made still richer, are deeply entrenched, and will tacitly insist upon the divine right of the rich to get richer, and the nonexistent right of the poor to get richer. So the courageous, deliberate and speedy efforts of all involved in this attempt to change the course of American economic history, and eventually world economic history, should remain uppermost in the minds of all concerned. The ownership of productive capital by a tiny minority of 5% of the consumer units of the population and the non-ownership of productive capital by the 95% of such consumer units, combined with their present practical inability to attain such ownership, is the weakness that insures the collapse

either of political freedom, or of economic stability in all market economies of the world. The proposal here under discussion is one that involves an attack on the cause of poverty, not another feeble stab at the symptoms or effects of poverty.

General Explanation of the General Stock Ownership Provisions of the Revenue Act of 1978

The Revenue Act of 1978 provides income tax advantages to specially chartered corporations which are broadly owned. These companies, known as General Stock Ownership Corporations, will be exempt from the corporate income tax which may be as high as 48%. Through this legislation Congress hopes to encourage broadened ownership of capital and explore the viability of capital income as a substitute for transfer payments. General Stock Ownership Corporations are to be privately owned and managed, but to insure that all of a state's citizens have an opportunity to become shareholders, Federal law requires that each corporation be separately authorized by the State Legislature or by referendum prior to January 1, 1984. For purposes of identification, we have in this report called the corporation to be authorized in Alaska "Alaska General Stock Ownership Corporation" or "AGSOC" for short.

Charter Provisions

Special charter provisions are required for a company to qualify as a GSOC under the new Federal law. To assure broad distribution of GSOC stock, the charter must provide for a single class of stock distributed to each "qualified resident" who does

not elect against receiving the stock within one year of issuance. Corporations, trusts, partnerships and other organizations are not eligible to become shareholders -- only individual persons. Transfers of the initially issued stock must be restricted and may not occur before the earliest of (1) the date five years from the date of issue, (2) death of the shareholder, or (3) the shareholder's emigration from Alaska. In addition, no shareholder may own or acquire more than ten shares of GSOC stock.

GSOC Investments

GSOC investments are subject to only two limitations. A GSOC may not own more than 20% of the stock in another corporation and it may not use the power of condemnation to acquire a business investment from an unwilling seller. The Federal law does not otherwise limit the nature of a GSOC's business nor the extent of its operations within the state of its incorporation. However, from a tax standpoint, investment by a GSOC in stock of other corporations defeats the special tax advantages offered GSOCs because the income of the subsidiary corporation, unlike the income of the GSOC, is subject to Federal corporate income tax.

Taxation of GSOC

If AGSOC meets the requirements of Federal law, it may elect to be taxed as a General Stock Ownership Corporation. This election may not be revoked without consent of the Secretary of the Treasury. The election exempts the corporation from Federal income taxes. Instead, the shareholders report their proportionate

share of AGSOC's income on their personal tax returns.

Income (or loss) is computed by the GSOC in the same manner as other corporations, except that the GSOC is not eligible for the dividend received deduction nor any tax credits. Credit adjustments by the Internal Revenue Service are treated as income or deductions of the corporation in the year during which they are finally agreed upon.

The GSOC receives special treatment with respect to net losses, should any occur, and investment tax credits. Net losses are retained at the corporate level and may be carried over as an offset to future income for ten years. Investment tax credits are treated in a comparable manner to income and prorated to the shareholders as a credit on an annual basis. Net recapture of investment tax credit will be treated as prorated additional tax liability to shareholders.

For tax purposes, the GSOC is required to use an October 31st fiscal year end and, in addition to filing an information return with the IRS on corporate operations, it must provide a statement to each shareholder of his GSOC income, withholdings and tax credits for the year.

Taxation of Shareholders

Shareholders of the GSOC report on their personal income tax returns their share of GSOC income for the GSOC year ending within the taxable year for which they are filing a return. This income will be treated as "ordinary income" for tax purposes and will not be eligible for the \$100.00 dividend exclusion or the maximum tax on earned income. If a shareholder disposes of

his stock during the year, the income of the GSOC will be prorated to him on a daily basis. The shareholder will increase the basis in his stock for purposes of determining gain on a sale by the amount of GSOC income attributed to him and reduced by the amount of cash distributions received by him from the GSOC.

Since the shareholders of the corporation report their pro rata share of corporate income on their personal returns and are taxed on that amount, distributions of cash from the corporation are generally tax free. Distributions greater than the amount of prorated taxable income which the shareholder reported will first be treated as nontaxable to the extent of the shareholder's basis in his stock and then the balance will be taxed at capital gains rates.

In order to assure that shareholders have sufficient cash on hand to pay taxes generated by their pro rata share of GSOC taxable income, the GSOC is required to distribute 90% of its taxable income by January 31st each year. If the corporation fails to comply with this requirement, the corporation itself will be subject to a tax equal to 20% of the difference between what should have been distributed and what actually was distributed.

To assure payment of taxes by shareholders, the GSOC is required to withhold and pay to the Treasury 25% of each distribution. This withheld amount is treated just like the payroll withholding on salary checks. The full amount withheld is a dollar for dollar credit against income taxes due at the end of the year. It is simply a prepayment of taxes to assure that a shareholder does not find himself cash short at tax time, having

failed to set aside an amount from his GSOC distributions to cover his taxes. Individuals who are not required to pay taxes (because of insufficient or tax exempt income) may avoid the withholding on their GSOC distributions.

THE ECONOMIC REASONING SUPPORTING ADOPTION BY THE LEGISLATURE
OF THE STATE OF ALASKA OF ENABLING LEGISLATION DIRECTING THE
ESTABLISHMENT OF A GENERAL STOCK OWNERSHIP CORPORATION FOR THE
PURPOSE OF FACILITATING THE BUILDING OF CAPITAL OWNERSHIP INTO
EVERY ALASKAN CITIZEN IN THE COURSE OF DEVELOPMENT OF THE
NATURAL RESOURCES OF ALASKA

Everywhere the realization is growing that something basic in modern society is radically wrong; that in the words of Pope Paul's economic encyclical of a decade or so ago, "The world is sick." This assessment applied to the U.S. economy by former Chairman of the Federal Reserve Board who, before leaving that office, observed, "The old rules do not seem to work today." The most obvious symptom of this sickness is the accelerating tendency of the rich to grow richer, and of the poor to remain poor. But while the evidence of defective social structure everywhere stands out, it does not readily lead its victims to identify the responsible institutions. The very familiarity of institutions makes them invisible; the efforts of critics and reformers are invariably deflected to what they can see -- symptoms and effects. This is what prompted Thoreau to observe: "There are a thousand hacking at the branches of evil to one who is striking at the root."

The proposal of Kelso & Co., Incorporated (Kelso & Co.) involves an application of the theory of Universal Capitalism or Two-Factor Economics, as it is called with equal propriety, to the development of a financial and economic design for a General Stock Ownership Corporation (GSOC) for the State of Alaska, showing the efficiency with which a properly designed GSOC for

the State of Alaska can build general affluence into all Alaskan citizens over a reasonably brief span of time. It will lay bare the false concepts and institutions responsible for the relentless concentration of wealth in an industrial society; it will show how they work, how they malfunction in the economy, and how many of the economic evils of contemporary life are directly and indirectly related to these false concepts and deficient institutions.

Endemic poverty in a world which has all the physical, managerial and engineering prerequisites for producing general affluence is only one symptom of the wealth concentration syndrome. Less obvious, but just as causally connected, are misuse of technology, resource waste, despoliation of the environment, declining personal freedom, increasing lawlessness and civil disorder, the waning of liberal education, the civil rights impasse, the youth revolt, urban concentration, rising public and private debt, public loss of confidence in leadership and the seemingly irreversible advance toward a totalitarian society.

We believe that our study, if accepted and underwritten by the State of Alaska, will demonstrate that the specific mechanisms that concentrate wealth are correctable through the detailed methods we have outlined for achieving the correction.

It is appropriate here to ask why society has so long tolerated, and indeed remained officially oblivious to, institutional defects that were brutally apparent even in the earliest years of the Industrial Revolution. Why have we ignored the solid facts and so desperately clung to the straws of illusion? Why, for example, are we still pretending to believe that

labor's productivity is rising? That technology creates toil? That we have achieved, within about five percent, legitimate "full employment" in the United States today, or in any other industrial economy, or that full employment is a possible, or even an adequate economic goal?

The explanation for such massive intellectual dishonesty, we believe, is to be found in a simple but ancient misconception about how wealth is produced in the real physical world. Transmitted through generations of economists like a defective gene, the misconception has kept economics from developing into a rational science -- very much as the doctrine of spontaneous generation kept medicine from developing into a science until Pasteur's experimental researches crumbled organized resistance to the germ theory.

What the doctrine of spontaneous generation (the "hypothetical" production of living things from inanimate matter) was to 19th Century medicine, the labor theory of value and its offspring, the idea of full employment as an adequate economic goal and a pragmatic solution to the problem of income distribution, are to 20th Century economics. The notion that labor is the only, or chief, factor of production is the keystone of the conventional economic wisdom. Laissez-faire, Marxian Socialist and Keynesian theoreticians all treat the physical things that are factually the chief producers of wealth in an industrial economy -- tools, machines, structures and increasingly productive land -- as if they were extensions of the worker himself (the hammer, an extension of the hand; the wheel, of the foot; the computer, of the brain), or as if they were magic helpers that

miraculously increased labor's productivity, or as if they were natural resources functioning gratuitously like the sun to raise labor productivity. So long as we indulge this myth, we need not concern ourselves with who owns what capital in the economy, nor with the fact that its ownership is unbelievably concentrated.

In the pre-industrial past, where labor was the principal factor of production and nature had endowed every individual with the power to labor, the labor theory of value was at least half a truth; the events that would expose the other, and most important, half had not yet occurred. But with the invention of the spinning jenny, the Newcomen engine, and the power loom, and hundreds of other non-human producers, the non-human factor of production moved explosively into the forefront and began its rapid conquest of the domain of production of goods and services. Unnoticed and uncomprehended, reality swiftly outgrew one-factor economic thought and the economic institutions erected upon it.

Technology was the momentum behind the Industrial Revolution, but pre-industrial laborcentric concepts were not able to provide a rational philosophy of technology; hence, enlightened, realistic human goals logically consistent with the tendency of technology were impossible to formulate. In the humanistic medieval world, toil had been only a means. Now in an industrial age where technology is eliminating toil, means has become elevated into end. Instead of toiling to live, man now finds himself obliged to live to toil. Under one-factor economic thought, technology itself must function to create toil, and the enormous evidence of the absurdity of this contention must be ignored, falsified,

or rationalized away.

In his great quarrel with the medical traditionalists who upheld the doctrine of spontaneous generation, Louis Pasteur wrote that "the characteristic of erroneous theories is the impossibility of ever foreseeing new facts; whenever such a fact is discovered, those theories have to be grafted with further hypotheses in order to account for them."

For the past forty-eight years, the public economic policies of the Western industrial nations, and the public philosophy advanced to justify them, have borne witness to the accuracy of Pasteur's observation, and demonstrated the theoretical inadequacy of one-factor economic thought. As expedients are grafted onto expedients, the official explanations of reality become more and more contrived; finally, the bonds of credulity are reached and overreached; the practitioners of the conventional wisdom are obliged to side-step reason entirely and resort to open intellectual fraud. In the United States, where advancing technology has created the widest gap between reality as it is and reality as it is interpreted through defective one-factor theories, the Federal Government spends an incalculable amount of man-hours and money to persuade an increasingly skeptical and suspicious public that policies and goals which are irrational, dangerous and destructive are rational, effective and sound.

When an intellectually false theory persists against all evidence, it must be drawing sustenance from a live, powerful, non-rational source. We believe that the viability of the labor theory of value, the exclusive full employment goal and the

Procrustean institutions built upon them can be traced to the Puritan ethic -- the idea that "if any would not work, neither should he eat." In essence, the Puritan ethic is a production ethic. Its meaning is that human beings ought to produce the economic equivalent of the wealth they wish to consume. This injunction is philosophically, economically, and morally sound. Experience shows that men hate being objects of charity just as much as they hate being the victims of parasitism; it is economically motivating both for people to produce the wealth they consume, and to receive the wealth they produce. In a pre-industrial world, where labor was the only active factor of production, it was natural that production was interpreted as synonymous with toil. The Marxian ethic is based on the identical assumption; it and the Puritan ethic are indistinguishable.

But what was practical common sense and moralistically sound in a pre-industrial economy becomes nonsense in an industrial one, not because the principle has changed, but because the methods and character of production have changed. The rhetorical statement of the rationale of the Puritan ethic for a one-factor economy simply will not suffice in a two-factor economy; it does not accommodate itself to the changed facts. Indeed, a principle of unquestioned justice becomes a source of woeful injustice. In attempting to impose a one-factor ethic in a two-factor world, older generations are unconsciously seeking to make new generations suffer the same hardships that pre-industrial life forced on them and their predecessors. The poet Robert Frost understood the intent, if not the mechanics, of conventional economic policies that uncomprehendingly exort toil and self-denial in an age

where technology has shifted most of the burden of production onto machines, and where mass consumption is essential to support the mass production which is the point of an industrial economy. Thus, a one-factor interpretation of the Puritan ethic threatens the very source of general affluence.

Institutional renewal and reform, we believe, must begin with the restatement of the Puritan ethic. If its moral essence is not that men and women should toil for toil's sake, but that they should produce for production's sake, the question becomes: How are people to be economically productive in an age when wealth is chiefly produced by things? An updated Puritan ethic would hold that individuals produce just as legitimately through their ownership of productive things as they do through their personal toil (i.e., through their privately and personally owned labor power). In the economic sense, the owner of a significant equity interest in an oil pipeline, or gas pipeline, or petrochemical production facilities is immeasurably more productive than the most skilled and industrious blacksmith in a pre-industrial village. Modern institutions must recognize this physical fact, and modern ethical and philosophical concepts must deal with it. Our reverence for toil is purely historical and hypothetical -- what sane man, in real life, seeks to toil for goods and services of subsistence that can be better produced with machines and processes? Much closer to reality is the historical fact that human slavery partially originated in man's revulsion for toil, and that moral sentiment was incapable of abolishing slavery until technology provided us with machines to take the place of the slave. Also much closer to reality than our pious

affection for "full employment" is the historical use of hard labor as punishment for crime.

Until we understand the modern implications of a pre-industrial interpretation of the Puritan ethic, we shall not be able to design a rational economic system for a two-factor world. We shall continue to misuse, misdirect and waste technology; to concentrate its ownership into those who already own too much of it, and to deny the just requirements of those who need to own it but who do not have any legitimate means of acquiring it; to squander resources, talent and human lives; to throw away man's opportunity for peaceful, affluent leisure in our political and institutional attempts -- futile, absurd and monstrously hypocritical -- to recreate the pre-industrial state of toil that management, engineering and technology constantly seek to destroy.

Not toil, but leisure; not the pinnacle affluence which has characterized all Western industrial societies to date, but general affluence -- these clearly must be the goals of a rational and free industrial economy. Moreover, once recognized and acknowledged, they are goals that are easily achievable, as, we believe, the Alaska General Stock Ownership Corporation feasibility study shows.

Since affluence is not the product of the human factor, but the non-human factor, it is necessary to structure the economy so that a growing proportion of families, and eventually all families, produce an expanding proportion of their incomes through their private ownership of capital stock representing tools, machines, structures, facilities and productive land that

produce wealth, and (under the irrefutable Say's Law) simultaneously generate exactly enough purchasing power to enable the producers to consume it. For although the "boom-bust" cycles characteristic of industrial economies are caused by insufficient purchasing power (this is the defect Keynesian redistribution purports to correct), the physical fact is that every production cost in a market economy is the income of some participant in production. Thus, there could be no physical shortage of purchasing power in an economy where every household made a viable productive input and received the income its input produced.

The techniques involved in the General Stock Ownership Plan are techniques for connecting every household in the economy with the productive power of capital instruments, through financing methods that make stockholders of all Alaskan residents, such as the Alaska General Stock Ownership Corporation. Today, under financing techniques inherited from the pre-industrial past, individual ownership of the non-human factor of production is concentrated in no more than the top five percent of U.S. families. Conventional business finance operates to shrink the proprietary base even further. Financing methods, such as the Employee Stock Ownership Plan (ESOP), the Consumer Stock Ownership Plan (CSOP), and the General Stock Ownership Plan (GSOP), developed by Kelso & Co., Incorporated, finance capital ownership for individuals at the same time they finance corporate expansion or changes in the ownership of capital assets. Thus financing techniques employing two-factor economic principles create new capital owners simultaneously with new productive power, and can

create broader individual ownership in connection with transfers of ownership from one entity to another.

New productive power is an absolute requisite for general affluence, simply because -- not withstanding the assertions of politicians and economists to the contrary -- no economy in the world today is physically capable of providing an affluent stream of goods and services to all the people in it, although the potential physical capacity to do so through accelerated growth of new capital formation and broad ownership of capital is present in most of the world's economies. The "affluent economy" of the United States, we flatly assert, is illusory. But the United States, Canada and most of the Western economies have or have access to the physical ingredients necessary to produce general affluence within a space of two decades or so, and so does the State of Alaska. The limitations that bind them now are not physical, but institutional. What is lacking is an economic system built on the rationale of two-factor concepts that would build the economic power of the people to consume simultaneously with building the industrial power of their economies to produce and distribute a level of goods and services equivalent to general affluence.

In today's illogical economies, the corporate sector puts new productive power into place by means that channel the income it will produce to the already affluent few who perforce must invest it, rather than to the many, who perforce would spend it on much-needed consumer goods and services, and in so doing, fully close the production-consumption circuit. Thus, consumption is increasingly achieved today through coercive re-

distribution by government and organized power blocs in the private sector (with the blessing of government) and through that delusive doctrine, full employment. Since the corporate sector produces 87% of non-agricultural, non-governmental goods and services, it also generates 87% of the economy's purchasing power. In not structuring the invisible sector of corporate enterprise so that a growing number of families are connected with the productive power of capital, management is neglecting one-half of its prime responsibility and opportunities. In so doing, it is spearheading the destruction of private property in the American economy, and hastening the totalitarian society in which the corporation will serve as the welfare arm of the state. The Alaska General Stock Ownership Corporation can correct this for Alaskans, beginning in a very short time.

The proposed GSOP for Alaska should appeal to the three executive powers of modern society -- business, labor and government -- to begin now to plan an economy in which every family has the opportunity to produce wealth in a way compatible with a technologically advanced economy: through employment (to the extent the legitimate demand for employment has not been technologically eliminated), and through its private ownership of the non-human factor of production. This is what the techniques of two-factor financing are designed to accomplish. Through updating the Puritan ethic to conform to the technological facts of production, we would be renewing our institutions in the spirit of the American ideal, rather than seeking, as do the proponents of the Negative Income Tax, the Guaranteed Annual Income, and similar schemes, to repeal the underlying ethical

law. For American political institutions assume a citizenry which is economically independent and productive. The Founding Fathers knew that freedom is inseparable from property. On that premise they designed political institutions that were an inspiration to all mankind.

The State of Alaska has before it the opportunity to lead our nation and the world through economic change that would underpin our political heritage with economic institutions designed to provide effective economic opportunity to the many in an industrialized world -- and to do it before time and hope run out.

STOCK AND FINANCING MATTERS

MARKET ASPECTS

We recommend that AGSOC be a private company as differentiated from a publicly-traded security, at least for its first five years of existence. Even though AGSOC will have some 400,000 shareholders, there are a number of considerations which suggest that private company status would be preferable to that of a publicly-traded security. Firstly, the Federal GSOC legislation places considerable restrictions on the transferability of shares during the first five years. Secondly, the requirement of the Federal legislation which limits shareholders to individuals will prohibit the ownership of shares by broker-dealers required for over-the-counter type trading transactions. Third, the unit of trading in security markets generally is 100 shares, yet in the case of AGSOC only one share will be issued to each eligible shareholder. While this is not an insurmountable obstacle, it presents unique problems if a public market were to be established. Fourth, the concept of AGSOC is as a long-term investment, rather than a short-term or transitory type of commitment. Fifth, ownership of shares is restricted to residents of Alaska, limiting the ability to develop a competitive and realistic market for the shares of AGSOC.

Section 6 of the AGSOC Act provides for the company to have a right of first refusal to purchase any shares of stock

offered to be transferred by the holder. Thus, AGSOC itself could probably provide an adequate market for those shares that must be sold. We further recommend that the price paid for those shares by AGSOC during the initial five-year restricted trading period be set at the tangible book value per share as of the most recent quarterly reporting date.

The acquisition by AGSOC of these limited number of shares each year provides a modest supply of shares which can be used to allow new residents to Alaska to participate in the ownership of AGSOC. The Board of Directors of AGSOC could set some reasonable waiting period before new residents would be eligible to apply for purchase of the shares acquired by the company in this manner. A waiting list could be established based on the date of application to AGSOC by the new residents. By this procedure those who had completed the necessary length of residence during the initial five-year period following original issue, would be able to purchase, at book value, the shares that are acquired by AGSOC from time to time. While constitutional issues with regard to this procedure will have to be carefully reviewed by the Attorney General's office, we believe that this procedure would offer the most fair solution to the problem of the new resident versus the resident who qualified as of January 1, 1979.

Over the longer term, the management of AGSOC and the Board of Directors will have to carefully monitor the market aspects of AGSOC stock. Economic and stock market conditions change as well as State and Federal law so that what is appropriate today may of necessity be changed in future years. There are several possible ways to accommodate the problem of the otherwise "qualified resident" who becomes such after the specific date fixed by the AGSOC law and as required by the Federal GSOC law. One approach would be, after a substantial number of residents who were not originally eligible has arisen, to issue a new class of stock, representing a newly-financed investment, and issuing the shares to all then-qualified residents. This would require modifications in the State and Federal GSOC laws which now permit only one class of stock.

STOCK TRANSFER FUNCTION

The essentials for the transfer of stock are (1) a change in ownership; (2) proper endorsement, either on the certificate itself or by a separate instrument; (3) surrender of the certificate for cancellation; and (4) issuance of a new certificate to the transferee.

A stock certificate assigned in blank may be passed from transferor to transferee any number of times without change of the assignment. If the name of the transferee is inserted, the certificate must be surrendered and a new certificate issued in the name of the transferee before it may again be transferred. If the certificate is delivered without endorsement, but is accompanied by an assignment, it has the same effect as an endorsement upon the certificate itself and must be surrendered for the issuance of a new certificate in the name of the transferee.

A corporation is responsible for any fraud or error committed by its officers or agents in the issuance or transferring of its stock. To prevent the possibility of liability or forged assignment, the corporate secretary or transfer agent should demand a guarantee of the signature of the transferor. Proof of the authority should be demanded when the assignment is made by an executor, trustee, and the like.

The management of AGSOC must decide whether to employ a transfer agent or provide the stock transfer function internally. If a corporation has a transfer agent, usually the issuance, transfer, and the detail of keeping a stock ledger are handled by him. The extent of the transfer agent's work and liability depends upon the agreement between him and the corporation. Generally, a transfer agent is authorized to sign and impress the corporate seal on the corporation's stock certificates issued by him and to maintain the stock books and stockholders ledger containing the names and addresses of all stockholders. The secretary should receive a daily record from the transfer agent of all stock transfers made by him.

If, however, the company does not employ a transfer agent, the secretary is responsible for the proper issuance and transfer of corporate stock and maintenance of proper stock books, ledgers and records.

i. registrar maintains a record of all stock certificates issued and surrendered showing the name of the transferor and transferee. He maintains a record to assure that there is no overissue of the securities. He passes upon the correctness of all certificates issued. If correctly issued, he countersigns them. The national stock exchanges require that securities listed by them be issued through a transfer

agent and registrar. This requirement is not applicable to AGSOC as no listing is currently contemplated. Article VI, Section 6.06, of the proposed AGSOC By-Laws prohibits the company from acting both as transfer agent and as registrar for its own shares.

It is our recommendation that AGSOC's corporate secretary assume the duties of stock transfer and dividend disbursement and employ an independent outside registrar. Our studies indicate that this decision would reduce costs, improve control and assure conformance with applicable laws and regulations.

PROJECT FINANCING

Section 11 of the AGSOC Act states that "at such time as AGSOC comes forward with a request for project financing that the Governor shall call a special session of the legislature to consider such request." In the event that the Legislature determines that the financing or the guaranty of the financing for an AGSOC project is necessary or desirable, the Legislature would then call a special election for voting on the approval of the extension of the credit or the guarantying of credit to AGSOC by the State of Alaska.

Prior to going to the Legislature with a request for financing, the management of AGSOC will have to accomplish many preparatory investigations and studies. Although each management function will be important to the overall success of AGSOC, buying a going business is probably the most important decision the company has to make. The objective of this section is to provide guidance by setting forth the elements of a buy decision: investigation, valuation, and financing proposals for the Legislature.

Each situation is obviously unique, but experience has shown that typically what hindsight concluded were purchase mistakes were not the result of poor judgment based on known facts. Most mistakes result, instead, from elements of the transaction that were not known at the time the decision was made.

1. INVESTIGATION

Much information is required prior to undertaking a business acquisition. This information can be gathered by trained people in the AGSOC organization, or with the assistance of independent accountants, lawyers, marketing analysts, management consultants or others who can be called on or combined to carry out an appropriate investigation. Set forth in the appendix is an outline to assist in carrying out an acquisition investigation. Obviously it is an assist only, for there can be no substitute for an experienced investigator performing the work.

2. VALUATION

The "value" of a business is normally meant as its potential for earning income, not the present replacement cost, that is, appraisal value of the assets.

Generally, the basis for determining the asking or offering price of a business whose present worth is dependent largely on a continuance of the business -- as against liquidation of assets -- is the present value of the potential for future earnings. The primary problems of valuation, then, are (1) the question of estimating the future earnings of the business and (2) the multiplier to apply to the estimate (price/earnings ratio).

FUTURE EARNINGS

Consider first the question of estimating future earnings:

1. Are past earnings a guide to earnings potential?
 - a) How many year's past earnings should be used in the computation?
 - b) Should average earnings for the past period be used or should earnings be weighted?
2. Alternatively, if past earnings are not a guide because anticipated changes will, it is believed, render historical earnings meaningless, an item-by-item sales and costs business forecast is called for.
3. In either (1) or (2) above, adjustments should be made for any cost savings as a result of the acquisition by AGSOC:
 - a) In personnel.
 - b) In elimination of facilities.

PRICE/EARNINGS RATIO

Having established potential earnings, what price should be paid for those earnings? There is considerable guidance in this area which must be searched out and evaluated.

SECONDARY FACTORS

In addition to earnings and the appropriate multiplier, there are secondary factors which should be weighed in determining relative values. No one of the secondary factors is necessarily determinative, but they tend to be cumulative in effect.

Capital Employed in the Business

Capital employed in the business is a factor which cannot be lost sight of completely, because there may be capital invested not required to produce earnings potential, upon which the primary evaluation is based.

Book Value

Occasionally, accounting book values possibly giving effect to replacement costs are a valuation factor, especially if a capitalized earnings power evaluation results in a figure below book.

Dividend-Paying Capacity

Dividend-paying capacity is a factor, for one aim of business is to pay dividends to justify the employment of capital in the business. Thus, a company should have not only earnings potential, but a cash throw-off potential sufficient to produce a return commensurate with the risk.

Profit Sharing, Bonus Arrangements and Employment Contracts

Profit sharing and bonus arrangements may be factors because the method of compensating the management in the company to be bought may effectively represent part of the

purchase price rather than compensation for services.

3. FINANCING AN AGSOC ACQUISITION

After the valuation question, the management of AGSOC's attention will be directed toward ways to finance the acquisition. AGSOC basically has two choices in a cash acquisition: 1) Debt capital from third parties; 2) Debt capital from the seller.

Debt Capital from Third Parties

Debt capital from third parties is frequently a necessary ingredient to effect a cash acquisition. The ability to obtain loans depends upon: 1) the specific assets that can be assigned or pledged as security; 2) the cash throw-off available for repayment of the principal of the loan plus the interest; 3) the earnings potential of the business to be acquired.

The security requirement can be met by the acquiring company's resources or the acquired company's resources. Security can include accounts receivable, inventory, real property and equipment. The ability to repay a loan with interest depends ultimately upon earnings power and cash throw-off. Lenders are usually more concerned about the prospective ability to pay off debt than the underlying net worth of the balance sheet, just as purchasers and sellers of businesses are more concerned about potential earnings than

asset power. The lender may look to the debt repayment power of the purchaser's present business, the business to be acquired (bootstrap), or the combined earning power of both (partial bootstrap).

Debt Capital from the Seller

In situations where the purchaser is unable to raise debt capital from his own or third-party resources, the seller may effectuate the deal by consenting to an installment payment of the sales price. This is another form of bootstrap. Another technique which may be applicable to AGSOC is the assumption of the debt of the acquired company. In addition to making a deal possible at all, an installment sale or assumption of debt is not without other advantages to the seller.

- 1) Versus payment in full, an installment sale with not more than 30% payment in the first year spreads out the tax payment on the capital gain.
- 2) The seller may receive a high interest return on the unpaid installment, possibly his best investment opportunity.

The principal disadvantage to the seller is his continued assumption of business risk for future installment payments or the possibility of default on assumed debt.

The problems of buying a going business are most complicated. They go to every aspect of the transaction. The

problems of investigation, valuation, and method of financing are challenges to management which require not only keen business judgment, but technical answers. There are many questions which AGSOC management must consider in a most careful way if it is to make the proper decision. The end product will be a financing proposal to be presented to the Legislature and, if approved, and if it involves the general credit of the State, submitted to a vote of the people. Each potential acquisition candidate will have different characteristics and require separate financing techniques.

START-UP COST

The appropriate way to obtain funds for AGSOC's start-up costs and expenses until it generates income would appear to be by way of a fiscal bill which would be separate from the enabling legislation.

Such a bill should provide sufficient funds in the nature of a short-term loan or otherwise to cover the organizational and start-up expenses of AGSOC, including but not limited to: organization and qualification as a domestic corporation; contracting for legal, accounting, investment banking counsel, analysts, and other professional services; employment of management and staff personnel to search out, analyze and evaluate potential investments and to create effective liaison with appropriate departments and agencies of the Federal and State Governments; arranging financing for acquisition of appropriate investments; identifying the persons who will be eligible to become stockholders of the corporation; preparing a data base of stockholders eligible for initial issuance of AGSOC shares; establishing or arranging for appropriate trust and escrow departments or services; arranging for banking, stock registrar and other appropriate services; paying directors' fees and expenses; obtaining necessary licenses and paying fees and taxes, if any; procuring office facilities, equipment and supplies, travel, communication expense, and all other expenses

normally expended in starting up a new enterprise.

The term, amount and rate of interest of such a loan would presumably be established by the Commissioner of Revenue of the State of Alaska. We recommend that an initial installment of \$2,500,000 be immediately loaned to AGSOC to allow the Board of Directors to proceed with the recruitment, selection and employment of the management group.

A BILL

FOR AN ACT ENTITLED "AN ACT ESTABLISHING ALASKA GENERAL STOCK OWNERSHIP CORPORATION; AMENDING CERTAIN ALASKA STATUTES; AND PROVIDING FOR AN EFFECTIVE DATE."

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

Section 1. ALASKA GENERAL STOCK OWNERSHIP CORPORATION ORGANIZATION. The Governor of the State of Alaska be, and hereby is, authorized and directed to cause the incorporation of Alaska General Stock Ownership Corporation (AGSOC), by the filing of appropriate Articles of Incorporation with the Division of Banking and Securities of the Department of Commerce and to appoint as incorporators and as the first Board of Directors of AGSOC nine (9) individuals, at least five (5) of whom are residents of Alaska.

Section 2. GENERAL STOCK OWNERSHIP CORPORATION UNDER INTERNAL REVENUE CODE. AGSOC shall be organized as a General Stock Ownership Corporation under Title VI of the Internal Revenue Code of 1954, as amended, and under this Act.

Section 3. ORGANIZED AS A DOMESTIC CORPORATION. AGSOC shall be a domestic corporation for profit under the laws of the State of Alaska, and shall not be an agency or political subdivision of the State of Alaska for any purpose.

Section 4. INITIAL BOARD OF DIRECTORS.

(a) The initial Board of Directors of AGSOC (hereinafter referred to as the "Board") shall consist of nine (9) members, at least five (5) of whom shall at all times during their terms as members of the Board be residents of the State of Alaska.

(b) Members of the initial Board shall be divided into three (3) classes, each class consisting of three (3) individuals, designated as Class One directors, each with a term of one (1) year and until their successors are elected and qualified; Class Two directors, each with a term of two (2) years and until their successors are elected and qualified; and Class Three directors, each with a term of three (3) years and until their successors are elected and qualified.

Section 5. ISSUE AND TRANSFER OF STOCK. Alaska General Stock Ownership Corporation is hereby authorized and directed:

(a) to issue only one (1) class of stock;

(b) to issue shares only to residents (eligible individuals) of Alaska as defined herein;

(c) to initially issue at least one (1) share of its stock to each resident of Alaska, unless such resident elects within one (1) year after the date of such issuance not to receive such share;

(d) to provide that no share of stock shall be sold, pledged, assigned, mortgaged, subjected to encumbrance, voluntarily or involuntarily, or otherwise transferred --

(i) by a shareholder other than by will or the applicable laws of descent and distribution until after the expiration of five (5) years from the date such stock is issued by AGSOC except in the event the shareholder ceases to be a resident of the State of Alaska and thereupon elects to make such transfer;

(ii) to any person other than an individual who is at the time of such transfer an individual resident of Alaska as defined herein;

(iii) to any individual who, after the transfer, would own more than ten (10) shares of the stock of AGSOC;

(iv) by any shareholder until such shareholder shall reach the age of majority, as defined by Alaska law;

(e) to perform all acts and conform to all legal requirements to qualify and thereafter to continue to qualify as a General Stock Ownership Corporation under the Internal Revenue Code of 1954, as amended, and under this Act, unless the Board, with the consent of the Secretary in accordance with applicable provisions of the Internal Revenue Code and regulations thereunder, shall elect to terminate such qualification; and

(f) not to invest in or acquire any interest in properties acquired by it or for its benefit through exercise of the right of eminent domain.

Section 6. RIGHT OF FIRST REFUSAL TO PURCHASE OWN STOCK.

AGSOC shall have a right of first refusal to purchase any shares of stock of AGSOC offered to be transferred by the holder thereof. Such shares may be held by AGSOC in the general escrow or trust account of its trust or escrow division, in which event such stock shall continue its status as issued and outstanding stock of AGSOC for all purposes, except that such shares, while so held, shall not be voted nor shall they be entitled to dividends declared on shares of AGSOC stock. The Board of Directors by resolution shall have the power to cancel such reacquired shares and such shares shall thereupon return to the status of authorized and unissued shares.

Section 7. ESCROW OF STOCK BY AGSOC. AGSOC shall have the power to make and enforce reasonable rules and regulations with respect to the establishing of escrow accounts either within its own trust and escrow department or otherwise for each stockholder of the corporation; for releasing shares of stock to the owner or buyer thereof subject to the continuing restrictions set forth in this Act at the expiration of the period of five (5) years following date of issue thereof, or the date upon which the shareholder shall reach the age of majority, as defined by Alaska law, or the date when the shareholder shall have complied with all reasonable rules and regulations of AGSOC pertaining to the release of such shares from escrow, whichever

of said events shall be the last to occur, except in the event of death of the shareholder or upon the shareholder ceasing to be a resident of the State of Alaska and thereupon electing to transfer such shares to an eligible transferee; for the operation of its trust and escrow division; for the transfer and recording of transfers of its stock if it determines to act as its own transfer agent; for the operation of its trust and escrow division if it determines to establish a trust and escrow division, and with respect to the issue, transfer, repurchase and other handling or dealing with its stock as its Board of Directors may adopt and promulgate. All such rules and regulations shall be published to the stockholders of AGSOC and shall be available in suitable form to any stockholder at any time upon request during regular business hours.

Section 8. DEFINITION OF RESIDENT.

(a) For purposes of original issue of shares of AGSOC stock under this Act, the terms "resident", "eligible individual", or "qualified individual" shall have the same and identical meaning, and shall mean an individual, born prior to 12:00 o'clock midnight on January 1, 1979, regardless of age, who, as of 12:00 o'clock midnight on January 1, 1979, was a resident of and was domiciled in the State of Alaska and who remains a resident of Alaska through the date determined by the Board of Directors of AGSOC and publicly announced as such, to be the date the shares of stock of AGSOC are initially issued.

(b) For purposes of transfer of AGSOC shares subsequent to

initial issuance, "resident" shall mean an individual, regardless of age, who is a resident and is domiciled in the State of Alaska on the date such transfer is made effective.

Section 9. IDENTIFICATION OF RESIDENTS OF ALASKA ELIGIBLE TO BECOME AGSOC SHAREHOLDERS.

(a) Prior to issuing any shares of stock, AGSOC shall take all reasonable measures, by public advertising, radio and television broadcasting, and otherwise, to make known to all residents of the State of Alaska its intention to issue stock to each person eligible to become a shareholder and to similarly notify all Alaska residents of the eligibility requirements to become a registered shareholder of AGSOC. Such efforts shall be made from time to time and shall continue for a period of at least ninety (90) days prior to the date for issuance of stock of AGSOC, and shall be made at least once each month over the next eleven (11) months, and as frequently thereafter as the Board of Directors of AGSOC may deem appropriate. The procedural details pertaining to the identification of such persons as shareholders, either in person, or if they are minors represented by a parental or legal guardian, or if they be incompetent persons by a legal guardian, shall be fully provided to each person making inquiry at a properly designated office by a representative of AGSOC.

(b) The duty and responsibility, however, of each qualified resident to make application for registration as a shareholder of AGSOC shall rest solely and exclusively upon such

qualified resident and upon the parental and legal guardians of qualified residents, and AGSOC shall not be liable for any loss, loss of income, disadvantage or inconvenience resulting directly or indirectly from the failure of such qualified resident to make such timely application except as herein specifically provided.

(c) AGSOC shall have no obligation to reimburse any eligible individual who may incur income tax liability as the result of failure to make timely application for registration as a shareholder of AGSOC, nor shall AGSOC be liable for reimbursing previously declared or paid dividends to which an applicant for registration as a shareholder would have been entitled had timely application therefor been made. Subject to these limitations, however, an eligible resident who would have been entitled to the issuance of a share or shares of stock of AGSOC, had application been made prior to the time of such issuance, or a transferee by will, or by the laws of descent and distribution, or other legal transferee, and had such qualification continued through the date of such issuance, may at any time thereafter make such application and receive the stock (or escrow certificate representing such stock) to which he shall thus be established as being entitled.

Section 10. CIVIL AND CRIMINAL PENALTIES FOR MISREPRESENTATION OF FACTS DETERMINING ELIGIBILITY TO BECOME AGSOC SHAREHOLDER.

(a) Any individual who shall have received stock upon orig-

inal issue by AGSOC through fraudulent or misleading representations shall, upon demand therefor in writing being made by or on behalf of AGSOC, return all certificates or other evidence of the ownership of such shares and the full amount of dividends, whether in cash, in stock or otherwise, received thereon, together with interest at the rate of eight percent (8%) per annum from the date that such dividend or dividends were received to the date of such repayment. In the event of failure of such illegal holder of shares of AGSOC to make such restitution in full, AGSOC shall be entitled by civil action in any Superior Court in the State of Alaska to enforce such recovery, together with payment of all legal fees and court costs incurred by AGSOC in effecting such recovery.

(b) Any person who shall obtain for himself or for a person as to whom he is or has represented that he is a parental or legal guardian the issuance of shares of AGSOC through fraud, misrepresentation or by any deceitful or illegal means, shall be guilty of a Class C felony.

Section 11. SPECIAL SESSION TO APPROVE FINANCING. It is the intent of the legislature that at such time as AGSOC comes forward with a request for project financing that the Governor shall call a special session of the legislature to consider such request. However, no special session need be called if the legislature is scheduled to meet within sixty (60) days of the date of such request. In the event the legislature shall determine that financing or the guaranty of financing for an AGSOC project is necessary or desirable, the legislature shall at the

earliest convenient time call a special election (unless an election is scheduled to be held within sixty (60) days) for voting on the approval of the extension of credit to AGSOC by the State of Alaska, or the guarantying by the State of Alaska or by any agency or instrumentality thereof of the credit of AGSOC.

Section 12. TRUST ACCOUNT WITH DEPARTMENT OF REVENUE.

There is hereby established a trust account within the Department of Revenue which account shall be used solely and exclusively for purposes of guarantying loans, public or private, to AGSOC for the accomplishment of its purposes.

Section 13. The following amendments shall be and hereby are made to the Alaska Statutes:

(a) Title 10, Section 10.05.012, is hereby amended by inserting prior to the first word in the second sentence thereof the words: "Except with respect to General Stock Ownership Corporations,".

(b) The last sentence of Title 10, Section 10.05.186, is hereby amended to read: "Except with respect to General Stock Ownership Corporations, no classification of directors is effective prior to the first annual meeting of shareholders."

(c) Title 10, Section 10.05.204, is hereby amended by adding a new Subsection (7) at the end thereof as follows:

"(7) Notwithstanding the foregoing or any other pro-

visions of Title 10 of the Alaska Statutes, dividends may be declared and paid by a General Stock Ownership Corporation, organized under AS _____, at any time and from any source to the extent deemed by the Board of Directors thereof necessary to comply with the distribution requirements of the laws of Alaska and of the United States, except that no dividend shall be declared when such General Stock Ownership Corporation is insolvent or which would cause it to become insolvent."

(d) Title 45 is hereby amended by adding a new Section 45.55.141 thereto to read:

"Section 45.55.141. The stock of a General Stock Ownership Corporation organized under the Alaska General Stock Ownership Corporation Act (AS _____.____) is not a security and the issue or sale of stock under that Act shall not be construed as a sale of a security for purposes of this chapter."

Section 14. AGSOC SHALL BE EXEMPT FROM PROVISIONS OF TITLE 6, CHAPTER 25, OF ALASKA STATUTES. AGSOC shall be authorized to engage in trust and escrow activities with respect only to matters involving its own stock and to such extent AGSOC shall be exempt from compliance with the provisions of Title 6, Chapter 25, of Alaska Statutes.

EXPLANATORY FOOTNOTES TO PROPOSED "BILL
FOR AN ACT ENTITLED 'AN ACT ESTABLISHING ALASKA
GENERAL STOCK OWNERSHIP CORPORATION; AMENDING
CERTAIN ALASKA STATUTES; AND PROVIDING FOR AN
EFFECTIVE DATE'"

Set forth below is a copy of the proposed Bill, to which footnotes have been added at appropriate places above the particular words to which the footnotes are pertinent. Thus the preceding draft of proposed Bill and the following draft of proposed Bill are identical except that in the following draft the footnote references have been added. The footnotes themselves appear immediately following the second draft.

A BILL

FOR AN ACT ENTITLED "AN ACT ESTABLISHING ALASKA GENERAL STOCK OWNERSHIP CORPORATION; AMENDING CERTAIN ALASKA STATUTES; AND PROVIDING FOR AN EFFECTIVE DATE." (1)

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

Section 1. ALASKA GENERAL STOCK OWNERSHIP CORPORATION ORGANIZATION. The Governor of the State of Alaska be, and hereby is, authorized and directed to cause the incorporation of Alaska General Stock Ownership Corporation (AGSOC), by the filing of appropriate Articles of Incorporation with the Division of Banking and Securities of the Department of Commerce (2) and to appoint as incorporators and as the first Board of Directors of AGSOC nine (9) individuals, at least five (5) of whom are residents of Alaska. (3)

Section 2. GENERAL STOCK OWNERSHIP CORPORATION UNDER INTERNAL REVENUE CODE. AGSOC shall be organized as a General Stock Ownership Corporation under Title VI of the Internal Revenue Code of 1954, as amended, and under this Act. (4)

Section 3. ORGANIZED AS A DOMESTIC CORPORATION. AGSOC shall be a domestic corporation for profit under the laws of the State of Alaska, and shall not be an agency or political subdivision of the State of Alaska for any purpose. (5)

Section 4. INITIAL BOARD OF DIRECTORS.

(a) The initial Board of Directors of AGSOC (hereinafter referred to as the "Board") shall consist of nine (9) members, at least five (5) of whom shall at all times during their terms as members of the Board be residents of the State of Alaska.

(b) Members of the initial Board shall be divided into three (3) classes, each class consisting of three (3) individuals, designated as Class One directors, each with a term of one (1) year and until their successors are elected and qualified; Class Two directors, each with a term of two (2) years and until their successors are elected and qualified; and Class Three directors, each with a term of three (3) years and until their successors are elected and qualified.⁽⁶⁾

Section 5. ISSUE AND TRANSFER OF STOCK. Alaska General Stock Ownership Corporation is hereby authorized and directed:

(a) to issue only one (1) class of stock;⁽⁷⁾

(b) to issue shares only to residents (eligible individuals) of Alaska as defined herein;⁽⁸⁾

(c) to initially issue at least one (1) share of its stock to each resident of Alaska, unless such resident elects within one (1) year after the date of such issuance not to receive such share;⁽⁹⁾

(d) to provide that no share of stock shall be sold, pledged, assigned, mortgaged, subjected to encumbrance, voluntarily or involuntarily, or otherwise transferred --

(i) by a shareholder other than by will or the applicable laws of descent and distribution until after the expiration of five (5) years from the date such stock is issued by AGSOC except in the event the shareholder ceases to be a resident of the State of Alaska and thereupon elects to make such transfer; (10)

(ii) to any person other than an individual who is at the time of such transfer an individual resident of Alaska as defined herein; (11)

(iii) to any individual who, after the transfer, would own more than ten (10) shares of the stock of AGSOC; (12)

(iv) by any shareholder until such shareholder shall reach the age of majority, as defined by Alaska law; (13)

(e) to perform all acts and conform to all legal requirements to qualify and thereafter to continue to qualify as a General Stock Ownership Corporation under the Internal Revenue Code of 1954, as amended, and under this Act, unless the Board, with the consent of the Secretary in accordance with applicable provisions of the Internal Revenue Code and regulations thereunder, shall elect to terminate such qualification; (14) and

(f) not to invest in or acquire any interest in properties acquired by it or for its benefit through exercise of the right of eminent domain. (15)

Section 6. RIGHT OF FIRST REFUSAL TO PURCHASE OWN STOCK.

AGSOC shall have a right of first refusal to purchase any shares of stock of AGSOC offered to be transferred by the holder thereof. (16) Such shares may be held by AGSOC in the general escrow or trust account of its trust or escrow division, in which event such stock shall continue its status as issued and outstanding stock of AGSOC for all purposes, except that such shares, while so held, shall not be voted nor shall they be entitled to dividends declared on shares of AGSOC stock. (17) The Board of Directors by resolution shall have the power to cancel such reacquired shares and such shares shall thereupon return to the status of authorized and unissued shares.

Section 7. ESCROW OF STOCK BY AGSOC. AGSOC shall have the power to make and enforce reasonable rules and regulations with respect to the establishing of escrow accounts either within its own trust and escrow department or otherwise for each stockholder of the corporation; for releasing shares of stock to the owner or buyer thereof subject to the continuing restrictions set forth in this Act at the expiration of the period of five (5) years following date of issue thereof, or the date upon which the shareholder shall reach the age of majority, as defined by Alaska law, or the date when the shareholder shall have complied with all reasonable rules and regulations of AGSOC pertaining to the release of such shares from escrow, whichever

of said events shall be the last to occur, except in the event of death of the shareholder or upon the shareholder ceasing to be a resident of the State of Alaska and thereupon electing to transfer such shares to an eligible transferee;⁽¹⁸⁾ for the operation of its trust and escrow division; for the transfer and recording of transfers of its stock if it determines to act as its own transfer agent;⁽¹⁹⁾ for the operation of its trust and escrow division if it determines to establish a trust and escrow division, and with respect to the issue, transfer, repurchase and other handling or dealing with its stock as its Board of Directors may adopt and promulgate. All such rules and regulations shall be published to the stockholders of AGSOC and shall be available in suitable form to any stockholder at any time upon request during regular business hours.

Section 8. DEFINITION OF RESIDENT.

(a) For purposes of original issue of shares of AGSOC stock under this Act, the terms "resident", "eligible individual", or "qualified individual" shall have the same and identical meaning, and shall mean an individual, born prior to 12:00 o'clock midnight on January 1, 1979, regardless of age, who as of 12:00 o'clock midnight on January 1, 1979,⁽²⁰⁾ was a resident of and was domiciled in the State of Alaska and who remains a resident of Alaska through the date determined by the Board of Directors of AGSOC and publicly announced as such, to be the date the shares of stock of AGSOC are initially issued.

(b) For purposes of transfer of AGSOC shares subsequent to

initial issuance, "resident" shall mean an individual, regardless of age, who is a resident and is domiciled in the State of Alaska on the date such transfer is made effective.

Section 9. IDENTIFICATION OF RESIDENTS OF ALASKA ELIGIBLE TO BECOME AGSOC SHAREHOLDERS.

(a) Prior to issuing any shares of stock, AGSOC shall take all reasonable measures, by public advertising, radio and television broadcasting, and otherwise, to make known to all residents of the State of Alaska its intention to issue stock to each person eligible to become a shareholder and to similarly notify all Alaska residents of the eligibility requirements to become a registered shareholder of AGSOC.⁽²¹⁾ Such efforts shall be made from time to time and shall continue for a period of at least ninety (90) days prior to the date for issuance of stock of AGSOC, and shall be made at least once each month over the next eleven (11) months, and as frequently thereafter as the Board of Directors of AGSOC may deem appropriate. The procedural details pertaining to the identification of such persons as shareholders, either in person, or if they are minors represented by a parental or legal guardian, or if they be incompetent persons by a legal guardian, shall be fully provided to each person making inquiry at a properly designated office by a representative of AGSOC.

(b) The duty and responsibility, however, of each qualified resident to make application for registration as a shareholder of AGSOC shall rest solely and exclusively upon such

qualified resident and upon the parental and legal guardians of qualified residents, and AGSOC shall not be liable for any loss, loss of income, disadvantage or inconvenience resulting directly or indirectly from the failure of such qualified resident to make such timely application except as herein specifically provided. (22)

(c) AGSOC shall have no obligation to reimburse any eligible individual who may incur income tax liability as the result of failure to make timely application for registration as a shareholder of AGSOC, nor shall AGSOC be liable for reimbursing previously declared or paid dividends to which an applicant for registration as a shareholder would have been entitled had timely application therefor been made. Subject to these limitations, however, an eligible resident who would have been entitled to the issuance of a share or shares of stock of AGSOC, had application been made prior to the time of such issuance, or a transferee by will, or by the laws of descent and distribution, or other legal transferee, and had such qualification continued through the date of such issuance, may at any time thereafter make such application and receive the stock (or escrow certificate representing such stock) to which he shall thus be established as being entitled. (23)

Section 10. CIVIL AND CRIMINAL PENALTIES FOR MISREPRESENTATION OF FACTS DETERMINING ELIGIBILITY TO BECOME AGSOC SHAREHOLDER.

(a) Any individual who shall have received stock upon orig-

inal issue by AGSOC through fraudulent or misleading representations shall, upon demand therefor in writing being made by or on behalf of AGSOC, return all certificates or other evidence of the ownership of such shares and the full amount of dividends, whether in cash, in stock or otherwise, received thereon, together with interest at the rate of eight percent (8%) per annum from the date that such dividend or dividends were received to the date of such repayment. In the event of failure of such illegal holder of shares of AGSOC to make such restitution in full, AGSOC shall be entitled by civil action in any Superior Court in the State of Alaska to enforce such recovery, together with payment of all legal fees and court costs incurred by AGSOC in effecting such recovery.

(b) Any person who shall obtain for himself or for a person as to whom he is or has represented that he is a parental or legal guardian the issuance of shares of AGSOC through fraud, misrepresentation or by any deceitful or illegal means, shall be guilty of a Class C felony.

Section 11. SPECIAL SESSION TO APPROVE FINANCING. It is the intent of the legislature that at such time as AGSOC comes forward with a request for project financing that the Governor shall call a special session of the legislature to consider such request. However, no special session need be called if the legislature is scheduled to meet within sixty (60) days of the date of such request. In the event the legislature shall determine that financing or the guaranty of financing for an AGSOC project is necessary or desirable, the legislature shall at the

earliest convenient time call a special election (unless an election is scheduled to be held within sixty (60) days) for voting on the approval of the extension of credit to AGSOC by the State of Alaska, or the guarantying by the State of Alaska or by any agency or instrumentality thereof of the credit of AGSOC. (24)

Section 12. TRUST ACCOUNT WITH DEPARTMENT OF REVENUE.

There is hereby established a trust account within the Department of Revenue which account shall be used solely and exclusively for purposes of guarantying loans, public or private, to AGSOC for the accomplishment of its purposes.

Section 13. The following amendments shall be and hereby are made to the Alaska Statutes:

(a) Title 10, Section 10.05.012, is hereby amended by inserting prior to the first word in the second sentence thereof the words: "Except with respect to General Stock Ownership Corporations,". (25)

(b) The last sentence of Title 10, Section 10.05.186, is hereby amended to read: "Except with respect to General Stock Ownership Corporations, no classification of directors is effective prior to the first annual meeting of shareholders." (26)

(c) Title 10, Section 10.05.204, is hereby amended by adding a new Subsection (7) at the end thereof as follows:

"(7) Notwithstanding the foregoing or any other provisions of Title 10 of the Alaska Statutes, dividends may be declared and paid by a General Stock Ownership Corporation, organized under AS _____, at any time and from any source to the extent deemed by the Board of Directors thereof necessary to comply with the distribution requirements of the laws of Alaska and of the United States, except that no dividend shall be declared when such General Stock Ownership Corporation is insolvent or which would cause it to become insolvent." (27)

(d) Title 45 is hereby amended by adding a new Section 45.55.141 thereto to read:

"Section 45.55.141. The stock of a General Stock Ownership Corporation organized under the Alaska General Stock Ownership Corporation Act (AS _____._____) is not a security and the issue or sale of stock under that Act shall not be construed as a sale of a security for purposes of this chapter." (28)

Section 14. AGSOC SHALL BE EXEMPT FROM PROVISIONS OF TITLE 6, CHAPTER 25, OF ALASKA STATUTES. AGSOC shall be authorized to engage in trust and escrow activities with respect only to matters involving its own stock and to such extent AGSOC shall be exempt from compliance with the provisions of Title 6, Chapter 25, of Alaska Statutes. (29)

FOOTNOTES

1. The proposed State legislation is intended to create a corporation conforming to the requirements of the Federal legislation adopted as part of the Revenue Act of 1978. This legislation (H.R. 13511) was enacted into law as Title VI of the Internal Revenue Code of 1954, as amended. That law is reproduced herein under the title "Federal Law" and its provisions are explained in footnotes under the title "Footnotes" following the text of the Federal law.
2. Section 1391(a)(3) of the Federal enabling law requires that the corporation be chartered "by an Act of a State legislature". We believe this Bill is such an Act, even though the procedure specifically directed to be used in bringing the corporation into existence is a direction by the Legislature to the Governor specifying, to the degree required by the Federal enabling Act and by expression of intent of the Alaskan Legislature concerning certain of the details of the Alaska law and resulting special corporation. For simplicity, this contemplates that the Alaska General Business Corporation laws shall apply where not inconsistent with the provisions of this Act.
3. It is assumed that it may be regarded as either necessary or desirable by the Governor, in appointing the incorporators, who, under the provisions of the Bill would become the initial Board of Directors, to go outside the State for certain expertise and experience that may not be available within the State. The Act does not preclude all directors being residents of the State of Alaska if such be the result of the Governor's appointment of the initial Board and the result of subsequent elections by the stockholders. This tracks the Federal enabling Act. (Section 1391(a)(4)(E).)
4. The General Stock Ownership Corporation Act, which became law on November 6, 1978, as part of the 1978 tax revision legislation, was the extraordinary accomplishment of Senator Mike Gravel of Alaska. Notwithstanding the absolute newness of the concept, he managed to convince Congress (and the President) of the soundness of tax legislation that made it possible for states to help the non-capital owning many among their citizens to buy capital ownership and pay for it out of what the newly acquired capital produced. This Bill is intended to take advantage of that pioneering law.
5. This tracks the Federal enabling Act. (Section 1391(a)(3) and Paragraph (d) of that section.)
6. The Federal enabling legislation is silent on both the question of the number of members of the Board of Directors of a GSOC and the question of whether such directors may be divided into classes. However, since Alaskan law permits such division of directors into classes, this has been provided for

in order to assure greater continuity of experience and policy once AGSOC becomes operational. Stockholders would elect three directors, each to a term of three years, at AGSOC's regular annual meeting of stockholders, or at a special meeting held in lieu thereof.

7. This tracks the Federal enabling law. (See Section 1391 (a) (4) (A).)

8. This tracks the Federal enabling law. (See Section 1391 (a) (4) (B).)

9. This tracks the Federal enabling law. (See Section 1391 (a) (4) (C).)

10. This tracks the Federal enabling law. (See Section 1391 (a) (4) (D).) It should be noted that the Federal enabling statute does not prohibit a stockholder of AGSOC from changing his residence from the State of Alaska to another jurisdiction after his eligibility to be a stockholder has been established by residence and domicile in the State of Alaska on the date specified by the Legislature and on the date of issuance of the stock. However, as drawn, the Alaska enabling Act would prevent such non-resident stockholder of AGSOC from transferring his AGSOC stock, either within the initial five year period when transfers in general are prohibited, or thereafter, to any person not a qualified resident of the State of Alaska.

11. This tracks the Federal enabling Act. (See Section 1391 (a) (4) (B) (ii).)

12. This tracks the Federal enabling law. (See Section 1391 (a) (4) (D) (iii).)

13. This provision is inserted in conformity to the general policy that property transactions by minors are either void or voidable. It also provides a measure of assurance that although a parental or legal guardian of a minor stockholder may spend the dividends income accruing to such minor stockholder from his holding of AGSOC stock on his maintenance, education, etc., the stock itself is, in effect, subject to a spendthrift clause that assures the minor stockholder's receipt of his share or shares of AGSOC stock intact upon reaching the age of majority.

14. The theory of the Federal enabling legislation is designed to facilitate the acquisition of stock by all eligible residents of a state adopting a General Stock Ownership Corporation law by eliminating Federal income taxes on the corporation at the corporate level. Under Alaskan law, this has the effect of eliminating State corporate income taxes on AGSOC as well. Certainly the acquisition of ownership of capital stock in a corporation primarily out of the earnings produced by the capital represented by that stock is made easier by the elimination of one level of income taxes. Each stockholder's share of the

corporate income is included in the stockholder's individual income for Federal income tax purposes (and, unless the Alaska Legislature should determine otherwise, for State individual income tax purposes). (Federal enabling law, Section 1393(a).)

The requirement of the Federal enabling law that a General Stock Ownership Corporation distribute at least 90% of its taxable income for any taxable year by January 31st following the close of such taxable year is intended to insure, so far as possible, that no stockholder shall have taxable income attributed to him without cash dividends to pay such tax. See the Federal enabling law, Section 1396(a). See Footnote 23 in the annotations in this report to the Federal enabling legislation.

15. This tracks the Federal law. (See Section 1391(a)(5) and Footnote 14 in the annotations to the Federal enabling law.)

16. Since a right of first refusal is merely a privilege which may or may not be exercised by AGSOC, the existence of such a privilege does not in itself impose any burden upon AGSOC but does permit the corporation to provide a substitute market, particularly during the initial five year period after issuance of AGSOC's shares when the only permitted transfers are incidental to death or, as the Bill is presently drafted, by stockholders who cease to be residents and elect to transfer their shares.

17. By authorizing AGSOC to establish an escrow and trust division, into which shares of its stock acquired pursuant to its right of first refusal, or otherwise, could be transferred, without causing such shares to automatically return to the status of authorized but unissued shares, many details in connection with transfers of stock to existing shareholders, who may acquire up to ten shares of AGSOC stock, or persons who become residents of Alaska in the sense required for eligibility as AGSOC stockholders except for the fact that they were not such on the date of original issue, the establishment of such a trust and escrow division could serve a valuable function. As the remainder of Section 6 indicates, the Board of Directors could cancel such reacquired shares, assuming that no individual rights with respect thereto were outstanding, causing them to return to the status of authorized and unissued shares.

18. Section 7 of the Bill is drawn to give the Board of Directors a variety of options with respect to establishing "in-house" facilities for handling the escrow accounts and stock transfer activities of its stockholders, or for employing outside facilities, such as those of a bank or trust company, for this purpose. It would seem that the maintaining of shares of stock in escrow accounts established for each stockholder during the initial five year period when, under the Federal enabling law as well as under the provisions of this Bill, the shares of AGSOC's stock are not generally transferable