

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 8672

590 SCOM118: HOUSE SPECIAL COMM. ON PERMANENT FUND 1978-80

also the metallic minerals. In what areas, and at what times, are these commercial resources of Alaska to be developed in order to yield maximum net returns, taking into account environmental costs? Since the most important resource in value terms, oil, is extracted via leasing arrangements, and the metallic minerals may soon be too, this question can be formulated in terms of leasing policy. As a matter of fact, the Commission recently (December 1973) held a conference on minerals leasing, designed to explore whether and how the oil leasing system could be used to obtain better value from the land bearing other minerals. Among the questions considered were, what should be the objective of a minerals leasing policy, and how can it best be realized? As suggested above, a plausible objective is maximization of net social returns from the mineral in question, taking into account environmental costs of extraction and transportation. How, then, is it to be realized? What areas should be leased, at what royalty rate, and so on? We conclude with some suggestions on these matters from the economist's point of view, drawing also on some of the principles of regional development discussed earlier.

V - Minerals Leasing Policy and Alaskan Regional Development

The first question we should address is, why have any policy charging miners for use of federal, state, or native lands? We said earlier that the related policy of charging for pollution would promote efficiency, but according to a well-known theorem, the same allocation of resources would result if the polluter had the rights to use of the environment, and was paid by others not to pollute.⁹

⁹Ronald Coase, "The Problem of Social Cost," Journal of Law and Economics, October, 1960

Changing liability, or property rights, would affect only the distribution of income. Similarly, it might be expected that charging miners a royalty or rent would not affect use of the land. It would still be employed in the use which maximized value, and only a certain amount of redistribution of income, perhaps better accomplished via an explicit policy for this purpose, would result.

Although the Coase theorem is well known, less well known is that it is applicable only under certain rather restrictive conditions, namely that transaction costs and income effects are negligible. In effect assigning property rights to miners (as under the 1872 Mining Law) can lead to inefficient use of the public lands in the increasingly common case in which mining is not the highest valued use, but the costs of gathering together all of the thousands of affected parties to buy out a mining claim are very high - or more than they can afford to pay!¹⁰ The situation is the same with respect to pollution (with the exception discussed also by Coase of producer-to-producer spillovers, for which transaction costs and consumer income effects are not relevant). There seems to be a case, then, for a policy of charging for environmental modification and extraction of mineral resources, along with careful benefit-cost analyses of alternative uses of the land. Also, though this is not subject to proof, it seems desirable that the rents to scarce mineral resources on their lands should go to the native population or Alaskans generally. As noted above, present leasing arrangements for oil and gas do

¹⁰This assumes that the non-mining values are not easily capitalized.

work this way, and access to the metallic minerals, though still typically free under the 1872 Mining Law, seems to be moving in this direction.

Although there are many varieties of leasing arrangements employed, in the U. S. at least the essence of the system is bidding by mining firms for a lease to a tract of land which confers exclusive rights to the mineral, say oil, there, subject to the payment of a royalty on production. The royalty is a fraction, often around $1/8$ to $1/6$, of the gross revenues from sale of the mineral, and the amount bid is called the lease bonus. In principle, the objective of the public agency or native regional corporation is, or should be, maximization of the combined sum of bonus and royalty payments (net of environmental costs, which we ignore for the moment). The policy instrument for this purpose can be the setting of the royalty rate. But since the royalty payments are received over a long period of time and are uncertain, it may not be obvious how the rate should be set to maximize rent. In what follows, we offer some guidelines.¹¹

Suppose the public agency is less concerned than the typical private mining firm with a quick return from exploitation of the site. This seems a realistic proposition since the government (or native regional corporation) is in the position of a steward of resources for future generations, as the private firm is not. Then a given future return from the mine would be worth more to the government. Put another way, the return is discounted at a lower rate (of interest). The government discount rate might be low relative to the pri-

¹¹ This discussion is based in part on an unpublished NSF grant proposal by Hayne Leland, and on conversations with Professor Leland.

vate firm's for another reason as well. The private firm would likely be more risk-averse, requiring a higher premium for risk-bearing in the form of a higher discount rate. Now, to the extent that future returns are less heavily discounted by the government for the reasons given above, a higher royalty rate would be desirable. This gives the government a larger stake in the long-lived investment, without unduly reducing the lease bonus it receives, since the firm's bonus bid will be relatively unaffected by loss on an increment of future income. In the limit, the government might set the royalty rate at 100 per cent, in effect assuming the role of entrepreneur, hiring factors of production to exploit the mineral deposit on its property. Against the gains from this policy would have to be balanced the possibly undesirable aspects of government as opposed to private enterprise (bureaucratic inefficiency, and so on).

Apart from its differential effect on discount rates, uncertainty about returns from the mining operation should influence the choice of royalty rate for another reason. If the government is more optimistic than mining firms about the probability of discovery at a site, the size or richness of the strike, or the price it will bring, a relatively high royalty rate is indicated. Again, this gives an expected future return greater than the cost in foregone bonus. Where private firms seem more bullish, on the other hand - or for that matter more inclined to gamble - the rent-maximizing royalty rate is correspondingly reduced.

How much land, or how many tracts, should be leased at a given time?

¹²For a review of the discount rate literature, including a discussion of the reasons why government would be less risk-averse than private firms, see Krutilla and Fisher, *op. cit.*, Chapter 4.

One consideration here is the owner's monopoly power, if any. Where the state of Alaska, for example, represents a substantial share in the supply of a resource to a market, it may realize greater returns by not opening up to development too much of the resource at any one time, i. e., by not "spoiling the market". Monopoly restriction of output, which this is an example of, is generally considered socially inefficient, but may not be in this case. Spreading out extraction over time is, after all, practicing resource conservation. To the extent this is considered desirable, some element of monopoly return to the state may not be contrary to national policy.

Another influence on the rate and pattern of leasing is the effect of experience with earlier leases on expectations, and hence bids, for new leases. Exploration by the leaseholder develops information about prospects for other tracts. A favorable outcome in one is likely to result in higher bids for others close by or in similar geological configuration. Certainly this has occurred in the leasing of North Slope oil tracts in Alaska. One counter consideration here is that exploration may be less vigorous if a firm expects that much of the benefit will accrue to others. Large lease blocks may be desirable for this reason.¹³

How do environmental effects fit in the rent-maximizing framework? Recall the earlier discussion of the desirability of polluter liability. It is applicable here, and should lead to more stringent control of pipeline breaks, oil spills, acid mine drainage, and so on, as well as compensation to the victims of these effects. In cases where potential environmental damages are very great,

¹³The "information spillover" in petroleum exploration and its implications for policy are discussed by Frederick M. Peterson, "Two Externalities in Petroleum Production", study for the Ford Foundation Energy Policy Project.

or returns from the mining operation marginal, firms may not find it profitable to bid for development rights to a site, and it would remain unmodified.

It is not only the incidental effects of commercial resource development that should be taken account of. Suppose a mineral deposit, a stand of timber, or a site for hydroelectric power production, is also valuable in its natural state, i. e., if not modified for any of these purposes. Minerals and timber often occur in scenic mountain areas, and a hydroelectric site may be a free flowing stream suitable for inclusion in the national Wild and Scenic Rivers System. Loss of the recreation and other values associated with unspoiled natural environments is, or should be, just as much a consideration as potential pollution damages in the decision whether to develop a site. In principle, efficient use of the environment would require that development take place only if the expected gains (net of pollution damages) are at least as great as the opportunity losses - the values that are sacrificed by conversion of the environment to developmental purposes. We should acknowledge that both the theory and the practice of measuring these values are currently rather primitive. Hopefully this is due only to neglect, nearly total to date, and will be remedied by future research.¹⁴

We stated just above that an area should be opened up to development via minerals leasing only if the expected returns, the rents to the mineral, are at least as great as the environmental costs. Although this has to be true, given that the land manager's objective is to maximize net social returns, it

¹⁴The only organized research effort we are aware of which addresses the issue of valuing the amenity resources of natural environments, and integrating these values into a theoretical resource allocation framework, is the Natural Environments Program at Resources for the Future. For a statement of results in theory and method obtained in this program, along with some examples of empirical studies, see Krutilla and Fisher, op. cit.

conceals a point that is not obvious and should be made explicit. Earlier we spoke of long lasting or irreversible environmental damage. Where the magnitude of the damage, along with the returns from commercial development of a site, is uncertain, development may entail a cost - the loss of "option value" - in addition to the measured losses from the damage (and, of course, the direct resource costs). Option value, as the name suggests, is the value to an individual of an option to consume a good or service sometime in the future. One interpretation is that it is the amount he would pay to avoid the risk of not being able to consume, to assure the availability of the good should he demand it.¹⁵

Another interpretation, which does not depend on risk aversion, and instead makes use of a Bayesian approach, is the following. Suppose a public agency has under review an (otherwise profitable) activity which will result in the irreversible loss of a natural environment. Suppose, further, that the passage of time results in new information about the benefits of alternative uses - development or preservation - of the environment. Since this information can be taken into account only if the irreversible decision has been deferred, there is a value to refraining from development. Conversely, development entails a cost - the loss of this option value.¹⁶ One important implication for leasing

¹⁵Option value was first discussed by Burton Weisbrod, "Collective Consumption Services of Individual Consumption Goods", Quarterly Journal of Economics, August, 1964. It is further discussed and the relation to conventional consumer surplus clarified by Charles Cicchetti and A. Myrick Freeman, "Option Demand and Consumer Surplus: Further Comments", Quarterly Journal of Economics, August, 1971.

¹⁶See Kenneth Arrow and Anthony Fisher, "Environmental Preservation, Uncertainty, and Irreversibility", Quarterly Journal of Economics, May, 1974.

policy is that development of different sources of energy (or for that matter other materials) should be sequenced in a way that permits planners to take account of new information about the full social costs of each.

VI - Conclusion

The main point of this paper is that Alaska presents an unusual challenge to the U. S. and to the world to use its non-renewable fossil fuels and other natural resources in ways, and at rates of use, which reflect maturity and responsibility with respect to the rights not only of current generations, but of future generations, not only of those who will use the resource, and gain from its exploitation, but also of those on whose land it has been found. Perhaps then Alaska offers the first and last great opportunity, at least for us in the U. S., to perceive regional development not only as a process of exploiting the earth, but of achieving a new balance between the claims of economic development and social and environmental responsibility.

SCOMM

#18:5

PERMANENT FUND FREE CONFERENCE COMMITTEES 1980

cassettes:

<u>Tape No.</u>	<u>Date</u>	<u>Significant Information</u>
1	2/12	House Permanent Fund Committee meeting
2	2/14, 2/19	Senate Proposal
3	3/17	Coffman and Fry
4	3/17	Bob Richards, Ak. Pacific Bank
5	3/18	Swick, Plaia, Demand
6	3/18	Demand (con't), McLean
7	3/19	Tony Deane, Bob Greeley
8	3/19	Bob Greeley(con't), Commonwealth North
9	3/20	George Wolf
10	3/21	Peter McDowell, Bob Dupere, Angie Krukenberg
11	3/21	Krukenberg (con't), Godfry, Johnson, Stephan, Trywell, Renk, Fonger, Castle, Darbey, Aleck Reiliss, Loesche
12	3/21	Loesche (con't), discussion
13 - 16	3/22	Mark-up
17 - 18	3/23	Mark-up

reel-to-reel:

19 3/28, 3/31 Final mark-up and passage of FCCS HCS SB161.

**See also notes and minutes of meetings in committee files

3/17

PF FCC

Side 1

Coffman -

- yes { 1. have imperfections in banking system caused cap. shortage.
 { 2. have good policies

role of surplus + PF.

state consider

abolishing -

- 145 state need not be in loan business
 state should subsidize people, not capital.
 Subsidize houses, not mortgage.

185 end of summary

190 conceptual issues

real capital vs. financial capital
 capital stock & capital flow.

capital shortage - defined in either stock or flow.

240 distinction b/w. positive (cc) & normative shortage.

340 positive capital shortage - 8 reasons. (p. 3)

1. temporary, due to changes in market supply & demand.

2. perm due to mt. rate ceilings

3. markets monopolistic

4. infrastructure.

400 5. govt. created risks & uncertainties

6. taxes + regs.

7. market mechanisms

425 normative (social) shortage.

perceived needs.

1. subjective - varies from person to person

2. ignores resource constraints.

3. ignores cost.

470 p. 4 - shortage

490 transaction + info. costs

515 confusion betw. shortage of capital + shortage of income.

530 confusion betw. shortage of cap + shortage of work

547 confusion w/ shortage of subsidies

562 end of listing of varieties of normative shortage

569 If there are positive shortages, cure should fit disease.

590 shattered illusions & failure

620 end of Coffman presentation

Qs

675 Mulcahy - different illusion -

690 Coffman response - "monopoly power" (concentration)

690 Hohman - abolishing (p. 1)

C - private capital markets would be more efficient.

725 Mulcahy - fishing & timber industries

C - capital - importing - international markets.

759 Mulcahy - concern about foreign control.

C - both parties benefit.

777 Hohman - lower int. rates offset neg. effects provide Alaskans an edge.

818 end of Coffman

820 Dr. Fry

minds are fairly made up.

Outsiders' look

2 corrections to summary.

Franchise tax (p. G+H) should be 7% gross receipts tax)

840 evidence - market imperfections in rural Alaska.

850 There is no rural Ak. capital market.
no discrimination in a sense.



Side 2 Fry cont.

24 Financial capital.

40 rural Aks. have $\frac{1}{3}$ wealth of urban

120 bank branches - high concentration in rural.

145 uneconomically small

170 branch network.

185 community reinvestment act.

200 state govt. has created cap. shortage
through subsidized lending (state loans)

250 wind down loan program.

cost of providing subsidized credit

278 state loan programs have replaced private.

292 destroyed high risk, high-interest lending
crucial for sm. bus.

300 recs.

312 you can't create capital plenty.

320 capital is fungible.

348 Q5.

Malone - item G. consumption tax.

370 Fry - consumption tax more efficient than income tax.
creates incentive to save.

415 pay fed. tax on savings thru state tax credit.

425 Chat - bus. loans. Is problem high int. rate
or lack of collateral?

450 both - cash-flow problem.

504 Malone - state loan programs.

530 Fry - give them more wealth, not more mortgages

Hohman - Bristol Bay

570 Mulcahy - Lending Criteria

650 Fry response.

680 Hohman

685 Fry - If you provide all those things,
you won't have rural Ak. anymore

694 Malone - p. H - rec. B - "subsidize housing, not
mortgages"

700 Fry

712 Malone pursues -

715 Fry - make cash grants to purchaser.

"That's what they get anyway." regressive.
go to heart of problem - to the people.

730 Chet - what do we call it?

745 brief recess.

resume

Hohman - Qs for Coffman + Fry.

760 Do you believe in concept of PF?

Coffman no opinion given. Therefore, what standards.
Fry.

785 Malone - "something on paper" basic issue

797 Mr. Bob Richards - Alaska Pacific Lend, pres.
"dramatic shift" - implementation of fund.

814 achieve + maintain effective level of govt.

Services in future - overriding consideration.

2 conclusions: 1. surpluses (100%) should go
into PF rather than overexpansion.

2. PF divide into 2 parts - endowment fund (most)
and development bank.

840 structure of administration - pass out paper.

850 adm. of fund should be mt. from poli. pressures.
"quasi public org"

Side 3 10 - word "permanent" - capital preservation
endowment fund. well-defined policy.
govt. securities etc.

- 46 social objectives - normative shortages.
channel investments. Thru. deposits in Ak. banks.
CDs.
- 79 decreasing liquidity of Ak. banks. - more loans.
- 120 deposits can carry strings
- 130 achieve both objectives - preserve cap + social
existing fin. institutions as conduits.
- 150 development bank -
expand Ak's industrial base to maintain
huge revenues in the future.
substantial investment needed
- 185 "whistling in dark" - large, large projects.
- 194 "World Bank" - dams, ports, transportation
facilities. must in private projects
(oil + gas lines, refineries, etc.)
- 215 floor level - must be big.
business loans but add elsewhere -
gen. fund.
- 235 10-year, 5-year, & 1-year plans - supplied
by management to leg. bd of directors should
have broad powers.
- 256 singular objective - sustainable revenue
over long run.
- 266 social objectives - kept out + in jurisdiction
of leg.
- 280 secondary effect.
- 290 in-state investment - blown out of
proportion. magnitude requires that
it goes outside 1. Ak. economy can
absorb only so much. 2. prudent man
rule - low-risk etc.
- 324 summarize 3 key pts.
1. singular objective
2. general 2 ways - earnings of ind. fund
& expanded industrial base

3. adm. of fund independent
345 end

Qs

- 350 Malone - endowment fund concept.
375 Richards - subsidies from gen. fund.
425 M - concern about downturn of eq, default
on loans. how do you modulate the fund
450 R - If fund rec'd market rate, rate
compensates for risk.
472 M - "holiday on state loan payments."
477 R - risks everywhere - NK bonds PF wouldn't
have moderate amt of money in Ak, even
if satisfied total normative demand.
496 market loss on mortgages -
515 M - dev. bank - gasoline - risk depends
on govt. policy.
545 R - public policy is a real risk.
570 Freeman - problems w/ argument
reasonable limit to what we can absorb
585 importing earnings
R - agree completely. As banks, banks could
put out more funds if had them.
600 Freeman - limit to banks?
R - absolutely. 2 kinds - what customers
can use, & prudence. - how much do I
want this one depositor to have in
bank. (policy - limited to 20%).
620 F - protect trust.
R - maintain purchasing power - generate
return equal to inflation + add earnings to
fund.
645 Chat - dev bank concept.
what about returns? from highways etc.
R - earnings opportunities cost.

- Chat - They are normal things for govt. to do.
- 670 CC - viability - what can dev. bank do that conventional bank system can't.
- R - credit decisions are value judgments. different attitude towards risk.
- World today - more cooperation between public & private sectors.
- 715 key pt is magnitude of kinds of investments. must alter magnitude of economy. alter ec. structure
- 735 Chat - take gasline.
- 750 R - immense social implications
- 757 Malone - what sort of standards. how to agree on what is a good project.
- 790 R - present annually 3 plans.
- 808 M. separate good projects from hype
- 819 R - I'll give it some more thought.
- 825 M -
- 875 side finish

Side 4 discussion when people leaving.
next mtg. tomorrow 1:30
discussion of scheduling of additional mtgs.

40 Malone - schedule.

78 end.

3/18 PF FCC

Swick + Plaid

Swick begins

- 62 SP - commercial loans
78 market acceptability
tax-exempt
200 scenario of default
205 bond buyer looks to p.f. earnings
299 bill fraught w/ uncertainties
marketplace would only look at revenue accts.
310 TS -
320 Chat - restates point.
340 Hohman - revenue acct.
Plaid - acct. as Lynch pm.
360 education in market place. additional premium.
strange animal
380 Hohman - lapsing gen. fund balances
400 SP - true collateral.
Ceiling
417 Hohman - do you know what needles in state
no.
450 problem w/ tax-exempt? (Hohman)
SP - could trigger violation of F-e purposes
470 Hohman - E.F. Hutton
500 SP - require them to try conventional financing first?
525 Chat - screening committee
580 Hohman - abdication of leg. responsibility?
600 power debt guarantee.
625 leg. overview
640 management by Rex vs PFCap.
685 Malone - capital needs
700 Hohman responds.
725 Malone - collateral

Side 2

Philo continues

- 40 Malone - managers might look to same source
(resource sects) instead of quality of loans
- 75 Chat -
recess.
- 110 Chat - House PF bill. criteria. "trust concept"
- 200 Mulcahy - mustmt. lost in lgt. of today's inflation.
- 240 Bob Greeley asked to respond.
- 310 end of Greeley.
- 333 TS - public purpose loans.
yield curves
- 447 bond buyer index - formula in SB1.
- 510 State will end up buying most of these bonds.
- 525 Malone - reduce interest on Hk. bond purchases
- 540 Dupere - agree w/ testimony. ^{drive down rates} ^{purpose} ² reduce
of agencies issuing bonds. ³ lots of public
purpose loans to allow enuf \$ for com. loans.
- 565 Chat - bond buyer of last resort.
- 590 student loans - direct subsidy.
- 630 Milce ~~Ter~~ Demand - for himself.
responding to Coffman + Fry
market discipline

Side 3

- 36 Qs to Demand
- Malone - reactions to Richard's dev. bank.
- 215 Joe McLean - for himself (Gunnar lawyer)
- 246 gains & losses - disguise.
- 309 Social programs belong in leg. process.
- 347 Q from Malone.
- 379 end of McLean
- 380 schedule discussion

3/18 PF FCC

Public Input / Nov:

have
these
caused
cap
shortages

Imperfections in capital markets?
Govt Policies? (US Govt is also a factor) Q

- State usury law
- repeal gross receipts
- reduce reserve req
- state loans

Concepts

What can be done to imp cap shortage.

- x abolish rate, gross receipt, reserve reqmt 20%.
- x abolish state loan program
- x new state loan act

budget Q earnings

social acceptable housing

A.H.F.C. price level adjustment

consumption tax instead of state tax.

capital
real & financial
capital stock & flow.
positive shortages.

capital markets



Intervention by

govt

State

Federal

- money supply

- money supply

Q infrastructure problems
widespread public benefits
govt created risk.
lack of market mechanisms ~~do~~ to deal
with risk.

NORMATIVE SHORTAGE.

NEEDS?

subjective.

overall resource constraints.

ignores costs.

} Demand.

Transactions & Info.

Capital v. Income.

Capital & work. - Will they
benefit net benefits.

Subsidies v. Capital.

II

General Policy

Positive shortages - remedies
limited to disease.

Mulcahy - Timber investments
cited as an example.
Ownership of capital.

Geo: Preferential rates are of benefit
to Alaskans.

Control of resources thru
Nat. Res. policy.
Disadvantaged because of
lack of financing!

Dr. Frey • Capital in Rural Alaska.

No separate market for Rural Al.
economic shortage.

However, less wealth and less
equity. Which provides less.
Increasing wealth.

\$80,000.

Producing more loanable funds.

Allocation of capital.

puts $\frac{1}{3}$ of amount of urban Alaska.
reasonable to suggest.

No regional breakdown of loans.

However, monetary agencies (Fed) says
that credit loans are

State Govt — capital shortage
due to subsidized credit. I

Development questions

Security Cash flow
"Utility" (

graduated payment
loans.
Sweetheart.

- subsidize homes - not mtgs .
... houses
cash grants to purchasers .

(other approaches - cash grts
for construction materials .

Bob Richard APPB.

Coffman High-yielding assets

→ Bob Richard →
A.P.B. - President.

Notes:

FOCUSES ON IMPLEMENTATION
ON FUND. MANAGEMENT.
ACHIEVING & MAINTAINING
EFFECTIVE LEVEL OF GOVT
SERVICES.

I CLOSE AS POSSIBLE TO 100%.
II Divide into
A endowment fund
B development bank.

Remain relatively independent.
F.R.B or A.B. - quasi-public

① Endowment Fund

- protect ~~Q~~ assets
- social questions $\square$ HOW DO YOU FORCLOSE. $\square$
normative capital shortages
thru deposits in Alt Banks (curr. rate)
(say $\frac{1}{3}$) ~~deposits~~
DEPOSITS 3X - 4X
70 53
80 76

SOCIAL POLICY / ~~Q~~ FORECLOSER?
RATES

see notes

① Be difficult to replace
O+G revenues thru small
scale investment.

Generate sustainable
revenue over the long
run.

Points / Magnitude!

⇒ 2-pronged approach
is not new.

~~XXXXX~~

General problem:

"How we determine what
infrastructure projects really
have net 'benefits' " Could reform.

3/19 PF FCC

- opening remarks - Hohman + Malone
85 - arbitrary deadline
156 - Tony Dean, John Naveen & Co.
appearing at request of bond committee
200 - beginning of testimony
260 - known pools vs. blind pools
374 - when they're all put together, they have a grandeur.
384 - matter of significant concern - assign rating
on basis of weakest link in chain.
465 - worst case scenario
528 - AA rating if manage oil wealth wisely.
no issues can have rating higher than state's rating
565 - concludes formal testimony
Q from Malone. re: conclusion to be drawn.
635 - Hohman amendments to BB 161.
Kocis explains. - contribution rate
655 - board of trustees (liet. gov. as chairman)
etc.
714 - Malone - eligible nutrients.
742 - Bob Greeley
Side 2. Greeley Cont.
inflation
50 case study - w/slides. United Kingdom
Switzerland
170 week double digit inflation, almost impossible to keep up.

192 - end of slides.

discussion of UK + Switz + US news to be learned.

278 - Trust funds.

307 - futures markets - hedging

325 - liquidity

342 - Eurodollar CDs.

357 - nice to have things available if you have to use them.

379 - Malone Q

510 - Mulcahy, Q - worried about foreign risk.

611 - Malone -

630 - mortgages - hard for PF to foreclose

643 - insured real estate loans not up to quality or other
one of Holman's OMendments - would not meet safety
of principal requirement.

720 - use S.F. to meet these special requirements
(mortgages etc.)

778 - Mulcahy - problems - exporting capital.

850 - end of Greeley

860 - Sheffield + Bill Donahue + John Arthur (?)

2 week away from completing report.

Side 3001 - part way into side 3.

property tax elimination effect.

3/20

PF FCC

- 47 beginning of George Wolf testimony
100 SAC. 103 IRS - tax-exempt.
210 novelty of this sort of bill - no precedent
for being sure of leveraging on a large scale
so contemplated.
256 Hohman - loaning money at cost + some
administration. profit? - arbitrage.
300 not clear it is government program.
380 Hohman - curious def. of profit. have to
go to IRS ruling.
318 replacement clause - arbitrage.
350 IRS would likely rule that pt earnings
should be used for loans instead of
bond proceeds.
390 need to be resolved before bonds are
issued but IRS will not rule on
hypothetical transaction.
410 could get "special ruling" - very rare.
440 ruling would take from 6 mos. to yr., +
litigation could take years.
455 Copied in other states - Congress + Treasury
would not like - could be prohibited then
as retaliatory action.
480 Hohman - If passed 3 yrs. ago, would
program have offered benefits to Alaskans?
508 garden variety problems.
515 Hohman - we would have enjoyed the special
status.
526 Malone - Ullman bill
600 Malone - financing problems other than uphousing?
630 Hohman - Oregon's program.
696 end of Wolf
744 end of tape

Side 2

#9 3/20/21 end of meeting

3/21 PF FCC

Side 1

- 30 beginning of Pete McDowell
127 new start after fooling w/ equipment.
137 SB 1
180 jt. chairman's report - 1976.
233 SB 161.
340 summarize SB 1 loan programs filed.
440 additional notes - last 2 pages of memo.
448 end of testimony
453 Q Malone - cap. vs. revenue.
543 Q Malone - ex. dir. vs. dir. within mmt system.
effect on day-to-day management.
596 Q Chat - possibilities on last page - which of
B listed would be most appropriate for PF.
610 PM - option B - ind. corp. would be appropriate
form. magnitude. along w/ tools + constraints.
645 Q Chat - which bill is closest
HCS SB 161.
Q Sumner - w/o regard to ec., social purposes.
examines single commitment.
718 Q Malone.
738 Bob Dupere - wants to clear up testimony.

Side 2 15% oil receipts to loan program

- 37 huge pool of cash - from repayment of old loans.
"balancing act".
70 McDowell omitted discussion of purposes.
284 Q Sumner - how much \$ would be available
for loans. - 1,280,000,000.
304 end of Dupere.
370 Angie Kriegerberg - FHCS. - OK Lumber Co.
came in 1973.
analogy - PF like a tree in forest.
515 Holman - back to Coffman + Fry.
527 Q Chat - what brought you to it. - challenge.
620 Q Mulcahy - 1/8. separate the issues.
733 end side 2

Side 3 Q Malone - state loans - didn't get to finish

40 Angie's answer

1123 end of Angie

180 Keith Gelfrey - businessman.

not much headway being made.

public is interested in sharing in resources.

235 more \$ at a reasonable interest rate.

268 Mr. Johnson.

well aware of intrigue + games.

Legislature doesn't want to help people + business.

you've made your minds up - flying in guys from Outside. Theoretical experts.

We object strenuously.

we want it first marked in At.

we don't care about Outside markets.

359 come election time, you'll see a mandate.

365 Pat Stephan - Anch. lifetime At. - ^{large number of} family businesses.

Loans are not giveaway.

Govt. is putting us out of business.

535 Q Malone - should state institute similar program for com. loans as municipal loans just put out.

PS - should eliminate loan limits.

580 Q Malone - loan limits.

PS - no limits - If viable, feasible + collateralized, then loan whatever is needed.

Malone - thru banks or state offices.

PS - private.

655 end of Stephen

675 Ned Trywell - Anch. ~~etc~~

720 end of Trywell

725 Al Renk

742 end

Side 4 Al Renk

52 Chat -

68 Max Fenge - Anch. - teaches bus. course.

- 215 end of testimony
- 228 Mr. Castle - wants to build apt. building.
came to Ak. for opportunities.
- 270 Ed. Dorbey - Ak. Truck Center manager - Arch.
- 333 not fair for bus. to pick up slack where
banks + govt. fail.
- 345 Bev. Aleck - accountant + real estate.
1/8 of what?
- 378 when Alaskans approved PF, they wanted it
for their own use.
404. bank vs. state dept - state agency on regional/local
basis.
- 435 Q Chat -
- 488 Jim Reilis - Arch. - helps people find financing.
14% earnings vs. 8% loans - take into account
multiplying effect (social benefits).
- 522 Hohman - mentions meeting at Westward.
int. rates - Sen. Rep. - 8% + 7% (vets).
- 550 Don Loesche - Totem Air - complaining about
Coffman & Fry. "lost \$900 million in 1969"
- 582 wants to keep \$ out of PF + into loans.
PF is supposed to develop renewable resources.
- 610 The people in the state are unhappier than I've
ever seen them. recall.
- 639 Can stop boom - bust.
- 729 end Loesche
- Q Chat - we're appropriating \$3B this yr. How much
more do you want?
- DL - That should be enough, if we get it.
- 745 end of side 4

Side 5 Hohman - results of some survey.
#12 3/21 need to direct it as people want.
praises citizen involvement.
more Loesche

197 end Loesche

- 202 Stephan kid - 16 yrs. old -
afraid won't have chance to get into
business as father + grandfather did
- 226 Johnson - gov. has law right now to
settle our problems (G. F. Maestri).
- 244 Joe Eishloch - Arch. businessman -
Don't put PF in existence until all state
problems are solved.
- 312 Capital move.
- 360 end of JE
- 375 discussion of mtg. tomorrow.
12:30.
- 386 end of mtg.

3/22 PF FCC

- 1 take up HCS SB 161 re make-up vehicle
35 leg. oversight
100 flag p.3 l.7 confirmation
170 p.3 sec.4 gov's responsibilities.
250 p.2 l.10-13.
300 p.3 l.25 - At Perm. Fund.
p.4 l.10 - 50%
Hugh suggests to limit to 25% but leave
silent additional contribution. (delete 3 +
leave 4).
360 l.17-18 corp.
p.3 l.29 - bonuses - also 25%
400 p.5 Fergie Q- corp. as ind - doesn't want
it to be.
440 leave up to other legislation as to use of
m. earnings & additional approps.
450 Holman - amendment on make up of bd of trustees.
485 Malone p.6 qualification of bd of trustees.
rec - delete (b). members of adm. could serve on bd.
525 If in state agency, would ~~not~~ want to look
at law having to do w/ duties.
543 Moore Fergie his op. on bd of trustees.
F - prefer to knock out portion of bill making it
separate corp. keep it in Rev.
565 Holman - his amendment as compromise
580 Freeman - wants to require most competent
people in financing. Holman's suggested people
might not be most competent.
610 Fergie - suggest putting 100% in PF for
5 yrs. - including interest - then hire competent
people to meet in At. (provide for budget).
628 Malone - there are ways to put it in Rev. + other
possible composition of bd.
659 Chat to Ferg -

- 676 Malone - p. 8 l 14-15. may contract to Rev.
715 Ferg - reason for motion. asks for vote up or down.
all \$ except what needed for budget.
5 years.
732 and side 1

Side 2 Ferg cont.

- 20 removes motion.
43 Holman suggests going to maintmt. section.
100 House Amendments. - Malone - p. 9
purposes:
1) provide additional flex as hedge against inflation.
reason for (12)
delete (h) + substitute check to provide only
for hedging
2) (13). notes secured by mortgages
195 Holman asks Jack Johnson how limiting that
would be. Johnson - realistic + workable.
240 p. 8 l. 16 - allowable %s of various maintments.
292 Mulcahy - problems w/ foreign markets.
2 pts. interest difference - worth not?
no problem w/ amd. 13 for At. mortgages.
304 Chat - 2 full mt. pts?
313 Malone - (h) could be amended. in regard to
foreign.
400 Mulcahy - foreign maintments?
Malone - (h) would give clear authority for futures -
domestic - unless 12 is adopted too.
435 (g) is careful to prevent foreign bonds or securities
452 Malone on procedures.
490 new Holman amend. - section k - shall.
in-state maintmts.
Chat - does this substitute for amd. #3.
Korris - no conflict.

Hohman amnd. #2 - delete " + expected yield" from k-1

570 amnd. #3 - yield no lower than 10%.

590 amnd. #4 - loans secured by prop. in new capital.

610 ^{Chat} Malone - discussion of cap. move.

650 Hohman response - cap. move.

667 Ferg - wants his motion discussed in caucus.

676 recess for 1/2 hr.
resume

677 Ferg. - delete (12) + adopt (13) + new (h).

693 Malone - clarification.

710 Ferg - amend motion to include both House amendments w/ exception of (12).

716 Malone - to make consistent, omit sentence in (i) relating to § 12.

734 end side 2

Side 3 discussion of motion - no unanimous consent.

17 Ferg - move adopt Senate amnd. re: let of trucks.

35 Malone - asks F. to withdraw for now.
done.

59 Malone - move adopt S. amnd. #1 (k). may to shall

86 Ferg asks to add amnd. 3.

106 like to consider as amnd to amnd.

126 Ferg so moved.

179 Malone discussion of amnd 3.

210 Ferg. - amnd. 10% "unless rates are lower"
Malone response.

238 F. withdraws old amnd. ^{move} - "unless comparative rates are lower."

277 Malone -

285 Chat to F. prudent man rule.

343 Malone -

362 Chat -

384 Malone - intent of motion to include or exclude
"4 expected yield".

400 Holman - delete.

p. 10 l. 4 - F. reads his complete amd.
cont. discussion.

462 vote on amd. - 3 to 3 - fail

470 Q on main amd.

unanimous consent. smt. 1 passed.
move amd. C

494 discussion - Malone. Limits would only accrue
to At. banks, not to At. cc.

Kocis reply.

544 Chat - Q - approp. to limit us %?
Mulcahy - leave open for management.

574 Malone - new house amd. N: CD's.

would require collateralization of CD's or
have secondary market.

611 Ferg. prepares proposed org. S. amd.

726 Malone - amd. to amd.
discussion.

729 short recess

740 Malone - additional amendments to

762 end of Side 3

Side 4

6 Q on

30 Holman to Tillion re: newspaper acct.

70 back to discussion of CD amd.

100 F - unanimous consent to hold amd.

115 F - move to adopt. D.

references to portions
delete 12.

include 13.

Malone object.

160 discussion.

240 ~~Holman amd to~~ Q 2-4 (Mulcahy) fail.

258 schedule discussion.
397 recess 'til 9:00.

TAPES #15 + 16

(SIDES 5-8) - no notes

KHS
3/24/81

3/23 PF FCC mark-up cont.

Side 9 continued.

- 212 Rhode + Vossis explain CS + changes made.
290 Malone should amend state licensing law.
380 38.05.100 (g). could add lang. to (2) p. 4.
380 Ordmt. adopted unanimously
390 ~~Malone~~ .050 changes
513 Ordmt. ~~then~~ adopted
516 p. 6 .090 + .100
530 changes in mustmt. list
677 effective date
700 Mulcahy moves 100% of (13)
713 Malone response
722 Ord. adopted
733 new Fergie Ord
740 end

Side 10 Fergie Ord.

passage contingent on adoption of Comprehensive Alk.
Loan Program

Malone response.

- 90 Fergie requests look at HCR 33.
180 F Ord. to Ord. - change Loan Program to
comprehensive ec. assistance program.
204 Fergie - Ord to Ord. would be consistent with HCR 33
300 " - HB 505 set precedent.
325 vote - 3-3 FAIL
330 F moves to adjourn.
370 recess to 8 p.m.
8 p.m.
effective date - house Ordmts.
Malone Explains
513 mtmt
680 Fergie - wants source of revenue for loan (ec. assistance)
706 recess
708 Fergie - moves his Ordmt. re: eff. date.

127 Feige - renumber

136 discussion. Feige - can also

146 end side 10

Side 11 discussion of Feige audit.

#18 3/23 Chal - haven't we voted on this already?

70 Q 3-3 vote FAILS.

Malone -

110 move House and - sec. 8-12.

115 Feige - and. to and. delete sec. 12, division of Q.

315 back to order after break

385 Feige withdraws and. to and.

395 Q 3-3 and. fails.

405 adjourn

SCOMM

#18:6

In making their decision on the Alaska Permanent Fund, the Committees have focused on the single most important question at this time -- the management of the Fund's principal.

It is to be, as the Governor has urged, "...an inviolate trust..." which, in the words of this bill, conserves "...a portion of the state's revenues from mineral resources to benefit all generations of Alaskans..." The contribution rate has been set at 50% of mineral lease bonuses (after deducting payments under the Alaska Native Claims Settlement Act and for the Alaska Renewable Resources Fund), 25% of the mineral lease royalties from present leases, and 50% of future leases.

It is to be an independent trust, yet made accountable in various ways to "...maintain safety of principal while maximizing total return..." (page 4).

Three major concerns -- safety of principal, accountability, and legislative oversight -- are addressed by the legislation.

Safety of Principal

The House Permanent Fund bill provides a framework for highly conservative and responsible management of the Fund's principal. It assures and emphasizes the safety of the assets while providing the responsible managers with sufficient investment latitude to achieve superior results. Under the terms of this bill, the Alaska Permanent Fund would consist of a wide variety of quality, high-grade investments.

The Fund is designed to be a trust which focuses on the safety of principal first and the maximization of earnings second (page 4). It is a trust held to a more restricted list of investments than most other fiduciary trusts including the Alaska State Pension Funds and it confirms in law the current state practice of evaluating performance according to nationally recognized and accepted standards. The investment managers are required to maintain investment diversification and are allowed to determine the investment mix of short, intermediate, and long-term investments; the flexibility allowed enables the managers to achieve a sound rate of return on the investments.

The bill provides the investment managers with the authority to place funds in direct obligations of the United States Treasury, federal agency securities, certificates of deposit, high-grade corporate bonds, quality short-term investments, and federally guaranteed loans (pages 8-9). Importantly, the bill has a minimum of investment restrictions yet provides a very definite and certain framework. It does not authorize investments in stock or bullion, restricts the purchase of corporate bonds to 25% of the Fund's total investments, and limits the purchase of loans and mortgages to 25% of the total. It also prohibits the Fund from either borrowing or guaranteeing the obligations of others (page 8).

The bill also provides for the handling of gains and losses and income (page 10). Any losses not offset by gains on the sale of securities shall be deducted from income and added to the Fund principal; this protects the Fund principal from erosion. Losses from sales of securities are spread over a period of time equal to the remaining life; this encourages the managers to get rid of bad investments. Capital gains are added to the Fund principal, helping to offset the effects of inflation. The Fund income is defined as the interest received on the investments, and the amount of income available for disbursement will be determined on an averaging basis; this insures a relatively steady income flow.

Accountability

It was the aim of the Committees to establish a management system for the Alaska Permanent Fund which would be protected from political influences but, at the same time, responsive to changes in state policy and accountable to the people through their elected officials. As former Permanent Fund Committee Chairman Clark Gruening has said, "We want insulation without isolation." It was agreed that the best way of achieving these ends was not to place the management within the Department of Revenue, but to create a public corporation distinct from state government. Although the Department of Revenue currently manages the pension funds as well as the general fund, it was agreed that the Permanent Fund, with its fundamentally different goals and large size, should not be in the hands of the same people whose primary duty is managing money for day-to-day use by the state.

The proposed Permanent Fund Corporation, therefore, has its own board of trustees which is made accountable in several ways (page 5). The five members of the board will be appointed by the Governor and confirmed by the Legislature. Terms are three years, staggered, and members may be reappointed subject to reconfirmation. Members may be removed from the board by the Governor only with the consent of the Legislature. The trustees must be three-year Alaskan residents, may not hold any other state or federal office or employment, and a majority must have recognized competence and wide experience in finance, investments, or other business management-related fields. They are subject to the conflict of interest law and must disclose any interest in entities in which corporate assets are invested. They will be paid honorariums competitive with the largest private corporations in the state, and they will employ an executive director who is also subject to the conflict of interest law and responsible for hiring additional staff with the board's approval.

The corporation's operating budget is from the general fund and is subject to the Executive Budget Act (page 10). This provision offers another check on the management and will prevent such things as the hiring of excessive numbers of employees or uncontrolled expense accounts.

Among the board's responsibilities is the publishing of a yearly report (page 11) including a financial statement reviewed by independent auditors, a statement of the earnings from each investment, a market-value appraisal of the investments, and a performance evaluation with recommendations for needed changes. These reports, which must be written in easily understandable language, will be available to the Governor, the Legislature, and the public. The income statement and balance sheet will be published yearly in newspapers and every two years in the election pamphlet.

The bill thus insures that the board of trustees of the Alaska Permanent Fund Corporation will be the best investment managers available in the state, will be accountable to both the executive and legislative branches through appointment and budget processes and oversight by the Legislative Budget and Audit Committee, and will keep the public informed about the Fund's investment performance.

Legislative Oversight

The House Special Committee, like its predecessor, found a need for co-ordinated, continuing oversight of all the state's investment efforts. Accordingly, the review will extend beyond the Alaska Permanent Fund to include the Alaska Renewable Resources Fund, loan programs, the several authorities, and the general fund. As well as building up a body of legislators with detailed knowledge of investments, this new approach will give the Legislature and the broad public better information on the policies and efficiency of the various investment agencies, on the extent to which these agencies conform to statutory intent, and on the extent to which the economic and social goals of the various programs are being achieved.

The House Finance Committee also considered providing in the Permanent Fund bill for a new interim committee to handle this oversight function but decided, in the interests of efficiency, to simply expand the powers and duties of the present Legislative Budget and Audit Committee (pages 1-3). As proposed, the Legislative Budget and Audit Committee will review the plans and reports of all state agencies involved in lending or investing, report to the Legislature its findings and recommendations, and provide for audits and performance evaluations of the Alaska Permanent Fund Corporation's investment program.

It is the Committees' intent, however, that these new duties be assigned to the Legislative Budget and Audit Committee on a trial basis and that that committee report back to the Legislature within two years, recommending how best the oversight duty could be carried out and including consideration of the option of delegating the responsibilities to a separate committee.

15th draft

HOUSE JOURNAL

The Future

As stated earlier, this bill addresses only the question of Fund management and leaves the separate question of how to use the Fund earnings to later legislation. It merely assures that there will be income and does not preclude any options for its use. Until another determination is made, the Permanent Fund earnings will be deposited in the general fund.

HUGH MALONE
Chairman
House Special Committee on the
Permanent Fund

ORAL FREEMAN
Vice Chairman
House Finance Committee

HOUSE JOURNAL

In making their decisions on the Alaska Permanent Fund, the Committees have focused on the single most important question at this time -- the management of the Fund's principal. It is to be, as the Governor has urged, "an inviolate trust" which, in the words of the bill, conserves "a portion of the state's revenues from mineral resources to benefit all generations of Alaskans." It is to be independent, yet held accountable so as to "maintain safety of principal while maximizing total return" (page 4). Thus three major concerns -- safety of principal, accountability, and legislative oversight -- are addressed by the proposed legislation.

Safety of Principal

The House PERmanent Fund bill provides a framework for highly conservative and responsible management of the Fund's principal. It assures and emphasizes the safety of the assets while providing the responsible managers with sufficient investment latitude to achieve superior results. Under the terms of this bill, the Alaska Permanent Fund would consist of a wide variety of quality, high-grade investments.

The Fund is designed to be a trust which focuses on the safety of principal first and the maximization of earnings second (page 4). It is a trust held to a more restricted list of investments than most other fiduciary trusts including the Alaska State Pension Funds and it confirms in law the current state practice of evaluating performance according to nationally recognized and accepted standards. The investment managers are required to maintain investment diversification and are allowed to determine the investment mix of short, intermediate, and long-term investments; the flexibility allowed enables the managers to achieve a sound rate of return on the investments.

The bill provides the investment managers with the authority to place funds in direct obligations of the United States Treasury, federal agency securities, certificates of deposit, high-grade corporate bonds, quality short-term investments and federally guaranteed loans (pages 8-9). Importantly, the bill has a minimum of investment restrictions yet provides a very definite and certain framework. It does not authorize investments in stock or bullion, restricts the purchase of corporate bonds to 25% of the Fund's total investments, and limits the purchase of loans and mortgages to 25% of the total. It also prohibits the Fund from either borrowing or guaranteeing the obligations of others (page 8).

The bill also provides for the handling of gains and losses and income

*next pg to line before "state govt. When the
Rep. of R. " moved in H 4
from "state ... dep. of finance to ...
H ending "uncontrolled government" ...
Along the bill's report to end of that pg - stand
in All
Last pg moved in 7/12*

The House Special Committee, ~~and~~ like its predecessor found a need for ~~a~~ co-ordinated, continuing oversight of all the state's investment efforts. Accordingly, the review will extend beyond the Alaska Permanent Fund to include the Alaska Renewable Resources Fund, loan programs, the several ~~and~~ authorities, and the general fund. ~~When the review is completed, the committee will submit a report to the House and the Senate.~~

building

As well as ~~building~~ up a body of legislators with ~~more~~ detailed knowledge of investments, this ~~new~~ ~~approach~~ ~~will give the Legislature and the broad public~~ ~~more~~ better information on the policies and efficiency of the ~~various investment agencies,~~ investment agencies, various ~~investment agencies,~~ on the extent to which these agencies conform to statutory intent, and the extent to which the economic and social goals of the various programs are being achieved.

(C) This agreement expires with the adjournment of the First Session, Eleventh Alaska Legislature, unless terminated earlier as provided in Clause II(B) of this agreement.

CLAUSE III. - PROJECT DIRECTOR

The project director shall be Representative Hugh Malone, Chairman, House Special Committee on the Permanent Fund.

CLAUSE IV. - COMPENSATION AND METHOD OF PAYMENT

(A) Contractors total compensation for providing the services described in this agreement shall be the retainer of Five Hundred Dollars (\$500) per month.

(B) Per diem shall be at the prevailing State rate. Out of pocket expenses incurred as a result of these consultations,

Three major concerns --- ~~safety~~ safety of principal, accountability,
and legislative oversight --- are addressed by the ~~new~~ legislation.

It is to be an independent trust, yet ~~held in trust~~ made
accountable in various ways to ~~the public~~ "...maintain safety
of principal while maximizing total return..." (Page 4). ~~When~~

In making their decisions on the Alaska Permanent Fund,
the Committees have focused on the single most important
question ~~at this time~~ at this time --- the management of the Fund's principal.

It is to be, as the Governor has urged, "...an inviolate
trust..." which, in the words of this bill, conserves "...a
portion of the state's revenues from mineral resources to
benefit all generations of Alaskans..."

The contribution rate

~~minimum~~ has been set at 50% of mineral lease bonuses (after deducting payments under the Alaska Native Claims Settlement Act and for the Alaska Renewable Resources Fund), 25% of the mineral lease royalties from present leases, and 50% of future leases, ~~will be paid~~ ~~placed in the~~ ~~Fund~~ Fund.

HOUSE SPECIAL COMMITTEE ON THE PERMANENT FUND

HOUSE FINANCE COMMITTEE

JOINT COMMITTEE REPORT ON CS HB 281 (FINANCE)

The House Special Committee on the Permanent Fund, in designing its Permanent Fund legislation, narrowed its focus to consider the single most important question at this time -- the management of the fund principal. The bill, CS HB-281, raises the contribution level to the fund from 25% to 50% for all bonuses, and from 25% to 50% for all other royalty payments from new leases (p. 3-4). Most importantly, the bill insures that the Permanent Fund will be managed as a trust; this conforms to the Governor's "bottom line" that the Permanent Fund be managed as "an inviolable trust fund." Three major concerns -- legislative oversight, accountability, and safety of principal -- are addressed by the proposed legislation.

1.3 Legislative Oversight

The House Special Committee on the Permanent Fund found that there is a need for oversight of the performance of state agencies, including the proposed Permanent Fund Corporation, which perform lending or investment functions. Legislative oversight would provide information on the policy and performance of the agencies, the extent to which the agencies conform to statutory intent, and the impact on the economy and state treasury.

House Finance Committee also
The committee considered providing in the Permanent Fund bill for a new interim committee to handle this oversight function but decided, in the interests of efficiency, to simply expand the powers and duties of the present Legislative Budget and Audit Committee (p. 1-3). As

proposed, the Legislative Budget and Audit Committee will review the plans and reports of all state agencies involved in lending or investing, report to the legislature its findings and recommendations, and provide for audits and performance evaluations of the Alaska Permanent Fund Corporation's investment program.

It is the committee's intent, however, that these new duties be assigned to the Legislative Budget and Audit Committee on a trial basis and that that committee report back to the legislature within two years, recommending how best the oversight duty could be carried out and including consideration of the option of delegating the responsibilities to a separate committee.

Accountability

It was the aim of the committee to establish a management system for the Alaska Permanent Fund which would be protected from political influences but, at the same time, responsive to changes in basic public policy and accountable to the people through their elected officials. As former Committee Chairman Clark Gruening used to say, "We want insulation without isolation." It was agreed that the best way of achieving these ends was not to place the management within the Department of Revenue but to create a public corporation distinct from state government. Although the Department of Revenue currently manages the pension fund as well as the general fund, it was agreed that a fund of the size of the Permanent Fund should not be in the hands of the same people whose primary duty is managing money for day-to-day use by the state.

The Permanent Fund Corporation created by CS-HB-281 therefore has its

own board of trustees which is made accountable in several ways (p. 5). The five members of the board will be appointed by the Governor and confirmed by the legislature. Terms are three years, staggered, and members may be reappointed subject to reconfirmation. Members may be removed from the board by the Governor only with the consent of the legislature. The trustees must be three-year Alaskan residents, may not hold any other state or federal office or employment, and a majority must have recognized competence and wide experience in finance, investments, or other business management-related fields. They are subject to the conflict of interest law and must disclose any interest in entities in which corporate assets are invested. They will be paid honorariums competitive with the largest private corporations in the state, and they will employ an executive director who is also subject to the conflict of interest law and responsible for hiring additional staff with the board's approval.

The corporation's operating budget is from the general fund and is subject to the Executive Budget Act (p. 10). This provision offers another check on the management and will prevent such things as the hiring of excessive numbers of employees or uncontrolled expense accounts.

Among the board's responsibilities is the publishing of a yearly report (p. 11) including a financial statement ^{reviewed} audited by independent auditors, a statement of the earnings from each investment, a market-value appraisal of the investments, and ^{a performance evaluation with recommendations} an examination of the impact of the ^{for needed changes in} investment criteria on the corporation portfolio. These reports will ^{be published in newspapers and reviewed by the Legislative Budget and Audit Committee.} be published in newspapers and reviewed by the Legislative Budget and Audit Committee. ^{and over the years in the election pamphlet.}

As proposed, the Legislative Budget and Audit Committee will oversee the performance of the Permanent Fund Board and Corporation (p. 2). The committee will review plans and reports, provide for audits and review independent audits, and present reports and recommendations regarding investments and appointments to the legislature.

The bill states
In summary, CS HB 281 insures that the board of trustees of the Alaska Permanent Fund Corporation will be the best investment managers available in the state, and will be accountable to both the executive and legislative branches through the appointment ^{+ budget} process and oversight by the Legislative Budget and Audit Committee. ^{and will keep the public informed about the fund's investment performance.} In addition, the Permanent Fund will be further safeguarded by the statutory limits placed on the fund managers concerning permissible areas of investment.

Safety of Principal

8/11/81
CS HB 281 provides a framework for highly conservative and responsible management of the fund's principal. It assures and emphasizes the safety of the assets while providing the responsible managers with sufficient investment latitude to achieve superior results. Under the terms of this bill, the Alaska Permanent Fund would consist of a wide variety of quality, high-grade investments.

3
The bill provides the investment managers with the authority to place funds in direct obligations of the United States Treasury, Federal agency securities, certificates of deposit, high-grade corporate bonds, quality short-term investments and Federally guaranteed loans (p. 8-9). Importantly, the bill has a minimum of investment restrictions yet provides a very definite and certain framework. It does not authorize investments

in common ~~or preferred~~ stock, restricts the purchase of corporate bonds to 25% of the fund's total investments, and limits the purchase of loans and mortgages to 25% of the total. It also prohibits the fund from either borrowing or guaranteeing the obligations of others (p. 8).

The fund is designed to be a trust which focuses on the safety of principal first and the maximization of earnings second (p. 4). It is a trust held to a more restricted list of investments than most other fiduciary trusts including the Alaska State Pension Funds and it confirms in law the current state practice of evaluating performance according to nationally recognized and accepted standards. The investment managers are required to maintain investment diversification and are allowed to determine the investment mix of short, intermediate, and long-term investments; the flexibility allowed enables the managers to achieve a sound rate of return on the investments.

The bill also provides for the handling of gains and losses and income (p. 10). Any losses not offset by gains on the sale of securities shall be deducted from income and added to the fund principal; this protects the fund principal from erosion. Losses from sales of securities are spread over a period of time equal to the remaining life; this encourages the managers to get rid of bad investments. Capital gains are added to the fund principal. ^{helping to offset the adverse effects of inflation} The fund income is defined as the interest received on the investments, and the amount of income available for disbursement will be determined on an averaging basis; this insures a relatively steady income flow.

As stated earlier, this bill addresses only the question of fund management and leaves the separate question of how to use the fund earnings to later legislation. It merely assures that there will be income and does not preclude any options for its use. Until another determination is made, the Permanent Fund earnings will be deposited in the general fund.

In making their decision on the Alaska Permanent Fund, the House Special Committee on the Permanent Fund and the House Finance Committee have focused on the single most important question at this time -- the management of the Fund's principal.

It is to be, as the Governor has urged, "...an inviolate trust..." which, in the words of this bill, conserves "...a portion of the state's revenues from mineral resources to benefit all generations of Alaskans...." The contribution rate has been set at 50% of mineral lease bonuses (after deducting payments under the Alaska Native Claims Settlement Act and for the Alaska Renewable Resources Fund), 25% of the mineral lease royalties from present leases, and 50% of future leases.

It is to be an independent trust, yet made accountable in various ways to "...maintain safety of principal while maximizing total return..." (page 4).

Three major concerns -- safety of principal, accountability, and legislative oversight -- are addressed by the legislation.

Safety of Principal

The House Permanent Fund bill provides a framework for fiscally conservative and responsible management of the Fund's principal. It assures and emphasizes the safety of the assets while providing the responsible managers with sufficient investment latitude to achieve superior results. Under the terms of this bill, the Alaska Permanent Fund would consist of a wide variety of quality, high-grade investments.

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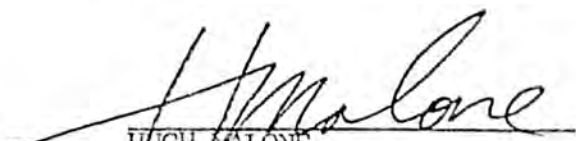
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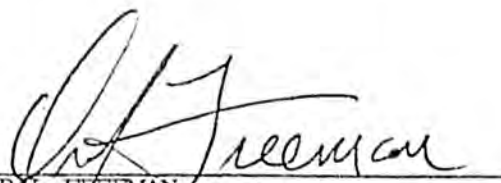
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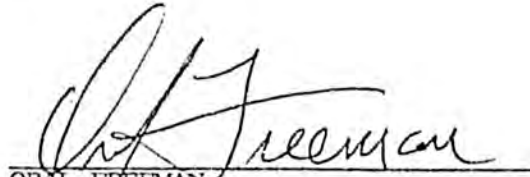
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(1) obligations of, or obligations insured or guaranteed by, the United States or agencies or instrumentalities of the United States;

(2) corporate securities which under the Securities Act of 1933 are freely marketable;

(3) short-term investments which meet the requirements of (a) and (b) of this section except for the term of the investments.

(4) loans secured by first liens on unencumbered realty or leaseholds;

(1) obligations of, or obligations insured by or guaranteed by, the United States or agencies or instrumentalities of the United States;

(2) obligations secured by reserves paid in by the United States or agencies or instrumentalities of the United States or obligations of corporations in which the United States is a shareholder or member;

(3) certificates of deposit issued by United States domestic banks which are members of the Federal Deposit Insurance Corporation and which are secured as to the payment of principal and interest in accordance with Alaska law and for which a generally recognized secondary market exists;

(4) corporate debt securities which are rated A or better by a nationally recognized rating service;

(5) short-term corporate promissory notes of the highest rating assigned by a nationally recognized rating service.

(6) bankers' acceptance drawn on and accepted by United States bank each of which have a combined capital and surplus aggregating at least \$200,000,000;

(7) repurchase agreements, the securities underlying the agreements being any of the items in (1) - (5) of this subsection;

(8) notes secured by mortgages of fully developed commercial or residential real estate if the mortgages are insured by a corporation which is authorized to do business in Alaska and has combined capital, surplus and reserves aggregating at least \$20,000,000;

(9) notes secured by conventional residential mortgages if the originating financial institution retains at least 25% of the mortgage for a minimum of two (2) years;

(10) notes secured by mortgages of fully developed commercial real estate if the originating financial institution retains at least 25% of the mortgage;

(11) the guaranteed portion of Federal Small Business Administration loans;

(12) first lien real estate mortgages guaranteed by the Federal Veterans Administration;

(13) FHA insured portion of business and industrial loans made under the Rural Development Act of 1972;

(14) the guaranteed portion of Farmer's Home Administration loans.

Mat 4/14

Suggested List of Investments

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(4) corporate securities which under the Securities Act of 1933 are freely marketable;

Option 1

(5) loans secured by first liens on unencumbered realty or leaseholds;

Add qualifying paragraph:

No portion of the assets of the corporation may be used for the purchase of loans if immediately following the purchase the proportional (market) value of all loans would exceed 30 percent of the assets of the corporation.

Option 2

(5) loans secured by first liens on unencumbered realty or leaseholds if the offering financial institution retains at least 25 percent.

INVESTMENTS PROHIBITED BY OMISSION

1. COMMON STOCK
2. PREFERRED STOCK
3. DIRECT LOANS
4. SECONDARY PERSONAL LOANS
5. NO SECOND MORTGAGES
6. FOREIGN SECURITIES
7. GOLD, SILVER OR PLATINUM
8. NONRATED CORPORATE DEBT
9. REAL ESTATE EQUITY



Alaska State Legislature

1975

Source:

SCS CSSS HJR 39(Resources) am S

HOUSE JOINT RESOLUTION NO. 39

Proposing an amendment to the Alaska Constitution, establishing an Alaska Permanent Fund for certain proceeds derived from non-renewable resources.

and the election laws of the state.

* Sec. 4. The amendments proposed by this resolution if adopted by the voters at the next general election shall become effective 90 days after the certification of the election returns by the lieutenant governor.

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

* Section 1. Article IX, sec. 7, Constitution of the State of Alaska, is amended to read:

SECTION 7. DEDICATED FUNDS. The proceeds of any state tax or license shall not be dedicated to any special purpose, except as provided in section 15 of this article or when required by the federal government for state participation in federal programs. This provision shall not prohibit the continuance of any dedication for special purposes existing upon the date of ratification of this section by the people of Alaska.

* Sec. 2. Article IX, Constitution of the State of Alaska, is amended by adding a new section to read:

SECTION 15. ALASKA PERMANENT FUND. At least twenty-five per cent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses received by the State shall be placed in a permanent fund, the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for permanent fund investments. All income from the permanent fund shall be deposited in the general fund unless otherwise provided by law.

* Sec. 3. The amendments proposed by this resolution shall be placed before the voters at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska,

Introduced: 2/22/79
Referred: Special Permanent
Fund Committee and Finance

1 IN THE HOUSE

BY THE SPECIAL
PERMANENT FUND COMMITTEE

2 HOUSE BILL NO. 281

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 ELEVENTH LEGISLATURE - FIRST SESSION

5 A BILL

6 For an Act entitled: "An Act relating to nonrenewable resource revenues; to
7 legislative oversight; and providing for an effective
8 date."

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

10 * Section 1. AS 24.20 is amended by adding new sections to read:

11 ARTICLE IV. INVESTMENT OVERSIGHT COMMITTEE.

12 Sec. 24.20.600. INVESTMENT OVERSIGHT COMMITTEE ESTABLISHED. The
13 Investment Oversight Committee is established as a permanent interim
14 committee of the legislature. The establishment of the committee recog-
15 nizes the need of the legislature for technical review and oversight of
16 the performance of all agencies of the state which perform lending or
17 investment functions.

18 Sec. 24.20.610. FINDINGS. The legislature finds that there is a
19 substantial need for oversight of the performance of all agencies of the
20 state which perform lending or investment functions since these func-
21 tions do not receive the detailed review to which other expenditures of
22 public money are subject, and therefore the knowledge necessary for
23 sound legislation in this area is not readily available. There is a
24 need for legislative oversight which will provide information on the
25 policy and performance of these agencies, the extent to which the
26 agencies conform to statutory intent, and the impact of their perfor-
27 mance on the economy and treasury.

28 Sec. 24.20.620. PURPOSES. The purposes of the Investment Over-
29 Sight Committee are to

1 (1) monitor and report

2 (A) the performance of the agencies of the state which
3 perform lending or investment functions,

4 (B) the extent to which the performance of these agen-
5 cies has contributed to the fiscal, financial, economic and social
6 improvement of the state and its citizens,

7 (C) the extent to which these agencies and the executive
8 have prepared and coordinated short and long term economic, fiscal,
9 investment and financial planning;

10 (2) hold these agencies accountable to statutory intent in
11 their performance by recommending, where appropriate, changes in policy
12 to the agencies or changes in legislation to the legislature;

13 (3) annually review the extent of capitalization of the
14 investment funds of the state and alternative investment policy for the
15 general fund surplus and recommend needed legislation.

16 Sec. 24.20.630. MEMBERSHIP. The Investment Oversight Committee is
17 composed of eight members: the president of the senate, the speaker of
18 the house, and three members appointed from each house by the respective
19 presiding officer. The membership from each house shall include at
20 least one member from each of the two major political parties. The
21 committee shall select its own chairman.

22 Sec. 24.20.640. TERM OF MEMBERSHIP. (a) The Investment Oversight
23 Committee shall be organized within 15 days after the organization of
24 each legislature. Members serve for the duration of the legislature
25 during which they are appointed. If a member is reelected or his term
26 of office extends into the next succeeding legislature, he continues to
27 serve until reappointed or until the appointment of his successor.

28 (b) When a member of the Investment Oversight Committee files a
29 declaration of candidacy for an elective office other than that of

1 member of either house of the legislature, and he has not resigned from
2 membership on the committee, his committee membership terminates on the
3 date of filing.

4 Sec. 24.20.650. VACANCIES. When a vacancy occurs in the statutory
5 or appointive membership of the Investment Oversight Committee, the
6 presiding officer of the house incurring the vacancy shall choose a
7 successor. If the office of the president of the senate or speaker of
8 the house of representatives becomes vacant and a vacancy from the
9 affected house occurs among the membership of the committee, the re-
10 maining committee members from the house incurring the vacancy shall
11 appoint a new member.

12 Sec. 24.20.660. MEETINGS. The Investment Oversight Committee may
13 meet during sessions of the legislature and during the interim between
14 sessions at such times and places in the state as the chairman may
15 determine. Members may receive, for the minimum time required to get to
16 and from meetings and for the period while attending meetings, the same
17 travel and per diem allowances provided by law for members of the
18 legislature when attending sessions, except that members of the commit-
19 tee receive no per diem during legislative sessions other than the per
20 diem allowance paid to other members of the legislature.

21 Sec. 24.20.670. POWERS. The Investment Oversight Committee has
22 the power to

23 (1) organize, adopt rules for the conduct of its business,
24 and prescribe procedures for the comprehensive fiscal analysis, budget
25 review and post-audit functions of those agencies of the state which
26 perform lending or investment functions;

27 (2) hold public hearings, administer oaths, issue subpoenas,
28 compel the attendance of witnesses and production of papers, books,
29 accounts, documents and testimony, and have the deposition of witnesses

1 taken in a manner prescribed by court rule or law for taking depositions
2 in civil actions;

3 (3) require all state officials and agencies of state govern-
4 ment to give full cooperation to the committee or its staff in assem-
5 bling and furnishing requested information;

6 (4) hold public hearings on the confirmation of the members
7 of the Board of Trustees of the Alaska Permanent Fund Corporation, and
8 the members of the Board of Trustees of the Alaska Renewable Resources
9 Corporation;

10 (5) prepare and distribute reports, memoranda, or other
11 necessary materials;

12 (6) make recommendations concerning the structure and operat-
13 ing practices of all agencies of the state which perform lending or
14 investment functions;

15 (7) receive and review reports and post-audit analyses con-
16 ducted by the Legislative Budget and Audit Committee relating to all
17 agencies of the state which perform lending or investment functions;

18 (8) enter into and enforce all contracts necessary or desira-
19 ble for the functions of the committee.

20 Sec. 24.20.680. STAFF. The legislative audit division and the
21 legislative finance division shall provide audits, reports and analyses
22 requested by the Investment Oversight Committee. The committee may hire
23 and determine the salary of the staff it considers necessary within the
24 limit of the budget approved by the legislature.

25 Sec. 24.20.690. DUTIES. The Investment Oversight Committee shall

26 (1) report to the legislature its recommendations relating to
27 the confirmation of suggested appointees to the Board of Trustees of the
28 Alaska Permanent Fund Corporation and the Board of Trustees of the
29 Alaska Renewable Resources Corporation;

1 (2) annually review the long-range operating plans of all
2 agencies of the state which perform lending or investment functions;

3 (3) review periodic reports from all agencies of the state
4 which perform lending or investment functions;

5 (4) present a complete report of investment programs, plans,
6 performance, and policies of all agencies of the state which perform
7 lending or investment functions to the legislature within 30 days after
8 the convening of each regular session;

9 (5) present to the legislature within 30 days after the con-
10 vening of each regular session a review of the report of the governor
11 under AS 37.07.020(b) with recommendations for any needed legislation;

12 1 (6) in conjunction with the finance committee of each house
13 recommend annually to the legislature the investment policy for the
14 general fund surplus and for the income from the permanent fund;

15 (7) provide for an annual post audit and annual operational
16 and performance evaluation of the Alaska Permanent Fund Corporation in-
17 vestments and investment programs.

18 Sec. 24.20.700. RECORDS. The Investment Oversight Committee shall
19 keep a complete file of all reports presented to it and all reports
20 presented by it to the legislature or to a legislative committee.

21 * Sec. 2. AS 37.07.020 is amended by adding a new subsection to read:

22 (b) The governor shall annually, before the convening of the
23 legislature, report to the legislature through the Investment Oversight
24 Committee the long-range fiscal and economic consequences of

25 (1) alternate levels of capitalization of the investment
26 funds of the state; and

27 (2) alternative investment policy for the general fund sur-
28 plus.

29 * Sec. 3. AS 37 is amended by adding a new chapter to read:

1 CHAPTER 13. ALASKA PERMANENT FUND.

2 Sec. 37.13.010. ALASKA PERMANENT FUND. (a) Under art IX, sec. 15
3 of the state constitution, there is established as a separate fund the
4 Alaska permanent fund. The Alaska permanent fund consists of

5 (1) one hundred per cent of mineral lease bonuses after
6 deduction of any amounts allocated

7 (A) to the Alaska Native Fund under the Alaska Native
8 Claims Settlement Act and implementing state legislation; and

9 (B) in AS 37.11.020 to the Alaska renewable resources
10 development fund;

11 (2) thirty per cent of all mineral lease rentals, royalties,
12 royalty sale proceeds, and federal mineral revenue sharing payments
13 received by the state; and

14 (3) any other money appropriated or otherwise allocated by
15 law to the Alaska permanent fund.

16 (b) Payments due the Alaska permanent fund under (a) of this
17 section shall be made to the fund once each month.

18 (c) The Alaska permanent fund shall be managed by the Alaska
19 Permanent Fund Corporation established in this chapter.

20 Sec. 37.13.020. FINDINGS. The people of the state, by constitu-
21 tional amendment, have required the placement of at least 25 per cent of
22 all mineral lease rentals, royalties, royalty sale proceeds, and federal
23 mineral revenue sharing payments and bonuses received by the state into
24 a permanent fund. The legislature finds with respect to the Alaska
25 Permanent Fund Corporation that

26 (1) the corporation should provide a means of conserving a
27 portion of the state's revenues from mineral resources to the ultimate
28 benefit of future generations of Alaskans;

29 (2) the corporation's [primary] goal should be to maximize

1 total return while maintaining safety of principal;

2 (3) the corporation should be used as a savings device
3 managed to allow the maximum use of disposable income from the corpora-
4 tion as needed for purposes designated by law.

5 Sec. 37.13.030. PURPOSE. It is the purpose of this chapter to
6 provide a mechanism for the management and investment of those permanent
7 fund assets allocated to the Alaska Permanent Fund Corporation in a
8 manner consistent with the findings established in AS 37.13.020.

9 Sec. 37.13.040. ALASKA PERMANENT FUND CORPORATION. There is
10 established the Alaska Permanent Fund Corporation. The corporation is a
11 public corporation and government instrumentality in the Department of
12 Revenue managed by a board of trustees but has a legal existence inde-
13 pendent of and separate from the state. The purpose of the board is to
14 manage and invest the assets of the corporation in accordance with this
15 chapter.

16 Sec. 37.13.050. COMPOSITION OF BOARD OF TRUSTEES. (a) The Board
17 of Trustees of the Alaska Permanent Fund Corporation consists of three
18 members appointed by the governor and confirmed by a majority of the
19 members of the legislature in joint session.

20 (b) The board shall annually elect a chairman from among its
21 members.

22 Sec. 37.13.060. TERM OF OFFICE. The members of the board shall be
23 appointed for terms of four years, and they may be reappointed. Terms
24 shall be staggered. Initial terms shall be one member serving for two
25 years, one member serving for three years, and one member serving for
26 four years.

27 Sec. 37.13.070. REMOVAL AND VACANCIES. (a) The governor may
28 remove a member of the board from office by and with the consent of a
29 majority of the members of the legislature in joint session. A removal

1 by the governor shall be in writing and state the reason for removal.
2 If the legislature is not in session, the governor may suspend a member
3 of the board. Upon suspension, a vacancy is not created but the board
4 member may not participate in board business and may not be counted for
5 purposes of establishing a quorum. The joint session shall be held
6 within 30 days from the date of removal if the removal occurs while the
7 legislature is in session or within 30 days of convening of the legis-
8 lature if the legislature is not in session. If the legislature refuses
9 to consent to his removal, the board member shall be reinstated to his
10 position.

11 (b) A vacancy on the board shall be promptly filled by appointment
12 by the governor and confirmation by a majority of the members of the
13 legislature in joint session, and an appointee to fill a vacancy shall
14 hold office for the balance of the term for which his predecessor on the
15 board was appointed. If a vacancy arises on the board while the legis-
16 lature is not in session, the governor may appoint an interim board
17 member who shall exercise all powers of a permanent board member until
18 such time as the legislature in joint session fails to confirm the
19 appointment of the interim board member

20 (c) A vacancy on the board does not impair the authority of a
21 quorum of the board to exercise all the powers and perform all the
22 duties of the board.

23 Sec. 37.13.080. QUALIFICATIONS OF BOARD OF TRUSTEES. (a) No
24 individual may be appointed to the board who has not been a resident of
25 the state for at least three years.

26 (b) No member of the board may hold any other state or federal
27 office, position or employment, either elective or appointive, except as
28 a member of the armed forces of the United States or of this state.

29 (c) At least one member of the board shall have recognized compe-