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Appendix
to
Final Report
of
The House Special Committee on the Permanent Fund

VOLUME I - Transcripts, Minutes

- Rep. Clark Gruening, Chairman
- Rep. Terry Gardiner, Vice Chairman
- Rep. Ernie Haugen
- Rep. Russ Meekins
- Rep. Bill Miles
- Rep. Leo Schaeffer
- Rep. Rick Urion

These transcripts were taken from tape recordings. They have been edited for the purpose of clarity. The original recordings are in the possession of the committee and may be heard upon request.

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice
Chairman; Bill Miles, Russ Meekins, Leo Schaeffer;
Hugh Maline; John Rader; George Hohman.

TUSSING: I am not going to read the paper, nor am I going to go through it point by point. Frankly, it is a little too heavily steeped in jargon and it is hard for me to get back and read it through a couple of weeks after I have done it and exorcise all of the economist catch phrases and financial catch phrases.

GRUENING: Arlon, give us a little bit of your background. There may be a few people who haven't heard of you.

TUSSING: I know almost everybody here. If they don't know me, maybe it is their hard luck. I am a adjunct professor of economics at the Institute of Social and Economic Research at the University of Alaska. I have been connected with the university in one way or another for eleven years. With the short study requested by Representative Gruening to cover some of the background of economic issues that the committee felt had not been really treated before the committee got into looking at the organization in terms of the permanent funds. I have read Dr. Daniel's paper, and let me assure you that until this morning I had never met him and we did not cooperate or collude in any way. So I found nothing in his paper that I could disagree with and a great deal I could

agree with.

GRUENING: I might just introduce the committee. I am the chairman of the House Permanent Fund Committee and sitting next to me is George Hohman, the chairman of the Senate Committee on the Permanent Fund. Two members of the Senate committee are here in attendance, the president of the Senate, John Rader. At the end of the table, Senator Pat Rodey, from the Senate. On my left, from the House, is Representative Terry Gardiner who is vice chairman, and Representative Bill Miles. Going down on the right side, Representative Russ Meekins and Speaker of the House Hugh Malone who is not a member of the special committee, but has an interest in the Permanent Fund.

TUSSING: Let me emphasize one issue in particular which is mentioned in my paper but does not have---does not really focus on as much as I would like to focus on. That is that the investment policy of the Permanent Fund will have far less influence on the rate and shape of economic development in Alaska than the amount of money in the general fund and the way the general fund money is spent. For one thing, the general fund is going to be much larger than the Permanent Fund according to the kind of numbers we are talking about, as far as revenue dedications to the Permanent Fund.

A Department of Revenue projection issued in February of this year, assuming a 25% contribution revenue to the fund projected in 1985 Permanent Fund balance of \$1.8 billion and a general fund

balance in the same year of \$6 billion, as based on the projections of existing programs and the anticipated gross rate in state spending. That \$6 billion is surely not going to accumulate in the general fund. There is going to be enormous pressure to spend it. But the general fund---the money available in the general fund will be much greater than the money available in the Permanent Fund. For another reason the general fund will have more influence is that its expenditures in general move directly into a spending stream in the state's economy through payrolls and procurement while the Permanent Fund money, much of it will be invested outside and, as I will explain in a moment, probably all of it will be in effect invested outside no matter what the investment policy the Permanent Fund is.

Thirdly, the Alaska demand for Permanent Fund investments is extremely low. There is very little additional demand in terms of potential income earning projects which can be funded by the Permanent Fund which would not be funded through existing financial sources and much of my paper is devoted to this. An examination of the question of whether or not there is a capital shortage or not---in other words whether or not the existing financial institutions are sufficient mechanism to bring capital into the state.

My conclusions are this: Major industrial ventures in Alaska, and this includes ventures in fish processing, mining

timber, major agriculture developments, major tourist operations, are very adequately served by existing financial institutions. That there is no financial obstacles to their continued rapid development in the state. The obstacles that exist tend to be problems of resource location and marketing regulatory problems including state leasing and permitting and federal leasing and permitting. But they are not financial problems, for the kind of large industrial venture that would significantly diversify the state's economy, or the kind of large industrial venture that would be piggyback on our oil and gas industry like petrochemical. These investments will be made by large national or multi-national corporations drawing on their regular sources of finances. For those that are independently developed within Alaska, the new ventures with new enterprises, there are a large variety of institutions in the capital market that are interested in the financing required investment.

I will give an example of this from my personal experience and involved in a new fishing port in a remote totally undeveloped site in Western Alaska. The preparatory work putting together of the land leases and getting the engineering design on the port facilities had just barely begun and we have made no public announcement of this, yet within a few weeks after this started we had been approached by three major outside banks---one New York bank, one California bank and one Canadian bank, who were very interested in putting together a financing package for this venture which is

just a beginning of a conception. All of these banks have specialists to deal in Alaska and there is no lack of information to prevent them from going and looking for more information and looking for investment opportunities. They are as aware of anybody in Alaska or as aware as the managers of the Permanent Fund of the opportunities that the expansion of U. S. National Fisheries jurisdictions and the growing world demand for protein and the opportunity that it will create for bottom fisheries and other fisheries in Alaska. One of these major New York banks has a specialist who is heading up a whole team dealing with these problems specifically.

Another experience we had was that directors of the new firm were immediately inundated with approaches from friends who had invested and who were looking for places to put venture capital. High risk, high potential return ventures with large tax write offs. People come in and say I have got \$29 million I have to place during this tax year, or I have got a problem. They want a potential rate of return but most of these big development ventures aren't terribly sensitive to the small differences and the amount they pay per capita. A major venture, a big venture, that where there are millions of dollars involved, those millions of dollars can carry a great deal of investment research and exploratory work on the part of either the ultimate investor or the financial intermedior, the insurance companies or brokerage houses.

So my conclusion with respect to major industrial venture, not only is there no problem, no specific problem, but that Permanent Fund investments in these ventures will essentially displace capital that would come in from the outside. So from the point of view of impact, the point of the impact in Alaska's economy, or the impact in diversification of Alaska's economy is going to be very little. A concentration on these ventures might on the other hand affect the security of the quality of the loan portfolio of the Permanent Fund because, in a sense, you are putting all your eggs in one basket called Alaska and the very thing that may make your regular revenue fall may make these investments in Alaska enterprises particularly risky.

Move on to another area in which the Permanent Fund probably has no role and no particular effect, and that is the commercial loans in the urban areas of Alaska. There is no capital shortage here. The existing financial institutions, the commercial banks, thrift institutions, factors, mortgage brokers, etc. and both the commercial and residential, it is the same way in Alaska as in the rest of the country---there is no substantial interest rate differential between Anchorage and communities of comparable size in the rest of the United States. There seems to be a greater availability of loan money, partly because the people in some of the outside financial institutions have a great faith in Alaska because the growth is assured. There is no problem, there is no capital shortage to be filled by the Permanent Fund in the area

of equipment financing, the kind of item trucks, construction equipment, generators, compressors, aircraft, etc., which are movable where the financing is available from vendor to manufacturer, from equipment financing companies, from banks and smaller units from credit unions and the like. No matter where you are in Alaska, if you need a backhoe and you've got something useful to do with it, and a prospect of some income, you can finance a backhoe. There is no capital gap for the Permanent Fund to fill here. The question of utilities and other utility type interest subsidy investments is often raised and I see quite a bit of talk about the Permanent Fund providing credit to the Alaska Power Authority or to the Susitna project. This could be done but it is another incident where the Permanent Fund would probably simply be displacing money that would be available from outside. If the Susitna project is viable, if it can prove that it can pay its debts or can be financed conventionally, and the reason that---there are several reasons why the Permanent Fund should probably not be involved in financing the long term debt of the Susitna project.

First is that the Alaska Power Authority can issue tax exempt bonds, while at the same time the Permanent Fund can invest in taxable corporate bonds, for example, or federal securities that get a higher rate of return than the Alaska Power Authority or any solidly based Alaskan utility would have to pay. It makes no sense for the Permanent Fund to be

getting a low rate of interest on its investments than it can get in the open market while at the same time the Alaska Power Authority doesn't get any break on the cost of capital.

Now, conceivably, the Permanent Fund could be used as a source of equity capital for joint ventures. However, going through most of the major categories of the capital market in Alaska, these are either areas which are adequately served by the existing financial institution or ones in which the Permanent Fund could probably not make a useful contribution anyway.

One area does stand out as an area of opportunity and in this very preliminary survey it seemed to me that the one capital market that is not serving its constituents well is that serving small community business, medium size business in the small communities and in the Bush in Alaska. The urban commercial banks in Alaska just don't reach out far enough. The cost of information gathering, of servicing loans, the cost of collections and repossessions, foreclosures, resale and things are just too much. Outside institutions don't deal with them. The demand is too sparse. So the tourist oriented business or a local store or a small locally owned fish processing venture or something on that order may not be able to borrow, or, for that matter, to obtain any sort of capital on terms comparable with a similar venture---a venture with similar early expectations in a major community. And so I think there is an area in which the state could look at the formation of regional development. Probably a statewide development bank would be too

big and would be too far from the---the problem in the Bush and the small communities have people on the scene oriented to problems of the particular community. I would suggest looking at the possibility of setting up a state-chartered regional development bank in each of the regional corporation areas and working together with the regional corporations, or having the regional corporations participate in these rural development banks, but having a professional management supervised by the Permanent Fund using Permanent Fund money. The problem here is that I doubt whether the aggregate demand for capital from all of these banks would be greater than forty or fifty million dollars at the present time. A great number of people in smaller communities in the Bush who feel that they are not well served by the existing banking system. But the total amount of real business they would generate is relatively small and you are not talking about billions of dollars---you are talking about tens of millions most likely. Just think of what it is in the Calista region which has induced the Calista Corporation to put its money outside of the region. How much potential private investment that could be locally developed does exist? How much opportunity is there in the Calista region? It is nothing like the kind of funds we are talking about with the Permanent Fund. So I would say by and large the potential role for the Permanent Fund money in altering the shape or

character of Alaska's economy on a business-like basis is rather small.

I go on to say the Permanent Fund is not a very promising tool for short economic stabilization. I am not sure how many people really think that it could be but I've heard it referred to as something that could feed money into the economy in a slump period and slow down the investment activity in a boom period. Now as far as dealing with the regular business cycle that lasts two or three years, there is a number of reasons why Permanent Fund is not a promising tool.

In the first place, its impact is less and slower than that of the general fund. The impact of the Permanent Fund investment policy is going to be very, very minor compared with what is done with the general fund. The general fund expenditures are direct injections into the state's economy. They occur now and secondly because Permanent Fund investments---many of them will simply be displacing capital which would otherwise come in but there is another fundamental problem that, even if these were not ---even if these previous problems were not involved, there is another problem that would probably make it impossible to use the Permanent Fund or general fund appropriations for that matter as a significant stabilizing force. That is by the time it takes the management to recognize that we are in an overheated boom situation that something ought to be done about, we may well be approaching a turning point. So it takes some time to recognize something ought to be done. Then you have to implement the policy. And by the

time the loans are made and the people or concerns who receive those loans start paying construction workers, it is very likely that we are going to be on the other part of the cycle. But the effect of the Permanent Fund---or for that matter the effect of the legislature---trying to use the capital budget as a stabilizing device is that you are going to zig when you ought to zag.

There is a very good persuasive case on the part of some economists that the federal reserve has been more often ---that the effect federal reserve policy nationally has been more often wrong than right. We could build a business cycle model of the Alaska economy and give legislators in the--- give them say \$4 billion on a computer to play with. We will start the thing off at 1964 after the earthquake and see whether there is any---see what you can do on the basis of the effect on unemployment, building starts, on gross products if you have gross products, and things like that. See what happens as you try to influence the economy with this. My intuitive guess is that it would create---no matter what you did trying to do it would create oscillations in the economy that wouldn't have existed before. I just don't think that it can be done.

There is another problem. It is a practical, political one. That is, when the money is available, when you are in a recession situation, when the money is available there is

resistance to spending it. You are in a boom, no matter how high the rate of inflation and how great the pressures that boom is creating on public facilities. It is going to be very hard to get anybody, whether it's in administration, legislature or managers of the Permanent Fund, to say we ought to turn off the water when the revenue is more available than it has ever been before and the needs are growing by leaps and bounds because of this boom and population influx. If you are skeptical about that, look at what happened to all the talk about stockpiling of public works projects until after the pipeline construction is over. It just is not going to happen.

Nevertheless, the Permanent Fund can be an important long-term stabilizing influence. That long-term stabilizing influence as the main intention of the people in voting the Permanent Fund and the legislature for establishing one. That is the result of the fact that state spending is the main engine of growth in Alaska. It determines in the long run the level of employment and level of population and determines the needs for government service. The principal influence of the Permanent Fund on growth and on the size of the state's economy is the amount of money it takes out of the general fund.

The Permanent Fund is going to influence the rate of growth of the state's economy, but not on the supply side. It is going to have almost no impact on the rate of growth by the way it spends

money, or the way it invests money. It will have a gigantic impact in terms of the amount of money that is dedicated to the fund because, for every hundred million a year that goes into the Permanent Fund, there is a hundred million that is not in the general fund for current operations and for state capital expenditures or for current consumption. In the next decade or two, the legislature is going to determine the rate of employment and population growth in the state and it is going to determine the rate at which the need for state services increases by the way in which it spends the money. It makes some difference whether this money is spent in tax reductions, in transfer payments such as Alaska, Inc. or welfare, on regular operations of government or on construction.

It would be worthwhile to have a comprehensive fiscal model of the state's economy so that you can look at what the differences are, but the differences aren't as important as similarity. The more you spend, the bigger the economy is going to grow, the more population we are going to have in the state and the greater the need for state services are going to be a year or two or five years down the line. So the more money that is not available for this process today, or the more money that is not spent, the smaller the employment and population base and the smaller the needs will be.

What the Permanent Fund does and its principal function

and principal predictable function is that it slows down the development of the state by diverting money from current expenditure. There is hope that it creates enough income and it grows to the point where it can sustain the state expenditures that sustain the rest of the civilian economy of Alaska in those days after the oil money is gone or when the oil money levels off or when the oil money stops increasing in amount as fast as the perceived need for population are increasing.

So if you take this revenue bubble and put it in the future, you stabilize the economy. I have two final points on this. The eye of the legislature ought to be much more on the amount of money that goes into the Permanent Fund than it is now, and probably a little less on dividing up the---or deciding what kind of portfolio the fund should have. And that the 6%, say 25%, does not solve the problem, it does not---25% of the nonrecurring oil revenue going into the Permanent Fund does not do away with the revenue excess, nor does it do away with the use of this oil money to create here in Alaska an economy.

It is just not when the oil money runs down and the oil runs out, that will be a long time, but when the rate of growth of state revenue starts to slow down. So putting 25% just means you got 75% left there with an enormous growth in those years when you have got a lot of revenue and very little when the revenue stops coming. So it seems to me we ought to start thinking in terms of what kind of formula for contributions to the Permanent

Fund will stabilize or create stable growth over the long term in the general fund and to do this you have to get some view---have some philosophy of growth for the state. That is, how rapidly should the state's economy grow. As I said, the legislature is going to determine how fast the state is going to grow by the amount of the money spent.

So you need some sort of formula and it should not be a fixed percentage. It should be something on the order of after your studies have determined the 6% or annual rate of growth, the real value of the general fund expenditures is what you need to sustain the reasonable growth in the standard of living in Alaska and a reasonable rate of population growth.

So, as far as what needs to be known, the research ought to be done. I think the legislature ought to look very heavily at just what are going to be future revenue needs. What is the projected income from other sources. And just how much of that gap is going to have to be filled from mineral royalties. Assuming that Prudhoe is the last big field and put in some speculative reserves and making assumptions about the price of oil and the rate of other resource development, and you say at what point are current revenues not going to be enough to sustain the level of government, the level of population, the standard of living that we want to maintain, and that will

tell you at what point you are going to have to start drawing out of the surplus in the capital fund to maintain this economy. If people are lucky, the growth will have a sufficient momentum that you will have future oil discoveries and you can keep putting off that day of reckoning, so that you may never have to draw on the accumulative surplus, much less the capital. But the principle remains the same. The most effective use of the Permanent Fund is to control what is available in the general fund, to make less available now and more available in the future. What should be in the general fund probably is the most important to know in setting up the Permanent Fund.

GRUENING: Thank you very much, Arlon. As usual, you have raised a few questions.

TUSSING: In summary, I think most of the investments of the Permanent Fund in Alaska will simply displace money that will come from somewhere else. Now it is possible to increase investment of various industries by subsidization or making loans available cheaply. The problem is that most of the ventures that would take advantage of them are ones that would be viable in any case. Both Dr. Daniels and I made the point that most new ventures, their feasibility is not very sensitive to interest. I mentioned in here that a new venture probably that expected to be able to be

written off in five years or so, which means a growth cash flow is in 30 to 50% of investment capital, and when you have got to have cash flow of that magnitude, a couple percentage points difference from what you are paying for, capital is not a crucial factor.

Well, I admit there might be some cases---in fact I was going to---there will for certainty be some cases which a prudent Permanent Fund manager might reasonably deem to be a prudent investment and managers of other outside financial institutions might not. Those marginal cases are probably so limited compared to the number of---if you are going to cover those, you are probably going to be giving money at subsidized interest rates or giving higher leveraging to a lot of other people who don't need it, and in those other cases you are simply giving away potential earnings from the Permanent Fund and for the propose of backing out capital which would otherwise be there. There may be some such cases at the margin, but I am very skeptical, first, about how many there are, and too the volume in terms of capital demand, and secondly, the ability of the Permanent Fund managers to discern those. I would ask why it is if these are trustworthy investments that can earn a market rate of return and the risks are not too great, why it is that some combination of investors and lending ---why the promoters who are putting it together haven't been able to package it attractively enough that somebody will

finance it in view of the enormous diversity of capital market. As I say, there is the availability of the insurance company money in large amounts for wealth secured investments of the availability of high return---high cost, high capital for the others and there is everything in between, I would just ask the question in this case, why is it that the Permanent Fund manager thinks it is so much better than the investment and there may be some---there may be some---but most of them are limited by resources or by the local interest structure or something of that nature.

GRUENING: I think Terry has a question here.

GARDINER: I have got a couple. What is the advisability of the Permanent Fund financing the El Paso gas line?

TUSSING: Well, it seems to me that the talk of the Permanent Fund financing is a political gimmick to get some support outside. There may be some resistance in Congress, the federal loan guarantees and if the State of Alaska will undertake those guarantees, maybe the Congress or somebody...

GARDINER: Are you saying that...

TUSSING: Well, I said in the past, I am skeptical about financing

viability of any of the gas pipeline projects in standing on their own two feet. That is, there is an enormous danger that the full cost of service of moving the gas from Alaska to the lower 48 is more than the gas is worth in the lower 48.

If there is a national decision that we ought to have a gas pipeline from---how do you cover the risk of that possibility? The financial market---that is, the bond houses and the insurance companies who are lending other people money are not going to be satisfied with a three-to-one probability the thing is financially viable, let alone only one-in-three possibility. So people are trying to come up with ways of providing that backstop. Now the pipeline companies essentially propose the consumers provide that backstopping simply by rolled in pricing, which means that the gas utilities use the fact that they have got a lot of gas that they hang on old long term contracts at regulated prices lower than the value of the gas to---they use that to subsidize the fact that Alaska gas will go into the market at more than it's worth, more than the consumers are willing to pay. You have rolled in pricing and you have the so-called all events tariff where the gas utilities, the buyers of the gas, will sign a contract saying we will pay for it, no matter how much it costs, and even if it is interrupted. We will pay the debt service on the pipeline. We will guarantee the debt service and will sock our consumers

for that debt service by adding it to the price of the other gas they get, you know, the gas that doesn't come from us.

Well, the notion of a state loan guarantee is just another attempt to find a gimmick to---or another backup for the fact that these things probably will not stand on their own feet economically. Now if there is a national decision to build a pipeline, there will be the national federal government finding some way of guaranteeing the financing. If consumer guarantees are not enough, there will be federal loan guarantees---and I really can't see Alaska coming up with a proposition that it wouldn't guarantee the bond of El Paso is going to have any effect on national decision. In fact, we may well be setting ourselves up to be sandbags on this if the commissioner of revenue comes back here and says that Secretary Blumenthal and Governor Brown and these people are going to support El Paso if we do it. And you rush it through the legislature in a special session before September 1st and the president makes his decision for Alcan on September 1st. Then they come back and say, well you lost your virginity, now we want you to do the same for the Alcan line.

The Treasury Department has been saying all along Alaska is the principal beneficiary of the pipeline. Alaska ought to be putting in the loan guarantees. Alaska ought to take the risks. And now they have got you. But what have you got? You've tied up a lot of Permanent Fund money at a public utility rate of return in a risky

investment that---I want to know on these loan guarantee programs the seniority of the state's guarantee; that is, if the pipeline can't pay, if it's revenue can't pay its debt obligation, who is it---is it Alaska that gets stuck first, or is it somebody else? If Alaska is going to be hit at the bottom of the list; that is, if somebody else is going to be hit first, it is not going to have much effect on the cost of financing the pipeline in its feasibility. If Alaska is going to be hit first, we have got a very expensive continued liability on the Permanent Fund.

GRUENING: I would like to just follow that up with--- do you intend to follow that question up? I just wanted--- before we got off---there has been a rumor around that there is some plan to suggest the Permanent Fund get into financing the gas pipeline. But assuming there are some business risks involved, does that---would that reflect on the reason there is a cause that the producers or the lessees of that gas had not come forward to finance a line?

TUSSING: I don't see any reason why a producer should want to finance it. They are not in the gas business, they are not financial intermediaries and the cost of capital--- is maybe 20% or 25% after taxes. That is their opportunity

cost. Now why should they acquire a contingent liability against capital that can be invested that way but limits what they can do with it. The most they can get from money invested in the gas pipeline system is the public utility rate of return. The cost of the capital to them is much greater. ARCO cannot go out and borrow money as a public utility at the kind of rate the public utility can. If the income is not guaranteed the---proposing to set up companies to guarantee the gas pipeline their revenue, have consumer guarantees, etc. ARCO and Exxon didn't have any guarantee of revenue. And so, from their point of view, I would regard it as an outrageous suggestion. They are not going to---of the notion before the Federal Power Commission that they are going to be that enormous beneficiary from the sale of the gas. Who knows what the price is going to be and whether it is going to be a great boom. It is very minor compared with the oil revenue. If the president adopts the FCC's proposed pricing scheme, that is to price the gas at Chicago on the basis of the price of No. 2 fuel oil, to set the price at \$2.25 in Chicago and subtract the cost of transportation from it, the oil companies really don't have a great interest in building that pipeline, or in helping build the pipeline.

MEEKINS: Yeah, but on the other hand, if they are concerned about, you know, increasing the wellhead and the state's case would

be similar, there might be---really don't know---there might be a motivation of an extra benefit that guarantees a substantial portion of the debt would reduce not only the interest cost but the---maybe the debt equity ratio and that might possibly, I understand, decrease the---it would lower the cost of service and increase the wealth.

TUSSING: Well, it might be, but the people who are advocating this approach are those who were saying a few months ago that the cost of service would categorically have no effect on a wellhead price. As I say, when the figures came out showing that El Paso would result from the highest cost of service, they said, well the cost of transportation has no effect on the wellhead price. Now you have the same people turning around and saying, well now let's commit our Permanent Fund money to lower the cost of service to El Paso and we will more than get it back in increased wellhead price. For the same people to make both of them is not credible.

MEEKINS: I agree.

GRUENING: OK, if we can get off the reality gap...

MEEKINS: I have another question. You were talking about the various economic growth of...

...and so the question is, when you are looking at it, did you come across anything that you felt could create, whether Permanent Fund or not, could create economic growth in the state that would be real economic growth in the sense that it doesn't necessarily increase population in the state but increases real economic activity...

TUSSING: Real economic activity increases population. The mechanism is you create jobs and people come in to fill the jobs. There are people coming to Alaska and leaving all the time. It is not a question of attracting people. What happens is the higher the unemployment rate here the more of them leave after... It is essentially the same question. Now, what industries you get may affect---and others---you know, they may have a higher average wage, but of course that will affect if they have a relatively high component of skilled and technical personnel and professionals they will attract and---the people who are qualified for those. No, I don't see how over the long run you can have a large effect on the---you can't create any real economic growth in Alaska unless you know, economic activities---the rest of the United States.

Oh, economic growth is proceeding in Alaska at a very rapid rate. Alaska economy is growing faster than that of any other state in the country. We are increasing in the sense we still have the same unemployment rate, or greater, and, you know, the people

after the pipeline---know what our average incomes show, but basically, we have got a bigger pie, but it is the same pie. And so what I am saying---you know, that is why I say, can you create real economic growth in the sense that people might be better off here, but it is still the same amount of people.

Well, what is better off, to reduce the seasonality? I think part of the extreme seasonality in the economy comes from the weather in the first place, but it happens because people like it. They want to go outside in the winter and they don't like to work construction in the winter. And things like that. It may be you can stabilize by spending the money on salaried state employees to work the year round in nice comfortable office buildings. That is one way of doing it. And you get...

GRUENING: Are there any other questions?

RODEY: You mentioned the Permanent Fund and financing those projects that normal private institutions won't finance. How can you avoid what Mr. Daniels called---that is Permanent Fund getting all that bad debt portfolio. There seems to be a consistent danger we are going to face as we develop some scheme for investing money.

TUSSING: If you look at the history of development bank

type institutions, of special lending funds in Alaska, look at EBA, FBA, BIA loan programs, etc. If you instruct the managements to make loans only to those ventures that can't get money otherwise, you are asking them to invest in those who are, by definition, high risk ones, and you are going to have a lot of bad loans and portfolios. That is the way it is going to be. If that is alright---if this is the way of spreading the money around, well fine. When the money first started coming in, the government purchased all the land in a city and then sold it back to the people at lower prices. That is the way of getting money into the---it was an urban development program. If you want to get the money into people's hands, that is one way of doing it. You get a lot of---projects that can't get financing when you got too much money. If you are going to give it away, well there are all sorts of ways to do that.

No, I don't think you are going to avoid that. I would like to see a real audit of loan quality in the existing state revolving loan program. And what the real subsidy is. When you take into account---when you classify these loans the way the banks are suppose to classify their loans and write off the ones that are really no good and write down the ones that are only partially collectable and then add the administrative costs, and say what have we got from the agricultural---for the small business loan. It frightens me to set up a multi-billion dollar---without taking a

hard look at what went wrong with the other loan programs. And taking a hard look at all these EDA projects, the EDA financing of industrial parks, the BIA industrial park projects and infra-structure projects that we were supposed to encourage in rural areas.

GRUENING: Hugh, did you have any questions?

MALONE: Thank you, Mr. Chairman. In the report that you prepared for the committee, in discussing the accumulation of surplus balances in the state general fund, it states that one way to make use of general fund balance would be to reduce the personal income tax. It says that the analysis showed a significant reduction in the general fund balance of a highly stimulative effect by the increase of disposable income increased demand, but it says that if additional revenues would be generated it would not be sufficient to maintain constant per capita at government expenditures. General fund balance would be depleted more rapidly than initial calculations indicated. It concludes by saying if the Permanent Fund is interpreted as a fund to benefit Alaskans the expansion generated by the income tax---I believe that would be the reduction of the income tax---could be the worst possible use of the general fund money. The question I have is---the next page at the

bottom there, discussed an idea that has been brought up from time to time, the transfer of payment directly to individuals. That would provide an economic increase in private---my question is, would the same considerations apply to that transfer distribution of monies to some form of Alaska, Inc., would apply to an income tax cuts. That is to say that you would generate additional revenues but you generate government costs that exceeded those additional revenues in that you might have a case where the expansion generated could be the worst possible use of general fund money and would you care to comment on that?

TUSSING: OK, as I said before, we can model the different impact tax deductions of Alaska, Inc., welfare payments, increases in state operating expenses, and there would be significant differences because they will be distributed differently throughout the population by income level and by region and some would have larger impact outside the state than others and it would be worthwhile to compare them. What we are saying here is all of these things do have impact and those that feed cash directly into the economy might well have more impact---or likely to have a greater effect on the management of state services than on the secondary ability to adapt to the time at which you couldn't maintain the services of the population you created. You may be asking---you said one of these uses may be worse, probably should say among the worst, from the point of view of stabilizing the growth. It could apply to the others as well.

GRUENING: Mr. Malone.

MALONE: Thank you, Mr. Chairman. Generally, one of the ideas was discussed when the various legislation creating Permanent Fund was under consideration. One of the ideas was that there would be some sort of buffer against the decline in state revenues with the dropoff in production of mineral resources. Does that make any sense to save money for a rainy day, or is that only a question of considerations. Can you put that into perspective?

TUSSING: Alright, you can model the situation. Assume that the demand for state services is going to remain constant in per capita dollars and you can add to say---increase 2% a year and you are aiming for a population growth rate of 2% or 5% a year, something like that. Then you can put it into your model and can see how much revenue is necessary. Then you can project how much your regular taxes would maintain the same structure of personal taxes in the state, the nuisance taxes, the gasoline tax, etc., how much that rate---and how much you are going to need from supplemental sources which would be either current mineral leasing revenues or Permanent Fund income. For every rate of contribution in the Permanent Fund you can show where the lines are going to cross, the point

at which the growth of the amount---the current revenue plus Permanent Fund income wouldn't be enough to sustain that level of service. Now for some amount of Permanent Fund contributions you may find that that point never comes. That the Permanent Fund may---and that you will always be able to maintain---well, your rate of increase in state services may be growing at 5% a year and the Permanent Fund's spendable income may be at 7% or something like that. It is entirely conceivable. But you would get that result only with very large early contributions, trying to minimize the budget growth---trying to keep growth in the next decade to a very low level.

If you spend 75% of the oil revenues every year, you are going to get to the point where the state's economy and the state government can no longer sustain the needs created and get to that point much faster. The model is very useful for that. The model did some preliminary projections on the basis of 25% contribution on the basis of various assumptions as to what happens to the general fund, but you can put together whatever assumptions you want. You can test various formulas for Permanent Fund contributions and come out with a theoretical golden path, where each year you assure that at least for 20 years, maybe for 30 or 50 years, there is always enough surplus revenue in the Permanent Fund to meet the requirements of the growth. But that can be accomplished only on the basis of an assumption as to what your goal is for population growth or growth of state gross income.

GRUENING: Are there any further questions of Dr. Tussing?

RADER: Doctor, in regard to the trans-Alaska gas pipeline, you are saying that if it is a viable economic project that money would be available to us at a public utility rate through normal public utility sources throughout the United States. It is possible that Alaska, in order to get in its royalty gas to tidewaters the trans-Alaska line would have an interest rate---would be justified in financing a line which would not be financable at a normal utility rate in order to have that option of 25 years of recall of our gas?

I have no idea of what the value of that option is. But I am only assuming, first of all, that you could establish going in, that the ability of Alaska to tax and the ability of Alaska to---the desirability of keeping that option of tidewater availability of oil and gas. Is there room for argument that we could participate in that situation in a project that a New York investor would not be interested in?

TUSSING: It depends how much it is worth to you to get to tidewater.

RADER: How do you think of that 25 year option with the gas pipeline? What do you think?

TUSSING: I don't think it is worth very much, myself. I think that we are going to have a lot of oil and gas explorations in the Gulf of Alaska or Cook Inlet, and there are presently uncommitted gas resources in Southern Alaska. If the state builds a spur from an Alaskan highway pipeline to Cook Inlet, for example, it is much more likely that the gas would go north on that spur than south. It is conceivable the cost situations may change sufficiently to make the Inlet area or Prince William Sound an inviting area for industrial development, based on the gas. No study has yet indicated that that is in the offing. There is no evidence for it and there is no serious argument anywhere that there is a petrochemical or major gas using industry waiting to be established because of the availability of gas at tidewater in southern Alaska. Any sacrifice the state makes now, either in gas revenue or in Permanent Fund earnings, speculating on what is going to happen five years from now, is that thing that happens 25 years from now has got to be awfully big at compound interest to justify the sacrifices made now.

The gas on the North Slope probably should not come to tidewater in southern Alaska. There is very likely to be a big surplus of gas in southcentral Alaska, the Gulf of Alaska, lower Cook Inlet, out the chain, etc. and it is going to be extremely difficult to market.

The trans-Alaskan gas pipeline is an idea, it is a vision, it's very little else in terms of the prospect for further development. It is a big payroll boom and that's why it is so attractive. Do we want another big payroll, big construction boom for the difference between the El Paso and Alcan in terms of the payroll. How much are we to pay?

How much is it worth to pay to get gas directly to Glennallen. Wouldn't it be a lot cheaper to give them the money to haul propane in for free, or something like that? I know how much it is worth but a lot of this discussion takes it completely out of economic reality. It has become a religious thing and I don't know how much it takes.

GRUENING: Now that we are into religion, can we get back to Permanent Fund? Do you have any other questions?

RADER: I have a couple of others, if I could, Mr. Chairman. During the discussion of Permanent Fund, it has been brought up from time to time that Permanent Funds can be used as a vehicle. You touched on this during your discussion and I apologize for not having read your paper. I assure you I will. It has been suggested that the Permanent Fund be used as a vehicle to handle the transition of Alaska non-renewable resources to renewable resources and I assume inherent to that would be that we would take the Permanent Fund and use it to

subsidize what would apparently be non-economic agricultural products or fishing ventures perhaps on the Continental Shelf and the 200 mile limit or something else, I don't know. To use---I don't know really---I am not one of those who made that argument. It was made that this fund could be used as a vehicle to get us from a non-recurring resource revenue to a recurring resource revenue. Do you really see that?

TUSSING: How long are we going to subsidize them and compare the cost of continuing subsidy to just how much income you could bring in by investing that money at the highest rate of return and using it to sustain normal state activity. I am no more sure than you are what the people who talk about this mean. I would like to see what kind of venture and what kind of subsidy is involved. Suppose the Permanent Fund contributes free half the money to establish a processing plant for bottom fish. Over long term the operating cost---or the revenue to cover the operating cost and the depreciation---are you going to just keep feeding in money from somewhere to keep that project going if it's not otherwise viable, and if you have to do that what do you want it for? Does this make the state's economy any less precarious than it was based mostly on oil? I don't quite understand the argument myself.

RADER: I don't either. I thought maybe...

TUSSING: Let me say, I have faith in the ability of the fish processing industry and of Alaska-based fisheries to grow and make enormous investment in the next two or three years or in the next five or ten years, and there is virtually nothing that can stop this aside from state and federal regulatory policy, but the pace and shape of that development is not going to be determined by the cost or availability of venture capital. That will be there if the projects can show that they are worthwhile. There may even be too much because there are a lot of Japanese and Korean companies who are writing down and writing off their previous investments in processing plants back home and who will want to get involved at almost a non-economic basis in Alaska industries and may want to get a foothold now and will invest at less than, you know, it thinks a prudent investor might hesitate at. That is true, we have another source of capital in the native corporations who have been doing that, too.

RADER: A different line of inquiry. Have you given any thought as to the governmental structure that you would recommend? You and I are both aware to some degree at least of our past, in the way we handled the past lending activities and whether they have been economic. I am like you. I have some question about the management ability of some of our agencies. Have you given any thought as to how the fund should be structured

for an executive and legislative oversight but with a view towards insulation from legislative pressures and public pressures, etc.?

TUSSING: Not enough to spend time on my prejudices.

RADER: That concludes my question.

GRUENING: Thank you, Senator Rader. Are there any further questions of the committee? Representative Meekins.

MEEKINS: Dr. Tussing, you were talking about providing some loans for small and medium enterprises in the rural area and that private institutions don't provide the capital needs there. Is it your view that in order to do that that we would have to set up regional development banks or some sort of development banks and that that wouldn't be possible or preferable to work through the financial institutions?

TUSSING: Well, I think most investments in Alaska should be done with or through or in partnership with existing financial institutions. I haven't given a great deal of thought to how this would be structured, but I would see the regional development banks being formed in some sort of cooperation between the Permanent Fund and existing financial institutions and the regional corporations. For example, they might joint venture, which would be utilizing the services and get money from the existing financial institutions. Might guarantee them and sell bonds---have a correspondent relationship---there is just many ways of doing it and I simply haven't devoted a lot of thought to its structure. It will be a

difficult problem. It is not an easy thing to work out.

GRUENING: On that line, Mr. Belden Daniels, who is our next witness, will give a little more thought to that. Are there any further questions from the committee? I want to thank you very much for a very thought provoking presentation. Thank you. I would like to call our next witness because I would like to wrap most of this up today. I think he is in the audience. Mr. Belden Daniels from Harvard University has submitted a very, I think very, comprehensive report and I would like to hear your initial comments, Belden. You have a resume here that looks pretty impressive. I know you are pretty modest and maybe you could summarize it for us.

DANIELS: Thank you, Clark. I am a lawyer, a former international banker. I teach development finance at Harvard and I am actively involved in putting development banks together in a number of places in Asia, Europe and in the United States. That provides me with a very good point of departure because I suppose that in the last 18 years of working in development banking and in the last 13 years or so in working specifically with regional and community economic development problems that I have read several hundred development banking acts and draft bills and I participated in drafting and having passed and funded a dozen or so myself.

I begin with a very strong feeling of genuine excitement about the quality of work which the State Investment Advisory Committee has already invested in this issue and which the consultants for the state, Price Waterhouse, White Weld and Bob Richards here in Alaska, have contributed. It is much easier for someone in my position to offer refinements and additions and clarifications on a draft which I think is essentially very sound. I am speaking specifically about House Bill 298 and I think somewhat improved version of that House Bill 300, which are the two that I have looked at in some detail.

I have about eight points, if I could kind of quickly go down them and make them fast, and then open it up to your discussion as much as possible. I guess I want to say one or two more preliminary things. I confess to being somewhat overwhelmed by both the potential size and scope of the Permanent Fund and also by the size and nature of the Alaskan economy in relation to your population base and I feel very cautious about wanting to be too quick in making judgments about the relevance of my own experience in many other parts of the world because, as Arlon Tussing has point out, you are faced with an absolutely unique situation. There are really no comparable situations in my experience in either Asia or Europe or in the United States which combine the particular concentration of extraordinary resources, capital and natural, in such a vast area with such a limited population. So I would like

to reserve the ability to be somewhat tentative in---as an outsider in offering too much advice and council about how you should proceed here.

I do think that there are at least three major areas in which that experience is relevant to you and useful to you; that is, the world wide experience is relevant and useful to you, without presuming what your goals are. And they get, Senator Rader, to some of your questions.

One, I think there is a way that you can look at your problems or your opportunities---a great deal of learning with regard to structure that is worth your careful consideration and I am mindful that having read all of the minutes of the Advisory Committee and the reports of your previous consultants, that through Price Waterhouse and White Weld you have had a rather thorough consideration of lots of that international development banking experience.

In the third area that I would offer some comment on, related to Representative Meekins' question, is the specific applicability of regional and community development experience to some of the structural problems that you are facing. The title of my paper I believe in very strongly and that is that I would urge caution on all of you in several levels. One I think, it is very important for all of us to recognize the very real limit on the capacity of any state government to influence profoundly the course and direction of economic

development within its boundaries and this is one of the areas which Arlon and I certainly share---one of the many areas in which we share a common kind of sense of caution.

Secondly, I think that all of us need to be extremely cautious in anticipating too much impact on the economic development of the state from the Permanent Fund. And, in my eight points that I would like to make, Clark, I think I can bring out the specifics of that in, I hope, at least quick conference. The punchline, of course, in suggesting this caution with regard to the role of the state in economic development and the role of Permanent Fund in economic development is that you have the opportunity of enormous scale, either to waste these tremendous capital resources that you have or to husband them very carefully, both in terms of the maintaining the value of the capital itself and invest in ways which will at least marginally contribute to the overall economic development of the state.

Point One: No development bank, no financial intermediary, can create any economic activity that isn't there in the first place. Development banks and any financial intermediary operate only on the supply side of the economic equation. If there is real economic activity for which there is not available capital, then the intervention of the Permanent Fund can affect that positively and can add economic value to the state. But if there isn't a market, if there aren't sufficient---if the costs of production are too high, the intervention of the Permanent Fund is not going to

affect that at all. Specifically, it is my understanding that at the present time petrochemical industries is not viable on a world-wide basis. The cost of production of petrochemicals in Alaska are too high to be competitive on the world-wide market. Now that may change and then maybe things that will lower those real economic costs. But there is nothing that the Permanent Fund can do to intervene in order to lower the costs sufficiently to compete in the world-wide market. Now that is very, very important, I think, in terms of lots of thinking about the Permanent Fund.

That means, for instance, in terms of Point Number Two, that subsidies are not the issue. We have a very interesting case in point in Massachusetts right now where we have very rapidly growing, high technology companies, between \$50 and \$100 million in sales, that are between 20% and 40% profitable and growing, and growing at the rate of 20% to 40% a year, which have a great deal of difficulty accepting capital in either equity or debt form for their needs. But these companies could be financed on Master Charge, and I think that that is a critical idea. In fact, there may be circumstances where you want to increase the price of capital in the Permanent Fund because it discourages non-economic activity and you want to discourage all of the dogs that will be attracted to the Permanent Fund if there is subsidy available. The issue is the availability of capital.

Point Number Three. The general fund is far more important--- and I am saying this in emphasis to Arlon's point---the general fund is far more important in terms of its impact on the overall economic development of the state than the Permanent Fund. I devote time to this in my paper, and I don't want to repeat any of that now, but the issue of expenditure policy, tax policy and regulatory policy will more profoundly affect economic development than the Permanent Fund. But the key punchline in Point Number Three is that you have got to operate your expenditure policy, your tax policy, your regulatory policy, and the use of the capital resources of the Permanent Fund as part of a coherent economic development effort in the state. If you don't the opportunities for sound investment on the part of the Permanent Fund will be less, the jeopardy of Permanent Fund investments in the state will be greater, and the likelihood of your general expenditure policy through the general fund and your investment policy operating against each other, I think, are very great. I suggest that there is extraordinary opportunity right now for the State of Alaska to think about a coherent overall economic development approach that recognizes the limits of all of its policies, individually and collectively, to affect the economic development of the state, but still is operated in combination, will have a much greater impact than operated separately. Just a simple illustration.. A couple of the issues that I have had the pleasure of talking about the last couple of days is from some of the native corporation areas

and with---in specific projects, one in the Aleutians, one in the Kotzebue area. You can't begin to talk about a significant fisheries project that is going to be sound unless you get the concrete in there for the pier first. And so, obviously, the infrastructure decision made through general fund investments has got to be made side-by-side with the Permanent Fund.

Point Number Four. The private market needs to be used first in terms of solving both market and capital issues within the state, and all of your planning and development in terms of any financial intermediary specifically that might be set up within it have got to be planned in collaboration with the private market and implemented in collaboration with them. This is essential if you are to husband your resources properly, both in terms of lowering the risk in which state funds are invested, and also lowering the cost. And I would suggest that ---and I will cite some specifics before we finish---that there are lots of opportunities for that kind of collaboration which are mutually attractive to the market sites, to the population of Alaska, and to the state government. And therefore, specifically, in the case of regional development banking subsidiaries of the Permanent Fund to deal with some of the problems of capital availability in the regions, I strongly support Arlon's position that they should be a collaboration between the native corporations, between the private market

place, and between the Permanent Fund. I will give a few specific cases in a moment. Without knowing in great detail the operations of the present revolving loan funds, what little I know confirms the experience in many other states and many other places that those funds which are in collaboration with the marketplace have a portfolio which is not only financially of better quality but in terms of the economic impact has a greater impact within the state.

Point Number Five. What are the potential areas for use of the Permanent Fund and how might the Permanent Fund be organized in order to deal with them? I think there are four that deserve very careful consideration by you and I will try to highlight those points which are either extending on a point that Arlon has made or in addition to them. First of all, in terms of large scale economic activity in the state, the very efficiency and consolidation which is taking place in money and capital markets on a worldwide basis means that there is capital available for those large enterprises and I think you should ask very carefully what the market imperfection is, either in terms of the private market or financial market, which would lead you to be asked to undertake either an equity investment in or a debt loan to or specifically a debt guarantee of a large activity which you should presume can be handled by the marketplace. Now, I would like to introduce another issue with regard to large scale enterprise. At the present

time large scale enterprises in Alaska are primarily being developed by resources from outside Alaska and you may want to ask yourself the question whether or not there is a reason to intervene in order not to change the underlying economic viability of the project, which is presumed to be sound, but to change the ownership, both in terms of who is bearing the risk and who is bearing the reward for that particular large scale undertaking. I am going to suggest a number of points a couple of models around the world which your---which the previous consultants of the state were not asked to look at because they were asked to look primarily at international development banking experience. There is very close to you a model that deserves your careful consideration in terms of this issue of shifting ownership for very large scale enterprises and it is the Canada Development Corporation.

Canada Development Corporation was created in 1971, I might note after a 10 year debate. I don't mean to suggest that this process may go on for a while, but I am fascinated that it did take 10 years to do it in Canada. It was created with an initial public investment by the federal government of Canada of a quarter of a billion dollars. Three years later it was able to have the largest public offering in the history of Canada, \$150 million public offering, primarily by small individuals in Canada, primarily because of the soundness of the investments which it had made. It now has total assets in

less than a 6 year period of over a billion dollars and is producing a significant return on investments and has repurchased a number of rather large corporations which were originally under foreign ownership, primarily American ownership. Now, it is a mixed success, depending on the standards that one uses. But it is one alternative form of use of the Permanent Fund in which you would be operating on a market basis but with a somewhat different public purpose.

Second, in terms of uses. There are on a world-wide basis--- there are problems of the availability of intermediate long term capital for small and medium size businesses generally and particularly in remote areas. Now it is very important to note that this is not an Alaskan problem. This is a world-wide problem. And the question then that you have to ask yourself is whether or not you have an economy that is in some way particularly dependent on those kinds of enterprises for economic growth and therefore there is warranted on the part of you and the Permanent Fund some intervention. In Massachusetts, for instance, we are a particularly dependent economy on small and medium size businesses. We are also particularly dependent on the creation of new high value added and high technology companies, which, as I mentioned earlier, have difficulty of access to the capital market. Therefore, we have created a series of new development banks in Massachusetts, two wholly privately owned and several that have a mixed and private capital in order to deal

with that problem. Very critical point. That activity must be undertaken, planned and implemented in collaboration with your existing commercial banks and thrift institutions both federally and state chartered in order to create a mode of investment that is sound, from a risk standpoint, spreads the cost and builds those institutions more deeply into the economy on a sounder basis.

There are a number of models that warrant your careful consideration. One, again, is the Connecticut Development Authority, which in my judgment is the soundest of the intermediate and longer term joint ventures between public capital and private capital. Every European nation, every Canadian province, almost every state in the lower 48, has this kind of intermediary. This one just happens to be the best of them. OK. Third. There is a particular problem that deserves your attention in terms of support for regional and small community economic development and I would say on the basis of my experience in Appalacia, my experience in New England, and my experience with regional economic development efforts in Europe, that without knowing precisely the nature of your own economic situation in the---outside of the major cities, that this is a very serious problem, as Arlon has already noted, and that---but I think the extraordinary thing is you have a resource that does not exist in any other state, and that is the existence of the native corporations.

What I think is worth your serious consideration is the regionalization of parts of the Permanent Fund to deal on a joint venture basis with the native corporations. And I would like to note that this is the one case in which I think, underlined many, many times, that there may well be a sound economic and financial reason for the Permanent Fund to take a significantly lower rate of return, and that is this: The native corporations have a very high need to produce at the highest rate of return at the lowest risk on a worldwide basis as they can in order to husband their own resources and protect their stockholders. They are therefore naturally looking to investment opportunities in the Anchorage area, Fairbanks area and outside the state, as they should, I think---because of their opportunity costs. I think that they are essential to the sound investment in their region. It is not sound for them to have all of their economic eggs in their local basket, or even in the basket of Alaska as a whole, but that development will only take place if in fact the Permanent Fund is willing to compensate for their opportunity costs. This will require much more careful consideration and analysis, but I think in principle the idea is sound. I just, in fact, had the opportunity to sit down and talk in more specific terms about a specific project in Kotzebue where I think this is true. The project will be financed but it may well not be financed as soundly as is good for the project in order to have the shopping mall to get started in Kotzebue.

Once again, there are very good models for your consideration, some new and some old, in terms of this kind of collaboration. One set that deserves your further attention is the British Columbia Central Credit Union, which has had an enormous impact on regional and small scale community development in an economy which I would presume is not radically different from the Alaskan economy in terms of its overall construction, political dimension and demographic dimension and underlying economy. Related to that is an extraordinary institution in Germany called the DG Bank, known as the largest bank in the world, starting from small scale community development, now investment opportunities on a worldwide basis. A new institution in Massachusetts not yet operational but I think conceptionally very sound, the Community Development Finance Corporation is an institution that I think deserves consideration by you in the planning. I might note a small kind of example of refinement I would suggest for consideration in HB300, and I know this---I think it is a mistake in the community development of units of the Permanent Fund to limit the form of investment to only debt and debt guarantee. I think equity is essential for community and regional economic development and the Permanent Fund should have the opportunity of making those kinds of equity investments on a joint venture basis in a minority position with the native corporations in the kind of case that Leo and I just had an opportunity to talk about.

Fourth and finally, in terms of uses of infrastructure investments. Be wary, be cautious. There is an enormous body of experience on a worldwide basis of public investments made in anticipation of private market investments following and those public investments are lying in the fields. Now, where there is the opportunity for a market investment like a fishery, like a fish processing plant and in the Aleutians, but an infrastructure investment needs to be made first, then we have---in order to realize the private investment---then there is a very great need for collaboration between general fund infrastructure investments and Permanent Fund income producing investments.

Point Six. Without having access to either private market projections for the economy or the university's projection, or the government's projection, under no circumstances in my judgment will there be the capabilities for absorbing substantial amounts of Permanent Fund resources in any of the above four categories over the foreseeable future. And it is interesting that I arrived at the need to make private market investments, not from the standpoint of security, not from the standpoint of evening out the long term ups and downs in the cycle of state government revenue, but from the standpoint of development banking. And I very much support the language of 298 and 300, which say no less than 40% in terms of investment grade security and---but no more than 30% in community development, or no more than 30% in productive private enterprise

Now, Point Seven I have already covered and that is good. There are other models in addition to the ones which you asked the original consultants to look at that are worthy of your consideration. There is no need for any kind of activity that you might undertake with the Permanent Fund to reinvent the wheel. Somebody has been there first and made plenty of mistakes and finally of all there were times creative models ---models are available for your use and should be used.

Eight. Looking at the structure of the development bank and is proposed in 298 and 300. A general proposition first, very important. Some members of the committee, I think, will be a little sick of hearing me stress this. There is one great strength in a development bank and one great weakness. The great art in design is to maximize that strength and minimize the weakness. The strength is that it is the most efficient mechanism for making a public capital investment that is sensitive to market conditions in order to contribute to economic development. It beats setting up a bureaucratically administered fund in terms of both equity and efficiency by a very long distance, and it beats tax expenditures and tax incentive by a very long distance, which are the two other principal forms of public investment. But the price that is paid is the price of accountability to a public purpose, both to the executive and to the legislature. There is a history of development banks

being lost from public control. Now, I want to re-emphasize that I think the basic plan of 298 and 300 is very sound. I think that in terms of both counsel and the decisions of the investment advisory committee and the drafts that have come from the executive and legislature are essentially sound in detail, as well as concept. There are 30 or 40 pages in my paper that literally go through the draft line by line, comment on them, the meanings of the phrases and any more detailed technical issues that I think deserve some consideration.

What I think deserves your consideration is how to insure that the resources of the Permanent Fund are planned and implemented in conjunction with the general fund for purposes of economic development, not for purposes of market security investments, investments for purposes of economic development, that insure that the planning is consistent, but that the investment decision-making of the Permanent Fund is in no way compromised. The whole idea of creating the Permanent Fund is in fact to remove---one of the major ideas as I understand it---is to remove revenue from the expenditures of state government. And if you think it is done in Alaska, you should see it in Massachusetts. The expenditures always rise to meet revenue whether you need them or not.

Forcing an investment pace which is not there is another problem. I have lived through disastrous efforts of the federal government in the '50s to try and jam money into ghettos at a rate that could not be absorbed. If you want to see economy in people's lives

destroyed, that is a good way to do it. So the issue here is to make sure that not only is this avoided but that the investment pace---that the legislature and executive do not insist on an investment pace which will create unwise investments that will only come back to be of much greater problems in the end. Now, I am going to take advantage of the fact that I am an outsider, unfamiliar with the custom and history of executive and legislative arrangement in Alaska and not propose a specific solution to that problem. I think my function in that case is better served by reacting as counsel to ones that fit the genius of the Alaskan situation, based on the experience in many other settings outside of Alaska. But I guess my summary feeling is that there is a---that a very fine start has been made through the drafting of 298 and 300, through the kinds of sensitivities I have been hearing from private market people, people in the executive and legislature, people in native corporations over the last couple of days. And the issue is to build on that excellent start in a process which continues to collaboratively involve the private market, the executive, the legislature and the users of---services in the further refinement and in the implementation of the plan.

GRUENING: Thank you, Dr. Daniels. Are there any questions from the committee? I have one, if no one else does, to

start with. Earlier, Arlon testified he saw the range of possible investments in the magnitude of \$40 or \$50 million range and you are aware, Dr. Daniels, of course, that the two bills that you mentioned---298 and 300---set aside 40% of the incoming Permanent Fund revenue to kind of savings, which wouldn't be used for that kind of investment in the state development banking and investment in the state. Given the fact that its magnitude is somewhat smaller than you might have guessed earlier, would you suggest that that percentage in investments---let's say not a development banking type in the state---be larger. In other words, that 40% ought to be raised?

DANIELS: Well, I would have several observations. One, if I understand Arlon correctly and understand the paper where he talks about this in somewhat detail, that's a hunch on his part subject to more careful econometric modeling on the part of the university, further grants that might be made by administration for consultant assistance in that regard. I think that one of the tasks that is before the committee is to take a very careful look at kinds of projects like the ones that Representative Schaeffer and I were talking about earlier, in order to see totally what is out there. You also do need to do some very careful modeling and you need some computing models so you get some different judgments because, as you know, you are still very much in the dark as to how to use some of

these econometric models. So that needs to be done before anybody can start making some more rigorous hunches.

Two. Having been through this for 18 years, and having just been through it in Massachusetts with six new development banks, in the end no way to know until you get out there. Because you are operating on the supply side, you take your best anecdotal information and you take the best econometric information, and on the basis of that you make a judgment. Then you create a mechanism which will grow according to real demand being out there. I want to give you an example. Massachusetts has probably the best housing development agency in the country---probably the world---in terms of the state housing finance agent. When that institution was first created in 1968---that is a very short time ago---that institution was created with an initial \$50 million. That institution less than ten years later is a \$2 billion institution because the demand was out there and it grew to meet the demand. The initial ceiling was set and the demand appeared to be greater than initially anticipated. The control was a ceiling of indebtedness which it could incur and the legislature consistently raised the ceiling as the demand was demonstrated.

GRUENING: Do you see a possible parallel in initially setting the ceiling for the development corporation that we

may establish in either 298 or 300 below that that would come into the Permanent Fund from the 25% mandatory contribution?

DANIELS: Well, I would make one other observation. You already have a ceiling.

GRUENING: Well, no. You have one in the constitution. You have another one from a draft standpoint. You already have a ceiling in 298 and 300.

DANIELS: That's right. A ceiling on two categories of presumably higher risk investments in which all of the balance must go into investment securities. I think I want to be cautious at this point in suggesting that it is possible that the legislature could set lower ceilings and then subject to proven demand to raise them. I think I would want to suggest that this is a possibility which others have tried worthy of your consideration. I don't think I want to make a judgment at this early stage in the game if that is precisely the rule that they follow. I would like to note, however though, that with regard to investment grade security, it is my understanding in reading the legislative history and reading the minutes of the committee, in reading the work that has been done today, that the intention is to invest in the full range of marketable securities that are available in order to maximize return at a prudent level of risk, and that what is at issue here is a

form of investment that is considerably beyond characteristic short term secured placement of debt on the part of the state with idle cash flow. I also think it is important to realize that the Permanent Fund is not only potentially one of the largest development banks in the world, it will be a very large investment bank by world-wide standards operating on a world-wide basis in terms of this portfolio investment and has got to have the most able management that money can buy. One of the reasons again, from an efficiency standpoint, that independence for investment decisions has got to be protected.

GRUENING: Questions?

MEEKINS: You have down in your paper and re-emphasized today it isn't enough for the Permanent Fund to plan what we would like to do with the Permanent Fund, but it must be coordinated with the expenditures of the general fund for a number of reasons and that brings up a question related to that, that the planning course in order to do any kind of planning or thinking needs to have information and judgment about what's going to happen in the future or what is happening. You have to take inventory of the current situation. It seems to me that---I have been thinking about that after reading your paper and others that one of the benefits of the Permanent

Fund, even though the major impact is going to be what we do with the general fund, one of the real benefits of the Permanent Fund provides a kind of catalyst or reason to get organized and that is what we are doing now. I am wondering how you feel---what kind of--- if you thought about what kind of things we need to do in order to start gathering information. I know that is necessary, but I can't really perceive what steps we take in order to have information that we can make decisions upon.

DANIELS: I really appreciate that question because it gives me an opportunity to say that we have this unfortunate tendency in the United States to think that planning somehow is useless in America---and yet what I would like you to do, and I think you precisely hit the nail on the head. The Permanene Fund creates an opportunity to begin to think about Alaska as a public enterprise, and what I am suggesting for you is simply that you begin to adopt as a state the same standards of planning that any multi-national corporation takes for granted as a mechanism for marshalling and husbanding your assets in order to produce larger return on those assets.

I do think that there is a way of thinking about the general fund and the Permanent Fund, in which the Permanent Fund is really the retained earnings of the people of Alaska. There is the difference on an annual basis between your revenue and your expenditures. Now, most states live by the hand-to-mouth business where they spend

every penny of today's expenditures to meet whatever revenue they have in hand without any thought toward investing those resources in order to create a sounder longer term public enterprise. I never thought about that idea before until I had put before me the kind of awesomeness of the Permanent Fund itself.

The issue every year is to expend and invest on a current and long term basis the expenditure of the state as a whole in order to, number one, produce a higher annual net earning which will go into the Permanent Fund, and in order to produce an increasing growing revenue base. Now, without going into all the details of it, I think we do need five year planning, or if that is too dangerous a phrase, pick three or seven, and that you need to begin to project both for the general fund and for the Permanent Fund expected revenue, levels and qualities of expenditures.

I do want to make one disagreement which I will illustrate in a moment. In order to be sure that you are husbanding all of those resources and maximizing them, you are going to make mistakes. You know, we do create Edsels in this world. And--- but you aren't going to make as many as you will if you just go willy-nilly. Now, I do want to make one, I think, distinction---and I don't know whether Arlon is still here to respond. Well, I want him to. I will get him in a bar or something afterwards, but we are unfortunately still living in the

never-never land of dear Keynes who told us that every public expenditure was a good as every other public expenditure and it ain't true and all you have to do is look at England and Massachusetts as two terrible cases in point if you want to see that it is not true. The Permanent Fund must also require that you increase the quality and productivity of your general fund expenditures so that they are made only in terms of the increase of return that they are going to produce. I further suggest in the paper that you must begin to project, not only the financial soundness of Permanent Fund investments, but the economic impact of them, and then as part of this planning process you must measure--you must audit the economic impact as well as the financial impact to determine whether or not those investors did in fact live up to their economic projections, as well as their financial projections. That is part of the planning process, too. In that regard I think 300 is better than 298 in one specific where 300 requires that annually the executive and the Permanent Fund management account to the legislature for what has been invested and report in terms of what future plans are.

RODEY: Let me shorten Russ's question down a bit. What is the best measure of the amount of additional capital that our economy can absorb and where do we go in the parameters of the desirable amount of capital?

DANIELS: That question is a little different than I thought. I can't give you the answer you want. The measures that you want are the specific fiscal measures of return to the state. If you make an investment of state capital, if the state takes some of its revenue and invests them in the Permanent Fund, then the returns for the state is not only the return to the Permanent Fund itself of the soundness of that investment, but the returns in tax dollars to the state itself. We are now putting on the new development banks in Massachusetts a two track accounting. One that accounts for the financial soundness of the enterprise and one that accounts for the reduction in social overhead costs and the increase in tax revenues created.

Now, we are very much at an early stage, all of us in the world, in being sharp in that kind of analysis and projection, and even the cost benefit analysis of the World Bank, the InterAmerican Development Bank, don't apply because for better or worse the State of Alaska does not have its own currency and does not---and so you cannot be as rigorous in the attribution of the economic benefits based on your investments. We have to factor that down. The process is two points. One, I can't say what the quantitative answer is, but I can say that it is the use of some of these techniques of measurement that are crude at this point, but I think over the next

ten years are going to become much more refined and you should be a part of that refining process.

Obviously, as public trustees, what we would like to do and must do is to draw a curve and we want to know the point at which the capital going into market can't be absorbed in an acceptable manner, whatever the acceptable manner is.

That starts by not subsidizing. That starts by the fact that those investments that are going to be made are going to be made in terms of a market return and that it's only in terms of infrastructure investments where the subsidy already, according to 298 and 300, is borne by the general fund and not by the Permanent Fund. It's really a capital subsidy and a proper one because the external benefits again returns to the state. And possibly with the one exception---the one that I introduced---the possibility of differential costs for joint ventures with the native corporations for essentially sound projects in order to correct for their opportunity costs, which rightly encourages them to invest outside of the region, not inside. Are we together or not?

RODEY: One last point. Are there a number of models we can look to for the limited purpose of development banking in determining what capital or proper capital absorption is in a market?

DANIELS: Well, analysis as I understand it right now is being proposed to be done with the executive---with consultant

help, using models which they already have available to them. I think that is absolutely essential to your purpose. I think that should then be corroborated by anecdotal evidence that you gather and I think it further then should be tested by putting a series of assumptions into the several models that are available to you. I was out of the room when Arlon was referring to the man in the arctic model, but I am aware of it and it seems to me that it is a tool, that is---you want to take the analysis that is done by the treasury and perhaps there is some other data that is now available and I am not yet aware of, and then you want to begin to make some assumptions in terms of investment modes through your econometric models and begin to see.

GRUENING: Representative Miles had a question.

MILES: Thank you, Mr. Chairman. Dr. Daniels, I missed a point that you made early in your presentatiao when you were speaking of the potential areas of use of the Permanent Fund in the regional small community development entities. We have been hearing quite a bit this afternoon about no subsidization and if it is an economically advisable program private capital will generally come in and take care of the project. But you indicated, and I didn't follow from Point A

to Point B that in the small community or regional development area we could take a lower rate of return. Can you tie those back in?

DANIELS: Yeah, the issue is something we call opportunity. First of all, I want to make one thing very clear, that any pre-eminence that we have in the money and capital markets today on a world-wide basis are precisely because of the increase in efficiency of that market and its consolidation of resources and the problem that is developing is that there are left behind lots of relatively small undertakings. Now some of these you have got to realize can get very big. We literally do have companies in the \$100 to \$150 million range in Massachusetts that cannot at the present time, because of the structure of the marketplace, get adequate equity and long term debts. Those are pretty good sized.

What happens is---is that the opportunity for substantial return at a lower risk are available to these increasingly large financial intermediaries on a world-wide basis that do not make it worth their while to take the lower return through increased cost and possibly through increased risk. The issue here---and I don't want to get too technical---the issue is to create mechanism in collaboration with the private financial intermediaries which reduce information costs and which reduce transaction costs. I give you specific case in point. John Hancock Life Insurance Company

today invests \$1 billion a year. Twenty-two people do that. It is not worth John Hancock's while to consider any investment smaller than about \$20 million in a firm that is smaller than about \$100 million. The cost of an office and the attendant risk, even though these are otherwise sound investments, just don't warrant giving the opportunity for placing their funds.

MILES: So they wipe out everything...

DANIELS: That's right.

MILES: ...under \$100 million...

DANIELS: Absolutely.

MILES: They don't even...

DANIELS: Won't look at it. John Hancock last year made one investment in one company below \$100 million. Now, the same is true of the native corporations. Their task is to maximize their return and their opportunity for doing that are greater outside of the region than inside the region. Now because of the enormous public benefit to reducing welfare

costs and reducing unemployment insurance costs---public benefits, forget it, state benefits --- right to the treasury of the state to lower these annual expenditures and to increase tax returns. I am saying, I feel on a hunch, that there are lots of opportunities for collaboration with the native corporations in which the return to the state, a fiscal return to the state, in specific dollar benefits warrant a reduction in return through the Permanent Fund and in collaboration with the native corporations. Now further with your own commercial banks and savings banks there are also mechanisms for making---for dealing with their opportunity costs in terms of extending the terms of financing, in terms of reducing their costs.

I will give you a case in point. We had an analysis in Massachusetts of our fishing fleet in light of the 200 mile limit. In fact, we just considered what are all the issues that we need to undertake in terms of a comprehensive approach on the---with regard to the state to try and see that Massachusetts which has a situation very similar to yours is able to really take advantage of the 200 mile limit. We found that the average life of fishing vessels in Massachusetts is 29 years and 7 months. We further found---you can imagine that there is some real dillies out there. On the other hand, we found that the commercial banks and even the thrift institutions were not making loans beyond ten years. They were doing that for sound reasons. The issue is for us to come up with an

insurance program operated through a development bank so that it is operated on a sound basis which will make it attractive for those banks to extend their term and also make it possible for them to lower their equity requirements from 25% to 10% in order to make it more possible for fishermen to be able to buy their boats and not, you know, be so totally depending on piling stuff up on the---until they could actually go out and get one. Now the point I want to make is that in every instance John Hancock is acting reasonably, your local commercial and savings banks in Anchorage or Fairbanks are acting reasonably, the native corporation is acting reasonably. You also can act reasonably in terms of your return on investment to the state by working in collaboration with them to create a joint venture situation that benefits you both.

GRUENING: Further questions of Dr. Daniels?

MEEKINS: Thank you, Mr. Chairman. In regard to infrastructure investment, it seems to me that some of those--- it goes back to the idea in my mind of fighting with the general fund. It seems to me that a lot or at least some infrastructure investments, the ones that come to my mind, would likely be good candidates for direct appropriation from the general fund, those that have anything to do with

transportation costs being lowered or dock facilities or something like that. And it would seem then that you would---in some cases it would be better to take money out of the Permanent Fund and invest it in those things and then take the general fund money for the return or just a direct appropriation of the general fund, or would it make any difference?

DANIELS: OK, well, we Americans do some other funny things, and one of the things that we do is we finance long term physical assets---50% of all long term physical assets are financed on a current account basis by government. You don't know, if one were a business one would never think of doing something like that. The point of using the Permanent Fund with regard to infrastructure financing is to take an actuarial view of long term physical assets and say that it is not necessary to pay for 100% of the cost of a dock facility or an airport or a road in year one, if in fact the useful life of that investment is going to be spread out over a period of time, the economic benefit, the tax benefit coming from it, etc. Not only is the cost going to be emphasized over a life, but the returns on the investment are going to appreciate to the state over the term of life. Now what I am suggesting is that I intuitively trust a development bank to make a sound assessment of the cost of that physical asset, you know to control the cost of building the airport and to police the maintenance of it. It is just a different way of thinking, different way of operating,

and you will create a more efficient asset that will be better maintained if the management of that financing--- and it will be financed on a more sound basis if the management of that has gone through the Permanent Fund.

Now what I am saying is that if there is any cost difference between the realistic return on the investment, if in fact it is something that is totally external like a road, and you don't want to put toll bridges up, or for instance you do want to assess part of the cost of that---maybe you do want to assess to the fishing venture part of the cost of that user charge for making the public investment to the extent that there is a return on the investment that is insurance, then that comes back to the Permanent Fund to the extent that it costs \$2 million and you are only going to get an internal return over 15 years of \$1.3, then the general fund has to pick up the difference of \$700,000, but I suggest that is more efficient than the general fund automatically going out and appropriating a million dollars in a rich year for a project which, because you are not paying attention to it, ends up costing \$3 million, which then is not going to be adequately maintained because nobody is minding the store.

MEEKINS: What about a case of an infrastructure investment that has completely external rate of return? For instance,

a road where you have one particular group of people, but you don't want to charge a toll because it limits the amount of use and therefore theoretically the total benefit to the public is reduced because some people won't use it if it has that cost. If that is the case you won't have any revenue produced from it. Or very, very little. When you think of efficiency in doing the Permanent Fund, would you think that the total return should be taken up by the general fund or...

DANIELS: Yeah, but you might finance it on a---I mean the Permanent Fund must---I was about to say, you know, hopefully---the Permanent Fund must be managed and will be managed, or else we are all gone, according to the high standards of a world-wide financial intermediary.

On that basis the Permanent Fund---this gives me an opportunity to make another critical point---don't think about the annual paid-in net retained earning as being the Permanent Fund. That is only the equity capital base of the Permanent Fund. Permanent Fund, if it is soundly managed, like any good development bank, will have the capability of accessing world-wide money and capital market in terms of its paper and the British Columbia Development Authority involved in New York, London, Paris; the British Columbia Central Credit Union that I referred to borrowed in world-wide capital market to support a dock that are in little villages in British

Columbia that no financier in London has any confidence in. But they had confidence in the British Columbia Federal Credit Union or in the British Columbia Development Authority. One good thing, it may well be much more effective for you to finance that airport by accessing international capital market and spreading the cost over a number of years. So you have to look at the expenditure side separate from the revenue side.

MEEKINS: Are you suggesting that that kind of borrowing by the Permanent Fund would be at a lower rate than, say, we can get general obligations bonds for?

DANIELS: It may well be. That depends at various times on the state of the municipal bond market. The municipal bond market is cheaper but it is a very inefficient market and it may not always be the most---it may be at certain times that it is cheaper to borrow on a world bond basis.

MEEKINS: It must be the state's general obligation bonds were more expensive so to speak---why would you bother to borrow through the infrastructure investments? Why would you want to borrow through the Permanent...?

DANIELS: Well, there are other considerations, and that is that the---to the extent that that is an obligation of the Permanent Fund---it is not a part of the indebtedness of the state and frees the indebtedness for other purposes. I don't know the specific structure of your state bonded indebtedness. To my understanding, it is relatively high on per captia.

MEEKINS: Yeah. Usually like these corporations have been set up are viewed anyway by the bond market as being part of the indebtedness, even though you say this is not a...

DANIELS: But the Permanent Fund is a somewhat different creature. It has got, eventually, \$1-\$2 billion worth of equity standing behind that bond just in and of itself. Why look to the state when you got that kind of a resource standing behind it? The point is that we want to separate out the decision as to whether or not to use the Permanent Fund. We want to look at the expenditure side with one set of eyes and the revenue side with the other set of eyes. It may be efficient to have it managed by the Permanent Fund on the expenditure side but financed through the general obligation bond market. It may be efficient to have it managed and financed by the Permanent Fund. It may be efficient on the revenue side to account for user charges which would come back to the Permanent Fund and make up the difference through the general fund, or it

may be efficient to finance it all through the general fund. I mean I can even envision, and this gets a little speculative for this type of discussion, but you know these facts between the Permanent Fund and the state, where financing constructed by Permanent Fund and the payment from the state is on annual revenues as a user charge by the state as a whole.

GRUENING: Further questions from the committee? He raises a thousand very important, very interesting questions.

GARDINER: I have got so many notes here that I can start with Point Number One.

GRUENING: I hope Dr. Daniels might be available tomorrow and in the future for that matter---that is something we need to discuss. Feel free to put your question in writing.

GARDINER: I appreciate that.

GRUENING: I just have one question. You mentioned something that you may want to follow up later. You mentioned regionalization of the Permanent Fund. What do you mean by that? In what way would it be regionalized?

DANIELS: OK, let me again---and I am kind of looking at Jim Edenso when I say this. In my view, the essential structure of 298 or 300 is very sound for a development bank, subject to specific comments and criticisms that are made in this paper, in which I simply raised further questions. I would suggest that both functionally and geographically consideration be given to some differentiation in terms of task. And if I may take the opportunity to speak for a minute on the functional side before the geographic, because I think they are related. The private market is very wise in separating out its sources and uses of funds, its risks, its management, according to different kinds of tasks. You know, we don't ask thrift institutions to be short term inventory and working capital commercial banks. We don't ask either of them to be venture capitalists because the risks are very different, the sources and uses of funds are very different and the kinds of people who are good at it are very different. My own experience, particularly in the United States in terms of development banking, is that it is wiser to separate out those functional operations as subsidiaries of an umbrella development bank, and I would suggest for consideration the possibility of the Permanent Fund as proposed in 298 or 300 actually having some operational subsidiaries who deal in venture capital in intermediate and longer term debt financing, infrastructure financing, etc., something we just recently did in Massachusetts.

Geographically, we have a world-wide experience. This is true in terms of international development banking, it is true in England, France, India, you name it, that if you are talking about a huge geographic area where the problems are different, the people are different, and the ability to access risk is different, it is wise to have your capital gathering capability and your kind of centralized technical support capability at the center, but to decentralize risk assessment--- I don't know Alaska. I mean, as I said earlier today when I was kind of out in the suburb, the furthest end of the Bush that I have been. I want to be careful. I don't know enough about Alaska to say that your distance is so large, your differences are so great, that it is necessarily important to do that. But my hunch is, it is, and that you would be wiser to have a series of regional subsidiaries of the Permanent Fund as designed in 300 that would operate in different parts of the country under very strong direction from central management in terms of their goal, you know, in terms of their direction and what they do, but not on a day-to-day basis.

GRUENING: OK, it is getting late, but we have other people. I would like to get the feeling of all the members here as to what they want to do. I want to wrap this thing up by early tomorrow and we could go later tonight or we could quit now. What is the general consensus of the committee?

Anyone want to go an additional half an hour? I think we could pick up a report. The next item would be a report from Jim Edenso on where the Permanent Funds are invested presently. Does anyone have any druthers on that?

RODEY: I have to leave personally, but what was your plan for tomorrow?

GRUENING: Start at 9:00 and wrap up about 11:00 or 11:30. I want to ask Mr. Edenso, Jim is it possible---you will be here tomorrow for that?

EDENSO: Yes.

GRUENING: OK.

GARDINER: What are your other witnesses for tomorrow?

GRUENING: We have Mr. Edenso from the treasury and Dick Haggart will be giving us some revenue projections, both short term and long term, and then we will get into asking what the committee members want to do on following up some of the big questions that have been raised today. We did an issue paper

that we want to send out to the people who are interested in the issue and would read the issue paper, and solicit responses and discuss the rest of the program. We may want to work out some sort of joint effort on following up some of these questions. I want to thank Dr. Daniels for a very enlightening presentation. Anything further? We will stand in adjournment until 9:00 tomorrow.

Proceedings
of
The House Special Committee on the Permanent Fund

SYMPOSIUM
September 10, 1977
Anchorage

Rep. Clark Gruening, Chairman
Rep. Terry Gardiner, Vice Chairman
Rep. Ernie Haugen
Rep. Russ Meekins
Rep. Bill Miles
Rep. Leo Schaeffer
Rep. Rick Urion

PRESENT: Dr. Barbara Bergman, University of Maryland; Dr., Donald Gordon, Simon Fraser University. Citizens' Panel: Dr. George Rogers, John Havelock, Dr. John Lindauer, Jamie Love, Tim Bradner. Members of House Special Committee on the Permanent Fund: Clark Gruening, Chairman; Russ Meekins, Bill Miles, Mike Doogan, Administrative Assistant. Senate Special Committee on the Permanent Fund: Pat Rodey, Vice Chairman.

Introductions made by Chairman Gruening--continues:

GRUENING: I had a long statement on the Permanent Fund and my views on it, but due to a self-inflicted wound playing racquet ball yesterday, I'm going to have to cut it short. I would like, before I turn it over to the economists, to state briefly, we do have a very challenging task before us. I know when I originally favored the concept establishing a Permanent Fund, I saw many goals and many objectives that the fund could accomplish. As I get into the subject and see the complexity of it, I see that maybe our goals can be achieved by finding that which is best achieved by a special fund such as the Permanent Fund.

Today, I want to explore that. I want to explore the possibility on a philosophical basis as opposed to what your pet investment may be. I know that people discuss various things the fund can do and we, as committee members, have received suggestions from people for investments-- everything from artifacts to wheat.

What we want to explore today are the reasons why that particular investment is consistent with your philosophy or your goal that you wish the Permanent Fund to seek. With that I'd like to turn it over to Dr. Bergman.

BERGMAN: Thank you. In trying to think over what kind of a contribution I could make, what occurred to me was to try to say some things that would sort out the issues, which would try to separate one issue from another and show how they're related. What economists have to offer, I think, is rules of thumb and wisdoms of various types. I think our major expertise is trying to sort out the issues. So let me try to do that. I don't think I'm going to tell you anything you don't know.

A good way to start out would be to discuss three kinds of scenarios for the state. Let me call the three scenarios: the spend as you get scenario--dole it out as fast as you get it--that's one. The development fund approach, which is to try to take some of the oil revenues and use it to develop the state. And the third scenario, let's call the gilt edge approach, which is to take the Permanent Fund and essentially invest it, for the most part, in the Lower 48, in the capital markets and use only the income.

Now, very kindly provided here was a thing which without which no professor travels--that is a blackboard. Let me try to contrast these and then show what they entail in some respects.

We have three panels here and measure time on the horizontal axis and dollars on the vertical axis.

This is the spend as you get approach. Let's assume, without inquiring for the moment where the numbers come from, that at more or less a current level of services there are certain financial needs which the state has. Let me for the moment put those down as more or less horizontal, perhaps with a very slight, a moderate growth trend; but certainly not a big growth trend. Let's call that need for spending. At the moment, there are some non-oil taxes, and let us assume that those also, tax breaks remaining the same, have a more or less horizontal trend. So these are non-oil related taxes. They depend on the economic state. They would presumably grow unless the tax breaks change as the days go. And then, of course, what we've got is this hump of the oil revenues which are going to exceed by some very considerable amount for some considerable time the needs for outlay of services at current levels. The spend as you get approach very simply is just to do this sort of thing: use them all up, and then when they run out, go back to that situation. Of course that is the approach the Permanent Fund presumably designed to avoid. I just put that in as a base line.

The next one represents the gilt-edge approach: g-i-l-t. I suppose some of those who want to see the development of the fund might spell gilt in another way. There again, people assume that the fund revenues will not be used for development purposes. All of it, and this is an extreme case, will again be devoted to gilt-edge investment. So the non-oil revenues will not be any different than they would have been, but the spending will look more like this. There will be perhaps some spending out of the oil revenues for current purposes--again I'm putting needs, the same in the second panel as in the first panel. But, after a while there will be considerable income from the Permanent Fund assets and the Permanent Fund income will take over as the oil revenues come out. So there might be some excess of the Permanent Fund income over needs; but in general, possibly that might be devoted to raising levels of services or sending some of the funds back, possibly lowering taxes or a variety of things.

The third approach is the development fund approach, and then the scenario is something like this.

I might say, the scenario from the developmental fund approach is somewhat controversial; that is, the first two I put down naturally you can't foresee even how gilt-edge investments will do. We all know that. Nevertheless, you might say, this is a conservative approach from the point of

a risk. The one we're about to talk about perhaps is, at least from the standpoint of a risk per se, somewhat more risky.

But the more optimistic scenario, from some points of view anyway, goes something like this. The use of the fund for development purposes will broaden the tax base, and instead of having the non-oil revenues flat, as we do in the other two cases, they sort of take off. Here again, we have the oil revenues helping us and they peter out. It may be that some capital has also been lost because there is going to be a greater risk--the kind of loans we make--so the income from the fund will probably not be as big as it would in case 2. But nevertheless, there'll be some and the non-oil base in the state will have done well enough to cover the needs. Those are the three scenarios.

Now, say the third one is not as sure-fire in the sense of being able to tell what will happen as the others. For example, Dr. Tussing's view is, in general, with certain rather limited exceptions, the use of the fund as a development fund would not have this take-off effect on the economy. In general, the economy is going where it's going. It's got a dynamic of its own. It depends largely on such

an opportunity, the investment opportunities there are will be financed through private channels, which will be adequate to finance in the deserving ones, the ones that will pan out. That kind of adjustment has what the private sector does well; if there is a shortage of some type in Alaska which can be remedied through capital flow ect. This is one view. That view is that, in fact, the development fund scenario that I've drawn here wouldn't really work out. That is the non-oil revenues will not be materially affected by whether it is used this way or that way. What will mainly be affected is the amount of the capital which is left and return on it. If you ask me what I think, I would say that you need to decide whether you do believe in the efficacy of the development fund approach. I'm sure a lot of people do. I may say, that since I knew I was coming here, I did some work in Washington trying to find out what some people in Washington who are in capital markets think about closed funds to places like Alaska. Ther general views that I got were that the market mechanism for getting funds into places like Alaska has much improved in the last 10 years: federal infra-structure, federal homeowned bank boards.

So if you believe that, then one might be rather doubtful that the development fund should have been. On the other hand, I tend to be skeptical of doctrinaire pronouncements

of that sort. I think there is some merit to that scenario, although I would certainly argue caution. I would say that, in general, the idea of the Permanent Fund--the thing that makes it different from the spend as you get case-- is a desire to preserve some of the resources for future generations. I think, in a way, the best way you could put this is comparing the people who have to manage the fund to the trustees for a family.

Suppose the trustees have been given the instruction to make sure the grandchildren are taken care of. That kind of instruction would argue to the gilt-edge route. Suppose the current adults in the family come and say, "we have a family business which is in terrible need of funds, and if we can get these funds, the grandchildren will be better off, not through the silly gilt-edge securities you're going to buy but rather through the business that we are going to develop. Come on, trustee, give us the money." Now should the trustee do that?

I don't think in a doctrinaire way the answer is yes or no. I think you can say the trustee ought to watch out. I think the question the trustee has to ask is why can't the present adults in the family get commercial funding? Does the trustee know something about the family that perhaps commercial markets don't know about that

family? Also, this leads to a rather different point, that you've got more than one grandchild, you have to worry about intra-personal equity; you have to worry about different groups in the constituent population.

Let me turn to that for a minute. I'm used to a much bigger blackboard. This is the only deprivation I've suffered since coming to Alaska. You can think of the cast of characters we have that the people planning for this fund have to take into account. Most planning models involve summary statements of this much income and that much expenditure; but the real guts of the thing are the benefits and costs to individuals or group. Not everybody in Alaska has the same interests and there are some opposing interests, I'm sure. For example, what interests the kinds of people we have here to consider. First of all, the people who are in business; there are people who work in those businesses; there are professional people; and there are native Americans. You can divide those into people who are here now and people who might come if you get this development fund scenario, if it goes the way this diagram says it will go. Even those people you can then branch off into twice as many groups by talking about different values. For example, some business people are here regardless of the special characteristics

of the Alaskan community and environment. They're here to make a buck. Others make a lot of bucks. There's nothing wrong with that; it's the good old American way. Then there are the people who are here because of the special nature of the Alaskan economy: the special nature of the Alaskan environment; the special nature of the people here. And they have an interest in keeping it that way. So you classify people in three different ways:

- 1) by their role in the economy
- 2) by their value system
- 3) by whether they're here or whether they're not here yet.

It seems to me, that it's very hard to do any planning for the state, should you in some formal way, try to weigh costs and benefits. For example, I would weigh costs to the native American community as very high, in my calculations. I wouldn't just subtract the native American communities costs from the benefits, say to a hotel owner. Usual calculations, you subtract the cost from the benefits; or you take a ratio of the cost and the benefits. If the ratio looks good, say let's go ahead. I think there's a waiting process that has to be put in here. I would discourage any planning process due to the fact that there are the different groups and they do have different interests and different values to be taken into consideration.

GRUENING: Doctor, I just wanted to mention that this hotel is owned by native Americans.

BERGMAN: Why don't I stop here.

GRUENING: That wasn't intended to cut you off. Incidentally, although we're elevated on this stage, it wasn't intentional. I think the audience here is just as elevated, and we want to make this informal. After the panel makes their statements and questions, I hope that people will feel free to come up here and make a statement and ask questions of either the economists, the panelists, or even us, for that matter. Go ahead, Dr. Gordon.

GORDON: Well, to some extent, I think I'll be overlapping with Professor Bergman, so I'll eliminate that kind of consideration.

I am struck, as the Chairman said, with what I consider the awesome responsibility of those people who are to decide what is going to happen to the Permanent Fund in particular, and other oil revenues. I am struck by that because while I find the numbers tossed around a bit confusing, they are all pretty big. If we take the kinds of figures that are in the little green pamphlet, we talk about numbers like \$8 billion, whether in the Permanent

Fund, as in some assumptions it is, or whether it's in the Permanent Fund or not, it's a transitory income from these oil revenues.

Now, it's very hard to get people to take numbers like \$8 billion and have it mean something. I find it useful to use this as a person in a family. So I got out my World Almanac, I find that there are about 400,000 Alaskans. Suppose this fund has by 1985 about \$8 billion, and suppose you can define an Alaskan, and as Professor Bergman pointed out, that may be the trickiest part of the problem, suppose we define Alaskan as people who were here when the oil was discovered, we say it legally belongs to the entity, the state of Alaska, it morally belongs to those people. It's their money. Those people who are going to make the decision have to spend that money for them. If we divide the \$8 billion by 400,000 people, we get \$20,000 apiece. If we estimate the average family is four persons; that's \$80,000 per family.

It's just as Professor Bergman suggested, It's like being in the role of a trustee. If you dress up the story, the father dies, he leaves a young wife and three children, but she happens to have \$80,000. You are a brother or a friend or something, you are appointed trustee. It's assumed in trustee agreements, as I've had the misfortune to read some of them, that people who are the beneficiaries of the trust

really can't be charged with spending their own money. So, somebody else has to spend it, and a guess is, the implication of the way the fund is set up. Now \$80,000 will set up their whole way of life different than it otherwise would be. The most important thing is to think of this as making a decision for about 100,000 four-person families out there, each of which has \$80,000 which you have been entrusted with spending.

Now, the tricky thing is going to be defining an Alaskan. For that purpose, I assume you can define an Alaskan in some limited way as consisting of a certain number of people and it's those people who, in effect, own the \$20,000 apiece or the \$80,000 per family.

There is another thing that struck me in looking around the world in the last few years. There are countries like Kuwait, Saudi Arabia and the press almost universally, and a lot of people who should know better, go to these countries and say, "You know, these countries have a real problem; they can't spend that money." These countries aren't democracies. So what they must mean is that the king and his bureaucracy can't spend the money, because we all know that if you passed this money around among the average Bedouin in Saudi Arabia, that with the help of Sears Roebuck, a thousand other firms from the

rest of the world, they'd have no trouble spending the money at all. In those countries the money isn't the people's money. It's the king's money. But, again, the notion that you have a problem spending the money is only appropriate for a very different kind of society than we think we have.

A third question that I think is very important, apart from what is currently in the Permanent Fund or what is in the Permanent Fund in the future according to different assumptions, there was a very significant question about what should be treated as income from a depleting resource and permanent income. In economics, there is a very common distinction between what you might call regular income and windfall income. Sometimes these are called permanent income and transitory income. In principal, it's just as every prudent household would treat those two things quite separately. If you have an income of \$15,000 a year and you expect it to continue forever, you treat it one way. If in one particular year an aunt dies, totally unbeknownst to you, she has some money and she left you \$15,000. Now it's hard to find one person, I think, who would say they'd treat that once and for all \$15,000 in the same way as their regular \$15,000. They wouldn't just double their spending that year because their income happened to double

The most important thing is to think of transitory income as different from permanent income. When some oil

money is going to last some 25 years, especially at the beginning, that money is partly transitory and partly permanent. For simplification, I want to think of it as transitory.

One way to compare any other ways of treating this money would be to imagine a world in which we don't live and imagine just giving that \$80,000 to each family--what it would do for them and what they could do with it. With that as a benchmark, consider alternative problems. In considering these other alternative policies, we have to make some critical assumptions. Perhaps we should investigate the facts.

We have to make some presumption about a very critical thing and that is the flow of labor and capital into and out of Alaska. That's part of the problem defining an Alaskan. That has been already alluded to by Professor Bergman and she referred to the paper by Dr. Tussing in which he argued that, subject to further research, capital flow is very easily into and out of Alaska, and therefore, the rate of return to capital in Alaska is primarily set in the United States, or even better in the world market. Capital flow is pretty easily around quite a few countries.

I would like to extend that and just for the sake of argument, subject to a lot of further research on the problem, that the same is true of labor. The labor flows

pretty freely from one part of the United States to another. If that's true, then there's nothing that can be done with this fund that can change the wage of labor. Now, of course, it isn't the wage of labor, there's a whole structure of wages--from high priced brain surgeons down to busboys. But those wages will be set, not in Alaska, they'll be set in the United States because there's free migration back and forth. I want to make those assumptions for the moment anyway. Assume that there is competitive capital market and competitive labor market. I will modify that later on.

Now consider two or three alternative ways of using this money. One of them I asked my conservative friends. They have the assumption that giving money to the government is pouring it down the rathole to some degree--they have different rathole co-efficients, but it's significantly bigger than zero.

So, they say cut taxes. If we cut taxes, then we won't keep the level of government expenditures at what it would be otherwise. Cut taxes, then the money would be used by the people for sensible purposes--cut sales taxes, cut income taxes, so forth. Now, if you ask yourself what that means, subject to the assumption that the flows of labor and capital between the United States and Alaska

are perfectly free; the initial effect of that would be that real wages after taxes would rise in Alaska relative to what they were in the United States. As soon as they did, more people would come from the United States to Alaska. The final result of that would be that the real wage would be precisely the same as it was before. The real return on capital would be the same. Nothing would happen.

Who would gain? Well, there would be more people. If you would own a local monopoly, with economy of scale, such as the local newspaper, you would probably gain, as opposed to being a barber or even a hotel owner. If more people came, more people would set up hotels. You wouldn't rake off big gain. On the other hand, if more people came, it is unlikely more newspapers would be set up. So that's one small way in which local people would gain. Secondly, local people would gain to the extent they own scarce resources, that can't be reproduced. Not a hotel because you can build another, but not the land on which the hotel is built. If you own scarce, high-priced land in downtown Anchorage, you would gain.

Finally, it could very well be that you have a labor union. I guess economists like to call that a labor monopoly. Unions don't like that word. They don't mind talking about market power, but these are all words. Let's suppose there is a labor group

here which has the power to raise the wage or lower the wage to some degree. Subject to, of course, to the constraint that when they raise the wage, not so many people will be hired as when they lower the wage. Now, if we imagine a cut in taxes, we abolish the competitive market for labor which we assumed. If we imagine cutting taxes, people will come here. The labor union can keep the wage. The people coming here won't depress the wage to make up for the taxes. The labor union can keep the wage the same way because the demand for labor will be the same as before. In the case of a local monopoly in labor, and in the small bits of income that are earned by land rents in scarce areas, there might be some gain. The overwhelming bulk of income, which is the competitive wage plus capital, won't be affected in the long run.

What will happen, of course, is that the \$8 billion will be spread over the rest of the United States, because by some small amount, as labor leaves the rest of the United States wages will rise--higher than they otherwise would be.

Let's consider another thing, another scenario. I think this is something like developing the economy. The word development is a bit tricky. It is generally used, always used, in economics to apply to so-called underdeveloped areas, developing economies in places like Bangladesh and

and Peru and Zaire, etc. But that's not true in Alaska, because clearly, even without making the rigorous assumption, those countries think of trying to take an economy where the real wage rises very significantly. Nothing is going to make the real wage rise very significantly in Alaska because that's set in the United States. Just as the real wage in Seattle is set in the United States. It's not development in the same sense.

I'm always a little confused about development. Sometimes people say, we want to create jobs. I see in Alaska, people talk about diversifying the economy and developing renewable as opposed to non-renewable resources. But all these things, seem to me, subsidizing local industry in some way so that there will be industries here that otherwise wouldn't exist.

Dr. Tussing, in his paper, was talking about situations where you don't subsidize. He said, as Professor Bergman indicated, that he generally believed that if you don't subsidize, then you're not going to create any more industry. But, he did not say, and I don't think Professor Bergman intended to imply that he did, that you couldn't subsidize industries and create industries that wouldn't otherwise exist.

If you did that, there would be more people. There'd also be a bigger tax base. There'd be more services to supply those same people, presumably required.

Basically, when you got all through that, just as in the, what I call, conservative case, this is the interventionist case. The people who trust government more than the rathole theory. The interesting thing is that they both come out with roughly the same conclusion. You have more people, you have more capital, the real wage is the same, the rate of return on capital is the same, and in the case of a few local monopolies, they have gained but nothing else has happened. The reason it happens, of course, is that the benefits are flowing to Alaskans, but an Alaskan is really defined as anybody who can benefit by moving here. Or by not moving here, for that matter.

Now, let's consider a third thing--amenities. You create amenities. The trouble is if you build a big opera house in Anchorage, I'd be much happier to come for a lower wage than I otherwise would. An amenity is a real part of the real wage. People would then have their real wage and amenities rather than lower taxes. Incidentally, when you talk about amenities and providing government expenditures, there is no difference in principal between whether the income is a renewable resource or a non-renewable resource. If income flows to the state, one question that should always be asked is, if this in-

come is flown directly to the people, it's their income, would they then be willing to be taxed some of that income to create the thing which they would consider building? A better university, a big opera house, play fields, golf courses--all those things. Before you build a golf course, which I'd be much in favor of, you've got to think about the fact, would the people be willing to be taxable on the course, if, instead of going first to the state, it had gone to them? That's of course true whether the funds are transitory funds or permanent funds.

Now, another thing mentioned is stabilizing the economy. I thought Dr. Tussing's paper had an adequate analysis of that question. It is very easy, when one has looked back on a time series, what happened to the economy. To say, if we had only put a little more money into the economy there, and then taxed a little more there, the economy would be much more stable. In fact, it is sort of inevitable to think it sensible to pour money in there and take it out there. The problem is, as anyone who tries to make money in the stock market will know, that's not nearly as simple. If you look back at the stock market over the last four years and you would say, "gee, it was easy to make money in the stock market--all you had to do was buy here and sell here." It may seem that the problem of sta-

bilizing the economy is not that different. It is a problem of prediction. It is the problem of getting the spending going very rapidly relative to when you need it. As Dr. Tussing says, those problems are not easy to solve.

I might add something. If you can predict the economy, then you can stabilize without any Permanent Fund. You borrow the money when you need and you pay it back other times. It's not hard to stabilize if you can predict, without having any special Permanent Fund.

When I think more about this problem, here's this money, which it is said, belongs to Alaskans; but what are you going to do with it so it will make some difference in Alaska, with some real difference to the average Alaskan? I come back to what I call the benchmark. The best thing would be to take it, the \$80,000, and spread it around to each family.

Suppose you can't do that. Is there some way you could spread the income from that? Not by cutting taxes. The income from that goes to certain people who, as it is interpreted, own the resources.

Incidentally, I think the idea of just giving the money to the people is somehow associated with conservative views, whatever conservative means. My understanding is that Milton Friedman has suggested that view. Everyone knows he's conservative enough. It must have occurred to a

lot of people since the beginning of time--it certainly occurred to people in Alberta at the time oil revenues were discovered there. Whether it's conservative or not, it's profoundly egalitarian because it would take \$80,000 and give it to each family. No depending on whether they're rich or poor. Exactly the same amount. It's not egalitarian because you're soaking the rich to help the poor. That money didn't belong to the rich any more on a one-for-one basis to begin with. So it would have a profoundly egalitarian effect on the distribution of wealth and the distribution of income, if you can't distribute the wealth.

I was intrigued by the suggestion in the green pamphlet of the Governor that you might pass out the income. I understand there's some legal problems in all this. The legal problem is again defining an Alaskan. I understand perhaps the legal problems will be solved if you think of pension for when a person's 55. There's nothing in nature that says a pension has to be distributed at 55--maybe at 45, maybe 25. Anyway, I think if you regard these resources as being morally belonging to Alaskans, you should think of some way to give it to those people you define as Alaskans. Otherwise, you might as well write a check for \$8 billion and send it to Jimmy Carter, because that's where it's going, for all practical purposes.

If you took \$20,000 per person and put it in the stock market, would he own it--\$20,000 per person; \$80,000 per family. You notice that the average Alaskan, who let's suppose, is like the average American now, wouldn't have \$4,000, rounding out the \$3,900 to \$4,000, but he'd have \$24,000.

Of course, there's other wealth besides the stock market. Houses, some wealth that isn't counted like future pension plans. But, I come back to a number like that to impress, because I'm impressed, to try to impress you with the awesome nature of this responsibility. There are a lot of poor people in Alaska. I can't imagine one way that would do better for those poor people and for some people who are not so poor than to contrive some scheme whereby you can benefit them, if you believe they morally own those resources. Now you may say they shouldn't own those resources, they belong to the United States. You might even say they shouldn't own those resources, they belong to Alaskans, it seems to me, that the thing is to contrive some scheme where, in fact, the Alaskans will do the benefiting. Some defined body of Alaskans.

To make one final note. If you talk about future Alaskans--that's pretty confusing. You see, there's where

the analogy with the family breaks down. If you think of a trustee and a family, you want to take care of the children and the grandchildren; and if Alaskans were defined that way, it would be simple. It would be the children and the grandchildren of the original 400,000. If you talk about who might live in Alaska who now lives in Alabama or New York City or Seattle, then it becomes very hard to do anything with it.

Of course, if you gave the money out as a grant, which you couldn't, chances are the parents would take care of the children; and they would take care of their grandchildren, as is the normal way we treat wealth. The normal way we treat wealth in the United States, we assume people are responsible and are capable of handling their own money better than the government. If we say that's not possible, then we should probably try to devise a method by Alaska, Inc. or a pension at some age, so that the people who morally own the resources get some access to the, really do the benefiting. You might ask them if they'd rather have the income from \$80,000 or some vague thing called diversifying the economy. There isn't such a thing as economy or state, there are just people there.

Anyway, I think it's a very tricky problem. It appears to be in a large respect a legal problem. The only economic aspect of it, I think, is to recognize that nothing you do

with this money can change, for all practical purposes, the real wage and the rate of return of the capital, and that's the bulk of normal income. Whether resources invested in Alaska or Tokyo, for that matter, or the New York Stock Exchange, it doesn't so much matter. I think it depends more on whether you use it to deliberately subsidize income or not. Presumably, as a prudent trustee, you invest it with considerations of real earnings after allowing for inflation, which makes it more complicated, and some safety. Thank you.

GRUENING: Thank you, doctor. Thank you, Dr. Bergman and Dr. Gordon. I think you've specifically trampled on a lot of people's assumptions. I think they ought to have the opportunity to trample on yours. We have a panel that will hopefully do that. I would like to make just one remark on the figures that are being tossed around today. \$80,000 is, of course, very hypothetical. The revenue projection includes both the Permanent Fund and the general fund, based on the pipeline, presuming a full design capacity, based upon a reasonable tariff, based upon a lot of things. We are dealing with a lot of if's. I think the point is well taken.

The panel can proceed in the order in which they were introduced.

HAVELOCK: We must make a determination of how it's to be managed in the future. Both of our panelists have referred to the analogy of the family. We are trustees for a family. You can reduce this to the position of a person in a family.

There are profoundly different ways in which a regional economy operates and in which a family operates. The differences, I think, need to be addressed. I think we need to get the Alaska public out of the situation of thinking about it in purely family terms--the kind of terms, which say, for instance, on the national level, that because the national debt went up last year we're worse off. Those kind of economics are very dangerous.

As far as the scenarios that Barbara pointed out, they're not real--any of them. That is, the scenarios of reality are sort of a merged concept of all three. There is a tendency to confuse oil revenue with Permanent Fund revenue, in fact, so far as you know, the Permanent Fund is only a committed percentage of oil revenue. I don't like little bumps like that, that sort of look like here today, gone tomorrow. We are not talking about a bump. We are talking about a very long curve. It may start high, but oil revenue isn't going to suddenly shut down. The economics of scarcity, we're the last major producer of oil on the American continent, so as the amount of oil available goes down, the value per unit will go up. The whole business of

Alaska running out of money strikes me as a basic error in viewing the situation which could get tangled up in managing the fund.

The discussion of what constitutes an Alaskan has been a troublesome one in this state. I'm not sure it's very fruitful, other than it provides entertainment in setting one group of Alaskans against another, based upon their longevity in the state. But, I think you do need in any scheme that's being set up to look at the winners and the losers under various schemes of investment.

One of the basic problems of the family analogy, of course, is that it assumes that when you put something away we aren't spending it. Particularly if you are involved in investment in Alaska. What the Permanent Fund is really doing is simply shifting the expenditure of funds from more of a tilt to the public sector, which is the effect of having a legislature the dominant controlling factor in the expenditure of funds, to having a predominantly private sector investment to the extent that Permanent Fund money is committed to profit-making enterprises automatically.

It is a long panel. I think one analogy I'd like to throw out for you to think about--it's a long panel so I'm just going to throw a few pot shots and then back out. There are a lot of analogies to what's happened in Alaska. One of them

is presumably supposing you'd had an Appalachian regional commission when they started getting into coal, would you have set up a Permanent Fund and devoted part of Appalachian money into that? What about the grandchildren today in Appalachia? How would they have benefitted from that fund?

BERGMAN: Stock in Gernerel Motors.

HAVELOCK: Well, if the function was to keep people in Appalachia, it worked because there was such a fund in a sense insofar as the United Mine Workers took money and put it into various pension funds, and so on. If we did that, and helped to pin people down to going on and living in an economy which was not self-sustaining, I don't think we've done anybody's grandchildren any great favors.

I think it's great to be an Alaskan, but if there are no jobs here, why the hell not move out--for those who have no employment? I don't see the public purpose served in subsidizing people who are two generations beyond me, who are only marginally going to be related to me, who, if you look at the general trends of the economy of the United States, are going to be far richer than I am anyway. Those are some of the reasons why I think you have to look at the management very carefully.

GRUENING: I have one question. If you want to discourage future generations, what about present generations?

HAVELOCK: The assumption of statehood incidentally, one of the assumptions on that chart, is that we have the income to sustain a moderate level of public need. The assumption of statehood was that we would use resource money in order to meet public need. All over the record of statehood hearings, the basic opposition of making Alaska a state was that there was not the income from regular tax revenues to sustain the public need level. I think you can invest. I would say that we've got to meet a schedule of unmet public sector needs before we start going on with a heavy dose of private expenditure, the worst risk of which is going to subsidize premature development of natural resources that we should be developing at the end of that curve.

GRUENING: Any questions here of John Havelock?

MEEKINS: Mr. Havelock, we hear a lot on this Committee about needs, you know it's very difficult to define needs, pressing needs expand to meet the amount of revenue that's available. I think that the concept is somehow inherent

In other words, saying that we should meet our needs first, we should spend all the money that we have to some people. This argument has been made to me, that we should spend all the money that we have simply because needs will expand infinitely.

HAVELOCK: Well, I think that the legislature can sort of define a minimum sustainable standard of living in Alaska, the kind of picture of Alaska you want and hold to. There is some truth in what you say, that needs will go expanding indefinitely.

The tendency of heavy private sector investments is going to be to spread the benefits to much more extremes. That is, losers in our society are going to go on being losers, even though you're putting all this in. Losers benefit out of public sector expenditure, some kinds of it. I'm not sure I'm ready for the opera house; there are a lot of things before that. I think that is a legislative problem and it involves taking a management approach to public sector needs in terms of establishing your baseline.

MEEKINS: One more question. You were talking about what you consider to be fallacy in the analogy of the family. I'm just wondering if I have it correctly. As I understood what you said, you seemed to be implying that investments are going

to be made with this money because people are going to deposit it in their bank accounts. If we did have an Alaska Inc., this money would then be deposited in the private financial institutions, they would make the relevant decisions about investments. Is that not as preferable in your view as the legislature making those decisions about how that money is invested?

HAVELOCK: Generally speaking, no. My basic point is simply you should know that's what's going on. That you are transferring the decision making process over the use of funds. I think that's obviously very healthy for a pure investment policy, for instance. I don't think you guys know what you're doing if you're giving the legislature the authority to run around money markets and decide what kind of instruments to buy and sell. Obviously, it's the kind of things you want to give to the private sector. Prejudice is the same in any form of development banking. I've seen too much development banking with heavy political control that amounted to shenanigans. I would rather see, if you are going to go into development banking, the use of banking standards of risk evaluation. I'd rather not have that muddied by politics.

GRUENING: Thank you, John. We have now next to him Dr. George Rogers. Incidentally, the two economists, if our panel isn't going to ask questions, you can ask them questions.

ROGERS: Clark, one of the things I'm going to do after this meeting is inquire into the nature of your racquet ball inflicted injury. I think as a public-spirited citizen I might suggest the state invest in racquet ball courts as a means of cutting down on public discussion somewhat.

I, like John, will make a statement and then be available for questions. I am an economist, but find it difficult to act as an economist when I get into a political setting for obvious reasons.

I, unlike John, was not opposed to the Permanent Fund but I was in favor of it for different reasons than the stated reasons. I know how the legislature acts when it gets a pot of money. I know it's going to spend every penny that comes in. I looked upon it as a curb upon legislative spending. I'm not too concerned about the intricacies of whether we call it a development bank or not. I agree with Dr. Tussing, that the development bank has very limited, or will have very limited, impact upon the Alaska economy, which gets me very quickly to my statement.

I would like to put the statements made by Professors Bergman and Gordon into the Alaska economic context. I think this is very important. In Jim Rhode's covering letter, inviting them to attend here, he made one passing remark that, I think the statement was that of every dollar gross state product \$.64 leaks out. I think this gives you an idea of the nature of our economy. It's a colonial economy in which the state product is largely exported, the value is largely exported.

BERGMAN: What do you think that statistic is for the state of Maryland?

ROGERS: It's probably something like that, but the point I want to get to quickly on that...

BERGMAN: Alaska's not that very much different from the rest of the country in that respect.

ROGERS: Okay. That's right, because we do--as states we are part of a national entity. There are these traits, etc.

First of all, the value is not an Alaskan value. It is something that goes into the national economy very definitely. Looking at the regional economy, however, you find that we generally define in the terms of such measures as per capita

real income earned by residents and other measures. You find that the Alaska economy is dominantly a government economy.

Very quickly, if you were to look at the basic part of our economy--the part that generates the whole thing--looking at the resource we find that before oil came along, it was very, very minimal. A fading fishing industry, a stagnant forest products industry, and then this great military establishment, construction industry that was generated by that. From 1940 on, whatever measure you use of the regional economy, you find that half or more of the employment, income, etc. generated by it is in terms of state and federal government income directly.

Then the support industry in the private sector is primarily in support. These people, these programs are living off them in some way. If we were to eliminate or reduce the rat hole coefficient in the Alaska economy back to a level that would be a more reasonable one in terms of Professor Gordon's philosophies, we would have something like the 1939 economy.

At that time, we had a thriving fisheries industry; we had mining industry, which, in terms of labor employed, was probably larger than the oil industry's going to be here. So in terms of a natural resource economy, we would be reducing

ourselves to something like 75,000 people operating primarily a few natural resource extractive industries with a minimum of federal and state government services required to maintain that work force in operation.

The thing is that the state government has become the driving force in our economy. This is the reason that the scenarios by Professor Bergman are relevant. I don't agree with John that they are irrelevant because she concentrated on state revenue. Each one of these is a hypothetical projection of what the state revenues might be, given three different scenarios or three different ways of managing the oil revenues: spend as you go; putting it into a development bank type operation; or working out the investment---I think the investment was the second and the development bank was the last one---because the reason we have a community like Anchorage is because of government spending.

The government spending has almost assumed a life of its own. When we are talking about stabilizing the economy, we are really, in essence, talking about stabilizing the level of government spending; because if it drops off, our economy drops off. If the private sector, for example, the oil revenue drops off, if there isn't anything else to take its place, then one way of doing it is to increase

government employment. If you are talking about distributing the money to the average Alaskan, you would, in many cases, be distributing to a government bureaucrat and his family. So that the Kuwait model is a relevant one in Alaska, except that the bureaucracy is much larger and represents a much larger segment of the population.

BERGMAN: What about the privates on the base?

ROGERS: The privates on the base. Yes. That's a whole sector of the economy that is generally there, they generate income in Alaska but they are only here for a couple of years on an average, depending on what their turnaround is. But we consider them part of the bureaucracy too, because they are paid by the government. They perform governmental functions of safety and protection.

But what I am saying is we've got to get our talk about investment, management, talk about the use of the fund into a realistic Alaskan economic setting. When we talk about diversification, we are talking desperately about trying to get something else besides government in the picture. Not simply to proliferate a lot of little business around, which is probably what we will end up doing. But it is a tough job to find something, an alternative, to continued government spending, government employment.

Another thing, I notice the Alaska Humanities Forum is one of the sponsors of this. When I saw this, I wondered, what a nice organization like that was doing in a place like this. I decided that we should make some comments on that too.

Professor Gordon talked about amenities. I think this is what the Alaska Humanities Forum is interested in: making Alaska a better place to live. Now this is something that economists can't give you advice on, except we can give you some analogies, cost-benefit type of analogies, help you in that way.

This is another thing we should consider. The Permanent Fund, we have two functions: one is to manage the investment policy of it. In other words, maintain the integrity of the fund, so that, in fact, the fund is a Permanent Fund; and that we do get the maximum income generated which we can then use for current spending. The current spending could be used for a number of purposes. We could use it for the creation of new development, or we could use it for amenities--a whole range of things we might consider. I don't want us to get caught in the development bank syndrome and just stick there. I think there are other things that we should consider as citizens when we talk about the use of the Permanent Fund.

I don't have any questions at this time. I made quite a few notes. As the discussion goes on, I think we can come back to that Clark, I think I'll stop now.

GRUENING: Thank you very much, Dr. Rogers.

Incidentally, thanks for mentioning the Humanities Forum. It is on the agenda the fact that they helped sponsor this. I should say again, we're very grateful to the Alaska Humanities Forum for sharing half the cost of the room and other incidental costs we have in setting this up.

Are there any questions for the economists or this panel? As soon as we get through the panel, we're going to open this up to the audience to inquire of anybody here. Rep. Meekins.

MEEKINS: Dr. Rogers, I have a question that really arose when Dr. Gordon was speaking. I'll direct it to you, and see if you have any thoughts on it.

He was indicating he felt very strongly, it seemed that the individuals in Alaska could make better decisions regarding the spending of what is morally their money than the legislature. We've coined a phrase here talking about the rat hole co-efficient. That's the implication of that phrase that the legislature isn't as wise and can't spend the money as wisely as individuals can or least not as efficiently.

One of the things that, I think, legislators are always confronted with is our system of government is representative in the sense that we are expected to know a little bit more than the general public. They are expected to vote for us, and then we are supposed to get more involved in the individual decisions. Sometimes we find that when we study something, at second thought, it's a little more complicated than it seems to the public. Even though we represent our constituents, we find ourselves voting in opposition to say, a majority view. We don't have a strict case of radical democracy in the sense that the majority view does not always prevail in the legislature. This sometimes is extremely good.

So, if you apply that thinking to decisions about how best to provide for the benefit of the people of the state, you sometimes maybe would have a contradiction between what the majority of the people would vote for, even allocate their own money for, and what might indeed be best for them.

It's a difficult question, but as an example, in some states, the public votes upon appropriations to education. In some of the states lately, they've had a very difficult time getting any appropriations at all. They've gone for weeks and sometimes even months without any appropriation

for their school system. It seems to me to be an example, at least it's quite obvious to me--I'm very supportive of education, I think there's a benefit distributed throughout the entire society, whether or not people have children, when we spend money on education. Using that as an example, I just wondered if you have any thoughts on that.

ROGERS: I don't have any profound thoughts on this. I think this is an extreme example of what might be done with the money. The assumption is that all spending is done by individuals. If that were so, I think this would certainly be a valid model to use. You mention education. Education is a group or a social decision. The individual may not have any children, therefore, that individual would not spend any money in education. However, society as a whole has some responsibility, whether you have children or not, so that there are a number of social decisions. We still have to have taxations.

I think what Professor Gordon is talking about, I think we had better get you into the discussion, is the distribution of windfall income, incomes that are transitory. We need the distinction between permanent income and transitory income.

This would be, for example, the \$900 million bonus we

received, which is all gone now. Would it have been better if we had handed it to Alaskans because it's going to go in three or four years anyhow, let them have a spree or invest it wisely, or set it aside in a permanent fund? We did neither. We let it dribble out into our general revenues and it was spent. The effect of that was difficult to trace. They are assigned to--how much the expansion of expenditures reflected need and how much merely reflected the availability of money to the legislature? I'm getting off the point. As I say, I think it was intended as a poll.

GRUENING: Dr. Gordon, would you like to comment?

GORDON: Well, some questions it matters a lot whether the money coming in is transitory or permanent; some questions, it doesn't matter much at all. Obviously, there are some things that we choose to provide collectively. There's some argument as to how many of those things we should choose to provide collectively. There's no question of some things with the exception of very few people. Everybody agrees that some things should be provided collectively, so that when the income of the community goes up, there should be, presumably, more private good and more public goods.

I think it's important, however, to distinguish between something abstract called the economy. The economy doing this and the economy doing that. What's happening to the individuals? Fundamentally, our whole system of government is set up on the idea that the people vote for these things. If the money happens to go to the state first, whether it's permanent or whether it's transitory, one always wants to keep in mind, suppose it had gone to the people first, then you could go to them and say, "Let's have a better school." They could allocate the money that way. If, in fact, it goes to the state first, I think really the people get a little unconscious of what's involved.

In a way, I'm amazed at some of the answers that have come, because I think, if you want to use this number \$20,000, if you said, "Would you want to dole out \$80,000? Maybe you can't spend a lot of money but you want to get the income on \$80,000. We'll take care of the principal. We'll give you the income." Or do you want to diversify the economy? You put that up to them. I find that incredible that people would say "No, we don't want the income; we want to diversify the economy. "

I'd like to ask Dr. Rogers another question. So the economy has expanded from 75,000 to 400,000 people, the economy has--and that's mostly from state spending. The question

is who's better off than they otherwise would be? The economy isn't somebody better off or worse off. It's individuals.

I don't think for a moment, and I don't think Dr. Rogers thinks otherwise, it would really go back to 75,000 people. If you took this money, invested most of it outside of Alaska, invest it as a prudent trustee would invest it, and then pay the income to the population-- I'd be wanting to know, not what happened to what some people call the economy, what happened to the individuals, who, morally own that money. Would it have any harmful effect on any other individuals? It's a little hard to see who would be hurt by it.

BERGMAN: I'd like to say one thing. The \$80,000 is not coming in an instant. It wouldn't be a check. I think that would be pretty hard to resist. I think realistically, that if the state of Alaska did propose to send every family a check for \$80,000, the people of the United States would re-think the ownership of those resources. The fact that it does come over a period and it is not being handed out in cash to the residents of the state, to some degree maps the fact that is in part what is going to happen regardless of the scenario you adopt.

I think when you talk about taking either the capital sum and doling it out as it comes in, or doling out the income in cash--particularly when you talk about the capital sum--doling out the capital sum, which I think is beyond the question anyway.

I think there is a difference in what individuals might do and what they might compact as a body politic to do. The government properly does have a longer vision, a longer horizon than individuals, certainly than many individuals. That is right and proper.

I am not as devoted to consumer sovereignty as many economists are, that is, I am not as devoted to the proposition that every citizen ought to have the right to handle, to make every decision himself, and that the government should not constrain any economic decisions. A lot of people would do things they would be sorry for if this money were handled that way. I don't think that's the question anyway.

I think the major practical question is the filling of public need, which governs how much goes into the Permanent Fund. Once you've got the Permanent Fund, the use of it or the investment of it, when I gave my list of different kinds of Alaskans what I was intending to do was, Professor Gordon was also calling attention to, and that is to try to get it from a gross concept called the economy down to people. I don't happen to think that the provision of amenities within reason

by the public sector is a bad thing. I don't think building a very good university here, building very good sports facilities, reducing some of the problems that are inherent in the geography of Alaska is really going to spread this benefit around to the entire United States. By the way, if it did, that wouldn't be so bad either-- if some of it went that way.

GRUENING: Senator Rodey.

RODEY: I had a question for Dr. Rogers regarding the rate of contribution. The proposal has been made that we put into the Permanent Fund 100% of the royalties plus all monies coming in from the severance taxes and allow the state budget to reflect only a base year figure, population increase, inflation, and perhaps an adjustment factor.

As a veteran legislative observer, this would deal with the question you mentioned previously and that was one of a budget constraint. How do you feel about proposals for this sort of input to the Permanent Fund that would essentially take all of the royalty and a good portion of the severance tax leaving only what is necessary for state expenditures on a predetermined level?

ROGERS: This would be, I don't have the figures-- I don't know what size figures we're talking--and the fact is I've been trying to avoid getting involved in the Permanent Fund controversies entirely. I certainly feel that this would serve the purpose of putting a damper or rather constraining by putting some limits on state spending in the future which would be a good thing.

The income, however, from that fund is still available for use. As I recall, some of the calculations made on that was that it began to become quite sizable, quite a monster in its own right. Even using a relatively low interest rate, you come up with annual income. This, then in a few years, becomes the critical thing. Not so much the principal as what is done with the income--if this is re-invested in the Permanent Fund, it then compounds the problem at a future date. I'm calling it a problem now rather than a solution. If it is then added into the general fund, then again it accelerates the level of state spending.

I can't really give you an answer until I've seen the actual solid figures on that. Certainly, the very crude projections we made using our Man in the Arctic model and using 25 to 50%, 100%, we found that the greater the contribution made to the Permanent Fund had a general dampening effect on the level of the economic attainment in terms of employment income; and this is simply because the assumption was that

the government spending would continue at that rate. It's a dog chasing its tail proposition. It does provide a great slowing down of the runaway process.

GRUENING: Thank you, Dr. Rogers. Next in order is Jamie Love of the Alaska Public Interest Research Group. Go at it Jamie.

LOVE: I don't want to repeat or go over a lot of the things that have been said by some of the other participants here, although there are a lot of important things that have been brought out. I know that most of us can agree that the money in oil wealth and Permanent Fund basically is to improve our qualities of life and standard of living. I know that there's one sort of philosophical difference that's emerging right now and that is on this issue of whether or not people should just be given the money so they can benefit themselves, or whether the government should spend it for them, and whether or not the main focus of the Permanent Fund ought to be some type of vehicle to get money in the people's hands--get the oil revenue in their hands. I know that's been the primary focus of the public debate that I've heard on the Permanent Fund, more than any other issue, is how you're going to disburse the earnings from the Fund. Realistically there's going

to be sort of a lot of ways the oil wealth is going to be managed to help us.

There's some areas, I think everyone's going to agree, that consumer sovereignty, or whatever you want to call it, makes a lot of sense. I don't want the government to do my grocery shopping for me or a lot of other things. But I think there are areas where some type of public actionary or adventurist is the only way that certain projects are going to get accomplished. I think it's going to be, in fact as we go along, probably a mixture of those two.

I would like to make one observation relative to things like the difference between a rathole and a pressing need for a lot of people. I don't always think it's just the project per se. There are examples, there are times when the same project can turn out to be either one.

Most of us are familiar with a lot of efforts to develop housing in rural parts of Alaska. It's difficult for people living in rural Alaska to provide housing through conventional, their own resources--people living not in a cash economy. Types of impact that we felt here in urban areas, I'm sure are even more dramatic in rural areas. In that area, if housing is going to be provided for people in rural Alaska, the government's going to have to provide certain types of subsidies for financing to accomplish that. Some people

look at rural housing projects as more in the rat-hole area than in the pressing needs type area--it's because they're poorly managed. There is a tremendous recognition by a lot of people. There's a lot of waste in mismanagment. There's some other reasons why the housing wasn't done properly in some areas. This is one of the problems the state's going to be facing as we go along and we come into a lot of wealth and we try and take a very activist role in terms of improving qualities, people's qualities of life.

We've taken a big quantative jump into a new area of running the government and providing services. We've been very interested, at least, in our organization, at looking at the ways and vehicles the state can best put together a lot of planning mechanisms and management functions to have more quality control or better evaluation system as we try to accomplish, whether it's a loan program or a cash subsidy or a number of different other things.

One thing I want to note briefly before I get into some other comments is when we talk about the Permanent Fund and we talk about investments, I'm sure that everyone in his mind is thinking that we're also talking about capital spending by the government in terms of just cash, just building projects that aren't really an income producing venture like infrastructure development--roads, highways,

that sort of thing--which don't produce revenue by themselves, but may help contribute revenue from another project and level of state services.

I know that it's critically important. I think, that the state, when they think about managing their investments, the social investments, that they make in the state of Alaska to be coordinating the development of their capital programs and studying for services with their investment policy--this has been elaborated in some detail by earlier consultants.

Dr. Daniels and Dr. Tussing touched upon this. I just wanted to bring that out. So when we talk about developing investments, we also have to be closely coordinating these policies with other types of problems we're faced with.

Other than those management issues, which, of course, we're very interested in, because our own examination of some of the state's projects in different areas including the state's existing loan program and the state's housing programs has not been good. I'm not talking about some of our absolute, right up-to-date current but I'm just saying as a general comment. In the last 10 years, for example, we've seen a lot of problems.

There are other reasons why we're concerned about the development of the Permanent Fund. One area, I'm talking primarily about social investments. Those monies that are invested domestically in Alaska, it's important that there be

a clear concept of equity in the benefits that people realize. Just as a very quick example: the tourism revolving loan provides loans, I think it's up to \$4 million, or it's up to 3. It used to be up to \$1 million. It used to be, I think 8% for developing tourism facilities. A lot of the loans went, for example, to the Captain Cook Hotel and the Baranof Hotel--they each got a million dollars a piece, as I recall, for developments--8% interest--to develop something, I'm sure would have been developed had they had to go to private credit markets for that money, probably at a higher interest rate. On the other hand, you have some student getting a \$2500 loan to go to the University of Alaska for a year or maybe go outside to school. Then you have a fisherman loan and a VA loan to buy a house. Just trying to determine the equity between all Alaskans to determine whether or not the so-called subsidy or the so-called benefit to the person with the student loan or the the home loan was equal compared to the person who got a cheap loan to build an extension to a hotel that could have been financed anyhow.

I think that's an important concept because the wealth is public wealth. When we set up the social loan programs, there's a degree of equity that's involved and the type of

social loans that are made. I think there probably will be some that will and ought to be made.

Another thing is the openness and fairness in the management of the Fund. It is not so much an economic consideration, I guess, after listening to some of the comments. Everyone has talked about what a big burden this is going to be to manage all this money and what a mind boggling kind of problem it is.

To me, what's mind boggling is you're going to give the public confidence that the funds are being managed fairly, that the funds are being managed in a way that respects the wishes of the public, and that it's not just controlled by certain interest groups, special interest groups, whatever you want to call them--certain groups or individuals--and that they have a sense of participation and that they feel that everything is on the table. One reason we were concerned is that the administration, I guess I sort of serve the administration in a capacity on the advisory board, there's a lot of discussion on making a \$900 million loan to guarantee financing for the gas pipeline. I sit on the state appointed advisory committee on state investment policies, which I've served on for almost a year now. Our 21 member committee has never had a presentation from the Commissioner of Revenue or anyone else on this mere billion dollar investment that we're thinking about making for the gas pipeline.

GRUENING: You might have to defend yourself. The Commissioner of Revenue, Sterling Gallagher, is in the room. He'll get a chance.

LOVE: I've made my views known already. What struck me as a bad thing to start out with, if we're talking about managing the Permanent Fund. We have an amount of money that is incredible. Almost four times as big as the Lockheed loan that Congress debated quite a bit before it even took action. To my knowledge, there has been no public presentation on the details, the official advisory board for the governor was never consulted. Negotiations went on for almost a year. We still have, as yet, to even have a memorandum mailed to us even though requests for information have been made. I'm not saying that to hop so much on Sterling, although I know it's coming across as criticism.

GRUENING: Sterling, we're going to let you respond to this if you want. You may decline if you want. Go on, Jamie.

LOVE: I'm saying it because I'm not worried. I thought that there was not a large likelihood that that loan would have been made, primarily because I thought that the El Paso line would probably not prevail. There may have been a

couple other reasons why those offers be made.

It sure is important, as we get into this area, that we force the people who manage this fund to disclose in as many levels as possible, the planning that is going on, the terms and types of arrangements they are making. The public should have confidence in the management of this money. Along that line, I think, we're very concerned that the public is convinced. I, personally, am convinced that there is integrity in the way that the money is managed. This again is not much an economic consideration, but it is an important social consideration, and it is an important thing that we've thought about quite a bit. I know others have.

I think in this area, there are two areas where we have to ensure integrity to manage the fund. The first one I want to touch on is the integrity of the programs. In other words, are the programs doing what they're supposed to be doing? If you have a small business program, does the small business program start small businesses that otherwise would not be functioning. Is it really matching its goals? Is the money getting out to who it should get out to? It's supposed to create jobs. Is there a way to measure whether they're actually creating jobs? Because you can really see kind of a rat-hole syndrome developing if you don't have an honest way of going

back and taking a look at what you've already done and seeing if actually, in fact, it accomplished your goals. Do agriculture loans stimulate or encourage agriculture. If so, how much can you quantify? A good way of having this program evaluation is important.

Now we had a presentation from Tony Motley when he was still Commissioner of Commerce on the state loan programs that the state already manages. He could tell us what their default rate was, what their interest rate was, and everything else; but he couldn't tell us a damn thing about whether or not the programs were accomplishing what the legislature wanted them to when they first created them. He said they didn't have any way of doing that. They didn't run program audits. In a way that's not surprising, because some of those programs are very big; some of them are kind of small. But as we get into the stage where we have the Permanent Fund, and we start talking about investment programs, then I think there's a much bigger responsibility on the state to tackle this very tough issue. How do you evaluate these things?

The next issue is the fiscal integrity of the fund. We don't want people stealing from the fund. We don't want people making bribes to get loans and this sort of thing. This is an area that is of concern to a lot of people. I, personally, have spent some time taking a look at some of

the other areas where we've been concerned about the fiscal integrity of some of the things that have happened in some programs. When you start talking about billions of dollars, the temptation level really increases. I think everyone realizes this. This is a tough problem. I don't know what the solution is. This relates to this whole area--the fairness, the openness, and the integrity of the way the fund is managed. These are areas that maybe aren't economic considerations per se, but we're really concerned about them.

I would like to say that it's been helpful to take a look at whether or not we ought to spend all the money right now, or whether we ought to invest all the money. There hasn't been much discussion about if we invest it, the types of investments we ought to do or if there's even any need to have any kind of investments on a local level beyond this issue of whether or not there's just a subsidy involved.

I'd like to discuss a couple of areas where I think it makes sense to have what could be called sort of a subsidized loan. It makes good economic sense, good bottomline economic sense.

There are simply some areas where capital markets don't work. Where they're not perfect. For example, in the area of redlining--housing in certain communities and certain areas within communities, you can't get a mortgage on homes or

you can't get rehabilitation financing on homes. There's been testimony before a committee in Anchorage, for example, in the area of Mountain View or Government Hill there is this kind of a problem. The reason I'm bringing this out is from an economic point of view, the cost of not providing mortgage, rehabilitation financing in a certain community may be that there's increased cost to the housing or that valuable housing stock deteriorates. It may not be a cost that the community has to pay for. It has to pay for higher housing costs, if that housing is lost and has to be constructed at higher cost. So there are external costs to the community that the community realizes in this area.

Just as an example, the normal market test of the sort of disinterested lender and the disinterested receiver of the money, they're not really the same. The bank doesn't have to worry about the social costs of redlining but the state of Alaska has to worry about it. If the state of Alaska becomes the lender, it can make some wise, some real contributions in that area and still make good bottom-line economic sense. I used that as an area. There are other areas where it might make sense--where capital markets aren't perfect. They certainly don't function as well for rural areas in Alaska as they do for urban areas.

In utilities, we've had testimony that good sound financial utilities can't get long term financing because they're not big enough and, therefore, as Dr. Belden Daniels noted, poverty line starts at \$200 million in sales a year. A company that's large, that's a big corporate entity, has better access to national capital markets. A smaller enterprise like some of the smaller utilities in Alaska can't get long term financing. That results in the very high utility rates. In that area, that's just another example where the capital markets aren't perfect. The state can put long term capital into local utilities, invest your own utilities, as well as publically owned utilities. The result is going to be a reduction in utility rates. This is an area where it might make sense to make a so-called domestic loan without the state really incurring any higher risk than it might otherwise.

Working on some problems in insurance financing where premiums are now being financed for as high as 80% by outside insurance financing companies in almost a risk free type of occupation area. There are certain types of consumer credit that could be from people who are really frankly getting gouged. I'm not speaking in terms of providing 3% financing. There are some areas of consumer credit where the state can get a return commensurate with what they get on the market except doing it here locally in certain lines of consumer credit.

Aside from this area of imperfect capital markets, there are other reasons why the state might want to make loans domestically besides stimulating the economy or trying to encourage growth. For example, you might want to own certain large resource projects. Russ Meekins gave me a little lecture one time on how if the state had financed the gas pipeline, it would be able to control local hire through contract.

GRUENING: Jamie, you might want to know, Russ Meekins just reminded me, that the legislature directed Sterling to investigate the possibility of financing the line so in fairness to him, he was following the direction of the legislature. Russ pointed that out. I thought it should be noted. Go ahead.

LOVE: Sure. It might make sense for the state to own certain types of large industry that occur. For the simple reason that (1) it may prove to be a good investment. Secondly, it may allow to implement such things as local hire and other types of social considerations. This is an area the state should be careful in, but certainly not something that should not be written off as not a potential type of thing to consider.

In other areas, they may want to change the ownership of something, for example, a foreign-owned fishing cannery. They may want to allow fishermen to form cooperatives and become the owners of the fish processing plant. The reason for that may be that maybe the public would see some use in that. They may feel that the fishermen are presently being exploited by the present owners. They may feel this may be a vehicle of overcoming that.

They may feel they want to use the money to help people capitalize and start credit unions to strengthen consumer-owned credit institutions which, incidentally, are the only credit intermediary that is feasible to provide financing to very small communities in Alaska. Commercial banks simply will not ever be a feasible economic intermediary in very small towns. Credit unions are probably the only things that can function in that area. There's a lot that can be done to strengthen the effect of credit unions beyond just consumer credit and to things of actual economic development financing particularly on a small community basis.

I'm going to have to cut this short because my notes are going a lot longer than I wanted to. I just wanted to tell you that a lot of the talk has been on the issue whether or not we should spend the money or whether we should give it

back to the public and what should we do with the earnings from the fund. I think that's very important, I think there's a lot of dialogue and discussion that has to take place relative to how we're going to manage the funds and what types of investments we might make. Thank you.

GRUENING: Thank you, Jamie. Do you have a comment?

DOOGAN: Just one question. Jamie, in speaking of social projects that could be financed, are you advocating then that they be financed through the Permanent Fund?

LOVE: Different types of social projects? The types of investments that I talked about--I'm suggesting that they could be financed by the state of Alaska using some other revenues we're getting from the oil industry. Whether through the so-called Permanent Fund or whether through the general fund or whether through another financial intermediary would depend upon the legal structure that the legislature sets up to management. It's possible to have more than one fund. I'm just talking in general about surplus revenue.

GRUENING: To follow that up you mentioned housing. There is ASHA, there's Alaska Housing Finance Corporation,

there's the veteran loan program. For what reason would the Permanent Fund be doing something that the general fund could do by setting up another loan program or increasing the size? Is there any special reason why the Permanent Fund, as opposed to another general fund loan program, would be used?

LOVE: I think the idea of setting up financial intermediaries in some of these areas, like the Housing Finance Corporation specializing in a certain area, might be the best way to manage these things. It could either sell its paper either the Permanent Fund or the general fund or somebody else on its credit rating. Dr. Daniels has done a good job of addressing, to some degree, if you're going to be involved in some of these areas, some different scenarios per se about financial areas. I, personally, don't think I've been addressing my remarks so much to the Permanent Fund per se as I have all state loan programs because we're talking about making investments, and I think it's important that we sort of re-evaluate our entire philosophy towards investments, loans and that sort of thing at a state level.

GRUENING: Thank you Jamie. Mr. Tim Bradner. Someone remarked that it's your money we're using.

BRADNER: Thank you, Clark. My thoughts about the Permanent Fund, and to an extent the larger question of the whole amount of excess or what some people call surplus revenues in the general fund, is essentially a political problem which we're going to have to be dealing with. Just a couple observations I'd like to throw out here real quick-- about the next 5 or 10 years in the dialogue that's going to have to develop in Alaska about how we're going to handle these things.

The Permanent Fund and the surplus wealth, the existence of excess revenues in the general fund and some estimates go to as high as \$10 billion by 1985 between the general fund and the Permanent Fund really puts Alaska in a unique position in the United States and even in the democratic West. No state, to my knowledge, or even any Western democracy has had this kind of a problem on this kind of a scale with a small population yet a large, diverse state with pressing social and poverty needs among many of its people.

We do have a situation we can look to in some states where they are coping with excess surplus revenues this current year. For instance, Texas right now has a \$2 billion surplus, I believe, in their treasury that they're debating

what to do with. Some other states have a small amount of surplus in the treasury. Nothing quite on the magnitude of the scale we're looking to here in Alaska.

Norway perhaps might be a situation in Europe that we could look at where there are large natural resource revenues and a small population. Nothing quite as extreme. There are extremes in the OPEC countries, but again, you have a different political situation there. Yet our per capita income over the next 10 years is probably going to be of the magnitude of some of the OPEC countries; in terms of the annual income from natural resources per person or per family unit probably range near what at least some of the OPEC countries are getting.

We have to ask some questions about how capable our democratic institutions are going to be handled, to handle these kind of problems. For instance, governments in the United States, state and local governments, are used to the whole idea of working with the scarcity of public dollars. The fact that tax revenues come from a lot of individuals and a lot of small businesses, there's always a scarcity in priorities. The logic by which decisions are made start from the standpoint that there's a shortage of public money, and the priorities have to be sorted out from that standpoint. In Alaska it's always been easy for the legislator to withstand the very severe constituent pressure he gets

for "what about that bridge" or "what about that dam" or "what about this program or that program" by saying "hey, there's just not enough money in the treasury this year. We just can't fund it." However, he's not going to have that excuse next year or years on down the road because there is going to be money in the treasury. There is going to be money in the Permanent Fund.

I am concerned about how permanent the Permanent Fund is going to be in the face of these kind of pressures, particularly if we have a situation in Alaska where we don't have a viable, steadily growing, private economy to generate jobs and income in the state's economy. People would tend to look to the government just as they did in the years 1970-1975 with the \$900 million for various kinds of help.

Already I hear people talking about the use of the Permanent Fund in its relation to the general fund. The Permanent Fund makes loans to income producing loans. Okay. Why can't the general fund borrow money from the Permanent Fund and promise to pay it back at 5% interest? I hear that sort of thing going on. I worry about that. No state has been in a situation like this, and I think, it's going to bring about some changes in some very different kind of pressures than we're used to in Alaska.

I think, we look at why people voted for the Permanent

Fund in the first place. I think the kind of dialogue that's going to go on this year where Clark's committee and other people are going to be going out and having meetings around the state to try to re-assess why people did vote for the Permanent Fund and what they were thinking about when they voted for it, and now that it's a fact, what is going to be done with it. To a large extent, people voted for the Permanent Fund because they had a feeling that there was going to be an excess in the treasury and they were concerned about the legislature spending the money. It was kind of a reflection of that traditional American hostility to government that we seem to bring along as a tradition in part of our political heritage.

So you set it aside into a fund that the legislature can't spend, but what you also do is you create another mechanism, and you create managers of that fund, and how accountable to the people are the managers of that fund? The legislators are really accountable to the people. If there's any fault in the system, maybe we should look to that rather than to setting up another layer for managing the fund that might not be responsive to public needs or public desires.

I am concerned about the Permanent Fund and the surplus revenue question from the standpoint of its effects on dividing the state politically in the future. Already we're having problems in differences of direction between urban Alaskans,

who live in Anchorage and Fairbanks and Juneau, and rural Alaskans, who live in small villages and have a different set of concerns and priorities. I think, you'll find that many rural Alaskans are skeptical of the Permanent Fund and the reasons by which it's been created. This whole dialogue we're going through here today is because the Permanent Fund is more of an urban orientated kind of a thing. They look at the requirement for safe investments to be made by the Permanent Fund; yet they know that many rural loans are in the frontier, high-risk area. They're concerned that a lot of those loans will wind up going to large scale development projects to benefit primarily cities and the urban areas and the urban work force.

They also realize that a lot of their benefits come from the state programs, state services in rural areas. They are concerned that if more money is dedicated out of the general fund, more than 25% of royalties into the Permanent Fund, then it will tend to short change the services and the kind of programs they are getting. I worry about that.

We have no place to really look for examples on how to cope with this problem. We do have a couple examples here in Alaska. We have the case of what happened to the \$900 million from 1970. Now, there was a situation where

there were surplus revenues, and we can look to how it was handled by the government. There's been a lot of debate and a lot of pro and con about what happened to the \$900 million. To a large extent, I think, the case can be made that the money was used for things people wanted. People asked for that money to be spent. If you look at the record, you'll see that a lot of it, probably most of it, went for education, because people asked for it. I think those kind of pressures are going to happen again in the future. That's really all I have to say.

GRUENING: Thank you very much, Tim. If there are no questions at this time, we'll proceed to Dr. Lindauer.

LINDAUER: I'd like to remind everybody that we really have two aspects to this thing. We keep running them together. We have the question on how to spend the income that's going to come off this thing. And we have the question of the investments that are going into it. It seems to me, that we're continually talking about the income, but as a matter of fact, it may well be that how we make the investments are going to have more impact on those people who are in Alaska today. I'm going to come to that.

There's also the question of what our objectives are.

I'm not so sure we've specified them. That is, how much of what we are doing is for us and how much of what we're doing should be for people in the lower 48 or for our grandchildren to make them even more richer than they're otherwise going to be, richer than we are. I don't think we've really decided whether it's for us or for the future.

We've had many, many proposals as to what to do. Almost all of them, as far as I can see, with the exception of the Alaskan, Inc. kind of distribution of income, would appear to have no real benefit for the people who are in Alaska today in terms of improving the general quality of the life of the mass of the people and their standard of living, perhaps even for future Alaskans. Most of them would tend to make Alaskans more numerous rather than better off.

I'm primarily concerning myself now with the investments and how the capital is put together rather than the income and how it is spent. I think it would be a terrible shame if we said that the main impact on the day to day life of the average Alaskan was, he got stuck in a few more traffic jams and was three deep at the Russian River instead of shoulder to shoulder. At the present time, I'd say that we're likely to be three deep. That bothers me because for better or for worse, Alaska owes nothing to the New York City bond brokers. It really does not have an obligation to

provide a job for everybody who wants to come up here to find one. Indeed, the panelists and their comments about labor mobility are all too correct because people will come up here to take advantage of these things. The average Alaskan will, in fact, not be better off. The goals for both income and investment, again separating them, should be to use them both to directly benefit and encourage today's Alaskans to have a better quality of life, more prosperity, and hopefully to do so, I think we can, in such a way as to build a tax base so that we will be able to continue that higher quality of life and standard of living at such a time in the future for our grandchildren when the oil runs out.

What I'd like to do very briefly is throw out my comments on the major proposals that I've heard in the most summary form and tell you why I've come to these conclusions.

Let's take the development bank project and let's talk about spending \$1 billion for a big power plant or some huge, massive traditional development bank. No matter what we call it, once we set up a major, highly financed development bank, it's going to function like a development bank of projects. I find it very difficult to believe that a dam that's going to take 20 or 30 years to build is going to have any great impact on the quality of life of people now living in Alaska. It's true that when the

thing comes on line there'll be more electricity, I assume that that will then generate electricity for the additional people who are in here building the things that the public development bank has promoted. The average Alaskan even then will be in no way better off.

In any event, such projects, for better or for worse in today's world, would be built by Washington, if they had any sense or any merit at all. The Corps of Engineers has never been known not to build a public works project if they could, in any way, be justified. So the fact that we would build those that they wouldn't, suggests to me, that we'd have a rat-hole factor there that would be monumental; approaching infinity, I think.

Big projects like that probably ought to go in front of the voters and certainly can be bonded by the legislature and discussed at the legislature and put on a bond issue if they really have merit, and we just can't get Washington to provide them the way they would for all the other states in the Union, if for some reason Washington will start to ignore us in that fashion, then the legislature can take action. I really don't see any need to have a development bank for major, huge subsidy projects.

There's also the possibility of gilt-edge investments,

maximum income. I find it hard to believe that pouring all that money into buying little white pieces of paper with I.O.U.'s from such major first class things, that we would have bought five years ago, as New York City bonds, would really do much for us, or in a sense, do much for us in terms of income being generated. In the future, I suppose that we would have the income and what they did to New York City, I assume, that is they would tend to migrate in and take advantage of the services provided with the lower taxes and/or higher revenues. I'm not so sure that in some years accumulating investments through the bond market in order to build a New York City is exactly what we ought to do.

There's also the suggestion that we ought to make such things as direct loans and guarantees to Alaskans and Alaskan businesses, and that has some merit in it. The trouble is that if we make them directly, there's too much chance that the loans and guarantees will be made on a political basis instead of an economic basis. Everyone who has a good loan will go to the bank; everybody who has a bad loan will go to the Permanent Fund. The net result of that is going to be that we will probably lose a lot of our capital. The Permanent Fund will unnecessarily be saddled with a great deal of public disenchantment. Overall, it's a net loss, I'd like to make

a suggestion which might kill the two birds that we need to have killed. That is to provide benefits for Alaskans as well as benefits for future Alaskans without having that kind of risk involved.

What I would think we should do heavily, at least with some of this money, would be to put it into the financial institutions of Alaska that are here today for the purpose of making the banks, the savings and loans, the credit unions, whatever the financial institutions are of the economy today and those that might be established for the purpose of making low interest loans in certain areas, certain socially desirable areas.

The one that particularly springs to mind is housing. It's very important that everybody realize that financial institutions do not make their money because there's an absolutely high level of interest such as 10% or 9 5/8 or whatever the rate is. They make their money on the spread between whatever it takes and whatever they loan it at. Getting it at 7 and loaning it at 9 gives them the same profits as getting it at 2 and loaning at 4. It's the risk differential and the administrative costs that must be covered. The Permanent Fund could definitely provide very low interest loans to the financial institutions to handle such things as making loans to the village utilities

if that's socially desirable, or any other things that would be so enumerated. Housing, what have you? I would really suggest that this should be done. If we can improve the quality of life for Alaskans by letting them have better housing, that's something that can be done immediately and will affect the whole mass of people. It's also building a tax base. The same thing through lower utility costs. It is a form of subsidy which will get out to all the people whereas a major subsidy that just causes one or two big dams to be built or major capital projects will fundamentally benefit a handful of engineering companies that are headquartered in New York City or wherever the major engineering companies are headquartered.

I submit to you again, that our responsibility is to Alaskans and to improve the quality of their life. It is not to provide jobs and incomes for people who do not live in Alaska. If we can build the tax base for the future through such investments and subsidies, and that's what they are, and simultaneously provide an access to a better quality of life, and the one thing we see right now in the economy of Alaska is a massive move toward the upgrading of housing. I would submit that that is an area in which the legislature and everyone else needs to take a very serious look.

The only other thing I would say is, please notice

that I'm talking about the investments in the principal in the Permanent Fund. I am not talking about how we ought to spend however the income comes. We should seriously consider such things as Alaska, Inc., or variations of that if that is politically impossible, which would get the benefits back to the people directly and not send them into a few large projects that are oriented towards outside the state and very delayed benefits.

This economy is growing and our grandchildren, no matter what happens, are going to be richer than we are. I'm not so sure we need to starve everybody in order to make them even richer.

GRUENING: Thank you for that optimistic outlook.
Barbara.

BERGMAN: Okay, I'd like to say a few things about Dr. Lindauer's remarks. There's a little confusion on whether present day Alaskans are too well off or not well enough off. Here you've got the oil revenues coming in. One sort of rationale, we're segregating them in the Permanent Fund is in some sense we're too well off. That is, the present day Alaskans are lavishly provided for in terms of public service if the money were not put into the Permanent Fund. What that would argue is that some of the

money should go into the Permanent Fund again primarily for the benefit of future generations of Alaskans. Some of it should not go into the Permanent Fund, some of the revenue should be used to lower taxes for example. That's what that would argue.

Now, I think that Dr. Lindauer shouldn't be allowed to get away with this implication that if the money were invested in the gilt-edge type of program, New York City bonds would have been bought with it.

LINDAUER: Five years ago they would have.

BERGMAN: That would not have occurred because they are tax exempt. It would make absolutely no sense for the Permanent Fund to buy them. More seriously, I think, what he's suggesting is that somehow or other the managers of the Permanent Fund would be poor in terms of that kind of investment. Even I'm smart enough not to have bought any New York City bonds. My record in the market is not too great.

LINDAUER: That's not what I suggested.

BERGMAN: I don't think that's a fair implication.

LINDAUER: I didn't mean that implication. Let me tell you

what I meant. I meant that if we send billions of dollars out of this state and get back little white pieces of paper that 30 years hence are going to give us some income when they mature, we're going to have little white pieces of paper here and damn little else. We have people who might rather have a better housing situation. We don't need to have additional spending to have local citizens make investments of their own in housing. There are a lot of people who apparently would like to have better housing. I see no reason why they should be denied that.

BERGMAN: That relates to the issue of how well off the present day Alaskans are. Do they have needs that ought to be met out of the present day oil revenues? What you're saying is yes. I think, that's something that is essentially a political question that has to be determined.

Now, there's sort of a subrosa question here which hasn't come out explicitly, perhaps it has, I think it ought to be out and discussed a little more, that is the problem--do you want to give benefits to the present citizens of Alaska and positively avoid giving benefits to people who will migrate subsequently or people who have migrated recently? There are pros and cons on this. Even if you

restrict the present benefits to people who are citizens of Alaska now---and by the way, I am thinking of renting an apartment and moving my voting residence here before the grandfather's clause takes effect---but seriously, if you do that, you are going to create a two class economy. Some people are going to move here subsequently anyway. There are social problems with that that would have to be faced. If, on the other hand, as has been ~~said and said~~ ^{said correctly} many times, you provide the benefits to whoever is to come here that will to some degree encourage immigration. That might be bad because it would spread the benefits more thinly, but also because it could be said that those people have no moral right to it in some sense. That as a practical matter you are going to end up having to give benefits to whoever is here, even if some of them have been brought in because of the generosity of these programs. I don't think you will want to, or can afford to, set up a two tier system where some people of priviledged nobility and other people are pariahs.

LINDAUER: I think you have misinterpreted. What you've done is you've gone back and you're confusing the discussion of how to spend the income with the question of how to invest the principal.

BERGMAN: No. Those are two different comments. Perhaps, I should have said I'm now moving from the area of how to invest the principal to the area of how to spend the income.

LINDAUER: I didn't really discuss how to spend the income. I have my own value judgement, without thinking it through, I would use it to have a form of property tax relief to encourage, again, the average citizen, who is in Alaska, to benefit by being able to afford a better class of housing, if that's what that person wants.

I was discussing the question of how to make the investments of the principal of the capital of the Permanent Fund and suggesting that we would be better off if the principal, wherever possible, was invested in Alaska in such a way as to build a tax base and in such a way as to benefit Alaskans. I still believe that we owe nothing to bond brokers in New York and we owe nothing to a handful of engineering companies who would come up here to make major capital projects and bring in itinerate laborers who would come in and out, we would get little, if any, benefit from this. I'd rather see everybody living in a better house, if that's what they want or having decent utilities in their villages, if that's what they want.

BERGMAN: Well, some of that itinerate labor is going to be required to build those better houses.

LINDAUER: That's right.

GRUENING: I would like to ask one question and that is how hungry is the audience? We're getting to the more important part of this symposium and that is letting the very patient audience get into the fray here and ask questions of whomever. We can go another half an hour and then break for lunch and come back if there are still questions to be asked. We can break right now. I'm asking for the Quaker sense. What do you say sir?

MAN (UNIDENTIFIED): I'd like to make a comment and ask a couple questions, but considering the time-now that he's had a cooling off period, I'd like to refer to Mr. Gallagher and let him make a comment in response.

GRUENING: Okay. That's fair enough, but I want to hear how hungry the rest of the group is. Representative Carpenter.

CARPENTER: We may not necessarily be hungry, but there may be other reasons to leave the room.

GRUENING: We don't have a sign out sheet. Anyone can leave. Okay. Sterling, you can make a remark if you want. We'll be back at 1:00 o'clock sharp. We have some people who need to catch planes. We can maybe wrap it earlier this afternoon. Thank you. I urge you all to come back because I think it will be the more interesting portion this afternoon.

LUNCH BREAK

GRUENING: We'll try to wrap this thing up in a time that's appropriate, we won't drag it out. Dr. George Rogers has to return to Juneau tonight and the last plane leaves at 3:00, so if you have any questions of him, specifically, you should ask them first. Before we open it up to general questions, Dr. Lindauer wanted to clarify a statement he made and from that point on you can ask any questions you want of the two economists, the panelists, or the legislature, for that matter.

If you have specific proposals for investments, I think we're also interested mostly in your philosophy for why that is a good thing for the Permanent Fund to do and why the Permanent Fund as opposed to maybe the general fund or the revolving loan funds that are created from the

general fund could not do it as well.

I only have one comment on what's transpired so far and that is it appears to the extent that the Permanent Fund becomes active in the Alaska economy, intervening in the Alaska economy, we have increasing problems with how to fairly distribute the subsidy, if there is one applied in the loan, and how to manage it in a way that it's accountable to changing desires in needs of the people. It doesn't mean that we shouldn't do it; it just means the problem is a little more difficult as the Permanent Fund becomes active in the economy. You may want to have a comment or a question on that. As long as the panelists are here, you might as well get your questions out first. Dr. Lindauer.

LINDAUER: Somebody asked me a question which led me to think that something I had said had been misunderstood. It had to do with development banks and development bank projects. My concern is not with the establishment of a development bank per se, particularly not with the establishment of a development bank kind of analysis of projects. My concern is with the kind of big project that one finds the World Bank engaging in. Something that would be a \$5 billion hydro project that would have overruns to \$8 billion. Something that would be a single project or a handful of projects which would be an all or nothing kind of use of the Permanent Fund monies. I am particularly opposed to

putting all the money into a big project such as a major dam. I am certainly not opposed in any way to the establishment of a development bank concept to analyze various and sundry projects.

GRUENING: Thank you for clarifying that. When you come to ask questions, please come to the microphone. The lights now are provided and the cameras are provided by Media Services, which is producing a program that may be used on channel 7. It'll be put together so you may see yourself on T.V. We also plan to do a transcript on this hearing. So when you come to the microphone, please identify yourself. If you wish to do so, tell us your occupation. Yes, sir.

GERSTENFELD: My name is So: Gerstenfeld. I've been in this neck of the woods about 30 years, so I've done this, that and the other thing. I've done some visiting Outside and kept coming back. Along the lines that Jamie raised, the thing that concerns me the most is not just how much we spend and how much we take in, but what we get for our money. I would like someone to explain to me how come criminal justice is a better investment than consumer protection?

GRUENING: Anyone want to take a stab at that?

HAVELOCK: I don't think that they're mutually exclusive objectives. Historically, over the last few years, there has been more of a trend. If I understand the question, my comment is simply, the trend in the direction of the question is addressing.

GERSTENFELD: Trends don't happen; they're made.

GRUENING: Okay. Trends don't happen, they're made. Now if you have any comment with which to follow-up your questions, I'd invite the audience to do that. As long as no one's making a long speech, there's time to follow your own question. Are you satisfied? Does anyone wish to comment further on that? Okay. Does anyone else have any questions from the audience?

CUC: Two questions. First, just a general information question.

GRUENING: Identify yourself please.

CUC: Okay. Dennis Cuc. Specifically, with the oncoming gas production and new discoveries that will be found in Prudhoe

Bay, how much extra are we going to have in the Permanent Fund? Does the Permanent Fund just anticipate Prudhoe oil and gas or does it anticipate other discoveries at all?

GRUENING: I can answer that. The amendment applies to all oil revenue produced through royalties and leases and bonuses on state land, so that if the Beaufort Sea, for example, were sold next year for a bonus payment, 25% of that bonus payment would go into the Permanent Fund; and if it were sold under the same arrangement where the state gets 12½% of the oil or the value of it, then 25% of that would also go into the Permanent Fund.

But, I think the impetus for the Permanent Fund was the vast wealth that people saw coming out of Prudhoe, although other revenues are subject to contribution. The projections that you see in that little green book that some of you picked up, and there are more out there, if you want them, are based strictly on Prudhoe Bay.

CUC: My second question is for Dr. Lindauer. Do you think the banks are willing to enter into some kind of arrangement with the state whereby the state does provide monies? Do you think the banks, as a private capital

resource, would be interested in this proposition?

LINDAUER: I would think yes. By the very definition of what you just said. They tend to be private, profit-making corporations. They make their money on the difference between what they pay for it and what they charge for it, not on the absolute rate. So that it would be very profitable to a bank to make low-interest loans if it can get the money at an even lower interest loan. Then again, let me tell you, I'm not just talking about banks, I'm talking about all financial institutions including state mortgage agencies and all related, anything that is presently acting as a financial institution could conceivably take money and put it into whatever the legislature thought was a good idea.

CUC: I haven't done any research on this and the only reason I ask the question is because the Commissioner of Revenue seemed to indicate he is a banker, of course, he was a banker. He seemed to believe it wouldn't fly. You haven't talked to him about it to find out the reason? I haven't either at length.

LINDAUER: I did speak very briefly with him during the lunch hour about that, and I think one of the things that was

discussed was the capital requirements of banks. It may well be that there would have to be enough profits involved in the break to generate additional capital so that they could continue to expand. I think that we're really talking about a conceptual thing here. The question of whether the money should flow through the Alaskan financial institutions or should it flow through a bond brokerage house in New York City. Other things equal, I'd just as soon let the Alaskan institutions make the money.

GRUENING: Thank you Doctor. That's a worthy objective, I'm told and I don't have the information before me, that when the \$900 million was deposited in local banks, most of it went Outside. Somebody may wish to comment on that.

BERGMAN: Let me say that when money is deposited in banks, the first thing they do is buy government bills with it.

GREUNING: Why is that?

BERGMAN: They want to expand their loans very quickly. Because very prudently they want to take care to see that they're good loans. So when they get a sudden big deposit,

what they will do is put the money to work in a relatively riskless way, which is the government bill market, where the funds are liquid and they get a rate of return. It's open to the Alaskan government to buy its own bills instead of putting large sums in interest free accounts, even temporarily. With large sums so that even putting them in interest free accounts for relatively short periods can lose a lot of money. Now you know, I hear sort of contradictory things. In one ear, I hear that you're so rich it doesn't matter, and with the other ear, I hear that you have a lot of slums that need attention and so on. No matter how rich you are, it's foolish to unnecessarily enrich bankers, even Alaskan bankers.

GRUENING: Any bankers in the crowd?

BERGMAN: I must say with respect to brokerage houses that Dr. Lindauer is warning us against, they now do negotiate down commission rates. So I'm sure, that for an account like the State of Alaska, one would get a rather low rate.

LOVE: I think what we are getting into is sort of technical discussion as to whether or not the Permanent Fund working through the banks buy CDs or whether they buy loans or whether they sell CDs or buy loans. I think what Clark was talking about, at one

point, they take the certificates of deposit down to the banks, hoping they'd make some local loans. Sterling Gallagher, I think, was quoted once as saying they put the money Outside into treasury bills outside the state to make a profit. They could also accomplish what Dr. Lindauer wanted to do by purchasing loans on the secondary money market, thereby ensuring that the loans were properly qualified Alaska investments under certain criteria. I'm not speaking so much to his proposal, but I think we're getting into a technical area, I'm not sure how helpful that is for the general audience in terms of discussing some of this stuff. I think there's probably different ways of accomplishing what Dr. Lindauer was talking about other than putting money in CDs.

LINDAUER: I never advocated putting money in CDs. In fact, quite the contrary. My whole point is that if you channel it through some restricted beneficial way to limit the loans not by CDs but let them draw on money they're willing to loan out at some lower rate of interest. The loans that they otherwise would not make--it could benefit Alaska. The whole thing is to keep the benefits and orient the loans within Alaska--not just throw them in the national economy.

MEEKINS: There is a precedent to that in terms of link deposits that, I understand, Colorado did that with their state deposits. They give them under the condition that they're used for certain purposes. I think that's one vehicle.

GRUENING: Sir, did you have a comment on that? It's open to the audience. Just come to the microphone.

FISKE: I am Roy Fiske. I'm a retired Lieutenant Colonel and a 15 year Alaskan. I think that what you've just been saying here on restricting where you make your investments can be legislated, and the money we're talking about could be put in the hands of Alaskan institutions with restrictions on it that it be invested in Alaska only and at specific rates. That specific amount of money, while it's in the bank, would not necessarily be handled the same as the other funds of the bank. I would like to later on make some further comments, if I may.

GRUENING: Sure, you may. Thank you very much. Mike, do you have a comment?

DOOGAN: Yes, I'd like to get back to a slightly more general question. This is directed more or less to Dr. Lindauer, but just generally to stated goals of the fund. When you discussed

making loan interest loans to Alaskans using the principal that way, taking the earnings and distributing them to Alaskans in some sort of direct manner, you raised the question of tradeoffs. You have two goals and they can, on this scenario, be accomplished; but you have to decide what your first goal is. If it's to put the most possible money in the pockets of Alaskans, obviously you don't make low interest loans, you try to make as much interest as you can, because you can put more money in. If it's to build houses, then you have to sacrifice the goal somewhat of putting money in the pockets of Alaskans. So the question is when you made that sort of proposal, what was your primary goal?

LINDAUER: When I first spoke, I said that we really had things divided into two separate parts--the question of how to spend whatever income came and the question of how to take the principal and how to build up the principal. I don't think the goals should be maximum. I don't think that was what the voters voted on. The voters voted on putting it into income earning things. You can earn an income at 3 or 4%; you can earn an income at 6 or 7%. Whatever the managers of the fund decide is the socially responsible thing to do should be what we do. I would, person-

ally, do not think that we should go for the high risk investments that would conceivably yield the highest incomes. I think that we should consider that how we invest that money is going to be as important, in my view even more important, than whether we get an extra one percent on the top by taking some risks for the money. Last time we took some risks I understand there were some big losses. You get more interest when you take a risk as a risk premium. Should we really be risking it? I think there should be something in between the final recipient and the state as a guarantor of the repayment of that money, so there is a guaranteed income. That's one reason, I like financial institutions, because if the loan goes sour, it's their loan that went sour. They would owe the state whatever they paid to get that money.

BRADNER: I have a more general question. What is the status of the definition of income producing? Are you going to try to do this through your statute? What's your present thinking about it? What are the words of the initiative? I can't quite remember.

HAVELOCK: Some currency depreciates very rapidly.

GRUENING: Down to zero? It means some interest. In other words, you couldn't do it, say, argue indirectly, give it as a grant and say, "well, that's incoming producing because they'll be side benefits." It has to produce some income, but it doesn't say how much. It could be anywhere from 1% to 10%. As a legal matter, I don't think you could argue it could produce no income and be income producing, based on kind of a spent off benefit thing. The interest range is wide.

BERGMAN: I'd like to say just a few words about the trade-offs. Say you take a million dollars and you subsidize loans in Alaska, or you take a million dollars and you invest it in treasury bonds and make a better return on it. You're giving up something in each case. Presumably the benefit is to the person who gets the concessional loan, and that, very frankly, tends to be middle class people. They're the ones who qualify even for concessional loans. What you're doing, in effect, is you are giving a benefit to a middle class person and sacrificing a benefit, as a result, for the beneficiaries of the income, which is the whole population. I don't say you should never do it. There may be very good

reasons to do it. But you have to be clear that whatever track you take, there are going to be costs and there are going to be benefits. You have to see who gets the benefits and who bears the costs. They're generally not the same people.

MC CUTCHEON: I'd like to ask Dr. Rogers a question before he leaves.

GRUENING: And you're Jerry McCutcheon.

MCCUTCHEON: Yes, Dr. Rogers, you raised a question of the philosophy of the Permanent Fund, and you never stated what your opinion was. Why do you believe there should be a Permanent Fund? Divorce it from whether or not political tricks were played in the voting process, or who introduced bills, and aside from all that stuff, strike all of that and get down to why there should be a Permanent Fund.

ROGERS: The purpose of the Permanent Fund--we're faced with an unusual situation, or what seems to be an unusual situation in which we have for a period of time the prospect of drawing upon resources that belong to Alaska in this case, they're state land, that will be depleted over a period of 20 to 30 years. The benefits

of these, if they are not put into a Permanent Fund, would be used for current expenditures, current benefits. One of the underlying things, I think, of the whole idea was that this was a way of creating a nest egg, which would be available, which would share some of the benefits with future generations. The other thing was because Alaska has been through boom and bust cycles in the past, we have this fear of there being a let down right after a particular period of prosperity comes to an end. Most of our past development has been gold, defense, construction, the Alaska earthquake briefly, and then oil development. Each of these have had different cycles. So the idea of creating this fund as a cushion at the end to give us a basis for moving..

MCCUTCHEON: I'd like to ask my next question.

GRUENING: Let him finish. Are you finished, Dr. Rogers?

ROGERS: That's one of the underlying points of creating a Permanent Fund. The other is, of course then we get into the use of the money. I think we've all talked about it this morning. But you asked me what the basic idea was. You had another question.

MC CUTCHEON: As to your anticipated number of years, I would suggest you get the State of Alaska's report of January 1976, having to do with the production of Prudhoe Bay Oil. I've got one question, why do you think this anomaly, this variation, or this large income occurred? Why is it occurring?

ROGERS: It's occurring because the oil industry is coming up to Alaska because of the energy shortage. Is that the sort of question you're asking?

MC CUTCHEON: Well, you're getting close. Why has it occurred? Tell us why it has occurred. Why couldn't it be level?

ROGERS: Why couldn't the income be level? Because there's an immediate national need for the resource, the energy resource. It's being developed during this period.

MC CUTCHEON: I understand the need for the resource will be greater in 1985 than it is today. If that is the case, will we not need it worse in the future than we do today.

ROGERS: You see, these are decisions over which we have no control.

MC CUTCHEON: I see, you say we have no control. Who does control those decisions?

ROGERS: If I understand your deep question which is emerging, is why do we develop oil today? Is that the question?

MC CUTCHEON: That could be one of them.

ROGERS: That is a good question. We had an alternative. As a state, we could've withheld those lands. The decision was made to develop them.

MC CUTCHEON: So in relation to the Permanet Fund, where does this fit with the philosophy that apparently we could not control?

ROGERS: The control of the timing of the income generation is what you're getting at, isn't it?

MC CUTCHEON: Correct.

ROGERS: We had a voice in that. It's a political

decision that was made. I don't think that, if put to a vote, the people would have come up with an answer different than the decision made, but that's a speculation. You're correct. The income is being generated now because the decision was made to develop the oil or to put the state lands up for lease.

MC CUTCHEON: Would you think then it might be prudent as far as the state is concerned not to have any further lease sales? In other words, not to enhance the Permanent Fund?

ROGERS: Yes. I think it might very well be prudent to do that.

MC CUTCHEON: Then the Permanent Fund can be considered in two ways. That which is resources you own, and that which is postponed?

ROGERS: That's right. Yes, it's one way of giving the resources that you're giving up now a life after death.

MC CUTCHEON: Thank you.

GRUENING: Thank you, Jerry. Are there any further questions?

MC GINNIS: I'm not clever enough to turn all these into questions, so I'd just like to make a couple of statements. My name is Tim McGinnis. I'm a citizen of the state of Alaska.

My first comment is that I believe that the Permanent Fund arose more in response to a political situation than an economic one. Here in Alaska since 1969, the question has been most often left by the outs wishing to get in the political structure. What has happened to the \$900 million? If they had devoted as much research or as much to research as they did to rhetoric, they could have found out what happened to the \$900 million. Again, and again, we hear, "What has happened to the \$900 million?" Even though everybody knows. I think in response to that, a lot of political people, generally liberals afraid of a conservative challenge, said, "let's make a Permanent Fund." A lot of the questions we're addressing today are the results of that kind of dichotomy between political need, which may or may not have reflected a true economic need.

My second point, from what I've heard today and what I, as an Alaskan, have been coming around to in the last couple of years, is that we really don't want the money. What is it going to bring us? More people. We've heard that from every edge of the room today. What is it going to

bring us?

There is an important qualification on that, which is we don't want the money now; but we do want it later. So that's one of the things that has to be worked around.

Something which hovers in the background of the entire Permanent Fund discussion up to now, is the question of what percentage of those monies subject to the Permanent Fund are actually going to end up being used by the Permanent Fund. Will it be 25; will it be 50; will it be 75; will it be 100? I think that it's absolutely the most important decision to be made right at the outset. There are numerous arguments about which is cart, which is horse; but the principal first effect of the Permanent Fund will be these vis a vis the general fund. There's been a lot of talk in this room today about how we don't need any more government growth. Obviously making 100% Permanent Fund would have quite an effect on slowing government growth. That may or may not be a worthy goal, but to bring all these comments to a head.

There is one kind of quality, we've been talking all day about social quality, we've been talking about economic values and investments. But no one has really touched on the subject of environmental quality. I would like to suggest to you people today that the Permanent Fund could be used to buy back Alaska.

To buy environment quality for this state. We all heard about trade-offs. It's a favorite economic word. We've heard about externalities. I'm not going to tell economists about externalities: they all know about it. The fact remains that our resources are not being developed by the same people who hope to profit by them or by the same people who would hope to keep a reasonable level of environmental quality while those resources are being developed. BP Alaska or the Alyeska Pipeline Service---they have their own, very rightly so, idea of what trade-offs are going to be and what they consider to be a wise trade-off. The Alaskan people are almost in a hypocritical stance because they want the values that come with oil development but they are screaming to high heaven about the environmental trade-offs.

Once in a film a fellow made the comment that Alaskans want wilderness at the back door and civilization at the front door. When someone moves in behind them, they've got a problem. That's one of the best comments I've ever heard on that matter.

To continue with the idea of environmental quality and trade-offs, I'd like to suggest some concrete things which have been brought up by the conversation of our last speaker, one of which is that the state of Alaska could buy leases, oil leases, with the Permanent Fund. It could've bought the

entire Northeast Gulf for half a billion dollars, that's one sixteenth of an \$8 billion Permanent Fund. We could've held it off the market. We could've particularly held off the market those tracts that were environmentally sensitive; and, when the time arose when we needed more development in the state, we could then have begun to develop.

The second thing, and this has been brought up before, Russ and I have talked about this before, is we could have decided unilaterally two years ago that we were going to build the Alaska gas line. Would Congress have told us not to build it? If we were going to invest \$4 billion building a state-owned pipeline to Alaskan tidewater, would there be an Alcan line now?

I think the most dramatic results of the Permanent Fund could be control over how those resources are developed. That to me is more the essence than the money which might conceivably come from those resources. We could control the environmental stipulations to a much greater degree, not only in terms of the letter of the law, but carrying out that intent if we were ourselves the owners and controllers, not of the conversation that was just here, control the sequence and the timing of development of resources if we do truly own them. A lot of our problem right now is the federal government can't control that; but we could form ourselves an oil company and bid against anyone who wanted to develop our resources before we did if we were lucky enough to cal-

culate what they thought they were worth and put ten more dollars on top of it, we would have control of it.

One of the conflicts here is that if we set up 100% Permanent Fund in order to try to keep state government from growing, we may unfortunately put into higher gear the mechanism of development, which has been the need for state revenues, that is by putting 100% in the Permanent Fund we might make the Beaufort Sea be sold 15 years earlier. That's a conflict, I recognize that. In many cases, we can't control that development or its speed or its tempo. We haven't even really wanted to, we've been so greedy. We want it all right now. We've got a long time to go in this state. A couple thousand years. Oil is going to get more valuable, everybody knows that. We're holding it as a national trust. It's nice that the Carter administration has the moderate views it has about development. But we had better, after Carter, get ready for another Nixon. Somebody who, you know, doesn't care about what's in the Northeast Gulf--somebody who doesn't know anything about, well, this wasn't federal, but somebody who doesn't know anything about Kachemak Bay and why not to put an oil rig there.

My faith in Alaska is the faith that we can control our own destiny, but in order to do that we may have to remodify

our idea of what is income producing or when it becomes income producing or when we would like it to become income producing. To me, that is one of the outstanding possibilities of the Permanent Fund, which so far, has not been touched.

One more comment, which is simply that it's really an \$8 billion Permanent Fund or \$10 billion or even \$6 billion, the impact on the state is going to be as incredible, as if we were creating an entirely new state government. The last time we created a state government, we had a constitutional convention, a couple years of debate. This time we're creating a Permanent Fund with an audience of about 25. I would hope that by the time we actually come to making those decisions about the Permanent Fund, that something of the scale of inquiry of a new constitutional convention will be attempted because it's going to be that important to the state. Those are my comments.

GRUENING: Tim, could you stick around for some questions? That was a very thought provoking statement. I think Mike has one question. We'll open it to the audience themselves. If the audience has questions of the participant without getting into an argument, they can ask them.

DOOGAN: It seems to me, that your statement hasn't really so much given us a solution to the problem of what to do with the

Permanent Fund, but rather to speak of Alaskans as though they were a homogeneous group. The Committee's goal is to try to get some sort of an idea of what Alaskans in general would like to see done with the money. If you postpone that just by saying we'll use the money to buy oil leases, then we'll have to have another committee with a different name trying to figure out when people want the oil leases sold.

MC GINNIS: That seems to be the nature of government; a committee about a committee about a committee.

GRUENING: Tim, I had one question. I agree that the question of the increased contribution to the Permanent Fund whether you're going to raise it above the mandatory 25% set in the constitution is important. I think you implied this in your statement, but I'm checking. Shouldn't we decide basically what the goal of the fund should be or what we think it should be before we decide to increase the contribution. If in fact a lot of these goals can be achieved through the general fund, why put it into the Permanent Fund unless that has a special goal? Shouldn't we determine that first before we increase the contribution?

MC GINNIS: I'm going a little bit backwards from your

deduction, which is I'm saying that it might better be put into the Permanent Fund as a place to put it when we don't know what to do with it, rather than to put it in the general fund when we don't know what to do with it. What I'm saying is that one of our big problems here, we spent all morning talking about how to keep people from coming to Alaska because we've got so much money. To my mind, that's the vital question about the Permanent Fund vs. the general fund.

MEEKINS: Tim, you mentioned, and I think it was a very good point, that one of the effects of putting 100% into the Permanent Fund may be, at some point, thereby reducing the surplus in the development of other areas by leasing oil leases or other mineral leases or any other resources the state owns. I think that's a good point. I'm wondering what you'd think about it in terms of, if I could remember my question now that I've said that. I'll come back to it.

GRUENING: Tim, you had a question, why don't you ask it?

BRADNER: I just had a question, Clark. The way the thing is now written, is it possible for the legislature to annually increase the amount of money into the Permanent Fund or does it have to be done by legislation. For instance, if the Finance

Committee were to find that they bent the budget for one year and there was X amount left over, could they, by resolution, put what was left over of the excess revenue that year into the Permanent Fund? Or does it have to be a set percentage?

GRUENING: Not by resolution or at least that's debatable, but by a bill which could be a budget bill, it could put additional amounts. In the constitutional amendment it does say at least 25%, which has interpreted to allow the legislature to make a higher contribution.

MEEKINS: I remember what I was going to say fortunately. I'm wondering if you find that same logic to Alaska, Inc.? Do you think that having an Alaska, Inc. proposal that you distributed money from the Permanent Fund investments to the public would have the same effect of generating an enthusiasm for selling the Beaufort lease sale so that 25% of those monies or 50%, whatever the contribution rate, would then go into the Permanent Fund and their shares would increase in value and that that would generate its own? I'm just trying to follow that logic out as applied to Alaska, Inc.

MC GINNIS: It's a definite possibility. Whether it's

Alaska, Inc, or any of a number of other things we've got in mind. It all goes back to whether we really want the money.

GRUENING: Any further questions? Jerry.

MC CUTCHEON: You raised the question of investing \$4 billion in gas line. I keep hearing about Alaska putting money in the gas line. Are you aware that the state of Alaska is--it would cost \$16 billion for the gas line. And there'd probably be an additional \$3 billion. And what would the cost of gas be and why when at Tidewater?

MC GINNIS: \$19 billion.

MC CUTCHEON: inaudible

MC GINNIS: I'm not sure that they have. El Paso--I guess they're not an oil company, they're a gas company, but they sure wanted it.

MC CUTCHEON: inaudible

GRUENING: As I understood the proposal was illustrative only of the type of resource investment that could be gotten into. I

have had enough of royalty gas right now. I hope we don't get into that debate again.

MC GINNIS: One variant on the proposal--we don't have to own 100%; we may not, in order to exercise effective control, even have to own 51%. We might do it with 30. We might be just a greater among many equals. I'm talking about co-venture as well as outright ownership. I don't feel that you're ever going to get a company from outside Alaska, wherever it's from, however many ads or dog races or whatever it is they sponsor to tell the way the Alaskan public is going to care. If the Alaskan public doesn't care, then we might as well bag it.

GRUENING: Thank you. Panelists or anybody can come up.

BRADNER: I have a question I want to address to you and Russ. What are the pros and cons more or less of money going into the Permanent Fund? Do you think it's a good idea to increase it to 50% or 75%? What do you see as disadvantages or advantages of that?

GRUENING: I'm not dodging the question, but one of the things we're trying to find out...I personally think you have to find out what you feel basically are the major goals. I

have some opinions on that. I haven't concluded yet to what the percentage ought to be--increased or remain the same. It's something I want to wait on frankly. That's my answer to it. I think I'd like to hear more from the public as to if they think it should be increased, why they do.

MEEKINS: I think one of the purposes of these types of things is to get some input on that question. We, of course, have spent a lot of time thinking about it. It's sort of funny because at the same time we need to make that decision up front, because a lot of things depend on it, we have very little information upon which to base it. We don't know what the prices of the oil and the tariff and all those things are going to be so we can't really project what our revenues are going to be. At the same time, we don't know what our population increases and our expenditures are going to be, or even our needs. So we don't know what our budget is going to be. Really our judgment on how much extra we're going to have to put one place or another is not very accurate at this point. So it's very difficult to say put 100% of it in. I guess we could always change it, but we're sort of in a dichotomy of wanting to do it up front and not having all the information we need to do it.

HAVELOCK: I just want to say since you don't know what you're

going to use the money for, it's absolutely insane to raise the percentage of money your're going to dedicate to the fund. Supposing you assume the purpose of the fund was to control random government spending of windfall funds, but you don't want a fixed percentage anyway. That is, what you need is some sort of a floating percentage that takes excess cream off the top. I assume since you feel that the legislature doesn't trust itself to do this on an annual basis, you need some sort of a formula system for doing that. I would not care to broach on how you put that formula together, but I'm sure that the economists in the room could do it.

GRUENING: We are looking at that, John. It's a complicated problem, but I happen to agree that a formula approach makes more sense than a fix of 50, 75, 80.

HAVELOCK: I'm also concerned. This is something that George and I talked over at lunch. The importance of preserving the distinction in whatever you do between investment policy and spending policy. As you've got all kinds of potential subsidy operations going on if just having a floating category of anything that makes a profit. The fact that you are, in fact, spending money to support housing, or

rural facilities, or whatever it may be, it becomes disguised. It seems to me, from the accountability perspective, you want to have some sort of standard as to what you would do in investment policy, that is, what do you do with money that you don't have a purpose for using to spend on something that would encourage some social end. Establish yourself some sort of an interest rate on that and appropriate the money that is necessary to fulfill social objectives on money which may be loaned beyond that to special purpose programs.

LOVE: I'd like to ask Dr. Gordon a question to briefly respond to some of the comments that Tim McGinnis, the fellow who was just up here talking. He was giving the description of the state using surplus money to invest in the resource industry to gain more control over a lot of management decisions or development decisions. I'd just like to hear you comment on that.

GORDON: I don't understand exactly what people mean by the word "control." By and large, I think it would be a bad thing to invest oil money back in oil. The very simple proposition about diversification, you don't want to have all your eggs in one basket. If you had a little money to put in the stock market, would you want to put all of it in one industry, the future of

which you could not predict. By taking oil money, which you are already getting, and reinvesting in oil, you are increasing the risk.

He made the statement that the price of oil, everyone knows, is going to rise. There's one thing that is clear--- everyone doesn't know what is going to happen to the price of things in general. It may be that oil is a very good investment, maybe it isn't. If you look at the price of oil company stock, it doesn't look all that good. But, I would think that it would be a more desirable thing to invest it widely in a diverse set of things and protect the income and distribute it, as I say, equally. It'll do more for the poor. It'll do more for equality in the state of Alaska than any other proposal I've heard, and I think by a large margin.

BERGMAN: Let me add a footnote to this. I think that Mr. McGinnis is right. I think the environmental problems have been given rather short shrift in the discussion. Then again, I think it's quite reasonable for Alaska to, in some sense, trade-off environmental benefits for either Permanent Fund capital or Permanent Fund income. It's, of course, up to Alaskans to decide what a reasonable rate of trade-off is. But if, as I think I hear, the environment is something that

is of great concern to everybody, then I don't think it's unreasonable to pay great attention to it, to sacrifice some income, possibly there's even some safety to it. I certainly think in terms of future leases, that perhaps environmental impact ought to be given greater stress than they have in the past. For example, insistence be made that people who exploit these resources ought to finance the clean-up or ought to use possibly high cost methods, which to the least damage.

I'm a little confused by the discussion as to whether Alaska's really very poor, or very rich. If we take the view that there is a lot of leeway here, then certainly saving the environment, creating environmental amenities, or not destroying those that exist, should have a very prominent place in the planning.

ROGERS: Clark, I'm going to have to leave.

GRUENING: Okay. Russ wanted to ask Dr. Rogers one question before he left.

MEEKINS: My question is if we are assuming that Alaska, Inc. proposal finally won out and that we were distributing a thousand or two thousand dollars a year to the share holders of Alaska, Inc. proposal, my question is what do you think about

the possibility of the feeding inflation and then that increase in income would just drive up prices and thereby the real income would stay the same.

ROGERS: This is one of the things when you ask an economist that question, you get all sorts of answers. We have first of all, put this into a total context. The distribution of income to Alaska--we have to have the total model of the economy we could relate that to--what would be driven up? It would mean that more money would be spent in Alaska possibly. Whether or not this creates inflation, I can't tell you off-hand because my experience with Alaska has been when more money was spent in Alaska, prices tend to go down because the scale of the market's increased and a lot of offsetting things came into effect. I can't give you an answer off the top of my head. We'd have to relate it to what is going to be going on. But, we would have to consider those things when we're talking about the effect on the economy. I'm going to have to catch a plane so I'll have to make this short.

One point, I just wanted to repeat what John said and what Professor Gordon mentioned. We've got to separate in our thinking the Permanent Fund, the management of the fund

itself, the investments of the money in the fund to create income--separate that from doing good providing loans and providing subsidies. If we do that, it's true we can do it, we can manage it. It puts upon the management of the fund an impossible task of accountability. If it's just a simple matter of preserving the capital, maximizing the income from that, then the annual income would be available for doing all sorts of things. We could throw it out the window; we could build a power plant; we could do a lot of things on an annual basis. That should be left flexible, because what we perceive is our needs are going to change. What Alaskans want will be changing. The whole scene will be changing. But, the management of the fund, as a financial entity, should be subject to straight forward attempt to get the most prudent management possible as a financial transaction. Don't clutter it up with a lot of other ends, no matter how valuable these might be. That's my final point.

GRUENING: Thank you, Dr. Rogers. I know you had a busy schedule. There'll probably be some disagreement with that closing statement. But you can escape.

ROGERS: I'm sure. I'll escape on that one.

GRUENING: Mr. Paul Fuchs, I think had a statement or question.

FUCHS: I'm a laborer and I'm a part time student out here at the University. What I want to say speaks to the philosophy of the fund. I think that we have to get away from looking at it as some way to maximize profit. We have to see how the fund can be used to help stabilize the Alaskan economy. The tool that's usually used by economists in looking at this, I haven't heard much about it, looking at the multiplier effects of different kinds of industries and what kind of re-circulation we get--money spent in certain ways. I think the Department of Economic Development comes out with those figures. They show some industries, like tourism, to be one point something. In other words, that money turns around and goes straight back out.

What I'm talking about the Permanent Fund being used for is to fund projects, let's say, we look not just at housing, but look more at a total system. Let's look at providing development funds. Going in with a native regional corporation to develop a sawmill in southeast Alaska.

(portion not taped)...where people could be sold these houses, giving the savings out along the line. Where now we have all these sponges called businessmen, which are raising capital along the line. I think we need to look at the needs of Alaskans and not at the needs of these companies.

They don't care about our people, only as much as they can make off us. Not just the small industries either. I think we ought to look at some of the large industries, as has been said, so we can control the rate of development more so we don't end up not only with a high unemployment rate because so many workers have flooded in, but we have such high population influx completely tears our cities apart. Where crime is just you know. Anchorage is not anything like it used to be. That's a reflection of that. That's a social cost that means something to Alaskans.

Another thing, I'd say is that you can't trust the current banking structure to manage these loans and just turn the money over to them, because what they've done is they have not used it in rural Alaska which needs the money more. Sure the bankers in Anchorage are rich. But when you go to the villages, any of them, even the ones that are better off, I think the living conditions that people just wouldn't believe, if they actually saw it. I think we can't leave it to them. If they manage it, to make the most money or if the Permanent Fund is managed to make the most money, the money is not going to be put into projects where it's needed most--like fishing cooperatives and things like that.

The other point I want to make is that, I think some of the forms of economic organization that we have seen here lately, like the development of some cooperative, is an important concept for

the Permanent Fund to look into, especially in the native villages, where it more lends itself to the cooperative culture that is already among the native people and also among non-natives. I think it's an important concept that we start, just people work at a place; they elect their management; and they decide on the work process, rather than having it shoved down their throats. People who are working on the line live with this every day. I think if you could look towards that, nearly the whole social picture of what it means to live in Alaska, I think, perhaps, the Permanent Fund could be used towards this end.

GRUENING: Thank you, Mr. Fuchs. Could you stay for a few questions. Mr. Doogan.

DOOGAN: It's not so much a question. I just would like to again restate my comment that I made after Tim McGinnis finished. We have a tendency to talk about Alaskans as though they were one thing. Let's put it like this. Bankers who live in Alaska, no matter how greedy or conspiratorial they might be, are also Alaskans. The appeal is not an appeal that you can deal with unless you can define Alaskans not to include conspiratorial bankers. Do you see the point? Granted everybody wants to make Alaska a better place

to live for Alaskans. The question is how do we do that?

FUCHS: I guess I'm talking about if you have to set up a non-profit banking service of the Permanent Fund. Why should we guarantee their profits? What are they doing besides shuffling the paper and doing the accounting? And sitting between us and our money?

DOOGAN: So you'd be prepared to trade that off against the benefit to bankers and stockholders of banks in Alaska?

FUCHS: I'd say so, yes.

DOOGAN: The existing financial structure?

FUCHS: At least to have some alternative to that, which there is not at this point.

RHODE: Do you believe that the kind of purposes you talked about, a non-profit cooperative fisheries, canneries, related small scale business---do you think there's \$8 billion worth of such ventures? And secondly, how are you to get into those ventures without attracting new people, crime, all the other things?

FUCHS: That's a problem that's a little bit bigger issue in terms of more people coming in. I was just reading in a Manpower report that there's more unemployed workers in Detroit than we have in our total work force. That's the kind of magnitude in a lot of the economic problems down in the United States that are forcing people up here into an area that's expanding. I don't know how to deal with that but I think any kind of immigration controls are unconstitutional. I agree with what the woman said here, I can't remember your name, about having two classes of citizens. I would never believe in anything like that. Yet somehow we have to protect ourselves.

BERGMAN: The only way you can protect yourself from new people coming is by being poor and unattractive.

FUCHS: Okay. Well that's a political question we have to face. In terms of our relationship with the United States, but I think that's beyond the scope of this. Another thing about the \$8 billion, there probably would not be that much of a need for that much money. But we could look towards oil development. Even if, in the beginning, going a little slow, even if we are a little more inefficient, we'd have to be really inefficient to not be able to make money. If the oil companies are going to make \$98½ billion out of Prudhoe Bay field, if we even recovered half of that by developing these resources ourselves, we'd be far ahead.

One other thing I wanted to mention, I think, just in terms of having control of our resources, that we could look more towards our oil resource, I think it's wrong to turn it over to an oil company, that's going to turn it into gasoline to drive the third Cadillac to the country club for some guy down in Arizona. I think, since we know petrochemicals are such important industries that people need, we should look more towards putting our resources like into agricultural inputs in countries where they have machinery standing idle because they can't get petroleum. Yet they have people starving in our country. I think, if no one else will look at that, then maybe we Alaskans ought to be looking towards that also.

GORDON: I would like to question the figure about the 98 and wonder where it comes from.

FUCHS: It comes from Wainwright Security Industries. It was a report made to the legislature.

GORDON: Let me say this year all the corporations in the United States, all over the world, in oil and everywhere else, and mostly outside of Alaska are going to make about that much after tax profits. That's all.

FUCHS: That's before taxes.

GORDON: Are you talking about long term future or are you talking about any one year?

FUCHS: That's over the 20 years. Life of the field. The other thing is what you're talking about--the figure you're talking about profits also doesn't include all the advertising and the high rates--hundreds of thousands of dollars paid to managers.

GORDON: It is also true that if you take all the high paid managers and reduce them to zero, it would not affect that figure by any significant amount. In fact, it isn't even true the owners of corporations take out anything like that. What they really take out is the dividend. The dividends are only around a third of that--about \$35 billion currently. About a third of those dividends in fact, go to work in pension plans. So the notion that there's a huge pot of gold there that you can get a hold of just isn't true.

LOVE: That may be true in all industries. But wouldn't you agree that in, for example the Prudhoe Bay development that it's more capital intensive than maybe certain other types of industries in terms of pension plans?

GORDON: Well, I'm not talking about returning to capital. Returning to capital includes the interest of course, as well as corporate earnings. I'm just talking about specific corporations. The corporation doesn't make the money they pay out in interest; they make the corporate earnings. However, there's a widespread misapprehension about the nature of corporate earnings and particularly how big they are.

LOVE: There's also, I think, a wide misapprehension, in this case, about the concept of how profitable Prudhoe Bay is. I think that it's unwise to compare the development of Prudhoe Bay to industry in general, or even the oil industry in general. Because it's a fairly special and unusual situation. I'm sure you know it's got more proven reserves in the entire, everything in Canada and about 30% of the nation. So it's a very unusual field. It's an unusually profitable venture that Mr. Fuchs is talking about. I don't think it avails itself to really simple comparison to standard industry practice.

FUCHS: Just even a small cut of how much they're going to make is what all this money is in the Permanent Fund. There's supposedly so much we don't even know what to do with it. That's just a fraction of it. It's a low test. Depending on how other nations act to it.

GORDON: I don't know what you mean. Do you mean that Alaska should attempt to expropriate that money? That hypothetical \$98 billion before taxes.

FUCHS: I don't think there's anything wrong with that. It's our resource.

GORDON: I don't know legally whether it's your resource or not. Do you mean morally it's your resource.

FUCHS: Well, let's say if they're going to make \$98½ billion, why.....

GORDON: You're not making \$98½ billion; that's just nonsense. You don't make \$98½ billion if that's gross. The question is the period over which they make it. But if you're going to do that, why don't you expropriate all the corporations. What's so peculiar about those corporations that they should be expropriated rather than all the other corporations?

HAVELOCK: Mr. Chairman, is there any rule of germaneness to this discussion?

GRUENING: Well, I was hoping that it would kind of peter out. See what you started, Paul? I think that we should talk a break. Rep. Carpenter has indicated that I was amiss in the beginning, and I won't do it again. This gentleman in the back wanted to speak. Would you like to do it now or after the break?

DI NARDO: I'd like to make a few points. I'm Dan Ni Nardo. I've made a few notes here. One is management of the fund, what to do with the money. When you do invest it, we're worrying about the profit sharing that might take place by the managers, the social cause, how you measure effectiveness, etc.

My suggestion is an alternative of doing away with the Permanent Fund. It's very much important for this reason; there was a doctrine signed, the Constitution of the United States of America, that laid the ground work for a system called free enterprise. Free enterprise means that every individual in this room, in this state, you answer the question as to whether social needs get the best allocation. This is up to the individual people to decide. They do not need another government agency to decide for them. This has been the cause of the present problem that you're talking about in the state of Alaska.

Free enterprise across the board, and I'll tell you buddy, on a historical basis, on economic basis, free enterprise is the most efficient system ever invented by man to allocate that resource called money to where it should go. (inaudible).....That's why I'm opposed to the Permanent Fund. (inaudible)

DOOGAN: I had a comment before the break. It seems to me that with the last few speakers we've more or less set possible boundaries in this discussion. Maybe when we come back, we can confine ourselves within those boundaries.

GRUENING: Five minutes. Thank you.

BREAK

CLIFF BLACK: My main question seems to state who really is going to administer the fund? It boils down to a very deep philosophical question. If we are going to allow the legislature in Juneau to dictate what happens in Alaska to funds like these which provide an unusual and great opportunity for Alaskans to somehow effect local decision-making, local

regional planning efforts, to me this strikes a very great disservice and injustice to areas of Alaska that have been left out over many, many decades. I was going to get into a number of other points, but I would probably just say that probably to me, it has to be re-addressed more than anything else.

I was going to get into things like how does that again measure the effectiveness of the utilization, the regionalization of utilization of the fund? Well, certainly it would more enhance the possibilities for decision-making, the possibilities for effectiveness measurement, the development of innovative and creative ideas as to how utilize rural areas of Alaska. I happen to be from Deering, Alaska, which is up by the Arctic Circle; and I certainly recognize there are resources in that area, renewable and non-renewable, that have not been tapped, that could be tapped, that certainly will be tapped--either through good, sound planning or through a process forced upon the regional corporations that are there now because of their non-involvement in a windfall fund like this.

What I'm saying is the state of Alaska certainly has an opportunity to guard its environment, to guard its integrity in all areas: streams, its wildlife, fish, to guard also culture that is fast disappearing. These are assets that

cannot be regained, cannot in any manner be brought back. What I'm hoping is that we will look at this fund in a different sense than we look at just another dollar or two in our pocket. What I'm hoping is that we can, in some manner, incorporate all of Alaska into this planning and utilization of these dollars. I think the regionalization of planning efforts certainly bring about a more in-depth review of what is there and has ever been done before. It will not only identify the resources that are there, renewable and non-renewable, but also the resources in human kind.

Too many times, asinine I have to say, we assume so much. Assume that we have no resources of the human kind out there. We assume that they are having yet language problems, problems of identifying with the different cultures, problems of getting to work on time, well you hear that from biased, judgemental, prejudiced and sometimes bigoted individuals. You'll hear that whether or not the rest of Alaska catches up and even surpasses the majority of society. You'll hear that from the natives as well as the non-natives. You'll hear that from the blacks as well as the Hispanics. You'll hear that from everyone when they have a problem of identification and a problem of realization that we are one. You'll hear that all the time.

What I'm saying is that this is an opportunity to do

away with a lot of those problems. This is an opportunity to incorporate planning endeavors and planning opportunities for other groups that are not now in the planning that's going on, who have not been asked to participate; yet have 40 plus million acres that they're going to have to incorporate to your system, their own system, simply because they're citizens of the state, citizens of the country. How are you going to say to them that you don't have to pull out your oil, you don't have to pull out your gas now, when they know they do have to now. Because the society is forcing upon them their own rules of the game, forcing them to become involved in the 20th century capitalist system. Overnight, which is the system I believe in, by the way, even though I feel that cooperatives certainly will, most likely, work best in rural Alaska for many years, because the communal system inbred into our people to do away with it very quickly for a capitalist system.

I guess what I'm trying to say is that I don't see how we can plan for the fund utilization until we have identified more clearly and more fluently who, in actuality, is going to administer the fund; because if you identify the areas by regions of the state of Alaska, and I view Alaska as six states not one, six areas of Alaska that are somewhat separate from each other. If you do identify those areas for planning purposes, you will identify how the fund will be utilized.

You have no real commonality between Southeastern Alaska and Northwest Alaska. One is fishing and timber industry base area and the other is a subsistence area. The two are not in any manner similar. The only similarity might be in the fact that some communal systems still work in both parts of Alaska. If we then recognize that there are different parts of Alaska that need to be taken into consideration in our planning endeavors and in the utilization of this fund, we then certainly must recognize that the administration and the utilization of the dollars and the actual expenditures and how they are best put to work for Alaskans, how they will best incorporate more equity into our lifestyle and how they will better do away with the inequities that cause prejudices and fears and the misinformation and the wasteland that sometimes we don't even like to think of and the fact that we do many times disallow each other a good lifestyle simply because we are different.

I think that we need to re-evaluate what we're doing with these dollars. We need to re-evaluate in the sense that we need to take into consideration that we can't, as one group of people sitting in Juneau, dictate for all of Alaska a system that will be compatible to all of Alaska. Simply because there has never been a time when anyone has really looked at my part of Alaska, for instance, and never really

been a time when anyone has looked at other parts of Alaska. It's an opportune time. It's an opportune time to make a pact with the national government on D2 lands. We should not actually determine what the D2 lands are going to be until Alaska has had the opportunity to utilize some of its new-gained wealth to evaluate our state, to thoroughly recognize what's under the ground before we determine what it should be called on top. I think that's something we should look at--some of the things that we need to fairly evaluate. A gentleman made the comment that the educated are moving into Alaska. I hope they're not coming from places like New York and places where it has been shown that their system has failed miserably.

BERGMAN: Let's not have any bigotry here.

BLACK: This is not a racial statement whatsoever. I'm hoping that what we have in Alaska is a start of a new planning effort that can incorporate more Alaskans on a regional basis. I hope that you gentlemen don't take this as a personal thing that I don't believe that the legislature should be by itself in handling these dollars. I think that the legislature has great wisdom, but I do believe the people out there can plan and have some policy control over these dollars. I would certainly agree that they should be involved in the final determination.

GRUENING: Thank you, Cliff. Can you stay for questions? Is there a question of Mr. Black? Representative Meekins.

MEEKINS: Cliff, I am wondering what you think about where would the greater benefit be, I suppose this is contained in your comments, but I wanted to ask you directly, if you think there would be greater benefit in an Alaska, Inc. type proposal where the income from the fund is directly distributed to people in the rural areas, for instance, or if you think a development bank concept with planning agencies and regionalized, as you have talked about, would be preferable.

BLACK: I haven't really made up my mind seriously on Alaska, Inc. Whether or not I could go beyond the distribution of funds beyond the retirement level so that Alaskans who have lived here all their lives don't have to leave the state to retire. I think that's a tragedy. They have lived here all their lives, then they retire, then are forced by economics to leave our state, simply because we lose their expertise, we lose their knowledge in vast areas that cannot be gained overnight. Only

those people who have lived here for many, many years understand Alaska. We are losing them very rapidly. I would say that the majority of dollars be put into, not the majority of dollars because I cannot even comprehend that kind of money, but a good amount should be put into the development of really significant homes for the aged, take care of them and keep them in the state so we can utilize their expertise. Beyond that, I have still to make up my mind. I would certainly have made up my mind further had I been more comfortable with who would be administering the fund in the long haul.

GRUENING: Senator Rodey.

RODEY: Cliff, could I ask you another question in regard to administration? I'm as concerned as you are. Do you favor a method of electing members to the Permanent Fund board or an appointed mechanism such as has been embodied in the governor's bill?

BLACK: Well, elected representation is always good if it is on a regional level. If you put it into a state level, a good portion of Alaska is left out of any major decision-making possibility. I view the Permanent Fund in the sense that it's

an opportunity for a full type of revenue sharing that would incorporate the different costs in Alaska. For instance, if you buy a dozen eggs in Barrow right now, it'll cost you \$2.00 or more. The cost of service, the cost of product, the cost of anything that happens in Barrow is tremendously different from the cost in Anchorage.

What I'm saying is simply that if there's a revenue sharing device used for the distribution of these dollars, it incorporates very clearly the different cost of living differentials and it is distributed in that sense, then I could see a regionalization utilization based on election processes and very well could even see it go beyond that to dictate that a particular community would be represented and a person from each community could be represented on the regionalized board. So that way you wouldn't have to have any communities left out in the process.

RODEY: Your main concern is to ensure that some of the areas of Alaska which have a smaller population are represented on whatever Permanent Fund administrative body is finally formed. Is that what you mean?

BLACK: I guess my concern is--I'll go back to comments about the federal system in Alaska, the paternalism system

that has for many, many years placed it's hand on our head and said, "we will do it this way," and have never reached the point where they've done anything that we've wanted them to. They've always gone and done things as they've wanted to do them.

What I'm saying is that in this case I would like to see, since we're all citizens of the same state, since we are all part of the same state, that there be some manner where all Alaskans will determine the direction and utilization of these funds.

GRUENING: Thank you, Mr. Black. Are there questions from the audience? We have panelist here; we want to keep them on their toes. If you have some questions. Representative Chatterton.

CHATTERTON: Thank you, Mr. Chairman. Can you hear me alright? Mr. Chairman, I want to congratulate you on getting this group together, I can assure you it has been stimulating and very thought provoking. I hope you'll keep up the good work because the total picture can only be seen once all the various, however conflicting they might be, parts of the picture come before you. Keep up the good work.

GRUENING: Thank you, Chat. I didn't ask for that plug.

CHATTERTON: I really have two questions for

the panel, that developed this morning, but I can't help feel a little bit facetious. There was a person who testified here a little earlier this afternoon and made a suggestion as to how to use some of the Permanent Fund funds. I felt I should provide you also with a corollary suggestion for their use. Instead of buying all the federal lands that are put up for oil and gas leases or along with that, I suggest that we buy the national interest land and thereby immediately solving the D2 question.

Mr. Chairman, through you I would like to ask the panelists or anyone that would care to comment--we did hear earlier comments about: 1. loaning money; 2. investing money. It was even suggested earlier--there was some comment about investing in a pipeline or a petrochemical plant--state funds. My question to the panel and to the economists--if they have any background on this, would they care to comment--does the potential for a conflict of interests develop when a taxing entity becomes a participant in the profitability of a taxable entity?

My next question is--is there a degree of parallelism, at least in some facets, between what is before you, Mr. Chairman, with this Permanent Fund and what had to be before the U. S. Congress some years ago when they were faced

with seeing that each and every native Alaskan got a fair share out of the Alaska Native Settlement Act? Is there a parallelism? That's my second question. Thank you, Mr. Chairman.

GRUENING: I'll leave that up to the panelists, the economists, anyone who wants to speak up.

GORDON: I am really no expert on the problems of taxable entities. The notion that some of the investment proposals put forth recently here remind me very much of where I now live. I happen to have moved to Canada in the last few months. In Canada, there are truly an astounding number--they talk about free enterprise like everybody--there's just an astounding number of what they call their Crown Corporation, Federal Crown Corporations, and Provincial Corporations.

Now when you say is there a conflict of interests, they attempt, at least, by this device called a Crown Corporation, to make the Crown Corporation totally operate like an individual enterprise, despite the fact that the state or the province or the nation owns all the shares--sometimes not all the shares, most of the shares. I think if you survey the record of those Crown Corporations, that it is dismal. They have a Crown Corporation selling what Westinghouse sells--

atomic reactors. They got involved in a little bribery, but the most significant thing is they managed to sell two of their atomic reactors to Argentina at a loss of \$130 million.

The Province of Alberta has something called Alberta Heritage Fund. They're visably in the business of setting up businesses that otherwise wouldn't be there--irrigation facilities, food packing plants, huge petrochemical operations. The other thing they're doing is providing more services than otherwise would be the case and lower taxes. They're the lowest tax province in Canada by some piece. The result is that an enormous number of people are leaving the rest of the country and going there. The wages are lower there than they are where I happen to live in British Columbia, but people are moving there--that's where the jobs are. Rents are going up. Land is getting scarce. I see very little merit, what apart from the conflict of interest problem.

GRUENING: Is there any comment on the second half of the question, which was--was there any parallel between the Native Land Claims and what we might be trying to do with the Permanent Fund? Mr. Love.

LOVE: Well, it is my understanding that in British Columbia, under the New Democratic Party, there's a lot of acquisitions in terms of the Crown Corporations. As a result, partially because of their policy for rapid acquisitions, there's a problem with the insurance industry that the New Democratic Party was defeated and replaced by the conservative government of Mr. Bennett. It's also my understanding that Mr. Bennett's conservative government has not divested themselves of any of the acquisitions made by the NDP and that most of them, in fact, are now on the whole profitable. Is that an accurate summation? Just as a parallel to the experience the Federal Crown Corporation as looking to British Columbia where you teach.

GORDON: No, not entirely. You see, to describe the present government as conservative is, I think, quite incorrect. We have two kinds of parties in British Columbia. One is socialist and the other is more socialist. It is not true that those have become profitable. It's not true--they've all been losers. In fact, if you investigate in the theories of finance they teach in business schools, it is extremely difficult to lose money consistently by investing. The NDP did not succeed in doing so. But more serious, some of their acquisitions, a distressing number of their acquisitions, have lost money.

They perhaps could have been defended on the grounds that they had some social purpose. There's a great dispute about what the social purpose was and whether it helped anybody significantly.

I'd say in Canada, there's all kinds of conservative government of another province in far east. New Brunswick. They bought all kinds of things, setting up another conservative government. They got into an endless stream of business--nearly all of which went bankrupt. The one advantage, incidentally, of the Crown Corporation is it isn't like many of the corporations into which the British government bails people out. When they set up a corporation, it is like a private corporation. When it goes bankrupt, it's bankrupt. So it doesn't continue forever. It's just draining off the public purse. That is a legal device which, I think, is of some usefulness.

I think there's a great parallel; it's a little hard to classify political opinion. It seems to be so simple that a liberal, radical person interested in the poor and egalitarianism should be for one thing. And that is give the money to everybody, if they could, and they can't. Okay. Invest it as good income as possible, and give that good income to the people. That would do more for the world

of Alaskans. It would be an immediately equalizing phenomenon. I cannot think of one thing that has been proposed here that is going to do nearly as much for the poor in Alaska as that kind of proposal.

LOVE: Which you stated on several occasions.

GRUENING: I think we've got the different philosophy pretty well outlined here. Is there any comment on the second half of that questions? Or another question from the audience?

HAVELOCK: I think the answer to Mr. Chatterton's second question is yes.

GRUENING: Okay. That's the kind of answer I like. Mr. Dave Hickok, did you have a comment?

HICKOK: I agree with John. I think the answer is very definitely yes.

GRUENING: I believe this gentlemen in the red shirt wanted to ask a question. Could you identify yourself please.

WICKS: No specifically a question or even an answer. My

name is Alan Wicks. I'm a recently retired teacher, in the Anchorage School District for the past 20 years. I came to Alaska initially in 1940, working for the Territorial Department of Health. At that time, I supported our Chairman's grandfather, Governor Gruening of the Territory of Alaska, in his efforts to roll back an unseemly rate increase by Alaska Steamship Company and have been more or less a Gruening supporter ever since.

One thing that is lacking in all of this commentary and discussion as to profits investment management--there's one thing lacking, because it seems as if everybody is making an effort to play God for everybody else. While we like our benefits and we like our dividends, and I like them as well as anybody else and have been lucky, and like the Wall Street Journal has said "nothing succeeds like dumb luck." A little bit of that can go a long way if you're on the lucky end. I want to put a diagram on that board. As a teacher, I just can't resist the opportunity. Then I'm going to come back and make a couple of comments about it and then a question at the end.

GRUENING: Okay. It's getting a little late. We want to keep everyone interested.

WICKS: I didn't need the eraser. I didn't want to wipe off the rest of that. There again, somebody made allusions and maybe I'm, well no, I'm not, just reiterating what a couple other people said. We've arrived at a place in international affairs. I'll flash back to pre-World War II and depression times. We've arrived now with technology and science and my background is basically biological science--we've arrived now at a place where humanity with it's science and technology doesn't really know where it's going. But I submit to you, and this is an independent, personal formulation, I won't give the blame to anybody else; but unless and until humanity arrives at a umbrella concept, and that's what that is, of first basic, foremost environmental, ecologic concern before the fund, before the investment of the fund, before the applications from the return from the fund. What I'm saying is that civilizaton and humanity, at this juncture is up against it. If we don't learn or haven't learned what the aborigines, the native peoples, learned long ago, was to live and operate in concert with nature, with earth. Not as it's master, not as God who says, "I'll scrape it, I'll build it, I'll erect the edifices in my own way and to my own needs and beliefs and likes." Now I'm going to leave that idea, but I think it's the one that needs the most emphasis, first and before just about anything else.

I'd like to turn to the panel, and while I respect and admire Dr. Lindauer's views, he is a relatively new and accurate able observer of the Alaskan scene. I'd like to ask him how he discriminates on one hand between the need for application for funds to this or that industry or development, to get to a specific point, or the abhorrence of the use of the funds because they would be an economic magnet to people elsewhere to come to Alaska, but on the other hand, my, and I'm tickled to death I've got it, my 5½% FHA, if it is made available to them, it's not going to just be a drove, a horde, who are attracted to the magnet of 4% or 5% or 7% Alaskan-style FHA. We're not going to be able to differentiate between those things in any way.

LINDAUER: That's really an excellent question.

One could easily say that you could do the same, for example, with Alaska, Inc. as using eligibility for loans for business. It could, in fact, be those people who are here now and could have such time variety for qualification or w0 years, and you pick the number in order to qualify. It wouldn't really qualify that they'd be eligible. What we'd assume the utility serving a native village would

be instantly qualified. We'd assume a long-term Alaskan would be instantly qualified. The question is where do you draw the line. That wouldn't seem to be that difficult.

BERGMAN: Let me ask a question about Alaska, Inc. Suppose you have two kids born the same day, and one of them is the child of a long term resident and the other is the child of someone who is not a long-term resident. Are you going to give one of them the Alaska, Inc. payment and not the other?

GRUENING: The governor isn't here to defend himself. The more you get into the Alaska, Inc., the more difficult it is to exactly define who an Alaskan is or who is the beneficiary. It doesn't mean it's impossible. But obviously if it's going to be a meaningful program, you've got to draw the line somewhere.

BERGMAN: I understand that you might be able to draw it with adults, but I think if what you're trying to do is enfranchise only those who are here now and their descendants, you've got a tough row to hoe. I don't think you can do that.

GRUENING: Alaska, Inc. does have a residency. The child isn't really eligible until it's been here a certain number of years.

LINDAUER: What would, for example, require 18 year residency, at least, so an 18 year old can enter into contract. So whatever is the legal age for entering contracts, that means every child will be eligible if they've lived here long enough. As would be anybody who arrived.

HAVELOCK: It's not going to stand up constitutionally though.

GRUENING: I know that's being studied. I'm sure there's some way you can find a way, but we're not here to discuss that. Somebody who hasn't made a comment yet. Mr. Hickok, would you like to follow up?

HICKOK: I'd like to say a couple things that tie in on this subject. My name is Dave Hickok. I'm the director of the Arctic Environmental Information and Data Center at the University of Alaska, currently the president of the Alaska Division in the American Association for the Advancement of Science. I think there's two or three items that seem to me have not been covered.

One of the things the economists appears to have said is that the need on the curves is a function of economics

alone. I'd like to say that I don't think it is. I'd like to give a few examples of what's happened to history in Alaska. One of the needs trends that has determined what has happened in Bush Alaska has been, for example, many years ago, in the Arctic latitudes here, we did a lot of research on ionospheric scatter and so on. We were able then to develop satellite communication systems for these latitudes which was not a possibility under existing technology of lower latitudes. Now what has happened here is because communication was available to Bush Alaska, technologically, and because there was a political decision made by very, very few people for the sale of the Alaska communications system about 1970, the whole need trend for communication and development for this kind of thing in rural Alaska changed. Not by virtue of economics, but by virtue of technology and science and by virtue of political decision.

There also have been a number of other of these kinds of things. In the health field, two doctors made the breakthrough in tuberculosis following World War II here in Alaska. The highest incident rate in the world in the early 1950's of birth rate and death rate in rural Alaska---beat the Kalahari Desert in Africa and everywhere else--were brought down by science and technology. The application of money, in that sense, of the political decision to stamp out disease.

These things make aspirations. These things make needs that are not just driven by the common market place. I would suggest, in addition to the economics of capital investment and so on, there are at least three or four other items that are driving the need co-efficient and that is law and politics, which I put in despite Mr. Havelock's qualms, hand in glove, science and technology and perhaps a population expansion. These things are making change in Alaska. The need curve is escalating at a tremendous rate despite what happens in economics.

The aspirations of the Bush communities, where there are hundreds of them, have no water, no sewer, no schools. These aspirations are real. They are going to drive a demand for public expenditure funds to satisfy these problems. I would certainly agree with John Havelock that the Statehood Act called for the expenditure of tax revenues and so forth to support a burgeoning new state. I would also suggest to you that the Alaska Native Land Claims Act also had the same effect. The one thing that Alaska has not recognized, or several things it hasn't recognized, but one thing it hasn't recognized is that rural Alaska should not pay the price for the public services that everyone else in Alaska enjoys in the urban settings. Through their compensation dollars that came under the Native Land Claims Act, they are entitled to the

same public services as anyone else. I guess that's about enough.

GRUENING: Thank you, Dave. Would you mind remaining for a minute in case the economists or the legal field would like to responds.

BERGMAN: I'm the one that introduced the word and when you started talking, I instantly regretted it. Then I recall that I had put quotes around it. I actually agree with you that there is no such thing as absolute need. You can't take a certain desire and say this particular desire is a need and this particular desire is not a need. What I'm trying to point out here, though, is that if the population were to grow, just to maintain a certain level of services would require a growing trend of revenues, which is an entirely different point.

HICKOK: I think you're right. But regardless of that, the need curve, the demand curve, perhaps, of social aspiration, human aspiration, is escalating at a tremendous rate, regardless of the economics of the state. Because of broader expansion in health, in education, in other factors.

BERGMAN: Well, I think what you're saying is what some other

people have said--that perhaps it would be more reasonable to use the oil revenues for this kind of purpose. Use them all for this kind of purpose--setting up schools, setting up water supplies, setting up electrification plants, instead of either sending it to these much maligned New York brokers to be kept for future generations or perhaps for giving concessional loans to people of Anchorage. That, I think, is a matter of simply social policy. You've got to fight it out. That's not a matter of economics. That's a matter of what you can get the people of the state to spend their income on. I feel that the Supreme Court had said schooling had to be provided throughout the state in a more or less equal way. There's a famous California case on that.

HICKOK: Well, we had one here in Alaska too.

BERGMAN: So I don't quite understand the fact that it hasn't been done already.

MEEKINS: Doctor, are you saying that expectations or needs, whatever you want to call it, are not related to the economics?

HICKOK: I think they're related, but I think there are a number of external forces that make new aspirations.

Prior to the research on ionospheric scatter and so on, that made possible high altitude communication systems, there were no aspirations for it because nobody knew it could be done. There are a lot of these kinds of sayings. Before you could put a sanitation system in Arctic permafrost, you have to know how to do it. Then by virtue of it being able to be accomplished, there's aspiration for it.

MEEKINS: I think that's the common denominator between the two. Because when you have money, it's, therefore, possible to build things, it's, therefore, possible that weren't before. It's the possibilities that seem to feed the needs.

HICKOK: No, the possibility may fuel the need, but not necessarily money. In the case, for example, of the communication situation here in Alaska that wasn't a function of money.

MEEKINS: I'm not limiting it to money.

HICKOK: It's research of science and technology and a political decision to sell the Alaskan communication system away from the military and to put it into modern science.

MEEKINS: Just to clarify--I'm not limiting it to money.

I'm saying that things being possible is the common denominator between technology and economics in your scenario, because even if the technology made it possible to have telecommunications, if we didn't have the money, even if we had the political will, we wouldn't have it.

HICKOK: Then, I would to back to Tussing's scenario. I think what Tussing is saying is that the private sector, the private demand for these things is running, and we have a large sector of private money, by virtue of Native Land Claims and the growth of the Alaskan economy.

GRUENING: Thank you, Mr. Hickok. Okay, in the waning hours, are there any more questions? Sure, you're welcome to ask again, if there's anybody who hasn't had a chance to ask...

FISKE: I'm Lieutenant Colonel Fiske--Retired. I'd like to say first that I strongly support Dr. Lindauer's position on adequate investment of Permanent Fund in Alaska and for the lowest, reasonable interest rates, and where present Alaskans can enjoy the benefits of employment, social amenities, health services, recreation, etc., etc., and etc.

I'm interested in providing something to occupy the leisure time of the many small communities, particularly during long

winter hours. Something that involves all ages, both sexes, from youth to octogenarian. Most of our rural communities have churches, bars, but many have little else to occupy the people when they're not busy at making a living or subsisting. It seems to me that an excellent way to use some of the earnings and possibly some of the Permanent Fund would be to develop a program to provide indoor recreation facilities--I'm referring to curling, skating, and I'd like to draw a comparison with what the Canadian government has done. Many, many of their small communities have been funded to build curling, skating facilities, which also provide a place for the community to assemble for all kinds of things. I believe that if the Permanent Fund and the native regional corporations get together, many of these small communities could be provided with something that would knit the communities together. Their needs, then, would be brought forth as a community requirement. I think, it would do much to knit the communities together throughout the state of Alaska. I would suggest that all of the other comments today have been primarily on what to do with the fund. I submit that this is just one idea that might be considered in providing for Alaskans who can enjoy it through all ages. Thank you.

GRUENING: Thank you. In bringing this to a close, I want to ask the audience once again if there's any questions they'd like to ask the panel?

HAVELOCK: I'd like to make a comment on that last statement. I think that if the Permanent Fund committee does adopt some sort of internal investment policy as part of the Permanent Fund, you should be careful at the same time to keep a count of the public costs that are going to be associated with that private investment. Perhaps, Dr. Gordon could comment on what kind of ratios those are. It's clear you're going to be giving money for loans for small business, that you are going to kick off at the same time a lot of pressure for public amenities to go with that. If you haven't taken proper account of that, you're going to create substantial social unrest.

GORDON: I can't really answer that. I would be very surprised, however, if you could make some generalization about that. If you subsidize investment on the private sector, it might entail a considerable amount of public spending outside of that. In other cases, perhaps a very much smaller amount. I think you'd have to investigate each on a case by case basis.

GRUENING: Mr. McCutcheon, you were going to ask the last question.

MCCUTCHEON: It will probably turn out to be a rhetorical question. There are several things here I'd like to state. Professor Gordon, you challenged Paul Fuchs's estimation of the greater return on investment of Prudhoe Bay. I don't necessarily share Mr. Fuchs's view of what should be done. I thought that you might possibly give us some idea of your estimation of the greater return on Prudhoe Bay, and maybe you could start with by getting to the size of the reservoir, the amount of recovery under current production practices, the amount left in the ground, the amount of additional recovery through secondary treatment, what will be the value of oil, price of oil on the West Coast, what will be the value of oil delivered at the West Coast, what is the value of the investment that's going to be happening? What are the profits contributable to tax relief, tax loopholes?

GRUENING: May I just interject here? These are very interesting questions. I think they, at least have some relevance to the Permanent Fund...

GORDON: I'd like to answer that. In the first place, nobody can rate that question. Anybody who thinks they can tell you the price of oil ten years hence, as has been suggested around here, is engaged in witchcraft. Let me explain one other thing. What I wanted to do was find out how this Prudhoe Bay figure came

out \$98 billion, and I happen to know that's the sum total of all American corporations from ma and pa ones up to Exxon--all over the whole world in any one year, after taxes.

RODEY: On behalf of the Senate Permanent Fund Committee and the chairman, Senator Hohman, I'd like to thank the House for putting this symposium on. This is the first in a series of meetings that the Senate and the House will be participating in. The House effort is more visible here in Anchorage because Chairman Gruening has done a very good job of getting the committee's work planned and accomplished. The Senate Committee's work is being done primarily in Juneau at this point; and we are trying to work in conjunction with the House to provide as much possible information on the Permanent Fund as we can before our January deadline of drawing up legislation. If there are questions or concerns, I know either the House or the Senate would be happy to address them.

Proceedings
of
The House Special Committee on the Permanent Fund

PUBLIC HEARING
September 14, 1977
Anchorage

Rep. Clark Gruening, Chairman
Rep. Terry Gardiner, Vice Chairman
Rep. Ernie Haugen
Rep. Russ Meekins
Rep. Bill Miles
Rep. Leo Schaeffer
Rep. Rick Urion

GRUENING: I guess we're all plugged in, and we can start. I really appreciate seeing some familiar faces and some unfamiliar ones here on this blustery morning for the hearing on goals for the Permanent Fund. I'm Clark Gruening, the chairman of the House Special Committee on the Permanent Fund. Starting from the right is the A.A. to the committee, Mike Doogan, whose newspaper background--you might have seen some of his work; coming down the line is your Representative Sally Smith; and LouAnn is the secretary to the committee; Representative Russ Meekins, a member of the committee; and Charles Parr, who is not a member of the committee but certainly will have a lot to say on how legislation affecting the Permanent Fund is devised.

This is going to be fairly informal today. We don't have a list or order. I think just raise your hand if you want to testify. We'll just pick one; you come on up. We want to have plenty of time for questions and answers. If it works out, we may allow a question from the audience of a witness as well.

We certainly want to hear what you have to say about the fund. What has struck us in dealing with it is that there are already established in state government a number of loan funds. Sometimes we hear--I've heard everything--I see that former

Representative Tim Wallis is coming in--we've heard everything for investment of the fund from artifacts to wheat. In examining it, we notice that they're already in existence state loan funds, which, at least statutorally, can deal with the kind of investment that people have stated they'd like the Permanent Fund to get into. So one task of this committee will be to examine where those loan funds have accomplished their goals and where they haven't. In other words, if you have a program you think the fund ought to take up, we ought to see whether there's an existing loan program and see what it's done to further the need of investment.

I'm just as interested, and I think the committee is too, in what you feel the Permanent Fund ought not to do as well as what it ought to do to the extent that you devise a very complicated system for the Permanent Fund, it'll be harder to achieve the goals.

With no further ado, unless any of the people here of the committee or the panel want to make a statement, we'll just start. Who would like to be first can raise his or her hand. Tim Wallis.

WALLIS: Mr. Chairman, members of the committee, for the record my name is Tim Wallis, president of Doyon, Limited. I would like to take this opportunity to thank you and the committee for traveling to Fairbanks to receive public input on the Permanent Fund.

In the early stages of the creation of the Permanent Fund, at which time I was a member of the Legislature, I opposed the creation of the Permanent Fund. After further consideration, I changed my position and voted for the Permanent Fund legislation that was vetoed, and voted also for the constitutional amendment for the creation of the Permanent Fund. As a result, comments or criticisms that I make now or in the future, I hope will be taken in the manner that I am trying to assist in establishing a workable Permanent Fund. Doyon, Limited has spent considerable time and effort to examine the proposals for the Permanent Fund. Because of other pressing issues, in particular the D2 issue, I am not fully prepared to comment on all aspects of the legislation. With the committee's permission, I intend to submit further testimony at a later date to become part of the committee's formal record. Also, I would intend on talking to you and other committee members on an individual basis as a Permanent Fund concept winds its way through the legislative process.

There are a couple of points I would like to make for the committee's consideration at this time. First, I recommend that the legislation be structured so that the maximum amount of leverage can be obtained from the prudent use of the fund. Certainly the same leverage tools commonly used by the private sector money managers should be available to

the managers of the Permanent Fund. There are at least four ways that increased leverage that can be accomplished in this legislation:

First, the fund should be permitted to purchase equity securities. This would permit private venturers to raise more funds from the private money market than might otherwise be possible.

Secondly, the fund should be authorized to subordinate its loan position in favor of private borrowers in large scale private development projects. Subordination is a time-tested tool which can be invaluable for Alaskan development projects when exercised with care by fund managers.

Third, the fund should be permitted to participate in syndicated loan arrangements. Once again, this is particularly important in the case of large scale projects.

And four, fund managers should be permitted to make loan guarantees. Loan guarantees by the fund would increase the debt capacity of Alaskan borrowers immeasurably. A debt guaranteed by the fund could be used to attract private money at favorable interest rates at no direct cost to the state. Such favorable interest rates might even make marginal projects feasible, or reduce the risk premium for high-risk projects.

It seems to me that a primary objective of the fund should be the attraction of private capital to Alaska by using these

tools and perhaps others, the fund could become a dynamic force in improving our state far beyond proportion to the fund's size. I encourage you strongly to give the managers of the fund the widest possible discretion in using tools to increase the leverage of the fund to attract private capital. It appears that great discretion will have to be placed in the managers in any event, since they will have custodianship for a billion dollar plus fund. It only makes good sense to go one step further and give them the same kind of investment tools that responsible money managers have in the private sector.

My second point will be brief. I believe the portion of the bill calling for a possible investment of 30% of the fund in "community development projects of municipalities and public corporations" may need to be spelled out in more detail in the statute. If that sizable portion of the fund is going to be available for this type of investment, the definition of community development projects should be broadly construed.

For example, in many large scale private development projects many quasi-public facilities such as roads and health care centers must be constructed. I believe that some fund monies should be available to private firms constructing these quasi-public facilities subject to conveyance. This section would permit private companies which must construct

quasi-public facilities access to the fund. Certainly many safeguards could be built into the administrative organizations which would require that these quasi-public facilities so financed would be available for public use at some specific time. I recommend the broadening of the language of the legislation to include public-type investments by private companies. The current language limiting investments to municipalities or public corporations is too narrow and unduly restrictive. As I indicated at the beginning of my remarks, Doyon, Limited will have a more detailed proposal at a later time.

I am certain that within the next few months a constructive and imaginative bill can be drafted to meet the manifold needs of Alaska's economy. Thank you, Mr. Chairman.

GRUENING: Thank you, Tim. Can you stay a minute for a few questions, if there are any? I appreciate that comment and I think we would like to hear more from you and especially anything you can give us in terms of experience that Doyon has had.

I think, as one of the largest native corporations, that probably it has gone through the ropes of trying to develop viable economic enterprises within its regions. To that extent, it may be parallel to the Alaska experience. Are there any questions from the committee? Mr. Meekins.

MEEKINS: Tim, I don't know if I understood it correctly; but when you're talking about such things as roads and other types of projects, do you have in mind the roads being the kind of project that would make a return to the state, which is a limitation on the fund--you have to make a return. Historically, we just appropriate money directly to roads and they're built, and they don't return anything, because they're not toll roads, so there's no return on the investment. Is there some financial mechanism that could do that?

WALLIS: Indirectly. I'm trying to think of an example-- I guess would be--in any large scale mining operation, the possibility of perhaps a new community will be established. Part of that community, of course, as any community would be access. So you would need to build a road to and from as well as...

MEEKINS: I suppose the fund could buy bonds from a municipality or any incorporated entity that might build roads and other infrastructure type things. But, I think one of the things we've run into is that in the state of Alaska, especially when you deal with the rural areas, and

I'm sure you're more familiar with this than the members of the committee, but in thinking about this we've found that a lot of the problems are that we don't have the infrastructure. We don't have the roads. If you're going to make an investment in some area, you can use the fund monies to provide a loan for something in the rural areas; but you can't use the fund monies to build a road, or at least it's not very easy to do so. So we need some other type of maybe additional investment from the general fund or something else to provide transportation in some of these areas, if you are talking about developing certain areas of the economy.

One of the things you might want to comment on later would be one of the things we've thought about in this area in regards to renewable resources, like fishing, agriculture, or anything like that, is that the Renewable Resources Development Fund can directly appropriate. That fund, which, as you may recall, takes the same revenue but only 5% of it instead of the 25% and puts it in a special fund which is separate from the Permanent Fund, which can only be used for the development of renewable resources. So that type of a fund could be used in concert with the Permanent Fund--one to build the infrastructure and one to loan money for a development project--at least that's possible. I'm not sure that it's a good idea, but it is a possibility that you might want to

consider in your further testimony written comments.

WALLIS: Thank you.

GRUENING: Are there any further questions? Incidentally, I'd like to invite Representative Carpenter up here if he'd like to sit with us and ask questions.

Tim, I'm curious. Someone mentioned in Anchorage about the parallel, the possible parallel of the Alaska Native Settlement Act with the Permanent Fund. As I understand that act, Congress wanted to mandate some dividends be paid out of some of that money, feeling that some of the present generation of Alaska natives would not benefit from the bill, unless some immediate money was shared and shared equally.

Applying that to the Permanent Fund, is there a possibility that when you establish a loan program, only certain people qualify for loans? As I understand some of the, say, rural Alaska's opposition to Permanent Fund was that they felt, as is the case with some of our loan programs, the urban areas would get most of the loans. That problem still exists to some degree. Is there any feeling do you think, for establishing a way that the Permanent Fund through payment of either dividends through Alaska, Inc. or say, through an annuity pension program could give out at least the earnings

of the Permanent Fund to every Alaskan so that there is some equity involved in terms of that state money? Does that have any appeal to you personally or does that make any sense?

WALLIS: Whenever I get free money, it appeals to me.

The Alaska Native Land Claims Act, I think perhaps, is a totally and completely different street of legislation. I think the Permanent Fund and its establishment and what the voters were looking for basically was the basis, the catalyst, which would give Alaska financial independence. If the fund was able to do that, and flexible enough to do that, the dividend aspect I don't think at this point, and I may change my mind at any time in the future, I would say you may want to look at other areas which affect people such as property taxes, income tax, and this sort of thing which would delete, reduce, or whatever. That'll lend the dividend to an Alaska, Inc. concept. Again, I reserve the right to change my mind.

GRUENING: I do the same. I find out I learn as I go along.

WALLIS: If I may, Mr. Chairman, just for a moment add this, I would recommend, perhaps, however it is to be done, the attorney general has a view and some other people have another---would be to

increase the 25% amount into the Permanent Fund up to at least 50%.

Also, the important thing in the creation of the administration of the Permanent Fund, I think, perhaps should be looked at carefully. You could find that in administering the Permanent Fund, it could become very political; in the sense that you have a board, trying to get away from the political aspect of it, you have a board and a commission or your loan review committee, then you'd have the then it gets that political overtone, where somebody is more influenced to get the loan and the guy next door couldn't get the loan, and as a result his project went down the tube. Establishment in working, in creating the whole organization, I think, needs looking into.

GRUENING: I agree. That's one of the more difficult problems--how you insulate it and at the same time, not make it so insulated from policy that you, let's say, have a fund with this amount of money doing investing in, someone suggested pickled sticklebacks, something that is doing nobody any good. There has to be some review function. To do that and separate it from, let's say, political favoritism is difficult. Did you have a question, Mr. Doogan?

DOOGAN: I do. Mr. Wallis, has Doyon found that there is a lack of financing either in the private or the existing public money markets for projects that would be economically viable if that financing was available?

WALLIS: To an extent that depends on what amount of money you're talking about. A large amount of money that we're talking about in the Permanent Fund--we haven't gone after that much money. A small amount of money that we have had before puts you in a position to get favorable rates.

GRUENING: Thank you. Any further questions? Thank you very much, Tim. Hope to be talking to you again. Mayor. Incidentally, if you could state for the record your name.

CARLSON: Chairman Gruening, distinguished panel, I'm John Carlson, mayor of the Fairbanks North Star Borough. I wish to personally thank you for the opportunity to allow the citizens of interior Alaska to speak up on how they feel about this Permanent Fund.

I think the proper utilization of the Alaska's Permanent Fund can become the single most important decision that Alaska political leadership will ever make. In most national political

decisions in that arena we have hardly very little effect on some of the decisions that are made in Washington, D.C. We certainly hear the important decision on a Permanent Fund and that we can have a say in and certainly guide to properly apply benefits to all of Alaska.

The use of the Permanent Fund and other royalty funds are to build Alaska's economic future. My own preference is we use the oil and gas royalty income and Permanent Fund leverage to establish a sound economic and cultural base for Alaska.

Specifically for the Interior, our future is tied to expansion of our transportation system. In discussing the potential here of oil and petrochemical development and any other development, it always comes out the problems that we have for transportation, that's the greatest liability for development of a sound and stable economy in interior Alaska. Our airport and our highways should be expanded and certainly the development would follow. A person cannot get out and the parks and the recreation facilities in interior Alaska without some mode of transportation, whether it be by air or by road. If non-renewable resources are used, or developed I should say, this would not encourage the development of the Interior, where the renewable resource development, such as

agriculture, would certainly develop and enhance the interior Alaska.

The worst would be to build expensive office buildings as a monument to political efforts of bureaucracy and the other use as a drain of our resources rather contribute to our economical or cultural stability.

I realize that Permanent Fund must be used in such a manner as to be permanent. However, low interest loans to aid in establishing better transportation system is a common factor and addition prime loans, tourism loans should be built upon. Once established, these industries would aid in getting interior Alaska out of the government dole, reliability upon government because we would develop a stable, an expanding economic situation or base here in interior Alaska. I want to thank you again for the opportunity to speak a few words to you and commend you on your all-out effort travelling throughout the state and getting the information from the citizens. Thank you.

GRUENING: Could you stay for a few questions? Any questions from the committee? I have one. You mentioned office buildings being an example of one of the worst investments. Would that follow through the Permanent Fund getting into, let's say, a guarantee for cities to build office buildings?

CARLSON: No. I think what I am referring to here is just the building of an office building for office building's purposes and just to be building it and no real need for it. Certainly, I realize that government needs office facilities, but not to make something with a lot of sugar-coating on it just because we have the--in other words, gold door-knobs just because we have the funds available. There are areas, for example, here when we look at a permanent building, certainly funding could be made available through the Permanent Fund or securing of the bonds would be necessary to build it would be a way to go. So I'm not excluding it, I'm just saying that we shouldn't be building office buildings for the building sake--just to have a hall here that would not be utilized.

GRUENING: Has Fairbanks used the Municipal Bond Bank with any success?

CARLSON: We have not had need of it. No, we've gone on our own bond. I think the Municipal Bond Bank is geared more in the past towards smaller communities who did not have the bonding capability that the larger cities have.

GRUENING: Do you see any need for that activity to be expanded to include Fairbanks? I'm trying to understand if

the city doesn't have need, then you're talking more about infrastructure, transportation, and so forth.

CARLSON: I think, it's my understanding of the bond bank the availability of it is if a community doesn't have the base to go on the bond market and get a good price could utilize this, then the state would then take and market the entire package, like Anchorage or Fairbanks, where we do have the base for a bond market and that we have not utilized this as a source. When I talk of transportation development, the airport and the rail facilities and the highways, it is, like I noted, we met with several people in the development of petrochemical opportunities here in interior Alaska. One of them even indicated should they select interior Alaska as a site, they would need a double rail to Anchorage for their commodities. This, of course, is a large scale operation. There is a continued need, to look at the transportation facilities and the means for funding them. Now we have to go to bond issues and there probably is an opportunity here for a pay as you go operation.

GRUENING: How would the, since the Permanent Fund, as you noted, has to earn its income and should be permanent, how would the Permanent Fund derive income, earnings from, say building a rail---would the petrochemical company pay for that?

Reimburse the Permanent Fund or how would that work?

CARLSON: The revenues, of course, on rail-maybe Alaska should buy the railroad with the Permanent Fund. It would have to be looked at as a source of revenue through the rail. It would have to be probably something worked out in that area, when you say that the petrochemical people or the oil people look at some way of funding the, or returning the funds, it would have to be on some type of scale for the use of it, if this is the way that we would have to go, if it wasn't available to go through other sources to the revenues that would be derived to the railroad would be a means of reimbursing the state.

GRUENING: Are there any other questions? Representative Parr.

PARR: John, we all saw your thing in the paper about the Fairbanks airport losing money. We all know that it usually does, because, obviously, the gallonage fees are all paid in Anchorage not in Fairbanks. If the fund were to invest money in the airport, have you got any ideas of the mechanism where we can make sure that the fund would get the, it would be a, you know, the money would not be a loss-- would be a making operation.

CARLSON: I think one of the things that was discussed in the paper the other night was the idea of a capability to expand the airport. It is my, in discussions that we've had with the oil companies or the gas companies that are doing this, until it becomes economically feasible or the demand for it, they would not put it in. Now if the state were to put this in, there would have to be probably a gallonage fee used to reimburse the cost of it. I think naturally the oil distributors are looking at their return on something like this before they would invest it and they'd be having to go into the money market. If the state could develop this, then there'd be a charge upon the flow of the gallonage through it. It would be a means of reimbursement.

GRUENING: Any further questions?

DOOGAN: Mayor Carlson, I just want to make sure that I understand--would it be accurate then to say that insofar as you can see a need for the use of Permanent Fund money that it would be on a relatively large scale for a large scale project?

CARLSON: Not entirely. One thing I didn't get into is, let's take agriculture in interior Alaska. The studies that we've had made over the years indicate that agriculture has a good potential and the climate is such that it would be well if not

better than we normally think of the Matanuska Valley. But the cost of clearing land is prohibitive to a lot of this development. Perhaps, something could be worked out on a smaller scale, where the funds could be made available for the land to be cleared over a period of years, so whoever is farming this is to reimburse it. So this would be probably considered a small scale development versus something in a larger area. I know that there probably will be more discussion on this agriculture aspect from other people.

GRUENING: Mayor, I just have one question on the agriculture. We do have an agriculture revolving loan fund, which is an aid--quite a few million dollars worth of loans. Do you know whether this fund presently is sufficient or whether it's one that we should expand? Are there problems with the loan fund itself, which make it incapable of doing what you'd like the Permanent Fund to do?

CARLSON: I haven't honestly looked into that to answer that question. The only contact I've had is with the people interested in developing; for example, about three weeks ago we had a contingent of people from Japan over here that were very interested in buying rape, which the university is experimenting with it, develops oil. It's a plant that will

grow where barley grows. It's a, for example, the oil that is used by MacDonaldis for their frying. It's not cottonseed oil; it's rape oil.

GRUENING: It's called rape?

CARLSON: Yes. It is being looked into seriously as a plant or a product that can be and should be developed in interior Alaska. In fact, since 19, I think, 52, Canada has been the largest grower of this product, the producer of this. It certainly would be advantageous in interior Alaska. We're looking at 3,000 acres to make it financially feasible. So it would be then an opportunity to develop agriculture as a stable economy in the Interior.

GURENING: I think we'd have to change the name of the product.

CARLSON: I had nothing to do with naming it.

GRUENING: Could you stay for one more question? Representative Russ Meekins has a question.

MEEKINS: Mayor, following up on that line, we have two Permanent Funds in the state. The one we're dealing with

today is so large that it sort of overshadows the other one--- hopefully, it'll be large. There's not much discussion going on on a public level on the Renewable Resources Development Fund, which also establishes a Permanent Fund. That fund starts accumulating money in 1978, beginning in January of this year. It will have, of course, all this is subject to change, but it will have 20, 40, to 60 million dollars a year coming into that fund. I don't know what the renewable resource potential in the area is, but I know it's somewhere in the Interior that they're considering increasing agriculture and that fund would be a prime source of funding for that kind of development. In that sense, in fact, it would be more appropriate for that fund than the Permanent Fund. One advantage of that fund is that it doesn't have a requirement that it be income producing. So that there is something that needs to be indirectly appropriated, money can be directly appropriated in that case from that fund. Just for your deliberations, you might want to start considering proposals in regards to the disbursement of money from that fund also.

CARLSON: Alright, thank you. I appreciate that.

GRUENING: Thank you very much, Mayor. Yes sir.

SEIFERT: My name is Rich Seifert. I would also like to take this opportunity to welcome you to Fairbanks and thank you for allowing us to have this opportunity to speak. One of the things I really enjoy about living in Alaska is the accessibility of the legislature to public input. I certainly appreciate this opportunity.

My employment, by the way, is with the Institute of Water Resources at the University of Alaska. I'm going to dwell on a specific topic having to do with what is kind of a professional fetish with me---it's energy and renewable resources. I have prepared an overview of what I think is a good suggestion, and I hope you will consider for use of the Permanent Fund.

Its purpose is in view of the inevitable depletion of our fossil fuel resources, even with Alaska's comparative wealth, it seems very prudent to begin to assess alternative renewable resources of energy. We have an inevitability facing us, so the transition to a renewable resource economy, the whole nation does---it's obvious to everyone now that sooner or later fossil fuels are going to run out. So we have to begin to assess our future. My proposal is future oriented. Everything I intend to state has a future orientation about it.

The proposal in specifics is to use the Permanent Fund and

other available earnings, and I am very familiar, by the way, with the Renewable Resources Development Fund---I certainly wouldn't hesitate to make this suggestion strongly toward that fund, because it has to do with research. Use for these monies, as I would propose, would be to research those projects which relate to renewable natural energy resources relevant for use in any and all regions of Alaska. The prospective types of energy resources which would qualify for that program include:

Hydroelectric power, including low head, low-gradient water power applications

Solar heating and solar agricultural applications

Wood burning research for heating

Wood lot management research

Wind power applications

Certain geothermal applications---not all geothermal is legally regarded as renewable, something many people don't know, but some geothermal sources are

Tidal applications

Earth heat and geothermal gradient systems

Bioconversion and waste conversion systems

Ocean currents

Any other naturally available energy source which can be shown to benefit Alaska and which can be demonstrated to be renewable.

In my proposal, I do a legislative review of the renew-

able resources development after 1974 and also all the pending and on-the-books legislation concerning the Permanent Fund use; I don't need to go into that. You're probably more familiar with that than I am.

I think the public mandate is worth considering in this whole process. I was fortunate to participate in the Public Forums that occurred throughout the state. I participated in the one in Fairbanks. Interestingly, Fairbanks had the highest of all areas, which the public attested to its recommendation that the Permanent Fund be used to loan to development of renewable resource industries. In Anchorage and Southcentral, 39% of the people who were polled favored loans for development of renewable resource industries. 32% in Southeast did likewise. A quote from the Public Forum proceedings was that "The enormous response to that choice as the top priority use of oil and gas revenues set the tone for the regional workshops and most of the meetings from Skagway to Metlakatla."

I was also primarily involved in the town meeting on energy which occurred here in March. Some of the ideas we polled on that were uses of renewable resources of energy. In particular I asked the question on the questionnaire, "Do you think that solar energy is practical in Fairbanks, Alaska?" Surprisingly, of the people who were present, 62% of the people said yes, and

only 16% said no, while 22% were not sure. We also asked for priorities for research in energy development, which were relevant to Alaska.

We asked that they be prioritized according to six questions, six topics, by the way, and the prioritization occurred in terms of research support, first was solar; second was geothermal; third was coal; fourth was hydroelectric; fifth and sixth were synthetic fuels and oil and gas. Now, I was called on the carpet there because I didn't mention nuclear. I didn't mention nuclear because I don't think nuclear bears much on the future of Alaska for the next 50 year, because of the scale of application. Please be aware that I wasn't slighting nuclear, but I didn't feel that it entered into the Alaskan picture in a relevant way. I think most energy authorities would agree with me on that.

So I think the mandate is clear that people are very interested in the use of Permanent Fund monies and the large amount of capital the state is going to invest in Renewable Resources Development Fund for renewable resources. I think the public consciousness is there. People are not comfortable with spending that money, I don't think. They like the idea of using that money for a renewable economy. It's not always not very easy to articulate that in public, but I think the Public Forum responses are significant in that respect.

Now in order to accomplish that goal, it becomes a political question, of course. I would suggest that not a large amount of bureaucracy would be needed to set up an ongoing research program. I would suggest that the obvious place is the University of Alaska. It's Alaska specific; there's a crying need for money to do Alaska specific research now because many of the problems which result in questions of relevancy in university research today are because research has to be nationally applicable to get federal funds. If the problems aren't of a national crying nature, it's very difficult to document the need from Alaska's point of view because Alaska has an, inevitably is the case, has Alaska specific problems. Consequently, we fall flat on our faces when we propose research that's energy oriented in an Alaska specific sense to a federal agency, and they'll say, "well, how's it going to work in Pittsburgh?" Obviously, it isn't going to work as well in Pittsburgh, and it doesn't have a whole lot of relevance to a lot of the lower 48 problems. So we just don't have the opportunity.

There are also more specifics on how I would suggest this be done, however, that remains to be worked out in a political way; but I would suggest again that the University of Alaska's ongoing research establishment is perfectly adequate, capable of administering this in a fair sort of way. I would also suggest that somehow, and I'm not astute or sophisticated enough in the politics

to know how it might be insulated to a proper degree, and I put proper in quotes from the political process. I would like some degree of autonomy here because again, as was suggested from two previous speakers, there is a problem of power and whatever the university's position is not always favorable in the public eye now, so we have a lot of political problems.

The level of support for an ongoing Renewable Energy Research Unit depends on several elements:

Of course, it depends on the amount of money available from the resources, the Renewable Resource Development Fund, and the Permanent Fund earnings. How much the legislature should appropriate for this kind of research program.

The level of support necessary to provide support for that research program, including what is felt to be adequate, in fact, which, again, is a political question. However, I'd be more than willing to try to document what I think is adequate.

The political importance and priority of developing alternative energy resources for Alaska. This is a question I don't think a lot of people have addressed. Alaska's been preoccupied with land issues and a lot of state-level problems. We haven't really had an energy crisis here. I think the

fact that these other problems have overshadowed the issue that a lot of attention hasn't been drawn to energy problems. I think it's inevitable that they will. I think it's very important that that kind of a consciousness be raised in Alaska, that we are always better off doing something which is not irreversible. Right now, every time we start up our car, we are doing something which is irreversible. I'm not saying we stop driving cars, but to get into a system which is renewable is where we need to go.

Okay, I was getting into the philosophical basis of why I feel this is an important thing to do. But our opportunities are enormous here. I have a quote in my prepared notes from Walt Kelly's Pogo comic strip which has supplied what, I think, is one of the relevant quotes for Alaskans, and he says, "We are confronted with insurmountable opportunities."

I think that is a very appropriate way to address the Permanent Fund. I think there are many problems in Alaska that are, indeed, insurmountable for various reasons. But I think the establishment of a Renewable Energy Research and Development Program is simply a matter of having the will and foresight to commit our Permanent Fund resources to this plan. It can be a great service to Alaskans and the nation to provide badly needed development experience for renewable resources, both to ourselves, to Canada, and to the rest of the nation. Thank you.

GRUENING: Thank you very much, Rich. There may be some questions. I appreciated your letter, incidentally, earlier. I hope you got back my reply.

SEIBERT: Yes, I did.

MEEKINS: You touched on a subject, I think, is so close to my way of thinking. I can tell you that the Renewable Resource Fund, although it didn't list that possibility, I think it's certainly within the definition of renewable resource. I was one of the people who drafted that legislation that finally passed.

SEIFERT: I was concerned about that, because a lot of the aspects that are, in fact, using the public documentation that I did, never was it specifically stated in any of the Public Forums that renewable resources would include renewable energy resources.

MEEKINS: Well, that's one of the problems, of course. Some people define even mining as a renewable resource. It depends on who you are, I guess, how you define it. In my mind, that was what we envisioned when we passed that portion of it. I have a couple of questions.

First, what are we doing now? What level of research in energy development is Alaska participating in currently?

SIEFERT: Most of it is still at the proposal stage. I would say there is an ongoing wind energy program. I'd like to consult. Lee, would you mind giving me a hand? This is my associate, Lee Leonard, who also has his name on our preparation. He also works for the University of Alaska Geophysical Institute.

LEONARD: From the University of Alaska standpoint, there are several research programs which are ongoing and offgoing. For about five years, we've been involved with some level of geothermal research, geothermal energy research in Alaska. But the amount of effort, which has been given to these projects is spotty; and the reason is, as Rich pointed out, that one of the problems doing relevant, applied research for Alaska is that the sources of funding are mostly on federal level. In order to get those funds, you've got to show that the work I'm doing up here applies to Alaska; but it's also, in some way, applied to national need. This is not always easy for us to document. We have had a great deal of trouble getting research funds to do energy research which is specific to Alaska. As we know, as with several other things, energy research---the environment of Alaska is so different compared to much of the Lower 48 that we require specificness which we cannot appeal to the funding agencies to show that we are worthy of so many dollars. We do, though, have---we are in the process now of maybe making a breakthrough---more money

has become available on the national level through ERDA, the Energy Research and Development Administration, in other areas. So it looks like some money is going to start to come through.

Another reason we've been frustrated is that in many states when you apply for research which is specific to a state's need on a federal level, one of the common techniques of getting research money at a university level and other levels is to say, "Well we're asking the federal government for X amount of dollars and a state agency, which is interested, is willing to put up so many dollars in a matching fund." Our state agencies, because of financial exigencies, have not been able to meet these requirements, which would have enhanced our proposals at a federal level. So we've been frustrated again.

We do have a solar project which is starting now. The State Energy Office is involved with some research in geothermal energy and some in wind energy. We do have an ongoing wind program at the geophysical institute, which is also suffering some of these frustrations of kind of on again off again. We have never---nowhere in the state, to my knowledge, is there an active program, which has been established and which is ongoing at a significant level of activity.

One thing I might mention is that recently I've heard comments in the media that there is a complaint that the University of Alaska is more research oriented than academic oriented and so forth. I think it's a testament in a way to the ambitions and aggressiveness of many of the university researchers, which has built up. It has been the work of these people which has built up a very big research facility at the university. They have done it almost with a majority of getting money from the federal area. They have not had the opportunity to get money from the state to do state-specific research. So I would say that the potential is there, that the people are there. There's a lot of good talent there. There's a lot of people who are interested in doing work which is state specific if they had a mechanism to keep their job and do it.

I think it's inevitable that this kind of---if monies become available from the Permanent Fund or from the Renewable Resources Fund to do these kind of things, we're going to see a growth in research; but we're also going to see alot more relevant research.

GRUENING: Thank you. Sally.

SMITH: Just one question. Lee, you and Rich and I have

kind of talked some of this over; but would you explain for the committee the relationship between the university research program and the State Energy Office?

LEONARD: The State Energy Office, when it was formed, there were ongoing energy research projects at the University of Alaska. At that time, which was 1974, I believe, the university entered into a joint kind of an effort to sponsor a seminar, a meeting, on energy in the state of Alaska with respect to geothermal energy and wind power. It was held in Anchorage. Since that time, this joint effort went on and we had this meeting and it was very well attended. People came from all over the state, from little fishing villages, from bush villages, not people that had vested interests but a lot of homesteaders and fishermen and carpenters and everything else that were just interested in getting off the high priced petroleum band wagon, so to speak, in rural areas mainly; because this, of course, is where energy research really pays off, when you get out in the bush where they're paying 25, 30 cents a kilowatt hour for electricity or a buck and a half a gallon for fuel oil. The proceedings of this were published and since then, the university has not had what you would call good relationship with the energy office, for a variety of reasons, some of which may be personal and some of which may be institutional.

But a problem with the university, with the university doing research, is that it must maintain its autonomy from political entities as much as possible. So the University of Alaska's research has always been conducted in the, so to speak, the world environment of research. That is, we go to funding agencies on the federal level and in some cases international level---in the case of the Geophysical Institute and Institute of Marine Science and so forth---to obtain funds. There were some problems with, when we were trying to deal with the state through the State Energy Office, there were some problems of a political nature, which suggested that the university might best channel its energy research through a state agency, such as the Alaska Energy Office.

Well, as you can see, I'm trying to make this as painless as possible. It was a very awkward situation. The energy office was, from the standpoint of the university, too political to really function as a proper funding agency or an agency through which the university could channel its research. As I said, as an academic institution and as an educational institution, there has to be a degree of autonomy. An individual investigator could go out into the world, whether it be the private sector, whether it be a federal agency and say, "I've got an idea which might pay off, if we can

do some work on it." Therefore, he either gets his funds or he doesn't. But it is very difficult to work through a bureaucracy which has political overtones in this situation.

GRUENING: Are you suggesting that they were tampering with the results?

LEONARD: No, no. I'm suggesting that a university normally to give a specific example---the feeling of the energy office was that if the university wanted to do energy research, let's say geothermal energy, let's say the university is interested in doing a research project which involves a technique for small scale electricity development at a hot spring---the idea was that normally this is the way it's done. The university or the investigator, who comes up with the idea---I don't like to keep using the word "university" because it really is individual people with ideas that go out and sell these ideas---an investigator gets an idea to do something. He applies to do research on this idea to somebody. He may go to an oil company. He may go to the state, a given state agency. He may go to the federal government, a given federal agency.

Well, what the energy office was interested in doing was being a channel by which energy research done at the university level in Alaska, that all proposals for this kind of work be channelled through the State Energy Office. The State Energy Office in turn would rewrite proposals or would apply for the money. When the energy office got the money, it would become the recipient of the grant. Then the energy office would sort of pass out the money to the university. Well, this is out of bounds in the normal way academic research is carried out in the United States. It became a little awkward for us to operate like that.

GRUENING: Do you have a question, Charlie?

PARR: I would like to make an over-generalization and see what your response is---that the state of art is that we know that hydroelectric power is feasible. We know that in Alaska solar power is probably not feasible. We know that wind power is feasible only in certain areas on a very small scale. We don't really know what the possibilities are for geothermal.

That's probably an over-generalization, deliberately so. But I'd like to know, in other words, the point I'm trying to make is do we really need to do research on all energy sources at this point? Or isn't the state of the art such that in some of them we already know the answers?

LEONARD: Well, one thing, which is another generalization, but might help explain this---there's been a lot of talk so far today about investment of Alaska's money in renewable resources and investment of money in the Permanent Fund in renewable things. Every big corporation in America, every multi-national corporation in the world, every government entity does research in one way or another to find out new ways of doing their things. That's how the United States became a great industrial nation, because of the Yankee ingenuity, so to speak.

In order for the Permanent Fund to wisely invest its money in Alaska, we have got to continue to come up with new ideas, new ways of doing things. What is possible to invest money in renewable resources, such as a lumber industry in the lower 48, which has been done maybe for a hundred years, may not be the way to do it in Alaska to make it economically feasible.

In other words, there are a lot of specific things in Alaska with regard to industrialization of the state, questions which have never been answered. So when people have, when you have a large, usually what happens is a guy comes up with an idea; and he gets an idea that you might be able to make money this way. He generates the idea and gets it going and then he finds somebody with the money.

In Alaska, we've kind of got this situation turned around right now. Right now, we're looking at a whole lot of money, and we're talking about investing it in renewable resources. But how? Are we going to use the same techniques which have been used for a hundred years or two hundred years in the Lower 48, or are we going to have to come up with new ideas? I think is the question. I would say, in answer to your question, we know hydroelectric power is feasible. But we have a lot of flat running rivers in Alaska. We don't know about low gradient hydroelectric power. A lot of this research hasn't been done. There hasn't been anything concentrated on it.

As far as solar energy is concerned, I have a folder over here, which has a concept of a solar hot water and shower facility to be used in a rural area. Now this is to provide showers and washing machines, coin-operated. A guy can make a little business out of this in a village to people who could not afford electric hot water at 24 or 30 cents a kilowatt hour and they don't have it now, and they won't have it in the future, as long as the price stays that way. This little system, which we've developed here, which we're proposing now to ERDA to do as a demonstration project, would only operate for about eight months out of the year. But if you're living in Venetie, that may mean alot to you---or some other village, which has a great deal of solar resources for a large part of the year.

Geothermal energy, we know, is feasible. The big concentration on the federal level and millions and millions of dollars of research has gone into researching big power plants, geothermal power plants, which are big; because the Lower 48 is faced with the fact of transferring their normal energy fuels, their normal energy resources to a new type. They already have the industry. They already have the business. All they've got to do is find a new fuel to use. In Alaska, we don't have that. We've got to find new imaginative ways to use alternate energy resources to spark industries. So that's one of the things. So, no, we haven't done enough research in geothermal energy as it applies to Alaska.

Similarly, with wind power. Wind power is an old technology; it's been working for many, many years. Alaska has a great deal of wind resources. When we consider our rural population, village populations, which, even if there is a big dam put on the Susitna River, you're not going to run a transmission line to Bethel and Galena and McGrath and Ruby and all those other places all over the state. You're just not going to do it. Sure, we can use the standard technology, which exists today, to give power to places like Fairbanks and Anchorage, where our big populations centers are. But what are we going to do about the rural areas?

If we develop, are we going to develop two huge meg-

alopolises, one in the center of the state and one down in Southcentral? Or are we going to diversify and develop small industrial, small businesses and so forth throughout the state, and include the native population, which for right now, exists in kind of a quasi-limbo outside of the normal economic structure? So I don't think it's enough to say that we know very much at all about how the potential of renewable energy resources and alternate energy resources apply to the state of Alaska right now.

GRUENING: Thank you. Do you want to follow that up?

PARR: One final question, if I might; and that is this: wouldn't it be desirable to do some of that research on the capability of transmitting power farther without losing so much of it? You said awhile ago we can't do this. We can't for example, build a Susitna project, get power out to McGrath and these various places. Right? Or similar things, okay. We all know there's a power loss as it goes---the farther it goes. This has been the thing. Wouldn't Alaska, in the long run, be better off with an overall grid for the whole state, if that became technologically possible somehow, rather than a number of small, independent, unconnected power sources scattered in a hundred different locations?

LEONARD: Well, I think that you may be right; I don't know. Let me preface my remark by saying that, there is a difference in philosophy in the technical community at large in the world today.

One philosophy says faced with diminishing resources, we're going to have to go back to the age of individualism. We're going to have to start looking at unitizing our energy resources on local levels and so forth. A large power company--- I recently was talking to somebody from Union Oil who was in my office talking about this same concept. This is a consideration in industry, big industry, as well as just in the academic community. That's one idea.

The other idea is well, maybe what we really have to do is find better ways to transmit energy, as you suggested. It's very likely that the state of Alaska should fund research which investigates cryogenic transmission lines and various numbers of transmission lines. Probably you wouldn't do that at the University of Alaska. You might fund MIT to do something like that because they've got more horsepower, but I would say yes that that's something that could be done. At the same time, you want to do the other kind of research as well and in that research, hopefully the better ideas will come out of it.

JGAN: Because the constitutional amendment stipulates

that Permanent Fund investments will be income producing, I wanted to ask one of these gentlemen how research and development is income producing?

SEIFERT: We are referring to the Renewable Resources Fund.

GRUENING: Either they're referring to the Renewable Resources Fund or the dedication of the Permanent Fund interest. I corresponded with Rich on that.

SEIFERT: I would like to reiterate what was said. It is very difficult, this is a question that researchers always have to respond to---how are you going to justify your existence? All I can say is one of the greatest testimonies to the value of research is the fact that every, as Lee stated earlier, every major corporation, every major government, every major entity in the world does research. Obviously, it's paying off. In the annual research budget in the United States, there is over \$36 billion invested in research.

The benefits of research are not easily made obvious, because they're hard to document. If we were to develop and demonstrate the feasibility of solar hot water heating in Alaska---which, by the way, is a feasibility, I know it is, I wouldn't stand here and

say it if I didn't believe it and hadn't done the calculations, it is a feasibility, and it's an economic feasibility today, because our electric is so expensive. Even if you only use it half the year, it's an economic feasibility. If we could demonstrate that to people, show them that it's an economic viability, decrease our use of fossil fuels sources, decrease the expenditures of the public---that's our documentation. You don't do it unless you get the chance to do it. But once you can give people the opportunity to see what the possibilities are, that's what research is all about, expanding the human potential, the obvious technical potential. That's the only reimbursement energy research can ever provide.

MEEKINS: I think most of the members of the committee I've talked to would certainly recognize that there are benefits from research. I don't think that's exactly the question. The problem we have is a constitutional one with the Permanent Fund in that even though there may be social benefits, if we can't quantify them, we probably can't justify legally investing money in areas that don't return money back to the fund with interest, so they can't be social benefits or benefits that are disbursed other than the.....

SEIFERT: I wouldn't be certainly up here and guarantee

a fixed rate of return in that sense. I look favorably toward the Renewable Resources Development Fund. It's a less risky political way to go about this, but nonetheless, I think, I have faith in it. I have faith in the idea. I think it will document some value.

GRUENING: Okay. As I said, I'd like for somebody here who can't make it back after lunch. I would like to reconvene right at 1:15 sharp. If there's somebody who would like to testify now because they can't make it back later, we can do that. Mr. Weeden.

WEEDEN: Mr. Chairman, my name is Bob Weeden. The Permanent Fund problem is a complicated one and neither we as citizens nor you as legislators are really used to dealing with the problem that carries such a tremendous implication way beyond the time when you are no longer legislators or I am no longer alive, etc. The problem of grappling with a long term future is a tough one.

We have a couple of general purposes, I think, with the fund. One of them is that to some degree we don't trust ourselves to be rich right now. We don't know that we will really make good decisions about a lot of money when we have been used to not having a lot of money. So we are adopting a strategy of trying to smooth out and length out that curve of income from exhaustible resources. We're saying let's live leaner and longer rather than fatter and

shorter, if indeed that's the choice we have.

Another general purpose though is that we feel that the oil wealth ought to be translated into human welfare, and I think the interesting thing there is the money that we all talk about is only the medium, it's not the message, it's not the end product, which leads me to conclude that what we are about is establishing a mechanism, an additional mechanism beyond the governor, beyond the legislature itself for making social decisions of a very major magnitude.

One of the stray thoughts that has occurred to me that I would like to leave with you is that the fund and the use of the fund has to be firmly guided by policies that are developed by all citizens of Alaska acting through a diversity of representatives, who are, in fact, accountable for their decisions on behalf of the public. I would not like to see both the policy-establishing group of the Permanent Fund and the managerial group dominated by bankers. I feel that although bankers can make good social decisions, that their chance of doing so is no greater than a trucker's or a forester's or anyone else's. I would use an analogy that when I would really like to have mechanics around to keep car running, but I rarely ask them where I should drive it. I think that's the essence of the difference there.

The income from the investments may, in the fairly near

future, turn out to be kind of an embarrassment itself because it may get to be fairly large. The constraints on that income are not as great as you have pointed out on the capital itself. I would suggest that we look very strongly at putting income, a large share of the income from capital funds investments, Permanent Fund investments back into the Permanent Fund unless we prove in the interim that we devise really firm public social goals and that we can spend that income money wisely in pursuit of those social goals.

I feel that the fund should not be used to underwrite projects that could not stand on their own in the market place, I say that knowing that there must be a qualifying thing. When representatives of the people have decided that there is a social goal that mutually can be agreed on that is so important and that cannot be taken of by the market place decisions that there must be some kind of a front end loaning of money, there must be some kind of subsidy, if you want to call it that, that's fine. I don't object to that at all. But I feel that should be the exception to the rule rather than the rule itself.

There has been some mention in testimony today about the scale of projects, and somehow people are focusing on the idea that the Permanent Fund can do big things in a big way that other funds cannot do and private money may not be able to do. I

would maintain that if you look at the product in terms of human welfare and society, the scale of the project is of very little consequence. There can be bad as well as good big projects and there can be good as well as bad little projects. The need of those projects, at whatever scale, for Permanent Fund support is what needs to be demonstrated. The fact also needs to be demonstrated that those projects, big or small, are really in pursuit of social goals that we agree on are satisfactory. That's one of the prime things we should focus on again. Money is only the medium. It certainly isn't the message itself.

I personally feel that we should not use the fund in ways that have as one of their major results a large increase in the population in Alaska. I say that because I know a lot of people who do not feel that we need millions of people up here. There are a lot of people who feel that some of our amenity resources are in scarce enough supply right now, the competition is keen enough for them right now that we would not really need to consciously go ahead and add more people to the state of Alaska as a goal in and of itself. I think it's fairly clear that certain proposals for use of Permanent Fund monies would have, as one of their major effects, the increase in numbers of people coming here. If you propose to eliminate income taxes, for example, you create a haven for

people who don't want to pay income taxes. That in itself would be a major incentive for people to come here, establish a residence, if there is a residency requirement tied to it, etc. Those are the sorts of things and I toss this out knowing that a good many people will not agree with this goal and that doesn't bother me a bit. All I'm saying is that we should decide mutually whether or not increasing our population is, in itself, a desirable goal. Whatever way that decision goes, that will be one of the policies that will influence the expenditure use of Permanent Fund monies.

That's really all I had to say at this time, Mr. Chairman. As I say, I'm easily embarrassed in this whole field of income investment. I don't deal in the figures that we're talking about here, personally. I will, however, try to acquaint myself with what seems to be the most important parts of the nuts and bolts of this thing as I become more acquainted with it.

GRUENING: I hope you do that. Thank you for the very thoughtful statement. I was intrigued by your comment on the use of the income. At the same time you mentioned the fact that you think the investment decisions sometimes, at least the policy of them and whether or not to make them in a particular area, could be better handled or as equally well handled by let's say laymen.

In that regard, would you think that the use of the interest,

in terms of paying it out, could be equally handled by the individual who received it? In other words, if everyone got an equal share of the income, aren't those individuals equally competent to spend it on what they see fit, as opposed to, say requiring that we re-inject it in the fund for whoever the fund managers are to decide what to do with it? See my point?

WEEDEN: Yes. I do, and what you are saying is that one of the channels into which we might like to put our oil wealth is immediately into the private sector for the individual to make her or his own decision. That's fine. Do you always then ask to what extent? Is 30% the right figure? Or is all of the income? Or, you know, what is the right figure?

That really is basically a decision of how much to favor the present generation as opposed to the future generations; that's only partly true, because presumably the private individual could put that money into a trust for children and so on.

But it's also partly a decision to increase activity in the private market place, which is already, by the way, being increased through the other channels through which oil wealth passes.

All we're talking about is the state, public revenues. We're not talking about the private wealth that is generated through exploiting the oil resource. Certainly a lot of the people who might get part of this Permanent Fund income monies as their very own are also getting a share of the oil wealth in other means by having jobs at high rates of pay, etc., making good business investments.

So, I really can't say that I have a preference there. What you do run up against though is the same thing I mentioned before---if it looks as though your decision to put Permanent Fund income monies back into the hands of private individuals is going to stimulate people to come to Alaska, so that they can gain a share, then you ought to recognize it and decide whether that's what you want to do. Is that a sufficient disbenefit, let's say, to override the benefits you see from doing it?

GRUENING: You mentioned subsidy that should be an exception to the rule. What entity do you think ought to be best to decide on who gets the subsidy? The legislature, the governor, I'm just giving you these examples---they're not the choice you could pick---if you're not going to use the market test in terms of, let's say the Constitution---what entity do you feel is the best one to decide who gets the subsidy?

WEEDEN: I think, in terms of who gets it, I presume you don't mean the individual applicant?

GRUENING: Which Alaskans, general, as a class? If you look at loan funds, there are certain classes of Alaskans that get more loans than others. If they are subsidized loans, they get a greater benefit than others that, say, pay loans at the market rate. So the political question, you, the political system allocates benefits. Part of that system, what entity, my question is...

WEEDEN: My feeling is that to provide a subsidy is an important decision that must stem from some social goal that you have and we are talking then about those decisions must be generated, in my view, by those who are accountable to the public for developing and articulating social goals, the legislature and the governor. Now, if you ask as between those which, well there are pros and cons on either side; but I would say that the legislature, being obviously more diverse by 60 times, is the one that should be setting the overall policies including the policies for how to disburse this broad subsidy benefits, if there are subsidy benefits to be disbursed. The governor and his administration help to carry that out, and the Permanent Fund policy group has

other levels of policy that they have to make decisions about. I think it's a tiered structure, but I simply see the legislature at the top.

GRUENING: Any other questions? Russ.

MEEKINS: Mr. Weeden, we've had some testimony from some of our consultants. It's a funny thing. They are very concerned about us sort of diluting the power or the benefit that we can distribute from investments or anything from the fund by the influx that people that that investment might create.

What they've told us, and I think it makes sense to a certain extent, is that amenities are also part of the real wage. People come up here for higher wages; they also come up here for more amenities. The person who was giving us this, he followed this logic out and came to a different conclusion---he came to the conclusion that we should distribute, if possible, we should distribute the principal of the fund, which, of course, we can't do constitutionally. But lacking that, at least all of the interest from the investments of the fund which should be maximized for yield, should be distributed to the public because he felt that anything else you did with it, any social benefit, any economic benefit at all would be completely diluted by the in-

flux of people to obtain that benefit and that the real wage counting amenities would always equalize.

WEEDEN: In other words, if we spent the income in these ways we would, let's say, diminish Alaska's stock of amenity resources. Therefore, people would have to use that income to travel somewhere else in hopes of finding them. Maybe that would be the case. I don't know. No, Russ, this is one of those areas where I am not convinced that I know where I would vote on this question of using income, but I think you obviously understand the overall goal that I'm looking towards. I don't know how to get there.

MEEKINS: It's sort of Catch 22 we're confronted with because I'm tempted to suggest that we use it for creating a better quality of life for people, economically and other ways. At the same time, I can see, we've had one example given to us, I think it was a very good example, that in New York state changing their welfare laws some time back, and as a direct result of that, two million people immigrated to New York, mostly Puerto Ricans, but other people also. Consequently, they then went into a deficit situation in their welfare; and they didn't have as much money to distribute to the large amount of people, so it just sort of under-

cut the benefits they were trying to give out because a larger number of people were claiming them.

Alaska, with its small population, is very vulnerable in that sense, it seems to me. One of our people testified, I'm not sure it was correct, that the number of unemployed in the city of Detroit is larger than our work force here. In a situation like that, if we attempted to create jobs or if we attempted even to make life better for people without jobs, we may find ourselves undermined in the very principles or very things we're trying to get at.

WEEDEN: I might point out that all of us are really puzzled and the Pogo comment of "insurmountable opportunities" is really neat, I think; but what we can understand, too, is that we can manipulate the amount of flow of revenue into the Permanent Fund in various ways. We can manipulate it by changing the tax structure, for example, changing our royalty share. You might say that well, if we don't know what to do with our money, why we just let the oil companies pocket all the profits and they'll certainly take it out of the state and solve our problem.

Another possibility is to approach the leasing of state lands for oil and gas, in other words, gear the development of the basic resources over time to that amount of income that you think you

can handle. I guess Norway has kind of approached that strategy that way. They say, "look, we just simply won't lease a piece of land until we think we want the money." That's another way of either starving or enriching the Permanent Fund over time. So there's lots of things we can do with our left hand if we can't do it with our right.

GRUENING: Any further questions? Thank you very much, Bob. We'd like to come back promptly at 1:15 and anybody who wants to testify, we'll be ready. Thank you.

BREAK FOR LUNCH

GRUENING: I think we can start to call this thing back to order, and call up anybody who wants to be first in the afternoon portion of this. Sorry about returning a little bit late. Go ahead. We had a slow waitress. A good lunch, but a slow waitress.

INOUYE: Thank you. I am sorry I have just a single copy to distribute to you.

My name is Ron Inouye. I'm a resident of Fairbanks and am employed at the University. My comments to you are strictly my own.

I appreciate the opportunity to share with you a few of my concerns regarding the Permanent Fund. Although the thoughts I express may not directly fit what may currently be the focus of your committee's discussions, I do hope that a few of my ideas may creep into some of the committee's minds and find a hospitable niche, to be retrieved at the appropriate time.

My plea is pretty much a standard one, that of increasing help to state agencies for the preservation of historic and cultural artifacts and manuscripts. I believe we are all aware of the usual arguments for such material, culture and manuscript preservation pleas resulting from vanishing life styles, big time economics decimating human values, and all of those kind of arguments. However, I would like to pursue the issue a bit differently.

If the purpose of the Permanent Fund is essentially economic and your concerns are accruing interest and getting "a good return on our dollar" I would like for you to consider the following:

Tourism is an example. It's becoming a larger and larger part of our state's economy. Why do tourists come here? I bet it's not to see how many new homes have been built in Anchorage or Anaktuvuk or to shop in any of one of the new malls that are popping up all over the state like puffballs after a lucrative rain. Many of these tourists come up to see the undeveloped areas and to look at the historic sites and artifacts of the past. The

tourists love the local museums and historic buildings. They stay in hotels and spend money on transportation and meals, they visit those museums and historic places. Without those records of the past, the tourists wouldn't be here.

What economic contribution comes from the current educational and research communities of our state which use as their raw material the resources of the past that are now discreetly preserved and made available for present use? Take a look not only at those on private and state payrolls servicing museums, archives and libraries, but also those who make use of those collections. Those depositories of information are located all over the state from Ketchikan to Barrow. The users of these depositories include the lawyer, corporation executive, environmental impact statement complier---all of whom are linked in their work to information from the past. They indirectly make their livings too from the past.

Needless to say, I believe there is a long-term return on the dollar for every penny spent by our state government in historic preservation and the acquisition and care of historic manuscripts and material collections. These are the kinds of things I believe the state should be promoting through its Permanent Fund development.

While I believe that Permanent Fund money should be partially devoted to such things, I believe too that good management

principles should be applied.

Several years ago the Kate Pullen Memorabilia Collection was lost to and by the state. That historic Skagway collection was offered to the state as an intact collection and would have been an asset to all of us. Unfortunately, the state was unable to get its act together and the Pullen Collection was sold off piece-meal to the highest bidder in Seattle. I was in Seattle during that sale and saw many Alaskans there trying to retrieve bits and pieces so that they could be returned to the local museums within the state.

Regardless of our personal feelings about the value of the Pullen Collection or those that that represents, the situation points out that our state has inadequate policies to deal with such situations.

When first teaching in Ketchikan, I was very interested in having my students learn more about Northwest coast art styles, particularly that done in the Southeastern part of the state. In checking for good examples from the late 1800's and early part of this century, I found that my students would have to go to Portland or Leningrad or Denver to see them. Is there not a way that some of those items could be returned to our state?

I feel guilty and powerless to do anything when I hear about another art dealer from Seattle, or Anchorage for that

matter, buying another collection for disposition when really the state has a legitimate right to look out for the public's interest in such situations. This pattern continues because we have yet to find a creative way to ensure that cultural materials and manuscripts of significance stay in Alaska, open to public use. Had we conceived of these materials initially as resources of increasing value and developed good management policies for their acquisition and use, we would not now be wringing our hands and bemoaning the loss of so many valuable aspects of our state's history. Thank you.

GRUENING: Thank you, Ron. Representative Meekins.

MEEKINS: Ron, thank you for those comments. I found them very persuasive, quite compelling, especially from a viewpoint of my duties as a Finance Committee member. Chairman Gruening is also serving on the House Finance Committee. My question is in regards to the specific purpose of this hearing which is a testimony in regards to Permanent Fund investments. One of the limitations on the Permanent Fund, which we explored and talked about quite a bit in the morning session, was that it must, by Constitution, be income producing. There is some debate about exactly what that means. We, I think, do have some agreement that the income producing must be a

direct income. In other words, dollars must flow back into the Permanent Fund. It can't be social benefits put into money terms. So I am wondering if you have any, if you thought of it in that respect, and if you have any ideas to how we could accomplish your purposes with the limitations of the fund.

INOUYE: Well, I think there are probably a number of ways to approach that. One would be to, in fact, find a way to squeeze around the intent of the law. The other is to maybe just change it, because we found that we're dealing in a very marginal area now, where there is very little support, because you can't quantify the benefits of such things. Similarly, you can't quantify the benefit of research. I think Rich Seifert pointed that out fairly well today.

There is really no other source for these kinds of things to remain in our state for all people to use. I think if maybe we broaden our definition of what income producing would be, to take a look at the fact had we bought that Pullen Collection, its value on the market now would be so many dollars more. If you arbitrarily wanted to sell it and spend that increased amount of money, you could.

MEEKINS: Maybe that's an idea right there. The appreciating

value of the artifacts or whatever we bought might, I don't know, I'm just thinking, but that the...I'd just like to say two things.

One is that I was in the legislature when we failed to purchase the Pullen Collection, and I was on the Finance Committee and voted for it, but unfortunately, it didn't prevail.

Secondly, I think that you have to remember that the words income producing are not in the law by legislation. That was in a constitutional amendment voted by the public. In order to change it, we'd have to have another constitutional amendment to change the language. As a political matter, that's very unlikely to happen, I would say, since the legislation other methods in order to accomplish that besides changing the law itself.

INOUYE: Right. I recognize that and I think in my earlier comments, I sort of addressed that by saying, "I hope you keep these things in your minds, and then when the appropriate time comes, that you as legislators will see a way to possibly help us." Because I am getting more and more concerned about those large collections in Alaska that are

just barely surviving. Certainly, we're aware of one major one in Southeast, probably two or three, that could very easily leave the state unless we have some strategy to have money available in a fairly fluid form to get those things purchased at the time they're available. If we have to wait for the legislature to appropriate the money with all the appropriate politics, our chances are gone. I think Kluckwan is a very good example of that. I think the history of that case is not unique and that it has been going on for many years. Some place in the middle of all of this, I think there is a string of logic that somehow we can attach to something. All I wanted to do was raise the issue with you.

GRUENING: Thank you. I always think there's more than one way to skin a cat. The Permanent Fund may not be the most appropriate institution to do it, but you could either do it through the use of the Permanent Fund income directly purchase these materials or set up a special grant fund in the General Fund to do that or again maybe the Renewable Resources Development Fund--- which doesn't have to make loans, it can make grants---could do it. I think maybe you could write under the tourism loan, maybe have a grant system and have some entity administer, be able to administer quickly enough, so it can, at an appropriate time, step in and prevent the loss of these priceless items. You might give some thought to how that might be administered in terms of---if

you're not going to have it directly run by, let's say, Commerce or a special department, how you might have it structured and who would serve on it.

INOUYE: I wanted to make clear too that there are many manuscript collections that I think would equally fit into that area. For instance, there are many things in the University Archives that are really invaluable; but I have a feeling there are a lot of other things that should probably have been deposited there, that unfortunately we don't have now.

MEEKINS: Ron, one other thing. I serve on the subcommittee that is looking into the Renewable Resource Development Fund. If it's alright with you, I'll send a copy of your comments to this committee to the chairman of that subcommittee, Terry Gardiner.

INOUYE: I'd be pleased if you would do that. Thank you.

GRFJNING: Thank you very much, Ron. Yes please.

MATSON: My name is George Matson, the Executive Director of the Fairbanks Environmental Center. I don't have any prepared testimony, but I would like to make an appeal to you

that the money from the Permanent Fund be invested in environmental research, environmental baseline studies, fish and game, fish and wildlife and habitat. These are renewable resources, and I know the question you're going to ask, how do they produce income? Well, I think, you can look at this in a number of ways. If you look in your booklet here, it refers to the origin of the Permanent Fund, and it says that the fund evolved as a means of preserving the Alaska lifestyle. I think fish and wildlife and the habitat are very much a part of this. So I think some of the statements and some of the reasons why the Permanent Fund evolved are very much in support of why a broad definition of income should be applied to how the Permanent Fund is spent.

I think, also, we're all familiar with the environmental impact state requirements and things like that. You can directly relate the quality of the baseline study to the potential for resource development. If the baseline data isn't there, the resource development is jeopardized. The resource developments produce the royalties and the leases and everything else from which the Permanent Fund feeds off of. So there's a relationship there.

Also, I think, you can relate the protection of the fish and wildlife and habitat to social costs. One thing I would like to point out to you, maybe you're not too familiar with it, I just came back from Barrow. I spent a few days up there, involved with the Inupiat in terms of the bowhead whale situation.

They're faced with a decision by the International Whaling Commission to, well, in fact, the decision has already been made, not to allow any bowhead whaling starting the spring of this year---next year.

It doesn't appear that the justified position on the International Whaling Commission's part, and in response to it, the people, the Eskimos in the North Slope area, have put together what I consider to be a very excellent proposal to look into the population dynamics and habitat of the bowhead whale, in fact the whole habitat, which you might define as the Arctic Ocean. They're very sincere about this. They want to protect the whale; they want to protect their culture, the two are related, but this proposal they have, which is sophisticated, uses an inventory as well as combines the knowledge of the whalers is a pretty extensive effort.

They're concerned enough that they have taken their dividends from the North Slope Borough---30 some hundred dollars and applied it towards the start of the study. However, the study is going to be about \$13 million and they don't have the money to do this. I think it would be very appropriate if the Permanent Fund were to put some money into this five year study that's being proposed. You can, here again, you have to, if you take the rigid interpretation of

what is income producing, you might not be able to justify it. But if you look at the alternatives and apply a little flexibility, you'll see the social costs, if the study doesn't go forward.

Without hunting of the whale in the Artic Slope, there's going to be all kinds of social costs in terms of welfare and transporting food up there and everything else. It's not desirable, I don't think, from the state's viewpoint or the people that live there. Like I mentioned, I don't have a prepared statement. I just wanted to point out that I think this is a legitimate need, and right now, I just came back from a very intense exposure to a very legitimate situation.

GRUENING: Thank you very much, George. I attended the Inuit Circumpolar Conference, and I remember when that was discussed, the people were very concerned about it.

I think the question facing this committee with your suggestion and that that was just made on artifacts is one of dealing with all the proposals with the appropriate tool.

One point we tried to raise in the brochure, and I don't know whether we made it clear, is that there are two funds that the legislature deals with. One is the General Fund, which in terms of revenue projections, is going to be probably larger than the Permanent Fund to the extent that we've derived money from

our oil wealth, the larger portion of it, as the constitutional amendment now stands, will go into the General Fund. There are no restrictions on the General Fund as to how it can be used. We could spend it to study peanut farming in Alaska or we could use it for, say, baseline data for the bowhead whale situation. That's one thing we have to address--- which is the most appropriate tool for it. I'm saying that your proposal, your suggestion that we look into it is a good one, I know, I think, I hope the governor, at least, who has been up there for that and has expressed some concern, will have a suggestion as to where the money should come from.

MATSON: He expressed concern but he didn't express any solutions or absolve the state from being a part of the solution. I think the state could be, they could exert some leadership here and say the state is just as concerned and is going to chip in to this \$13 million or whatever it's going to be to do this study.

In terms of income producing, you might point out that what they want to do is develop a sophisticated monitoring system to measure a number of different types of signals from whales, acoustical signals and everything else. This type of monitoring system has all kinds of applications in other OCS areas. So attached to this, you could have a license.

The license would generate income because it would be bought, you know the concept or maybe even the whole package, the hardware and the software could be bought by someone else to monitor some other species or maybe even by the Defense Department to monitor submarines for all that matter. But basically, the mix of sensors they want to put into this, I think, has a lot of potential in other areas, and so, like I say, if you use a little imagination, you can find out how it would produce income. Just having a license would be one way. Patent, I should say.

MEEKINS: Just to define terms here---we have, of course, as we've mentioned, there are several funds. We have the Renewable Resource Fund, which your suggestion would probably fit under that definition---it does not need to be income producing.

Then we have the General Fund, which is used for budget purposes, but there is, at this point, projected to be a surplus of revenue over and above what we spend on the operating expense for government in the General Fund, so there'll be a surplus in the General Fund.

There'll also be a surplus revenue in the Permanent Fund. The Permanent Fund is the only one that's limited to income-producing investments.

In fact, the revenue from the Permanent Fund is not limited.

If we make 5% or 10% return on a billion dollars in the Permanent Fund, that's quite a substantial amount of money in itself. That money is not limited and not subject to the same constraint. So you have of the four vehicles there, you've got three of them that are not limited.

MATSON: One reason I wanted to point this out is that time is of the essence here. This whole system would have to be operating sometime next spring. Now if money comes from the General Fund, the legislature would have to be in session first. I'm under the impression, it may be wrong, that you have the ability right now to commit money from the Permanent Fund.

GRUENING: No. That is one impression I want to clear up. The Commissioner of Revenue---there's about \$7 million that has collected in the Permanent Fund now. That's a total amount because the pipeline hasn't been in operation very long---the Commissioner of Revenue is authorized to put that into essentially a savings account. He wouldn't be authorized to do anything else with it. We'd have to change the law to authorize him to do other things with it.

Because of the constitutional requirement, I doubt whether we could change the law to allow grants or investments to be

made that didn't produce direct income. Now this doesn't mean we couldn't use the income from the Permanent Fund to do what you're doing, or these other loan funds. Actually, your problem probably is only addressable by the Permanent Fund in terms of the time frame you're talking---I mean the General Fund---in terms of the time frame you're talking about, because the General Fund has right now, it's got a cash turnover of close to a billion dollars. That's the only fund that has the kind of money you're talking about. I don't know how much you're suggesting the state kick in, but...

MATSON: Well, the Department of, they're approaching the Department of the Interior. They're using their own money as much as they can. I think it's a significant commitment to take all the dividends from last year from the North Slope Borough and apply it towards this study.

MEEKINS: Of course, if time is your problem, the Renewable Resource Fund has no money in it yet. It doesn't even start collecting till 1978. The Permanent Fund has just a few million dollars and there's no income of any great amount being produced by it yet. That income is going to be reinvested anyway under the current law. So nothing could happen till the legislature meets. Your most likely vehicle, in fact I think, your only one

if you want it within---by next spring is the legislature. Out of the General Fund, just a regular appropriation.

MATSON: Well, I think there's another point I'm alluding to, I haven't brought out is very much in accord with what Bob Weeden mentioned. I'd hate to see the Permanent Fund be defined according to what's acceptable to bankers. I think the tone of how this whole thing started was it's for the basis of the people; it's not for the basis of feeding more money to the bigger and better for fewer and fewer. I think, unlike our rate structures and some of the other things, it should be structured so it benefits the smaller person more so than the bigger person, the bigger corporation. I appreciate what you're saying but taking a rigid interpretation to me comes across as it's going to favor those who are higher up in the power structure to tap into this.

GRUENING: We're trying to avoid that. I'd hate to see it, like Mr. Weeden, benefit the bankers. They need it least.

CARPENTER: I was just going to elaborate a little, George. We have to keep a clear focus, I think, on the principal and then the income from that principal. One of the basic thoughts here is that if we adhere as we are mandated to a strict fi-

nancial interpretation of the income producing for the investment of the principal of the Permanent Fund, then the types of projects you involve to speak of, the research that's necessary and so forth will ensure us of monies down the road income for which these restrictions are not placed. I think, though, that if we try to depart in the investment of the fund from a strict and literal interpretation of income producing will be, in fact, defeating your interests and Bob's in the future. We don't want to dissipate, cannot dissipate the fund.

MATSON: I'm not sure the best way to address these needs that I mention, but I want to be sure that in the mix of all the tools you have to work with it does get its fair share.

GRUEING: You don't fall between the cracks.

MEEKINS: I might just say something too. I think that the points you make are very good ones, and the committee, I feel, is in agreement with your attitude essentially. We see it---what we're trying to find out and what I don't think we do have any great consensus on in the committee or in the legislature is how to go about getting benefits to Alaskans and Alaska society. We certainly don't want to benefit just the economic part of the state, just the bankers and other people who are involved in

financial dealings. The question is, is it better to do that by investing that money in very high yield activities or investments and then using the income from that for social benefits or whether we should use the principal and directly invest the principal in things that might be socially beneficial? That's the only question.

MATSON: There is a potential for high yield on these things, I think the availability of fish and game in Alaska has a very dispersed high yield to a lot of people. To Rich Seifert, it was asked how you quantify this. I think it's not easy to quantify, but it's clear how you quantify these things. It's difficult because the benefits are dispersed. Its not the same as if some corporation has their income coming in and selling products all over and they can work at their bottom line. The benefits don't channel into one area---channels to the whole public and what you have to do is do some economic research and breakdown of who benefits by this and who loses by that and through the EIS process, I've seen other areas where there are quantified things like recreational benefits. In fact the Corps of Engineers has become pretty good at saying, "Well, so many user days is worth this much to the economy." I think you can do the same thing here. It's just not as obvious because the benefits are dispersed.

GRUENING: Thank you. Any further questions? Thank you very much. Do you think it's quiet enough to open the door now? Sandra, love to hear from you.

STRINGER: My name is Sandra Stringer, and I'm here speaking for myself.

First of all, I would like to thank you for coming to Fairbanks to ask for opinions. I think that this is certainly a step in the right direction in terms of getting public input and also spreading knowledge on what the Permanent Fund is and what it can and cannot do. I think it's evident from some of the people who spoke earlier today and certainly from myself, from my own lack of knowledge as to what are the real specifics in terms of what the Permanent Fund was designed for. I found myself, a little earlier, in listening to George and agreeing with a portion of what he said and listening to Rich and to Bob Weeden. I also found that I agreed, a little bit to my surprise, with Representative Carpenter. I think that I really do agree that money is a means of transaction. Therefore, we must be extremely careful that the principal is invested in such a way that we are going to continue to get money from it, that the interest from the principal is going to continue to come to the state.

However, it seems to me that there must be a way, there should be a way in which to invest this money so that the money could

perhaps be invested in the state itself, in various enterprises within the state hopefully or at least a portion of the money, and that there would be spin-off, good spin-off on that, and that the interest drawn from this investment can be used to subsidize such things as research and as projects, various projects which have been mentioned, which have no source of funding right now and which could bring great benefit to the entire state, even though that benefit could not necessarily be quantified in the monetary fashion.

I wish I were able to suggest some way of doing this; I really can't. I'm quite ignorant in terms of investment, in general, and certainly don't have any specific suggestions to offer you as to how to invest the Permanent Fund. However, I do feel, as Bob Weeden also stated earlier, it would be a very good idea to be sure that there is some general citizen input along with your money managers, along with your bankers and your investment brokers that there are some ordinary citizens whose opinion is asked, not, of course, for the technical end of things, but just to get an idea. Some people who have lived in Alaska for awhile and who plan to live in Alaska and who want to see the state prosper and grow however prosper and grow is defined by the individual. That's really about all I have to say. Thank you for coming. I hope you come again.

GRUENING: Thank you, Sandra. Any questions? I am glad that you got up and didn't feel intimidated by the seemingly technical nature of it because none of us know any more about investment banking than you do. That's not what we're interested in. We're really interested in how people think the Permanent Fund could help Alaska. I'm glad that you came up here and gave us your philosophy. That's really where we're at, at this point. We hope to come back to Fairbanks too when we have a proposal and hear some more.

STRINGER: Thank you. I think that certainly the people in this room are reflective of a vocal portion of the community. I think they'll have a lot of good ideas.

However, I know that there are many others in the community who might have come today if they felt they had something to offer. Many people that I've talked to felt that because of their lack of technical expertise, they really didn't have anything to offer to the committee and were reluctant to take up your time and their own coming down and offering some sort of general comment. Please be assured that there are a lot of people in the community who are concerned and who will continue to try to become informed. I think that the Alaska Forum last spring, for instance, there was a discussion of the Permanent Fund at that; and a lot of people started thinking at that time about the subject.

Most people don't have the technical background, as we've already gone over, to offer firm suggestions; but I think they shouldn't be discounted as being, say, disinterested. They are interested; it's just that they don't have the background.

MEEKINS: Sandra, do you think that there is a need for more information about the Permanent Fund to be distributed in some way or another to the public?

STRINGER: I think it's not so much---certainly there is an amount of information available. I think it's not so much lack of information, as most people in our society, which is already so highly specialized in so many areas, most people who know nothing about oil, for instance are somewhat reluctant to talk about oil policy. Most people who don't know much about mechanics are reluctant to offer their suggestions about mechanical things. I think it's generally just, not so much lack of information as a lack of, I don't know what, an assurance on the part of the people on what they're speaking about.

I think you should continue to attempt to get word out to people that there is a Permanent Fund because, often in the

rush of every day life, people tend to forget---"oh, yes, I remember reading something about that or hearing something about that a month ago or two years ago or whatever." Since it's something that will continue to affect us, and far more so than right now, in a few years, that a continual stream of information must be put out and also you must always assume that when you put out that particular piece of information, that no one knows anything and start from point one recapitulating, if necessary, because people do tend to forget, even those who are interested.

PARR: Sandra, you mentioned that you would like to see at least some of the money invested in the state. If the state could get, and I'll take figures out of the thin air here, if the state could get, let's say, 7% in New York in some kind of investment and could only get 6% in the state of Alaska by investing it in the state or 5% or something, does that seem like a good trade-off to you? In other words, not those specific figures, but would you think it would be desirable to accept perhaps a lower rate of return by investing in Alaska? Do you think the benefits would outweigh the loss of interest dollars?

STRINGER: I think probably that it would depend a great deal on the projects that you know what the two projects were that were being invested in, and the exact amount of loss being

experienced and also whether you're talking about investing 100% of the money this way or maybe 50% or 10%, it would vary a lot. But it seems to me that under certain given circumstances, the loss of financial return to the principal, if it were not too great and the project were sufficiently worthwhile---of course this is all a very subjective evaluation---that it would indeed be a trade-off that could be acceptable. Because after all, the money should be benefitting Alaska.

PARR: Thank you.

GRUENING: Sally.

SMITH: Sandra, if I may just add for the benefit of anybody else who lacks self-confidence to come and speak as you have, I know of one person sitting on this panel that's in the dark in a lot of it and that's me. This is where we need to get some of the people out to learn about it. Perhaps, some of the fault with all of us is when we send information out, it's already too technical for anyone to understand. There again, I can fall under that category on more than one subject. When I pick up background information, I have to sit there with a dictionary. We need to really, all of us, kind of re-evaluate how to present information to the public,

so that it's short and concise and does bring about their interests and let's them feel that they have something to say too. I'm really glad you said that.

STRINGER: Well, thank you, Sally. I think that a lot of times people are so caught up in the general business of living, sending the kids to school, getting to work on time, bringing in the pay check, and maybe taking off an evening for fishing, that they don't have time to read the legal page or they've seen an advertisement on television about something, but it's real hard to follow up. A brochure of the nature which we picked up today is most informative but sitting here, trying to scan it while the meeting was going on, I found that I should have probably gone home and gotten a dictionary and come back too. But you can only make a certain amount of effort in that direction, I'm sure.

DOOGAN: Unfortunately, this is a rather technical question.

STRINGER: You probably shouldn't ask it of me then.

DOOGAN: Those sorts of things have to be answered. Really the purpose of my comment is to say that the committee has been cooperating with the Public Forum and one of their four main sets of questions is going to be Permanent Fund questions. I believe they're scheduled into Fairbanks sometime later this month.

GRUENING: September?

DOOGAN: I think so. I don't have the schedule with me.

GRUENING: It's after October. I think the first one is in October.

DOOGAN: Yeah. What I am talking about? It would be later in October. I'm sorry. But the purpose of that comment is simply to say that we hope to derive some information for the committee's benefit as well as for the general benefit of the public through the Public Forum. So we would hope that everyone here would participate.

STRINGER: Well, it was well advertised last time. Hopefully, it'll be equally as well advertised this time.

GRUENING: Thank you, Sandra. Allen Bloom.

BLOOM: Thank you, Mr. Chairman. My name is Allen Bloom. I'm here also just as an interested spectator more than anything else. Originally, I hadn't planned on testifying but I was going to use this as an opportunity to familiarize myself as well with the technical mechanism of the Permanent Fund. I'd like to point out I'm not an economist, but I

do have two recommendations for long term utilization of the principal for the Permanent Fund.

The first is that after we've solved, to a great extent, the investment problems that are facing the state of Alaska, and we've funnelled whatever principal into the programs that may be funnelled in, 25 years from now or 50 years from now, it may be advantageous to take the principal of the Permanent Fund and make a quantum jump on the part of the state of Alaska investing the Permanent Fund monies in the emerging nations around the world, the lesser developed countries of the third and fourth world so that we can tie them to a certain extent to our own economic well-being and potentially act as brokers for more stable economic systems in other parts of the world. This goes on beyond just a simple step of perhaps investing in growth bonds and proposals of other states. I'm talking in this case of going to the poor countries such as Chile or Malaysia or such areas as that with the idea that we act as the broker both as a multi-national corporation, called Alaska, and we do it along the lines of the principal of the Japanese superstate in dealing with Korea, Taiwan, the Soviet Union. I think we have that potential in terms of the long-term net effect the accumulation of principal capital in the Permanent Fund.

I don't have any mechanisms for how to set this in motion. I don't have any real strong recommendations on how to manage it

and how you allow the taxpayers in this state to make the decision to make that kind of an investment. But I think it should be explored at this stage, so that when we've solved our own problems and, so to speak, fed our own poor, then we can extend out to that particular level as a stabilizing economic interest, possibly a competitor to the International Monetary Fund, I don't know.

My second point, and it's sort of a composite of what Mr. Matson, Mr. Seifert, and Mr. Inouye were talking about in terms of the research component. Perhaps one of the ways that the principal from the Permanent Fund can be used in a research component is to create a maximum learning center on the north through the University of Alaska system. The attendant return to the Permanent Fund could be in the form of jobs, just the whole potential of employment through the creative and intellectual exercise in the state of Alaska, broadening of the cultural experience and an acceleration of the cultural experience by using some of that principal to actually create a new category of professional employment for the people of the state of Alaska. This is a potential mechanism, and again, I don't have the details worked out.

My last point is---and this concerns just the structure of fund management---we hear a lot here of the difficulties of the constitutional amendment that was passed in creating the

Permanent Fund and then the management device itself. One of the things that I fear is that we may end up creating a constitutional mechanism that is as rigidified and as autocratic as the Federal Reserve System. I would hope that in creating the management tools for the Permanent Fund that we do not create an autocratic empire for another Arthur Burns. We may have to make a concession in form to the general politics of the people of the State of Alaska. We may have to rely very much on the urban or Fairbanks against Anchorage, when it comes down to that, to managing the fund in such a manner that everybody really has a chance to play in it. Thank you.

GRUENING: Thank you, Allen. Any questions from the committee?

The thing that strikes me, you know you hear two suggestions that were very innovative. I've never heard them before for potential use of the fund. But since it's something that might take place down the road quite a ways, it would seem to me that whatever the fund did between that and the time your proposals, let's say, looked good, it would have to be left flexible for the fund to be able to change directions.

BLOOM: I see that as being absolutely essential. What we cast in concrete could turn out to be a real Catch 22 for the taxpayers, for the consumer in the State of Alaska. We're going to

have to develop a mechanism, I think, to encourage people not to come to Alaska; but at the same time, we've got to develop that same mechanism to give the people that are here a decent lifestyle and employment.

One of the things I'm referring to in this structure is the AFL-CIO national position that was developed last year. Do we develop the concept that business and investment will be the whole purpose of the use of the Permanent Fund or do we use what organized labor calls the most important priority, which is jobs, period? I think that has to be addressed in the context of how we use the money in the Permanent Fund.

DOOGAN: The obvious difficulty with that scenario is that jobs is sort of a neuter word. Since we cannot close our borders if we create jobs, we create jobs equally for people that are here and people who may come up to take the jobs. If you were to attempt to develop a mechanism to sort that out, we would be very interested, at least I would, because it's a question that does not seem to be soluble.

BLOOM: The wisdom of Job I don't have. Again the problem is tossed sort of in your laps for consideration. We've got 20 to 25 years to begin addressing this. I think it should be addressed now.

GRUENING: I think it's the patience of Job; the wisdom of Solomon.

BLOOM: Something like that.

PARR: I'd like to say I'm glad that Allen brought that up because everybody who's been around Fairbanks for any length of time knows that one of the problems has always been we've had a seasonal economy. In the past, we've only had really one major, year-round payroll, and that was the military bases. In the last decade, perhaps, the University of Alaska started to offer us a second one. But that's been it. We definitely could use some sources of year-round jobs in this area---no question about it.

The second point that Allen mentioned, perhaps Mike, how do we keep from being flooded by people from the Lower 48 if we do this. I don't have any good answers but I would hope that we may have learned something from our fiasco with Alaska hire on the pipeline that would permit us to do something, at least, to give a preference to Alaska residents.

BLOOM: Perhaps, we use the interest to pay people not to come to Alaska.

PARR: With bodyguards every hundred yards.

SMITH: Send the Alaska, Inc. money Outside.

GRUENING: The dividend money to stay out.

MEEKINS: Allen, I think you pointed up a problem that continually seems to flare up in front of us and that is that if we do assume that our labor supply in Alaska is essentially the United States labor force, that if we increase jobs up here or the real wage up there that it's just going to increase immigration into Alaska to fill those jobs. The attendant social costs, so that if we create a lot of jobs, we're talking about more people coming up and the real wage is, therefore---the equilibrium wage, therefore---remains the same after that influx; but the only difference is that the demand for government services is vastly increased, so that we'd spend more of our surpluses on normal revenue-sharing and building roads and those types of things.

That seems to be sort of a vicious cycle that we get into. Along that line, I've sort of been, by the discussion we had this morning, I'm sort of toying with an idea and that you sort of touched on when you talked about research. Research does really seem to be within the limits of the Permanent Fund. But we're trying to invest the Permanent Fund we get some sort of social benefit out of it. We may, in-

deed, find a way---somebody may find a way for us to do this without all these attendant problems; but one of the things is that real wages are based upon productivity---that if you increase jobs, if you just increase the number of jobs or if you increase the supply by producing things that are not supplied now, and therefore increase jobs, you're really not increasing the wage. You're not increasing the wage until you increase productivity. You can have a differential wage if productivity in Alaska is increased.

BLOOM: This is what leads me to the concept of investing through the lesser developed countries, but also just by extension, we could also extend into the Pacific Rim, and we can also conceivably grab onto the concept that Mayor Hobson has been talking about, which is circumpolar investment as well. That means if we are funnelling the money into the human employable markets, that are market specific perhaps, then we're in a position to run that money out, manage it well, and not encourage an influx of people at the same time that we're putting people to work in a productive manner.

I'd like to see the idea, say 50 years or 100 years into the future, that the State of Alaska becomes a significant economic force as a stabilizing and pacifying force among other nations, other geographic centers of power around the

the world. This is not an Alaska separatist argument; it's just that I think we can start exercising the economy of the United States, in general North America and other parts of the world. Thank you.

GRUENING: Step right up.

HAKKILA: Thank you. I'm Jack Hakkila. I am an economist. I had the good fortune of spending a great deal of my early adult life studying the field of economics. Most recently, I've had the good fortune of spending the last eight years most of it in business development here in the interior of Alaska. I'd like to, first of all, commend the panel for the conduct of the meeting. The proceedings here, unlike hearings I went to two and a half weeks ago, we are speaking equally.

For a non-economist, I think, the last statement we heard was an excellent beginning. I think we should be looking forward to 50 years. I have run some of my own calculations on some of these figures, and I have seen figures of up to a trillion and a half dollars that could be returned just from oil revenues in 50 years time. Alaska could, indeed, be a stabilizing influence in the worldly, economic community.

I have a short, prepared statement here that I'd like to read.

The Alaska Permanent Fund, through its creation, has two immediate, important connotations. It is permanent and it is for Alaskans. I'd like to footnote a non-economic comment here---I don't know how we're going to limit Alaskans with what we define as Alaskans as people who are here as a state of the 50 states. It reminds me some of Representative, former Representative Bradner's comments I overheard on the radio interview one night before the pipeline, him stating that we should keep the people in Seattle at the airport unless they had a job in Alaska. The interviewer asked Representative Bradner what job he had when he came to Alaska, and his reply was that he was looking for a job. I think that the United States of America was built on Ellis Island, the Statue of Liberty---this was the home that welcomed the tired, the hungry, the poor. I think for Alaskans to suddenly realize that we're coming into great wealth and to limit this wealth to that particular group that happens to be here at the time, is going to be a very difficult thing.

It is important, as a Permanent Fund for development purposes, it is important that long term goals for development of the state be established concurrently. If we're talking about accumulating wealth over a period of 50 years, we must, ourselves, set long-term goals. I had the good fortune of working with some of the native communities over the last year in trying to implement, develop long term goals and objectives for them. I would

hate for us to be guilty of stepping into a long-term venture such as the Permanent Fund without establishing our own long term goals. I think this is one of the things that should definitely come out of these hearings and out of the legislation establishing it. Having as its objective the assistance to Alaskan business development, it is important that the goals be achieved through the administration of the fund by Alaskans.

I read in the papers here about Outside consultant roles being handled by Outside economists, and again, we're doing the same kind of talk that we had using the oil lease money in 1969, the great opportunities for Outside investment. Meanwhile, Alaskan businessmen starve, go broke, and die. I'd hate for us to not remember the lessons of the investment of the funds in 1969.

The basic factors of economic production for several hundred years have been recognized as land, labor, and capital. Land is an all-inclusive term in macroeconomic usage for natural resources. We're all aware that Alaska is abundantly endowed with this one economic factor of production. Similarly, in recent years, human capital has become the all-inclusive term for labor and the other human factors in economic production. In much of our discussion here today, we've recognized this term implicitly through our ventures as such things as research, development, human ingenuity

through invention. Human capitalist today, in textbook term which is all-inclusive for the old traditional term of labor.

While the Permanent Fund considers the disposition of that third fundamental item for economic production, capital, it must be remembered that effectively capital can only be used with the other two resources. We are abundantly endowed with natural resources.

Nowhere can capital be more effectively combined with natural resources and human capital than in Alaska itself. The construction of a single pipeline, which will carry 20% of our nation's energy in oil is testimony to that fact.

Now let us examine where lower 48 investment banking firms, insurance companies, and banks were during the eight years from 1969 to '77, from oil lease sale to oil flow.

I speak from personal experience.

On December 31, 1973, after spending three and half years with New York Life Insurance Company, one of the largest of the American insurance companies, and having submitted for consideration investment proposals on shopping centers, apartment projects, and other projects such as a medical clinic here in Fairbanks, at no cost to the company (I was doing this as a service for my company and my clients), I was told that New York Life would rather invest its money in projects associated with another pipeline to Texas. Alaska is too speculative. When the vice president making this statement was asked which is more speculative, investing

where the oil is running out or where the largest resources on the continent are being tapped, a blank stare was the reply. The mortgage department covered its annual meeting and Alaska was not on the agenda.

Having learned from three and one half years of experience with the leading insurance investor in Alaska that investment in interior Alaska included the 1967 power plant at the University of Alaska and no more, that New York Life simply was not the vehicle and neither were any of the other insurance companies. At that time, New York Life was the leading insurance company in interior Alaska. In 1974, I entered a partnership to find investment funds for Alaskans.

At the Bank of America, one of America's leading banks, a vice president admitted in August 1974 that the company had twenty billion dollars in loans it would like to consider in its own backyard. They did not have time to consider investments in Alaska. Once again, sound economics could not justify business decisions.

In 1975, I worked with the firms of Merrill, Lynch, Pierce, Fenner & Smith in their California Street office in San Francisco. I worked closely with the investment banking division there in San Francisco and with the bond offices in New York. In May of 1975, the head of this firm's office doing business in Alaska told me that if anyone comes from

New York to underwrite energy related issues out of the North Pacific region, they would first come to the Seattle area and underwrite issues related to nuclear power plant construction there.

Personal experience in securing investors for the greatest investment experience in history through lower 48 institutions has not been good. Alaskans should not be asked to commit their development funds to these institutions for their decisions, but the decisions should be retained right here in Alaska.

As far as what could be done immediately at the present, turning back to our world of reality today, Alaskans are being asked to transmit the most fundamental resources to lower 48 markets without processing. An immediate opportunity exists right now for investment in petrochemicals. Five million dollars would provide a pilot petrochemical plant. Within a matter of months or a year, we could all be carrying around little samples of petrochemicals. We could be marketing them to other countries. People could take some pride in developing the petrochemical industry domestically here, just as we did a few years ago carrying these little vials of oil from Prudhoe Bay before the oil pipeline went on stream.

Of course, this is a gigantic industry. I've been told by one of the, well, by Ed Hayes of the Northwest Pipeline Corporation that we could foresee a one billion dollar plant per year in the Tanana Valley for the first ten years of the functioning of the Alcan pipeline. This is the economics of it. It remains for us to do it

here in Alaska.

At that point, I'd like to take exception to some of the statements in your study right here. Arlon Tussing is quoted as saying that usually it makes more sense to invest the major portion of the fund outside the state. One of the major threats of Dr. Tussing's testimony was that there is no function for Permanent Fund investments in major industrial or commercial enterprise in Alaska, unless special reasons to subsidize them. Our petrochemical industry doesn't need a subsidy; it's a very profitable industry. And we do have in Alaska the last great domestic resources in these petrochemical basic factors, ethylene. I'm sure many of you are aware of this. The discussion has been rather prominent in the last several months.

The development fund could provide the basic financing for a myriad of projects which leveraged---we heard some testimony on this this morning---would multiply its value. Those projects planned for the oil pipeline and never built such as airplane hangars, hotels, and apartments might be built through adequate mortgage financing. This financing has not been available to Alaskans because past experience has been too short to justify lending based on traditional banking evaluation.

Over and over a couple years ago, we met the answer when

we brought the best Alaskans to bankers in the lower 48. We met the question they don't have three years business experience. Yet we were asked to build the largest project in history here. We have the largest airlift going off the airport here in Fairbanks during the pipeline construction and we couldn't get hangars financed. We couldn't get helicopters financed for Alaskans because they did not have the business experience, although they had the flying and the Alaskan experience that it took for these projects. So traditional banking evaluations are not necessarily sufficient.

Now let's turn for a moment to creative financing. I'd like to enter some of my own thinking here. Where can the greatest return be secured for society through the operation of the private enterprise system?

It was mentioned above that the basic factors of economic production are natural resources, human capital and capital. Alaska will now have both natural resources and, through the creation of the Permanent Fund, capital. How then might the Permanent Fund be used to create human capital?

I am proposing here the formation of an exchange for patentable ideas.

Our system of economic enterprise operates through a system of organized markets. Stock and bond markets and commodity markets operate by bringing investor and speculator together in an organized fashion to bid on tangible and intangible products, such as

coffee, sugar, or wheat---tangible items and intangible such as stock certificates, representing the value of their particular company.

The only provision made today to capitalize on that most fundamental of economic resources, inventive ingenuity, and we heard reference to that this morning, can be made through the incorporation of its value in the price of stock in existing companies. Research and development is generally thought of as being a function of the universities or private companies. Yet ingenuity, ideas come also to the people who are outside the mainstream of organized production. Necessarily so, to be a creative person, he must be outside or have time to think and come up with the ideas. Fortunately, we in Alaska here, especially in the Interior are endowed with a number of these types of individuals; because we have the time here to think and do these things. A Wall Street Journal article about a year and a half ago documented a television program called "The Inventors in Australia"---this, by the way, was a most popular program in Australia. Each week a family of four inventors would be brought on with their inventions, and the best one was selected. More often than not, the best inventions came from the outback, from the outlying regions; because these people had the time to think.

The inventor today is afforded patented protection for a period of 17 years by the U.S. Government but his patents have no exchange value on an organized exchange unless their value is incorporated into the value of stock of a company, which is traded through the stock exchanges. In the case of a patent whose value lies further down the road than 17 years, no incentive lies in its disclosure.

I'd just like to comment here---I think with more testimony in all of these hearings this summer on D-2 hearings here---we hear considerable amount of testimony on preserving traditional values. While I think that it's deplorable the bowhead whale, for example, will not be allowed to be hunted out here, there are many people in society who like to go to the stars. The picture "Star Wars" and its reception in Anchorage, I think is adequate testimony to this. People love to think about 50 years down the road, 100 years down the road, when we're travelling not just to the planets but interstellar travel. If an inventor were to have such an invention today, he has no incentive for its disclosure. It's very difficult to uphold the patent protection of 17 years on an invention to have something that's utilized 50 years down the road to want to disclose it. In many cases, he may be laughed at.

I mentioned earlier, the most creative of our inventors are in Alaska. The Alaska Permanent Fund could establish a provision to form an exchange for patentable ideas. Going back to the type

of thing that we were talking about earlier in commodity exchanges, the stock and bond exchanges, a system of speculative houses could be established that would bring investor and speculator together and purchase the ideas of the inventor, whereby he then would have immediately funds at his disposal to go out and get another idea on the market. That's the idea of organization of dependable ideas.

In conclusion, creation of the Alaskan Permanent Fund for development connotes the long term goal of the economic development of the State of Alaska, most importantly, the people of the state. This goal can be achieved best by using the capital of that fund and combining it with the abundant natural resources and the creativity of the human resources of the residents of the State of Alaska. Thank you.

GRUENING: Thank you very much. Could you stay for a few questions?

HAKKILA: Sure.

CARPENTER: Thank you. I missed your name.

HAKKILA: Jack Hakkila.

CARPENTER: Sure. Do you have a present affiliation?

HAKKILA: Presently I'm consulting. I just concluded---I came in the day before yesterday from Galena. I've been working with the Tanana Chiefs and the University of Alaska. We established an agricultural experiment station there this summer and one in Ruby. I'm also consulting on some other ventures in Alaska and internationally.

GRUENING: Charlie.

PARR: Mr. Hakkila, you mentioned something early in your testimony about, if I understood you correctly, about perhaps using Permanent Fund investment to get petrochemical off the ground. My understanding is that right now, in any kind of energy market, that it is seller's market. We have a worldwide shortage of energy. Those people who have energy are in the drivers's seat. It's not a buyer's market, but a seller's market. If that is true, is there any reason that state money, whether it's Permanent Fund or any other kind, should be used? If it is a seller's market, shouldn't the private companies be jumping at the chance to put their own money into it?

HAKKILA: My point is that we should be jumping at the chance to put our own money into it.

PARR: In other words, the state would be the one who would

be selling this and not the private company? It would be running the petrochemical complex, for example, and selling the product.

HAKKILA: No. I am speaking of state support for private enterprise, domestically created private enterprise here in Alaska. Let our own people create the industry.

PARR: You are saying, in other words, instead of letting Dow Chemical or somebody come in here and set up one, that the state could furnish the money so that local Alaskans then could establish this, instead of having a company from Maryland or Texas or somewhere.

HAKKILA: That's right. Let us take the lead, and let them participate to whatever extent they would like. For example, about three weeks ago, I was told by a representative of El Paso Gas that if we were to go into this type of an arrangement, they would be more than happy to provide us with all of the expertise in petrochemicals. On the other hand, at such time as we wanted to, they would enter into an agreement to finance some or be a participant in it. They would show us the way and help us create our own industry here.

PARR: In other words, the main thrust of what you are saying, and this is what I missed, I guess, is that the principle ownership would be Alaskan ownership and not out to the state ownership.

HAKKILA: That's right. It could be through the Permanent Fund, and then, when I mentioned, you know these figures generate and they are tremendous figures, because nowhere in the United States, have we had these types of resources before. These investments will also generate income or could generate income for the Permanent Fund. Nobody is going to get these projects off the ground like Alaskans, because we'll have our own interests in running it.

PARR: You are not suggesting in any way a subsidy of the petrochemical.....

HAKKILA: No, sir. This is where I take exception to Arlon Tussing's statement.

MEEKINS: I guess what you are getting at there is that those projects are financable, but not to the people in Alaska. The banks, because of their requirements, you're talking about three years of experience and different other kinds of requirements that the banking industry has.

HAKKILA: That's right.

MEEKINS: That those projects are financable, they don't need to be subsidized or anything, not finance them for the people that you think...

HAKKILA: That's right. An Outside financial institution will not finance projects for Alaskans who have no experience. But the experience can be brought in. For example, a venture with El Paso Gas---they have an El Paso Petrochemical Division, and they will provide us with the assistance right here in building a domestic petrochemical industry.

MEEKINS: I find that to be an extremely interesting comment or a point because, as you noted, one of our consultants, Arlon Tussing, said in his memo to the committee that in his view there really isn't a capital gap in the sense that he said that he felt that all sound, in most cases, sound projects could find financing. But what you're doing is making a distinction between financing for whom.

HAKKILA: What I am saying is that Alaskans can do these projects. It's the same thing I was saying three years ago.

We couldn't get our projects financed up here because we did not have the experience. Then I'm saying we can start small---just like this agriculture experiment station we started in Galena and Ruby this summer.

The state can develop projects. You start out with a small plant. A five million dollar plant could produce a lot of petrochemicals and give us experience.

MEEKINS: How would a development bank protect itself? Certainly they could say that the project itself was a sound one. I know there was a reason for the requirement of business experience, and that's to be sure that the people know how to run that type of business. How would the development bank protect itself, if it were trying to develop things in Alaska that otherwise would be done by multi-national corporations?

HAKKILA: My point is that they may not be done by multi-national corporations. They just may simply not come here. They may go to Saudi Arabia or some other place. This has been our experience, because we have not taken the lead in petrochemicals to this point. I think there has been some testimony that several of the large multi-nationals came to Juneau, wanting to work with the state, and found no encouragement. I think if we had the lead here that that problem would be solved. I think you could be assured

that with the cooperation of other companies that have expertise that the projects could be built.

CARPENTER: I guess I am puzzled by something. If we don't go outside with any of the investment, for whatever reasons, whether it's because we weren't treated properly, historically by outside banking institutions or because we want to simply use the money inside Alaska, for whatever reasons, if we were going to invest it all in Alaska, can---do you think that our very small economy in Alaska can absorb that kind of money? I picture a guy somewhere in the management structure of the Permanent Fund with a desk full of two feet of applications and analyses trying to pick winners and form ventures and projects fast enough to keep absorbing the money. Do you think really we can...?

HAKKILA: You think it would be a problem to dispose of the money?

GRUENING: Prudently.

CARPENTER: Not dispose of it prudently.

HAKKILA: Prudently. I don't think so. This is what I am saying. There exists a need right now to finance, or pos-

sibility financing a world scale petrochemical plant of a one billion dollar investment per year for the first ten years of the gas line in the Tanana Valley. I don't think you'll have that kind of money in the Permanent Fund.

GRUENING: Probably not. Mike.

DOOGAN: Excuse me. A couple of questions. At one point, you said that Alaska businessmen starved, went broke, and died--do you mean by that that there have been failures of Alaskan businesses that have been caused strictly by a lack of being able to get capital?

HAKKILA: Yes, sir. And I could document the cases that I have worked with and individuals. I don't care to do so publicly, But I'd be glad to discuss this with you.

DOOGAN: That's fine. I just wanted to make sure that I understood that. Would your---the second question is would your characterization of the outside banking community extend to the Alaska banking community as well?

HAKKILA: No. Not necessarily. The Alaskan banking community traditionally has had a very small amount of capital for its dis-

posal. Perhaps, they could be a part of the solution in this case. The Outside banking community has suffered from a lack of education on economic opportunities in Alaska. They just cannot comprehend or have not traditionally been able to comprehend the economics as it exists within the State of Alaska.

MEEKINS: One more question. Are your comments, your disagreements with Arlon's remarks only limited to large scale projects or does it apply to small projects also?

HAKKILA: No. No. Small projects also. There's a great need for the small things. I'm speaking of hotels, airport hangars, apartment projects. We were not able to get the projects financed. Fairbanks is living testimony. When the pipeline came, we did not have adequate projects. Prior to the pipeline, even after Senator Gravel pushed it through the Senate, in July of 1973, we were not able to get financing for capable individuals.

MEEKINS: Was that the same reason, I'm assuming that the projects fit the format that the banks wanted in the sense that the projects themselves looked like they were sound, and that they might produce a handsome profit, but there were

some other structural deficiency, like they weren't---people didn't have quite the right background or something like that. Was that the problem?

HAKKILA: Alright, it's practically a problem, as I mentioned earlier, of the individuals themselves, not having had sufficient background to do project work on the scale being asked of them for the pipeline. What was the other question?

MEEKINS: Well, that's sort of what I'm getting at. I'm trying to think of, comparing your remarks with what I remember from what Arlon's remarks were and trying to see whether or not they're---you see he makes a good case for the fact that if we invest money in small businesses, that we're just displacing capital that would otherwise go there because we would limit ourselves to the same types of investments the banks would.

HAKKILA: We don't have the capital available within the state for those types of ventures in the economy that we have here today. We just don't have it.

MEEKINS: You see, your comments sort of jive pretty well with my intuitive feeling and what a lot of businessmen tell

me that that's, they claim, of course, they're turned down by banks and they claim that it's not true---there's capital available for good investments.

HAKKILA: It is not true. You could study the amount of public capital, capitalization in Alaska's banks. In comparison with the funds that you will have available through the Permanent Fund, the capitalization of Alaskan banks is very small.

GRUENING: I just want to remark that I'm glad you analyzed the report and had a comment on Arlon's report, because the consultants' testimony or their views are not necessarily those of the committee. We do hire consultants to toss ideas out there, but in the end, it's the people on the committee who have to decide.

I have one question. You mentioned that the tremendous capital needs that, say, petrochemical would have like a billion dollars annually. At the same time, you mentioned the fact that there are needs for smaller scale investments, hangars and so forth. Given the fact that, as you pointed out, the Permanent Fund probably isn't large enough to even take care of the petrochemical capital needs. Where would you place emphasis? It occurs to me that you can't do both

HAKKILA: I would place emphasis on leveraging the money by taking and using that as guaranteed money and getting Outside participation in the ventures. I'm sure that participation would be willing participation, if Alaskans took the lead and went after it.

DOOGAN: I would assume that one of the reasons behind banks' refusal to make a loan in Alaska to somebody who didn't have two years business experience was that they would consider it an unacceptable level of risk. Now that may just reflect their lack of knowledge of Alaska, but would you---what would your opinion be to a statement that it would be relatively riskier, in terms of risking the money, to make investments in Alaska as opposed to Outside investments?

HAKKILA: Well, I'm referring specifically to the pipeline community set in '73 and '74 and some of this personal experience. It just isn't, was not, good banking. They did not understand what we had here. They were looking at 20 year loans that paid themselves off in five years, but they couldn't understand what was going to happen here. I would venture to guess that if time goes by, we'll have greater participation from Outside investors here certainly. But we can take the lead is the only point I'm trying to make here. To be in control of our own destiny.

GRUENING: Any further questions. I'd like to take a short break here. Representative Carpenter reminded me in Anchorage that I'm sometimes neglectful of that. About a short five minute break. Then we'll come right back.

BREAK

GRUENING: I think we can start now. We have return reservations at 5:30. I'd rather stay here in Fairbanks tonight but we have a hearing tomorrow in Anchorage. Either that or we've got to catch a later plane.

PARR: They have a 7 o'clock in the morning flight.

GRUENING: Thank you, Charlie. We're running this kind of like a Quaker meeting. If anyone has anything to say, they can get up and walk to the podium. Yes, sir.

HOPKINS: My name is Donn Hopkins and I reside at 5.3 mile Chena Pump Road, just out of town.

Mr. Chairman and members, I do believe that the policy of distributing natural resource income directly to Alaskans, as proposed in the Alaska, Inc. concept, is far superior to the current policy of allowing the state government agencies

to spend that income. However, there is a third alternative for the use of non-renewable natural resource income, which I favor over the Alaska, Inc. concept. That third alternative is to use such income as a loan insurance fund to encourage Alaskan ownership of new buildings and other land improvements in Alaska.

I have a specific proposal to make in this regard:

1. The Permanent Fund (and preferably the entire non-renewable natural resource state land income) would be invested in U. S. Government securities, with the income therefrom being added to the fund to help compensate for the reduced real value of the fund over time due to inflation.
2. These securities would be used to guarantee 100% of the value of loans made to Alaskans for constructing and equipping new industrial and commercial enterprises and residential facilities in Alaska.
3. The loans would be made through normal banking procedures and could pay for up to 95% of the value of the project used as collateral.
4. A fee would be charged the borrowers, sufficient to cover the losses due to loan defaults plus any loss in real value of the Permanent Fund due to inflation, beyond that covered by the U. S. securities income.

5. Annually or biannually the uncommitted balance in the fund would be divided equally among all persons who vote in the general election to use as guarantees for loans.
6. Such amounts could be saved for a five-year period, but if not used within that period, would be returned to the uncommitted balance for reallocation.
7. The loan guarantee amounts allotted to each voter would be non-transferable, except upon the death of the owner and then only if they had been used.
8. As loans are repaid, the guarantee amounts would be reduced proportionately and the reductions returned to the uncommitted balance.

The general policy and specific proposal, which I favor, has two major advantages over the Alaska, Inc. concept:

1. It does not establish what in effect is a guaranteed annual income precedence. It does not pay people just to live in and endure Alaska.
2. It does help all Alaskans, forever, not just while the natural resource income lasts, to invest in the progress of our state, and through such investments, improve their own lives and the state as a whole.

This policy and proposal discourages dependency and encourages creative thought and constructive action by all

Alaskans forever. It encourages Alaskans to join together in the promotion of projects to improve their state, their communities, and their lives. Thank you.

GRUENING: Thank you. That was an intriguing proposal. Any questions? I have one.

First of all, do you have investment banking experience?

HOPKINS: No.

GRUENING: What is your occupation, if I may ask?

HOPKINS: I have some log cabins that I rent out. Before that, I used to work in government planning offices, including I was director of Planning and Research for the State of Alaska in their State Department of Economic Development and Planning. I worked as planning director here in the borough, and I've done planning consulting for the City of Fairbanks. I have an educational background in planning.

GRUENING: Could you explain what you mean by loan guarantees and how they would work?

HOPKINS: Well, in the event that the collateral was used by

the borrower was insufficient to cover any loss that might result from its default, then the state would have to pick up the difference, and that's what would be guaranteed with that difference. So that any person who wanted to loan money in Alaska would be guaranteed that he would get that money back no matter what happened. That would encourage Outside money to come into Alaska. We would be able to get a great deal of capital up here that we do need. Ever since I've come to this state, it's been a problem to get Outside investors to bring their money up here where they don't know what's happening, instead of loaning it out down in California or New York, where they do know what is happening. By guaranteeing their loans 100%, they would be better off than they are at home. Therefore, we would be able to get all of the money up here, I think that we'd be able to guarantee. We'd be able to guarantee quite a lot. I don't know what the leverage would be on something like that. But if you could get five times the amount of money that was in the Permanent Fund, that's a lot better than just loaning out the Permanent Fund. You could probably do better than that.

GRUENING: To the extent that these loans weren't paid back, you'd have to sell the securities or hand them over to the people that make loans...

HOPKINS: Well, in theory, you would have the securities there to sell. But if you operated this program on sound banking principles and didn't make a lot of irresponsible loans and if you did charge a fee to cover the default, just as the Federal Housing Administration to cover defaults on their house loan insurance program---it's the same idea as FHA, the only difference being that it's extended to commercial and industrial loans as well as housing loans---but this fee should cover all of the losses, so that the Permanent Fund would remain intact. But it's there to give a feeling of security to people who would loan money up here.

GRUENING: Who gets charged the fee?

HOPKINS: The borrower---just as the borrower is charged the fee on an FHA insured loan.

GRUENING: Who makes the decision as to whether the loan that this individual Alaskan or group of them wants---is it a good one?

HOPKINS: It would have to be done, I think, as far as just what I would say, just normal good banking procedures. I would hope that it could be worked out with the existing banking industry in Alaska for them to handle, to do all the paperwork, all the investigations of these loans.

GRUENING: If the Permanent Fund, in essence, guarantees all the loans, what incentive does the bank have to make sure it's a good loan? If the deep pocket, the one who has to ultimately pay it back if the borrower doesn't, is the Permanent Fund, why wouldn't they loan it to a guy who has---wants to grow watermelons on Mount McKinley?

HOPKINS: Well, I suggested that the loan be good up to 95% of the value. If the bank wanted to pick up a little extra on these loans and loan beyond whatever was appropriate for the state to guarantee, they would have that to lose.

GRUENING: So the borrower would have to put in some equity.

HOPKINS: Either the borrower would have to put in some equity or the bank would have to take a second mortgage. I suppose if you found one bank that was doing a bad job, that had a lot of defaults, you would have to cut that bank out and not use them any more. Or you may want to set up a special arm of government that was separate from the banking industry, but I don't favor that. I would think that the banking industry would be responsible.

GRUENING: Okay. Do you have a written statement?

HOPKINS: Do I what?

GRUENING: Do you have a written statement?

HOPKINS: Yes. I do. I'd be glad to give you a copy of it.

GRUENING: Incidentally, the last gentleman, Jack Hakkila, I think, did you give us a copy of that? Or could you?

HAKKILA: I don't have a copy, but I'd be glad to run one off for you.

GRUENING: Thank you very much. Are there questions of the witness? Russ.

MEEKINS: You, as I understand it, you limited this proposal to people who voted in the general election---

HOPKINS: Yes.

MEEKINS: Why did you do that? Which election are you talking about?

HOPKINS: The biannual elections.

MEEKINS: The one coming up then?

HOPKINS: Every two years.

MEEKINS: It would change as the elections change.

HOPKINS: Right. But the, I don't know, the amounts might be allocated annually rather than biennially. Either way it would work.

MEEKINS: Why did you happen to choose that as a....?

HOPKINS: As a vehicle?

MEEKINS: Yeah.

HOPKINS: It's just an easy way to identify an Alaskan. This business of having people have to come in and justify their residency here seems to me like it's going to be very difficult to do. To provide evidence---because I've seen so much of these people coming in from Outside to work on the pipeline getting these residency cards, even foreigners, who don't even have a work visa in the country, work up there.

MEEKINS: On the other hand, we have the problem in Kodiak,

people in other areas of the state, people that have fished for or have claimed to have fished anyway, for 15, 20, 30 years up here, whole families, were not eligible to receive, to get limited entry permits. So we find that whatever, however we try to define who is eligible for something, there is always a tremendous problem.

HOPKINS: I think, once a person established residence up here and becomes a voter, he can maintain that residence even if he doesn't stay up here all the time. One thing that's important about this program is that all of the money would be invested in Alaska. You wouldn't take any of it Outside. It would be invested in permanent facilities. It wouldn't be spent for ongoing operations. So it would actually increase the total captial investment in Alaska. It would be done without decreasing the Permanent Fund.

GRUENING: But the primary investment, the investment in, say, government securities would be Outside.

HOPKINS: That is just so you get a little interest on it. The U. S. securities because they go down, we all go down. Some of these so-called blue chip securities aren't so blue sometimes.

GRUENING: Charlie.

PARR: Maybe I misunderstood something, Donn. If I understood you rightly, you would in initial investment would all be---the complete thing would be U. S. Government securities. That would not be simply this 25%?

HOPKINS: Well, I don't think any of the non-renewable natural resource income should be spent on ongoing programs. I think that should all come out of tax---or other current revenues. However...

PARR: All the money would go into this.

HOPKONS: However, since you are addressing yourself to the Permanent Fund, I'm saying that all of the Permanent Fund should be used as support for this loan program.

PARR: Well I thought, I understood what you were saying was that we should take that Permanent Fund and put into it all of the money that comes from the non-renewable resource areas.

HOPKINS: Yes. I'm in favor of that too.

PARR: Then, the second point, but...so what we'd really

be using in the state would be the income from the Permanent Fund. The income from these government securities. Is that right?

HOPKINS: In a way, but not directly. We'd be using the income from the securities to offset the loss of the value of the money due to inflation. We want to maintain the same purchasing power of the fund. We don't want to lose the purchasing power of the fund over time, which we would do if we only maintained the dollar value.

PARR: Then the, instead of using the income as a loan fund, what you'd be doing is simply the securities themselves would be pledged as collateral.

HOPKINS: That's correct.

PARR: Where would the money come as actual cash?

HOPKINS: The actual cash would come from private investors from anywhere in the world. Whoever wanted to come up here and be sure that they would get their money back, because we guarantee their loan by 100%. There'd be no chance of loss.

PARR: So the state itself would not need to, say, appropriate money every year to put into that loan?

HOPKINS: No. There'd be no appropriation at all. No tax cost at all. The whole operation would be self-sustaining, and as the Permanent Fund grew from, you know, additional income from non-renewable resources, there'd be more loans that could be guaranteed. Of course, there'd be more demand too as the state grew.

PARR: Thank you. I'm clearer now than I was initially.

GRUENING: Mike.

DOOGAN: I just want to get this straight. I think you said that at some point, you would decide whatever money hadn't been used to offset inflation would be divided up equally among current residents based on their voter registration, but that if they did nothing but save it for five years, they'd have to give it back?

HOPKINS: No. I didn't suggest that they get any cash out of this fund at all. All I suggested was that they get a loan guarantee that they could use. If they wanted

to borrow money in the private sector. That's all they're getting is the guarantee of these loans.

DOOGAN: I see.

HOPKINS: An equal share, a guarantee that's available.

DOOGAN: Well, then anybody who got a loan guarantee and didn't use it in five years, he'd have to give it back to the fund.

HOPKINS: Well, it would just revert. If he didn't use it, if there's no point in having it just hang fire indefinitely. You want to put it to some use.

On the other hand, maybe a person would like to think about what he's going to invest in for awhile, whether it's a house or some business or a share of an industry or something like that. But that way, you'd find all Alaskans trying to figure out how they could get into business in Alaska and get their own homes. It would, I think, really would stimulate our economy tremendously up here.

GRUENING: I think one problem might be is not everyone is going to have some collateral. I guess it's finding the collateral for the loan.

HOPKINS: Well, that 5%. You've got to be able to save a little bit on your own. But you know, you can start out small. It doesn't have to be a big investment.

GREUNING: Any further questions?

MEEKINS: If people over 18, I guess it is, can vote in the general election, it seems to me, of course these are very small parts of what you are saying, I suppose, but just in regards to that five years, I'm not sure that by somebody knowing when they're 18, that they'd know what they want to do by the time they're 23 really.

HOPKINS: I think there are a lot of people who start out at an early age and, you know, have made it by the time they're in their early twenties. It depends on the individual. Maybe all their investing in is a home or in shares in an apartment house or something, just they can get started building up some capital of their own. This is the important thing. They'd have some more incentive to save part of their income than to just spend it on consumptive items.

GRUENING: Any further questions? Thank you very much.

HOPKINS: Thank you.

GRUENING: You next? Great.

COLLETTE: My name is John Collette. I live in Fairbanks on 3 Mile Sheep Creek Road. That's just out of town. It's not often that we get invited to speak on things that we know nothing about. So I'll take full advantage of it.

GRUENING: We're invited to that all the time. That's a prerequisite for the job.

COLLETTE: Like everyone else, everyone I've talked to has very loose ideas about everything and because it's governmentally orientied, we're hesitant to bring this up. A lot of the ideas I have emerged from what I do every day. I'll run through a few of those ideas that I've just been kicking around.

I'm a life long Alaskan and I'm proud of it and all this. This precedes everthing I'm going to say. What I'd like to see for the Parmanent Fund generally is us not to relinquish our responsibilities. We shouldn't give our responsibilities, meaning our money, to other people to invest. The good and the bad that they do with the money is not their moral burden; it's ours because we made it. It's our money. I don't think that an investment banker on Wall Street is going to be taking that kind of morality in mind and while we may here. How to enact that is a very diff-

icult thing. I don't have any conclusions there.

Also I'd like to see Alaska remain somewhat as it is, encouraging the same virtues that Alaska has encouraged. I enjoy them because I embody some of them. One of the things that allows me to do this is the land, of course. When we have another 5 or 6 million people in Alaska, that land isn't going to be available and these virtues won't be encouraged. So I think anything that's done with the Permanent Fund should encourage as small population growth as possible. The petrochemical industry in Fairbanks is anathema to that.

One of the ideas I have about investments is in the tourist industry. Now, right now, as we're told from the federal government that they're going to be making all sorts of national parks in Alaska. Well they'll also be taking a lot of the tourist dollars from the private industries, I think they'll be encouraging private industries to produce capital things in order to compete with national parks. They'll be apart from metropolitan areas. We won't have transportation systems to them; we won't have gas stations along the way or eating places. They'll be flying in and flying out or maybe by boats.

I think that the state of Alaska should go in with some of the Permanent Fund money and invest it in the tourist industry. One of the things I have, an idea I have, is building

a sternwheeler for the Yukon River, a huge, huge boat painted white and make it very grand and charge an exorbitant amount for tourists.

GRUENING: I'd like to join the venture.

COLLETTE: Keep people on the boat; they'll only dock in certain areas. Places like Tanana will obviously change, but they're not so good right now. There are other things too. But that's the only specific answer I have for the tourist investment.

Again we're generally, health in Alaska is really a big problem. I think with our Permanent Fund, we've got a chance to affect that positively. Another thing we can do is create a preventive structure in medicine. A structure of preventive medicine alongside the existing medical facilities. The existing people, the doctors, the clinics have grieved themselves to a crisis situation in medicine and have put very little of their energy in preventive medicine. We can, as a state, do this on an educational level, in schools and in colleges, and just create a healthier environment.

Let's see. Also too, I just recently got back from Europe. One of the things I saw there that I was most impressed with was the economy of Denmark. The Danish I've always responded to really well. I love their architecture; I love the products that they produce; I like the people too. But they've got a country there

which is poor in natural resources yet they have a fantastic standard of living through the exportation of their talents and their brains. Their people are very energetic and inventive. I'd like to see Alaska create an educational structure, through the Permanent Fund, which would create a net exportable talent.

Another thing I'd like to see too is, an interest I've had for years is in housing, and I'm teaching a course at the Community College in cold weather design in housing. I see a huge area there where we don't have the expertise available, because no one has bothered to look at Alaska, when they design houses. I have, and other people I know have, and we're going to try to be teaching these things to the community.

But there are a lot of other areas within technology, which Alaska gets ignored. The United States is temperate and all the resources temperate...their research is temperate. We get overlooked in our automobiles, our houses, our clothing, everything else. I'd like to see more research being done to create an Alaskan technology, which we may be able to export too.

I guess in conclusion I can say that I'd like to see an Alaska, Inc. being made. I'd like to see a more socialist

state. I'd like to see a socialist state investing in people and hopefully we can take this investment and find out a few answers about what to do with our Permanent Fund. We can actually invest in wisdom. That's all I have to say.

GRUENING: Thank you. Are there any questions from the committee? You just mentioned one thing about investment bankers. I think Bob Weeden probably touched on it when he said he'd hire a mechanic to fix your car but you don't necessarily ask him where you're going, where you should go with your car.

VOICE: Talk into your mike, will you? We can't hear you.

GRUENING: I'm sorry. Okay. I was commenting on an earlier testimony that it was pointed out that you have a mechanic fix your car but you don't ask a mechanic where you want to drive it. It may be that the institution would use expert advice in terms of investment counselling. But I think your point was that they shouldn't be necessarily fixing the directions of the Permanent Fund.

COLLETTE: Definitely. Right. We have at our disposal much power. I can see a lot of destructive power there.

GRUENING: Any other questions? Thank you very much. Yes sir.

DESPAIN: My name is Glen DeSpain. My address is Box 1255, Fairbanks. I live at 2 1/8 mile Chena Pump Station Road.

In December of 1969 or January of 1970, before our local legislators went to Juneau after the windfall that we got on Prudhoe Bay bonus lease sale, a group of people, a large number of Fairbanksans met with the legislators in the Chamber of Commerce log cabin in the basement. It was a packed house. To the man, everybody agreed that we had no right to spend this money from the non-renewable resources that we were taking out of Alaska. We should live off the income from it. Well, I don't---between the time that we met with them and the time that they got out of Juneau, they had taken pretty much care of the \$900 million.

I don't know how many billion we're in the hole now with the type of bookkeeping that our government uses. They sell oil in the ground and they'll take it off---in a few years from now when they take the oil out and, of course, according to our state constitution, it's against the law for the state to go in debt. However, there are ways of getting around that. They have certainly found all of them, I believe.

As far as the Permanent Fund is concerned, I think that every penny that comes into the state from the sale or the bonus or the lease of non-renewable resources should go into a permanent fund. And I mean a permanent fund. I don't think

it should be distributed to everybody that's lived here for 30 days and went down and registered to vote. That is really a socialist concept.

I, as you probably know, am not a socialist by any stretch of the imagination. I think that the government should be forced to live within the income off of this. The interest or whatever is derived from this Permanent Fund is what our government, that along with whatever taxes or levies they decide---the legislators decide to put on things is what the state should live on. I don't think that we have any right to spend the money that comes in from these non-renewable resources.

It'd be just the same thing as taking Southeastern Alaska and selling it to some other country or some other entity other than the state. Lose all control of it; I mean we don't own it any more; we sell it; and we live off the money that we get from it. I think that future Alaskans have every right to these resources that we are exploiting today. The only way that I can see that this can be done is to keep that money intact and live off the income from it. It's just like a fellow that has a tree farm; he doesn't just cut down every tree he's got and spend all the money. He harvests what he can and lives off some of the income, but he plows some of it back. In this way, we wouldn't be plowing it back but we would be keeping it intact. I'm very much opposed to the tremendous growth of our state government since 1969.

As far as giving the money back to the people, any time the government takes from whatever source and gives it back to the people, the people get very little of it. I mean very little---just crumbs. The bureaucracy eats up the money. I can foresee a tremendous amount of people working for the state figuring out who's eligible and who isn't eligible for this bonus or Alaska, Inc. or whatever you want to call it.

An example I'll give you, as I had a discussion with the governor, two or three of them, while he was in town here a couple, three weeks ago. One particular day I went down to the license bureau to get a driver's license. It had expired some time before I became aware of it. I was the seventh person in line. There were six people ahead of me. I was number seven. There were six people working in the driver's license section of the state building down here. They had four of these big computer consoles and desks and everything. It was 50 minutes before they issued the seventh driver's license. I was the seventh one. Fifty minutes for six people to issue seven driver's license. Now the state took in \$35 on those seven driver's licenses. As I pointed out to the governor, there's no way that we can afford to issue driver's licenses under that program. I also told the governor, I said, "I've seen glaciers move faster than some of

those people back there." A couple of them, I was a little surprised that they were still alive. But I guess they must have been because they left at 5 o'clock. But the point I'm trying to make and I'm trying to put a little humor into it is that the state can't do anything, even give back money, without losing money on it.

I think there's a drive afoot here to lock up this money into an area where the legislators can't get all of their little pet social projects going. I would hope that we can do that, and when you're considering this Permanent Fund, I would like to have you consider the total income from non-renewable resources that are sold or leased or royalty or whatever we get off of it, put it into a fund and then get some kind of a thing into the framework of our government, the constitutional amendment or whatever, that that money cannot be spent. It has to remain intact.

The interest or the income from that money is the only thing that should be used to live off, if you will, to maintain our government. That and whatever money that they take in in taxes---income taxes or whatever.

I'm not in favor of doing away with the income tax. If we do away with the personal income tax in the state---man, what a haven this will be for the deadbeats who want to come up here and live off of our income. I'm not in favor of that in any way.

This revenue sharing is another thing I'm not real happy with

at all. All it does is encourage local governments to build up a huge bureaucracy like we have here in the North Star Borough, and I suppose Anchorage has got the same thing. Then pretty soon the state gets everybody hooked on spending lots of money in the local government. Revenue sharing sounds awful good. But boy, it's sure an awful headache the next morning.

I think that pretty much covers what I have to say, I didn't write anything out but my main point is that I think all of the money from all of sale or lease of non-renewable resources should go into the Permanent Fund. The Permanent Fund should be absolutely inviolate. I don't think it should be given back to the people in the form that I've heard of here while I've been here, in loan guarantees or anything else. Boy that could get to be an awful kettle of worms.

Some bank for whatever reason makes a bunch of loans and the state has to pick it up. There's nothing in there to ensure that those loans are going to be sound investments. The state government should be forced to live within the income they get off of this Permanent Fund.

If they had kept that \$900 million intact at the time it was producing \$53 or \$54 million a year. That was more than the state budget was the previous year. But of course, it isn't any more, because they spent that plus income off it and everything they could hock from in the future. I think, regardless

of what kind of administration we have in Juneau or who we seem to send down there for legislators, they just can't resist that giving somebody something for nothing. There isn't any free lunch, as we all know. Thank you.

GRUENING: Thank you. I think we got your point loud and clear. I wanted to ask you about you say you want it invested and none of it spent. What would you invest it in?

DESPAIN: Well, of course, I don't invest in government bonds. I think they're one of the poorest investments there are. Everybody seems they're pretty safe, but we talk about keeping up with inflation. I invest most of my money in precious metals; it's done real well. I've invested---I'm a coin collector---and I've invested in rare coins. I have several coins I've paid just like five or six dollars for that are worth fifty dollars or more.

Now I don't suggest that the state go into the rare coin business, but there are other investments that beat the federal bonds all to heck. At one time, I had part control of a fairly large sum of money here in one of the banks and we invested in some short term securities in Bank of America, which paid more in interest than the federal bonds were paying at that time, treasury notes or whatever.

GRUENING: Thank you. Russ.

MEEKINS: I think the point you're making is one that, in general, is supported by many people in the legislature. I think that's where the generation of the Permanent Fund concept has come from. The idea of taking money from the day-to-day operation of government. I think, implicit in that is the assumption that spending will increase to the amount of money available for spending.

DESPAIN: It certainly has.

MEEKINS: But there, of course you know, the Permanent Fund can't really be spent on operation of government unless you---well, it could in a sense---but it can't be spent....

DESPAIN: It will be. It can't be, but it will be. One way or another, it will be.

MEEKINS: The other point, I think is important to make, just for the record, is that, although it is true in many people's view, the money from the \$900 million was wasted, because it was spent on the operation of government and the increase of the number of people employed by the state. Not all of that money has been spent. In fact, there are hundreds of millions of that \$900 million left.

DESPAIN: But it is committed though. It may not have been drawn out of the bank, but there's been money borrowed against it and spent.

MEEKINS: Well, it went into such programs as Veteran's Administration loans to Alaskans. The purchase of those loans...

DESPAIN: Do you have any idea of what percentage of the money went into the veteran's loan fund?

MEEKINS: The point is that there are hundreds of millions that aren't spent, that are indeed earning a return. I think that's important, just for accuracy, that while three years, \$500 million may have been wasted, in your view, not all \$900 million.

DESPAIN: Well, if it wasn't spent, why did we sell the oil in the ground up here a couple of years ago?

MEEKINS: It was invested, just like you're advocating the money in the Permanent Fund be invested. Invested where the principals return plus interest. Of course, one side the principal is committed, it can't be used for the day-to-day operation of government. So in that case, that was a good use of that money.

DESPAIN: That's a good use of the money, yes. Loan out with fairly secure loans. That's fine. But we're talking about tremendous amounts of money.

I've seen some of the shenanigans that went on here after the flood, where there were tremendous amounts of money loaned to different people here through the SBA. Then they went out to Arizona or wherever and bought huge tracts of land with this money. Believe me, these things happen. That's what I see is going to happen to the Permanent Fund. The right people are going to get their hands on it, or big portions of it. I've only lived in Alaska for about 36 years. But there's some of them that have been here a long time. Believe me, I've seen some pretty fine shenanigans go on.

MEEKINS: That's a good point. I think, one of the problems with loan programs that we've had in the state is not so much that they're operated in a poor manner or even an inefficient or corrupt manner, but that, generally speaking, the people are aware of those kind of programs and have enough knowledge of---enough financial background to work the paperwork and apply for them are only people who don't need those funds. So you end up in a situation where the general public, or a group of people you've designed for---the loan program

for---don't really get those funds, because they're limited to people that are already dealing in high financed things in the state and banks Outside.

DISPAIN: In my experience here in Fairbanks, I've borrowed from the veteran's loan fund several times; have always paid it back with the interest on it. I don't owe anything now; haven't for 10 or 15 years. But it certainly was a boon to me to be able to borrow money at a reasonable rate of interest and---I was in the plumbing business here from 1950 on my own. I mean I went into business for myself in 1950 and I'm not retired---lately, I just quit working.

But the veteran loan was a wonderful thing. There's no question about it. I saw very little abuse of the veteran loan fund. If something like that could be worked out in the state government, that's fine. But letting the banker make the loan, then guaranteeing to pay it back---I think we're asking for lots of trouble.

GRUENING: Mike.

DOOGAN: Mr. DeSpain, the governor makes a great point of telling us, and I don't---haven't seen anything to disprove this--- that roughly 60% of the current state operating and capital budget

I believe, is financed through some sort of revenue from petroleum production. If you advocate putting all of the money from all resource development in the Permanent Fund, then I assume you're not...

DESPAIN: Non-renewable resource.

DOOGAN: Okay. A broadened definition. I assume you're prepared to live with 60 cents less on every dollar for every state program that now exists?

DESPAIN: I'd like to see about 20 cents on every dollar state program right now. I lived under a situation like that here in Alaska for a good many years when the state wasn't trying to wipe my nose and everything else for me. I don't think that the people in Alaska--I'm not talking about these 30-day voters, but I'm talking about these Alaskans that have lived here for any length of time---want or need the state to provide all of these things that they are providing for them.

I would suggest that some of you people might get an education if you would go out here to the highway department and just go in there and sit down and observe what goes on out there.

I went out there one time to see a party. I spend about 50 minutes in that office. There was three in the office. I

waited for somebody to come in the office, was what I was waiting for. I just sat down and didn't bother anybody. For 50 minutes and there was three women in the office, secretaries, I assume, or something. Anyway, they had desks and typewriters. Maybe they were the kind that couldn't type, I don't know. Anyway, one girl was sitting there reading a book. One was sitting looking out the window. The other was just sitting, just with her arms folded. She had a piece of paper in the typewriter, but she never hit it. And for 50 minutes there wasn't one of those girls did a thing. Now that's why our highway department spends so much money. Because they hire people to sit around over there in that office and do nothing.

I mean literally do nothing. So if the money that goes into the highway department was spent on maintenance crews and people working out on the highways and doing some work, we could have a tremendous road system and probably 20 cents or 25 cents on the dollar would do it.

You name any division of government and, I think, the same thing applies to it. When I talked to the governor about this deal over at the license bureau, he said, "Well, I don't know what to do about that." I said, "Well, pay them by the licenses they issue." I said, "well, contract it out and let somebody else do it." Do away with the license bureau as far as the state's concerned and contract it out and let somebody do it on a bus'el basis.

Pay them so much per license. Give them all five bucks. It would save lots of money. Give them the whole five bucks. Okay.

GRUENING: Thank you. I have one question. I asked you about the investment. You suggested that one investment that would at least look good was an Outside one in the Bank of America short term.

DESPAIN: Well, no. I used that as an example of one that we had used one time on a large loan for a year. We got a CD from the Bank of America and it paid one and a half percent more than the treasury notes were paying at that time. There are other investments, other than treasury notes, federal mortgages that pay more money. Maybe they're riskier, I don't know, but anybody who thinks that the interest on the treasury notes keeps up with inflation, they're just not very well versed, because inflation is always 4 or 5, at least 5 points higher than they're paying on treasury notes.

GRUENING: My point was did you infer that it might be that some of the Permanent Fund money or at least the majority of it might be invested Outside if there were no sufficient programs for investments in the state?

DESPAIN: I think that the---absolutely, I don't think that

the state has enough industrial wealth or capitalization to absorb that kind of money. I think it would have to be---the majority of it would have to be invested some place Outside but the income from it is what the state government should be living on. I think it should be invested where it does the most good.

Now I'll tell you. It would be a tremendous boon to business and private enterprise in the state of Alaska if the state lived off that kind of income, rather than keep raising the taxes and raising the taxes on gasoline, raising the taxes---business license tax and these things---that hasn't been raised recently, but---if the government would just leave private enterprise alone and not keep taxing them to death. Of course, I know these socialists, they think that the big business is the one that is hurting the working man and the people in the lower income bracket. But believe me, without big business, these people in the lower income brackets are going to be way down the line along with the business. Because when you knock the businesses out, people don't have the money, they don't have a job. Maybe they work for the government and don't produce anything, but they don't have anything that really sets them up and they don't have a chance to go into business for themselves when government gets so oppressive as we're getting right now.

GRUENING: Okay. Thank you. Are there any other questions

from the committee? Thank you very much. Have we exhausted everyone? Please.

BRAVARNEY: My name is Stanley Bravarney. I'm a citizen of the United States, who's lived in Alaska since about 1954. I work as a surveyor, construction surveyor. I notice that Mr. Collette teaches how to build things. I build things. I don't teach people how to do it. I just do it. If you don't know how to build things, you teach other people. If you do know how, you get a job building.

I have some small investments in market stocks. I've had them since 1957. They're very modest. I make some modest returns on those things. I like to think that I beat inflation out. There are a few rules about investing. One is you got to win. All's fine---you wheel and deal and buy this and buy that. You do all those things. But you still want to win, you have to make money.

When you get guys like Arlon Tussing and Rex Fisher and people like that handling the money---these people are socialist, Communists. They think that government, big business is immoral. They're born losers because they feel that money, making money is wrong. You give them the money, they'll lose it.

GRUENING: I want to put your mind at rest. We're not going to give it to anybody.

BRAVARNEY: Well, you have been giving Tussing millions of dollars for programs which he hands money to people to have these study programs. These people of socialistic government in Alaska gets very, very large funding. They don't give us anything out of it. Incidentally, Mr. Parr might tell us how much the University of Alaska got this year because I haven't been able to get that from anybody. How much is the total budget for the University this year?

PARR: I'm sorry I can't tell you.

BRAVARNEY: It's a state secret---either that or the evasion of rights. You can't give a budget total for the University of Alaska.

PARR: Well, there are two reasons. First the total funding is not available because a good amount of the money was held back by the finance division pending application by the Board of Regents. Until the regents have applied for it and showed they have a genuine need for it, they won't ge it.

BRAVARNEY: Very interesting. With our million dollar

computer we threw it away and we got a three million dollar computer. So now we don't know about this computer enough to tell us how much money we're spending. This is one of the situations.

The second situation is again like if you're investing money as a private investor, you can be eaten up by commissions if you're buying and selling and again having lots of fun. But after five or six years, you find out that the commissions will have eaten up all your profits.

It's the same way. We have spent tremendous amounts of money for all kinds of expert advice. The only thing we got out of this was a bunch of expert advice that didn't give us any money.

Okay. So those are the things that we shouldn't do, but what should we do? As far as I'm concerned, I'm speaking as a non-Alaskan---here for 20 years. I've got maybe \$35 or \$40,000 and I can invest it in something. I can buy some land in California or Oregon or Washington. I can buy land in Alaska. I find land in Alaska is about five times the cost of comparable land in California. If I can find land say in Washington for \$2 or \$300 an acre, you can't induce me to invest my money in land in say Delta, if anybody is looking to buy it.

So my idea is I don't want to invest in me; I want to

invest in you, young people in Alaska. I work as a surveyor, I said, and all the people that I work with they're the young. Some of them have more talent and more education than I. Some of the best surveyors are some women that survey for me. They're real hot shots. When they're not surveying, they're not sitting around here doing this. They're taking courses. For the young people in Alaska, are we going to have roads, are we going to have acres that we can let them develop, that we can let them build on? Are we going to let the young people use the resources, their minds, their talent, or are we going to let people like Dr. Walden, Dr. Drew and all the rest of those people decide what we are going to do? Are we going to say have 150 acres or 250 in Big Delta, that you can squat on, do anything you want with it?

If I want to invest in anything, I don't want to invest in government. I don't want to invest in the University. I think that our university has a very, very bad program. We got this because it's ours. I'm saying we got to make our own minds. Thank you.

GRUENING: Thank you. Any questions? Next. Thank you very much. You're the first woman to testify today. I'm glad. No. Wait. Sandra was the first.

WESTCOTT: Well, I wasn't going to testify today but I am one of the young people in Alaska that would like to do something.

First of all, I think I've heard inflation here today.

GRUENING: What is your name?

WESTCOTT: Excuse me, Rynniva Westcott. I live at
6 1/2 mile Richardson Highway.

I've heard inflation, I've heard a lot of ideas of what we shouldn't do with our money and what we should do with it. I think I'd just like to bring forth a few thoughts. I think the only way that Alaska is ever going to fight inflation is to develop a manufacturing economic base utilizing our renewable resources in a way that is beneficial in several aspects to our cash flow and our destinies. I think we should be re-circulating money in Alaska instead of seeing the money spent in our current flow system where the money eventually, through the economic chain, ends up in the coffers of an industrial corporation on the East Coast. By establishing an industry with our renewable resources, we also decrease the liability on our less than desirable transportation systems from the West Coast.

I think also, by establishing an economic base revolving around our renewable resources, is that we establish once and for all, a stable economy that is composed of production and processing within Alaska versus our current system and our past system of being reliant on the government and on our

boom and bust cycles.

In Kansas this year, farmers are getting \$1.85 per bushel for their wheat. But going back to the cycle that we are living in, by the time it gets here, we're paying a dollar a loaf for our bread. This is what we've got to get rid of or we'll never eliminate inflation.

Of course, the other question is why do we need agriculture here? That question is always brought up. Well, in the lower 48 right now, we're losing prime agricultural land at the daily rate of 5,500 acres per day and while technology increases production, the multiplying factors of population increases kind of pours water on the fire.

Now this land is being lost because of population increases. You have higher home demand. New industry comes in. New services area businesses come in so you're losing land.

Regardless of what our likes are in the way of recreation or any other aspect of life, food is one of the basic requirements of life. Alaska is already in the position where we are highly dependent on importing our foods. I think we should be producing our foods, not only growing our food, but producing--processing the by-products of the initial crops, and taking care of Alaskans. Once we've taken care of Alaskans, then we can use it as an export commodity. Of course, what I'm condoning here is for Permanent Fund monies to be used for low interest loans for agricultural

development. Not just farming, but the actual processing of the products. When I say this, I'm talking about canned goods, frozen goods, lunch meats, the red meat industry, etc., so that we do have the food here. I don't know what the current statistics are, but a year ago we had a seven-day supply of food in the state at any one time. I think it's essential that we have more than that, because with a major strike of our transportation system, most Alaskans would get very hungry. The Alaskans that wouldn't get hungry are going to cause others to starve, because they're out in the stores as soon as they get a hint that there's going to be a strike, buying up all the food products in the stores, and the shelves are empty. Any questions?

GRUENING: Thank you for your statement. Any questions? When you mentioned agriculture, I thought of Charlie's bill and his work to promote it. A question comes to mind of you know, why it hasn't really flown in the past? Maybe you have some insight into that.

WESTCOTT: I don't think our state administration has ever supported agriculture. The federal...

GRUENING: The present one?

WESTCOTT: I'm talking about present and past. The federal

government has never encouraged agriculture development. In fact, there was a team of so-called experts sent here in the 1930's to explore the possibilities of utilizing agriculture lands in Alaska. At that time, they documented that it was unfeasible to utilize the agriculture lands in Alaska because they didn't need it.

Well, basic composition of this panel that came up here were farmers from the Midwest. Naturally, they're not going to want the competition that could be incurred from farming in Alaska. This brings up another point that's probably very far-fetched, but one possible utilization of Permanent Funds money, if the right set-up could be established, would be to buy some of the agriculture lands from the federal government.

GRUENING: You mean some of the D-2 lands that are proposed?

WESTCOTT: Not specifically D-2. There are lands in the D-2 that could be utilized for agriculture that are class 2 and class 3 soils. Of course, the federal government has told us that we don't have class 1 soils because of the climatic limitations within Alaska.

PARR: I'd like to reinforce what Ms. Westcott said. Of course, the bill which Governor Hammond vetoed would have been, at least, a start, first step in the direction of agriculture in

the Interior.

But I know that Dr. Burton from the university has published a series of studies on agriculture in Alaska. He may be a little optimistic but his figures indicate that we would eventually have about a \$4.4 billion agricultural sales in the state at an investment cost of about \$3 point something billion per year. So about a billion dollar's profit a year in agriculture alone. It may be a little optimistic but they are big numbers. It does require a big investment.

I think, those of us in the Interior, certainly look at agriculture as being one of the prime sources, prime targets for investment in the Permanent Fund.

WESTCOTT: I think there's a few aspects of the legislation, although I endorse the concept of it, that I have certain problems with. One is agriculture rights. These rights have never been clarified in documentation as to exactly what agriculture rights will be.

First of all, agricultural rights are going to have to be a bankable commodity that the farmer has. The other thing is, of course, that people do not invest their lives in something they don't own. What I mean by that, say a farmer lives on his land and farms it for 25 years and through circumstances that are beyond his control, he becomes vitally ill. He is the bread winner in the family, and he is going to be forced to

sell his property to pay for his medical bills and support his family. This is one thing that should be taken into consideration on agricultural rights. The way it was defined in the Delta land use study, if the land was not farmed, it would revert back to state ownership. This is not owning land.

GRUENING: If I may just comment, I appreciate your testimony on that. One of the problems around the Anchorage and the Mat Valley is that land is rapidly eaten up by subdivisions. Now I think, one of the points to try to restrict it to farming was to prevent the Mat Valley situation. Maybe that's not the way to do it, but I am too concerned with the fact that more and more farmland is irreversibly converted to other purposes. Once you get a subdivision on it, it's not going back to farming.

WESTCOTT: Well, this is correct. You shouldn't be able to subdivide farmland, but the other thing is, of course, that the farmer can sell the land to another farmer. But the way it's written up, if you can't farm the land, it reverts back to the state ownership.

I'm not saying this is the way that agricultural rights will be defined, but they haven't defined it yet. No one is going to go in and purchase land from the state until they know what they have. This would be the same circumstance with Permanent Funds. How can

you take money that has been raised through revenues of non-renewable resources and loan it to someone without clarification that he does have control on the land? Of course with your state system, it's fine and great because it's the state's money; it's the state's land if it's reverted back to the state. Nobody loses. It loses some of the personal property appreciation that individuals have.

GRUENING: Okay. I understand that. Any other questions from the committee? Thank you very much.

VOICE: Could I make another comment?

GRUENING: I'd much...we have a plane to catch. I'd like to hear from you if we have time. But I'd like to hear if anybody else who hasn't testified would like to. Is there anybody out there who would like to make a comment? That hasn't testified. Mr. Murphy.

MURPHY: Like most of the people, Representative Gruening, I didn't plan to testify, so the gist of the...

GRUENING: Could you give your name, just for the record?

MURPHY: My name is Frank Murphy. I live at 308 Noyes Street. The gist of the testimony seems to be as how we might invest the Permanent Fund. I was wondering, my understanding of the Permanent Fund was a safety valve against the day when our declining oil revenues no longer supports the state's budget. I was wondering, if that was the case, perhaps the paramount criteria for how we spend the money is the amount of return we get on it. Is that a correct view of the Permanent Fund or...I guess that's a philosophical question.

GRUENING: That's what we're asking you. That is one philosophical stand that I've heard a number of people state. But there are others, if you sat through today, you'll see there are other goals that people are interested in.

MURPHY: The General Fund is probably more flexible than the, and possibly larger in dollars and cents than the amount of money in the Permanent Fund. It would address itself to most of these investment names which I thought I would agree with, as far as developing Alaska.

But in terms of, and I don't know whether we are going to have people project this situation that the state might be in 10, 20 years down the line, of not being able to support its operating expenditures due to a decline in oil revenues. If we are

faced with that, the Permanent Fund then would be our guarantee against being in that embarrassing situation and should be defended as such would be. And that's all I really wanted to say.

GRUENING: Thank you, Frank. Any questions from the committee? Thank you very much. Is there anybody out there who hasn't had a chance to testify? Yes, sir.

MORGAN: I guess somebody's got to be last. I'm Ray Morgan. I live at 2½ mile Farmer's Loop Road sometimes and sometimes on a homestead across the river in Delta Junction, which I'm still trying to improve upon. I'd like to take off probably where Rynnieva left off and say a little bit about what I'd like to see about the Permanent Fund and also zero in a little bit on the agricultural possibilities in Alaska.

First, it's been my impression since we've been talking about, what I've read in the news media about the Permanent Fund and it was supposed to have been a Permanent Fund for the development of renewable resources in Alaska taken from the non-renewable resources. I guess in the last few months or a year or so we've changed that, so now, also including non-renewable resource development in this, and this I would not argue with. I think we need the non-renewable resource development along with the renewable resource.

I would like to see about half of the non-renewable resource funds put into the Permanent Fund. Just using the interest on this money for the development of non-renewable resources.

There are four non-renewable resources as I see it in Alaska that should be a part of this development. I'd put on the bottom of the list, I think, tourism. I think tourism is a renewable resource, whereby funds can be used to help support this industry.

I think the third one I'd put would be the fisheries industry. Fisheries have certainly not been explored very much in Interior Alaska, but is one of the biggest incomes we have in the state. Probably the second one outside of all our mineral industry today probably I'd say would be the timber industry. This is not again in Interior Alaska, has not been talked about, has not been explored very much at all.

The first one, I think, the top priority I'd put would be agricultural development. Last year we exported from Alaska about \$100 million to buy food that we can produce here in the state. If you take this, carry this out over another 10 year period, you can see this is going to master quite a few hundreds of millions of dollars that we're going to send down to Seattle and to California and other states to buy the food that we can produce here. I'm not talking about food that we can't produce here, just the food that we can produce, the red meat and about 35 different kinds of vegetables.

What I'd like to see us do is to provide funds for two phases

of an agriculture program that we don't have.

One is for the infrasturcture to help support an agriculture program. Without an infrastructure to help support it, we will never succeed in agricultural program. I think the 5,000 acres the state is going to sell in the Tanana Loop area down to Delta Junction will never become an agriculture supporting program. It will become a lifestyle where people want to live in the rural area and will become a kind of a rural homesite, the kind of area that I like to live in too, but I can't afford to do it. Suppose the infrastructure means the machinery dealers, the repair stations, the warehouses--- this is the kind of infrastructure I'm talking about. You can imagine now we don't have that in Alaska. It's almost comparing a railroad to a---what do you have if you have a railroad without tracks or without a railroad yard? You have to have an infrastructure to support the railroad. You also got to have this to support an agriculture program.

The second thing we don't have in agriculture program goes along with infrastructures and marketing system. Until we get a marketing system developed to market within the state and outside the state, the things that we can produce and program jobs for the unemployed and the underemployed, we will again be doomed for failure in any kind of an agriculture program.

So I'm talking about---think I've said this---use the

Permanent Fund, the interest from the Permanent Fund and allow it to be controlled by the people in the state, as some other people have said, let's keep control of that 50% of the non-renewable money that we have and let's spend the interest on it and save it for, the principal part of it for the children that's coming along. I've got three that'll probably be in the state for quite a long time after I'm gone. I'd like to see them have a part of this. But the agriculture program, I think the marketing system and the infrastructure that it takes to support an agriculture program--without those we're going to see some more Matanuska Valley, like you folks have seen in Anchorage, happen right here in the Tanana Valley too. Thank you.

GRUENING: Thank you, Mr. Morgan. Are there any questions?
Mike.

DOOGAN: I'd like to make a statement for the record. There is nothing in the law right now that stipulates that the Permanent Fund will be used for development in Alaska; there is, however, nothing in the law that stipulates that it will not. One of the purposes of these hearings is to find out what people think about that proposition.

GRUENING: I had one question. You know, I know so little about agriculture that I hate to make any statements, but I have

a question in my own mind of why it hasn't flown in Alaska. I've heard this has been suggested that in the Outside agriculture business, called the agribusiness, it's huge, through its massive size and efficiency, can out-compete anything we do up here. Now does that mean to compete we have to get on the same scale? What advantages do we have that would enable us to, say, produce food as cheaply without, say, heavy subsidy as is done Outside?

MORGAN: I think I'd include agribusiness enterprise in this infrastructure as a part of it. And yes, there is a volume that has to be produced before you can do it economically an agriculture program. Some of the folks at the university have said---it's the best information they have---that about a barley development project, the minimum is needed to support the infrastructure, the marketing system to be able to go in the state.

This, of course, is what the governor's planning for the 70,000 acres in Delta Junction. I think we have never had that volume to be able to support the infrastructure, the machinery dealers, the kind of equipment that is needed to be able to supply the market for our own use, and this is why today we're importing about 96% of the food we consume.

GRUENING: Do I understand your proposal that the interest

from the Permanent Fund earnings would be used to help agriculture or was it that actual investment of the principal of the Permanent Fund would be used? Or both?

MORGAN: No. I think I'd like to see just the interest used for the promotions of the non-renewable resources as well as some other kind of economic developments like a phosphorus mining operation, a petrochemical operation which would supply the state, other kinds of nitrogen for agricultural programs. I think these too would need to come along with---to support the non-renewable resources too. Using just the interest, right, not the principal.

GRUENING: Now what about---agriculture would receive loans or grants from the interest---is that the thrust?

MORGAN: I would not say grants. I would say we would receive loans. Yes. I'm not too much in favor of grants.

GRUENING: Okay. Any other questions? Charlie.

PARR: Only one. I might comment, of course, as it was pointed out by somebody, must have been a few minutes ago---there will also be money available in the General Fund, which can be used for some of these things. It wouldn't necessarily have to come---all of the agriculture help wouldn't have to come out of the Permanent Fund monies.

GRUENING: There was a newspaper article, I think it was in the Anchorage papers---it may have been statewide---about some of the defaults in the agriculture loan program, the state agriculture loan program. In other words, the loans are in default and the state isn't getting paid back on some of them. I think we want to try to avoid that. Any suggestions we can have, and maybe it's the fault of the way it's administered. But I think we want to, if we're going to put more money into it, we want to discover what went wrong.

MORGAN: I think this is true. And again, I'd say any of the reasons for the defaults has been just a lack of volume. You just cannot operate an agriculture program in the state of Alaska unless you have the volume to support the infrastructure and the marketing system, those two things. Until you're willing to invest in those, I think it's doomed for failure. I'm sure the agriculture program in 5,000 acres in Delta Junction will never succeed as an agriculture program. It'll be a lifestyle, that some people who buy the land, have agriculture rights, will be living there. That'll be about basically it.

GRUENING: Okay. Since our time is limited, we're only going to have one or two witnesses. We may try to make that

plane. Is there anyone who hasn't testified yet who would like to?
Yes, ma'am, why don't you comment on that?

WESCOTT: Can I just speak from here?

GRUENING: Why don't you speak in the microphone? We're recording this. We'd like to preserve it.

WESTCOTT: You are referring to the agricultural revolving loan fund---correct? I think one of your basic problems with that program is that it's very political and very isolated. You have a recommending board, that is made up---the majority is made up from the Palmer area, residents of the Palmer area. I have seen case after case where a loan is approved through that program more on who knows who than the actual economic basis of it. That would be my only comment on it.

GRUENING: Well, I appreciate that, because you can see that same problem facing the fund. We can have it all go out in bad loans, depending on who Permanent Fund managers are. We have a real problem.

WESTCOTT: In fact, I think you may be aware of the fact that Bill Lewis, who is director of agriculture, was dismissed three

months prior to a new director being put into the office basically because he was going against one loan on the basis it was not backed up properly with collateral; it was not an economic venture that he thought was a good banking loan. It was approved after he was dismissed from his office.

GRUENING: Do you have any comments, suggestions on how these loans might be administered differently?

WESTCOTT: I don't have any suggestions. I have suggestions of what not to do, and that's to set it up the way the revolving loan fund, is, with just a geographical board sitting in Palmer making the decisions for a statewide development program.

GRUENING: I sense also that you feel too many of the loans aren't getting up in this area. Not enough of the money is getting to this area.

WESTCOTT: I think that would be a legitimate complaint. Yeah.

GRUENING: Okay. You, Mr. Bravarney, is that it? Could you make it short, because there's one other comment in the back? Thank you.

BRAVARNEY: Very short. I want to briefly state a couple

other things. I'm from Pennsylvania originally. We folks are Polish people, many of them were farmers. I've seen exceedingly skillful, dedicated people with small farms. My attitude about farming and growing things---you can grow on two acres; you can grow on two million acres. You got to be a farmer. That's all there is. I have a degree in forestry from the University of California, 1954. We didn't know economics. We had chemistry, physics, mathematics, botany, and all those things. We didn't know too much about economics. (inaudible)...a hell of a successful forester. Wouldn't mind seeing (inaudible)...farmers for, if they think they've succeeded (inaudible)...It's the same with farmers (inaudible)...I could perhaps go to an area and maybe have (inaudible)...sort of thing. I could put the type of energy that it would need into developing something, young people can. Right now this (inaudible) business, but everything comes to Alaska late. (inaudible)...the university is notorious for that. They get the (inaudible)...There's a nice thing about this great, big (inaudible) Marxist Socialism. If it's succeeding here, (inaudible) is falling in other places. (inaudible)...but in many cases, it isn't. It (inaudible). There are lots of...the state is (inaudible)...We can't plow the ground with (inaudible)...

GRUENING: I think there'll be a hearing some other time on the university.

BRAVARNEY: We're not developing students; we're developing PhDs. Thank you very much.

GRUENING: Thank you. I saw Mr. Spencer enter the room, and since everyone has testified, did you want to say something, Jerry? We're trying to catch a plane out, not because we want to get out of town, but because we have another hearing tomorrow.

SPENCER: Okay. Thank you, Mr. Chairman. I just had a couple thoughts. I'll try to be brief. I appreciate very much your coming to Fairbanks and collecting opinions on this Permanent Fund idea, which I don't really know much about, but it seems to me it's got some extraordinary possibilities.

GRUENING: Excuse me. Could you identify yourself please, for the record?

SPENCER: I'm sorry. Yes. Jerry Spencer. I'm a 17-year resident of Fairbanks and director presently of the Fairbanks Town and Village Association. We're a regional, non-profit development organization.

I think the only thought I had to offer to you, I'm sure you've heard some very good testimony this morning---when I was here. I'd like to second many of Mr. Wallis' and Mayor Carlson's thoughts on the nature of the Permanent Fund and these

types of investments and so forth. Some of my concerns, though, have to do with, you know, just the whole idea of how you deal with a billion dollars or two billion dollars in a state this size with 400,000 people in it.

The state's budget this year---and Mr. Gruening, I think you and I would probably find a great deal in common on how the state spends its money---but the idea of a billion, one hundred billion dollar budget is just overwhelming to me. The idea of the Permanent Fund having, you know, what are we talking about, two billion dollars in it a few years down the line. This is just mind boggling as far as I'm concerned.

As you deliberate how to manage this thing I would hope that there'd be not only decisions on how the fund is to be allocated in terms of what kinds of things are financed, but you spend a great deal of time on how, you know, the general public is going to be able to keep in contact with the managers of the fund.

As far as I'm concerned, the general public doesn't have much to do at all of the expenditure of that---talking about how you accept policies, how you set up administrative practices in the spending of the billion dollar state budget. I think it's causing some serious problems. That may be an unfair statement, but I feel that people just don't feel like we have the management tools to manage that kind of money. I feel it often myself.

Now you're contemplating something of this sort, which is really

going to make Alaska, I would assume a force in the international money markets. People of Alaska are going to want to watch that very closely. They're going to want to feel they've got good communication with the evolution of the fund. You can't set up administrative mechanism at the front end and just sort of say that's all we need to do with it. This thing is going to evolve day by day in terms of the theory, the thinking about it, how the money's going to be spent, how you're going to allocate parts of it, whether you're going to spend a bunch on rural communities, whether you're going to dump a bunch in the banking system, whether you're going to get involved in investments in Saudi Arabia, or whatever.

The public, you know, that device for making sure the public is constantly in tune with the evolution of the fund, I think is equally as important as deciding how to spend the money---more important, because without that, you're going to be---distance I'm afraid is going to be so great that you're going to have a serious credibility problem and a constant political hassle. We've had enough of those. I'd like to see less of them in the future. As long as we've got this immense gap between the people and their understanding of how to spend or even consider a billion dollars, I think that's where I would recommend the committee and other interested in the development of this fund---I hope they would spend a good deal of time on that.

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GRUENING: Thank you, Mr. Spencer. You just mentioned one of the more difficult problems and that is how you make the funds responsible to public need yet not, let's say, acceptable to a lot of political maneuverings where you have bad loans made because your friends are asking for loans. Any suggestions you have along that line would be helpful.

I only can say that the General Fund is managed by, of course, the executive; but the budget is made up by the legislature. If you don't like the way the legislature does it, you can always vote the legislator out of office. With the Permanent Fund, if you have a structure that doesn't have elected officials, I don't know how you would directly respond. So we have a difficult problem.

SPENCER: These comments that I am making now, by the way, have no parties in cast to them at all. I think it's a problem both Democrats and Republicans are going to have to address themselves to.

You know, you're quite right. The legislature, there's a term for it---the legislature appropriates, the administration spends. The nature of the spending is a problem for both branches. I think it's a serious problem and it's going to get worse, I suspect, because I don't see that the people are that concerned about the mechanism for managing all of this money. You know. And I'm not talking about the services people receive. I'm talking about how you actually put the policy together with the administrative mechanisms and the

communication with the people that, I think, is necessary constantly. I just don't see that. I don't see much movement towards trying to develop those things. That's my concern. I appreciate your...

GRUENING: Any questions? Thank you very much. Has anyone not testified who would like to? Yes, sir.

LAUESEN: My name is Elstun Lauesen. I live at 2416 Gillam. I assume that you're after some broad, general ideas. You're just here to get people's feelings.

GRUENING: To get a nutshell. What's your philosophy on the Permanent Fund?

LAUESEN: Alright. In a nutshell, I feel that the Permanent Fund should keep a...let me read from my notes here, because I have a lot of ideas and I want to get them out systematically. Alright.

I want you first to consider this---that public equity and private equity are fundamentally different, because the definition of value changes as one moves from consideration of the public good to concern for the private profit picture.

I feel that, as much as the Permanent Fund is capable of

doing so, that it should be considered a public trust. While remaining secure, it must have the flexibility to penetrate the thick overlayer of corporations and institutions that exist in the state and be able to reach the individual and the group who have a legitimate and reasonable need for funding.

The question is what defines reasonable.

I would like to suggest then that the major criteria for the reasonable kind of development to be encouraged by the Permanent Fund and also for the Renewable Resources Fund is principal of economic self-sufficiency for the Alaskan People. That is a real public equity, but that would be an investment nightmare.

I envision the development of both production and distribution co-operatives in this area as large numbers of individuals undertake programs of resource-pooling in order to deal with long-term unemployment which exists here, either by circumstance because of the seasonal nature of a lot of the work here, or by choice, by those individuals who seek to be de-intensify the economic future of their lives. I see nothing subversive or wrong with this. There's a lot of people who are trying to approach that kind of style of living. Now obviously these are not the kinds of conditions that traditional money-managers would enthusiastically embrace, but they are on the horizon. I see them increasing. They will require servicing.

Excuse me for breathing into this microphone, but...I would

like to see two conditions, therefore, created within the Permanent Fund and Renewable Resources Fund. First I would suggest a generous allotment of capital for risk, what I call risk capital or venture capital based upon the assumption that the public equity derived from programs and projects designed to foster self-sufficiency are worth the more liberal risk structure.

And number two---the uses of the fund be monitored by public agencies as well as the Permanent Fund committee because of the range and the special condition of these investments will require an understanding kind of review and analysis. For instance, the Cooperative Extension Agency might be the review agency for family and small group investments dealing with commodity production, such as small agricultural cooperatives. Risk capital is review analysis. The latter is important because in some cases the only public equity would be the knowledge derived from the risk taken. This would include individual excursions and alternative energy resources in the building of their homes or whatever.

I'm of the conviction that the existence of risk capital might ignite success in community terms. For each enterprise it successfully interfaces with community need and lending, thereby, a greater self-sufficiency to the community as a whole, represents a public equity and not measurable in dollars.

I wanted to bring this thing, but I didn't get a chance to type it up, that is illustrating this whole point through the development of food cooperatives. In an attempt to quickly establish a source of local economic developments infrastructuralization, where there is a cooperative arrangement between producers and consumers to avoid what, in the future, is going to be a spiralling cost in macro-economic factors affecting Safeway stores and that kind of thing. We have to localize our production and localize our development.

GRUENING: You can submit a written testimony any time later on.

LAUESEN: Okay. I have just one final thing before you off to the airplane.

I would like to end this part of my testimony by questioning the advisability of what may have called the tools of the money managers. By encouraging large scale investment, you create an elite class of borrowers. Unlike that gentleman, I think either loan guarantees or syndicated loan arrangements should be de-emphasized because it is the internalization of the Alaskan economy, that I believe, ought to be encouraged, along with, I'd like to add, stabilization of the economy.

Even if these conditions weren't such huge blocks of capital unless it is a sizable project, which I would submit, might be more efficiently and effectively funded co-ventured or owned by

the state directly rather than having to launder it through private enterprise in order to give a patriotic or traditional appearance to your undertakings. This is precisely the condition that I fear the Hammond administration recently proposed to \$750 million loan guarantee to El Paso's gas lines.

In any case, I realize that the Permanent Fund will represent a considerable sum, but we're not under any gun to invest it as fast as we can. If the business community is worried about the Permanent Fund maintaining parity with the eroding value of the dollar and thus urge us to "put our dollars to work" I would suggest that the logical thing would be to ignore the advice of the so-called Alaskan business community and convert the holdings of our Permanent Fund from the all-American dollar to the Canadian dollar and sit on it. Thank you.

VOICE: Could I ask the gentleman a question?

GRUENING: I would like to let this go into debate, but I saw Mr. Dempsey come into the room. We are debating whether we're trying to catch the plane. If you...

VOICE: No. That's okay. Thanks.

GRUENING: If anyone has a written statement that they want to make later, please feel free to submit it to the committee. Is there anyone who hasn't testified who would like to? I want to thank everyone for turning out. I've enjoyed this. I really have. And I plan to come back to Fairbanks before we recommend anything final to the legislature. Thank you.

Proceedings
of
The House Special Committee on the Permanent Fund

PUBLIC HEARING
September 15, 1977
Anchorage

Rep. Clark Gruening, Chairman
Rep. Terry Gardiner, Vice Chairman
Rep. Ernie Haugen
Rep. Russ Meekins
Rep. Bill Miles
Rep. Leo Schaeffer
Rep. Rick Urion

GRUENING: Good morning. We'll call this meeting to order. We've got a list of people that want to testify and I think there are some that are not on the list and we'll just take you down on a Quaker basis. You raise your hand and come forward and testify. Don't let the ads put you off. I saw the ad in the paper that this was called the House of Permanent Fund like the House of Pancakes. This is the House Special Committee on the Permanent Fund.

Representative Ernie Haugen on the committee from Petersburg told me this morning that he heard on the radio that this meeting was to hear from you folks on how to spend the fund. I can assure you that is not our intention. We want to hear we can preserve that fund and we are just as interested in what you don't want the fund to do as what you want it to do.

We had a very interesting hearing in Fairbanks. We heard a lot of what people wanted it to do and what they didn't want it to do. Since it's your fund and before we actually draft specific legislation for consideration of the whole legislature, we want to hear your philosophical approach. So this is---don't feel you have to be an investment banker. We are really talking about philosophy today.

Also with the committee is Representative Bill Miles

and Representative Russ Meekins who is on the committee will be here shortly. Our A.A. to the committee is Mike Doogan and he may be asking some questions today. Do you have any statements, anybody, that you would like to make? OK, our first witness is Senator Joe Orsini.

ORSINI: Mr. Chairman, members of the committee. Thank you for the opportunity to make a little pitch here. I will be brief. My concern is not at this point with what the use of the Permanent Fund is going to be, but how the uses are determined. To a large extent, the legislature will undoubtedly set broad policy guidelines, but the actual management of those guidelines will be done by some body or some group of people and I'd like to address my remarks to how that group of people come into being chosen.

The Permanent Fund was overwhelmingly adopted by the public last year, as we all know. I suspect that your hearings are turning up a variety of opinions when it gets down to the specifics of how that money is going to be used. I would also imagine that probably there isn't a great deal of coalescence of public opinion at this point and people are kind of vague about it except for those people who happen to be in investment or other kind of industry that is directly involved with it. I would also suspect that, despite the good efforts of this committee in trying to get the issue before the public, that until something really happens or

until the fund is viable such that the impact is being felt substantially in whatever corners that money is going to be spent that the general public will not become involved in this. I could be wrong, but I think that is likely to happen.

On the other hand, people who are knowledgeable about such things as large investment fund maintain that those who control this fund will be extremely powerful in a political-economic sense in the state and probably to the extent that the size of the fund in the next 5-10 years is probably unprecedented with respect to any other state in the Union as a proportion of our state budget. This concept of the power of the fund manager will probably come to pass.

For these reasons, it is my opinion that the managers of the fund ought to be people who are directly accountable to the people, the voters and the general public of the state as opposed to being selected by some other secondary method --- as a panel selects potential people from whom the governor selects. This is sort of a circuitous approach which, in my opinion, ought not to be implemented. I think that one man ought to be directly accountable to the public. As the public sees a need for change in the way in which that fund is invested or used, that change will be reflected in the debate when these people run for their office. And, of course, it

ought to be a full pay, full time office, not just a token or a commission, but a full time, full pay position. The people that run for that, I would think, the public would demand that they have some ability and expertise in handling money in that it is more strictly aimed at than, say the legislature, which is a very broad type thing.

I think the problem with, say, a gubernatorial appointment is that every four years the governor runs for election and there are many, many issues that the governor has control of or discusses and the Permanent Fund will be lost in so many other issues that the governor is involved in --- any governor. I think that this is important enough that they ought to be separately elected.

The frames of the constitution, the state constitution, of course, determines that the governor is the one that has the appointing authority and there are no other elective officers on a statewide basis other than the legislature. But I think that the constitution was framed more than 20 years ago and the state has changed its standards. And we are into an area now, with the oil starting to flow, of a yet greater change than we have seen in the past. And this change should give one reason to take another look at the constitutional concept of only the governor being elected and look at those kind of offices that are perhaps of genuine statewide importance and have statewide input for that particular concern.

That's really the extent of my testimony. I would urge you to take a look at the concept of having elected people managing the funds. It can be done without changing the constitution as long as the governor has some choice, you could have an elected official---is what I'm told by the Legislative Affairs Agency. Of course, the cleanest way is a constitutional amendment.

GRUENING: Thank you, Senator. Can you stay for a few questions? Any questions from the committee? Representative Haugen.

HAUGEN: Senator, how did you set up the---you mentioned qualifications for the fund manager---that it would have to be people with expertise. Have you got any idea as to how you would qualify that? How would you set these qualifications up?

ORSINI: I wouldn't. I would let the public---presumably ---running for the legislature, there is---you don't have to be particularly have to be an expert in anything. The legislature deals with all kinds of things.

I think the Permanent Fund is different. It is a function of investment. I would think that the public would always

vote for those people who at least have some sort of ability or have evidenced some sort of experience in finance. Maybe he's been a banker, maybe he's been a union fund manager, maybe it's been a whole raft of things that have become involved in the financial implications.

HAUGEN: But you would first have the public set up the background essentials and then ...

ORSINI: No. I think it ought to be an elective office, period, with no other than--I would have no more restrictions on that office than I would have on an office of the legislature.

HAUGEN: Oh, I see. I thought you were implying that you wanted restrictions.

ORSINI: No. I think the public, as the public, will vote for those people who have some of those qualification.

HAUGEN: OK, thank you.

GRUENING: Mike.

DOOGAN: Senator, have you given any thought to whether these people should be elected on a statewide basis or by region or anything like that?

ORSINI: I would support a district basis to assure that there are a variety of interests. I suspect that you are hearing from various parts of the state has borne that out. That different parts of the state do have different concepts as to how that fund should be used. I think that on a district basis it would be preferable. It may be, my suggestion would be some combination of existing election districts where you group---an individual would run for a seat that would be comprised of several election districts so that you wouldn't have the new election districts to try and fit in.

GRUENING: Senator, you hit on probably one of the more difficult issues for the legislature and that is the issue of control. When you have a sizable fund, people are concerned about who is going to control it. It occurs to me that what we'd have there is---we'd be establishing two legislatures to the extent that you increase the size of the Permanent Fund, you'd have a competing legislature. And whether you needed a constitutional amendment or not, I think you do. Do you see any problem with establishing essentially two

legislatures and---with a very strong executive in this state? Wouldn't that kind of tip the balance in the constitution where we have a legislature, although not, maybe not a match for the strong executive, at least it is one body and has the power of the purse. This might fragment it into two. Have you considered that aspect of it?

ORSINI: Mr. Chairman, I don't think you'd have two legislatures. I think you may have two legislatures if you, for example, took certain legislators and put them into Permanent Fund managers. They would almost be operating a separate legislature. But this is a separate body and this body would still be subject to the law as passed by the legislature and signed by the governor. I would presume that we would have laws of general conceptual of appropriateness to the way in which the Permanent Fund is used and this group would have to operate under those laws.

But still, like any law, whatever executive authority it is has a varying amount of leeway, depending on how tightly those laws are written. I don't think you'd be---you'd have another group just as you have the executive and you have the judiciary and you have the legislative groups now. This would to some extent, with the more narrow confines, I suppose, would be almost a competing group who would have also direct public accountability. But I

don't think you are getting into a separate legislature. A lot of it depends on what the ultimate will of the legislature is with respect to the types of use this Permanent Fund is put to.

Basically, if the legislature decides anything other than maximizing a safe return on the investment, then you are subsidizing some group. It may be homeowners, it may be investing people, it may be fishermen, it may be farmers, it may be any one of a number of groups, whether a narrow constituency or broad statewide groups. It is still some special group or a series of special groups. As opposed to having maximizing returns, having them coming into the general fund for use of legislative determination of how the funding should be spent.

GRUENING: You raised an interesting point there. You were saying that, if I understood it correctly, that when you are dealing with anything but a sole criteria of maximizing income, there is usually some subsidy involved and if you are going to do that there ought to be some equity or some representation.

In other words, if you are going to dole out subsidies, it ought not to be done, let's say, at the decision of some expert, but rather somebody that's responsive as an elected official.

ORSINI: Yes.

GRUENING: Well, let me toss this out as an alternative to that. The extent that you get into the programs which involve subsidies, what do you think of handling it as we do now in the general fund loan programs, in that we establish them out of the general fund, that with the Permanent Fund, you establish that criteria of maximum---of conservation of principal and return the income.

In other words, rather than do everything you have been doing with the general fund, put the Permanent Fund off to the side and say, "OK, we're not---that's the one fund that is not going to be, let's say, doled out, as, say, political pressures dictate, but will be at least for the short run set aside for just preserving capital and producing income." In that way, you don't have that accountability problem that is difficult when you do get into subsidies.

ORSINI: I think I have been on record as personally supporting that concept. Certainly in the short term. As the Permanent Fund grows and as the public becomes more aware of it, you will make a policy at some point. But I think that in the near future it ought to be managed for maximum return, maximum safe return on investment.

GRUENING: Thank you very much. Any other questions? Thank you, Senator. Our next witness is Robert Rutherford. Did I pronounce that right?

RUTHERFORD: Yes. Mr. Chairman, members of the committee. Thank you for the opportunity to appear. I'm not exactly--- consider myself very experienced with these things. I hope I understand the intent of the hearing.

My business, as you may know, is a consulting engineer working primarily with the electric utilities throughout Alaska. So, most of my experience in Alaska since I came here in 1950 has been related primarily to the electric utilities industry. Along the way in working with these utilities, of course, the business of providing money for the development of electricity, that unique energy that really contributes to the quality of life, is one of the things that we are constantly dealing with and I have some thoughts to share with you and I hope along the way that I can understand the intent better so that I can add to this with some written testimony which I can supply later. Will I have the opportunity to submit some things in writing later?

GRUENING: Yes. And I'd like to say for everyone here that we'll accept written statements any time until the time

of the session. There are kind of informational booklets the committee has prepared with a questionnaire on the back. Feel free to help yourself to that and, Paul, why don't you take a stack of that so people don't have to come up. Grab them and they can help themselves. Go ahead, sir.

RUTHERFORD: Let me recite a few areas where it's occurred to me that the Permanent Fund or something similar to it, at this point, I'm just trying to understand what some of the concepts for it might be, what the committee might be thinking about it. Let me talk about these briefly. There are several areas where I believe that the use of the Permanent Fund might be valuable to Alaska.

First off, I'll start out with saying that I believe that my understanding of the Permanent Fund that its use should be on a basis where it's returned. In other words, that it is not intended as a gift, that it should be used in a manner that it is returned to the Permanent Fund if it is loaned on various bases. My own personal feelings are that the fund should be used in that manner. So that it does not definitely become part of the system of grants, perhaps.

GRUENING: Incidentally, that's a constitutional requirement,

the way they---it can only fairly be read to preclude grants. It would have to be income producing.

RUTHERFORD: That probably was in my head from back a ways and I'd forgotten it was already a constitutional provision.

One of the areas where I believe the fund could be used, I like to talk about a minute, is perhaps might be considered as marginal in the sense of whether or not it might be a grant, but, let me explain. There are a number of projects that I have seen as potential in Alaska which are the nature of being somewhat unconventional because of the unique requirements of some Alaska situations. So there are some areas where ---I'm speaking of the electric utilities business where the utilities could use some support for projects that engineers such as myself believe are feasible projects and good projects, but at the same time they may be somewhat unconventional and on that account may have some difficulty in obtaining funding from the more usual sources. I'll give you an example or two.

There has been under study by the Alaska Power Administration some ways in which electric energy can be brought to some of the small villages of Alaska on a basis that, perhaps, is a little more reliable and feasible than some of the present

systems that are in use, mainly small individual generating plants scattered around in the various isolated villages. In an effort to evaluate whether there are some alternatives to that, and in particular see if there is some possibility of being able to deliver forms of energy that can displace fossil fuel, the Alaska Power Administration has in this case asked us to do some studies relating to interconnecting villages with transmission lines, or lines of some kind whereby a group could then receive energy from a larger central supply source or perhaps a small hydroelectric project. And of course, as you know, hydroelectric projects are determined by where the water is and where there's the head and invariably it's necessary to take that energy and deliver it. So, in the small village communities, the only alternatives are to figure out a way to interconnect.

There is a concept that I have presented in these reports that is not unique in the world, but it is somewhat unconventional and it's what I've called a "one wire ground return system" of transmitting electricity. It's been used in many parts of the world. The technology is well known. It's not something that's R & D. It is unconventional. There is a small report here that's been prepared suggesting a demonstration project along the Kuskokwim, perhaps centered around Bethel, to interconnect some of the villages that are now supplied primarily by little individual

generating plants. In some cases each home has its own plant. In some of the villages there is a centralized system.

For such a project, I'm convinced that eventually a project of this kind can probably be financed by REA funds, for example. But at the moment its unique characteristics is such that REA says that, well, it isn't exactly according to our specification, our standards. I've had some nice discussions with them, for example, and I can see their engineers believe me. But there's a few hangups that relate to the uniqueness of the system and I'm suggesting that, perhaps through the use of the Permanent Fund and whoever operates it, that some of these unique solutions that may be adaptable to Alaska be given consideration that perhaps some of this fund could be used as a pilot project.

Which I'm saying again is not R & D. It may be unconventional, but I'm convinced would be feasible. You could then produce what you might call a yardstick . That word has been used in other areas to say this is a feasible project. And that means generate additional support from such as REA by saying, "Here's a project that works." This is the way it's doing. We'd like to build a lot more of it.

In the case of REA, the whole philosophy behind it--- their own program is such that, to me, it's a natural to do

this kind of thing. But it does need a little yardstick, something to get it going. Maybe the Permanent Fund, as an Alaskan fund, can help produce a yardstick program that is required for Alaskans because of the unique or unconventional nature of some of the solutions we have to deal with.

Along with this one wire scheme, it just happens also that in the Bethel region there are some interesting records regarding the wind. There is some possibility for the use of wind as power to supplement diesel generation. Because the delivery cost of the fuel, etc., are pretty high, why the cost of energy in those regions are exceedingly high. And even though wind power generation is a very high-cost scheme, basically today, some of the figures we have digested make it look as though it might be useful if it were part of an integrated system where it's not the sole source of energy, but simply used as a supplement to displace higher cost diesel fuel. So the little report suggests the possibility of adding a little wind generation to find out if that is true.

In another area of the supplying power, electrical power, to small villages, you are all acquainted with AVEC, I think most of you know about the Alaska Village Electric Co-op, which is attempting to do the job throughout Alaska, using REA money. Practically all the clients that are in use are diesel clients isolated with

the same problems that I'm talking about here. I think in some cases we can show that interconnection can help that.

But there are some other things that can be done besides the one wire line, for example, and that would be some improvements in the design of diesel electric generating equipment. Here again, there are a number of things that are available in industry. We're not talking about R & D, but we're talking about something that would be a little bit unconventional. Somebody would have to spend a little bit of money to put in the first step.

One of the areas I'm talking about is the operation of diesel electric equipment. One of the big difficulties in these isolated areas in operating the equipment in a reasonably efficient mode and with the electric load bouncing up and down over the daylight, nighttime hours, it's difficult to keep a generating unit running at an efficient load. So, conventional designs of such equipment, having been developed over the years, using the trade-off of fuel cost and other things that generated those designs by the manufacturer, have resulted in designs that are not necessarily adaptable to some of the problems we've got now resulting from high fuel costs and the very isolated nature of some of these systems. Here again, we believe, and there are other engineers who would

go along with this, I'm sure, that there are some modifications of standard generating devices that can be developed, put in a pilot project and shown to be workable. Perhaps that is something that could be done in some other ways too, but I'm using it as an example to say there are some solutions that I believe, as an engineer, are adaptable to Alaska conditions where they might not have been thought about or even useful on the basis of the trade offs in other areas. And perhaps the Alaska fund, Permanent Fund, can look with a different eye on the things that are peculiarly Alaskan in terms of some of the solutions that we need to find.

Getting away from the pilot nature or yardstick nature of projects which the first ones I talked about are, I would suggest some other areas where I believe the Permanent Fund could do some great things for communities of Alaska in energy. And that would be for the fund to participate in some manner with communities in funding for a renewable resource project such as hydroelectric development. I don't have to tell you about hydro---I know that Ernie has been pounding the table for hydroelectric in the communities of Southeastern Alaska for a long time and I'm sure that he would feel that this Permanent Fund could be a tremendous aid to the community to that area. What I'm suggesting is perhaps there is three modes of participation that might be considered.

One of them, of course, would be just a complete funding of a hydroelectric project on a loan basis, long term at appropriate interest rates, lower interest rate, loan to accomplish a hydroelectric project. Through the use of the Water Resources Revolving Fund, which has been operating for a year or two, some communities have been able to get front money to investigate such projects and get them up to the point where it's a go or no-go proposition and then they are faced, of course, with going to the bond market or looking for other sources of funding to actually accomplish the project itself.

And that's where I'm suggesting that the Permanent Fund could participate, either complete funding, perhaps partial funding, and maybe there would be other sources of money, but there would be mutual benefits in lowering interest rates, etc., if the Permanent Fund could participate with a portion of it.

And perhaps the third way would be using the Permanent Fund in a guarantee mode of some kind to guarantee a project rather than using the money directly, backing up a community in the offering of a bond with the guarantee of sorts.

Perhaps I'm influenced to some extent and been sold by the fact that I've been working with REA for a long time, the federal agency. And today they used those three modes for

working with utilities that they finance.

One is a direct loan program, in which, as you know, I'm sure they have two interest rates that are used. They have a certain amount of the money that's loaned out at 2% interest on a 35 year basis and they have some other direct loans they make at 5% interest on 35 year loans.

And they also have a participation program with other lending agencies where they loan part of the money.

And they have guarantee programs.

I'm suggesting that perhaps the Permanent Fund could look to communities for help in energy projects in a similar manner. That there may be something really worth looking at there for the use of that Permanent Fund.

To be a little more particular about renewable resource projects and what it means to Alaska, the hydroelectric development has one thing about it that is---well more than one thing, but---the thing I'm referring to, one thing about it that is quite different than other energy projects and that is that once it's built, its cost, for all practical purposes, do not escalate. And as a practical matter today, we know that almost everything else has been escalating at a pretty substantial rate and most of the economists that make any kind of forecast at all agree generally that escalation is part of the real world and is some-

thing that ought to be considered when you compare alternate projects of one kind or another.

This is one very important difference between the hydroelectric development and alternate energy, electric energy supply systems that you fuel. Because, as we all know sorely, fuel costs certainly have been escalating. And it looks like they're going to continue to escalate because of the fact that we're running out of fuel. Just for the purpose of finding more of it and developing the lesser profitable fuel resources, we know that we are looking at escalation.

On the other hand, the hydroelectric project, once it's built, the sun does the job. It's solar energy, really, and it's free. The falling water is there, it does not escalate. So that obviously there are tremendous benefits to a community when hydroelectric development can take place and displace the fuel they might otherwise have to buy at an escalating rate. And I've made some estimates over a period from now to the year 2000 and the differences are startling if you compare and if you assume some reasonable escalation rate and make a comparison. So, while the support of a project of that kind, I'm suggesting by the Permanent Fund, would be on a loan basis, you'd get your money back like any other loan, it would have a tremendous spinoff on the community itself and obviously

the state in terms of number one, electric cost to the community, number two, stretching the fossil fuel resource because it displaces what would otherwise have to be consumed in the fossil resource.

Another area that the Permanent Fund might find use, and this one is perhaps a little more way out, pardon the expression, I think it is real however and there may be some opportunities for the Permanent Fund to be used this way and that would have to do with some more major developments of energy systems in Alaska. Such as, the support, perhaps through the use of guarantees, I'm not suggesting direct loans in this case, but that it could be very influential in the feasibility of such projects. A major project such as a generation of transmission system for Central Alaska which would extend from Anchorage to Prudhoe Bay. As come of you may know, I've suggested electrification of the gas line and oil line route. I believe that it's feasible because the energy displaced by such electrification has a pretty fancy value today. And if you look at the value of the energy you displace, that would otherwise be burned in the simple transportation of the energy through Alaska, you can show that the electric isolators, that the electric generation would be feasible just from an economic point of view. And of course it would again substantially impact those fuels which---the ones I'm talking about now are oil and gas.

Now where do you get the electricity to do this? Well, there's other fossil resources such as coal. I believe that coal fired electric energy can probably be feasible to displace oil and gas. Coal at the present time---and I'm thinking about fuel is at a lower priority than gas and oil---and so it might be useful to displace that oil and gas.

Obviously, hydroelectric energy could certainly be used to do the job. It does also appear along the way, though, that the hydroelectric project that we are looking at today in this region---which in this case would be like a Susitna development---that most of that hydroelectric energy can actually be absorbed for other purposes in Alaska. It can be used by the community for their normal load growth of Anchorage and Fairbanks and the Central area. I'm suggesting that, if projects such as this catch on in any sense, that perhaps the Permanent Fund can be helpful in improving the feasibility of such a project.

A similar project could be accomplished in Southeastern Alaska. And this is one of the concepts which was talked about many, many years ago by the Forest Service when they made their little study of the water power of Southeastern Alaska. They suggested the possibility of an energy intertie throughout the whole of Southeastern Alaska through the use of sub-

marine cables in many cases because of the rugged nature of the country. And I'm saying now, that while this concept may be slightly way out, there are developments happening in Alaska which very likely may bring such a suggestion to the fore again. But because of the Alaska conditions that exist, it's going to take horsepower to make it go and that Permanent Fund is certainly---it's going to be a device that would impact projects of that nature.

And I'm simply saying that I believe those projects are likely to show feasibility as reviewed by Alaskans. We Alaskans do have some difficulty communicating with other parts of the financial world on some of the things that are unique to Alaska. And this is an area where I believe the Permanent Fund, using good judgement ---I'm not saying do anything silly---but because there will be Alaskans involved, they're probably in a better position to evaluate the kinds of things that I've been talking about in Alaska terms and arrive at a conclusion that says it's a good deal where the general financial market that we usually look to might not be able to evaluate it that same way and thereby something might go begging that really is a good project. The Permanent Fund, to me, would seem like it could perform a valuable function in supporting some of those concepts when they develop.

I guess that's about it and I'd be---I'm intending to put a little more of this in writing and perhaps you can tell me what

portions you feel at this point in your hearing would be appropriate related to the Permanent Fund. I haven't been at any of the other hearings so I don't have the benefit of that.

GRUENING: Well, thank you very much for your interesting comprehensive statement of the possibilities of Permanent Fund participation in energy development. I think we'd like very much to have your written statement. You might include in it some of the reasons REA funding isn't possible for these projects and any more specifics you have on how the financing might work.

RUTHERFORD: Yes, I have some of that and I can do that.

GRUENING: Are there questions from the committee for Mr. Rutherford?

HAUGEN: Well, I could ask a lot of questions but I think it would be a repetition of what he said.

Principally, what you're saying is that maintaining the idea that the Permanent Fund principal will remain but, if those projects could be financed on a long term, low interest basis, the state would get its money back, it would be just

the thing in the early period that---we're using hydro only as an example---the early costs are the ones that put most of us---I'm talking about Wrangell, Petersburg area---out of business if we could have that money loaned to us on a long term, low interest basis say at an early cost of 3 or 4% for the first ten years, knowing how the state fund managers in other funds operate, they want, of course, to obtain the maximum yield.

But, farther down the road, when these utilities got on their feet, they could probably have an accelerated rate of interest. They jump it from 4% to 5% and 5% to 5½% and that of course depends on the size of the project to take. My idea was to have one that had 30 or 40 years of life which, even if we ration it out on a 6% annual growth rate, the state would still get a good return on its money in the long run.

I'm not talking about any giveaway projects, I'm talking about good projects. That if they could get this foot off of the ground and the state would get its money back, we'd retain the idea of what the Permanent Fund is. It would do all kinds of things. It would save the consumer. It would maintain the interest of the consumer down the road if we're going to displace these Mickey Mouse projects we've got now with diesel power. It's just the peaking load---you're acquainted with our problem in Petersburg that throws the rate schedule out to the point that you never

get out of the woods as far as debts are---in fact the peak-
ing power costs you more than the primary power. I appreciate
the comments that you've made to the committee and it's along
the lines I've been thinking. I look forward to some more
of it.

RUTHERFORD: Well, I say again that I believe that the
Permanent Fund can perform a unique function and I know there's
lots of ideas for the use of the Permanent Fund, so whoever
manages that fund has got a problem of spreading it around
the state in a fair and best manner---for the best interests
of the whole state.

But, when you look at the communities themselves in
general and potential spinoffs, I think the energy area is
one place where the use of that fund can result in benefits
that will spread throughout most of the population of the
state. There are particular problems related to Alaskans
and now Alaska is going to have a particular fund that's
also Alaska's. And I'm just suggesting that right there we
have an opportunity to do some of the things, that we have
a little difficulty convincing the rest of the world, that
are feasible. Through the use of the Permanent Fund, I be-
lieve you can yardstick some stuff so we can get some more

money in besides. And since the Permanent Fund can perhaps be used to really generate additional spinoffs to a lot of the communities.

GRUENING: Any questions? Thank you very much.

RUTHERFORD: Thank you.

GRUENING: Our next witness is Carl Steeby.

STEEBY: Thank you, Mr. Chairman and members of the committee. Thank you for the opportunity to be here, appear here. I do not have an entire text or anything, but I would like to offer some of my thoughts to the committee on the Permanent Fund.

I have asked quite a number of people the question what's the purpose of the Permanent Fund to see what their thoughts were when this Permanent Fund was set up and, needless to say, I received numerous answers, mostly to curb legislative spending, to help all Alaskans, to have some money left when the oil runs out and a few had the same opinion I did when the Permanent Fund was set up. It was to mainly develop renewable resources from the income of non-renewable resources, whether it be oil, gas, minerals, whatever they might be.

I was at the hearings Saturday over at the Anchorage Westward and listened to Dr. Gordon and Dr. Bergman make their presentations and, really, I couldn't agree with either one of them and their thoughts on the Permanent Fund. Dr. Bergman split her ideas straight down three different ways. She had three scenarios, you may remember. One was spend it as you get it. The other was the gilt-edge investment. The third was a development fund.

I don't subscribe to any of these scenarios, per se. I subscribe more to all of them. Not necessarily spend it as you get it. Maybe spend the income that would go to the general fund for things like parks, recreation, campgrounds, pioneer roads to the attractions and so forth.

There was several mentions of the \$900 million that disappeared. I might say that, for personal reasons, I had to leave the state from 1963 to 1973. I first came to Alaska in 1942 and have been here most of the time since and in 1963 our roads were in a terrible mess. You couldn't find a campground anywhere, you couldn't find any rest areas, you had to go by the nearest tree or anything else. When I came back in '73 we had campgrounds like no other state has that I know of. They're everywhere, there's lots of them, we need more. They're crowded. But, a lot of that \$900 million did some

good. It wasn't all rat holed as Dr. Gordon said.

On the second scenario of Dr. Bergman, I believe that we should have a portion of the Permanent Fund go into gilt-edged investments. These would be long term, high interest bearing investments that would go into our general fund, the income, and reduce some of our taxes. Everybody all over the state--- the Permanent Fund is supposed to help everybody and I think that we could reduce our taxes from the income a certain percent. I'm not offering any suggestions of what percent of the Permanent Fund should be used in gilt-edged investments. I think that would be for somebody that knows a little more about economics.

Thirdly, the development scenario, which I subscribe to wholeheartedly, is long term, low interest loans or participation loans or guarantee loans as Mr. Rutherford pointed out.

And I might say that I am an engineer with Robert W. Rutherford Associates, so I---however there is no collusion. We haven't talked together or anything. We didn't even have time to prepare a text.

But these three different methods of financing projects should be considered. Again, no giveaway program---it has to be returned to the state. And in the development, I think that we should consider first our renewable resources for these funds.

The world is going hungry now for protein. We have a lot of bottom fish. Somebody is going to develop the bottom fishery.

Who is going to do it? We need more canneries. We were flying fish to British Columbia, to the lower 48. They were telling me the other day they lost a planeload of fish flying them from Yakutat to Anchorage. We need more cold storage plants. Timber Resources. A lot of the smaller communities could develop small shingle mills, veneer plants, finished lumber. Who's going to do it? Are we going to do it or are we going to let the Japanese come in here and do it---take all of our lumber, our bottom fisheries, build our canneries. Or are we going to do it ourselves?

And, another renewable resource that goes to my heart is the hydroelectric development and I would like to say right along with the hydroelectric development, fish hatcheries. You may wonder why I combine these two, but I have worked from Kotzebue to Ketchikan and this past summer I have lived in nearly every community in Southeastern Alaska from Yakutat to Metlakatla many times. And although they had an excellent fish run this year it was a very dry year in Southeastern Alaska. There were a lot of smaller streams where the salmon were dying in the mouth of the stream because there wasn't enough water to get up to spawn. And I'm wondering what it's going to be

3 or 4 years from now when those fish that would have spawned normally came back.

In Petersburg, there is a hydroelectric plant. The water from the tailrace is utilized in the state fish hatchery. If it had not been from the Petersburg hydroelectric plant, they would not have had enough water to operate the fish hatchery. Also, fry from the fish hatchery was put into streams where the salmon could not get into spawn. So, in my way of thinking, we can build hydroelectric plants and fish hatcheries at the same time and we can go Mother Nature one better. We can do a lot of things to enhance the fisheries as well as develop hydroelectric power.

At the present time in Southeastern Alaska, the average fuel costs per kilowatt hour of energy generated is running a little over 4¢ a kilowatt hour. Nearly all the smaller communities are using diesel electric, while the largest communities are using diesel because of the front-end money. It's hard for a community of, say, a thousand people to go to the market and say we would like to borrow \$8 million to build a hydroelectric plant. Well, that's kind of unreasonable for a banker to say here's a thousand people that's come in here and wants to borrow \$8 million. They're out of their, way out of their league. Personally, I start pulling my hair out when I get my electric bill and I'm paying about 2¢ a kilowatt hour for it delivered to

my home.

And these people are paying over 4¢ now just for fuel. And in 1995 they're going to be paying over 13¢ a kilowatt hour for diesel fuel. I maintain that if you can build hydroelectric plants at fuel replacement costs at the time it comes on the line, it should be built. And I would like to have the committee really dwell on this development portion of the scenarios that Dr. Bergman set forth. And I think we can use some of the income, say, from the low interest we get on our development programs or the high interest from our gilt-edged investments to even build a few amenities for Dr. Gordon, but I would say more in convention centers and that sort of thing and not opera houses and golf courses. Thank you.

GRUENING: Thank you. Were there any questions from the committee? I just have one. My brief experience with looking at hydroelectric projects, at least explained on paper, is that they are expensive. If we're talking about a \$2 billion fund and we consider all the uses that people want the fund to accomplish---like in Fairbanks it's everything from artifacts to whales, literally, yesterday.

Buy, hydro wasn't mentioned, but I know in other regions

of the state it's probably more feasible and it's popular. But, how many projects do you think the fund could get involved in and still accomplish some of the others here. You see a limitation in terms of the number of hydro projects that the fund can get involved in.

STEEBY: Yes, that's why I brought up the three different types of financing. Possibly if you had finance money, there wasn't a demand for it, you could go in and make a complete loan package for a hydroelectric development. Now, I'm talking more---the smaller outlying villages, Dillingham, Kodiak, Petersburg, Metlakatla, Hydaburg, Klawack, where ever. More so I think than I would in actual development of Sitka.

Like I was preparing the energy cost. The rail belt area along the pipeline I feel has benefited economically from the oil and gas business. This same economic enhancement in this area has made a hardship for the rest of Alaska by increasing the wages, the prices of fuel, one thing and another that people have to pay. It has done nothing to increase the price of fish or how much a cant of lumber or something like that is going to bring in. But, still they're paying the higher prices and one thing and another. It hurts them and it is more or less, I think, helps the Anchorage-Fairbanks area.

And to make it a more equitable thing, I think the fund should be spread out and not one huge hydroelectric plant for one specific area of the state, unless there is the money available. But, if you have a limited amount of money, I would say participation. Pay a project off, a small project, say in Petersburg, maybe \$8-\$10 million. Maybe you can say well, we'll loan you \$3 million; we'll guarantee \$6 million; we'll guarantee the loan. You find the money someplace else, but we'll guarantee it. And with that guarantee, they could get a whole lot lower interest rate from somebody else. I mean, it depends on how much money you have available for the different projects and it would be a matter of allotting the money throughout the state.

GRUENING: Thank you. Are there any further questions from the committee? Thank you, Mr. Steeby. Our next witness is Peter Van Dilla, if he's still here. OK, Betzi Woodman.

WOODMAN: I have mine written up because if I were to just talk, I would spend all the rest of your hearing time because of---this subject has such broad interests. I'm not an expert in investment and management things and I won't address myself to that particular of it, except to suggest

to the committee that there be an investigation of the state bank concept, that is, and the Dakota is not going to like this, but I don't know whether it's North or South Dakota, has it. I know a little bit about it. But, I do have a statement and I'll read it for you. First I'll identify myself.

My name is Betzi Woodman and my profession is writer. I first met Alaska in 1953 when my husband was assigned here with the Air Force. We extended his two-year tour because we had fallen in love with the place. After a brief hiatus in California where he decided to retire from the Air Force after 20 years service, my husband and I came back to make our home here in 1959. Since then, our three children and their children also live here so we have a broad stake in this, our adopted home. I have been involved in numerous volunteer activities over the years and, after writing for both newspapers in Anchorage, I chose at the end of 1963 to become a freelance writer, which profession I still follow. The work has taken me around the state often and brought me in contact with many people. Much of what I present here has been discussed with several of these persons who concur with my thinking.

You will be besieged by suggestions on where to invest the Permanent Fund, how to spend its income. Choosing among these suggestions will be a most demanding job and I hope that you can maintain your thoughtful approach and not succumb to impulse or sudden pressure of a particularly vocal group.

When the state received the then-unprecedented \$900 million in oil and gas lease bonuses in 1969, the last Gene Guess convened a series of seminars to get public opinion on how to use the riches. He invited a group of Alaskans from all regions and representing a broad cross section of interests in the state to meet with a faculty from the Brookings Institution. I was privileged to be an editor for the series and helped to record and summarize the final report of what the people wanted.

It was noteworthy that with one exception, everyone who came, no matter how regional his prior feelings, soon put regionalism aside and truly addressed the subject of what was best for Alaska and its people as a whole. The specifics are on record, but the overall finding showed that it did not matter how much money the state had---a lot or a little---the desires would be the same: to maintain that peculiar quality of life and to enhance it.

Brainstorming sessions revealed that defining quality of life was a bit more complicated. Each related to his or her particular experiences, attitudes and life style. Basically however, accomplishing this goal would include these things:

Protection of environmental values.

Conserve non-renewable resources.

Develop renewable resources, particularly fisheries.

Provide educational opportunities which fit the people's needs and desires.

Encourage cultural development.

Support the strong, independent character of Alaskans.

It was suggested in the discussions that Alaska could skip certain historic phases of development---such as industrial---and could find innovative approaches to economic questions, although few specific programs were presented by the faculty.

At the same time the Brookings' findings were making their impact, a new phrase was heard throughout the land: Alaskans have the last chance to do it differently, to profit from mistakes made in the South 48.

The phrase was used most often by those from the lower states as they addressed various publics on such matters as Building the Pipeline. (That's capital letters.)

Soon it will be a decade since those first "riches." How and where that money was spent is not the issue here. But attitudes of people, particularly leaders, and how they've approached the ideals are very much the issue. They, too, can be and often are greedy, shortsighted, impulsive, unwilling to consider all the options. They find it difficult to live up to their own statements of how to achieve a better society.

But perhaps this time the leadership---you, in fact--- can

help guide the people toward fulfilling lives. You will certainly be asked to help make life a little easier for Alaskans, and that, if done with wisdom, is a valid consideration. But I fervently hope that totally cutting out various taxes which support our necessary institutions and government functions will not be the way you ease their lives.

The evidence is everywhere that when people do not pay their own way, when they are unaware of costs for services, when they have no grasp of what it took to make or build something, when they put little value on the "somethings" which come with no effort and that they also lose in strength and character.

On top of that, if costs of living are reduced too greatly in Alaska, it will open the flood gates for all the freeloaders who want only to be in on the "freebies" but not to contribute to the growth and stability of the state.

And finally, I would ask that you look to ways of enhancing what we have rather than getting more or of setting up the machinery which would lead to the "more and more" syndrome.

So, with that for background, here is my specific suggestion:

Establish a percentage of the income from the Permanent

Fund to be available on an annual basis to Alaskan communities for use in connection with cultural facilities.

GRUENING: Would you say that again, please.

WOODMAN: Establish a percentage of the income from the Permanent Fund to be available on an annual basis to Alaskan communities for use in connection with cultural facilities.

A formula would be developed for communities according to population and could be weighted in a manner to be more helpful to those communities with less economic viability.

The funds would be available on application and would not require matching in kind or money. A community would have to demonstrate fiscal responsibility in use of the funds and show that a cultural facility (as defined later here) actually exists or is actively being planned.

There would be no "strings" on how the money was used for the facility. That is, the only "approval" of use would be to show that the money would be used for some aspect such as: design for a new facility or complex; contribution to actual construction of such, maintenance or programming for the facility or addition of a wing, etc.; acquisition of art works or museum material; salary for a curator or a director; assistance in re-

tiring a debt on an existing facility; furnishings for such a facility---new or to upgrade; sponsorship of a program recognized as valid for the type of facility, for example, instructor in management of such an institution, artist in residence, special performance assistance to outside group, etc. These could be specified or it could be shown what would NOT be allowed.

The facility would have to be truly representative of public interest.

To define a cultural facility: It is defined as a facility or complex which has its principal function serving the arts activities of the community through theatre, concert hall, museum, and/or gallery; with additional compatible uses such as conventions, community meetings and library services as determined by each community.

The money could be allocated through the offices of, for example, the State Council on the Arts, and its member local arts councils---always keeping in mind that the local interests get true representation. The object would not be to add another layer of government, but to safeguard allocations so that communities would indeed have local authority and the projects be valid.

The percentage of the Permanent Fund thus allocated could be invested in a separate account, thus earning and enlarging while applications were pending.

Penalties could be established for misuse of funds. An annual application date would have to be determined for such applications and grants so that the amount available could be related to requests.

There is extensive justification why this is an important consideration. A 1975 report found that 93 percent of the adult American population felt that cultural activities and facilities were important to their lives, and the growth of the arts has reflected this appreciation.

A professor interested in views on art of the average working person talked with 400 blue collar workers---maids, clerks, mechanics, bus and truck drivers, cab drivers, secretaries, hotel desk clerks, waitresses, carpenters and street laborers as they went about their daily tasks. Their opinions were written up in the study, Opinions of Working People Concerning Art. Some critics hailed it as the first "tell it like it is" audience "pulse feeler" done in a long time.

Generally, the professor said, workers interviewed believed that art is necessary to the enjoyment, fulfillment and pleasure of living. A majority also think that tax money should be used to fund artists and art projects. And this is a quote from the report. "We found that contrary to the general belief, they (man and woman on the streets) like art, enjoy it, feel it worth-

while, know much more than we (the arts world) give them credit for . . . and of course, we discovered what we should have known all along: that most of them dabble in it themselves, as Sunday painters or collectors of everything from antiques to Ming vases, and coins, stamps---that they act in neighborhood groups, sing in choruses and quartets or save their money for tickets for special performances of plays, operas, ballets--which appeals to them."

As a bartender told one interviewer: "Art brings most of us closer to what we really are and what we feel."

A similar survey done in the Anchorage borough three years ago revealed the same points of view and willingness to help support arts projects.

The preamble to the bylaws of an eleven-community Cultural Facilities Development Committee---and I believe you are aware of it through some appropriations to the Southeast Regional Arts Council, or beginnings of it, and I can tell you the names of the communities involved in this at present, are Dillingham, Naknek, Anchorage, Haines, Skagway, Juneau, Sitka, Ketchikan, Wrangell, Hoonah and Petersburg. And I'm on the executive board of that committee.

Now then, where was I? The preamble of that committee reads, "We who are involved in the arts know the importance of cultural facilities to the life of a community. We also

know how stifling the lack of such facilities can be to cultural growth. Our task will be to make the voters of the state aware of what cultural facilities can contribute to our communities. Cultural centers can become the focal point for a variety of community activities, (and can answer the question of young people--- what is there to do), providing entertainment, cultural enrichment, recreation, instruction and social opportunity for all the people in the community as well as for those who visit our villages and cities.

"Along with Alaska's rapid economic development, there is a growing awareness of Alaska's renewable human resources. Civilizations are remembered for their lasting contributions to the arts, artists and Alaska's ever-growing arts audience, these centers proposed for Alaska will contribute to such an endowment." That's the end of the preamble.

If ever there were something which would contribute to and enhance the quality of life in Alaska, participation in creative endeavors is it. And having a facility where it can happen, a situation usually beyond the capabilities of any but the wealthiest cities, would be the catalyst.

We can do it differently in Alaska and this is one exciting, beautiful way. And we do care how they do it Outside because that's where we learn, both what to do and what not to do. Thank you.

GRUENING: Thank you very much. I appreciated the philosophical bent of your statement. What we are really asking today, not the technical aspect. Someone said in Fairbanks yesterday, we can hire a mechanic to fix our car, but we don't ask the mechanic where we want to drive it. And I appreciated your point of view. Are there any questions? Bill?

MILES: Thank you, Mr. Chairman. I really appreciate your outstanding presentation. Betzi, while you were putting your presentation together, did you at any time at all wrestle with the problem of the income producing limitations under which we are restrained?

WOODMAN: Say it again, please.

MILES: Insofar as the Permanent Fund, we're somewhat limited to income producing...

GRUENING: She mentioned dedication of the income for this purpose.

WOODMAN: Yes. Not the main fund, but a specific percentage which---and I wouldn't think that it would be our

responsibility to figure out the formula when the management group is there just so it could be done. But it would go on in the community, you know, forever.

MILES: Thank you.

GRUENING: Representative Meekins.

MEEKINS: Mrs. Woodman, one of the questions that keeps coming up, and I think it's a good one, is why would a certain proposal be more appropriate or better accomplished through the use of the Permanent Fund than through the general fund or some of the other funding mechanisms available to the state?

The reason I think that's a good question is because I'm assuming that people voted for the fund in order to circumvent the normal funding mechanism which is through the general fund. And if we were to fund all of the needs that have been demonstrated or even the good ideas that have been demonstrated to us in just a couple of days of hearings, I think we'd end up with something very similar to the general fund, because there are, of course, a great many needs in the state and we try to address them through the normal budget process.

So, it's becoming clear to me that, or at least I'm starting to think that the Permanent Fund being used for activities that

are more appropriate to it than to the general fund and I'm wondering if you had any chance to think in those terms at all.

WOODMAN: I suppose I'd go in terms of what our experience has been in trying to get such things from the general fund. The demand for very basic economic related things has been so intense that it is very difficult to address to this. And it's kind of too bad always to have this one left over thing when I have a feeling that this---I've lived long enough and been experienced enough to realize that this kind of thing is more important than an awful lot of other things.

We use the phrase, as you know, that we don't live by bread alone, and we say it very glibly. But, the great deal of investigation into the internals of how people think and how they live---the young people's protests have been to discover that they really don't answer their needs. They are not the same.

I had the opportunity to gather a great deal of information from people who participated in "Cry of the Wild Ram" over the years at Kodiak. And this was an amazing thing. What it meant to individuals to be part of this. It had nothing to do with who came, who saw, who benefited as an audience. It had to do with the person relating to other

people. A sense of creativity, a sense of belonging, a sense of history of their area which they gained. And they were very emotional about it. They felt it had given a direction to their lives. And, you know, not everyone has ski boots or can afford them and not everybody wants to go down the mountain and not everybody can play in an orchestra. But in a cultural facility, there is a place for anybody who wants to be there. And the responsibility of course is on the community to generate how it's used. And in Naknek, the museum and saving of their artifacts seems to be their major need now. This might change over the years. In some of the larger urban areas, the dramatic presentations and the music presentations become more important.

But, I've taught school over the years. I've taught music and I've worked in theatre and so on. And it's my experience that over and over again it has been the saving thing to many a person because he found a place where he belongs and it's important to him. His community is the life.

MEEKINS: I think you make a very compelling argument for the need for these types of things in our lives. But, I guess, what you are saying because historically, you don't feel that it has been funded enough or quickly enough, or something, through the general fund, and since the Permanent Fund would allow us to, in essence, dedicate a certain percentage year after year and you

wouldn't have to continually make presentations and try to get them from the state since it would be a dedicated fund, that that would be a more secure way of funding it and that's the reason you look to the Permanent Fund, then?

WOODMAN: I think so, yes.

MEEKINS: Thank you.

GRUENING: Any further questions? Thank you very much.

STEEBY: I'd like to comment on the question there.

GRUENING: OK, well normally---we'll go out of order---we don't like to do that---as long as we don't get involved in a debate. Go ahead.

STEEBY: Her ideas are quite a bit like mine on using the income from the Permanent Fund for recreation facilities, campgrounds, art galleries, medical centers and things. I think we're going to have to keep our taxes up to keep all of the freeloaders from coming in and, rather than take income from the Permanent Fund and put it into the general fund to maybe reduce our taxes too low, designate some of

this money for some of the more social aspects of our living.
Rather than just having it all go into the general fund.

GRUENING: I guess your only disagreement is on opera, right?

Thank you very much. I think we have time for the last listed witness, Harold Pomeroy, and then at that point I think we'll break for lunch and then it's a free-for-all. The way we did it in Fairbanks is anyone who wanted to testify next just came up and the first one to get here got it. Everyone was very gentlemenly about it.

POMEROY: Mr. Chairman, members of the committee. I was plagued in attempting to prepare testimony because it seemed to me that I didn't have anything to say that you didn't already know and I'm not a specialist or a professional in a particular field of finance. I was uncertain as to how to proceed and be useful. I decided to take a look at your preliminary report by the House Special Committee, that it might aid you a little bit in your further deliberations. I also thought that I could be most useful, if useful at all, by proceeding from my own experiences in the field in Alaska and make reference to them. I have prepared my testimony, you have copies of it. I think it well to read through it so that if there are any questions...

The work of your committee merits high marks. It is clear that you are laying out as many pertinent facts and as much useful information as feasible. The preliminary report by your committee on the Alaska Permanent Fund is evidence of the quality of your efforts.

The report is a good start. The issues and considerations bearing on the Permanent Fund are so complex and extraordinary, however, that enough data from which to draw well-considered conclusions will tend to make any report for general distribution overly long. This is a handicap.

And I interject there that we are possessed of a great many illusions, a great many hopes and aspirations that are just that. For example, recently the urban conservatory conducted an attitudinal study in the lower end of the Kenai Peninsula and contacted more than half the families there. And, in asking about what the people would like to see developed, what they'd like to see evolved, 92% of them said the emphasis should be on agriculture. Well, agriculture started on the Kenai Peninsula in 1949 and it is negligible now. And however a person might feel emotionally about agriculture versus industrialization, for example, there is a large part of illusion there as there is in some of our other hopes and aspirations.

Such qualifications as I may have to appear before you

on the Permanent Fund come mostly from actual experiences.

My first contact with Alaska was in 1948 when I flew here from Vienna, Austria, to take a look. In addition to personal interest, there was also the purpose to do off-the-record reconnaissance for groups representing war weary Europeans looking for a fresh start by resettlement. General Kepner provided me with a C-46 to fly around the Kenai Peninsula, Matanuska Valley and Susitna area for an entire day. When I returned and talked with John Gorsuch, then president of the Chamber of Commerce, and queried others, it seemed to me the potentials for economically sound large scale settlement, and particularly with reference to an agricultural industry, would be too meager to be feasible. It looked as though importing tens of thousands or twenty thousand or thirty thousand people would be an extravagantly expensive and hazardous effort in the absence of conditions more favorable to viability. Perhaps my original interest had been stimulated a little bit by a statement by Interior Secretary Hickey's in the 1930s that Alaska's future would rest on very large scale settlements of people, that is to build up population.

I was raised in alfalfa ranching and dairying in Los Angeles County and after six wearying years in Europe during and after the Second World War, the peace of Alaska as seen in 1948 was so appealing that we homesteaded at Bear Cove on the Kenai Peninsula in 1949. We sawed lumber for fishermen around Kechemak Bay,

operated hothouses and commercial gardens. We would have enjoyed this life a little longer had there been very low interest capital investment money, but this would still not have produced enough efficiency to be commercially competitive. We saw and knew scores of once-hopeful homesteader-farmers on the Kenai Peninsula who are now gone. And I know of one viable farm on the Kenai Peninsula and there maybe a few more, but it is negligible.

In 1965 the executive director of the Tolstoy Foundation, the world-wide White Russian refugee service organization, asked for a conference on behalf of peasant Russian emigrees from Siberia who had arrived in the U.S. via China and Argentina and wanted to establish themselves on the Kenai Peninsula in a village where they could retain a simple lifestyle. We aided them, working with Roscoe Bell of the state division of lands to arrange a sale of land and leases.

The Russians were enthusiastic about agriculture and they were peasants. But we cautioned that they should be ready to do anything as agriculture might be too meager. They are now hardworking, successful fishermen. Initially they were prepared to be hardworking farmers but found the potentials just too limited.

They have been self supporting from the outset and now

have more children in their grade school than there are in the Anchor Point school. If more consumers produce prosperity, I imagine this success story is a good thing.

When the legislature ordered boroughs organized I became the first borough chairman of the Kenai Peninsula Borough. We initiated a tax program, including a tough 3% sales tax that produced as much money as the 5-mil property tax, which has been maintained every year but one since then. The purpose was to encourage industrial development by stability and a property tax about 25% of that paid outside. There was much enthusiastic talk about conditions coming right for diversified industrial development. Considerable effort and money went into economic development plans, but neither the petroleum industry nor its support activities produced conditions enhancing the potential for varied industrialization. Nothing happened. This, of course, excludes the plants established by the petroleum industry itself.

There was hopeful talk that the high-value nitrogen fertilizer urea could be a big boost to agriculture. And now, anyone can drive his truck to the plant and have it filled with bulk urea. This has not been enough to improve the agricultural outlook.

In 1972 the legislature passed the "New Cities" bill which was promoted as being a great boon to industrial development in

remote areas. The immediate stimulus was the prospective Lost River fluorite enterprise. The bill had significant subsidy implications. I assisted in drafting modifications and supported the bill before the Senate Natural Resources Committee. George Silides testified there were six more enterprises ready to go ahead on passage of the bill.

The City of Lost River was incorporated. I learned subsequently that the Canadian promoters expected the law would open the way for substantial U. S. Federal Government grants for the infrastructure required. The underlying problem however was economic feasibility---the product simply could not compete in the international market. I have heard no more of the other six just waiting to go.

Experience on the Kenai Peninsula has indicated that in periods of normal levels of activity as well as during boom peaks there is a continuing flow of newcomers who compete successfully for jobs. With negligible exceptions employers hire the persons who seem the best qualified, whether just off the plane or lifelong Alaskans.

In view of much effort to promote local hire the actual situation is of compelling interest. To try to understand better what is involved, I have been interviewing persons at random since the end of the Cook Inlet-Kenai Peninsula oil and gas development boom---hundreds of them. The persons

queried are as varied as: truckdrivers, a new clerk in a pet food store, a new face at Petrolane, men at United Building Supply, restaurant workers, persons waiting for their cars at auto service centers and many, many hitchhikers in Anchorage and on the highway between here and Homer. Core questions are: How long here, why did you come, what do you do, did you have difficulty getting work, are you staying? Not one has told me that he was disillusioned and leaving or couldn't get a job. Of course this is not a professional survey, you understand and there is a great big turnover among people in and out of Alaska, but it does appear that we simply have a constant pressure.

From experiences and observations since the organization of the Kenai Peninsula Borough following the October 1963 election, I can only conclude the proposition that economic expansion will cure unemployment is pure illusion. The pressure of newcomers just never lets up. New enterprises and increased economic activity seem to offer enough attraction to keep the pressure on.

I have puzzled over the problem endlessly. But it seems to me that whatever policy we may pursue that stimulates economic development we should do so without the expectation that it will lead us to a plateau of full employment---or even reduce unemployment to a moderate level.

Recently I had occasion to consider the economics of a mining property in connection with writing about severance tax.

The property is a substantial body of copper ore which is reasonably accessible. Development would employ 600 people, which, with dependents, would total about 1800 residents. This number would probably account for another 1800 people in service activities. On the question of the enterprise paying a property tax, the response was that this would be impossible. Neither would a severance tax be supportable.

A preliminary guess was that copper would have to be \$1.20 to \$1.25 per pound for the enterprise to break even. Copper on the world market was then between 50¢ and 60¢ per pound. Obviously the property cannot be developed until economic conditions become far more favorable. Waiving all state and local taxes couldn't buy economic feasibility, but the state would be incurring a cost of several million dollars for public services for the persons involved.

In the report you have said that "our task is to find out what Alaskans want the Fund to achieve and to recommend legislation..." This is a difficult task as it is next to impossible to comprehend all the implications of the huge oil and gas revenues. Yet this is a central reality to which we must relate our thinking about the Permanent Fund and everything else concerning the future.

If anyone believes, however, that we should spend as convenient as we go along and accumulate in the Permanent Fund

only what is left over (with the minimum of 25%) he should stop listening now. If anyone is convinced it is safe to rely on future Prudhoe Bay-size discoveries he should stop listening.

Since we began to have petroleum revenues in large quantities the people have aspired towards a variety of level of public services common in most other states. This is far costlier than personal taxes and the productivity of the economy had previously been able to support. Costs in Alaska are higher than elsewhere--- for public activities as well as for doing business and living and thus this has aggravated public expenditures. It may be some comfort to rail at the legislature and a "bureaucracy gone wild." There are of course always some inefficiencies, extravagances and poor judgements. The effect of these is insignificant in relation to the total budget. Anyone who thinks some big reform or return to "grass roots" will bring expenditures way down is deluding himself.

The upshot of the situation is that the state is disbursing close to \$1000 per person per year more than it takes in, exclusive of petroleum revenues. This is a central reality with implications hard to perceive or to accept. It makes the proposition to diversify the economy in order to broaden the tax base for the time petroleum revenues diminish an almost total delusion. There is absolutely nothing on the horizon to indicate that any prospective "diversified" enterprises will be able to do much more than

pay our currently relatively moderate taxes. In fact, the report implies the probability that use of Permanent Fund money to diversify will require benefits such as low interest rates---meaning some measure of subsidy.

Taking account of the central reality of our situation one can only conclude that effective promotion of diversification will result in an unfavorable balance sheet of costs and benefits, thus eating into resources we are committed to preserve.

The second paragraph on Page 9 of the report is an excellent statement. I would change only the second word from "may" to "will" so that it reads, "subsidies will only make sense if the loan will be supportable and the enterprise will pay for its cost." This paragraph is generally consistent with the testimony of Drs. Tussing and Daniels touched on in the first and second paragraph on Page 4.

What I have said about diversification applies equally to renewable and non-renewable resources. With respect to agriculture I suggest that the report on Matanuska Valley farming in Section B, Anchorage Times, September 4, 1977, be given close attention. It states inescapable facts, but also quotes what seems to be pure wish-thinking. Jalmar Kerttula is the source of statements about massive capital investment aid. He is quoted as saying, "In fifty years

farming and prices might no longer be marginal. It's something to plan and work for." And, "it would take five years to get a grain project really going here and overall we're talking about fifty years from now before agriculture could become an established state industry."

And I interject here, I am not against agriculture. I simply am hopeful that we will not go overboard and will not pursue a course that may be illusionary as far as its ultimate effects. And I refer to your quote in the preliminary report to agriculture as a special fund so that we can rapidly develop agriculture throughout the state. It will be a long, slow, limited process.

I had occasion to make a study on the Kenai Peninsula with respect to a proposed forage project on which the Bureau of Reclamation had spent some \$300,000 and the gas line was going to provide the heat for pelletizing the forage for the many thousands of horses and other livestock we have around here. And it was easy to find very quickly the fatal defect. It was simply that in order to be feasible from the standpoint of justifying the capital expenditure, capital investment necessary for that project, it would have had to operate 24 hours a day for something like 95 days. Well, the optimum for the production of forage, because of our adverse climate, may be only about three weeks. And that project, even if it had gone ahead and been realized with individual operators having 500 to 1500 acres of land, it would have taken

care of maybe 25 or 30 pounds, that was all.

In general, "diversification" and "renewable resources" seem to be similarly deceptive as to broadening the tax base and stabilizing the economy when oil revenues decline.

The third paragraph on Page 5 of the report states, "As oil wealth declines, the Permanent Fund may bear the responsibility of supplementing the general fund through income from fund investment, ..." I would change "may" to "will". A qualification might include words such as, "...barring some unpredictable windfall."

The first paragraph on Page 5 touches on the underlying concept of the Permanent Fund by referring to preserving the dollars into which the oil and gas wealth is being transformed. And that's one of the most sophisticated statements you have in your report. Dr. Barbara Bergman of the University of Maryland speaking on a panel on September 10th said, "The idea of the Permanent Fund is to preserve resources for future generations." Unfortunately the fast transformation of oil into dollars means a considerable wasting away of the dollars from inflation; increased price of the oil in the ground would probably offset inflation, but this is not possible. Managing the fund for high return can help preserve the value of the dollar resources.

And I note here a little bit from some of the discussion so far that I think it appropriate to say that the whole concept of the Permanent Fund is rooted in economics. And there must be a purpose of a hard-headed approach from the standpoint of economics because the idea is to take this resource that has to be gotten out fast rather than spaced over 50 or 60 years because of the economics of transporting it, is to take it and put it into a form that will save it. And it will keep it up so that it can make a permanent contribution.

There is probably no more important statement in the report than the sentence on Page 9, "If no in-state opportunities exist, the Permanent Fund cannot create them." In other words, if the requisite conditions for economic viability are not present the state can't buy them. Further, as a general proposition, if requisite conditions are present, money is available and the state need not go into the financing business separately. This of course excludes some social purpose which might be deemed worthy.

And I interject here something concerning electric power because of what has been said here. I concur in the testimony presented. I concur in what Representative Haugen has said because the development of electric power, if done of course on the basis of good sound evaluation of a project and the longevity of it, can make just very good economic sense. When we started producing

oil in Alaska, oil was about \$3 a barrel. No one thought then it would be priced at \$14.60 and no one may think that it will be priced at \$30 in twenty years. I do. I think that it won't be long before it will be \$16, \$18, \$20 and more, simply because of the pressure on world wide resources. And so, if an investment is made in a hydroelectric project as in Ernie's area, for example, and it is sound, even with a moderate rate of interest, the feature that Ernie referred to of an accelerating interest rate as time goes on would still make it very, very good sense from the standpoint of the users and from the standpoint of the investment of the fund as to overall return in the long run. You heard testimony here that per kilowatt diesel fuel now represents 4¢ per kilowatt. Well, as it goes on up it may represent 13¢ or 14¢ or 15¢ per kilowatt. And by that time electric power---those projects which are thoroughly sound---can make very, very good sense.

So that's the only point at which I make observations specifically as an object of expenditure and in that connection I would say, Russ, I'm not worried about money, that is, if I had the say of what we did with respect to the Permanent Fund, because I would save a helluva lot more than \$2 billion and hope that we do arrive at that point.

This of course, referring again, coming back to the text, referring to your statement about if no in-state opportunity exists. This, of course, excludes some social purpose which might be deemed worthy enough to have attention from the Permanent Fund. Any action in this direction should be based on a clear-cut identification of the results to be produced and the costs involved.

I have said that the petroleum revenues are a central reality to which we must relate our thinking and projections for the future. The significance is in the sheer magnitude of money, what we have done so far, and where it is taking us.

Some comparisons may help in relating, and therefore in evaluating. You know this of course, but maybe there is somebody who don't. If the state's budget is increased an average of 10% per year, the budget in less than 20 years will be \$6 billion; the 10% annual increase might be made up of 5%-6% inflation, 2.5% plus or minus population increase, the rest in services expansion. Now as to comparisons, gold production in 1976 showed a big increase over '75. If the state revenues totalled \$20 per troy ounce for gold for '76 (a ridiculously high figure, I think), this revenue would be equal to about four hours of the revenue produced by oil and gas when Prudhoe Bay production is at 1.6 million barrels per day.

Recently an exuberant state official said the 200 mile limit

provides us with such a potential bonanza in bottom fish as to overshadow gold and oil combined. A very rough estimate, based on the official's enthusiastic figures, indicates that the revenues to the state by 1990 for a year might equal about seven and one-half days of the oil revenue at peak. At the present rate of oil production from the "giant" (by outside standards) Cook Inlet-Kenai Peninsula fields, it would take 150 years to produce as much as will flow from Prudhoe Bay in about 20 years. And I note that just simply to indicate the pure magnitude of what we are dealing with.

It seems to me that the central reality is in the question: what do we really want the fund to do for us in the future and that this takes precedence over how we invest whatever money there is in the fund. I construe the size of the fund to be basic to "what do we want the fund to do for us." The people have already expressed themselves in principal. But it seems to be that we haven't made clear enough the picture as to the possible total of the abnormal oil and gas revenues---not just the revenues of which 25% must go into the Permanent Fund. Figure 1 on Page 6 of the report is a good start, but it isn't enough. I suggest there should be an expenditure chart starting in '74 or '75 and projecting on to about 1997. Of course it would have to be on an "assuming that" basis.

This should be accompanied by a similarly based chart of revenue with all the oil and gas revenues (including the pipeline tax), and the "normal" revenues, shown separately. Now this may seem like an impossibility, but I think almost anything is better than nothing so that the people can get a better picture of the whole dimension of everything with which we are dealing. It seems to me the people need to be more fully informed, if possible, in order to make value judgements on any aspect of the oil and gas revenue. More information might lead to better perception as to a basic goal for the long time future and perhaps influence a person's judgement as to "diversification" and "renewable resources" versus "investment in high yield, low risk securities", for example.

It seems to me that presently there is danger of people becoming excessively attracted by sacred cow catch phrases which are deceptive because they sound so nice. They are also deceptive because the rate of state expenditures we have reached plus exceedingly high costs, brought on by our own inflation from the sheer velocity of money, is further depressing the potential viability of many ordinary economic activities. Consider: our agricultural wages are the highest in the U.S.; the average of seven construction industry classifications, including laborer, had risen to \$15.43 an hour, excluding fringe benefits, by last January.

If people should believe it desirable to feed and nurture the Permanent Fund to maximum feasible size and productivity, the

result might be the greatest assistance that could be extended to future prospective enterprise through the simple effect of helping to hold future taxes down. Obviously, every citizen would benefit, too. In this connection the obligation to preserve the wealth, converted into dollars, necessitates enhancing it with earnings to offset its wasting away from inflation to maybe half its face value in 20 years.

GRUENING: Thank you, Harold. You have obviously devoted a great deal of time and thought to this. Are there any questions from the committee?

POMEROY: Well, I just hope that it may give you some few thoughts that will help you in your consideration. You know that I'm a member of the Growth Policy Council and we are taking some of these questions to the people in a series of Public Forum meetings. I expect to spend almost my entire time in November and the first part of December in that. I don't know how good a job we'll do. It's so difficult to get enough information into the hands of the people so that they can form good judgements without the person leading the group, actually leading them and suggesting what he thinks they ought to think. We try to avoid that. We try to do what you're trying to do---

is to gear what we have to say. And thank you for listening to me.

GRUENING: Thank you, Harold. We'll return at 1:15 and try to start at 1:15 sharp. If there is anybody here that hasn't testified, I mentioned that we did do it on a kind of free-for-all basis. But if there is somebody that couldn't testify other than right after lunch, just see me.

LUNCH BREAK

GRUENING: I want to welcome everyone back to the continuation of the hearing by the House Special Committee on the Permanent Fund.

This morning we heard from several people who have various ideas and philosophies on the Permanent Fund. We just returned from Fairbanks, a one-day hearing in Fairbanks and there was a series of suggestions by the Fairbanks people. Some of it ranged from very conservative philosophies to investment in everything from artifacts to whales.

And today, this afternoon, I am as much interested from the witnesses as to what they don't want the Permanent Fund to do as what they want it to do. As people will recall, we do have a general fund in which the greater portion of our oil wealth will be going unless we change the law as it now stands. Twenty-five

percent of that oil money of course goes in the Permanent Fund. The other 75% together with all tax revenues goes into the general fund and from that the legislature decides among all competing priorities, everything from artifacts to whales, again, as to how much of that money will be spent for what.

We have a Permanent Fund which separates that amount of money---25% of that oil revenue---from the general fund and from the legislature to appropriate. Today we'd like to hear about your philosophy, how that should be treated differently, how that should be invested and how the income should be used. And I think our first witness this afternoon is Paul Brown.

Incidentally, I'd like to introduce the rest of the committee. I'm Clark Gruening, the chairman. And sitting to the left of me is Representative Russ Meekins, to the right of me, Ernie Haugen from Petersburg, and Representative Bill Miles of Anchorage and our A.A., Mike Doogan. Did any of you gentlemen have a statement or anything you'd like to say?
OK. Paul.

BROWN: Thank you, Mr. Chairman. I would like to address the issue also of the quality of life in Alaska and some of the observations that I have having lived in the state now for nine years and some of the changes I've seen that I think

are both positive and very negative in this state. And I believe that that ties into both the Permanent Fund and the larger general fund that you spoke of. Whether or not money should be used in the general fund for particular needs within the state or the Permanent Fund, I think it's probably better decided with a great deal more planning and by people far more knowledgeable with the finances of our state government than myself.

Dealing in a particular area, and mine is the---professionally ---is the producing director of the Alaska Repertory Theatre, I am aware of the continuing and changing needs within, not only the theatre segment of the arts in our state, but in a larger sense the statewide arts needs and getting even more general than that, what I come down to call my version of the quality of life.

First of all, I think that what Mrs. Woodman testified to earlier this morning relative to the vital role that the arts are playing in the development of our state is, if anything, understated. For one reason or another, and there are many theories on the idea, the arts in Alaska are more important in this state than they seem to be almost anywhere. The study that was referred to this morning on the number of Americans who appreciate, who seem to want the arts in their lives is one conducted by the National Research Center for the Arts which is an affiliate of Lewis Harris and Associates.

It was that same firm three years ago that got this what is

called an attitudinal study under sponsorship then, partly from the National Endowment to the Arts, the Greater Anchorage Borough and the Alaska State Council on the Arts. That study, which is available, and I recommend that you take a look at it, didn't ask people how many plays and concerts they wanted. They asked the people's attitudes towards the arts. What they wanted and where they felt funding should come and if in fact those so called amenities could be available or should be available only by private contributions. In general the study found out that people in Anchorage, Alaska, at least---and unfortunately there wasn't enough money at that time to do a statewide study---seemed far more sophisticated in their understanding of what the cost of the arts were, where the arts had to be funded from and even more basic, that is the needs of the arts here in our lives. I'd like to say that maybe one of the reasons it is important in Alaska is that we don't go to the beach a great deal. I think it's partly due to our climate.

There is a program, to get specific, there is a program that has been operating now for quite some time in Canada which has dedicated funds to an arts endowment. At the time the Canadian Council on the Arts was formed, millions of dollars at that time were---created a fund which then dedicated the money to the continued growth of the arts. Essentially that

money is administered by a special committee of the National Council for the Arts in Canada and in addition to the appropriations---and this is the key to it, there was some misunderstanding at the time that the endowment created---that this should replace the annual appropriations from the states and from the provinces in Canada. But that this fund which helped to develop and to continue to fund the arts does come from the earnings from the money that has been appropriated by Canada. The income is averaging something like 7½% annually, the fund managers, because of some investments that were not as wise as they hoped they would be, are making changes and hope now that they will be able to bring that up to at least 8 1/5%. The administration costs from the Canadian Council are kept low, they are 12% of the earnings annually. It allows the arts in Canada, the various institutions, to undertake multi-year projects that are not tied to appropriated annual dollars. All grants are then made from the special committee of the Canada council.

Now, that system works in Canada and I would suspect that it might work here because it takes the administration of arts dollars away from, or at least partially away from, the year to year political fluctuations that occur in their government as of course they do in our government. The arts are not, should not be political. Apparently, too often they get political and when we have our legislature determine what is good art or what play should be

supported, then we're really attacking the very root of art, which is self-expression. And I think that every member of this committee would agree that the legislature need not determine self-expression from the people of this state.

There is a problem that exists now within the arts in this state, that is oddly enough related to at least the conventional wisdom and the rest of the country about our new found wealth. I can remember a time only three years ago when I was going in search of funding at the national level and at the national foundation level when to merely be involved in what seemed like a sound arts project way up in the frozen north would create a great deal of excitement. And there seemed to be almost a special treatment in Washington and elsewhere in private foundations in New York and Los Angeles, merely because a state that was perceived to be so backwards was interested in the development of its---of other size programs.

Just about the time that I was in Los Angeles and the day before I approached the Schubert Foundation this spring, there was a banner headline in the Los Angeles Times. That banner headline read, "Oil Companies Lose, Alaska Wins." Now the story that followed beneath that banner headline wouldn't have been a surprise to anyone. We were all following the great debate in the state as to what the new tax

revenues might be on the oil companies. But the impact that that press had---and certainly the Los Angeles Times is not the only one to blame---the national impact, rightly or wrongly, is that we have new-found wealth and that we needed to begin to look internally as to how we were going to support some of the programs that had been funded for many, many years at a federal level. What I'd like to point out to you here is that the arts are by no means an exception to the national perception that we have the wealth and we need to do more of the job ourselves. I suppose that is true and it weakens our arguments.

We have an added problem that is an old problem but it continues to be a problem. Traditionally, as many of you know, the arts in America have been funded by the wealthy, they have been funded by private foundations and corporations in a more recent time, but by people in the private sector who had the money to make up the difference between what the arts could earn and their actual cost. Alaska is a late entry into private wealth. There is, as you probably know, only one private foundation in this state that is active. It is a small foundation and has disbursements of roughly \$65 million a year for 1 programs. It does support the arts. It cannot do the job alone.

What I'm suggesting here is an idea for an endowment to the arts is certainly not for the state to take over the role of the small amount of private money that is available or the corporate

contribution which has been rather generous, particularly since at least the advent of the oil companies, but rather to increase or hold out the carrot for further private contributions to the arts. If an endowment were created by the state, it certainly could be created in a way that would encourage further private corporate donations to that endowment. I certainly don't think state money should ever replace what is available to be raised from the private sector, nor should it decrease the interest on the parts of those of us who manage the arts in the state in the potential for earning. I think it is first and primary that the arts try to earn every bit of the income that they possibly can, but that we cannot hamstring them with impossible tasks that we are now beginning to do.

There is no question that the audience exists. And to use the statistics that are quite familiar to me because I use them all the time the first session of the Alaska Repertory Theatre, the state's first professional company, drew in an audience in Anchorage alone of over 20,000 people in its very first short season. In one week's time in Fairbanks, we drew in an audience of nearly 6,000 people. Because of limited funding, as a matter of fact because of state funding, not so much by the legislature but by the administration, the statewide programs that have been envisioned in the inception

of this organization have yet to be realized.

I'm going to get away from the arts in particular and make one other suggestion that this group might look at. We have seen, and particularly in Anchorage and Fairbanks, the loss of the character of both of those towns due, at least partly, to development. I hate to admit it, and I say it sort of embarrassed when I'm outside---my friends, because my love of Alaska exists or I wouldn't be here---but Anchorage distinguishes itself as certainly one of the ugliest cities that I know of. The reasons for that are numerous. But what there was in terms of a character in this city, and I think that this is probably true certainly in Fairbanks and maybe elsewhere in our state, has been lost. We have scattered development, we've had to build quickly in order to handle this tremendous oil boom that you are now trying to decide some of how it's benefits should be spent. There is no program that I know of that it's going to encourage the small businessman. It's going to encourage the commercial side of this city to invest in what the aesthetics might be of their businesses. And I'm talking about the improvement of the exterior of buildings. Spending the extra dollar with construction costs as high as they are to take into what is not considered important because of the economics. The architectural considerations. We are probably sitting in the building in Anchorage now that distinguishes itself above all others architecturally and it certainly isn't going to win any awards

anywhere. And of course it was built by state money. Maybe the Permanent Fund needs to address itself to the changing character of Alaska cities and maybe there has to be some incentive from, again from earnings from the Permanent Fund, to encourage business and local government for that matter, to turn the urban areas of both, particularly Anchorage and Fairbanks---and I single them out because they are the only communities in this state that qualify as cities, at least by outside standards, and have more of the problems of cities---into making this a better place to live.

We no longer have the tiny little pioneer towns that they once were. We're going to build urban areas. We read reports that Fairbanks will be 70 and 80,000 people before too many years and that Anchorage will go up over a quarter of a million people pretty soon and 300,000 by 1985 or 1990. I'm interested, and many other people are interested, in what those cities are going to feel like. What are they going to look like. What are they going to be like to live in as they are in real cities. Is there some way, is my question, to turn some of the state's resources, through the Permanent Fund, into the encouragement of---so long as we're going to have cities---building cities that are far more pleasing for every Alaskan who lives in those cities or everyone who visits those cities to be in. Thank you.

GRUENING: Thank you, Paul. Any questions from the committee? I take it, Paul, that you have at this time no comment on the actual investment of the fund. Your comments relate to possible dedication of the interest or earnings in the fund.

BROWN: That's correct. I think a great deal more study would have to go on to determine specifics.

GRUENING: Thank you very much. I appreciated that. Is there anyone at this time who would like to testify?

WILSON: I wasn't really prepared to make a statement today. My name is Richard Wilson and I'm working with a citizen's group in Anchorage which is called Breakthrough and I'm one of the volunteer participants. My job happens to be the local financial resources to pay for various improvements, some of which the previous speaker referred to. I'd like to broaden my concepts into a much more Alaska-wide framework.

The first thing that strikes me when I look at Alaska is that we have a state that is going through tremendous change, rising aspirations in terms of the services the government provides, in terms of the amenities of life. Everything from electric, dependable electric, service on through to cigars. We have so many wants and the presence of a Permanent Fund is so all pervasive that the

two have got to clash or be reconciled in some way. And I think the thing that I would---my suggestion to the special committee would be on behalf of Breakthrough---and really on a statewide basis is to---not to preclude the possibility for utilizing these funds for purposes of community improvements.

I noticed in the publication that the committee put together, the green-colored publication, one of the possible strategies for use of the funds mentioned was the assistance for local capital improvements or municipal projects. One of the things that struck me is that under the possible implications column on Page 9 you find that almost all four of them, three out of four, are more or less of a downplay implication. In other words they do not really say positive things about the idea. And I think that may well be true. One of the comments was that it was not a good rate of return to the Permanent Fund to subsidize a municipal electric system, for example. Where they had no electricity previously. Other investments would bring more money back to the Permanent Fund. But in terms of the broader social purposes to which I think this fund has to address itself, this committee has to address itself. The net return to the fund can be maintained and yet you can apply some of the fund to worthy community improvements, that not be a high rate of return, but are, you know, of long run appeal kind of investment.

I would like to give an example, just along the these that was employed this morning by several speakers, the energy theme. Energy conservation wasn't mentioned. I think perhaps this is one of the fields that should be explored. For example, every community, every city borough in the state has municipal facilities. How many are begun in such a way as to conserve energy---get the maximum energy efficiency possible. Well, maybe one of the best investments that could be made is, and on which a return is possible, is to fund a refurbishing of the municipal facilities around the state. You can naturally cost out and project out the savings in energy costs over the future as fuel costs rise and you can do this in conjunction with the various demonstrations and pilot projects that are proposed by one of the earlier speakers this morning. Mr. Rutherford. such as your wind power and hydroelectric.

But, here's an example of a community improvement that may produce a long-term benefit to the citizens of this state. Economic as well as social. And I think it should be considered and not precluded by the committee. And the list of examples is endless and I won't go any further.

I think the point is that we have an existing and growing demand around the state, as Mr. Pomeroy mentioned to me over lunch. The Alaska Public Forum, various hearings around the state, produces an almost unanimous feeling that what the fund really could be useful for is funding community improvements.

Whether they be a hydroelectric facility or a library. And given this really felt need around the state, I think the legislation should be written in such a way as to be broad enough to authorize the use of a certain proportion for these purposes and I think this is a statewide need and that's about all I have.

GRUENING: Thank you, Rich. We appreciate your comments. Are there any questions from the committee? I only have one. I believe your profession is investment counselling, is it not? Or what is...

WILSON: Well, it's municipal finance and community planning and development. I'm consulting with municipalities and boroughs and hopefully with the state in certain circumstances to basically achieve a more efficient use of public funds.

GRUENING: Now, we heard from consultants who recommended against the Permanent Fund getting into bonding, purchasing bonds because the income is generally lower. Although it's tax-free, the Permanent Fund being a government institution, a public institution, will have tax free earnings anyway. It was suggested we get into some of the other areas that are higher and I'm interested in your thoughts on that and the

thought that once you start devising various ways to invest the fund that involves social implications, you, what you are doing in effect is allowing certain subsidies for certain classes of people. Then we have an accountability and an equity problem. To what extent do you feel we could solve that problem so that the most benefits get derived? Is that the thrust of your testimony? That through city or municipal improvements you reach, let's say, the division of the assets of the funds in a more equitable manner if you distribute it that way?

WILSON: I think that is one of the points I would make, yes. And I didn't make it specifically, but that is one of the major points, I feel, to consider by the committee. If you ask me what I thought the purpose of the fund were, I would answer it is to maintain a nest egg for the future. In case, for that rainy day in the future. It's constitutionally required. But the constitution does not preclude a net return to be maintained. And what I mean is every investment that is made doesn't have to be the highest rate of return. It is only the net return on all of the investments, whether they are high, medium or low, or even lost subsidies in effect. Just so that the net return is positive and you make money. That's what I think is the constitutional requirement. Given that, I think, it's only a question---and

given the fact that you have demand for services that is existing, and you as elected officials must feel it every election. We need to do this. We need to do that. We're talking about facilities, we're talking about municipal improvements. And this pressure will maintain itself and it will grow. The question is, in what form can that assistance to help those community improvements be funded take without producing a net loss.

Basically, a small proportion should be the limit. And I think that one of the things that I would propose is that the committee consider utilizing a decentralized system of decision making for those investments that aren't intended a net high return. Decentralize that part of the process and centralize the profit making part.

GRUENING: OK. Mike, do you have a question?

DOOGAN: I just want to make sure that I'm clear here. You are saying that your interpretation of the constitutional amendment will allow a certain proportion of these investments to be made regardless of whether or not they were income producing. That is, that you could make investments even though you were going to lose some money?

WILSON: No, I didn't say that. I don't think that we should go into it with the idea of losing money. That concept is---it's not the right way to say it. The word subsidy was used in place of that. And I think there is room for certain subsidies to be made within the confines of that constitutional requirement, but a very small proportion of the total investment. Out of--2% even, just to take a figure out of the air. I haven't studied that part of it. Don't hold me to a figure. But it's possible that the net return could be made even though you do subsidize certain investments. And it is---the question is which do you subsidize? And in analyzing the relative net benefits and costs of each form of subsidy is a tremendous task we have before us.

GRUENING: Thank you. Are there any other questions from the committee? Thank you very much. If there is anyone, because of time that wants to testify right now, we'll take another witness. Otherwise, we'll take a short break. If there are no further witnesses, we'll get home and get some rest before we go to Kotzebue tomorrow. We'll take a five minute break.

BREAK

GRUENING: Call the meeting of the House special committee back to order. We have a witness, Mr. Bob Posey, who would like

to give us some of his thoughts.

POSEY: Thank you, Mr. Chairman. As a long-time Alaskan, I also am quite concerned about quality of life in Alaska and this afternoon we have heard some comments about the importance of quality of life here in Alaska. One of the things that all long time Alaskan's remember, though, is that for many, many years, the only employment within the state was by the government. Everybody was either on the government payroll or worked in a service industry that provided services to those who were. I believe that any investments of this fund should take into account that we should keep Alaskan residents employed.

I notice here in your report, preliminary report here, that you published, that we talk about risk. Well, I have an answer, I think, to that question which you raised. There has always been risk in Alaska. The people who came up here in the gold rush were taking risks, there was no guarantee. The farmers who came to the Matanuska Valley were taking a risk. There was no guarantee. There are many people here in Alaska today who took a risk to come here. There were no guarantees. We have a wonderful state, we have a dynamic state and dynamic people here.

But, unless we look to the future, it's entirely possible

that our children and our grandchildren will not have jobs because it's entirely possible, in fact it is even probable, that when the oil resources are depleted, the oil companies are going to pack up and leave. They are under no obligation to stay here. And I should hope that we would have built Alaska into some type of business or industrial base to where we will have jobs for Alaskans in the future. That's all I have, thank you.

GRUENING: Thank you, Mr. Posey. Questions from the committee? Representative Meekins.

MEEKINS: Mr. Posey, I agree with your statement quite strongly. I've been concerned about exactly how is the best manner of going about that. One of the problems that we've been confronted with on this committee is that our consultants tell us that if we go on a program to increase jobs directly that, because of legal problems with limiting those jobs to Alaskans, and because the labor supply that Alaska utilizes is basically all the rest of the United States because they can move up here and they have. If you're a long-time resident, you certainly know that. Then, how it is we can give this benefit to the people that need it the most? We want to give it to the current residents of Alaska. What they're saying is that we won't have any effect on unemployment, we might increase it because of the number of people that

come up. And they may be in fact, compete successfully against residents for jobs that are in existence currently.

POSEY: There certainly is that possibility and we have a recent trans-Alaska pipeline project to look back upon. I think probably one of the answers to this is that, if we encourage Alaskan industry that, rather than use the fund to develop jobs directly or to do training directly, that there are monies available from the federal government which we receive in this state at this time for training programs. The native corporation certainly has a certain amount of money. I would hope that some of their funds would be used in developing training programs within their various regional areas.

MEEKINS: One of the suggestions we've had to get around the constitutional problem of Alaska hire provisions is that the state participate in large scale development similar to the pipeline---maybe not quite that large, but whatever large scale developments might be going on in the state. That the state participate in those at least enough to get a contractual agreement by the owners of the company that the development hire Alaskans first. And that would be in fact legal and get around the constitutional problems that we have. Would

you favor such a use of the Permanent Fund?

POSEY: Well, that's certainly a possibility. The only problem with it is that it's only a short-term solution. We are interested here in the long-term possibilities, the long-term effects of what we do today. I think one particular pet project of mine would be the state participating in hydroelectric projects because this will not only create certainly a large number of jobs during the construction phase, but having relatively available and hopefully inexpensive electric power within the state is going to encourage development of industries throughout the state, or at least throughout those areas where electric power is available. And the state is certainly going to benefit no matter who is employed ---we hope that it's going to be all Alaskans. I think certainly, probably a major percentage would be. But the state is going to benefit from the increased revenues that we have, not only in individual income tax, but the business taxes.

GRUENING: Any further questions? Mike?

DOOGAN: You sort of addressed my question in that last statement, but, if the Permanent Fund is to sponsor development which in turn can be supposed to bring up at least some additional people from outside to live in Alaska, that it in itself would create a

demand on government services that would not otherwise exist and particularly at a time when the residents of the state seem to be against spending in the public sector. Have you given this any thought? Do you think that the revenues generated through personal income tax, which for instance is relatively low and stable at this time, would pay for the services demanded by the people who came up? Or would we need to increase the level of government spending from oil resources?

POSEY: That's a good question. There's an old saying, in effect, that there is no such thing as a free lunch. I think part of our problem is that we are deluding ourselves to a certain extent in that government services cost regardless. We're going to have to pay for them. There are many places, one example is Delaware. Throughout the state, other than in their major cities, they have volunteer fire departments which bill the people on an annual basis. So, no matter what services you get, you have to pay for them. If people within the state of Alaska want the services, they're going to have to be paid for. How it's paid for is going to be up to the voters.

GRUENING: Thank you. I'd like to ask a question I think every witness may want to examine. What do you think

is the primary purpose of the Permanent Fund. Why do you think we should have one?

POSEY: Well, quite honestly, I voted against the Permanent Fund.

GRUENING: Then tell us why you think we shouldn't have had one. That might be instructive.

POSEY: I can understand, I think, the reasoning behind it and it's to help keep the money in Alaska and make some long-range benefit to Alaskans from the oil revenues so it won't just slip through our fingers as monies have done in the past. My primary concern about the program is the possibility of mismanagement. It scares me to death to think that this money can be mismanaged. I think that as long as we have the proper safeguards within this that that possibility diminishes. But this is always going to be there. When you have large amounts of money to be managed by a group of people, there is the possibility of intentional mismanagement and deliberate mismanagement, but then there is always the possibility of human error. It is going to exist.

GRUENING: As you are probably aware, the general fund now is managed by the legislature and the executive to the extent that

we make an expenditure, the legislature decides who gets it and how much and generally the governor through his staff and departments administers that money. Do you think that there is a greater potential for mismanagement there or one for the fund?

POSEY: That's a very hard question to answer. I think it's probably a toss-up at this point in time. As I said before, there are no guarantees. I think we have to, now that the decision has been made to establish the Permanent Fund, pick up the ball, as you gentlemen are doing, and run with it and do the best we can.

GRUENING: Thank you. Are there any further questions? Thank you very much Mr. Posey. I notice a few people came in the room. Ma'am, did you want to testify? Representative Osterback is here, would you like to join us? We'll be a little while longer, I think. Do you want to be in the audience? We've got fewer of those than committee members.

OSTERBACK: Do you want me to join you?

GRUENING: It's up to you. Great, we'd love to have you. Would you state your name.

WOOSTER: I'm Marjorie Wooster. I live in Anchorage. I represent a group of people who are interested in developing agriculture in Alaska.

GRUENING: I think I received a letter on wheat from you. I hope you received our reply.

WOOSTER: Yes. I received your reply. Thank you. However, it's always good to reinforce a letter. What the gentlemen was saying about looking ahead to the future we are very much in favor of. Money is money. We just can't eat it. What we hope will happen over the next 10 to 15 years is that agriculture will really be stressed.

There has been many views on how the world should feed itself and Schumaker, one of the economists, recently passed away, said that each large metropolis should have surrounding it a number of farms to feed it which would cut down on transportation and so on.

Well, Alaska is in a delicate position as far as food is concerned in the world in that we ship in most of our foodstuffs. And we would certainly like to see a change in this status in the next years. The Permanent Fund money is helping to establish and---farmers can farm, but a lot of processing marketing that gets in an area where there is a big lapse, and Permanent Fund

money can help there in just establishing those areas of processing and marketing. We feel that way. And that's part of, that's what I wanted to say.

GRUENING: Well, thank you. We had an interesting observation in Fairbanks. They were quite interested in agricultural as well and I asked one witness why she felt that present agricultural loan fund was failing, at least it appeared to be not accomplishing its objectives in terms of where agriculture is and the loans were in default. She felt that the loan program was mismanaged, that the loans were given out on a favoritism basis. And, of course, she felt that the interior wasn't getting it's share. Do you have any reflection on what we are not doing and what we are doing that seems to keep agriculture in its kind of poor stepchild kind of industry?

WOOSTER: When I grew up in the valley, there was a lot of farming going on. And last year, I talked to an Iowa farmer who was taking a trip around the valley and said there was many fields laying without being turned over. And I think the farmers are being outpriced, you know, by developers. And another thing, in my opinion, there is no cooperative area where they can---some of the potato farmers have gotten

together and made a market for potatoes, but a pea processing plant came up a few years back, folded. I have a friend who started a freezing plant up there and just ran out of funds, and I believe it has almost bankrupted him. And some of these ---a lot of it is just getting started. Once a process gets rolling and this is where the Permanent Fund could help to get the system started, then they can use the fund to put the produce into the economy.

MEEKINS: I think that is the important part you just touched on, is that---I certainly would like to encourage agriculture and we may end up doing that---but the question is, of course, if it's just, it needs a little push to get going, that the Permanent Fund could help it and then it could eventually sustain itself. Then I think it is an appropriate consideration. But, I'm wondering, as you said, so many of these things folded. Is the reason is that it is just not economic or because they just needed a little more investment money and couldn't obtain it or something?

WOOSTER: This was the case in that freezing plant, I know that. That he ran out of his own money, couldn't find financing and those freezers sat there for a long time.

MEEKINS: But you feel it could have made it if it had some sufficient backing and then sustained itself?

WOOSTER: Yes. Yes. Surely, a large freezer plant for all the vegetables in the valley and then it could be put on the market if it was time for them and so on. Holding is very necessary.

GRUENING: With, say, adequate capitalization, do you think the products of the valley would compete, let's say the massive agri-business or farms of the lower 48?

WOOSTER: I think we'd have to stimulate "Buy Alaska First". Instead of looking for---I know Totem eggs are a lot different than the eggs sent up from the states, I mean you can't compete---\$1.25 for Totem eggs and they are what, 80¢, 90¢ for the others. So naturally people buy the other ones.

GRUENING: Aren't they forced to do so, I mean the prudent homeowner or householder is going to stretch the budget as far as it'll go. I mean, "Buy Alaska" may be a couple of cents difference, but isn't there a point at which patriotism will not go?

WOOSTER: We may be forced into feeding ourselves.

GRUENING: You are saying that the transportation systems may fail?

WOOSTER: I'm saying energy altogether---there's an article in the December Reader's Digest, I'll refer to it so that I don't get anything wrong. This is a five page ad and it's bought by Americans for Energy Independence. And the title is, "The Energy Shortage Could Bring Starvation - Have you Ever Thought of That?" Well, we've been looking at this since the world food crisis back in the early 70's. And, where is Alaska fit into the scanner? We have to feed ourselves. I think it is a must. And everything is shipped in here. That's put a higher cost on everything. I think we have to. There is no doubt about it.

MILES: What percentage of Alaska's current population, can you guess, would their agri-products be?

MEEKINS: Four.

MILES: Four?

WOOSTER: Did you say four?

MEEKINS: Four percent. That's what the testimony was yesterday.

WOOSTER: Now, with stimulation, it could change, you know, to 15 or 20, I'm sure.

MEEKINS: There was some interesting testimony yesterday. It said that we had in the state at any one time only a seven day supply of food.

WOOSTER: I'm sure that's true. If you had been here during the strike, you know how delicate the situation is.

GRUENING: Mr. Osterback, I think had a question. Go ahead.

OSTERBACK: Mr. Chairman, you know, I brought up this about transportation out on the chain. It's not that many people, but I would think, they use a lot of produce. And to get produce out of Anchorage you have to pay 38¢ a pound. If you bought a sack of spuds and you want it shipped out real quick, it cost you \$38 on a 100 pounds of spuds. That's why I brought up this fairy tale. They say, why don't you order your stuff on the ferry from Seattle. It takes them

about two weeks to get up here by the time your fresh produce comes up through the chain, the food is spoiled. You'll feel a head of lettuce and know what I say. If we could get a ferry system or some kind of freight transportation from here, everybody would buy from them. The valley up here.

WOOSTER: Or establish some controlled environment agriculture. Now there has been a good experience down Soldotna way. There are some quick-growing products, but a controlled environment type of a---in a building say, you know, could help feed an area, cut down on costs, once the initial cost is spent.

MEEKINS: One other thing I'd just like to comment on is that yesterday we had a great number of people testifying in favor of---a great number compared to how many testified, only three or four probably---but in favor of agriculture and we always noted to them that there is a renewable resource development fund.

WOOSTER: We know that.

MEEKINS: OK. And I just---just for informational purposes ---because it in fact for agriculture in some respects is much more appropriate than the Permanent Fund.

WOOSTER: Now that's for growing, right? That's not for processing and marketing.

MEEKINS: Well, it depends on who you are and how you look at it.

GRUENING: Are there any further questions? Thank you very much. I notice there is one gentlemen who hasn't testified. Do you have any...? OK. Thank you.

I don't see any point in waiting for the next witness. So with that, we'll call these proceedings closed. We'll have further meetings in Anchorage. For those of you who haven't picked up a copy of this booklet, please feel free to do so.

Proceedings
of
The House Special Committee on the Permanent Fund

COMMITTEE MEETING

November 18, 1977

Anchorage

Rep. Clark Gruening, Chairman

Rep. Terry Gardiner, Vice Chairman

Rep. Ernie Haugen

Rep. Russ Meekins

Rep. Bill Miles

Rep. Leo Schaeffer

Rep. Rick Urion

GRUENING: This is the meeting of the House Special Committee on the Permanent Fund. I'd like to introduce myself, I'm Chairman Clark Gruening and sitting at the end of the table is Ernie Haugen from Petersburg. Ernie has been in the legislature a few more years than I have and sitting next to him is Leo Schaeffer from Kotzebue. That's a little bit north of here. To my immediate right is Mike Doogan who is the administrative assistant to the committee and, just walked in, is Bill Miles from Anchorage. Bill and I both represent downtown Anchorage.

We have today some people that know something about money management. The committee is now at the point where it is about to work on a draft for a piece of legislation that deals with the Alaska Permanent Fund, an institution we may call the Alaska Enterprise Investment Fund, and Renewable Resources Development Fund, which is an additional dedication of our oil revenue for a specific purpose. But there is a lot we have to learn about money management and we have essentially three groups today. One, the Hanover Trust, which is involved in kind of bank management. A gentleman from Minnesota named Mr. Blixt who represents a method of---a board that has a method of in-house or state ---public state investment of funds. And then representing

the Fidelity Management Group of Boston is Terry Magrath who is not in the room.

So, we'll just go---I think in the kind of order that we originally met you gentlemen so we'll start with the Hanover Trust people and maybe introduce yourselves again when you are speaking or testifying, use the microphone right at the end.

MCCANDLESS: Thank you, Mr. Chairman. Can I be heard standing or shall I sit?

GRUENING: It would be more comfortable sitting, I think.

MCCANDLESS: I'd like to identify myself. My name is Jake McCandless. I am vice president of Manufacturers Hanover Trust Company in New York and the purpose of my being here really is that my responsibilities include the development of new business opportunities in the public arena for our trust division.

GRUENING: Representative Osterback, would you like to join us?

MCCANDLESS: Before I introduce my colleagues from the bank, may I say first that we respect the opportunity that we have to

testify on money management before your committee. We are aware of the responsibilities that your committee shoulders as you look to the Permanent Fund and its future and, indeed, the fact that we have chosen to bring representatives from various segments of our management team, totalling at a group of four and, myself included, five, gives you some idea of the importance we place on the responsibilities that you as a committee and the citizens of Alaska shoulder when it comes to a decision on these matters.

If I may, as you face our group, from left to right. I would like to introduce our senior vice president, Mr. Willard Wheeler. Will is responsible for the employee benefit trust department in the trust division and in that department we are managing \$7½ billions of dollars in pension assets. We are using our experience in the area of pension fund management as a proxy for the investment guidelines to be established for the fund. And Will will begin our program in just a moment by describing some of the historical background on the development of these funds and how we look at the Permanent Fund in relation to the experience we have had with the pension fund.

Next to Will is Mr. Vic Melone. Vic is the senior vice president responsible for the investment philosophy, basically, of our division and his testimony before you will include our

basic investment approach, as well as the equity investment philosophy that our departments maintain.

Next to him is Harold deRopp. Skip heads our fixed income management team at the bank and has been with Manufacturers Hanover Trust Company since 1961. In his capacity as head of our fixed income team, of course, Skip has a very large group of support people that he will describe to you as he describes our approach to fixed income management.

Behind these three gentlemen, Dimitri, would you just raise your hand? Dimitri Balatsos is one of five economists in our bank's economics department and Dimitri will be talking to you during the course of his testimony about the capital and financial markets and also discuss some of the ideas we have regarding the investment of your fund.

Without further ado, then, let me introduce Will Wheeler, our senior vice president who has overall responsibility for \$7½ billion of investments. And I should point out to you that, before Will starts, our trust division is large. We are managing over \$11 billion in trust assets which makes us the sixth largest trust entity in the United States. Thank you, Mr. Chairman, and I will turn it over to Will Wheeler.

GEJENING: OK. Before Mr. Wheeler starts, we'd like to introduce Mr. Al Osterback who is the representative from Sand Point

which is considerably west of here. Thank you. If we could, none of us is an expert, if we could break in and ask for clarification in case the words get a little fancy for us. Would that fit into your presentation?

WHEELER: Sure. Please do. As Mr. McCandless has indicated, we think that perhaps there is a good deal of similarity between pension fund and your Permanent Fund. Where we find the similarity particularly is that, number one, pension funds for the most part are very large pools of money.

The second similarity, of course, relative to the Permanent Fund is that they are tax exempt as the Permanent Fund would be and therefore are invested differently than taxable pools of funds are.

And then, finally, pension funds, particularly since the recent legislation on pension funds, pension funds are not in the private domain. They are considered legally as in the public domain and those involved are responsible to the public in terms of their management and, again, we see a great deal of similarity between that and the Permanent Fund as well.

We have provided you with a booklet; I wonder if you could turn to page 4 where we have prepared a chart which tracks for the most part the historical, at least the recent

historical development, of the investment pension fund.

Now, actually, before World War II, pension funds were almost entirely insured. In other words, the concept in that point in time was that the pension to be paid over the lifetime of the employee was a fixed liability in which you promised the employee that you would pay him \$1, let's say, 25 years from now. And at that point in time you would place, let's say \$55 in an insured annuity contract and then at the end of 25 years the insurance company would pay the employee \$1.

And accordingly, almost all the assets that were funded prior to World War II in pension funds went into this kind of a single premium annuity contract, something similar to what you and I would buy as an individual. Now, after World War II, two significant things came to light in terms of pension funds viability. Number one, that in point of fact, if you were required over time as you improve people's compensation, it required over time to improve this pension benefit. In other words, the dollar that you promised really was not a significant amount of money and that you had to improve it and let's say as a result it became apparent you were going to have to pay him \$2.

Then, really a little later in time, as inflation began to become a problem and you found that not only did you have to improve his benefits, but you had to try to do something in terms of keeping him up with inflation. And typically, that had to do

with giving him an average of his final years of pay. And in many cases since then, with higher rates of inflation, this has actually resulted in increasing his benefits after he retires.

So, the liability that you thought you had that was fixed was no longer fixed. Actually it was a moving target. And accordingly, a simple, single premium-insured kind of funding was not appropriate for a moving target. Now we think this is a similar problem for the Permanent Fund in that certainly one of the things you are going to have to overcome in time is trying to offset inflation. Now inflation over the next 15 or 20 years is unpredictable. But nevertheless, I think most of us would agree that we'll have some sort of inflation over the next few years. So you can see when you refer to page 4 that the funding has switched from the insured type of funding to the non-insured type of funding. In fact, from the time period 1958 to 1975, as indicated on this chart, the insured assets grew at 413% rate, the non-insured assets of pension funding grew at a 537% rate.

If you turn to page 5, we have given you the statistic of state and local retirement funds, what we call public retirement funds and, if I may, just to digress for a minute, when we say private pension funds, we mean pension funds

established by a corporation or multi-employer, union negotiated funds. When we say public pension funds, that's just for state and local employees. And they have had, interestingly enough, they have had a significantly different history in their evolution. Now, we don't have the statistics on the insured versus non-insured as you can see on page 5 for the state and local retirement funds, but typically the state and local funds were not insured. In fact, typically when state and local pension funds were established, what they did was buy their own obligations. Their own municipal bond. Now the concept on this was, well, we'll try to save the taxpayer money by funding---using cur--- the taxpayers' funding of the pension fund to hold down---to buy our own bonds and hold down the interest rates. But this clearly was not appropriate because, as you know, state and municipal bonds are tax exempt and therefore the coupon on state and local bonds is significantly less than the taxable bonds, and if you have a pension fund which is tax exempt anyway, it's not logical to invest in a tax exempt type vehicle.

And so many of the state and local funds of course have been switching---rolling out of investments in tax exempt bonds. Do you have any questions on that up until now?

Alright, if you'll turn to page 6, we deal with---we have some historical information on what has happened in terms of the investment, the types of assets---the assets mix---used in the

non-insured portion of the assets. And again here we are dealing with private pension funds and what has occurred here, as you can see by the line, is that there has been a distinct rise in the use of corporate stock in an attempt by the funding agencies to overcome this moving target that I talked about---that the perception was the stocks would provide a higher return than bonds and therefore we would try to get as much yield for total return as we could in order to offset ever-growing inflation, and you can see on that blue line that corporate stocks has risen to approximately 60% of all of the assets invested for private pension funds. You can see, historically, back in '58 they---there was a higher investment in corporate bonds that has declined over time. Mortgages, as you can see over time, has never been a significant portion of the investments now for private pension funding. It has declined significantly.

I would only make this comment. That it's our conception that probably the use of corporate stocks for private pension funds has peaked. Now, probably over the next 10 or 15 years, you'll not see a big increase in the use of corporate stocks versus fixed income investments for private pension funds.

GRUENING: There are a lot of decreases.

WHEELER: Certainly there is a possibility for a decrease and that's a good question. The reason for that has been---is that over the last 12 years common stocks---the strategy to use common stocks has been unsatisfactory. In fact, instead of out performing corporate bonds or government bonds over the last 12 years, they have under performed bonds. Now, my only answer to that long term is that if---and this will be dealt with a little bit by Mr. Melone---but just let me give you the long term concept---is if common stock---if our type of capitalism remains in the form as it exists today in the type of pecking order in terms of balance sheet structures of corporations, that obviously the common stockholder is at the bottom of the list. And the axiom is that if you have a riskier investment you will get a higher return over time. If you do not, it would be irrational to invest in stocks. So it is our assumption that, over a long period of time, that common stocks will do better than bonds as long as the system stays in place as it is. Does that answer your question?

GRUENING: Well I see--I don't---you're not making any predictions, then?

WHEELER: Well, year by year, no. What I'm predicting is that long term, and I don't want to take too much on this because Mr. Melone is going to show you some statistics on that, long term

common stocks will do better than bonds, but they'll be more volatile. I do not think that there will be a large increase in the use of common stocks for private pension funds, nor do I think there will be a large decrease in the use of common stocks for pension funds.

On page 7, you will see that the history of the development of assets for state, local pension funds and you can see the blue line---it shows federal and state and local securities at 60% of all the assets originally invested in their own type tax exempt instruments and that has declined significantly and you can see the big rise over time in the use of corporate stocks. But you'll note that corporate stocks are only 20% of the total asset mix at this time. It would be my projection that, while there probably won't be any increase in the use of stock for private pension funds, there will be an increase in the use of stocks for public pension funds.

One other thing I just wanted to comment on was ERISA. The legal aspect of ERISA and how we see that applies judicially to this type of fund, i.e., a fund that belongs in the public domain. Now, if we make---it is unlikely that any of the type of protection---individual protection under ERISA---will apply to this type of fund because that has to do specifically with pension fund; entry, vesting, things

like that. We think it certainly unlikely that any of the funding assets of ERISA will apply to this type fund. But we think it highly likely that all the fiduciary standards set forth under ERISA will apply to this fund and---you know, over time will be tested that way.

Now, what I mean by fiduciary duties is ERISA has sent me this. It essentially says that a man---excuse me---any person involved in this type of fund is---must act as a prudent man would and I'll detail that a little bit in just a minute.

Number two is the funds must be operated exclusively for the benefit of the participants.

And three that the investments must be diversified.

Now they have not told us exactly what they mean by the investments must be diversified. In fact, we know more what it is not than what it is. But we do know they have a 10% rule. You can't invest more than 10% in any one issue. So that tells you one thing. It does not mean that you could not take a fund like this and invest it all in bonds. But what it would mean in our perception is that you couldn't invest it all in one bond and you would have to stagger your maturity and the type of bond---the problem is the type of bond you would invest in.

Now, in terms of the prudent man rule, that we now have what is called a federal prudent man rule. Before we had state and local prudent man rules. We now have a federal prudent man rule

and that's the way everybody is going to be measured as we see it. And all that really means is that you have to act responsibly with other people's money. And that's all the prudent man rule means. It's a common sense kind of rule. Now there is one new element to this prudent man rule. It says those people involved with other people's money must be familiar with the matters he acts on. Now this is a new hooker in the prudent man rule, in other words, ignorance is no defense is essentially what the law says at this point in time.

OK, given that as a background, I would like to turn it over to Vic Melone to discuss the assets as we see them and your opportunities.

GRUENING: Thank you.

MELONE: Alright, I'll talk about the investment process at Manufacturers Hanover. The system that we use to make decisions with respect to the kinds of assets we get involved with. I mentioned system. Why do we need a system? Why can't we use something like just seat-of-the-pants judgement or gut-feel or intuition or---we think that's fine and can be successful, but not running large pools of money. If you'll look briefly at the chart that is on page 7A of your

chart book, there is a table there showing the total rates of return. You got that? Page 7A. That table indicates the rates of return for different classes of assets in the period 1926 to 1976, both in nominal terms and then adjusted for the inflation that has persisted over this period of time.

I think it would be helpful if you could, as I have done here, bracket the fifth line down which is the consumer price index. The numbers above that line indicate the nominal return that has persisted for common stocks, long term corporate bonds, long term government and treasury bills in the fifty-one year period. The middle column indicates the volatility around that return as existed for those various classes and, of course, you've got a '66-'76 experience.

You'll notice first that inflation and volatility are the two items that pervade this table. Common stocks in the 51 years returned an average of 9.2%. However, the volatility around that totalled 22.4%, which meant that in 34 of the 51 years of this survey, the range of returns for common stocks went from a plus 31% to a minus 13%. So your average may be 9.2, but there was a great swing around that average. In the period the last 10 years, you'll see that the return on common stocks, the column on the far right, is sharply lower. You as treasurer...

MILFS: Wouldn't it follow that the deviation---that deviation

percentage follow in the last 10 years or would that just relate to the 50 years?

MELONE: No, the deviation refers to the 51 year period.

MILES: There would be essentially no relationship to the current 10 years?

MELONE: We didn't calculate it, but if anything I would think the deviation is at least as great. In fact, the next two tables on pages 8 and 9, if you could take a quick look at that, you'll see the light blue line on page 9, referring to the years you are talking about. You can see the light blue line which represents the return from common stocks. And the pattern from '66 to '76, particularly the last four years of that, continues to show very wide swing. Treasury bills, which are considered to be totally risk free assets, returned a 2.4% annual return which was just about the inflation rate that persisted over this 51 year period. So, if you go down to the inflation adjusted return on treasury bills, the last line, you'll see that treasury bills, when you do account for inflation, return actually nothing. Now, there is no tax affect on this table either, that may not be important here, but for individuals,

they would have paid a tax, obviously, on the return they got from the treasury bills and then also have the impact of inflation. So, their return would have been below zero. After taxes. I won't detail each of the others. I think they are self-explanatory. Typically, you've got a lower rate of return from corporates and governments which your volatility, that middle column, was considerably below what it was for common stocks.

Mr. Gruening, your question on the future, the professors who did this calculation did make an estimate of what the return for common stocks might be like after the year 2000 and the projection was that it would approximate 12.2 or 12.4%, something like that. Higher than the 9.2% experience that we have experienced in a 51 year period. The inflation rate is there, including was, I believe, 5.3%, and the volatility factor remained very high. I don't remember what the...

GRUENING: You have a lower rate of inflation...?

MELONE: Than the most recent 10 year experience, yes. Well, when you are making assumptions for a 25 year period, things have a way of smoothing out. The volatility on the inflation rate would be as wide as the volatility on the return from equities. I think what this table indicates is that it's a little more difficult to pick the right assets, particularly for the right accounts. It's

a process that requires a system, a discipline, and we think a large organization, if we are talking about large pools of money. I think the charts on pages 8 and 9 are---clearly---graphically illustrate the volatility we talked about. It's particularly the impact you get from common stocks. The chart on page 10 is just a graphic illustration, really, of the table.

So, as I said, we believe that it requires a large resource, a commitment, etc., and I'm going to just take one or two minutes and---I don't think you want to hear about our organization in great detail---but let me tell you what we do at Manufacturers Hanover and try and anticipate the problems that are presented by this record.

Our commitment began first of all by having a senior investment committee which the senior policy making committee for the investment decisions. On that are three senior vice presidents, the executive vice president in charge of the division and the heads of all major departments in the trust division. There are 10 people total. The function of that committee is primarily to determine the overall economic forecast and to make forecasts of the direction of the capital market, short and long term interest rates, and of course the stock market itself. And we try to do this in detail for a two-to-three-year period. In this case, out to the

end of 1979. We are also working with long term factors as well, within which we look for deviations for the near term.

We get help in this task by a very large organization. Being the fourth largest bank in the country you might suspect we have a large economic department. And they provide a lot of economic input, do a lot of the interpretations for us.

In the equity management side, we have three groups. The first is a group of ten portfolio managers who specialize in equity investments. Two of them deal in small capitalization companies and one other in intermediate sized companies.

We have a staff of investment analysts who are industry specialists. There are 16 of those. They cover in detail 25 industries and well over 300 companies. And within the investment research department there is a great deal of specialty as well.

The third part of this equity management group is a special support group. We carry on very precise and again highly specialized analysis, whether it be in long portfolio theory, econometric studies, economic simulations, etc. We also have a team of six equity treasurers who themselves have specializations within that organization.

The fixed income staff, which is a third contributor to the work of the senior committee, is also broken into three groups.

We have, the same way, we have a group of portfolio managers

who specialize in the fixed income area.

The second group is a specialized support group which is headed by Skip Duarte that has within it a lot of fixed income specialists dealing with arbitrated lots, cash management, etc. Skip will talk more about that later.

The third part of this group is free credit analysts who do the work that might be familiar to you from the stock security analysis standpoint. It's the same kind of work. And they prepare a proprietary bond representative list for example which is used by our portfolio managers.

The final point is that a bank of our size obviously gets a lot of attention from the investment banking community on Wall Street and around the country. So that we can tap a lot of the resources from other people and we get a lot of attention with respect to blocks of stocks or bonds that may become available, can get specialized help.

Alright, now, we believe that in the senior investment committee we have to systematically analyse a whole series of risks and opportunities presented in the economic picture. We don't believe and we have not found that it's practical to take a particular economic forecast and say this is it and spill off from that a capital market forecast which suggests that bonds are going to do "x" and equities are going to do "y" and this is the way we go. What we have chosen to

do---it's our way of doing it, we're not saying it's the only way---we think it may be the best way. If we thought there was a better way we'd be doing it. But for us it has proved effective.

For us, we developed a series of four economic scenarios and these take into account the risks and opportunities if you will that are currently being talked about in the business community. And we present these in the senior investment committee. It was discussed in great detail and then they are given a probability of occurrence. And we do this by weighing each of the scenarios on the basis of objective information, some judgement from each of the 10 members of the committee, and we wind up with a weighting that can be applied to each of these scenarios.

Now what we are trying to do is to quantify uncertainties. And it's very rare that you find that everyone will agree that scenario one or three---whatever it is---is the one that makes the most sense; it has a 100% weight. If that were the case, it would be logical for us to take the capital market forecast that comes out of that economic scenario and say with 100% degree of certainty that we should tailor all of our investments to meet that particular conclusion. To the degree, however, that other forecasts are given weights and let's say equal weights across the board, then obviously the uncertainty that's in the system is taken into account.

GRUENING: Is there a rating system to compare your performance to, let's say---Mr. Blixt is sitting over there and, as I understand it, his operation is done mostly by state employees. Is there some way that you are rated along with him as to his cost overhead relative to results?

MELONE: Well, there are a number of organizations that do that kind of performance measurement. I don't know if our bank, our trust department, is in the same weighting system as the State of Minnesota. I couldn't answer that particular question. There are plenty of people we can be compared to because a lot of firms have made a great deal of money doing this. We do it ourselves when the results are available. We are interested in knowing how well we are tracking and how we can improve our system all the time.

GRUENING: I don't think this committee or the legislature will probably get into deciding who---a lot of these technical problems, but I do think it would be good to understand what are some of the groups that do investments outside maybe the operations of government---or not under---not state employees, so that's why---essentially what I'm interested in in a broad sense as to what you are doing.

MELONE: Right. I might say I think part of your question

was that this sounds like a very expensive organization and it is. But it is spread over assets that at the moment total about \$12 billion and that helps. But it is still expensive and we make it the kind of commitment you have to make to be in this business.

GRUENING: My original question was really---is there some way you measure your cost overhead relative to the results you provide your clients? In the same way could you compare it to some of the systems that are---some states use in which they use essentially state employees, although I realize in the equity area they probably contract that out.

MELONE: I personally don't know of any measurement system that ties in the cost of the procedure itself. Since---I just don't know of anything that's done that way. Cost effectiveness in effect.

GRUENING: But your customer---I mean, he gives you some funds, whoever he may be. I assume you invest state funds as well.

WHEELER: If I could answer the question for a minute. What you can do---to cut your question two ways---one is there are

plenty of---and I am sure your consultants are aware of this
---there are plenty of information on performance put out by
all bonds, by stocks, by type of bonds, and certainly we or
they could supply you with that information. And it is
readily available and doesn't cost anything. If you wanted
to compare the expense ratio of money management under an
organization like ourselves, all you have to do is take our
fee and crank it against whatever your projected market value
would be for your fund and then relate that to whatever---
people like Mr. Blixt will tell you what it costs to run
internally. Now, I don't have information on that and I
don't know exactly how you'd get the information. You'd
have to talk to those state funds to find out exactly how
much it costs for them to run it internally. But for
example, you could use a fee ratio for us, let's say one
tenth of one percent of the market value and that would
tell you how much it would cost. And that covers all this
cost. And then relate that to whatever help you could get
in terms of other costs.

GRUENING: Alright.

MELONE: If I could ask you to just look briefly to
page 15. This will demonstrate the four scenarios that we

are currently using and they are labelled: Delayed Expansion, Extended Expansion, Recession, Stagnation. And this chart shows that the real GNP growth forecast in the---that are currently being used by a dozen prominent economic firms or economists are represented by the shaded area in that table. And this indicates how the four scenarios we are working with cover virtually all of those possibilities. The chart on the next page, which has to do with inflation, the GNP deflator, shows similarly that three of our scenarios are assuming a wider range on the inflation front than is currently described by the 12 economic firms. Speaking of economics, I would like at this time to introduce Dimitri Balatsos, who is a financial and capital market expert in the economics department at Manny Hanover, and have him describe a little bit the process in some detail. And I think you'd be interested in his comments on the current economic scene. And maybe I can come back for a minute after that.

GRUENING: Thank you. Excuse the two gentlemen. They are probably going to have to read part of the transcript to catch up on all of it, but they are also on a committee called Budget and Audit which just called for a vote. They need a quorum. They'll be back, however. Go ahead, excuse me.

BALATSOS: It's alright. Mr. Chairman, I think your question

about justification given the overhead of the operation would quite appropriately be addressed by an economist. As you know economists the last few years have a rather poor record in terms of performance. However I don't feel that in our case you have to worry too much about it. After all, we are still a very small item in the bank's budget.

In addition to that you find, interestingly enough, that despite their record, the demand for economists, if anything, has increased. Now there are reasons for that. As a nation I think we have become quite a bit more sensitive to economists and let us not forget that last year's presidential election was the economics battleground. I don't have to take too much of your time to justify my presence here. What I'm supposed to do is take a few minutes and show you an example of how at Manufacturers Hanover we use economics and economic analysis in this otherwise murky environment.

So let me then start off by putting things in perspective. I'd like to refer to page 11 of the booklet. There you will see the recovery that is currently underway that started in the beginning of 1975, the blue line lies rather appreciably below the average of the previous recovery. What this shows is that, despite massive fiscal and monetary stimulation, our economic system has not performed---has not rebounded from the depths of the recession as rapidly as it did in the past.

Another way of looking at that is by comparing what we were actually doing economically today with what potentially our system could produce. There are many other paradoxes of this ongoing recovery that to a large extent explains why economic records have been so poor in the last few years. I'd like to refer you to the consumer pattern of spending. There you find tremendous strength in housing, in automobiles, other types of spending have failed to catch on. They're all going expansion. The same thing is true particularly with the business sector. I refer you to the table on page 12.

There you will see that with the ongoing recovery business outlays in real terms through fixed investments have fallen appreciably below the path of previous recoveries. Let's look at the employment-unemployment situation. For the last two and a half years, our economy has registered record gains in employment. And yet the level of unemployment continues to be severely high. Let's look at another example. What's happened to interest rates, the price of credit? Referring to page 13. There you will see the yield or the interest rates for short term commercial paper. As you can see in previous recoveries, there was an appreciable increase in money market rates as reflected by the commercial paper rate. This time around---depending---we had an overall decline until the last few months when the commercial paper rates started going up again. Also, let's look at the loans of

interest rates.

HAUGEN: Let me ask you a question.

BALATSOS: Yes, sir.

HAUGEN: When you talk about that commercial paper. Is that that short term for inventory and things of that nature that you are talking about?

BALATSOS: That's correct. The commercial paper used by companies to fund short term working type capital requirements. Let's look on page 14. There you see the course of long term interest rates as reflected by AA utility bonds, long term. Again the same path---overall declines this time around instead of the increases. Also, quite significant is the fact that three years into the recovery course if anything our deficit in the federal budget is expanding, it is not shrinking. And I'm referring to the expanded debts as projected for 1978 fiscal year.

Now what I want to emphasize then is that the nature or the structure of our economic system is changed and has changed in a rather fundamental way. And for the purpose of these hearings today I can only refer very briefly to two or three

underlying causes. The first one is the rate of inflation. This is something that economists have a great deal of difficulty coming to grips with. And by very, very contemporary standards, meaning the last two or three years, the rate of inflation today, roughly about 5 to 6 percent is appreciably below the 12+% we had in '74. Yet, when you compute it with the kind of inflation we had in previous recoveries, this is about three times higher. And inflation is a problem because it destroys the stability of the relationships between let's say income and spending and all these other economic variables that economists count on.

Part of this inflation package, if you wish, is of course the leaping energy cost. To put it very briefly, the system is still trying to adjust to steeply higher energy costs, something that was not the case in previous recoveries. There is another thing, too, that economists use, let me brush over very quickly, and this is a poor rate, poor state rather, of liquidity and the extended use of debt. To put it differently, in order to produce a unit of output today, our system consumes a great deal more debt. And this is a crucial aspect because it raises the question and it raises the requirement of very careful financial market analysis. Analysis of corporate balance sheets, analysis of consumer's finances and so on and so forth.

Again, I want to take you then through some of the ways that we incorporate in the bank, simply the emphasis that has been placed on financial market analyses and use those inputs on investment decision processes. So, as Mr. Melone, my associate, indicated, the whole process is basically a two step approach. This investment committee ascribed or puts or places odds to three or four alternative economic scenarios. This way, we get a handle on the risk factor, the uncertainty factor, then using the most probable scenario, we try to implement our investment decision.

Let me refer you to page 14A. There we have laid out for you four alternative economic forecasts. I realize that this is not an economic forecast session. I just want to very briefly touch on the two extremes, the so-called extended expansion to which we ascribe a 49, almost 50% probability, the first column. And then the other extreme is the recession which, as you can see, is a 34% chance.

I don't have to again give you all the justifications why we put a 49% probability that the ongoing recovery will stretch through 1978. You hear a lot of talk about the fact that the economy---that the recovery is already three years old. It seems the average expansion of the post war period lasted about three years. There is a rising group of economists that says another recession is just around the corner. Well, the answer to that is that economic recoveries do not

die of old age. They usually fall victims to imbalances. So after we've done our homework we discover that there are no excesses on the horizon, no excesses on the outside, any significant excess. We don't have a kind of bottleneck, a kind of instability and so on that we had back in 1973. So, I think you can make a strong case, 50% chance that the recovery will stay here so long as those excesses on the outside particularly do not materialize.

To go to the other extreme and look about recession again very briefly, we have given a rather high probability to that outcome because of two basic downside risks. The first one, again you don't hear much about that, is our growing deficit in our balance of payments. Roughly \$30 billion will be paid out to foreign countries this year. And although all the imports we bring in show up as goods and services consumed by our system, the wages and salaries that go to support that kind of consumption at a loss to subsidize to the foreigners.

Another basic downside risk is the chart I showed you earlier, the very sluggish performance of business investment. Unless we see some steam build up in that particular category next year, I think we will have a recession later on in 1978.

And there then we list the five or six key variables in that determine investment performance starting with the GNP, the Gross National Product, on down, pressures on the inflation front in

terms of unit label cost, corporate profits which are the lifeline of dividend payments, and then of course interest rates which determine the mix between bonds and stocks. Unless you have any questions, I would like to return the microphone back to Mr. Melone to take you a little bit more carefully about the investment decision process.

HAUGEN: Let me ask one question. On corporate profits, do you feel that minus ten there, does that mean that corporate profits are dropping? Is that what that means?

BALATSOS: If we have a recession in 1978 and '79, you can see that by '79 corporate profits will be declining 10% or will decline in the year of 10%.

HAUGEN: Can you give a reason for showing that figure? What is your analysis of it?

BALATSOS: Well, the analysis starts with sales, what kind of sales we expect in 1979, which you see a decline in sales; obviously in the face of rising costs, it's going to bring about declining profits. Profits in the case is nothing more than sales minus costs. If sales come down and costs keep rising, you are bound to see some squeeze in profits.

That's why we have the 10% in 1979. Across the board if you go for scenario three and four. There is usually a slow down in corporate profits as the business cycle matures and the expansion continues because what you are doing in effect is spread your sales volume over a relatively higher cost factor here. A slower growth in your sales is spread over a higher volume of cost. And that's why the slowdown in profits is inevitable in every economic expansion, but it turns into a decline if your sales volume drops as well.

GRUENING: I'm sympathetic with a client who told me one time he wanted to see a one-armed attorney and I can appreciate--- I'd like to see a one-armed economist who is not on the other hand...

BALATSOS: Mr. Chairman, this has been a serious session. I have some anecdotes because I like to do things in perspective for the use of anecdotes, but I think I'm going to skip them...

GRUENING: Thank you.

MELONE: There are several pages of descriptions of economists somewhat like the one you just made.

Let me just summarize again the use of this weighted forecast. It is first of all to describe the uncertainties that exist

in the minds of professional investors, investors and economists and to somehow quantify that uncertainty so that it has an impact on our capital market forecast. The second thing is that it gives our portfolio managers an opportunity to assess whether the outlook that we are looking for not only is the most probable outlook but across the span of these four forecasts, whether the eventualities of that have already been discounted in the marketplace.

You know, very often things will happen exactly as you expect, yet nothing will happen to stock prices or bond prices. Or on the other hand stock prices or bond prices will do something entirely inconsistent with the facts as they seem to be presented. And what we've tried to do here is to take that into account and realize that the opportunities of catching the single best set of circumstances, or the single most accurate are very remote. And we're trying to understand the uncertainties in the world and quantify it in our decision making process.

If you will look for a moment at table 14A, you can understand a little bit how this is used. For example, under the first scenario under 1978, the S & P 400 index would range from 102 to 132---it is currently about 102. If scenario two, delayed expansion, which is the most favorable in effect, were to have a hundred degree of certainty or probability,

the range would be 118 to 152. And then you have the two recession oriented scenarios and here you see that the range from the low end drops to 85 and 86.

The chart on page 17, I'm sorry, page 18, shows in graphic terms where each of the scenarios would lead you in terms of the 1978 stock market. The shading indicates the range that comes out of the weighted scenario. The blue line, extended expansion, which is the most probable, is leading to a midpoint in effect. Now the band around it shows what the weighting of the other three probabilities does to the capital market forecast that would ordinarily spill out of this. And you can see through the shading that it is skewed downward because of the weighting that our portfolio managers and the senior policy committee have given to the recession possibilities.

OK, let me just take another minute or two to talk to you about the equity side. All of these disciplines and overview procedures are really preambles to get us to decision making processes---the selection of stocks or bonds. I mention that we have a very large and effective research department covering about 25 industries. These analyses are given our most probable forecast and working through that and understanding the relationships of various parts of the economy to the industries that they follow, they attempt to develop earnings and dividend forecasts. We have found that---and they use a lot of tools for this,

the usual analytical tools, balance sheet and income statement analysis, study of unit growth, price growth, competition and they talk to the management, they talk to experts in many fields. What we are looking at here is to get the best estimate we can of corporate earnings and dividends. Now we have found and studies have shown that the tracking of earnings growth and dividends growth is the best determinant of future stock prices. We've got three charts and I'm afraid I've got three or four more to show you.

On page 19 you see a chart depicting the growth and earnings per share---the red line, and the growth and dividends per share. Earnings here are compounding at 4.4% over the 51 year period and dividends at just about 4%.

GRUENING: Wait a minute. The red line is what, now?

MELONE: Earnings per share, using the S & P index as a proxy for stocks. So that there is a parallel growth in earnings and dividends.

The second chart...

GRUENING: Earnings includes the appreciation of stocks?

MELONE: No, that would be the appreciation of costs,

so that would come out first.

GRUENING: What's the difference between the earnings and dividends?

MELONE: Earnings per share, the profitability of the company.

GRUENING: Oh, OK.

MELONE: The next chart on page 20 shows the relationship between dividends and stock prices. You will see here that in the period stock prices generally track the rather short moves we've had in dividends, so there seems to be a relationship between the two except when you come to 1971. And you see there that dividends, at least in nominal terms, continued to go up but the market has come down over that period of time. This chart does smooth some of the wiggles a little bit.

GRUENING: It's about time the state took a bath.

MELONE: There were a lot of people in the tub at that time.

GRUENING: I think there is somewhat of a bias up here because...

HAUGEN: A year later though they kind of hung on there, could have come out a little bit better, you know.

GRUENING: Sure.

MELONE: Well, that's why I say this smooths a lot of the pattern. There were very wide swings in the period after 1970. You did get a lot back and you gave a lot away again in the '74 period and it came back sharply in '75.

HAUGEN: Well, I think the reason for that was that the people got excited from the political point and jumped on the fund manager and he started to unload, you know. Some of it they should have unloaded ahead if we wanted the top half of it back, you know. Anybody can do that.

GRUENING: Plus they had a cash flow problem, they had to liquidate.

HAUGEN: Well, I want to talk about it a little later.

MELONE: Well, I don't have to mention what happened to the price of oil and in Anchorage I am sure you are aware of that. That did influence things quite a bit.

But the next chart is the one on page 21. I think at

least partially explains that anomaly of dividends going up with the stock market going down. You can see that if you adjusted the dividends for inflation they actually turned down in 1966 and at least partially this would be a reason for the market not performing as well as it had in the past. This is investor perception that they were not getting in real terms the kind of dividend returns they were expected to or needed to stay in the stock market.

Now in addition to this kind of work where we track the dividends and earnings carefully and in real terms, we rank the industries that we follow in the chart which shows the top 12 and the bottom 12. Here we are talking about the increase in corporate profits year to year. We have found that it makes sense for us to concentrate our holdings in those industries and companies which rank in the top quartile. At the same time the system gives us an opportunity to introduce a selling discipline. You don't hear a lot about this generally. But in the same way that it makes sense to concentrate your stock in the top third of this ranking by industry and by company, we found that we ask questions of our analysts and our portfolio managers as to why we continue to own companies that are continuing to show up in the bottom third of this ranking. It is not an automatic system. If the portfolio manager or the analyst doesn't have a good reason for holding that stock or holding it in that amount, the senior policy committee will then take an issue with it and either reduce or eliminate those

stocks. So it is asking the proper question is the important thing that comes out.

Finally, one more chart, the last one by me, page 22, the product of all of this system and all of the special talents that are in the division has produced and is aimed at producing an equity portfolio which can graphically be described as you see on page 22. The green bar represents the portfolio and the black bar represents the S & P 400 so that we can and have---this is an existing portfolio---put together a portfolio where the stocks in that portfolio show an historic growth over the past five years of 17.9% compared to the market of 12.2%. And more important, an estimated future growth rate---the next bar---that's about 50% higher than for the market itself.

GRUENING: What's the period of time that this thing is covered? Covering?

MELONE: What?

GRUENING: What's the period of time that this graph is covering?

MELONE: It's a five year historic where it's indicated

and five year future.

GRUENING: From what...

MELONE: This is an existing portfolio as of September 30th, the last time it was calculated---this is not a performance, this is a graphic description of the security, the actual stock in the portfolio. Taking into account and weighting each security.

GRUENING: This is your total stock portfolio, of just one...

MELONE: This is a portfolio, but it is a representative portfolio or a group trust which is a representative portfolio of all our trust programs in fact.

GRUENING: And that was from what, this year five years back. This is a five year period and a selected portfolio?

MELONE: This is really, if you will, a snapshot of what the stocks in that portfolio look like with these characteristics at the moment. OK?

GRUENING: OK.

MELONE: It's not a trend or a movement or a performance.

It's just the---certain financial or growth characteristics of the company itself. So, moving further down you see the historic dividend growth has been twice as high in stocks that we own in this portfolio compared to the S & P. And the estimated growth in dividends is 9.9% versus 6%. So it's 66% gain. There are two profitability or qualitative ratios here as well. The five year return on capital is 30% higher than it is for the S & P. And debt as a percentage of total capital, the final column, shows that these companies are considerably more liquid in their balance sheets than are stocks in general.

The next to the last column, the estimated PE shows that despite the higher growth, the higher dividend and the stronger qualitative aspects of the stocks in this portfolio, that the multiple that were paying for those stocks is 10 times versus 8.1 at the moment for the S & P 400 which is not, in our opinion, a very big risk.

OK, if there are no questions, I'd like to get to Skip deRopp who is our senior man in the fixed income area in charge of the special support group for fixed income and I'd like to say the architect of one of the best bond records in the institutional field today. Skip.

GRUENING: OK. We've kind of advised our three main

witnesses today that we are trying to keep everyone down to an hour and that's exclusive of questions. So, go ahead. We're approaching your hour.

DEROPP: Well, I'll give you a quick 1-2-3. I'll be as quick as I can. The central philosophy for managing fixed income portfolios at least is to try to preserve capital and maximize total return---I'll explain what I mean by that in a minute. And also to the extent possible preserve purchasing power through active management techniques. Total return is the concept of investment return which is not only cash in hand but also price change---we apply this to bonds as well as stocks.

The number of active management techniques to achieve this management bond portfolio---and I'll just touch on those in a moment. But there are two realities a manager of a fixed income portfolio has to keep in mind in facing his task. And one is the profound important, interest rates fluctuate. If you turn to the chart on page 23 which shows historically yields of new AA industrial bonds 1969 to 1976 and almost every year there has been a fluctuation of yields of interest rates of 100 basis points or more. So this is of utmost importance in terms of timing, the committing of new cash or else in lengthening and shortening of maturity.

The chart, table on page 23A, shows that the impact on the

total return of a bond given 100 basis point change in interest rates, 100 basis points is the same as one full percentage point, like from 7% to 8%. It is a function of maturity. In other words, the longer the maturity of a bond, the greater the impact a change in interest rates has on the price of that bond. And what we have in effect done here is net the coupon income with the price changes, so that's the total return. So 100 basis points change increase, bond price will decline. Of an increase in rates for a 5 year bond, the total return would be 4.8% for a 20 year bond, the total rate of return would be a negative 1%. In other words the price change decline of the bond would exceed the coupon income that was received.

Now a second reality in the marketplace is the fact that there are changes in credit ratings of corporate securities and we have plotted here very briefly the number of upgrades and downgrades that Moody's assigned to industrial and utility issues. You can see that during the recessionary period of '73 to '75, for the number of downgrades increased markedly, reflecting a deterioration of credit conditions and substantial increased use of debt as corporations found it necessary to do so in a highly inflationary environment as business slowed down. The situation improved somewhat in '76.

The table on page 25 shows just some elements here of the principal involved in active management techniques and basically this involves positioning the portfolio: anticipation of interest rate changes by varying maturity, by varying quality, and by varying representation in certain sectors of the bond market, for example, industrial bonds, utility bonds, government bonds, finance obligations, etc.

The second important technique here is arbitral swapping: exchanging one bond for another bond, otherwise quite similar, in order to gain an incremental return and these opportunities are made available in the marketplace as a result of aberrations and peculiarities incurred in temporary supply and balances, the dealer having been caught on the wrong side of the market in a short position and wants to cover, technical factors of that sort.

The last thing is the element here is avoiding losses resulting from credit deterioration. We go to a chart on page 26. It shows long term interest rates, intermediate term interest rates and short term interest rates. What the pattern has been since 1970 and, again emphasizing the fact that it is very important to pay attention to---to try to anticipate---changes that occur in interest rates in the position of the portfolio properly.

The chart on page 27 is a relative chart. It shows the yield of AAA, AA, A, and BAA industrial bonds compared to governments, the spread. In other words the latest figure would show that the

top line, which is a sort of purple red, looks like it is about 75 or 80 basis points higher yield than the treasury obligations.

GRUENING: Where are you?

DEROPP: I'm sorry, am I going too fast?

GRUENING: No, I just---incidentally, the \$11 million or so that the Permanent Fund has accumulated is invested largely in treasury bills as the commissioner of revenue was telling us between 6 3/4, I would guess. That's what he claims. So what does this red line represent?

DEROPP: The red line represents our forecast of where we think 90-day bills are going. It must not be shorter maturity bills you are apparently investing in.

GRUENING: They must be longer. OK. So the longer term treasury bills would---would would 6 3/4 usually be?

DEROPP: Well, close to a year on this kind of basis.

HAUGEN: I don't think they fiddle around with 90-day

bills in government management, do you?

DEROPP: Sure we do, occasionally. Certain types of accounts...

GRUENING: The point is, was the 90-day treasury bill possible?

DEROPP: This is really just a proxy for short rates. I mean, that's just one indicator for short term interest rates--- we happened to select 90 days. We could have selected commercial paper.

GRUENING: Oh, I see. OK. I didn't know the purpose of the graph.

DEROPP: Well, just to show you how the---the relationship between short rates and long rates, how they could change. When you have periods of very tight money as in '74 and '75, why short rates can actually exceed long rates. And then when you get a restorational equity of assessment then short rates normally back away from long rates. And this is what you would expect. In other words, the longer maturity of the investment you make, the more you should expect to be compensated, the greater the risk

you take. Not only in terms of money market, in fact, but also in terms of credit deterioration if you are investing in the corporate circle.

GRUENING: What was the reason in '73 that we had that what looks like an unusual swing?

DEROPP: In short rates?

GRUENING: Yeah. Between '72 and---well, actually maintained late into '73 before the short term started to...

DEROPP: Well, that's actually---yeah---in '73. Well, we had as you recall, we had a commodity---a world-wide commodity inflation and...

GRUENING: Is this the result of oil prices, essentially?

DEROPP: Yeah, it started---got it away before that and that certainly aggravated it. The corporations were concerned that they would not have enough raw materials in many cases to be able to fill their orders, so they started buying and trying to buy in advance. This increased the working capital requirements, therefore they had to borrow more money and

this placed pressure on the short term credit market. The monetary authorities were trying also to contain the thing, the vigorousness of industrial activity.

HAUGEN: They also have to take into consideration the federal government, the federal reserve bank. The national fund deficit. Doesn't that play an important picture in...

DEROPP: Yeah, well, that really came later when we had a magnitude of...

HAUGEN: You have two competing for the money---that...

DEROPP: That's a very important consideration. Any more questions on that?

The table on page 27 is a relative chart. It shows a yield spread between AAA, AA, A, and BAA industrial bonds. Different sectors in the bond market against government bonds. The government bonds are the base credit market for the whole system. That's suppose to be the best credit in the system---you measure other things off of that. At the present time, the BAA industrials, which is a sort of purple line at the top---we're starting about 80 basis points off of long governments. And if you go back to 1974, why there were as wide as 235 basis points---I'm sorry, as

wide as 325 or 330 basis points off long governments.

The point is that when you have very tight credit conditions and you have a lot of other factors going on there at the same time---concern about England and the possibility of a credit collapse occurring, investors got very nervous and insisted on highest quality obligations and also---they also wanted it quick---short term obligations. So, the spread actually---the point of this chart is to show how the spread widened between AAA industrials, which is the light blue line on the bottom and BAA industrials which is the sort of purplish line. And that was about 235 basis points at its widest during the period and essentially it has since narrowed down to about 55 basis points. So that demonstrates quality shares and how they change.

The next chart on page 28 shows the yield spreads really between some different sectors of the bond market, not only governments but also industrials and AAA utilities. And if you look at '70 and the point of extremes, particularly on interest rates, why investors still would rather own government bonds because of the risks perceived to exist than even AAA utilities so that there is 150 basis points spread between long governments and AAA utilities. As credit conditions improve and liquidity came back into the system from the extreme pressures that existed in '74, why that spread narrowed down. Also, investors would with cash looking for yield increasingly

---put their money into higher yielding obligations as equilibrium returned and the risks were abating. AA industrials followed pretty much the same pattern in relation to governments as AAA utilities.

Don't forget that in an economic cycle and this past cycle we had was a very deep one, one of the deepest, well two deepest, but not the deepest, in the post war period. The earnings of industrial companies, many of them were very cyclic. And particularly highly leveraged ones, so there's more concern, there has to be more concern arise in a period of general credit concern and for obligations in many industrial companies we have had.

Now in connection with credit evaluation, it is very important as an investment organization that you have the ability--- the capability of monitoring along a substantial list of credits. And to be sure that you are not holding in a portfolio any credit that may encounter severe problems. We develop a computerized ratio ranking system for monitoring the credit we follow. We divided---determined that there were eight financial ratios which portray the profitability, the basic profitability of the company. Do you go with that company and incur additional debt and the asset protection of the bond holder? These actual projected ratios are listed there on the left hand corner of the page. We computed the ratio---each ratio for each of the companies---600-odd companies that we follow. And we ranked them in the deciles. So if there

are 500 companies, why obviously a company who has the highest ratio will rank in the first decile, etc.; they are ranked in that order. And then simply by adding up the decile ranking which is the number that appears here on the page, you can decide company "A", for example---the first ratio it appears in the 8th decile, in other words will down the list---ranks pretty well. You add up all those decile rankings for each of the financial ratios and the total score of 54 gives it all down to one number the overall financial standing of that company. And we rate that---that would rate down on company "A", for example, 54.

We compare the latest years of financial ranking with the three year average, which is useful to do so, (a) to determine a trend and (b) to see in case of a cyclical company to try to normalize it. We can compare the total score of each company with a score for its industry to see how it ranks within its industry and also how each industry ranks--- how the industries rank with other industries and how the--- an individual company compares with other comparably rated companies by the public rating agencies. In other words, is that score high or low compared to the ratings that apply or the score achieved or comparably rated companies by a standard score as Moody's.

And the summary of those scores appears in the two right

hand columns---how it ranks with other "A" rated companies, how the industry ranks, we also attempt to look out ahead and our analysts---credit analysts---try to give us an indication here of whether they view the companies overall financial position as either improving, declining or remaining unchanged. So this is a pretty central part of fixed income management. You've got to make your own decisions with ranking credit.

MCCANDLESS: Skip, I'd skip to the last chart.

DEROPP: Alright. We have on page 31---it's a very brief form---make up a profile of a suggested portfolio in very general terms that oversimplifies what is really involved in coming up with a portfolio. We did this pretty blind. We don't have enough detailed information on how much accumulated funds there are, how they are now invested and we don't have the data on the cash flow or financial investment data. In making up this portfolio, we wouldn't want to rule out the possible use of common stocks. But based on the limited information we have, it seemed like this kind of portfolio profile made sense.

As you can see here, we have 50% of it in Government National Mortgage Association mortgage backed securities which are backed with the full faith and credit of the United States. Another 40% of the portfolio is AAA industrial securities and finance securities

and 10% in the AA companies. We think the quality spread now as indicated in the previous charts is sufficient to indicate that you are not being compensated sufficiently to take the additional risks involved in, you know, buying lower rate securities.

At this point we just want to leave this with you based upon very...

GRUENING: The commissioner of revenue just walked in. Just as I had a question you could answer. Sterling, the mortgages that we put in the pension fund are invested in--- like the state employee's pension funds---are they Government National Mortgage Association backed, or what...?

GALLAGHER: No, they are private mortgage insurance backed mostly. Either that or the bank participates.

GRUENING: OK.

DEROPP: Well, these are readily marketable rates in a very closed and very tight market. The market building factor here is a lot higher than...

GRUENING: We'd like you to join us, John. We're going

to take a break here. I want to thank you very much and we may have questions of you later. We'll take a pause for the cause and we'll hear from Mr. Blixt after that.

MCCANDLESS: Mr. Chairman. May I point out that we have the booklet that basically we have developed with this group available and we'll give each of you a copy of that which says verbally what we've been saying here or...

GRUENING: Thank you very much. I hope you can stay. I'm sure the other gentlemen may have some questions then. We'll just take a break now.

BREAK

GRUENING: Call the meeting to order. We have at the end of the table Mr. Robert Blixt, the executive secretary of the Minnesota State Board of Investment. The new people that have come in, Bob, are the Speaker of the House, Hugh Malone, and you've been talking with the Commissioner of Revenue Sterling Gallagher and Jim Rhode who is sitting right to your left there is an assistant to the Finance Chairman Steve Cooper. So, the floor and the microphone is yours.

BLIXT: Thank you very much. It is an honor to be here, but I must say I don't know exactly why I'm here. I certainly have nothing to sell. But on the other hand, it's good to be here. And I hope that we will be able to tell you a little bit about what we are doing and I hope it interests you. And maybe a different aspect of the situation to look at.

First I want to say that I recognize most of the people behind me and they are the financial leaders of the nation. I don't pretend to compete with them. I operate out of a little set of offices like this except we have sort of plywood board with paper on top of it that looks like wood. And the rugs aren't as thick as this. And still I feel that we can do a better job within the state than these folks can in New York because they are at my beck and call too. They are here all the time.

Now you just told me, for example, sir, that you don't have a college education--you played football. Why don't you call Washington and get a real politician here in the legislature? If you're too young to run the legislature, why don't you call somebody in Washington and say, now we'll handle things just fine. I'm sure you aren't as versed in government as the speaker of the house he gets in Washington, but what I say is baloney, isn't it? Because all of the time

you have to talk to the people of Alaska about Alaska. About their money. And you folks get advice all the time and say the best thing to do is turn on Wall Street and buy stocks and bonds and watch it grow and the people of Alaska say, wait a minute, it hasn't been explained to us. Maybe we can give Alaskans business.

Have you ever had pressure? Boy have I had some my 17 years. The people in Minnesota always say we don't want stocks and bonds, we need minority housing. We need this industry. We need to help this distressed area. We need homes in this area. Still I'm trying to point out we need an investment. So what does it take? It takes going around to the churches and the civic organizations and the Kiwanis Clubs and everybody else and telling them the story. Telling them why we have something to do in saving our Permanent Trust Fund. And I think that's what you have right here. I sent out a little piece of paper, now we don't have time in Minnesota to send this out for everybody. You notice up here I put, "Representative Clark Gruening, Chairman." Don't feel you're a big shot because of that. If I was in Minnesota and we were at the Presbyterian Ladies Aid, it would be "Mrs. Uplift, Chairman."

Why? Because we go to the Presbyterian Ladies Aid and say, folks, we have something to sell. We want something that is good for the State of Minnesota. We want something here that's going

to have that support. And that's the only reason I've been able to be there for 17 years. Everything on earth has happened to us. We've been condemned, we've been criticized, I've been worked over, I was going to say by the Republicans and the Democrats. I've had five Democratic board members; I've had five Republican board members and the only way I can get going I've found is in that state you have to be able to speak faster than Hubert Humphrey, Orville Freeman and Fritz Mondale put together or you don't have a fighting chance. That's why we are here.

Folks, I am convinced that in Alaska you can do something for Alaskans. I'm not selling anything. For God's sake, we're not going to sell the Minnesota Investment Board. But these folks are magnificent. We need them for investment work. But when I go to New York, I'm the little Bob Blixt with his little briefcase and says, "Say, folks, I need a little help, we'll be able to give you some business, or maybe we can put a measly deposit in your bank by putting in a little in the First Bank at St. Paul and they can put a few million in your bank or a few hundred thousand." For some unknown reason they're willing to open the door. I'm able to get in. I'm able to talk to them.

But at the same time, just as important than meeting the people in New York, it's going to be meeting that Kiwanis Club in Fairbanks. Maybe you should go up north and talk at

Prudhoe Bay once and a while. Maybe you should go to some of the churches in Anchorage. Just a few minutes ago, for example, we had a little question come up---what was it? On treasury notes. I don't mean to criticize you, sir, that's the last thing to do here, but you say, "We're doing pretty well on treasury bills, 6 3/4%." Right. Right. That's good. But the first thing I'd like to say to you folks is my goodness, if it is the Permanent Fund, the last thing we want is treasury bills. They're due in 90 days or 6 months and then it's down.

And in 1974 I had a legislator say, "Buy treasury bills, Bob, they're up at 10%. Commercial paper is at 13%." And it was exactly the wrong thing to buy. Because that's the time we could have gotten long-term bonds for 30 years up at 9% and 10% and I found it's best to buy the things that yield the least. When treasury bills yield 12, buy something that yields 10. The long term bonds. Sometime when treasury bills yield 3 1/4, that's the time to buy treasury bills. Because long term bonds might yield only 5 1/2 or 6. Wait until the bills go higher, but then the long term bonds will go higher, too. If I don't want to buy long term bonds yielding 6% and be locked in for 30 years after interest rates go up to 8%.

But folks that has to be explained to each Kiwanis. It has to be explained to the men's clubs. Because you folks aren't operating in a vacuum and here I guess I can talk like any politician who has been there quite a few years. Folks, you can have

any kind of high standard you want. You can be convinced that you know exactly how to run the Alaska Permanent Fund and if you are knocked out of office, what good does it do? You've got to be able to relate to these people. You've got to be able to tell them how you think it should be done. If you don't know the details of finance, fine. You can find that out in a hurry. But are you in a position to look at their needs? And I guess that's all I'm going to talk about this afternoon. Economic charts, yes we can go over that. But we've been able to build up a department. I have everything in here including my budget. What we're doing this year, what we started out with and I'd like to tell you a little bit about Minnesota and how Minnesota is very comparable to Alaska.

We got in this business about 100 years ago. They set up a Permanent School Fund for Minnesota. I'm sure you've heard of a permanent fund. We were one of the first states to have this. One section of land in every 36 in Minnesota was put in the Permanent School Fund and the Permanent University Fund.

But we had a very unusual state, nobody in Minnesota liked to pay taxes. They said, let's not pay taxes, let's sell off this land. Oh, if we only had it now. One square mile happened to be all of downtown Minneapolis at the present

time. But they sold this stuff for one buck an acre. Well, we got rid of most of it. It was a disgrace. But I'm sure we had in Minnesota a hundred years ago people exactly the same as you have in Alaska today. They say, come on, local development. You don't want to invest in New York. Local development. You know, there's not a single thing like a railroad between St. Paul and Minneapolis?

So ten companies were formed to build a railroad between St. Paul and Minneapolis. All this money out of the permanent fund. They all got five miles along and quit. So what happened? We had issued some bonds. The defaulted. Minnesota had to default on its credit rating, so some years later it took the whole permanent swamp land fund to pay off the bondholders and that's the thing.

We did exactly what I advised you not to do. We sold every bit of the land from the permanent fund for one buck an acre except some old ranch lands we owned in northern Minnesota that were so worthless we couldn't find any fool that would pay one buck an acre for it. And I'm sure 25 years ago if you had tried to sell a whole area around Prudhoe Bay for a buck an acre, you'd have had trouble. But what happened under those sand hills? That, folks, is the Mesabi Range. You know what happened. Iron ore and the First World War and the Second World War built it up to about \$250 million, which was a lot of money in those days.

But then we had everybody working---just like I'm sure you are working here in Alaska today---and during the 1950s they said, let's not build it up, let's spend it now. We have more school problems. So we did decide to use part of the money for school aid, but then of course you've heard what happened in the Mesabi Range. It completely dried up. But that was the beginning of the fund in Minnesota. This \$250 million Permanent School Fund which has been stable ever since.

When I took over in the late 1950s---I was negotiating, I took the job in 1960, we had a Permanent School Fund that was not growing, all invested in treasury securities yielding 2 3/4%. With a nice constitutional provision that said this fund must be inviolate and undiminished. And, according to the lawyers, that meant I couldn't sell anything at a loss. So, if interest rates changed and the bottom went down from par to 99, I couldn't sell it. I had to wait until it went down to zero, then I could write it off. Now that's really fine investment management.

Well, we first changed the constitution, so instead of inviolate it said perpetual. And inviolate. But not undiminished. I don't know what perpetual means. I don't know what that phraseology means. Well, we decided that it means that if I build it up I can sell at a loss. So now I sell at a loss every year. I sell these old, old coupon bonds,

but on that new income gradually build it up over a period equal to that of the maturity of the bond. It works out just fine. But how do you explain that one---that I'm not getting rid of the permanent trust fund by selling out those 2½s which I did in the 1960s. At 58¢, 68¢ on the dollar. That works, folks, included talking to the Presbyterian Ladies Aid Society of Minneapolis, to the school boards, the PTAs, all over the state. And I think that's the way you get things done.

I believe you are honestly in the situation where in handling money it's not necessarily ignoring everything. Now I'll just have to admit today that I'm sure the folks behind me know a lot more about finance than I do. But it's also a matter of communicating that knowledge to the citizens of your state who have the votes and are able to tell you what to do or elect you---I don't mean it's all a political thing. I'll admit I spend 99% of my time on politics and one percent on investments if I have time. But still you need that kind of operation with a basic knowledge of investments. And with a staff that's pretty good and that's what I'd like to present this afternoon.

On the first page we have the fund that we have in Minnesota. If you want to talk about budget today, I'm going to leave out all of my chat about economics and what's going to happen because you can hear that from the others. I'm just going to talk about this little department.

When they hired me on the staff, they put up a whole \$30,000 for the whole department in 1960. I got \$12,500 a year at that time. I took a secretary, an analyst for \$5,000, a bookkeeper from the Treasury Department and some used furniture. That was it. Now it's built up until our annual budget is about three quarters of a million dollars. But of course we have to plead for that the whole way through.

Now, the department is not just an investment department, but we've been able to keep ourselves completely independent. For example, the person in the state, the commissioner of finance. I presume I have a job similar to yours. Or the commissioner of revenue. We would tend to argue a little bit. But we want the investment department completely separate because we want to go our own way, so to speak. Still, we want to be very good friends. We must be that. But we find it good to have this separate department, separate apart from everybody and not under the commissioner of finance or the administration.

I have five members on my board: the governor, auditor, treasurer, secretary of state and attorney general. Nobody in the department has civil service. Nobody has any tenure. All 29 of us could be fired in one minute and told to leave. Now that keeps you on your toes. Any three of my five board members could fire all of us at any time. And still we've

existed under all Democrats, all Republicans, all kinds of mixtures. I'll admit that I've had two wanting to fire me most of the time. But, unless I have one or two wanting to fire me, I feel I'm not doing my job. But if three ever want to fire me, wow, that's bad. But you just have to operate that way and have to be willing to explain what you are doing.

You go as far as you can and then you have to cut back a little bit. But that's the way it is. It works out fine. But we have to be able to explain what we're doing and explain in terms that people can understand.

You'll notice on the first page here our permanent trust fund is now \$263 million. We can go up to 20% in common stocks there and we have that. We have quite a few corporate bonds and you heard the Ginny Mae mortgages mentioned in the last presentation. We use quite a few of them because we are very dependent upon income here for the schools.

Then you will notice the various retirement funds now total \$2 billion, \$77 million in Minnesota. Here we have quite a large common stock percentage, 49% which is nearly comparable with the percentage in equities that some of the banks have of 60% and 70% in New York. We are, I suppose, one of the public funds that's the highest in common stock percentages in the nation. Now, many will say, well isn't that dandy. Maybe. I guess we'll have to look into the future. But we have found that

by buying yield stocks recently and buying in the lows of '74 and now---and not trying to beat everybody that's on this growth binge, we've found that we've been able to lower our average costs to the point where as of today I think our common stocks might be even a little bit above, even though we bought a lot the last two or three years at very high levels and then of course in the '72-'73 era at very high levels, we're as---our bonds still show a little of a loss for the simple reason that all of the bonds that we bought in the 1960s still are 5%, 5½%, 6%, 6½% couponed. We've traded out of some of them, but we feel there is a good argument for equities.

Then you'll notice the highway funds, \$215 million. These are trust funds for the highways, various departmental funds, \$210 million, that includes almost a hundred different funds, by the way, and then the current tax receipts, \$398 million. By the way, Minnesota is one of the few states that has a treasury surplus. In other words, our legislature ---they're like you are, they're mostly Democrats, liberals, like to spend, they still can't spend as much money as we take in. You know, that's great. And when we sell a bond issue, you don't know what it is to say, well, now, look, what do you have behind this. We have a \$300 million surplus, we have \$3 billion investment funds and, of course, Minnesota has a AAA rating. And, I'd like to present that to you, too.

If you're going to be borrowing money for improvements, if you're going to be doing anything to help Alaska generally, a nice, well-managed fund certainly helps. Because they know all these assets are behind it.

Let's turn to the second page. The second page shows what has happened to our little fund in Minnesota. You will notice in 1959 they had only \$139 million; now we are over \$2 billion. That's in the retirement fund. Now the trust fund is in addition to this and with the invested treasurer's cash we actually have over \$3 billion.

The this shows what happens with funds that have growth. If you will notice that first four years, pardon me, two years, it went up 35%. Then by December 31, '65, the growth was an additional 71%. The next four years, 100%. The next four years, 85%; the next four years 74%. We're looking for funds totalling about \$3.6 billion by 1981. Then another 80% growth the next four years. So these public funds are just astounding as to their growth and you have to have departments that are able to handle huge amounts of money. In other words, we don't try to piddle around with the small stocks, the tiny companies. It just takes too much time. We must concentrate on the leading stocks, on the bigger ones, that's the only ones worth it.

Now, will you turn to the next page. You'll notice the difference we have between the investments in the private pension

fund and the state and local retirement fund. We are similar here, but you'll notice how fast these funds are becoming. The chart on the left, and this is from the latest Federal Reserve bulletin, shows that the public funds throughout the country are now at about \$125 billion. This does not include the Alaskan trust fund or the Minnesota trust fund or New Mexico---and they are about the three that have them, and then, of course, we have Texas with the oil. That would add a comparatively small amount, about \$2 billion. But you'll notice the state and local funds total about \$125 billion, whereas the private pension funds only \$160 billion. So, we're catching up on them right away. This management sometimes is local and sometimes it's with the big banks and mutual fund operations. But you'll note here that the percentage in common stock has gone up very high recently in the public funds as with the private pension funds. Admittedly, we've had some rough stock markets lately. But you'll notice we're still going in there and still have quite a bit of faith.

On page 4, you'll note here we have the asset diversification of the various bonds. First the basic retirement fund. And I do advocate a centralized investment office because the investment work here is so similar and you are able to use the same people for these funds.

In Minnesota, we have separate teacher's retirement fund, public employees, police and fire, state employees, highway patrolmen, judges retirement fund. All with different groups, all with their own executive secretaries; all are great lobbyists, as you know, especially our judges, if I may say so. And they are all going full blast all the time, but they have similar needs. So our job in there is to work with all of them, try to get their funds invested.

Then, of course, we have this adjustable fixed benefit fund. I know what you think, if something is fixed in government and then is adjustable, you know there is something wrong with it, most likely crooked. It isn't really. All this means is all the money for retired people is transferred---all the retirement fund when a guy becomes 65 years old from then on, if the market goes up or the income goes up above 5%, which is the actuarially assumed rate, then they get more than their regular pension.

HAUGEN: Let me interrupt you. In other words, the general fund doesn't build in an inflation factor against this...

BLIXT: No. This isn't the general fund at all. But in Minnesota, we have the employees contributing 4% of their salaries to a retirement fund. The state government contributes 4%. In addition, because the state government has not contributed in previous years, we have another 2% makeup. So, in essence, we

have 10% of everybody's paycheck going into a centralized retirement fund. Well, when that individual becomes 65 years old, then out of the retirement fund, whether there is enough money to fund his benefits in an entirety, the total amount on an actuarially sound basis to fund those benefits at a 5% rate is transferred to this separate fund called the adjustable fixed benefit fund. Then we have to play with the benefits, but we better not do too much playing. But it depends on the two year ratio of stock prices to the cost of the stock; it depends on the bond yield and that type of thing. In the early 1970s, we gave very significant increases, about a 13% increase, in pensions based on this. And then, of course, we had the downswing in 1974. It looks as if we shouldn't have given anything for a while. Now it's coming up again so we're going to give another 4% increase in pensions this coming January and we feel in another couple of years we'll be able to do that. So the purpose of this fund, this adjustable fixed benefit fund of \$758 million ---you see it's sizable, three quarters of a billion---is entirely to pay pensions based on market action.

Now we have fallen into trouble here frankly. You can imagine how a 78 year old public employee with cancer who's going to pass away next year says, "Well, I realize I don't get an increase this year when the market went down." Nope,

that's not the way to look at it. They want it every year. So, I think we're going to change this. We find that we can give about a 3% increase in pensions every year and do it on an actuarially sound basis to more or less match the cost of living increase. Not quite, but it is certainly going to satisfy everybody. It looks as if a 3% or 4% increase is possible. But there again this is something---you need a centralized investment department to work with the heads of the various retirement funds, to beat the prices, talk to the Minnesota Educational Association ---I'm sure you have your Alaskan Educational Association or teachers here. We have to talk to the teachers union, we have to talk to legislative groups, again the Kiwanis Club, the Lions Club and everybody else to explain what we are doing to try to get this straightened out.

Then you'll notice we have these supplemental funds. And those are interesting... Yes?

HAUGEN: One question before you get there. Does your employee put into the social security system?

BLIXT: Yes.

HAUGEN: Oh, OK. That's all.

BLIXT: Some do not. Our policemen and firemen do not. And

I think you are aware of that big debate going on throughout the nation.

They want a lot of benefits without it. I don't handle police and fire funds directly except those that have elected to join a state police and fire fund. Otherwise I regret to say we have about 400 independent funds in the state. And my, when the legislature meets to try to control the police and firemen, I don't know how it is here, but they all come with the uniforms and the guns and the night sticks and they say, "Whoopee, don't you dare cut our pension." Well, then what we have been able to do there is help them along in their investment and still let them have their individual police and fire retirement fund. The way we do that is next.

You'll notice the Minnesota supplemental retirement fund---an income share account, growth share account and fixed return account. They're like little mutual funds and anybody who wants to invest there can do so. Now, would you take out this little prospectus here while we're on that. The little white page I use there---we send this out every year and these policemen and firemen, if they want to invest with us, they don't have to. If you tell them they have to then they don't like it. If you say they can if they wish, oh, that's completely different. And they can buy units in this fund. In the late 1960s we set up a growth stock fund which of course is supposed to double every year. You know

what happened. We're lucky---it's worth about what it was in 1970. We're luckier than most. But some people still want it. You'll notice the income share account which has been most popular begins on page 10 of this prospectus. It's 50% in bonds, 50% in stocks. The yield here is about 691 and units of this are purchased by the various police and fire funds and individuals in deferred income plans.

You see when you have a centralized investment department you can do so many things right there. I don't know if you have that here yet or not, but some legislators for example from the Minnesota legislature---or, for example, we have a man by the name of Pillsbury. I don't know if you ever hear of that name, but his income isn't primarily from his legislative salary. Let's put it that way. And the way we do it with Mr. Pillsbury, he wants it all put away for when he retires. So he gets no salary. He puts it all out in one of these funds. And, of course, the Department of Revenue knows and that's OK and therefore it's not taxed. It's a terrific benefit. And we do all of that through these funds. We use it for police and fire funds, for this deferred income business, anything else.

Then we also have recently a fixed return account. If you turn to page 14 in this prospectus---you know in the last few years nobody likes stocks anymore. Everybody likes bonds. So,

if they want a green suit, we turn on the green light. I don't advocate all bonds, but everybody wants all the bonds. So we said, OK folks, let's do it. So we set up this little bond, the yield is 8.72%. I'm trying to build up reserve ---you'll notice all these AAAs here---you folks in back will have to admit that's pretty good. We don't want risk. So we just want the people here that just want income. They don't like the stock market and out of this 782, we're able to guarantee them about a 8.1 to 8.3% return. And, needless to say, that's good for these funds. But again, it takes somebody locally to explain it, to go out and talk to all these folks and say you have an advantage in working through us and, of course, we print about 10-20-30,000 copies of this little handout every year and it's given to these people and they feel some incentive to work in the schools or the local government or the state, of course, of Minnesota.

Then let's go on here. We have the variable annuity fund. Now that's a concept that came up at exactly the wrong time. But this shows what happens in a state when you do something that you admit is wrong and then have to back out of it. In the late 1960s, everyone realized you didn't need a guaranteed benefit. All you needed was to put money in the hot stocks and, of course we all knew they'd double next year or the year after that. We decided to buy some stocks like

IBM and Minnesota Mining and they're less than I paid for them now. We bought an awful lot of Eastman Kodak and that's the lowest stock in our portfolio now. We bought a little Buckley Meers, which is a local company which is in television screens, and I remember it got up to 44 and I got a call from a teacher at one of our colleges, said, "Blixt, you stupid fool, why are you buying all these big companies. Put it all in Buckley Meers, it's at 44 today and it'll double by next week." Well, I explained that it might be speculative, I think the stock sells at 3 today and has most of the time since. You've got to get the people out of that thing. But still, they wanted the variable annuity. Well, they couldn't understand how that thing went up and down whenever the variable annuity went up, it's because I was lucky. When it was down, it was, "That stupid Blixt." And that was going on all the time. Especially because we had a two year moving average for our variable annuity. We decided it was wrong to take the market price at any one time. So instead we have a two year moving average.

Let me show you the trouble I got into on that one. Turn to page 4 and 5. You know the market really hit the skids in late '74. What they didn't realize was with every two month average we were showing this thing in '75 and '76. And in 1976 some people called me and said, "Blixt, how can you be so stupid?" You showed a minus 0.10% income even though the market went up

last year." I had to say, yeah, but we still have the '74 figures in there. Well then, this last year the market went down quite a ways, but you notice we showed a 15.94% increase. Well, you need just a little book like this to explain.

Well, needless to say the variable annuity concept is not one that is going over. Wisconsin with a \$500 million variable annuity is going to eliminate theirs this year. This has been half eliminated. Teachers can only put in half of their salaries. Some still want it. But again there is a lot of hand holding. This is the first time we came up with a separate annual report on this, July 1, '77. We are taking it to the legislature. We expect them to more or less eliminate it from the standpoint of new money this coming year.

But here again, if you need something, explain something. The school teachers were going to the legislators. "What's wrong, why do you have that stupid investment man? Why don't you legislators get good investment laws?" You see how it helps to have something float for a few years. And, of course, I have to speak to the teacher's union; I had to speak to the Minnesota Educational Association, give them copies of this, of all the information so their field representatives could go out to the schools of Minnesota to explain the situation.

This is evidence that my department is partly an invest-

ment department, isn't it? But also a hand holding department, public relations department and really we have to do in a sense what you do in the legislature---it's selling your program. It's selling what you know is right. But it is selling. It is not just doing what you know is right. Or you won't get elected. And when we are in business like we are, we have to look at both sides of it. I don't mean compromise with what is right. I don't mean that at all. But if you want to do a program and if you want to do it true and want to do it the right way, you simply have to be able to get the public behind you and that's the reason for all this stuff. We don't have fancy brochures or anything. We have to do it on green newsprint or white newsprint in state offices. But it works. And we get the message across.

OK, then to this little handout here, Permanent School Fund shows our other investments and we pretty well go through our stock and bond portfolio.

On the next page, page 5, I inserted this for no particular reason except that it is more detail of where we were at the end of October. This is just a little worksheet that is put out in our department every month that we look at, my analyst can see what we have, the money that is coming in, the growth in funds and that type of thing.

And then I'd like you to turn to page 6. This is an excerpt from our new annual report. As you know, people have different ideas as to what makes good investments, depending on what has

happened lately. Four years ago, nobody asked me what the yield was. Nobody asked me. They asked me just one thing. What has your performance been lately? How much has your account grown? How long did it take your account to double? Now nobody asks that. They ask what is the yield. Until it's time to explain that, look the yield is going up, we don't want an 8% yield. If we had an 8% yield on a long term bond; if Carter gets in trouble and has to fire Burns and it goes back to 3% interest rates, give me a few years. The telephone bonds are sure to be refunded right away. They have 5 years. The other corporate bonds will be refunded in 10 years. We're going to have just a 4% or 5% yield again. "I want something more than that." Folks, won't you please go along with me and give me time.

Well, in our annual report we're going to have a chart like this. You'll note it has a sort of gentle movement upward. And when the folks come in and say what's happened to the yield; I say, no, we don't give 8%, we don't give 9%. But please look at the general trend of the chart. Now they are so accusing me of stock market action that you'll notice ---now this is the first draft of my annual report. This is the cover that's going to be on it and then you'll have--- this is the new annual report. The old one is the green book. But this adjustable fixed benefit fund went down so much with

the stock market decline, you don't find a graph of this showing this terrible canyon so to speak right here. But I'm saying that isn't an accurate resume really of what happens to the stocks. We cannot base what we do on the fact that the market goes from 580 to 1050 and back to 800. What I'm interested in are the dividend increases coming through every year. So we keep good track of them this year for example the dividend increases along---that's the little dollar or two, pardon me, cent or two, that comes in per share in addition to what we had before. Those dividend increases might give off \$5 million so far this year. I say that's what we want in the growth. So that I want to keep that income coming in.

As you'll notice, from 1956-7, it was 2.9%. Then about 1960 it was just a little over 3%. Now the yield is over 6% in these Permanent Funds. We feel we'll be able to continue this until about 7% with this present portfolio. If we keep in stocks, we aren't going to be able to increase much above that because, of course, stock yields just aren't that high. But many said, "Oh, it went down. That must be when the market crashed." Not at all. It was just the opposite. We put these here to show what happened when the market went up. If you'll notice that peak was reached in '71 and then it went down in '72 because when we started buying stocks at these extremely high priced earnings ratios in 1972, until early '73, the yield went down. So I'm trying to show the folks from the legislature there that this yield we hope to keep

in the general swing upward. But that it will tend to go down a little bit when you have an extremely high market simply because when the Dow Jones is at 150, of course, or 1050 rather, and the yields are 2%, you don't get the current yield in the account.

On the next page, you'll see a little bit about the money we handled. You'll notice we have short term money of \$819 million in governments and \$250 million in corporate bills. I just have two men handling that. They do a very good job. For a while I think we were the 10th largest short term fund in the country, right under Bank of America. We had over a billion bucks. You know for a while we had a surplus in our treasury of about \$600 million in Minnesota. And then we had the \$250 million highway fund and we had \$150-\$200 million in the various retirement accounts. So the short term money debt is just a lot of fun. I have two people handling it; they do a good job. Then you'll notice we keep in equities, common stock, about 32%, fixed income 35%. And then in the big circle on the bottom, you notice our Permanent School Fund is only 8% of our assets. But we're able to use the same department because we have similar types of investments in all of these funds.

Would you turn to the next page. So many of you are asking something that I am sure is very important. What do you have to do to get a department internally? As you know,

my salary and the salaries of all my clerks and everything else are public knowledge, so I just put it on paper here. Some of you ask what does it cost. I don't think you could compare our department with what you need up here. I guess we had folks running around making speeches all the time, some spending their time in the legislature, holding hands as I mentioned with every teacher group and Kiwanis Club, attending meetings of the various retirement associations. We had to work out financing for a national park, we also tried to work out financing for this reserve mining problem there. And it is a sort of overall financial and investment advisory office. It's going up from three people back in 1960, four actual little files, to 29 people at the present time. But this is our budget for this year and I'd like to explain what we're doing. Obviously, I would suggest nothing anywhere near this large for Alaska if you were starting a permanent fund. First you have to get your feet on the ground.

But I'd like to mention two things that are important. You've got to pay salaries to get people that are adequate. I mean, you can't hand somebody \$200 million a year and give them \$10,000 and a canoe and say you can have all the fishing you want up here, I mean that doesn't work.

Secondly, you've got to give them some travel money. You can sit on the phone and take calls from brokers who say I've got this today, it's a good deal. No. He has got to get to the

financial centers. He would have to get to New York, to Chicago, to Los Angeles, San Francisco and meet some of the people. Meet the people you are dealing with. Meet the correspondents and the bankers, make it to some of the banks there. That I would say is important and our budget is a little weak there. You will notice the general administration of our department, which is 29 people. There is myself, the state pays me \$41,000 a year. I might say the wages in Minnesota---I don't know they compare with yours---our governor gets \$59,000, our attorney general gets \$49,000. We have somebody that seems to be comparable to your position, he's called the commissioner of finance. But it's a political thing.

GALLAGHER: Ed Rymer?

BLIXT: What?

GALLAGHER: Ed Rymer?

BLIXT: No, Rymer is the commissioner of taxation or of revenue. Now he gets \$41,000, which is what, about the top 10 of us get. But there is one above that, the commissioner of finance, who works on the budget and he can get thrown out, he will get thrown out, with every governor.

So he gets \$45,000, mostly because of that lack of tenure. Rye Murphy is going to stay on because he's a good professional man, our commissioner of administration will stay on, Democrats or Republicans. So there are about 10 of us getting \$41,000 a year. We get more than the treasurer or the auditor, they get about \$29,000 a year. The other department heads in the state get about from \$30 to \$34,000. I don't know how that works in Alaska, but you see where we are.

Then I have an assistant executive secretary that gets \$35,000; he does most of the portfolio work. The portfolio coordinator is a young lady who seemingly is able to deal with the legislature, brokers, everybody else a lot better than I can and she's a real brain. So you'll notice we pay her quite a bit, \$22,000 a year. My main secretary is called an administrative assistant, we pay her \$12,800. And the secretary to Art is getting \$10,000. Our short term money department: the head man gets \$24,000, the, pardon me, \$34,000, the second man gets \$24,000. Our fixed income group: the department head gets \$28,000, we have two analysts getting in the mid-twenties, an accounting coordinator---he's a CPA by the way. He does a real fine job at trying to work out all these accounting problems with bonds. He's a young man, gets \$22,000. In the equity department, we have a department head that gets \$32,000, five analysts and the treasurer and then in investment operations you'll notice we have a director, transaction supervisor, three accountants, a secretarial staff of five people and

a computer operator. Salary costs to the department are \$590,000 this year, with our retirement and group insurance we have \$667,000.

Then on the next page---you know for rent space---I don't know what it is in Anchorage---we get our rental for about \$5.95 a square foot per year. We rent space because there is not room in the capitol. But then we mostly have a Xerox lease, market information, all this other information here you see where it is---travel. \$198,000. Office supplies, equipment purchases, our budget is \$875,000. You wouldn't need that here in Alaska to start with by all means. I would say \$250,000 would get you a very good investment department at the present time.

Could we turn back to some of the other information. One thing we find it is extremely important to do is to work with the legislature and the people in our work and show them what we are doing, not only from an investment standpoint, but also from a distribution of business standpoint. I know in Minnesota, and I suppose it is the same here, you all have people who say, "But I have an office in Anchorage. You've got to butter me up first. I have an office in Fairbanks."

Or maybe you have something like we have in Minnesota ---they're called local bankers. I have a bank here therefore I need a deposit of so many hundred thousand dollars

or so. That frankly stymied our investment program to begin with until we had a Republican, Bell Bjorenson, the governor, Orville Freeman, maybe you've heard of him, he's the secretary of agriculture, who simply went around to the bankers associations---the two of them---a Republican and a Democrat---in 1960 and said folks, we've had enough. We can't have our deposits in your bank. At that time it was 1% by the way. We can get more. And they still cried and say, "Yeah, but you're doing so much for the state of Minnesota." Well, they say, well then we aren't going to do that for the state of Minnesota, but I am the leading Republican and this guy is the leading Democrat and you bankers better vote socialistic then because we're going to take the deposits out of your bank. We did. And put them in long-term governments and other things that have worked out very well.

But it was bad. The ramifications were tremendous. We had to take the time deposits out over a stage of two years. The bankers literally wouldn't give us our money all at once. We withdrew half of it, two years later we withdrew the rest of it. Then one bank said, "Now about governments, you have to do it through us because we've always had the state accounts." So we always did it through them and found that they always went to New York to one particular investment house because that bank had its chairman of the board on the board of this investment house.

So it took another four years to pass legislation requiring us to go out for bids and offerings every time we traded in governments. We had all kinds of fights until the early 1970s and then we simply went out to the banks with bids and said you will handle this amount for how much. We've taken all the accounts back from the various banks in Minnesota except when we have an analysis made. One bank will handle the investment work. One bank might handle the account for the welfare department. One bank might handle something else but in a general account, a bank, you know, that we caught on to financial management and said you can---we'll do all your work for a zero balance. They didn't realize that that's the way we worked it. The zero balance. We had a previous auditor that meant zero on the books, but of course after you pay school aids, which we do in Minnesota and did last week of \$350 million, you know your books can say zero, but really you have \$350 million still in the banking system until the mail comes back. And I don't know how you are here, but we always have a superintendent of schools in Minnesota who gets his check for \$2½ million and, instead of cashing it and investing it as he should, he puts it in his pocket and goes to Lions Club, "Say you guys, have you ever seen a check for \$2½ million?" I mean that's sort of baloney. It takes 2½ weeks until we get the money back. So what we

do now is actually invest that money and keep it entirely invested and the poor bank found they were operation on a zero balance. So they gave up the accounts the last year on a bid basis and now another bank has it. Yes sir?

MALONE: Thank you. Mr. Blixt, what did the banks do with the money when they had it if it was doing so much for the state? Was it invested within the state or was it invested in something else?

BLIXT: Now that's an interesting question and I would hate to say something to you, sir, that---a banker would say I'm a liar. But they always say, "We are investing in Minnesota businesses!" Especially independent bankers of which we have 400 in Minnesota. But when you start looking at their banking statement, their loans to Minnesota people were about 54%. And Poppa would sell the bank to the son or otherwise when he died the son got it. Instead of Minnesota, the son was always in Hawaii in the winter, he was up here shooting big game in the summer. He had half the bank assets in treasury bills and was he really invested in Minnesota? No. Not our independent banks. Northwest Banco and First Bank stock were, yes. But they're the big ones everybody is fighting. But we found that we could put all this money in Minnesota banks and yes, some of it came out, but were they investing in

Minnesota and the answer is no, no sir, they weren't. They were investing in treasury bills and municipal bonds and that type of thing. Admittedly most of the municipal bonds were Minnesota municipal bonds because the bankers got double tax benefits, you see, both on their state income tax and the federal income tax.

But when somebody says you've got to invest in Alaska for Alaskans, mind that you're in the legislature sir, you decide who in Alaska should get the money. Maybe it's somebody that needs relief here or somebody that needs help here. If you believe in the trickle down theory, you give enough to the bankers and after you've given him \$10 million, he's apt to let a little trickle down, that's fine. We didn't find it that way in Minnesota, sir. It just didn't work that way.

But we have some very good bankers and I don't mean to criticize the banking community. We found our leading bankers, the folks at Northwest Banco and First Bank Stock Corporation, our First Bank System is called now, are just marvelous. They were asking for account analysis all through these years. They said, "Look, we would like to open a bank in this little town. We would like to serve it better." But of course every time they go before the banking commissioner, there would be five little independent banks in that town. Three of them say, "We're serving this community, don't let the big holding

companies in." Now we have a silly situation. Our governor, Perpich, who, as you know, is quite a rabid Democrat. He's up there advocating the big bank holding companies and some of the others, some of the little independent banks, all the state's assessments are all mixed up at the present time, and of course the leading contributors, the leading politicians on both sides, it's a very delicate question. But folks, you just---because you put idle balances in a bank does not mean that that money will be invested in Alaska. They might be buying treasury bills and other government debts which will pay for all the boats that are on Midway Island and the Battle of Midway that have been down there for 20-30 years. I guess that's where we got our national debt.

But is that for Alaska? No. Treasury obligations, federal loan bank bonds, lots of municipal bonds, maybe from here or somewhere else. I don't mean to get off on banking, you'll notice my temperature goes up. We have those same arguments there and I think you face them here. They're in every state in the nation.

GRUENING: I just want to follow up on that. Are banks selectable for portions and if so how are they selected?

BLIXT: Banks get no balances in Minnesota today on any of these funds. None of the funds I've mentioned to you have a

single time deposit. We don't have one dollar in the time deposits in Minnesota. The state treasurer does have balances in banks, but instead of banks all over---you know in the old days you said every county had to have a local bank for something, recent handle costs, everything. Now we've gone down from 300 banks to less than 100 and we have banks only in areas where we have a state institution, where we actually need that bank. If we have a university or state college, if we have a department of highways office there, we might have a little balance in local banks to handle the payroll. We want to treat them fairly in every way. But our balances have gone down---I think for a while they were a hundred million dollars in the early 1960s. Now the dollar is worth more and we've come down to about \$60 million, \$40 million, and now you'll find \$10-20 million. And that's plenty.

GRUENING: How do you select those banks that do manage the...

BLIXT: On a term basis. We'll let them all come in--- we hired a man who knows something about banking. He used to work for the banks. We've been able to do a real good account analysis and analyze did on this type of thing, how much they charged per check, how much per item the whole way

through and we compare the data and give it to them on that basis. We don't care whether the banker is Republican, Democrat, who he supported in the last campaign, that doesn't bother us at all. It's completely open, all the banks can be there, they can all see the figures and they can see what the competition said. And it works marvelously and, frankly, we get on much better terms with the folks at Northwest Banco and First Bank systems since all this happened. It works, it works very, very well the whole way through.

OK. I see I have just a few minutes left. I would like to explain how our board works. My bosses are the five top elected people in the state: governor, auditor, treasurer, secretary of state and attorney general. Obviously, they have changed parties many times, but my position has to be non-political.

We also have an advisory committee of 10 leading people---I didn't mean to talk about bankers---they're going to shoot me. The trust department people, they're wonderful. Trust department people are my best supporters there. You'll notice our advisory committee includes all the bank trust department people, the top managers of money in the Twin Cities, the insurance company people, we're all the very best friends, I must have to say we've got a lot of our advice on bank management, so to speak, if you want to call it that, from these people. These folks meet every two months, under a recent law they're going to meet every month to give advice,

these meetings begin at nine in the morning, all morning, through noon, until two in the afternoon. So it's a long meeting. We go over everything.

And I'd like to show you something more in this annual report. A few people want their palms greased. By the way, I might mention, when banks and brokers get together to fight, it gets a little rough. We had the little attorney general there, he came in in 1962 and wanted to handle this bank thing. And it's the only thing he really lost in his life. Finally it got so bad that he said he was never going to take them on again. Well then luckily, our then governor, a Norwegian by the name of Rolag, appointed him a senatorial job at the time, or I don't think he'd been reelected---you might have heard of him---Fritz Mondale---and he was a dandy board member, but he was trying to solve this stuff and he just couldn't do it. But this is what I'm saying he told me to do---please turn to page 35 in this report, please.

It says give out the business to anyone you want, be he Republican, Democrat or anything else. Just be able to justify it and tell them exactly what you do. So if you'll notice here on page 35, 36, 37, 38 and 39, 40 and 41, we tell just how we distribute the business. Then on page 43, 4, 5, 6, and 7, we have every order mentioned. But we gave it to them. Now there's a fine representative, I am sure he

wouldn't do it here, will come up to me, "Blixt, uh, my brother-in-law works for this corporate shop in Anchorage and, you know, he's having a hard time getting things started. Now I'm sure if you give him an order for a thousand shares now and then, it will work." Hell, I say, you know, fine, you know that'll just work very well. We'll just put a little footnote, "This order placed at the request of Representative Clark Gruening." For some unknown reason, the Clark Gruenings in Minnesota have never asked me to do it. It works beautifully. And we have found that if you just keep everything above board, it works well.

Now we have another senator who wasn't as good as the other. It's the first time we ever had politics enter it. I'm going to show you who that senator is who literally told me that his palm had to be greased. He now heads the retirement commission in Minnesota. It got a little difficult. But what do you do with something like that? Well the way we did it is in our recent report---take out the loose leaf folds here---pass a little bill that says that my council members have to be honest. Well, on page 41, we list why we think our people are honest. If you have a pencil maybe you should underline that a little bit. Then on this next page, halfway down, we list the representatives names who even work for a brokerage house, even if we give them no business. You'll notice the investment department has been informed, I'm talking about this third paragraph down, of only two

members of the legislature who work for brokerage houses that deal with the State of Minnesota and therefore may present an appearance of a conflict of interest. And then we list the two people, one of whom is very innocent and one of whom is guilty as sin. But it says here a senator has no direct benefit from the state account, we have been informed of bla, bla, bla. But by simply putting his name there we don't deal with him by the way, we deal with the firm, but I think it will do a little bit to inform---to keep it that way.

I don't mean this in sarcasm, and I don't mean this in a way in which a bureaucrat is doing something that maybe elected officials wouldn't like. But my top bosses have read through this, that is, the governor, auditor, secretary of state, attorney general, and the man in your position, the commissioner of finance, that says, "Bob, you've got to do it. You've got to do it. If there's anything that pushes you, put it right out in print and then it becomes honest." And folks, that's something else that I think would help you very much here in Alaska. You're going to get pressure from banks, you're going to get pressure from brokerage houses, you're going to get pressure of other things.

I'm leaving copies of both of these. This won't be printed until next week. You'll notice I just have the cover

with some Xerox copies which aren't too good. I'll send you the final copies when they're ready.

But I think we'll point out the things we do to try to inform the people of Minnesota of what we are doing. Obviously these reports are too expensive to send to everybody. We give them to the legislature, we give them to anybody that wants them, the entire brokerage community. By the way, this distribution of business is interesting; we send it to 10 German libraries every year. They want to know just how Minnesota---or how a United States public fund is handled. And we sent it to public funds throughout the country. So we find there is some interest in there.

As far as our operation, I have mentioned that we have a board, we have an advisory council, we have a pension retirement commission made up of 10 legislators, we deal with other legislative groups all the time, so we're under all kinds of controls. We do everything in-house. We have a legislative auditor. I don't know if you have that. You should have an auditor directly under the legislature. Not under the government---if there's some fraud ---I don't mean---the administration. The legislature gets there too. He comes and goes all over our books.

I place all these orders but I'm not allowed to pay for one dime of it. See, I place the orders. And somebody in my staff then writes a memo to the treasurer. The treasurer then gets our memo and then a couple of days later gets billed by the brokerage

house. And it's the treasurer that pays for it. Then, not only do we have that double check on ourselves, but then the legislative auditor comes in. So, I think it's a pretty good check and we have all the various departments.

GRUENING: Is that a---would you list that as one of the prime reasons to separate the revenue and investment functions of government?

BLIXT: I think they should be separated. And I think the investment function should be completely separate. There are so many things there, if taxes go down, or say if oil receipts go down, we want to do something with the investment. And, by the way, I have another suggestion that I want to pass out which may be wrong and maybe you haven't heard before.

Folks, I would cut down your investments in your--- pardon me, in your Permanent Fund portfolio in the oil industry tremendously. We just don't use iron ore stocks in Minnesota. For one reason. Our politicians are always fighting the iron companies. They always want more taxes out of them. They always want this and that. And if I had U. S. Steel and Inland Steel, we'd be going up there fighting them all the time saying we're stockholders, we're going to come to your meeting and everything else. In the paper last night,

they're still disagreeing here about the taxes to be paid on that pipeline. Why in the dickens do you want to get mixed up in the oil industry? Do you realize your investment is so fantastic in the oil industry right now that if somebody discovered you could run an automobile on hot air or steam, if somebody decides to use nuclear power plants entirely, the oil industry might be out of business. I don't expect it. But on the other hand, you are so invested in oil right now that I don't think you should just follow the charts of an average investment portfolio and say, well this percentage in oil is something else. I would cool your oil investments. You're invested up to here right now. Your revenues are so dependent upon the oil industry. Why don't you diversify in other areas? And you're here literally in the center of the world, you folks should be looking at Japanese investments. You're so close to that economy. You could get all kinds of information. You should be looking maybe at British and French investments.

GRUENING: That would be a switch. If we bought up in Japan.

BLIXT: Then next time they declare a war and attack Pearl Harbor, you won't have to worry that they're going to bomb Anchorage next. You'll own half the place.

GRUENING: We'll have a proxy battle and win, huh?

BLIXT: If you have a proxy battle, it'll mean the legislature will be able to appropriate funds and those legislators will go to Tokoyo, you know.

Now, I don't mean to be facetious, gentlemen. But I don't think you should get a double whammy by investing that way. I think there again, I would suggest that you tailor your investments to Alaska. Not just because---oh, Manufacturers does this, First National City Bank does this, First in St. Paul does this, Blixt does this. No. No. What I do isn't right for you. You folks might want a heavier investment in iron ore, a heavier investment in steel. I would cut way down on your oil investments in your portfolio because you are so invested already. Again, I think your portfolio should be handled entirely, as I said, for Alaskans and for a special use here.

I would like to spend just a couple of minutes, and I see that's all I have left, on some of the pressures we've gone through. We've had tremendous pressures from the municipal bond agents and the Twin Cities who let the bonds. They're tax exempt. We've been threatened. We do not buy municipal bonds from any Minnesota municipality or the state or anything else. We keep that out. The state finance agency, a housing agency, wants to buy housing bonds. Of course not. We can sell housing bonds on the tax exempt market. Why

should we use trust funds that we can invest in corporate bonds ---we're getting over 8%, when our housing agency can sell bonds at about 6%. So, therefore, we do it on that basis and, by the way, we're able to get better rates on our state debt because we have the state retirement fund and the state trust fund invested at a higher interest rate.

Also there is always the pressure on us to invest in some local interest. Somebody wanted us to put up a paper plant in northern Minnesota. All I have to say is I don't know how to run a paper plant and we didn't do it. But what we really had in the line of pressure was someone that came to us and said invest in Cedar Riverside and Jonathan and some housing projects. We said no. There were some of these young towns, maybe you've heard of them, they've all gone bankrupt throughout the country, but we waited until we got a U. S. government guarantee. Then we bought it. Sure they've gone bankrupt. But we buy these government guaranteed securities and don't take the risk. We use some government guaranteed shipline bonds, government guaranteed hospitals, government guaranteed Ginny Maes, and it works out very well. But with the state investment here you can work out everything. The banks said they needed help in student loans, so we helped buy student loans in the sense by using student loans rather than government paper. Somebody said you've got to get into the Small Business Administration loan. I don't want to get into that, it's

too political. So we have a bank representing the Minnesota Bankers Association taking these small business loans. The banks will take the 10%; they'll sell to us only the 90% that's fully guaranteed. We buy that at a good market rate and if anything happens the banks handle that for us. So you see, we're able to handle things by being a state department and working through these agencies so very well without taking any risk at all.

MALONE: You were talking about young towns a moment ago. Alaska is in the process---a long drawn out process---of relocating its capitol city. I take it from your remarks you wouldn't advise investing in that.

BLIXT: Not with permanent school money. For the simple reason that you have so much welfare, so much permanent school coming in, I think you should sell bonds on the full faith and credit of Alaska and do it on a municipal bond basis. A tax exempt basis. And the---let the folks in high income brackets, have the banks, have the insurance companies, buy those full faith and credit Alaska bonds, and one thing that will add to that full faith and credit will be a real good investment portfolio in governments, in Ginny Maes, in AAA corporates and some common stock. Now I think that you defeat

your purpose by taking money that can earn 3% and putting into a project where you could get the money at maybe 5%, 5½%---what would a full faith and credit Alaskan bond sell at today?

GRUENING: I don't know. Ask the commissioner

GALLAGHER: 5¼%.

BLIXT: 5¼%? OK. Well, if you can get over 8% and a U.S. government guarantee, why do you put something in a security when you could get the money at 5¼%? You see you can just make 3% on the difference there. By all means...

GRUENING: Unless you want to get around the voters. That's one way. I'm not advocating that.

BLIXT: Why don't you have a local investment man, and a finance man, and a few others go and talk to all those voters at the Presbyterian Church and the Lions Club? You know, the people in Alaska aren't all that stupid. I really feel that way. I think if you can talk to them...

GRUENING: I agree with you.

BLIXT: ... if you have a local base of operations so to speak

and are able to explain it. It's so logical. But you need a little enthusiasm right here. We do in other states. Why don't you do it here? You're not any more stupid than any of the rest of us. We're so much afraid of being Swedes in Minnesota.

GRUENING: We have a couple Norwegians.

BLIXT: Well, they're worse, of course. I say I went to a Norwegian school, I'll have you know. Pay no mind... OK, I think maybe I've said all I needed here except that I would strongly suggest that you resist the pressure for higher yield in a diversified portfolio, review your revenue projection, the loan fund activity that you've already done ---sure---I think it's extremely good. I would of course suggest that second thing down, as you can presume any investment man would suggest, that---the second column---on page---right here? The investment one? I think it's a good ---this is a very good brochure by the way, whoever did it. And be careful with what you do, but keep control here. But have an agency that's working under you so that they can be subject to your ideas and can do studies for you to help your commissioner of finance or the administration and taxation do a better job in that way.

On the last page I have just mentioned a few thoughts which I don't mean to include anything you haven't thought of already. But you'll notice if you hold incoming oil wealth as a permanent investment, it provides a stable source of income, it would contribute toward minimizing future economic problems. And of course it minimizes the amount available for these current purposes, but I point out why that might be a minor disadvantage. If you'll notice the problems involved with using this money for Alaskan development just like in Minnesota is that a loan or guarantee often becomes an outright subsidy. We found that so often in northern Minnesota. Investment risk often becomes confused with political practicalities and pressing current needs become less mandatory when viewed from the future.

I then mention here the tax exempt bonds that could be used for many of your projects. I point out that there are disadvantages from a long-term investment standpoint and that citizens do not often understand why you would put your money in investment and then borrow money. But I think they could be educated.

My conclusion, you'll notice that the last page, is that leaders of all states with trust funds recognize the validity of holding funds for the future under proper investment management. Yet many states have modified or stopped accumulating all funds during periods of low interest rates such as we experienced in the 1940s and the 1950s or when demands to satisfy current needs that seemed paramount. It is logical to hold as much as possible

for future generations, but holding any amount is better than holding nothing.

Legislators may take a course which is politically feasible in order to protect and save whatever possible for future generations of state citizens. To protect a part of the assets is better than to lose everything because of public demands for current expenditures. And I think you people are doing a tremendous job. And these programs here---you're saying we may have to spend a certain amount for current expenditures. We have to build up our government, but on the other hand I think that you're doing a tremendous job in just going through everything and looking at what other states are doing. I have copies here of some of the Minnesota statutes that may interest you.

GRUENING: What all is in here? Is this---cover all the investment statutes?

BLIXT: Our investment statutes, rule like proxy. Let me try to find the one here, I guess this is the one I have. The first page here is just the Minnesota constitution where we have an old Permanent School Fund, the words now perpetual and inviolate that I talked to you about which is interesting there.

The next page, first on page 152, you'll find the Permanent

School Fund investments. A very conservative investment policy as outlined here, 20% in equities, 80% in bonds, and only 40% in corporate bonds. So, in other words a good part of this fund must be in governments. But that includes Ginny Mae mortgages of course and we can get a higher yield there than in many other things. Then you'll notice on the next page, 153, we have a general appropriation language for all the investment programs. On page...

GRUENING: On mortgages, I just want to interject...

BLIXT: We have no mortgages allowed here.

GRUENING: OK.

BLIXT: For a very good reason. You say, why? I don't want to be the guy that kicks a welfare mother and 10 children out on the streets of St. Paul when it's 30 below zero. Everybody all wants us to buy a mortgage. We have more mortgage salesmen in the state than anything else. But I don't want to buy a mortgage unless it's a government guarantee because I don't want to make that decision.

Now, by the way, there are more people in there trying to sell us mortgages in Minnesota than any other kind of

security and they always mention that they gave \$100 to the governor's latest fund raiser. They mention that first and then they show us the mortgage. The governor told me not to listen to them. Because if it was a really good mortgage the banks and the insurance companies and others would be in there.

Now at least we could have bought the real estate. And you know real estate has done far better than stocks and bonds. In fact a year ago I talked to the Continental Illinois Bank and they said they were going to set up a little fund of farms in Minnesota, Iowa, Wisconsin and asked if we'd like to buy it. I said, oh, that's just fine. Our secretary of agriculture a few months ago, as you know, and the first thing he did was complain that some vicious corporation was out to buy farms in the upper Midwest. And he didn't realize that it was me and my equivalent in Wisconsin and Iowa and Illinois that were going to do that. So, we haven't been able to get into real estate that way. But I don't want to hold the mortgage unless it's a government guarantee behind it. Ginny Mae, yes. We tried to buy a lot of Ginny Maes of Minnesota mortgages. Do I---yes?

GALLAGHER: How about the PMI? Private Mortgage Insurance?

BLIXT: We have not gone into that yet at all. My legislature has said cool it. We do use Ginny Maes on some hospitals. We buy a few bonds which are really mortgages. Like for example one insurance company, I believe it's Gulf Life in Florida, sold a bond issue a few years ago which really is a mortgage. But they felt they had not enough analysts that they could buy some secondary securities and they knew they'd get an AA rating so we bought in essence a mortgage on their life insurance building, but it was presented in the form of a bond.

We have no mortgages in Minnesota. The demand has been tremendous, but every time the legislature looks at it and thinks that the state could be in there kicking people out on the streets when it's 10 below zero, that's the argument. They say they just want no part of it because there is enough capital in Minnesota. The banks can always get from correspondent banks in New York or Chicago, the savings and loans are very strong in Minnesota. I realize that it's an individual situation. We may get in there yet. We may have a mortgage committee. It's being talked about all the time, but we don't have a cent in mortgages today except the government guaranteed ones. We feel it is advisable and far less political.

If you want to go through the statutes, we have treasury statutes---I don't want to go into the time for the next people here---on page 155, just about---by bond---then you'll notice the

state bond fund is mentioned on page 156. The retirement system is generally on page 157. That would be our main investment statutes right there. Then we have modifications, for other funds. Like the highway bonds on page 160, the various retirement funds, the supplemental fund is on page 161, we have the income share account, the growth share account, and the fixed return account there.

GRUENING: Is your statutory framework in here, too?

The---

BLIXT: Of my department?

GRUENING: Yes.

BLIXT: Yes, how I'm set up is right in these statutes. I regret to say there is not a good order because, I bet it's just like Alaska. You pass a statute this year and it's put on the end of the chapter. And the next statute goes on the end. We really should have a modification. Yes, sir?

MALONE: Thank you, Mr. Chairman. You may have mentioned this, but I didn't hear it, Mr. Blixt. The expenditures of the investment program are appropriated by the legislature

like any other state expenditures?

BLIXT: In great detail. Yes, yes sir. Yes, they question me on everything. Frankly, I disagree with them a little bit. They tend to have more people than I need. I have one or two extra people this time that I'm not going to hire. I don't get what I need for travel.

MALONE: But it is part of the general...

BLIXT: But it's part of the budget. It's a line item, sir.

GRUENING: Does the operation expenses come from the actual investment income or what we call the general fund which is...

BLIXT: It's been coming from the general fund, but we've had a debate there. A few years ago, because the governor wanted to save on the general fund budget, he said, wouldn't it be better to take "x" amount from the highway funds, "x" amount from the invested treasurers cash, a certain amount from each retirement fund ---that would be better. That way you have no general expenditures. You're just out of income. Well, everyone said, well that's fine, but then the treasurer's fund earns more, the highway department earns more, and by the way, we ended up with a bunch of people

like this in the capitol who said, well the highway department does work for this and this, let's transfer money from all the departments to the highway department. And welfare does something for them---let's transfer that in. We decided we'd have to have a floor on the new building just to have accountants transfer money back and forth.

Now the legislature wants to question me and boy do they do it. I'll spend an hour in a session like this with a grilling of---even the subcommittees are composed of about 12 people down there. As you know we have a 200 person legislature. It's a big one. And we really get grilled on everything. But it's a line item budget.

GRUENING: What committees do you report to? Is there a specific oversight committee that you report to? What's your first---how do you go through the gears there?

BLIXT: Well, we have many gears. An appropriations--- in the House, appropriations committee, a Senate finance committee. We have subcommittees of both committees that look at my budget in detail.

Then beside that we have a House operations committee and a Senate operations committee which are concerned with general state operations. Now all the pension law, retirement

fund law, must come through the operations committee. They in turn have subcommittees. One is on---well, five persons in the Senate, five in the House that are on legislative subcommittees looking into pension law. Now those five senators and five representatives meet together, which I hear maybe you don't do here so much---I think it would be very good of the Permanent Trust Fund legislation---I enjoy those smiles, but really in Minnesota, some of the time the representatives and senators are on speaking terms, really they are. And they meet together and they've even been known to have meetings together if it's something more or less non-controversial. The five senators will say, "Yeah, I'll move ---let's go with the House members---yeah, OK." So they have one hearing together and then they go through their respective operation committees.

But that's generally the framework. Now, as I described it, I've gone before tax committees, all kinds of committees, rural committees on farming, committees on housing and everything else because when you have a state investment department, you literally end up going to every committee in the legislature talking about something.

But that's generally the framework, but it is a line item budget and we have to send it first to the commissioner of finance, then the finance department, then the staff who works for the legislature and they're rough.

GRUENING: Which legislators and which committees seem to have, if any, the greatest understanding of which your operations takes?

BLIXT: You still have---boy, this is a blunt question you are asking me to criticize my bosses, but I will. I hope there is no members of the press here from Minnesota. There used to be a group of people in the Senate and House on the pension committee which were just fantastic. They were from the banking community, insurance community and wanted to do a better job. And my first 10 years, which was very smooth sailing.

Recently we got some new people and they got in mostly on the basis of telling people they'd increase pensions. So here one of them says they'd double and quadruple pensions without thinking of actuarially accounts and feasibility and then they got in some difficulties. At that point I'd say the really rough question was supervision of me tended to go more toward the finance committee and appropriations committee rather than the pension committee.

And in finance and appropriations we have some people who have spent just enough years listing the people wanting funds, wanting appropriations. So they can just smell out something that's false. I don't know if you have that here. But soon

they can just see a crooked request on paper. Yes, they really question you. And they ask you about these policies. Is it necessary? Do you need people for this. Do you need bond analysts. Do you need stock analysts? Do you need to go to New York and shouldn't you have more of a phone bill? Do you need this subscription? God, they'll be very pointed in their remarks.

But, as you know, I suppose you have it here too, you have a few people become experts---and we also have a few people who think they are experts and they give us a rough time. We have some of those including this one broker who has his hand out and he's giving us a terribly rough time at the moment. But generally we've had very, very good response from the appropriation and finance committees. Now I've taken too long. I've gone into the next deal here. I have a lot of things...

GRUENING: If there are any questions...

BLIXT: I appreciated the opportunity...

HAUGEN: Yes, I just wanted to ask one quick question. What's the total state budget?

BLIXT: It's up in the billions at the moment. I believe it's ---the last legislative budget was about \$6 billion. For two years \$3 billion.

HAUGEN: Bi-annual? \$3 billion a year? Relating it to the number of state employees.

GRUENING: One other thing on the competition of banks for management of these department funds, is that statutory or is that regulation or is that---how does that...?

BLIXT: They set up a new finance department 4 years ago and took this power away from the elected treasurer. The finance department is now under the governor. And yes, now we must do it on a bid basis. Below this will be explained. I'm going to send a copy here to your committee...

GRUENING: Is that including the statutory material--- how the due processes work?

BLIXT: No. But I could send it to you. That is under the executive council, under the treasurer and the commissioner of finance. It's not in investment board statutes. By the way, a little bit of how we operate, I'm just going to send--- these are copies of my latest annual---or my latest board meeting. You'll notice tab runs here of every purchase, of every treasury bill, including who we bought it from and the commission. And this was given to the Minneapolis Star,

the Tribune, the Pioneer Press, Associated Press every time.

I'm going to---yes?

MALONE: Mr. Blixt, how often is that generated?

BLIXT: This board meeting is every two months. And that's a board meeting there. We also have a meeting of our advisory committee every two months and my analysts turn out this material on every stock we have which is similar to what the big bank trust departments have---we don't pretend to be in detail---like you have heard this afternoon, but I want my analyst to keep track of it. If you just want to send this around too, it shows some of that material.

I have some other information, but---oh, yes, and when my advisory committee meets, they want to know generally what's in the fund. We have a marvelous computer system so if the market is closed today, in another hour or two I can have a run of every asset I have in all the accounts. The computer is right in our office, including tonight's prices on the New York Stock Exchange, the dividends, the yields and everything brought up to date. And we give this to our advisory committee. Also, this is not real recent, it's November 4th, it's not real late either, but this is from our last committee. It's what we used there in managing funds and I think the main story we have there is we simply...

GRUENING: Is this the advisory committee?

BLIXT: The advisory committee is 10. Ten people chosen by the State Board of Investment, the leading institutional people.

GRUENING: And they're per diem---they're not full time?

BLIXT: No per diem, they get no expenses. It started a volunteer committee, one man comes from Duluth, one from Rochester, we try to give them the equivalent of a train fare. Except there is no longer a train there. They don't get much. They are on their own entirely and they've done a tremendous job. We feel it's in the interest of these financial institutions to try to keep the state in good financial order. We've never had any problems getting the best advisors in the state.

I appreciate so much the opportunity to appear here. As I say, I still don't know why I was asked. I have nothing to sell and I assure you Minnesota doesn't want to take over the Alaskan funds. I've had a lot of fun. We've had a lot of fun being here, I've talked to folks all over the nation on this. There is about 10 of us that manage state funds throughout the country that like to speak with others.

I guess you might say we're missionaries in a sense because I think we are able to accomplish quite a bit by just dealing with people. By being available to talk to legislative committees. By being available for the church groups and the Lions Clubs as I mentioned. Because whenever you have a program like this it's so important to have the citizens of the state realize that it's better to put the money away for the future generations than to spend it on them so they can buy booze tonight. And you know that's a very difficult thing to get across. Thank you very much.

GRUENING: Thank you very much. Mr. Speaker.

MALONE: Mr. Chairman, Mr. Blixt, I'd like to thank you for a very articulate presentation.

BLIXT: Thank you. It was a lot of fun being here.

GRUENING: Are you headed back to your home state or what? What are your plans?

BLIXT: I'll be honest. I'm a tourist. I get up to Alaska so seldom that when you folks were nice enough to pay a plane fare, I'm going to stay here a couple of days and see what Anchorage is like.

GRUENING: Well, welcome to Anchorage. Terry Magrath has been waiting patiently in the back and it's running a little late. Terry would you like to...?

I should say a little bit about the hospitality Terry gave me in Boston. I came up the day and he showed me around the place and he talked to me a little bit about their operation and he represents a management group that is not---it sounds pretty progressive and I would like to maybe just relax a second. Those that want to get coffee can go get it. And we'll start in just a second. Terry?

MAGRATH: Ready to begin? Well, as Clark mentioned, the reason I am here is that he came to visit Fidelity in Boston and mainly to ask us to describe to him more or less the state of the art of large institutional investing to give him a framework and his people a framework so that as you go down the line in setting up legislation for your opportunities here, you would at least see sort of what is happening.

Fidelity is a money management organization. Manufacturers Hanover---one of their functions is money management, but Fidelity's sole function is money management---that's all we do. One portion of Fidelity manages about a billion dollars in assets for a large corporate pension funds as such. The part I'm responsible for is---manages international assets for this same type of client.

Now, I'm not here really representing Fidelity. There is nothing really we can do for you at this point. If at some point down the line you are interested in seeking outside management for a particular function or something, we would be glad to participate or compete just like Manufacturers Hanover, or anything.

All I'm really here to do is to respond to Clark's and Beldon's request to more or less lay out the general framework of institutional investing more or less so you can see some of the problems, some of the structures you're going to have to face as you set this up. As I mentioned, Mr. Blixt has pretty much covered most of what I wanted to say and I'd like to cordially invite him to come talk to the Massachusetts Legislature and see if he can bring some of his efforts to bear at our zero credit rating state.

One other point, Clark did say that when he was down there that he would like me to come up and talk to you people and that if I came up here he would show me a polar bear. He promised to show me a polar bear. He then suggested that I stay at the Captain Cook Hotel and after I got to the lobby and saw that stuffed polar bear I realized why he had asked me to stay there. Actually I do want to say---this is an incredible state and I'm very personally pleased to have been asked to come up here. I think you people have a wonderful state and it looks like the way you are going you will be able to keep it that way.

About asset management, I was going to cover a little bit of the history which Manufacturers Havover has already covered. Some

of the current state of the art. And some of the trends in force in institutional investing. And I think this is an important point. You saw a lot of investment verbage today, some of the ins and outs, some of the particularly professional things that go on in institutional investment. Seventy percent of the market today is institutional investors. You people coming in with what---\$2 to \$8 billion---are going to be a very key factor in this market.

One major point I want to leave with you is that you--- this is a profession. It is just as difficult a profession as the legal profession, dentistry, lawyering, medicine, etc. You're going to have to get professional management to run these funds. There are lots of ways to structure this. You can hire it out, you can contract with an organization or you can go in-house as Mr. Blixt has done.

The second point is the trends are such that it's not so much the individual day-to-day investing that's making the key difference. What's making the difference is the policy. Setting up the basic policy under which the funds will be managed. By policy, this could be a debt-equity structure, constraints on the funds. In setting policy you are really setting the primary deterrents of how these funds will be managed. These are big bucks. A little bit of difference can make an awful lot of investment difference down the road.

In setting policy, I understand you have a legislative problem that is facing you right now. Arbitrarily limiting the investments for political reasons may be a necessity, but the penalties can be enormous. If there is any plea I would like to leave with you, it is you set the policy structure or mechanism so that you can change it somehow as conditions change.

You heard a presentation from Manufacturers Hanover which, if there is any one theme that was constant in what they said, is that investments change. There is a time for growth stocks, there is a time for this, there is a time for that. Mr. Blixt showed how he had to change his portfolio to bring it up to date from when he had the 2½% bonds. I know it's a difficult task, but I do know that if you structure the investment policy by limiting your investments, there will be a point down the road that you will really wish you hadn't.

Alright, from this point, let me go on to just lay out a little bit of the function you're going to set up. Now I'm talking about an investment management function. You can think of a little company over here--Fidelity is a company that runs investments. We have a department for fixed income, a department for equities, my department is in international securities, one group runs nothing but pension funds, etc. The components of this organization or the organization you are going to have to set up as Mr. Blixt has, or the organization you may hire out, has to have administration. Now the administration means control, the review, the

handling of the funds, the accounting of the funds.

The second major component is a planning function. And here I alluded to it---it's one thing to execute the investments. It's another to be able to plan the policies or constraints under which the investments are going to be made. Now, there are tools that are available and that are becoming available that makes the planning function a lot easier. Makes it a lot more "scientific", if you will. Access to these tools I think would be critical so that you can more or less have some independent way to oversee the evolving and planning of the fund.

And the last function in asset management is the investment management function itself. This is the staff that Mr. Blixt has or, if you hired an outside manager, this would be the actual staff---the staff that he has.

Now in today's market---and I won't spend much time because it's quite late---in today's industry, investment industry, there are two polar types of investments. Two polar types of investment organizations or ways to invest money. There are shades of gray in between. You have a particular problem. You may want to take a shade of gray. The two poles are the following: One is totally in-house. Hire a staff, hire a set of professionals. Run them, control them entirely in-house so to speak. This is the way Minnesota does it; this is the way the U. S. Steel pension fund does it. I used to be an

investment manager with the U. S. Steel pension fund. There were nine of us. We managed \$4 billion, which is in your ballpark. We ran it---we were effectively a subsidiary of the steel corporation doing nothing but managing these pension assets for U. S. Steel.

GRUENING: Excuse me, Terry. Doesn't Mr. Blikt, if I understood it, contract some of the equity out? I may be wrong, I just had the impression that there were some people being contracted by your department.

BLIXT: No. In one case we buy... It's just for information. And from brokerage houses all over the country we get all the information.

MAGRATH: In generating the information for their internal investment decisions, they will use what is known as soft dollars, commission dollars to pay brokerage houses to get research to help them in their decisions. In that extent they are.

GRUENING: It's still considered...

MAGRATH: It is still considered in-house. We at Fidelity do the same thing. We have a large in-house staff of investment analysts, but we also will use brokers to buy investment research in

certain areas that we want to have special advice on.

The other pole is the multi-manager approach. Now, this is the, by far and away, the mainstream or the current way that very large pools of money are being handled. The multi-manager approach means that you hire outside managers, usually quite a number of them, depending on the size of the fund and the purpose of the fund. You hire the outside managers to run particular portions of the fund in accordance with how you want it done. This is American Telephone, for instance. Out of the top 200 corporations, I believe there is only 10 to 12 that run it inside. All the rest use the outside management approach.

I'll go over just briefly the pros and cons of both and how they might apply to Alaska because, while Mr. Blixt's solution seems good at first blush, you may have some particular problems up here being where you are and also with the growth of the assets you may not be able to gear yourself up quite readily. As Mr. Blixt may confirm, to build an organization requires a good long period of time. You have to get the right people, pay them the right amount and give them the incentive to do this.

Alright, first off, the multi-manager approach. As I say, this is by far and away the way that is done more so than any other way. What you require here to do this would be a central administrative staff. And these must be high quality

people, people like Mr. Blixt, and a good core than understand Alaska's problems, work for Alaska, that's controlled by the limitations, etc., imposed on them---on him by you. The central administrative staff hires managers, sets policy according to the guidelines that you set, measures performance and effectively manages the managers. The managers report to them.

Say Fidelity or Keystone or Manufacturers Hanover, whoever it may be, would report to this central administrative staff, the ongoing progress of the funds. The advantages of this approach is low overhead---low direct overhead. You have a lot of flexibility. Hiring somebody is a commitment to somebody's career. If you've hired the wrong person, you have hurt yourself and the person. So it's a way to more or less rent somebody until you may get yourself better situated into knowing how you want to go. You provide competition between managers and also you can select specialized managers. Manufacturers Hanover showed you some of the areas where they are special in. There are other organizations that provide, say, real estate investment advice may be one thing. If ever you want to go international, I can show you some of the things that we do. Different managers can specialize and, as I said earlier, this is a profession you are dealing with and just as doctors can specialize in certain areas, so you will find investment managers that can specialize and do a lot better job than a generalist.

The disadvantages of this type of approach---there is a very high service cost. Investment management, just like lawyering and

doctoring, does not come cheap. You're more or less duplicating your cost in the sense that if you want to run \$4 million, they can do it with a staff, but if you're going to run 10 pieces of \$400 million, you are more or less funding each of the ten managers. Their fees are on an asset basis or a funding basis.

Administration is complex. Ford Motor Company has 25 managers. They have a staff of three people. And when we go to talk to Ford Motor Company, they give us a presentation. They tell us where we are; where their objectives are, what we have to do to hit certain objectives. It's gotten to be a very sophisticated business, the idea of matching the investment manager to the ongoing needs of the fund in itself.

And the other disadvantage is the central staff is fairly critical. If you can hire Mr. Blixt to do it, as a matter of fact, that really may solve your problem for you.

The other side is internal management. Which has already been well covered by Mr. Blixt. You are really here setting up a separate company, just like an entire investment company, except you don't have a marketing department. This company is working for you, for the state of Alaska, just like the central staff of the multi-manager approach. Here you have a staff that is doing nothing but worrying about the investments of Alaska. You have relatively low cost. Some of the advantages of this---relatively low cost. But now you've got to weigh

the cost of investment management with the difference in return. Think of a 1%---if you could increase the investment return by 1% on your \$8 billion by spending more money on investment management, I think you will find that you can pay your investment managers an awful lot of money. So cost, when you are talking investment management, really has to be subjugated to the benefit that you are getting. You really have to look at the benefits or the incremental return that you can get from buying very good management.

GRUENING: Yield or net return, is that what you are talking about?

MAGRATH: Total return. We deal in total return. You can look at it in yield for capital appreciation, but just think of a 1% increase in return on your portfolio of \$8 billion is one year's worth: \$800 million? \$80 million? This---when you look at some of the return figures and differences of yield, you apply that to \$8 billion and you are talking about a lot of money. So it may behoove---forgetting the governor's salary, forgetting a lot of things, it may behoove you to spend well to set up good investment advice. Because it will pay for itself if it is done correctly.

GRUENING: How do you go about analyzing the state of the art as you say in terms of comparing Mr. Blixt's performance to your

performance in some areas. It becomes all very subjective to me.

MAGRATH: There are very objective ways to measure investment performance. We didn't touch---Mr. Blixt didn't touch on it, but---the performance of the funds. There is all sorts of ways. You can look at this---there are services that do this. And it would behoove you, in any case by the way, whether you set it up entirely or whether you buy multi-managers, it would behoove you to have independent investment management service to look at how well they are doing. Almost an ombudsman for the state.

GRUENING: It's complicated because your time frame is important. As Mr. Blixt pointed out that things are very faddish. Somebody will say why aren't you in the stock market, look I could get this and that. And I can realize that. So are the analyses, are they sophisticated enough to give...?

MAGRATH: It's tied into policy, Clark. You have the luxury---with the amount of assets you have and the long time frame which you have---you have the luxury of being able to look longer to set up your structure or your investment policy so that you can have a better chance of maximizing your longer-term returns.

GRUENING: One of the problems we have in terms of analyzing that is that we haven't determined yet what we are going to do with the income. The constitution provides that it is reinjected in the general fund, so technically right now, all it's doing is use operating expenses. The committee will consider tomorrow, I think, just some general thoughts on what to do with it. One suggestion might be reinject it into the fund. Use some of it maybe to meet current needs, whether that's to leverage additional funds I don't know yet. It's very complicated. The governor had Alaska, Inc. So we don't have that as a criteria to measure investment policy. It's the one odd thing about this. Maybe you have a comment on that.

BLIXT: I have a comment. We have three outside firms measuring our performance. We do just as you do many different ways. One way is simply to compare us with the IDS fund and with the banks in the Twin Cities. If they fire me and went locally or went to places that they've got to hire, would they do better or worse? Then we take these overall services in which they compare us to others. Merrill, Lynch has it, Hamilton has it, Becker has it, we deal with local organizations besides.

GRUENING: Is that mandated in your statutes?

BLIXT: No. But we feel it is mandated individually because

somebody that's against our department is going to come in all the time and ask what it is. We want three different records on hand all the time.

GRUENING: Thank you. Go ahead, Terry.

MAGRATH: It is important to have an investment performance management and it can be done. And it can be done in the context of the risk levels that you have set or the ---once again the policy level which you have set.

GRUENING: Sterling, do you have a comment?

GALLAGHER: We use Becker's Services.

MAGRATH: The other particular problem you may have---and this has already been touched on---in setting up an internally managed fund that you could solve easily and it would behoove you to do so. One is that your location, while it is absolutely one of the most beautiful locations I have ever seen, is a desert as far as an investment professional is concerned. It would be difficult to have a team of good investment professionals up here. Your time frame---you have to be up and going when the markets are up and going, which is five hours different from the central market here in the United States.

You have to be in day-to-day contact with other investment professionals and have a good communication network. So, if you do go internally, you may even want to consider not having it located here. For instance, with U. S. Steel, when I was investment manager with the U. S. Steel pension fund, the corporate headquarters was in Pittsburgh, but the pension fund was on Wall Street. And it was quite important to be able to do that.

The second we have already touched on is the fees---the salaries you'll have to be paying for a good qualified staff. I was quite---I congratulate you, sir, I was quite surprised at the fees Minnesota pays. I don't know what the turnover is, they must be quite high quality people looking at the result. To get that quality of person, I think you are going to have to pay at least a few of them more than the governor. Just like you have to pay a doctor more than the governor if you had a full-time doctor on your staff.

So these two factors may prove a problem for you. I'm not sure. The other disadvantages is you have little flexibility. If you get the wrong person or the wrong team, you've made a career commitment to these people and you cannot turn them over at the drop of a hat. You build a staff---you build a business like this slowly, carefully, and make sure you have the right people and you must make sure they can work together.

The second is, I understand your asset basis will then be growing quite rapidly. That means you're going to have to be

gearing up and doing something quite rapidly. I don't know how fast you can set up an internal staff.

There is some middle ground. One way---Yale University did some years back---and that is to contract their large funds. They went to an organization and contracted out setting up their fund to be managed. In other words, the other---it wasn't Yale, it was another organization, I'm sorry. Yale did something else. But this organization went to a money management organization and effectively---the money management organization set up a separate company if you will, affiliate, that could draw on the money management organization's capability and feed this capability in as the assets grew. In other words, you really set up a joint venture. And here you have a lot of the advantages. You have a group that would be doing nothing but managing Alaska's money. You could be drawing on the substantial capability. You heard from Manufacturers Hanover just some of the capability you need to run a big amount of money. Well, this organization had that capability, so this one management organization had that capability, so that the endowment fund came---set up a joint venture and, as the assets grew and were funnelled in, the money management organization could draw from its capability to apply it to the running of these funds. It's flexible. You can terminate the deal whenever you start to build your own organization. You are not committed to people. It is relatively low cost

compared to your multi-manager approach.

That's essentially the three options I thought you had. At least the two polar options and the various shades of gray in-between. If there are any other questions. I just want to summarize by saying a couple of things.

No matter how you do it, you've got to get good professionals working only for the state of Alaska.

Number two, they have to be independent. You don't---they shouldn't be turned over, they shouldn't be under political pressure ---at least minimized as much as possible. As Clark knows when he first came to us, we won't even talk to states. With one exception the State of Oregon, which is a very well run organization. But normally, if a public fund came to us and wanted us to talk about managing, we wouldn't talk to them. Mainly because of the turnover of the personnel of a political nature. What you people are doing ---I commend what Minnesota is doing, I commend you in Oregon. Maybe it has something to do with cold air, I don't know, but you seem to be doing it quite well.

GRUENING: A mixture of hot air and cold air.

MAGRATH: The third thing I want to leave you with is that planning is getting to be a very important function. And that you ought to have some of these tools at your access to help you meld your end use of the funds, the cash outflows if you will with

the investments you have so that the two can be put on---
am I making myself clear on that? OK.

It's a bit of a digression, but there are computer models available which you can more or less model the future. Set up a lot of circumstances. What if you wanted the fund to amortize over "x" number of years? What if you wanted it to stay at a certain level or to grow? What are the cash flow buildups going to be in this fund? That's more or less your asset side. Your liabilities. What are you going to be paying out? How do you want these things to be done? Well, given these two, you can then see what the implication of various debt-equity ratios would be. What if you went all equities? What are the probabilities of getting this return "x" number of years out? What if you went all debt? What are you giving up by doing all debt or all short term cash? You'll find it will be substantial.

But no single---no two funds are the same. And what I'm suggesting to you is that there are vehicles available. Fidelity does not have one of these, by the way. There are independent consultants that have them. But there are vehicles available that would enable you to better plan the constraints that you are going to be putting on these funds.

The last point I want to make is that if at all possible, try not to put fixed constraints. If you go back in any point in history the constraints that you would have put on at

some point would have been wrong at a later point.

GRUENING: Thank you, Terry. Aren't there some constraints--- I mean, literally, you could open it up to any kind of investment. I mean, obviously, there are some constraints. Are you meaning like percentages on equity investments or what do you mean by constraints?

MAGRATH: Alright. Let's say you put in a constraint of 15% ---no more than 15% equities. Alright. Right now that might be a very politically advantageous thing to do. If you put it into a statute like that, there may be some point down the road that you may find that this has seriously curbed or impaired your investment performance substantially.

Let me give you one example that happens to be the area that I'm involved in. Most U. S. corporate pension funds have a constraint of no foreign securities. It was an arbitrary constraint put in way back when they thought it was a bad thing to do, to go into international markets. There has been a vast amount of work done that shows that a small amount of international diversification of your portfolio has a lot of bang for the buck. It reduces the risk substantially. It spreads the risk on markets outside the country. So now instead of having a highly volatile returns, you have some of it balanced in the Japanese market, the German market, and it smooths them. It smooths the return substantially. And this adds substan-

tially to the potential for your return. These are fairly technical things which I don't want to spend--I don't want into too much here, but it has now become clear that a small amount of foreign assets makes a lot of sense. As a result a number of corporations are going back and having to go through the agony of amending their trust agreements, which is a difficult thing, to allow this type of investment.

So, all I'm trying to say is if you minimize the arbitrary constraints and more or less focus on the mechanism to set policy and let that be your controlling guide, I think you'd be a lot better off.

GALLAGHER: You talked about foreign investments. Do you think it's appropriate for public funds to have this option?

MAGRATH: Would there be an emotional bias against it? You mean to buy options or underwrite options? A lot of U. S. corporate pension funds are indeed underwriting options. Yes. Now five years ago that would have been an anathema. There may be a place for options. There may be a place for private placements. I don't know. But at certain times this may make sense. Markets change. The options market was not available to pensions five years ago because there was no options market. Now there is a viable options market and some of them are good.

I'm not saying it's appropriate. We don't do it. But some are seeing it as an appropriate investment.

GRUENING: Doesn't the rule of diversification---it's a principal that comes up---require limitations in these areas anyway? As long as you are stating---maybe restating the rule of diversification---it may have some political value. And it may not hurt. There must be some point where you are violating the investment policy to put a lot of money in the stock market. I mean a high percentage. Especially if it's money that has to turn over. Now, there probably is a bias in this state even though pension funds are invested in the stock market. But I'm wondering---isn't there the rule of diversification requires some limitation anyway? Even though it isn't stated statutorily?

MAGRATH: No. The rule of diversification almost implies the opposite. If you really truly wanted to diversify, say in equities, you would have 60% in the United States market and 40% outside the United States.

GRUENING: OK. Does diversification cut across investment categories?

MAGRATH: In other words, here you are looking at two different things. If you want to buy, let's say 20% you want to be in bonds,

80% in equities. OK. That's a policy decision. And inside these two classes of securities, you want to diversify. For instance, you wouldn't want to buy one bond.

GRUENING: No. I understand that. But does good investment policy---doesn't it demand in terms of classes or types or kinds of investments that only a certain percentage go into it? I mean, I can see you can diversify your equity holdings, but if they are all in equities, they are not very diverse within categories.

MAGRATH: One way to handle this is to put outer limits and allow a shift. You saw Mr. Blixt's presentation. You saw a big change in the various mixes as he went through time.

GRUENING: That's what I was talking about. No more than a certain percentage now. What is the outer limit?

MAGRATH: Here is briefly just a Xerox just in case. This is how we have allocated assets around the world over the last two years.

HARGEN: Let me ask a question right now. Are you saying that you don't---I may not understand you---are you saying that the legislature shouldn't put a straight jacket on the way the

fund managers operate? There ought to be some---I can agree with that. But sometimes I think I'm by myself. Everyone's got different ideas. You get the emotional problems and everything built in to---that's talking---just like here you would say why don't you invest in capital markets. I'll just use myself as an example. I spent four years and eight months fighting the Japanese. I'm not that inflexible but now I did feel that way.

MAGRATH: This chart shows how we have invested assets around the world over the last two years. The basis chart is in color. I'm sorry I couldn't get it reproduced that way. On the left and right columns you'll see a neutral position. Instead of a constraint, we have a neutral position here. In other words, that's a preferred position. We can deviate from that position. As you travel through here you will see the international situation very clearly. You can see the Japanese---we've moved above a neutral position in Japan and then in the late---late '76 there was a major run up in the Japanese market which we participated in. You can---backing up you can see France. You can see the political problems that developed in France and we pulled out of France. Certainly you wouldn't want to have any constraints that says you couldn't be in France. Because if ---you'd be sitting there with the potential of having all the money absconded by the Communists so to speak. Then the political situation changed and over here on the

right we start to build a French position. What I'm trying to say is, instead of setting constraints on our international policy, the same things goes for our domestic policy, we set a neutral or preferred position and then can deviate within bounds. We'll go maybe twice a weighting in any one particular country. But by setting bounds you are allowing a manager flexibility to work within a framework.

GALLAGHER: Do you usually go in U. S. dollar denominations securities or...?

MAGRATH: Oh no, these are yen and duetchmarks or whatever. These are the investment capsules. We have a staff in Japan, a staff in London, etc. But this is just---I'm not suggesting international securities for you at all. This is just an example of...

GALLAGHER: If we allow under our statutes that maybe U. S. dollar demoninations...

MAGRATH: Well that's not really---Canada follows very closely to the U. S. and we are really not diversifying very well. The Canadian market and the U. S. market are very highly correlated. We are much better off to go in Japan than in Canada. That's another issue. Once again, I'm just doing the

international thing just as an example of something way out in left field to show that if you set constraints you may wish you hadn't at some point down the road. That's all I have unless there are some more questions.

GRUENING: OK. Are there any questions? Terry, thanks a lot. Thank you everybody for going through there and bearing out this room. It's rather stuffy and hot. We'll be in adjournment until 9:00 o'clock tomorrow sharp and we'll start on the---recess until 9:00 o'clock---and take up a piece of draft legislation.

Proceedings
of
The House Special Committee on the Permanent Fund

MINUTES TO MEETINGS

Anchorage--July 16, 1977

Kotzebue--September 17, 1977

Juneau--October 20, 1977
(Public Hearing)

Juneau--October 21, 1977

Anchorage--November 19, 1977

Anchorage--December 12 & 13, 1977

Rep. Clark Gruening, Chairman

Rep. Terry Gardiner, Vice Chairman

Rep. Ernie Haugen

Rep. Russ Meekins

Rep. Bill Miles

Rep. Leo Schaeffer

Rep. Rick Urion

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice
Chairman; Russ Meekins, Bill Miles, members.

Mr. Dick Haggart presented long- and short-term revenue projections (July 7 and July 14). He also spoke on the tariff.

Mr. Jim Edenso gave a report on investment of permanent fund. At this time it is in excess of \$4 million. There are treasury notes invested in \$3 million plus and the savings account has \$928,259.21.

There was a discussion and suggestions on the brochure. A wide distribution and summary of two reports were suggested. Committee members were advised to bring comments, suggestions, and changes to the staff's attention the first of the week so the booklet can be sent in to be printed.

Rep. Terry Gardiner gave a short account of renewable resource development.

The budget's allocation for consultants' fees was discussed. When a contract is proposed, it will be circulated to members of the committee.

The budget will be discussed in greater detail at the next meeting.

Tentative meeting schedule was approved.

It was suggested and agreed to that members send monthly budget reports.

Mr. Jim Edenso discussed the A. D. Little contract.
Any concerns regarding this contract, let him know and
he'll revise it.

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice Chairman; Russ Meekins, Ernie Haugen, Rick Urion, members; Senator Pat Rodey, Senate Permanent Fund Committee Vice Chairman.

The meeting convened at 10:00 a.m. The first order of business was public testimony.

Mr. Ed Bohnert, counselor with the University of Alaska Extension Center, testified on sources of energy for the Kotzebue area, including a windmill being installed at the Extension Center. His testimony pointed to the high cost of petroleum-based fuels in the Kotzebue region and the potential benefit of developing alternative energy sources in that region.

Mr. Marty Straus, environmental planner for Mauneluk also testified on alternative energy sources, including a pilot windmill at Kivalina, steam generation at Kobuk and geothermal potential at Kotzebue. In answer to a question from Rep. Gruening, Mr. Straus gave a brief outline of fisheries potential in the Kotzebue region.

Mr. Charlie Edwardson, Washington representative of the North Slope Borough, testified on management structure and investment goals of the Permanent Fund. A transcript of Mr. Edwardson's testimony is attached.

Following a lunch break, Mr. John Schaeffer, president of NANA, testified on his corporation's experience and investments it had made within the region. The main investments had been

in a hotel, wildlife museum, and jade processing operation in Kotzebue. These, Mr. Schaeffer said, had been subsidized by the corporation's profits from other investments outside the region.

Rep. Gardiner presented the Renewable Resources Development Fund subcommittee's first interim report and discussed the "leading edge" theory and the subcommittee's work plan.

Dr. Belden Daniels, committee consultant, presented his paper Models and Options for the Alaska Permanent Fund: Functions, Regionalization and Accountability. Discussion followed, during which Dr. Daniels pointed to the latter portion of the report which detailed accountability problems of existing development banking structures.

Rep. Gruening then moved that he would direct the committee staff to begin preparation of draft legislation structuring the permanent fund. The motion passed with unanimous consent. There followed discussion of the committee's schedule.

The meeting adjourned at 4:45 p.m.

EDWARDSON: The basic point of development in Alaska or any other place in the world is that somebody has always had to finance it--wherever, that's where it came from. All the way through the development of man, especially Western man, the only thing which did not change even when you went to war was the financial arrangements that were made at the time that war had commenced. The victor always had the financial institutions with him.

What does this have to do with state of Alaska? It has a lot to do with it. For the simple fact that prior accumulation had, prior savings had, vested in certain individuals in Alaska, whether we like it or not.

The opportunity here that the state of Alaska has is not so much who is going to be a manager of this portfolio, but how is the citizen going to have a role in the financial infrastructure of his citizenship? This basically means what types of access will the citizen have?

Although the standard of care and the standard of conduct for according and recording, I feel at this time, is quite sufficient, the thing that I would recommend very heavily is the simplicity of a financial statement, not its complexity.

When the history repeats itself more than once and it has its own weight and its own inertia, and when you look at society, it says who does the public take care of? In the past, our history of our welfare program in this country emerged from

communities--that it was communities that took care of a few marginaly cautions, and the cities and then they find the way to a state program. The most important thing and the potential that the state of Alaska has is are we at the political development in time when capitalism can be a birth-right? Or are we going to selectively, through regulation, discriminate and create a social elitist managerial class in this state?

The dynamics of a corporation as a tool are, and still is, probably the most creative tool that is available to man at this time. The success allowed capital venture in the state of Alaska will depend upon acceptability--acceptability to the citizens.

How does one arrive at this point--the state legislature at this time is responsible for the administration of the public good to all of its citizens. What is the meaning of public good? The meaning of public good means that you have a public manager. Although the public manager may be at fault in realignment of the economy by the political process, best friends and best relatives, is how our political economy in America has been social.

Today that is no longer an acceptable mode. The gap in America--although we have recognized that there is poverty--is how one gets into that state of mind, that state of consciousness, which is totally intolerant. The way that it has arrived in the past is that in an arrogant,

organized society that those that have the ability to be organized, to get organized, always come into par with the rest of society.

Not only do we see poverty of the mind in rural Alaska but poverty of organization. The state of Alaska, at this time, is one hell of an underdeveloped organization. We are charged with very little responsibility and obligation, yet we fail to give to our citizens the basic desires, basic needs.

How does this affect our citizens? The thing that is most pronounced is a very archaic administration. Very few groups of people in Alaska regulating the conduct of enterprise, and not only do we have constitutional problems, but in order for our citizens to be fully endowed, this endowment must come from the constitutional genesis of the people in Alaska. The current wealth in the state of Alaska is being handled haphazardly in the eyes of the public good that if a corporation can lease 'X' areas of land that the loss, significant loss, has already occurred, when ownership of the citizens gets wasted to few friendly corporations.

In order for the Permanent Fund, I feel, to be successful in Alaska the citizens that it's supposed to serve must have a propriety relationship to the fund. Not only must the governor be accountable, but all of its managers must be accountable to all of its citizens, not just an elitist managerial class who are able to shuffle the paper and foster more intolerable situations called corporate fascism in this state.

The responsibility and the opportunity is to develop a portfolio of citizens with a capitalistic class, capitalistic mode. What we have done 200 years ago means no longer self-sufficient, that we must then accept this greater right to capital--to all of our citizens. It's the total portfolio of this thing that whatever gets appropriated in the name of the public good must also have a proprietary class meaning. Direct ownership to that community, to that citizen at that village of Anchorage so that the citizen of Alaska will have a direct law of acquiring capital even though it may be an improvement in the community. How does one create enough administration for this? The first form of creativity--America is quite ruralist in its capital financing development.

We have had not had a change because the only experience that one follows throughout the world has been a multi-national bank. The banking model, I feel, is so tyrannical that it leaves us very bad, leaves humanity in great masses behind. Therefore, it is very hard to fill the American image elsewhere--throughout the world.

The Permanent Fund in Alaska must have a character of a community; the community not feel elitist managers who are saying, 'we will now do it for you.' And this growth and this evolution, if you take a total fabric of the community in Alaska, the highest cost of any administration in Alaska is energy development. If we worry about what we are going to do about our natural resources, when is the state

legislature or a would-be governor going to treat its citizens as a producer not as a payer. Not until we are able to give a hope to all of our citizens in relationship to capital producing instruments by a constitutional convention. The present underclass society, the other class, whether it's black, white, Native is still growing at a rapid rate. We still mean that there is some fraudulence in our structure, in our system, which we can no longer shelter and leave it for the banks and the corporate directors. The same conduct and the same potential for insider information of the insider run away with this type of portfolio are still too great, thus leaving the citizen back in his original deplorable state.

When you impose a limitation, such as to own and acquire portfolio to those capital producing infrastructures, that tells me that we are going to have that fault. That means that the very country, very state who is probably incongruous with its natural resources and had lost its managerial decision because Alaska has lost its lease hold does now have a different manager called Exxon Corporation or Standard Oil of Sohio who is not interested in how your community infrastructure gets developed. But whose vested interest is to ensure the political weakness of the capital producing infrastructure? And the experience of this model is done already in the North Slope Borough. We should make conditions upon the state leases,

that no oil company, no U.S. corporation or any other corporation go after the taxing authority of this municipality.

Otherwise those that have ability to be organized make a policy mobilized field and thus leaves a great gap of poverty in Alaska. Although it was done in a fashion of public good. The greatest weakness of our annual appropriations and the fallacy is that under the designs of public good, those that always have the access to further reach the benefits.

So the nature of the plan, unlike any other state, the state of Alaska need not to lease these resources. But it can buy back at least other land. The Permanent Fund, as I view it at this time, can be that holding company that the state of Alaska has for all of its citizens in a proprietary class, making all of its citizens capitalists to gaining those benefits which the federal government is going to lease the land anyway.

So the state of Alaska is in the business. The grand public fraud that has been committed by the public officials is self-denial while the state of Alaska is in the business. We are in the business of oil and gas. Why have we denied an appropriate conduct of our...and the necessary standard of care and conduct? When the state legislature must have a proprietary relationship to all of the wealth that state of Alaska has and the biggest problem of the past that the state of Alaska has failed to realize is that we can escape to the biggest bandit in town,

the Commissioner of Natural Resources, who has the necessary technical infrastructure to give the resource away at the cheapest cost possible and therefore create a thing for your people and class who already have.

It therefore makes socialism for the few possible and makes capitalism for the masses impossible. And how does one view its citizenship or is that no longer a sacred thing? Have we substituted a managerial class and put our citizens at the back door--I feel this is very dangerous.

There are controls and unless Alaska defines its communities, what type of community we are to have and who lives in that community, we are going to fail, and still have this type of greater population, dislocation. Once we develop an infrastructure where a citizen can always benefit, not in lieu of service, but in capital formation. I feel that the time has come where we must look at basic definitions and see if community-owned citizens' banks, infrastructures can be developed. Then the chances for fraud, when one has inherited equal rights, diminish. Where accountability is too fine. When you are equal on paper, on statute or in the constitution, that the chances to find a basic violator are higher than the present format, that is you are administering the public good, which you can get away with and rationalize that under the prior proposal that the Tesoro had the best proposal, although it was bad, but it was still the

best proposal, therefore, we had accepted a bad portfolio to start out with, with all the structural problems and because that something has made, therefore, that this type of a public trust because socially respectable and correctable.

The only way, I feel, is that the state legislature must have a greater control on the proprietary of this public resource and not making it into a class of public good where anybody in the governor's office, the governor. And the chief executive of Alaska, at this time, is the largest single one-armed bandit in the state of Alaska. In this light I would not seek to give higher sanction to the governor.

I would highly recommend to the state legislature that they would vest a veto power in those classes of proprietorship of the management of all of the citizens' portfolio. The biggest problem that we have in this state is our chief executive does not know how to administer, not only that but we also have a place for the strongest tyrant in a democratic process to exist in Alaska is governorship of Alaska. That there is no governor in all the 50 states that has the powers that our governor has. It is amazing that practitioners of that office have not totally given our state to be tapped by others, but it is, and I hear sounds that you must be of stock to come in and manage, that the best experience is from the biggest voice, which I don't feel is the case. The best experience I know of and have always vested in the people

that the proprietary of the fund must go directly back to the people not to any managerial groups and that none of the commissioners or the investors of this fund should not serve in any other capacity but for the fund to manage the portfolio of the citizens of this state. The chances of insider information, I'd say, is too high, too great. The concept of the Alaskan Native community must be clearly defined, otherwise that instead of--I see if your procedure becomes in the technocrats' hands, such as an investment portfolio from our biggest threat, apathy, that the chances of that experience are equally great.

So, therefore, I do not think that the exception of a rule just because the guide was successful in managing a portfolio in Peru creating corporate fascism. I feel the same advisor is equally dangerous to the state of Alaska, Milton Friedman. His experience is a classical one that one must not forget, that corporate fascism and corporate capitalism are the same when you have a very strong managerial chief running the portfolio.

I would suggest a permanent committee in the state legislature whereby the legislature and the governor achieve parity. Without that, that the fund will still go to those few and friendly few unless that the populace have a majority and have the control. I would not, I would have a majority of the citizens versus majority of man. I do not trust managers. That the conduct for legal managing has--is in

the books--has always been slammed. And while limiting to capital-producing infrastructures in the state of Alaska that means that Alaskans arbitrarily have cut their noses off and say that I am, now that Alaskan wealth has changed managers overnight--that it is no longer the Permanent Fund; it is now back to the top 500.

The state of Alaska will be buying back, must buy back, and must invest its wealth on federal lands in the state of Alaska. The Permanent Fund must be prepared to find more oil in the outer continental shelf. It must make funds available, necessary so that all of the citizens can grow with the development of our country. If we cannot make--the state of Alaska, as you well know, we've got the coastline. But the coastline has been auctioned off to the largest multi-national corporations already. It is because that the citizen has lost a proprietary relationship for that resource. It is because that the color is under public good, therefore, that the citizens do not have a direct relationship, a primary relationship to that resource. If we develop a proprietary class for its citizens for state of Alaska in whatever development or investment at this time that I see chances of saving ourselves to the maximum benefit of all of our citizens, not just those who have the ability to be organized.

I am for controls. If the controls are to exclude citizens, as far as I am concerned, that is an unconstitutional

assault, a very direct violation. The citizens' access to this resource, I would say, and the state legislature proprietary control--not the governor. I would vest the proprietary of the fund in the state legislature and go fight the governor. Thus it would make administration checks and balances a lot easier then. I would feel safer if Ernie would have more a say-so on the Permanent Fund than Hammond himself.

GRUENING: So would I. Charlie, thank you; can we ask a question or two?

EDWARDSON: Sure.

GRUENING: You mentioned the Alaska community having problems with the corporations. How do we define community in a way that includes everyone? Should it include everyone in the world?

EDWARDSON: The most significant development in defining community that is occurring throughout this world has occurred in Norway. The Norwegian government, at the time of development of the North Sea, the Norwegian government took the lowest denomination of sovereignty in Norway and examined it, lowest denominator of sovereignty and the best unit,

administering unit, known to Western man has been family. I would say it is high time in state of Alaska that we attempt to actualize in ourselves what is construction and maintenance of Alaskan family and what it means. I see a chance for the first time to develop an actuarial analysis of what constitutes an Alaskan family in this state and to arrive at parity. If state of Alaska is to remain intact, its citizens must have parity and the citizens of state of Alaska should only accept parity, not dislocation.

This means parity in construction, parity in service, which means it may cost more. It may appear to cost more, but in the long run, if you have parity, it has a high survival rate. The basic needs and the basic expenditures which we are going to have is still going to be energy. We already know what those basic components of a community are.

This is 1977 and all of those charges and all of those assumptions of responsibility have not been met, therefore, leaving the state very vulnerable to internal attack.

And although it is beneficial to another segment of the community called lawyers, that the dislocation of its parity of services still is intolerable and with equal access and to arrive at parity, then I say that if this type of dislocation occurs, further occurs, that I see a disintegration of Alaskan society. Not just Native but total disintegration of heavy regionalism. Regionalism occurs structurally because of numbers, because of the nature of administration of public

good gets executed in that fashion because there is no proprietary relationship. If you have proprietary relationship in equity, you will have justice.

RODEY: Charlie, what sort of intervention do you think is appropriate in the economy of the Northwest by the Permanent Fund?

EDWARDSON: I cannot speak for the Northwest. I can speak for what we see in the Arctic. I see the chances of international development in Alaska. Not because of Alaskan resources. State of Alaska has underexamined its strategic location in the universe. State of Alaska is in probably the best location and let's examine strategic positioning of international trade and put Alaska in the Arctic Ocean. If we are to, say, I would propose for the sake of conversation, I am now going into a submarine transportation business, nuclear subs with very large capacity. Maybe all I need is one or two. The 21-day savings, 21-day transportation costs are closing the gap in the Pacific Ocean. The value of Alaska's position in international commerce and the lack of facilitating the hook-up. What happened to Alaska in 1951 has revolutionized the whole commerce of the world? What happened to Alaska in 1951 was the first SAS trans-polar flight occurred. Overnight that, say 22 hours of flying time all over the world that instead of 26 at that time, they made it to 11 hours.

When you put this, state of Alaska is already in the transportation business. When you take a look at the marine development, our potential, as I see it in Alaska is not so much the land but the estuaries. The greatest breadbasket in the world, if we were to keep our estuaries halfway clean, halfway decent, is Alaska in the protein business. And the scale, the present archaic scale of how we used to view Alaska and how it is presently viewed at this time is totally unacceptable.

We must develop a psychology for who we are, where we are from, and state of Alaska, as I see it at this time, can get into an international commerce, international trade of not going through Panama, not crossing Atlantic Ocean, not crossing Pacific Ocean, not crossing Indian Ocean, but crossing our own ocean where it cuts down traffic as long as 23 days. This 23-day savings is sufficient capital saving to go into that type of development but in terms of our community that the citizens in the street must become an owner to a community based infrastructure.

I feel that by getting these numbers--you know, we play number games--we all have a bad habit of that, and it has limitations and what state of Alaska needs at this time is an actuarial analysis of its citizens. With an actuarial analysis, we will learn from this incidence of disease, standard of care where our community vulnerabilities are.

If you have healthy people, we also will have healthy economy. If your people are sick, if your citizens are sick, your economy will also be sick. There are two financing models which I feel should be looked at--is amazingly well is Hydro Quebec. Hydro Quebec is the world's largest utility company. I would like to see state of Alaska come into that class of proprietorship--selling power to the world. Hydro Quebec is so successful that it can finance the government. It is the only situation that I know signs the bonds of a government--than the government signing a bond for Hydro Quebec. So when a state that is already in the business, if they really want to become experienced, the Hydro Quebec model is very good. On our oil and gas activity, a KOB0 leasing model is very good. That is a financing technique where investors pool--like you and I pool our monies together and get an outer continental shelf lease. It is a little more complicated than that, but it is a direct line where a non-technical development can get into oil and gas business without buying unnecessary overhead.

HAUGEN: Where do you have access to the two models you are suggesting--Hydro Quebec and KOB0?

EDWARDSON: I can make them available to the committee. I don't have them here with me. I got them at Washington, so I will be going back probably around the 24th.

HAUGEN: Will our staff be able to acquire them through you?

EDWARDSON: Sure. And the other model that is quite interesting is U.S. Steel in Ontario. Why that is interesting is U.S. Steel provides the coal and Ontario provides power to U.S. Steel. It is a very interesting model in terms of financing large scale industrial activities and also financing power so Ontario and U.S. Steel financing techniques have lots of flexibilities. It warrants attention. Ontario and U.S. Steel are in the power business. It may work very well in this state because there are some areas where there is a lot of coal and mining industry, as we all know, is well. One of the things, one of the bad policies we got a lot of bad habits in our government. We have even had to become practitioners of bad habit especially in large scale energy development.

We have a psychological problem that we must take something to the community and the best type of development, as I see it, is at the resources and not taking the community and, which I was happy to hear, it was realized by Fairbanks that the community infrastructure, the social governmental capital to provide sewer and water was more expensive than all of the total, that the secondary community infrastructure got work and it still will be burdensome. The state legislature will still have to pump in more sewer and water. This is why that

I always suspect portfolio managers and always suspect bankers. So if I was in the state legislature, man, I would go after the power that the governor has and vest it in the people, vest it in the state legislature, that is probably the most significant fact that the permanent fund committee can have to have a portfolio run by citizens who do not have loyalties to prior practice, that the chances of an investment banker being loyal and his chances of loyalty will not change but will have an expeditious intercourse with that prior practice. I feel it in Alaska has proven itself to be continuing practice and have not seen to exist but now that I see instead of what used to be for people now.

GRUENING: Thank you, Charlie.

PRESENT: Clark Gruening, Chairman; Russ Meekins, Bill Miles, members.

After a break for lunch, two letters were read and public testimony was heard.

The American Association of University Women delivered a letter asking for consideration for allocating part of the income derived from the permanent fund for the support of cultural facilities.

The Juneau Lyric Opera Association also presented a letter. They request priority consideration and affirmative action in funding cultural activities for municipalities.

Ms. Shirley Rediker, state coordinator of the Cultural Facilities Development Committee, suggested that income from the permanent fund be used for cultural facilities. Ms. Rediker stated that the state had a great need for places for performances, art exhibits, artifacts. She gave an account of several communities' needs for the facilities and offered to furnish the committee with more information if desired.

Mr. Eric Hanson spoke of Alaska's need for education on such things as aquaculture, arctic health, arctic research, mountaineering, skiing, general aviation, fishery science, and hatchery science. Mr. Hanson suggested that institutes be established in the above areas with educators with excellent qualifications--that could draw

international interest. Loans to students with minimum interest charged was also suggested by Mr. Hanson.

He encouraged flow of information to the public as the permanent fund committee progresses.

After a short break Ms. Allison Horton, representing the Audubon Society, stated that the society is more in favor of shifting the money to out-of-state investment than they are of a development bank. They believe that saving it for a future resource is the best.

Ms. Horton did suggest research be done on energy, technology research, alternative sources of energy, establishment of a state office of technology, recycling, and transportation alternatives.

Mr. Doug Pope and Mr. Bill Berrier discussed separation of powers--Bradner vs. Hammond.

Mr. E. O. Brackins, development specialist for minerals in the Division of Economic Enterprise believes there is too much emphasis on renewable vs. non-renewable resources. He thinks that mineral resources are renewable--renewable the same way a farmer's field is renewable. As you go in depth, the resource expands. Mr. Brackins suggested investing with a resource company (using Quebec as an example).

The meeting adjourned at approximately 3:00 p.m.

PRESENT: Clark Gruening, Chairman; Russ Meekins, Bill Miles, Leo Schaeffer, members.

The meeting convened at 9:00 a.m. The first order of business was White Weld's report.

Mr. Robert Greeley gave the recitation for White Weld on a study relating to descriptions of principals and management of trust funds, principals of various types of trusts. The study includes Wisconsin and Minnesota, as well as a series of investment funds. Also included in the report are the following: organization in management structure, description of different types of corporate securities, money market instruments, investment performance, and a listing of different criteria.

Dr. Belden Daniels discussed the development bank and existing loan funds with the committee.

It was agreed that the draft include a finding--there should be no duplication of already existing loan funds.

It was agreed to capitalize the development bank out of the permanent fund.

A separate paper of alternative approaches to accompany the bill was agreed upon.

The proposal was made and approved to raise the contribution rate to 30%, taking 1/6 of that to capitalize the development bank. The remaining 5/6 would be used to capitalize the investment function.

COMMITTEE MEETING
Capital Building, Juneau

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To keep the three commissioners on the Alaska Enterprise
Investment Fund Policy Board was ratified.

The meeting adjourned at 5:30 p.m.

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice Chairman; Ernie Haugen, Bill Miles, Leo Schaeffer, members; Hugh Malone, Speaker of the House; Alvin Osterback.

The meeting convened at 9:00 a.m.

The committee agreed to adopt the bill which was presented as a working draft. The bill creates the permanent fund as a separate trust investment whose sole function is a high grade investment money-making vehicle. It also creates an Alaska Enterprise Investment Fund to invest in financially-sound medium and small scale enterprises.

A note was made of the Alaska Enterprise Investment Fund inadvertently called the Alaska Development Bank in several sections of the draft. The changes will be made.

The following changes in the draft were made by the committee:

To drop the words "in the Department of Revenue" in Sec. 37.13.010.

To change Finding 2 to read: "the primary goal of the fund should be to maximize total return while maintaining safety of principal;"

It was decided to define capital gains as return to capital and not as earnings and to add language allowing the trust fund managers to spread gains and losses over a five-year period.

Finding 4 was deleted.

Rep. Gruening suggested that something be drafted for use of the income of the fund. His suggestion was to re-inject 50% of earnings back into the permanent fund; and use the remaining 50% to finance alternate energy development--hydro and other non-fossil--to be used to secure a lever of private financing with capital gains returned to principal. It was agreed that the committee members would consider this suggestion.

After a short break, the following changes were made:

For the next meeting, the three-man board of trustees is retained. Staff to draft language putting operation into effect when a total of \$50 million accumulates in trust fund.

Page 8, line 19 to be amended to general language to chose persons to perform services.

Language to be added to 37.13.160 to show performance based on goals and objectives.

Section (f) on page 8 to be rewritten by staff and advisors to allow broad manager discretion.

Operating budget on page 9, lines 13 and 14 to come from general fund.

Language to be added to page 8, lines 5 and on to compare trust fund performance to institutions of similar size.

After a break for lunch, the following changes were made in the draft:

Section 44.55.010(b) will be changed to be consistent with permanent fund heading (Sec. 37.13.010).

Finding 3 under Alaska Enterprise Investment Fund be re-written so that it is not limited from working with federal agencies.

Finding 2 under Alaska Enterprise Investment Fund be written to modify enterprises, small and medium scale, productive, private and community development enterprises. (The same language will be used each time "enterprises" appears.)

The Finding and Purpose sections will be broadened from the limitation of private sector and will allow the community development sector in both.

The commissioners are removed from the Alaska Enterprise Investment Fund Policy Board and one member from the executive branch is added. Also in that section the language will be changed to "six public members appointed by the governor with due regard to geographic location within the state--two of which have broad investment financial background and two have broad experience in community and regional development." There will be one governor's appointee (a voting member) who will be responsible for coordination with other funds. In total the board will have 7 voting members. The terms will be four-year staggered terms.

"The chairman of the governing body of the renewable resources development fund serves as chairman of the policy board but is not a voting member" is deleted and that section will state that the board elect a chairman.

In the section dealing with the quorum of the board,

the sentence "decisions of the board shall be taken by a majority vote, including not less than a majority of the appointed members" the sentence will now end after "vote."

The monetary amount board members receive will be blank.

The section on the investment committee is to remain the same until the next meeting.

Operating budget will be specified in the section pertaining to the investment fund's budget.

The investment fund has the power to borrow up to 150% of its paid-in capital--changed from 50%.

The investment fund may not undertake any new investments till its paid-in capital reaches \$50 million.

The permanent trust fund will invest the idle cash balances, of the investment fund as a separate account, in such a manner that it will meet the cash needs projections of the investment fund.

"Purchase currently sound evidence of indebtedness from the tourism fund, the agricultural revolving loan fund and the small business development loan fund if the loan was made after the effective date of this Act and if the loan meets the criteria of sec. 120 of this chapter" will be eliminated.

The membership of the State Investment Oversight Committee be changed to the President of the Senate, Speaker of the House, and six other legislators, two of whom must be minority.

The meeting adjourned at 4:45 p.m.

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice
Chairman; Ernie Haugen, Russ Meekins, Bill Miles,
members.

The meeting convened at 1:30 p.m. The first order of
business was a report from the Institute of Social and
Economic Research.

Mr. Lee Gorsuch and Mr. Scott Goldsmith presented a
summary of findings from research over the past three months.
Included in the report were the following four points:

1. Looking at effects of varying contribution levels of
the fund.
2. Looking at uses of the fund.
3. Examining alternative types of investments of the
fund.
4. Looking at what happened to in-state placement of the
\$900 million bonus monies received in 1969.

Mr. Bill Berrier reviewed changes in the draft bill
from the last meeting.

The meeting adjourned at 5:00 p.m. and reconvened at
9:00 a.m. the following day, December 13, 1977.

The following changes were made in the draft bill:

To drop the word "state" from State Investment Over-
sight Committee.

Rearrange subsection (f) so that the first sentence is a separate subsection; re-letter subsections following. (Page 8, lines 24 -25).

Add word "surplus" to sentence deposit surplus funds, or invest surplus funds through the permanent fund in such obligations as it may determine; (page 16, line 19).

Change language in subsection (3) to read, "review periodic reports from all other agencies of the state performing lending, borrowing and investment functions." And in (4) to read, "present a complete report of all other agencies of the state performing lending, borrowing, and investment functions."

Draft a findings and purposes section for the Investment Oversight Committee.

Under staff of the Investment Oversight Committee add Legislative Finance Division and in the same section add "or contract for services" after "the committee may hire."

Add "financial and economic planning" on page 2, line 22 after the word "fiscal."

In the duties section the language will be altered to give overview of long range fiscal planning, prescribe procedures.

Finding 3 (page 5) changed to "the permanent fund should be used as a savings device managed to allow the maximum use of disposable income from the fund as needed for purposes designated by law."

On line 8, page 5 add "with respect to fund established in this chapter."

The term of office of the members of the board changed from three years to four years.

Section dealing with qualifications of trustees in (c) remove words "be knowledgeable" and substitute "have recognized competence and wide experience."

Changes in removal and vacancies to be consistent with salaries, etc. Pay is \$250 as an honorarium.

State \$250 per meeting day in compensation of trustees.

Change language in section 37.13.040 to "ALASKA PERMANENT FUND CORPORATION BOARD OF TRUSTEES. There is established the Alaska Permanent Fund Corporation Board of Trustees. The corporation is a public corporation and government instrumentality in the Department of Revenue managed by a board of trustees but has a legal existence independent of and separate from the state. The purpose of the board is to manage and invest the assets of the corporation in accordance with the guidelines established in this chapter."

The Alaska Enterprise Investment Fund Investment Committee changed to Corporation Investment Committee.

On page 8, beginning with line 15 (f) is changed to (b) and the lettering altered to read, "(b) The corporation assets shall be used only for income-producing investments. (c) The board shall seek to maintain a reasonable diversification in its investments unless under the circumstances it

is clearly prudent not to do so. (d) The board shall submit long-range and quarterly investment reports to the Investment Oversight Committee. (e) The corporation may not borrow funds or guarantee the obligations of others. (f) The board may enter into and enforce all contracts necessary, convenient or desirable for purposes of the fund except it may not contract with agencies of the state."

On page 8, line 8, changed to read, "fund assets. The prudent man rule with respect to making investments means the board shall exercise" and continue with the rest of language.

On page 8, line 29 add the word "full" before "faith."

On page 9, line 5 delete after "used" to the word "nor" after the semicolon on line 7.

On page 9 delete from line 15 through line 4 on page 10.

Insert new section on averaging income to read "the board shall establish and from time to time as needed modify guidelines for the corporation's assets. Prior to adoption of any guidelines the guidelines shall be reported to the Investment Oversight Committee for review and comment."

On page 9 delete section (2) and insert language limiting investments to no more than 30% in stocks.

In the section concerning audits (page 10) the Legislative Budget and Audit Committee is changed to Oversight Committee. Language for outside audits in all three funds is added.

Under the section concerning reports and publications the financial statements will be audited by an outside CPA in lieu of the Legislative Budget and Audit Committee. Also in the same section the time frame for reports requirement is changed to 90 days after the end of the fiscal year.

In section 37.13.010 add language to have money paid in at least monthly.

A transition must be added for transfer to permanent fund of monies now held by the Department of Revenue.

New language for conflicts of interest will be written to state a member or employee acquiring a conflicting interest shall disclose the interest but does not have to disqualify himself.

Add transition section for both corporations.

Add language to use earnings up to 25% of outstanding loans in guarantee account.

Salary language changed to read, "members of the investment committee other than the president receive an annual salary within Range 30 in the salary schedule for state employees established by AS 39.27.011."

Remove the Commissioner of Revenue from the audit committee.

Add section on president's staff of 298 to this bill.

Add investment requirements.

Page 16, line 13--49% changed to 25%.

Page 17, line 19--\$1,500,000 changed to \$2,500,000.

Page 15, line 24--maximum of one (changed from one half).

The renewable resources draft bill was discussed and several changes made.

The meeting adjourned at 10:30 p.m.

P. O. Box 746
Juneau, Alaska 99802
November 17, 1977

Permanent Fund Committee
528 West 5th Avenue
Anchorage, Alaska 99501

Gentlemen:

Because I think it pertinent to your purpose, I should like to relate to you an incident which took place at the Constitutional Review held at the University of Alaska in Fairbanks in 1976, 20 years after the document was completed and ratified. Present on that occasion was John Bebout, who was a consultant at the Alaska Constitutional Convention.

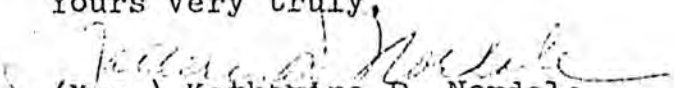
John Bebout is now retired, but he has long been regarded as an eminent authority on state government, including constitutional structure. He had assisted New Jersey, which was one of the first states to revise its constitution. After having served at the Alaska convention, he was called upon by several states to guide them in revision of their state constitutions. And by the way, the Alaska Constitution was used extensively as a model for reform. A provision in many state constitutions permitting the dedication of funds, or not specifically prohibiting it, had proved disastrous. Hence, the Alaska delegates became convinced that our new state should not fall into that error. However, it has done so through amendment.

I seized the opportunity in 1976 to ask John Bebout what he thought of the proposed constitutional amendment establishing the Permanent Fund. He replied immediately, "You are establishing a Fourth branch of government!" It was a shock. The more one ponders his comment, the more one realizes that he voiced a very serious problem facing Alaska. Great power attaches to the control of so large a sum of money. Unless it is managed very carefully and vigilant scrutiny is exercised every step of the way, the people of Alaska may reap little benefit, but millionaires may be created to the detriment of the general welfare of Alaska.

I have no solution to suggest. I am only voicing my own fears and trusting that better heads than mine may be able to devise a way to safeguard the potential benefits, which should inure to the good of the state and its people.

It is obvious that amendments to the constitution are proposed without the exhaustive research which should precede their submission to the voters. The constitution is not a perfect document, but amendments should improve it, not erode its recognized excellence. You have my best wishes.

Yours very truly,


(Mrs.) Katherine D. Nordale

November 28, 1977

Katherine D. Nordale
P.O. Box 746
Juneau, AK 99802

Dear Katherine:

I very much appreciated receiving your comments on the Permanent Fund. A number of legislators, including myself, share your concern on the possibility that the Permanent Fund could become a "fourth branch of government."

There are a number of possible safeguards against this eventuality. Some of these safeguards already exist in the way the Permanent Fund constitutional amendment is structured.

The Permanent Fund is not based on any tax revenues but receives money only from the one-time sale of non-renewable resources. The constitutional dedication of 25 percent of only royalties and bonuses from the lease or sale of minerals will not place any tax revenues in the Permanent Fund. In terms of total revenues (taxes and proceeds from the sale of mineral resources), the Permanent Fund, unless the legislature decides to deposit a greater percentage of royalties, will contain less than 25 percent of the actual total revenues accruing to the State of Alaska.

Moreover, the Permanent Fund is not a fund dedicated for a specific purpose such as those found in New Jersey and many other states. The legislature will, under the Constitution, retain the power to specify those Permanent Fund investments eligible for Permanent Fund money. The Permanent Fund should be, therefore, more responsive to policy directives from elected officials than some of the dedicated funds in other states.

Nevertheless, the potential size of the Permanent Fund, although smaller than the General Fund, requires serious legislative examination of how the Fund will be managed and who will

November 28, 1977

manage it. In this regard, the House Permanent Fund Committee is considering draft legislation to recommend to the whole legislature which would establish a board of trustees for the Permanent Fund to be appointed by the Governor and confirmed by the legislature.

The trustees and their operations as managers of the Permanent Fund would be subject to conflict of interest law, regular audit and performance reporting and the Executive Budget Act. Bringing the board of trustees under the Executive Budget Act does require that the legislature approve the operating budget of the board.

Finally, the principal management goal, under the latest proposed draft, is that the trustees are to invest the Fund monies in such a way to bring the highest net return to the Fund consistent with the safety of the principal of the Fund. Any investments over a certain size will require legislative approval.

As the legislature provides a more detailed statutory framework for the Fund, I hope you will continue to raise pertinent questions and comment on the various proposals. When our proposed draft is completed (about December 15, 1977), I will send you a copy. Thank you for writing.

Cordially,



Rep. Clark Gruening
Chairman

October 20, 1977

Regulation against Energy
Agency
Sandy
Hait Hwy 3101
Jackson, Florida 99801

R.E. Harwood Fuel Committee; allocation
Gentlemen:

Redwood Fuel Open Association
respectfully requests your friendly consideration
of appropriate action in providing cultural
attention for municipalities.

Your best help is!

Thank you for your kind attention
to this request.

Sincerely,
Fred Harwood
President
Redwood Fuel Open
Association
307 Roberts Avenue
Jackson, Florida 99801

P.O. Box 381
Douglas, Alaska 99824
October 18, 1977

The Hon. Clark Gruening, Chairman
House Permanent Fund Committee
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Dear Representative Gruening:

The Juneau-Douglas Branch of the American Association of University Women respectfully requests that the House Permanent Fund Committee consider allocating part of the permanent fund income for the support of cultural facilities throughout Alaska.

We must preserve Alaska's cultural heritage which is in danger of being lost due to the cultural and technological changes in the state; new arts resources must also be encouraged. Creative efforts of artists in Alaska should be promoted.

Cultural facilities will promote citizen awareness and participation in the arts and cultural enrichment on state and local levels.

Cultural enrichment should be a vital part of every Alaskan's education and way of life.

Sincerely,

Alison Farnan

Jan Hickey & Alison Farnan
Co-Presidents
American Association of
University Women
Juneau-Douglas Branch

3228 Illiamna
Anchorage, Ak. 99503
August 30, 1977

House Special Committee
on the Alaska Permanent Fund
528 West 5th Ave., Suite 270
Anchorage, Ak. 99501

Gentlemen:

This letter constitutes written testimony in response to the flyer sent to our home this month. It seeks to make the one point that the value of the Permanent Fund must be judged relative to the size of the population and the need for government services.

Assuming the Fund finally totals \$5 billion. If that Fund has been used to diversify the State's economy by direct investments or guarantees, we can expect to have a larger population and demand for government services. Unless that diversification pays very clearly in tax receipts for the needs of the larger population, when the oil flow stops or declines the \$5 billion will have to cover a large shortfall between receipts and the demand for government services.

Assume again that the Fund finally totals \$5 billion but that it has been invested out of state with the objective of growth in capital and maintenance of purchasing power, Fund loans and guarantees will not have been added to State general fund investments, ANCSA corporation investments, OCS investments, capital move expenditures, and other private investments in the total of funds injected into the economy. The State will not attract as large a population. The need and expectation of services will be smaller. The shortfall between receipts and the demand for government services should be smaller.

A smaller shortfall should give the State time to react to any decline in the economy since Permanent Fund moneys will not have to be used up quickly to maintain our standard of governmental services. More funds will be available per each individual in the population.

The desire to maintain maximum value of the Permanent Fund as a "nest egg" is the primary reason I believe most people voted for the Fund. Any of the alternatives which involve either major investment projects or guarantees or loans to businesses which would not otherwise be funded will only increase the eventual shortfall and thus lower the value of the Fund as a reserve. Those investments are also among the most likely not to pay their way in taxes beyond the costs they add to the public.

House Special Committee on
the Alaska Permanent Fund
August 30, 1977
Page Two

I believe that the State should rely primarily on private capital and general fund capabilities for in-state investment and that the Permanent Fund should be invested with an objective limited to growth in capital and maintenance of purchasing power, preferably in out of state investments.

Very truly yours,


Olof K. Hellen

Alaska State Legislature

SPECIAL COMMITTEE ON
THE ALASKA PERMANENT FUND

(907) 276-3433

528 W. 5TH, SUITE 270
ANCHORAGE, AK. 99501

[POUCH V. JUNEAU, AK. 99811]

(907) 465-3673



MEMBERS

REP. CLARK GRUENING, CHMN.
REP. TERRY GARDINER, V. CHMN.
REP. E. J. HAUGEN
REP. RUSS MEEKINS
REP. BILL MILES
REP. LEO SCHAEFFER
REP. RICK URION

House of Representatives

September 12, 1977

Olof K. Hellen
3228 Illiamna
Anchorage, AK 99503

Dear Olof:

Your written testimony is very much appreciated and will be made part of the record which will accompany this Committee's recommendations to the full legislature

After thinking a good number of hours about basic goals for the Permanent Fund, I have come to the same conclusion that Permanent Fund investment policy ought to emphasize preservation of capital and income production. To the extent the Permanent Fund becomes actively involved in "developmental loans" in Alaska, the problem of equitably distributing the loans and any subsidies inherent in those loans becomes greater.

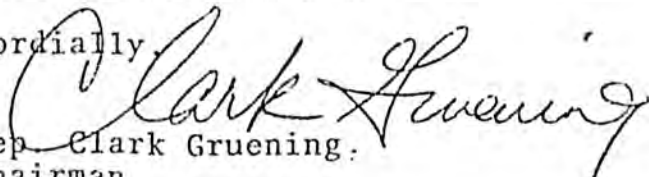
While I do not believe the legislature ought to be involved in the administering or making loans, the legislature should be involved with the public in policy debates surrounding state financing of a large hydroelectric project or pipeline, for example.

The use of the state's general fund to supply capital to special purpose loan funds--as is done presently--is wiser than attempting to place every special purpose in-state loan program into the Permanent Fund.

Nevertheless, present Alaskans may wish to see some more immediate benefit from the use of the income earned by the Fund, and we are exploring some possible ways to distribute Permanent Fund income directly to "Alaskans"--the problem is how to define "Alaskans" equitably and constitutionally.

Thank you, Olof, for your perceptive comments.

Cordially,


Rep. Clark Gruening,
Chairman

3228 Illiamna
Anchorage, Ak. 99503
August 30, 1977

House Special Committee
on the Alaska Permanent Fund
528 West 5th Ave., Suite 270
Anchorage, Ak. 99501

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A smaller shortfall should give the State time to react to any decline in the economy since Permanent Fund moneys will not have to be used up quickly to maintain our standard of governmental services. More funds will be available per each individual in the population.

The desire to maintain maximum value of the Permanent Fund as a "nest egg" is the primary reason I believe most people voted for the Fund. Any of the alternatives which involve either major investment projects or guarantees or loans to businesses which would not otherwise be funded will only increase the eventual shortfall and thus lower the value of the Fund as a reserve. Those investments are also among the most likely not to pay their way in taxes beyond the costs they add to the public.

House Special Committee on
the Alaska Permanent Fund
August 30, 1977
Page Two

I believe that the State should rely primarily on private capital and general fund capabilities for in-state investment and that the Permanent Fund should be invested with an objective limited to growth in capital and maintenance of purchasing power, preferably in out of state investments.

Very truly yours,


Olof K. Hellen

TO: ALASKA STATE CHAMBER OF COMMERCE

DATE: FRIDAY, SEPTEMBER 30, 1977

AS PART OF A PANEL: "PROSPECTS FOR THE PERMANENT FUND"

DEVELOPING GOALS AND EFFECTUATING LEGISLATION FOR THE USES OF THE PERMANENT FUND MUST START WITH A REALIZATION THAT THE PERMANENT FUND IS A UNIQUE VEHICLE IN A UNIQUE POLITICAL AND ECONOMIC ENVIRONMENT IN THE UNITED STATES. THE PERMANENT FUND IS UNIQUE IN CARVING OUT OF GENERAL FUND REVENUES, A PERCENTAGE OF RESOURCE REVENUES WITH THE EXPLICIT RECOGNITION THAT THE RESOURCE REVENUES ARE FINITE AND ARE NON-RECURRING. IN MY VIEW, THE VOTERS RECOGNIZED THIS IN STATING THAT THERE MUST BE A RESIDUUM OF CASH ASSETS AVAILABLE FOR FUTURE GENERATIONS WHEN NORTH SLOPE OIL IS EXHAUSTED. ALASKA'S ECONOMIC AND POLITICAL SITUATION IS UNIQUE SINCE WE COMBINE A STATE WHICH IS PREDOMINANTLY DEPENDENT UPON GOVERNMENTAL ACTIVITIES, AS WELL AS OIL AND GAS RESOURCES FOR THE FORESEEABLE FUTURE. THUS, ALASKANS FEEL SOMEHOW THAT OUR ECONOMIC BASE MUST BE BROADENED AND THAT THE FUND MAY PRESENT AN INVESTMENT VEHICLE FOR THIS PURPOSE.

IN LIGHT OF THESE PROPOSITIONS, IF THEY ARE ACCEPTED, THE QUALITY OF THE PROCESS OF DEVELOPING PUBLIC VIEWS AS TO

THE GOALS AND USES OF THE PERMANENT FUND BECOMES IMMENSELY IMPORTANT IF WE ARE TO EXPECT A RATIONAL RESULT. AS YOU KNOW, THE INVESTMENT ADVISORY COMMITTEE WAS THE INITIAL EXECUTIVE EFFORT IN CONSIDERATION OF USES OF THE PERMANENT FUND. THIS EFFORT WAS PREDOMINANTLY EDUCATIONAL TO THE COMMITTEE. ADVISORS WERE CONSULTED TO EDUCATE THE COMMITTEE ON DEVELOPMENT LOAN AND PERMANENT FUND SYSTEMS IN PLACE ELSEWHERE. THE EFFORT DID NOT INTENSIVELY INVOLVE THE PUBLIC BUT BASICALLY WAS DESIGNED TO DEVELOP A KNOWLEDGE BASE AS TO WHAT HAS HAPPENED ELSEWHERE. CURRENTLY, THE TWO LEGISLATIVE COMMITTEES ARE APPARENTLY HOLDING PUBLIC HEARINGS ON THE SUBJECT MATTER THROUGHOUT THE STATE. AT THE MOMENT, I DO NOT SEE THE BRIDGE BETWEEN THE EDUCATIONAL EFFORTS OF THE INVESTMENT COMMITTEE WITH THEIR ADVISORS AND THE PUBLIC HEARINGS BEING HELD BY THE LEGISLATIVE COMMITTEES. IN MY VIEW, PUBLIC EDUCATION AS TO THE PARAMETERS OF THE ISSUES OF DEVELOPMENT LOAN BANKING IS NECESSARY TO EVOKE AN INTELLIGENT PUBLIC RESPONSE. FAILING THIS, I BELIEVE THAT PUBLIC RESPONSE WILL CONSIST OF REQUESTS FOR NEW LOAN PROGRAMS BY SECTORS OF THE ALASKA ECONOMY IN THE NATURE OF SPECIAL INTEREST PLEADING OR RELATIVELY REPETITIVE TESTIMONY FROM

INDIVIDUAL MEMBERS OF THE PUBLIC. IN FACT, THE WHOLE ENDEAVOR TO ESTABLISH GOALS FOR THE PERMANENT FUND COULD BE MADE THE SUBJECT OF A BROAD BASED EDUCATIONAL EFFORT THROUGH THE SCHOOL AND UNIVERSITY SYSTEMS. IT PRESENTS A FINITE PROBLEM IN ECONOMICS AND FINANCE WHICH COULD STIMULATE THE DEVELOPMENT OF SPECIFIC COURSES IN SECONDARY, UNIVERSITY AND ADULT EDUCATION. THE COURSES WOULD BE TOPICAL AND INTERESTING BECAUSE THEY INVOLVE PROBLEM SOLVING IN THE IMMEDIATE CONTEXT OF THE ALASKA ECONOMY AND ITS PROSPECTS FOR THE FUTURE. SURELY, SUCH A COURSE OF STUDY WOULD BE OF INTEREST TO ALASKANS SINCE IT INVOLVES THEIR MONEY AND FUTURE.

PERHAPS FORMULATION OF SUCH A PROGRAM IS UNREALISTIC GIVEN THE EXISTING FORMAT OF PUBLIC HEARINGS ALREADY ESTABLISHED AND THE APPARENT INTENTION TO DEVELOP LEGISLATION FOR THE PERMANENT FUND DURING THE NEXT LEGISLATIVE SESSION. IF THIS IS FELT TO BE SO, I WOULD SAY THAT MINIMALLY THE COMMITTEES SHOULD COMPILE A DIGEST OF THE EXPERT TESTIMONY ALREADY RECEIVED AND THAT OTHERWISE AVAILABLE TO IT AS TO WHAT HAS HAPPENED ELSEWHERE WITH PERMANENT FUNDS CREATED WITH NON-RENEWABLE RESOURCE REVENUES AND WITH PUBLIC DEVELOPMENT BANKING. I FURTHER SUGGEST THAT SUCH A DIGEST BE MADE

BROADLY AVAILABLE IN ALASKA TO CONSTITUTE A KNOWLEDGE BASE FOR PUBLIC HEARINGS. IN ADDITION, I THINK IMMEDIATE WORK SHOULD GO FORWARD ON AN ECONOMIC ANALYSIS OF THE EFFECT OF STATE LOAN PROGRAMS TO DATE. WE DO HAVE A KNOWLEDGE BASE IN ALASKA, BOTH WITH THE STATE LOAN PROGRAMS WHICH HAVE EXPANDED IN SIZE SINCE 1970, AS WELL AS IN THE HISTORY OF NATIVE CORPORATION INVESTMENTS IN THE STATE. TO THE EXTENT CASE HISTORIES OF SUCCESSES AND FAILURES IN NATIVE CORPORATION INVESTMENTS ARE AVAILABLE, THERE SHOULD BE AN ANALYSIS OF THIS ACTIVITY AND DISSEMINATION OF THE RESULTS.

AS TO SUBSTANTIVE MATTERS AS OPPOSED TO PROCEDURE, I HAVE SEVERAL OBSERVATIONS. FIRST, AN EARLIER STUDY OF DEVELOPMENT LOAN BANKING OPPORTUNITY CARRIED OUT BY THE STATE IN THE EARLY 1970'S, ELICITED THE FIRM RECOMMENDATION OF A REPRESENTATIVE OF THE WORLD BANK THAT STRUCTURING OF ANY DEVELOPMENT LOAN PROGRAM BE PRECEDED FIRST BY AN INTENSIVE INVESTIGATION OF DEVELOPMENT LOAN OPPORTUNITIES IN THE AREA TO BE SERVED. DEVELOPMENT LOAN BANKS ELSEWHERE IN THE WORLD HAVE BEEN STRUCTURED FOLLOWING AN INITIAL EFFORT TO ASCERTAIN THE SCOPE AND MAGNITUDE OF INVESTMENT OPPORTUNITIES. IN OTHER SITUATIONS, A COMMISSION OR COMMITTEE OF BUSINESSMEN,

ENTREPRENEURS AND INVESTORS IN VARIOUS SEGMENTS OF THE ECONOMY HAVE BEEN FORMED TO MAKE THE STUDY AND HAVE PRESENTED INSIGHTS WHICH HAVE SHAPED THE STRUCTURE AND GOALS OF THE DEVELOPMENT FINANCING INSTITUTIONS BEFORE THEY ARE CREATED. THIS IS A NEEDS ASSESSMENT PROCEDURE WHICH I THINK IT IS VITAL TO BE UNDERTAKEN IN ALASKA BEFORE A DEVELOPMENT FINANCING STRUCTURE IS LEGISLATED INTO LAW. AGAIN, I THINK THE NEEDS ASSESSMENT CANNOT BE ADEQUATELY ACCOMPLISHED THROUGH THE HEARING PROCESS, BUT MUST INVOLVE A BROAD SECTION OF THE BUSINESS, ENTREPRENEURIAL AND INVESTMENT COMMUNITY IN MAKING AVAILABLE KNOWLEDGE OF THE CONFIGURATION OF VARIOUS FINANCING OPPORTUNITIES IN THIS STATE. THIS EFFORT IS PARTICULARLY IMPORTANT IN VIEW OF THE FACT THAT THE DEVELOPMENT LOAN ASPECT OF THE PERMANENT FUND IS NOT STATED IN THE CONSTITUTIONAL AMENDMENT BUT IS ONLY ASSUMED TO BE A COMPONENT.

SECONDLY, I FEEL THAT PERMANENT FUND MONIES DEVOTED TO PUBLIC SECTOR FINANCING SHOULD BE USED ON A "LEVERAGED" BASIS. PUBLIC SECTOR LOAN USE OF THE FUND INVOLVES SOME ESTABLISHED ALASKA PRECEDENT. ESTABLISHMENT OF RESERVE FUNDS WHICH WOULD CONSTITUTE SUBORDINATED LOANS FROM THE

FUND IN SUPPORT OF LOCAL GOVERNMENT BORROWING OR STATE AGENCY BORROWING FOR CAPITAL IMPROVEMENT PURPOSES IS PREFERABLE IN ALL CASES TO DIRECT LOANS TO MUNICIPALITIES. A REASON FOR THIS VIEW IS THE FACT THAT LOCAL GOVERNMENT BONDS ARE TAX EXEMPT. IN ADDITION, THE TEST OF THE MARKET IS A VALUABLE BRAKE ON VARIOUS TYPES OF PUBLIC IMPROVEMENTS WHICH WOULD NOT EXIST IF LOAN FUNDS WERE DIRECTLY AVAILABLE THROUGH AN AGENCY CREATED TO MANAGE THE PERMANENT FUND. RESERVE FUND SUPPORT OF LOCAL GOVERNMENT BORROWING FOR PURPOSES WHICH CAN BE FINANCED IN THE PUBLIC MARKET SHOULD LOWER INTEREST RATES FOR THIS FINANCING AND IS IN ANY EVENT ECONOMICALLY EFFICIENT IF THE DEBTOR ENTITY CAN BORROW PUBLICLY AT TAX EXEMPT RATES. SATISFACTORY PRECEDENT FOR THIS PROCEDURE NOW EXISTS WITH VARIOUS STATE BORROWING ENTITIES AND I COMMEND IT TO THE LEGISLATIVE COMMITTEES IN FORMULATING THE STRUCTURE OF THE PERMANENT FUND MANAGEMENT VEHICLE.

THE EXAMPLE OF WHAT HAPPENED WITH FORMULATION OF PLANS FOR THE \$900 MILLION BONUS SALE PROCEEDS OF SEPTEMBER, 1969, SHOULD BE STUDIED. IMMEDIATELY AFTER THE BONUS LEASE SALE, BROOKINGS INSTITUTE SEMINARS WERE HELD THROUGHOUT THE STATE

TO RECEIVE PUBLIC INPUT AS TO USE OF MONEYS IN DEVELOPMENT OF THE STATE OVER THE NEXT TEN-YEAR PERIOD. SOMEHOW, THE RESULTS OF THE BROOKINGS INSTITUTE MEETINGS WERE NOT PROPERLY TRANSLATED INTO THE LEGISLATIVE PROCESS. INSTEAD, WITH THE CONVENING OF THE 1970 SESSION OF THE LEGISLATURE, HEARINGS ON THE CONFIGURATION OF THE STATE'S INVESTMENT OF THE LEASE SALE PROCEEDS BROUGHT FORTH AN ARMY OF INVESTMENT BANKERS AND FUND MANAGERS TO CONVINCING THE STATE THAT INVESTMENT IN THE STOCK MARKET WAS THE ONLY SURE PROTECTION AGAINST EROSION OF THE FUND THROUGH INFLATION. THE FORD FOUNDATION'S REPORT PREPARED BY MCGEORGE BUNDY IN 1970 HEAVILY INFLUENCED THE DISCUSSIONS AND PERCEPTIONS OF STATE OFFICIALS. THIS WAS AN ACADEMIC FORMALIZATION OF THE TOTAL RETURN THEORY OF INVESTMENT IN COMMON STOCKS. THE BEST THING ABOUT THE REPORT WAS ONE OF THE DISSENTS IN WHICH IT WAS STATED THAT IT IS POSSIBLE THAT THE EXPERIENCE OF THE PAST SEVERAL DECADES WAS A SPECIAL SITUATION IN THAT THE VAST UPWARD MOVEMENT OF EQUITY MARKETS MAY BE NEARING ITS CULMINATION. THE LEGISLATURE AFTER MANY MONTHS OF INPUT BY INVESTMENT BANKERS AND OTHERS FINALLY IN JUNE, 1970, ENACTED AN INVESTMENT STATUTE WHICH PERMITTED THE STATE TO INVEST UP TO 1/3 OF THE GENERAL FUND IN THE

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STOCK MARKET AND CONTAINED EVERY OTHER CONCEIVABLE INVESTMENT PERMISSION. THE ACT WAS A MIXTURE OF GOALS, MANY OF WHICH WERE CONTRADICTORY.

THIS IS NOT TO BE CRITICAL OF THE LEGISLATURE, BUT TO SUGGEST THAT AT LEAST PART OF THE PROBLEM AND THE CONFUSED INVESTMENT ACT WHICH RESULTED, MAY HAVE BEEN BASED ON FAILURE OF COMMUNICATION BETWEEN THE PUBLIC SECTOR THROUGH THE HEARING PROCESS WHICH PROCEEDED THE SESSION AND THE LEGISLATIVE HEARING PROCESS WHICH WAS SO HEAVILY DOMINATED BY INVESTMENT BANKER ADVOCATES. THE EXAMPLE IS GIVEN TO SHOW HOW ACUTELY IMPORTANT THE PROCESS OF PUBLIC EDUCATION, PUBLIC HEARING AND COMMUNICATION CAN BE IN THE FORMULATION OF A PUBLIC POLICY RESPECTING STATE INVESTMENT.

FINALLY, I FEEL IT IS NOT UNDEMOCRATIC TO DOUBT THAT A MAGIC FORMULA FOR PERMANENT FUND MANAGEMENT CAN EMERGE FROM PUBLIC HEARINGS. THE CONCEPT IS UNIQUE AND FURNISHES LITTLE, IF ANY, ANALOGY IN AMERICAN LOCAL GOVERNMENTAL EXPERIENCE. THE ONLY HOPE WE HAVE FOR NOT REPEATING SOME OF THE MISTAKES OR HALF SUCCESSES OF THE PAST IS INTENSIVE STUDY AND PUBLIC EDUCATION WITH EFFICIENT DISSEMINATION OF THE RESULTS TO THE PUBLIC. TO THE EXTENT THIS PHILOSOPHY IS NOT REFLECTED IN

CURRENT EFFORTS, I ADVISE THE LEGISLATORS INVOLVED TO BACK UP AND EXAMINE THE PRODUCTIVITY OF THEIR EFFORTS TO DATE. IF WE LOSE SIX MONTHS ON A STUDY FORMULATION PROCESS, IT IS A SIX MONTHS EASILY LOST IN VIEW OF THE FACT THAT THE PERMANENT FUND WILL NOT ACHIEVE ANY SIZABLE VOLUME UNTIL TWO OR MORE YEARS FROM DATE. IF WE FAIL TO STUDY OUR EXISTING LOAN PROGRAMS, THE FOUR YEARS OF NATIVE CORPORATION INVESTMENT EXPERIENCE, AS WELL AS WHAT HAS HAPPENED ELSEWHERE THROUGHOUT THE WORLD, WE ARE CONDEMNING OURSELVES TO REPEATING PAST MISTAKES AND MISSING THE OPPORTUNITY OF ENHANCING THE ECONOMY OF THE STATE OF ALASKA TO THE BETTERMENT OF ALL THE CITIZENS.

* * * * *

Proceedings
of
The House Special Committee on the Permanent Fund

MINUTES TO MEETINGS

Anchorage--July 16, 1977

Kotzebue--September 17, 1977

Juneau--October 20, 1977
(Public Hearing)

Juneau--October 21, 1977

Anchorage--November 19, 1977

Anchorage--December 12 & 13, 1977

Rep. Clark Gruening, Chairman

Rep. Terry Gardiner, Vice Chairman

Rep. Ernie Haugen

Rep. Russ Meekins

Rep. Bill Miles

Rep. Leo Schaeffer

Rep. Rick Urion

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice
Chairman; Russ Meekins, Bill Miles, members.

Mr. Dick Haggart presented long- and short-term revenue projections (July 7 and July 14). He also spoke on the tariff.

Mr. Jim Edenso gave a report on investment of permanent fund. At this time it is in excess of \$4 million. There are treasury notes invested in \$3 million plus and the savings account has \$928,259.21.

There was a discussion and suggestions on the brochure. A wide distribution and summary of two reports were suggested. Committee members were advised to bring comments, suggestions, and changes to the staff's attention the first of the week so the booklet can be sent in to be printed.

Rep. Terry Gardiner gave a short account of renewable resource development.

The budget's allocation for consultants' fees was discussed. When a contract is proposed, it will be circulated to members of the committee.

The budget will be discussed in greater detail at the next meeting.

Tentative meeting schedule was approved.

It was suggested and agreed to that members send monthly budget reports.

COMMITTEE MEETING
Anchorage Courthouse

July 16, 1977
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Mr. Jim Edenso discussed the A. D. Little contract.
Any concerns regarding this contract, let him know and
he'll revise it.

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice Chairman; Russ Meekins, Ernie Haugen, Rick Urion, members; Senator Pat Rodey, Senate Permanent Fund Committee Vice Chairman.

The meeting convened at 10:00 a.m. The first order of business was public testimony.

Mr. Ed Bohnert, counselor with the University of Alaska Extension Center, testified on sources of energy for the Kotzebue area, including a windmill being installed at the Extension Center. His testimony pointed to the high cost of petroleum-based fuels in the Kotzebue region and the potential benefit of developing alternative energy sources in that region.

Mr. Mart, Straus, environmental planner for Mauneluk also testified on alternative energy sources, including a pilot windmill at Kivalina, steam generation at Kobuk and geothermal potential at Kotzebue. In answer to a question from Rep. Gruening, Mr. Straus gave a brief outline of fisheries potential in the Kotzebue region.

Mr. Charlie Edwardson, Washington representative of the North Slope Borough, testified on management structure and investment goals of the Permanent Fund. A transcript of Mr. Edwardson's testimony is attached.

Following a lunch break, Mr. John Schaeffer, president of NANA, testified on his corporation's experience and investments it had made within the region. The main investments had been

in a hotel, wildlife museum, and jade processing operation in Kotzebue. These, Mr. Schaeffer said, had been subsidized by the corporation's profits from other investments outside the region.

Rep. Gardiner presented the Renewable Resources Development Fund subcommittee's first interim report and discussed the "leading edge" theory and the subcommittee's work plan.

Dr. Belden Daniels, committee consultant, presented his paper Models and Options for the Alaska Permanent Fund: Functions, Regionalization and Accountability. Discussion followed, during which Dr. Daniels pointed to the latter portion of the report which detailed accountability problems of existing development banking structures.

Rep. Gruening then moved that he would direct the committee staff to begin preparation of draft legislation structuring the permanent fund. The motion passed with unanimous consent. There followed discussion of the committee's schedule.

The meeting adjourned at 4:45 p.m.

EDWARDSON: The basic point of development in Alaska or any other place in the world is that somebody has always had to finance it--wherever, that's where it came from. All the way through the development of man, especially Western man, the only thing which did not change even when you went to war was the financial arrangements that were made at the time that war had commenced. The victor always had the financial institutions with him.

What does this have to do with state of Alaska? It has a lot to do with it. For the simple fact that prior accumulation had, prior savings had, vested in certain individuals in Alaska, whether we like it or not.

The opportunity here that the state of Alaska has is not so much who is going to be a manager of this portfolio, but how is the citizen going to have a role in the financial infrastructure of his citizenship? This basically means what types of access will the citizen have?

Although the standard of care and the standard of conduct for accounting and recording, I feel at this time, is quite sufficient, the thing that I would recommend very heavily is the simplicity of a financial statement, not its complexity.

When the history repeats itself more than once and it has its own weight and its own inertia, and when you look at society, it says who does the public take care of? In the past, our history of our welfare program in this country emerged from

communities--that it was communities that took care of a few marginaly cautions, and the cities and then they find the way to a state program. The most important thing and the potential that the state of Alaska has is are we at the political development in time when capitalism can be a birth-right? Or are we going to selectively, through regulation, discriminate and create a social elitist managerial class in this state?

The dynamics of a corporation as a tool are, and still is, probably the most creative tool that is available to man at this time. The success allowed capital venture in the state of Alaska will depend upon acceptability--acceptability to the citizens.

How does one arrive at this point--the state legislature at this time is responsible for the administration of the public good to all of its citizens. What is the meaning of public good? The meaning of public good means that you have a public manager. Although the public manager may be at fault in realignment of the economy by the political process, best friends and best relatives, is how our political economy in America has been social.

Today that is no longer an acceptable mode. The gap in America--although we have recognized that there is poverty--is how one gets into that state of mind, that state of consciousness, which is totally intolerant. The way that it has arrived in the past is that in an arrogant,

organized society that those that have the ability to be organized, to get organized, always come into par with the rest of society.

Not only do we see poverty of the mind in rural Alaska but poverty of organization. The state of Alaska, at this time, is one hell of an underdeveloped organization. We are charged with very little responsibility and obligation, yet we fail to give to our citizens the basic desires, basic needs.

How does this affect our citizens? The thing that is most pronounced is a very archaic administration. Very few groups of people in Alaska regulating the conduct of enterprise, and not only do we have constitutional problems, but in order for our citizens to be fully endowed, this endowment must come from the constitutional genesis of the people in Alaska. The current wealth in the state of Alaska is being handled haphazardly in the eyes of the public good that if a corporation can lease 'X' areas of land that the loss, significant loss, has already occurred, when ownership of the citizens gets wasted to few friendly corporations.

In order for the Permanent Fund, I feel, to be successful in Alaska the citizens that it's supposed to serve must have a propriety relationship to the fund. Not only must the governor be accountable, but all of its managers must be accountable to all of its citizens, not just an elitist managerial class who are able to shuffle the paper and foster more intolerable situations called corporate fascism in this state.

The responsibility and the opportunity is to develop a portfolio of citizens with a capitalistic class, capitalistic mode. What we have done 200 years ago means no longer self-sufficient, that we must then accept this greater right to capital--to all of our citizens. It's the total portfolio of this thing that whatever gets appropriated in the name of the public good must also have a proprietary class meaning. Direct ownership to that community, to that citizen at that village of Anchorage so that the citizen of Alaska will have a direct law of acquiring capital even though it may be an improvement in the community. How does one create enough administration for this? The first form of creativity--America is quite ruralist in its capital financing development.

We have had not had a change because the only experience that one follows throughout the world has been a multi-national bank. The banking model, I feel, is so tyrannical that it leaves us very bad, leaves humanity in great masses behind. Therefore, it is very hard to fill the American image elsewhere--throughout the world.

The Permanent Fund in Alaska must have a character of a community; the community not feel elitist managers who are saying, 'we will now do it for you.' And this growth and this evolution, if you take a total fabric of the community in Alaska, the highest cost of any administration in Alaska is energy development. If we worry about what we are going to do about our natural resources, when is the state

legislature or a would-be governor going to treat its citizens as a producer not as a payer. Not until we are able to give a hope to all of our citizens in relationship to capital producing instruments by a constitutional convention. The present underclass society, the other class, whether it's black, white, Native is still growing at a rapid rate. We still mean that there is some fraudulence in our structure, in our system, which we can no longer shelter and leave it for the banks and the corporate directors. The same conduct and the same potential for insider information of the insider run away with this type of portfolio are still too great, thus leaving the citizen back in his original deplorable state.

When you impose a limitation, such as to own and acquire portfolio to those capital producing infrastructures, that tells me that we are going to have that fault. That means that the very country, very state who is probably incongruous with its natural resources and had lost its managerial decision because Alaska has lost its lease hold does now have a different manager called Exxon Corporation or Standard Oil of Sohio who is not interested in how your community infrastructure gets developed. But whose vested interest is to ensure the political weakness of the capital producing infrastructure? And the experience of this model is done already in the North Slope Borough. We should make conditions upon the state leases,

that no oil company, no U.S. corporation or any other corporation go after the taxing authority of this municipality.

Otherwise those that have ability to be organized make a policy mobilized field and thus leaves a great gap of poverty in Alaska. Although it was done in a fashion of public good. The greatest weakness of our annual appropriations and the fallacy is that under the designs of public good, those that always have the access to further reach the benefits.

So the nature of the plan, unlike any other state, the state of Alaska need not to lease these resources. But it can buy back at least other land. The Permanent Fund, as I view it at this time, can be that holding company that the state of Alaska has for all of its citizens in a proprietary class, making all of its citizens capitalists to gaining those benefits which the federal government is going to lease the land anyway.

So the state of Alaska is in the business. The grand public fraud that has been committed by the public officials is self-denial while the state of Alaska is in the business. We are in the business of oil and gas. Why have we denied an appropriate conduct of our...and the necessary standard of care and conduct? When the state legislature must have a proprietary relationship to all of the wealth that state of Alaska has and the biggest problem of the past that the state of Alaska has failed to realize is that we can escape to the biggest bandit in town,

the Commissioner of Natural Resources, who has the necessary technical infrastructure to give the resource away at the cheapest cost possible and therefore create a thing for your people and class who already have.

It therefore makes socialism for the few possible and makes capitalism for the masses impossible. And how does one view its citizenship or is that no longer a sacred thing? Have we substituted a managerial class and put our citizens at the back door--I feel this is very dangerous.

There are controls and unless Alaska defines its communities, what type of community we are to have and who lives in that community, we are going to fail, and still have this type of greater population, dislocation. Once we develop an infrastructure where a citizen can always benefit, not in lieu of service, but in capital formation. I feel that the time has come where we must look at basic definitions and see if community-owned citizens' banks, infrastructures can be developed. Then the chances for fraud, when one has inherited equal rights, diminish. Where accountability is too fine. When you are equal on paper, on statute or in the constitution, that the chances to find a basic violator are higher than the present format, that is you are administering the public good, which you can get away with and rationalize that under the prior proposal that the Tesoro had the best proposal, although it was bad, but it was still the

best proposal, therefore, we had accepted a bad portfolio to start out with, with all the structural problems and because that something has made, therefore, that this type of a public trust because socially respectable and correctable.

The only way, I feel, is that the state legislature must have a greater control on the proprietary of this public resource and not making it into a class of public good where anybody in the governor's office, the governor. And the chief executive of Alaska, at this time, is the largest single one-armed bandit in the state of Alaska. In this light I would not seek to give higher sanction to the governor.

I would highly recommend to the state legislature that they would vest a veto power in those classes of proprietorship of the management of all of the citizens' portfolio. The biggest problem that we have in this state is our chief executive does not know how to administer, not only that but we also have a place for the strongest tyrant in a democratic process to exist in Alaska is governorship of Alaska. That there is no governor in all the 50 states that has the powers that our governor has. It is amazing that practitioners of that office have not totally given our state to be tapped by others, but it is, and I hear sounds that you must be of stock to come in and manage, that the best experience is from the biggest voice, which I don't feel is the case. The best experience I know of and have always vested in the people

that the proprietary of the fund must go directly back to the people not to any managerial groups and that none of the commissioners or the investors of this fund should not serve in any other capacity but for the fund to manage the portfolio of the citizens of this state. The chances of insider information, I'd say, is too high, too great. The concept of the Alaskan Native community must be clearly defined, otherwise that instead of--I see if your procedure becomes in the technocrats' hands, such as an investment portfolio from our biggest threat, apathy, that the chances of that experience are equally great.

So, therefore, I do not think that the exception of a rule just because the guide was successful in managing a portfolio in Peru creating corporate fascism. I feel the same advisor is equally dangerous to the state of Alaska, Milton Friedman. His experience is a classic one that one must not forget, that corporate fascism and corporate capitalism are the same when you have a very strong managerial chief running the portfolio.

I would suggest a permanent committee in the state legislature whereby the legislature and the governor achieve parity. Without that, that the fund will still go to those few and friendly few unless that the populace have a majority and have the control. I would not, I would have a majority of the citizens versus majority of man. I do not trust managers. That the conduct for legal managing has--is in

the books--has always been slammed. And while limiting to capital-producing infrastructures in the state of Alaska that means that Alaskans arbitrarily have cut their noses off and say that I am, now that Alaskan wealth has changed managers overnight--that it is no longer the Permanent Fund; it is now back to the top 500.

The state of Alaska will be buying back, must buy back, and must invest its wealth on federal lands in the state of Alaska. The Permanent Fund must be prepared to find more oil in the outer continental shelf. It must make funds available, necessary so that all of the citizens can grow with the development of our country. If we cannot make--the state of Alaska, as you well know, we've got the coastline. But the coastline has been auctioned off to the largest multi-national corporations already. It is because that the citizen has lost a proprietary relationship for that resource. It is because that the color is under public good, therefore, that the citizens do not have a direct relationship, a primary relationship to that resource. If we develop a proprietary class for its citizens for state of Alaska in whatever development or investment at this time that I see chances of saving ourselves to the maximum benefit of all of our citizens, not just those who have the ability to be organized.

I am for controls. If the controls are to exclude citizens, as far as I am concerned, that is an unconstitutional

assault, a very direct violation. The citizens' access to this resource would say, and the state legislature proprietary control--not the governor. I would vest the proprietary of the fund in the state legislature and go fight the governor. Thus it would make administration checks and balances a lot easier then. I would feel safer if Ernie would have more a say-so on the Permanent Fund than Hammond himself.

GRUENING: So would I. Charlie, thank you; can we ask a question or two?

EDWARDSON: Sure.

GRUENING: You mentioned the Alaska community having problems with the corporations. How do we define community in a way that includes everyone? Should it include everyone in the world?

EDWARDSON: The most significant development in defining community that is occurring throughout this world has occurred in Norway. The Norwegian government, at the time of development of the North Sea, the Norwegian government took the lowest denomination of sovereignty in Norway and examined it, lowest denominator of sovereignty and the best unit,

administering unit, known to Western man has been family. I would say it is high time in state of Alaska that we attempt to actualize in ourselves what is construction and maintenance of Alaskan family and what it means. I see a chance for the first time to develop an actuarial analysis of what constitutes an Alaskan family in this state and to arrive at parity. If state of Alaska is to remain intact, its citizens must have parity and the citizens of state of Alaska should only accept parity, not dislocation.

This means parity in construction, parity in service, which means it may cost more. It may appear to cost more, but in the long run, if you have parity, it has a high survival rate. The basic needs and the basic expenditures which we are going to have is still going to be energy. We already know what those basic components of a community are.

This is 1977 and all of those charges and all of those assumptions of responsibility have not been met, therefore, leaving the state very vulnerable to internal attack.

And although it is beneficial to another segment of the community called lawyers, that the dislocation of its parity of services still is intolerable and with equal access and to arrive at parity, then I say that if this type of dislocation occurs, further occurs, that I see a disintegration of Alaskan society. Not just Native but total disintegration of heavy regionalism. Regionalism occurs structurally because of numbers, because of the nature of administration of public

good gets executed in that fashion because there is no proprietary relationship. If you have proprietary relationship in equity, you will have justice.

RODEY: Charlie, what sort of intervention do you think is appropriate in the economy of the Northwest by the Permanent Fund?

EDWARDSON: I cannot speak for the Northwest. I can speak for what we see in the Arctic. I see the chances of international development in Alaska. Not because of Alaskan resources. State of Alaska has underexamined its strategic location in the universe. State of Alaska is in probably the best location and let's examine strategic positioning of international trade and put Alaska in the Arctic Ocean. If we are to, say, I would propose for the sake of conversation, I am now going into a submarine transportation business, nuclear subs with very large capacity. Maybe all I need is one or two. The 21-day savings, 21-day transportation costs are closing the gap in the Pacific Ocean. The value of Alaska's position in international commerce and the lack of facilitating the hook-up. What happened to Alaska in 1951 has revolutionized the whole commerce of the world? What happened to Alaska in 1951 was the first SAS trans-polar flight occurred. Overnight that, say 22 hours of flying time all over the world that instead of 26 at that time, they made it to 11 hours.

When you put this, state of Alaska is already in the transportation business. When you take a look at the marine development, our potential, as I see it in Alaska is not so much the land but the estuaries. The greatest breadbasket in the world, if we were to keep our estuaries halfway clean, halfway decent, is Alaska in the protein business. And the scale, the present archaic scale of how we used to view Alaska and how it is presently viewed at this time is totally unacceptable.

We must develop a psychology for who we are, where we are from, and state of Alaska, as I see it at this time, can get into an international commerce, international trade of not going through Panama, not crossing Atlantic Ocean, not crossing Pacific Ocean, not crossing Indian Ocean, but crossing our own ocean where it cuts down traffic as long as 23 days. This 23-day savings is sufficient capital saving to go into that type of development but in terms of our community that the citizens in the street must become an owner to a community based infrastructure.

I feel that by getting these numbers--you know, we play number games--we all have a bad habit of that, and it has limitations and what state of Alaska needs at this time is an actuarial analysis of its citizens. With an actuarial analysis, we will learn from this incidence of disease, standard of care where our community vulnerabilities are.

If you have healthy people, we also will have healthy economy. If your people are sick, if your citizens are sick, your economy will also be sick. There are two financing models which I feel should be looked at--is amazingly well is Hydro Quebec. Hydro Quebec is the world's largest utility company. I would like to see state of Alaska come into that class of proprietorship--selling power to the world. Hydro Quebec is so successful that it can finance the government. It is the only situation that I know signs the bonds of a government--than the government signing a bond for Hydro Quebec. So when a state that is already in the business, if they really want to become experienced, the Hydro Quebec model is very good. On our oil and gas activity, a KOBO leasing model is very good. That is a financing technique where investors pool--like you and I pool our monies together and get an outer continental shelf lease. It is a little more complicated than that, but it is a direct line where a non-technical development can get into oil and gas business without buying unnecessary overhead.

HAUGEN: Where do you have access to the two models you are suggesting--Hydro Quebec and KOBO?

EDWARDSON: I can make them available to the committee. I don't have them here with me. I got them at Washington, so I will be going back probably around the 24th.

HAUGEN: Will our staff be able to acquire them through you?

EDWARDSON: Sure. And the other model that is quite interesting is U.S. Steel in Ontario. Why that is interesting is U.S. Steel provides the coal and Ontario provides power to U.S. Steel. It is a very interesting model in terms of financing large scale industrial activities and also financing power so Ontario and U.S. Steel financing techniques have lots of flexibilities. It warrants attention. Ontario and U.S. Steel are in the power business. It may work very well in this state because there are some areas where there is a lot of coal and mining industry, as we all know, is well. One of the things, one of the bad policies we got a lot of bad habits in our government. We have even had to become practitioners of bad habit especially in large scale energy development.

We have a psychological problem that we must take something to the community and the best type of development, as I see it, is at the resources and not taking the community and, which I was happy to hear, it was realized by Fairbanks that the community infrastructure, the social governmental capital to provide sewer and water was more expensive than all of the total, that the secondary community infrastructure got work and it still will be burdensome. The state legislature will still have to pump in more sewer and water. This is why that

I always suspect portfolio managers and always suspect bankers. So if I was in the state legislature, man, I would go after the power that the governor has and vest it in the people, vest it in the state legislature, that is probably the most significant fact that the permanent fund committee can have to have a portfolio run by citizens who do not have loyalties to prior practice, that the chances of an investment banker being loyal and his chances of loyalty will not change but will have an expeditious intercourse with that prior practice. I feel it in Alaska has proven itself to be continuing practice and have not seen to exist but now that I see instead of what used to be for people now.

GRUENING: Thank you, Charlie.

PRESENT: Clark Gruening, Chairman; Russ Meekins, Bill Miles, members.

After a break for lunch, two letters were read and public testimony was heard.

The American Association of University Women delivered a letter asking for consideration for allocating part of the income derived from the permanent fund for the support of cultural facilities.

The Juneau Lyric Opera Association also presented a letter. They request priority consideration and affirmative action in funding cultural activities for municipalities.

Ms. Shirley Rediker, state coordinator of the Cultural Facilities Development Committee, suggested that income from the permanent fund be used for cultural facilities. Ms. Rediker stated that the state had a great need for places for performances, art exhibits, artifacts. She gave an account of several communities' needs for the facilities and offered to furnish the committee with more information if desired.

Mr. Eric Hanson spoke of Alaska's need for education on such things as aquaculture, arctic health, arctic research, mountaineering, skiing, general aviation, fishery science, and hatchery science. Mr. Hanson suggested that institutes be established in the above areas with educators with excellent qualifications--that could draw

international interest. Loans to students with minimum interest charged was also suggested by Mr. Hanson.

He encouraged flow of information to the public as the permanent fund committee progresses.

After a short break Ms. Allison Horton, representing the Audubon Society, stated that the society is more in favor of shifting the money to out-of-state investment than they are of a development bank. They believe that saving it for a future resource is the best.

Ms. Horton did suggest research be done on energy, technology research, alternative sources of energy, establishment of a state office of technology, recycling, and transportation alternatives.

Mr. Doug Pope and Mr. Bill Berrier discussed separation of powers--Bradner vs. Hammond.

Mr. E. O. Brackins, development specialist for minerals in the Division of Economic Enterprise believes there is too much emphasis on renewable vs. non-renewable resources. He thinks that mineral resources are renewable--renewable the same way a farmer's field is renewable. As you go in depth, the resource expands. Mr. Brackins suggested investing with a resource company (using Quebec as an example).

The meeting adjourned at approximately 3:00 p.m.

PRESENT: Clark Gruening, Chairman; Russ Meekins, Bill Miles,
Leo Schaeffer, members.

The meeting convened at 9:00 a.m. The first order of business was White Weld's report.

Mr. Robert Greeley gave the recitation for White Weld on a study relating to descriptions of principals and management of trust funds, principals of various types of trusts. The study includes Wisconsin and Minnesota, as well as a series of investment funds. Also included in the report are the following: organization in management structure, description of different types of corporate securities, money market instruments, investment performance, and a listing of different criteria.

Dr. Belden Daniels discussed the development bank and existing loan funds with the committee.

It was agreed that the draft include a finding--there should be no duplication of already existing loan funds.

It was agreed to capitalize the development bank out of the permanent fund.

A separate paper of alternative approaches to accompany the bill was agreed upon.

The proposal was made and approved to raise the contribution rate to 30%, taking 1/6 of that to capitalize the development bank. The remaining 5/6 would be used to capitalize the investment function.

COMMITTEE MEETING
Capital Building, Juneau

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To keep the three commissioners on the Alaska Enterprise
Investment Fund Policy Board was ratified.

The meeting adjourned at 5:30 p.m.

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice Chairman; Ernie Haugen, Bill Miles, Leo Schaeffer, members; Hugh Malone, Speaker of the House; Alvin Osterback.

The meeting convened at 9:00 a.m.

The committee agreed to adopt the bill which was presented as a working draft. The bill creates the permanent fund as a separate trust investment whose sole function is a high grade investment money-making vehicle. It also creates an Alaska Enterprise Investment Fund to invest in financially-sound medium and small scale enterprises.

A note was made of the Alaska Enterprise Investment Fund inadvertently called the Alaska Development Bank in several sections of the draft. The changes will be made.

The following changes in the draft were made by the committee:

To drop the words "in the Department of Revenue" in Sec. 37.13.010.

To change Finding 2 to read: "the primary goal of the fund should be to maximize total return while maintaining safety of principal;"

It was decided to define capital gains as return to capital and not as earnings and to add language allowing the trust fund managers to spread gains and losses over a five-year period.

Finding 4 was deleted.

Rep. Gruening suggested that something be drafted for use of the income of the fund. His suggestion was to re-inject 50% of earnings back into the permanent fund; and use the remaining 50% to finance alternate energy development--hydro and other non-fossil--to be used to secure a lever of private financing with capital gains returned to principal. It was agreed that the committee members would consider this suggestion.

After a short break, the following changes were made:

For the next meeting, the three-man board of trustees is retained. Staff to draft language putting operation into effect when a total of \$50 million accumulates in trust fund.

Page 8, line 19 to be amended to general language to chose persons to perform services.

Language to be added to 37.13.160 to show performance based on goals and objectives.

Section (f) on page 8 to be rewritten by staff and advisors to allow broad manager discretion.

Operating budget on page 9, lines 13 and 14 to come from general fund.

Language to be added to page 8, lines 5 and on to compare trust fund performance to institutions of similar size.

After a break for lunch, the following changes were made in the draft:

Section 44.55.010(b) will be changed to be consistent with permanent fund heading (Sec. 37.13.010).

Finding 3 under Alaska Enterprise Investment Fund be re-written so that it is not limited from working with federal agencies.

Finding 2 under Alaska Enterprise Investment Fund be written to modify enterprises, small and medium scale, productive, private and community development enterprises. (The same language will be used each time "enterprises" appears.)

The Finding and Purpose sections will be broadened from the limitation of private sector and will allow the community development sector in both.

The commissioners are removed from the Alaska Enterprise Investment Fund Policy Board and one member from the executive branch is added. Also in that section the language will be changed to "six public members appointed by the governor with due regard to geographic location within the state--two of which have broad investment financial background and two have broad experience in community and regional development." There will be one governor's appointee (a voting member) who will be responsible for coordination with other funds. In total the board will have 7 voting members. The terms will be four-year staggered terms.

"The chairman of the governing body of the renewable resources development fund serves as chairman of the policy board but is not a voting member" is deleted and that section will state that the board elect a chairman.

In the section dealing with the quorum of the board,

the sentence "decisions of the board shall be taken by a majority vote, including not less than a majority of the appointed members" the sentence will now end after "vote."

The monetary amount board members receive will be blank.

The section on the investment committee is to remain the same until the next meeting.

Operating budget will be specified in the section pertaining to the investment fund's budget.

The investment fund has the power to borrow up to 150% of its paid-in capital--changed from 50%.

The investment fund may not undertake any new investments till its paid-in capital reaches \$50 million.

The permanent trust fund will invest the idle cash balances, of the investment fund as a separate account, in such a manner that it will meet the cash needs projections of the investment fund.

"Purchase currently sound evidence of indebtedness from the tourism fund, the agricultural revolving loan fund and the small business development loan fund if the loan was made after the effective date of this Act and if the loan meets the criteria of sec. 120 of this chapter" will be eliminated.

The membership of the State Investment Oversight Committee be changed to the President of the Senate, Speaker of the House, and six other legislators, two of whom must be minority.

The meeting adjourned at 4:45 p.m.

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice Chairman; Ernie Haugen, Russ Meekins, Bill Miles, members.

The meeting convened at 1:30 p.m. The first order of business was a report from the Institute of Social and Economic Research.

Mr. Lee Gorsuch and Mr. Scott Goldsmith presented a summary of findings from research over the past three months. Included in the report were the following four points:

1. Looking at effects of varying contribution levels of the fund.
2. Looking at uses of the fund.
3. Examining alternative types of investments of the fund.
4. Looking at what happened to in-state placement of the \$900 million bonus monies received in 1969.

Mr. Bill Berrier reviewed changes in the draft bill from the last meeting.

The meeting adjourned at 5:00 p.m. and reconvened at 9:00 a.m. the following day, December 13, 1977.

The following changes were made in the draft bill:

To drop the word "state" from State Investment Oversight Committee.

Rearrange subsection (f) so that the first sentence is a separate subsection; re-letter subsections following. (Page 8, lines 24 -25).

Add word "surplus" to sentence deposit surplus funds, or invest surplus funds through the permanent fund in such obligations as it may determine; (page 16, line 19).

Change language in subsection (3) to read, "review periodic reports from all other agencies of the state performing lending, borrowing and investment functions." And in (4) to read, "present a complete report of all other agencies of the state performing lending, borrowing, and investment functions."

Draft a findings and purposes section for the Investment Oversight Committee.

Under staff of the Investment Oversight Committee add Legislative Finance Division and in the same section add "or contract for services" after "the committee may hire."

Add "financial and economic planning" on page 2, line 22 after the word "fiscal."

In the duties section the language will be altered to give overview of long range fiscal planning, prescribe procedures.

Finding 3 (page 5) changed to "the permanent fund should be used as a savings device managed to allow the maximum use of disposable income from the fund as needed for purposes designated by law."

On line 8, page 5 add "with respect to fund established in this chapter."

The term of office of the members of the board changed from three years to four years.

Section dealing with qualifications of trustees in (c) remove words "be knowledgeable" and substitute "have recognized competence and wide experience."

Changes in removal and vacancies to be consistent with salaries, etc. Pay is \$250 as an honorarium.

State \$250 per meeting day in compensation of trustees.

Change language in section 37.13.040 to "ALASKA PERMANENT FUND CORPORATION BOARD OF TRUSTEES. There is established the Alaska Permanent Fund Corporation Board of Trustees. The corporation is a public corporation and government instrumentality in the Department of Revenue managed by a board of trustees but has a legal existence independent of and separate from the state. The purpose of the board is to manage and invest the assets of the corporation in accordance with the guidelines established in this chapter."

The Alaska Enterprise Investment Fund Investment Committee changed to Corporation Investment Committee.

On page 8, beginning with line 15 (f) is changed to (b) and the lettering altered to read, "(b) The corporation assets shall be used only for income-producing investments. (c) The board shall seek to maintain a reasonable diversification in its investments unless under the circumstances it

is clearly prudent not to do so. (d) The board shall submit long-range and quarterly investment reports to the Investment Oversight Committee. (e) The corporation may not borrow funds or guarantee the obligations of others. (f) The board may enter into and enforce all contracts necessary, convenient or desirable for purposes of the fund except it may not contract with agencies of the state."

On page 8, line 8, changed to read, "fund assets. The prudent man rule with respect to making investments means the board shall exercise" and continue with the rest of language.

On page 8, line 29 add the word "full" before "faith."

On page 9, line 5 delete after "used" to the word "nor" after the semicolon on line 7.

On page 9 delete from line 15 through line 4 on page 10.

Insert new section on averaging income to read "the board shall establish and from time to time as needed modify guidelines for the corporation's assets. Prior to adoption of any guidelines the guidelines shall be reported to the Investment Oversight Committee for review and comment."

On page 9 delete section (2) and insert language limiting investments to no more than 30% in stocks.

In the section concerning audits (page 10) the Legislative Budget and Audit Committee is changed to Oversight Committee. Language for outside audits in all three funds is added.

Under the section concerning reports and publications the financial statements will be audited by an outside CPA in lieu of the Legislative Budget and Audit Committee. Also in the same section the time frame for reports requirement is changed to 90 days after the end of the fiscal year.

In section 37.13.010 add language to have money paid in at least monthly.

A transition must be added for transfer to permanent fund of monies now held by the Department of Revenue.

New language for conflicts of interest will be written to state a member or employee acquiring a conflicting interest shall disclose the interest but does not have to disqualify himself.

Add transition section for both corporations.

Add language to use earnings up to 25% of outstanding loans in guarantee account.

Salary language changed to read, "members of the investment committee other than the president receive an annual salary within Range 30 in the salary schedule for state employees established by AS 39.27.011."

Remove the Commissioner of Revenue from the audit committee.

Add section on president's staff of 298 to this bill.

Add investment requirements.

Page 16, line 13--49% changed to 25%.

Page 17, line 19--\$1,500,000 changed to \$2,500,000.

Page 15, line 24--maximum of one (changed from one half).

The renewable resources draft bill was discussed and
several changes made.

The meeting adjourned at 10:30 p.m.

P. O. Box 746
Juneau, Alaska 99802
November 17, 1977

Permanent Fund Committee
528 West 5th Avenue
Anchorage, Alaska 99501

Gentlemen:

Because I think it pertinent to your purpose, I should like to relate to you an incident which took place at the Constitutional Review held at the University of Alaska in Fairbanks in 1976, 20 years after the document was completed and ratified. Present on that occasion was John Bebout, who was a consultant at the Alaska Constitutional Convention.

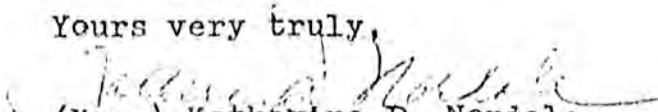
John Bebout is now retired, but he has long been regarded as an eminent authority on state government, including constitutional structure. He had assisted New Jersey, which was one of the first states to revise its constitution. After having served at the Alaska convention, he was called upon by several states to guide them in revision of their state constitutions. And by the way, the Alaska Constitution was used extensively as a model for reform. A provision in many state constitutions permitting the dedication of funds, or not specifically prohibiting it, had proved disastrous. Hence, the Alaska delegates became convinced that our new state should not fall into that error. However, it has done so through amendment.

I seized the opportunity in 1976 to ask John Bebout what he thought of the proposed constitutional amendment establishing the Permanent Fund. He replied immediately, "You are establishing a Fourth branch of government." It was a shock. The more one ponders his comment, the more one realizes that he voiced a very serious problem facing Alaska. Great power attaches to the control of so large a sum of money. Unless it is managed very carefully and vigilant scrutiny is exercised every step of the way, the people of Alaska may reap little benefit, but millionaires may be created to the detriment of the general welfare of Alaska.

I have no solution to suggest. I am only voicing my own fears and trusting that better heads than mine may be able to devise a way to safeguard the potential benefits, which should inure to the good of the state and its people.

It is obvious that amendments to the constitution are proposed without the exhaustive research which should precede their submission to the voters. The constitution is not a perfect document, but amendments should improve it, not erode its recognized excellence. You have my best wishes.

Yours very truly,


(Mrs.) Katherine D. Nordale

November 28, 1977

Katherine D. Nordale
P.O. Box 746
Juneau, AK 99802

Dear Katherine:

I very much appreciated receiving your comments on the Permanent Fund. A number of legislators, including myself, share your concern on the possibility that the Permanent Fund could become a "fourth branch of government."

There are a number of possible safeguards against this eventuality. Some of these safeguards already exist in the way the Permanent Fund constitutional amendment is structured.

The Permanent Fund is not based on any tax revenues but receives money only from the one-time sale of non-renewable resources. The constitutional dedication of 25 percent of only royalties and bonuses from the lease or sale of minerals will not place any tax revenues in the Permanent Fund. In terms of total revenues (taxes and proceeds from the sale of mineral resources), the Permanent Fund, unless the legislature decides to deposit a greater percentage of royalties, will contain less than 25 percent of the actual total revenues accruing to the State of Alaska.

Moreover, the Permanent Fund is not a fund dedicated for a specific purpose such as those found in New Jersey and many other states. The legislature will, under the Constitution, retain the power to specify those Permanent Fund investments eligible for Permanent Fund money. The Permanent Fund should be, therefore, more responsive to policy directives from elected officials than some of the dedicated funds in other states.

Nevertheless, the potential size of the Permanent Fund, although smaller than the General Fund, requires serious legislative examination of how the Fund will be managed and who will

November 28, 1977

manage it. In this regard, the House Permanent Fund Committee is considering draft legislation to recommend to the whole legislature which would establish a board of trustees for the Permanent Fund to be appointed by the Governor and confirmed by the legislature.

The trustees and their operations as managers of the Permanent Fund would be subject to conflict of interest law, regular audit and performance reporting and the Executive Budget Act. Bringing the board of trustees under the Executive Budget Act does require that the legislature approve the operating budget of the board.

Finally, the principal management goal, under the latest proposed draft, is that the trustees are to invest the Fund monies in such a way to bring the highest net return to the Fund consistent with the safety of the principal of the Fund. Any investments over a certain size will require legislative approval.

As the legislature provides a more detailed statutory framework for the Fund, I hope you will continue to raise pertinent questions and comment on the various proposals. When our proposed draft is completed (about December 15, 1977), I will send you a copy. Thank you for writing.

Cordially,



Rep. Clark Gruening
Chairman

October 20, 1977

Legislative Program Agency
Sandy
Mail Stop 3101
Jackson, Florida 99801

RE: (Emergency Fund Committee) allocation
Fellows:

Paul Howard Lynn Opera Association
respectfully requests your friendly consideration
& generous action in providing cultural
attention for municipalities.

You can help us!

Please give your kind attention
to this request.

Sincerely,
Paul Howard Lynn
President
Paul Howard Lynn Opera
Association
307 Bethesda Terrace
Jackson, Florida 99801

P.O. Box 381
Douglas, Alaska 99824
October 18, 1977

The Hon. Clark Gruening, Chairman
House Permanent Fund Committee
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Dear Representative Gruening:

The Juneau-Douglas Branch of the American Association of University Women respectfully requests that the House Permanent Fund Committee consider allocating part of the permanent fund income for the support of cultural facilities throughout Alaska.

We must preserve Alaska's cultural heritage which is in danger of being lost due to the cultural and technological changes in the state; new arts resources must also be encouraged. Creative efforts of artists in Alaska should be promoted.

Cultural facilities will promote citizen awareness and participation in the arts and cultural enrichment on state and local levels.

Cultural enrichment should be a vital part of every Alaskan's education and way of life.

Sincerely,

Alison Farnan

Jan Hickey & Alison Farnan
Co-Presidents
American Association of
University Women
Juneau-Douglas Branch

3228 Illiamna
Anchorage, Ak. 99503
August 30, 1977

House Special Committee
on the Alaska Permanent Fund
528 West 5th Ave., Suite 270
Anchorage, Ak. 99501

Gentlemen:

This letter constitutes written testimony in response to the flyer sent to our home this month. It seeks to make the one point that the value of the Permanent Fund must be judged relative to the size of the population and the need for government services.

Assuming the Fund finally totals \$5 billion. If that Fund has been used to diversify the State's economy by direct investments or guarantees, we can expect to have a larger population and demand for government services. Unless that diversification pays very clearly in tax receipts for the needs of the larger population, when the oil flow stops or declines the \$5 billion will have to cover a large shortfall between receipts and the demand for government services.

Assume again that the Fund finally totals \$5 billion but that it has been invested out of state with the objective of growth in capital and maintenance of purchasing power, Fund loans and guarantees will not have been added to State general fund investments, ANCSA corporation investments, OCS investments, capital move expenditures, and other private investments in the total of funds injected into the economy. The State will not attract as large a population. The need and expectation of services will be smaller. The shortfall between receipts and the demand for government services should be smaller.

A smaller shortfall should give the State time to react to any decline in the economy since Permanent Fund moneys will not have to be used up quickly to maintain our standard of governmental services. More funds will be available per each individual in the population.

The desire to maintain maximum value of the Permanent Fund as a "nest egg" is the primary reason I believe most people voted for the Fund. Any of the alternatives which involve either major investment projects or guarantees or loans to businesses which would not otherwise be funded will only increase the eventual shortfall and thus lower the value of the Fund as a reserve. Those investments are also among the most likely not to pay their way in taxes beyond the costs they add to the public.

House Special Committee on
the Alaska Permanent Fund
August 30, 1977
Page Two

I believe that the State should rely primarily on private capital and general fund capabilities for in-state investment and that the Permanent Fund should be invested with an objective limited to growth in capital and maintenance of purchasing power, preferably in out of state investments.

Very truly yours,


Olof K. Hellen

Alaska State Legislature

SPECIAL COMMITTEE ON
THE ALASKA PERMANENT FUND
(907) 276-3433

528 W. 5TH, SUITE 270
ANCHORAGE, AK. 99501

[FOUCH V. JUNEAU, AK. 99811]
(907) 465-3873



MEMBERS

REP. CLARK GRUENING, CHMN.
REP. TERRY GARDINER, V. CHMN.
REP. E. J. HAUGEN
REP. RUSS MEEKINS
REP. BILL MILES
REP. LEO SCHAEFFER
REP. RICK URION

House of Representatives

September 12, 1977

Olof K. Hellen
3228 Illiamna
Anchorage, AK 99503

Dear Olof:

Your written testimony is very much appreciated and will be made part of the record which will accompany this Committee's recommendations to the full legislature.

After thinking a good number of hours about basic goals for the Permanent Fund, I have come to the same conclusion that Permanent Fund investment policy ought to emphasize preservation of capital and income production. To the extent the Permanent Fund becomes actively involved in "developmental loans" in Alaska, the problem of equitably distributing the loans and any subsidies inherent in those loans becomes greater.


While I do not believe the legislature ought to be involved in the administering or making loans, the legislature should be involved with the public in policy debates surrounding state financing of a large hydroelectric project or pipeline, for example.

The use of the state's general fund to supply capital to special purpose loan funds--as is done presently--is wiser than attempting to place every special purpose in-state loan program into the Permanent Fund.

Nevertheless, present Alaskans may wish to see some more immediate benefit from the use of the income earned by the Fund, and we are exploring some possible ways to distribute Permanent Fund income directly to "Alaskans"--the problem is how to define "Alaskans" equitably and constitutionally.

Thank you, Olof, for your perceptive comments.

Cordially,


Rep. Clark Gruening,
Chairman

3228 Illiamna
Anchorage, Ak. 99503
August 30, 1977

House Special Committee
on the Alaska Permanent Fund
528 West 5th Ave., Suite 270
Anchorage, Ak. 99501

Gentlemen:

This letter constitutes written testimony in response to the flyer sent to our home this month. It seeks to make the one point that the value of the Permanent Fund must be judged relative to the size of the population and the need for government services.

Assuming the Fund finally totals \$5 billion. If that Fund has been used to diversify the State's economy by direct investments or guarantees, we can expect to have a larger population and demand for government services. Unless that diversification pays very clearly in tax receipts for the needs of the larger population, when the oil flow stops or declines the \$5 billion will have to cover a large shortfall between receipts and the demand for government services.

Assume again that the Fund finally totals \$5 billion but that it has been invested out of state with the objective of growth in capital and maintenance of purchasing power, Fund loans and guarantees will not have been added to State general fund investments, ANCSA corporation investments, OCS investments, capital move expenditures, and other private investments in the total of funds injected into the economy. The State will not attract as large a population. The need and expectation of services will be smaller. The shortfall between receipts and the demand for government services should be smaller.

A smaller shortfall should give the State time to react to any decline in the economy since Permanent Fund moneys will not have to be used up quickly to maintain our standard of governmental services. More funds will be available per each individual in the population.

The desire to maintain maximum value of the Permanent Fund as a "nest egg" is the primary reason I believe most people voted for the Fund. Any of the alternatives which involve either major investment projects or guarantees or loans to businesses which would not otherwise be funded will only increase the eventual shortfall and thus lower the value of the Fund as a reserve. Those investments are also among the most likely not to pay their way in taxes beyond the costs they add to the public.

House Special Committee on
the Alaska Permanent Fund
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Page Two

I believe that the State should rely primarily on private capital and general fund capabilities for in-state investment and that the Permanent Fund should be invested with an objective limited to growth in capital and maintenance of purchasing power, preferably in out of state investments.

Very truly yours,


Olof K. Hellen

TO: ALASKA STATE CHAMBER OF COMMERCE

DATE: FRIDAY, SEPTEMBER 30, 1977

AS PART OF A PANEL: "PROSPECTS FOR THE PERMANENT FUND"

DEVELOPING GOALS AND EFFECTUATING LEGISLATION FOR THE USES OF THE PERMANENT FUND MUST START WITH A REALIZATION THAT THE PERMANENT FUND IS A UNIQUE VEHICLE IN A UNIQUE POLITICAL AND ECONOMIC ENVIRONMENT IN THE UNITED STATES. THE PERMANENT FUND IS UNIQUE IN CARVING OUT OF GENERAL FUND REVENUES, A PERCENTAGE OF RESOURCE REVENUES WITH THE EXPLICIT RECOGNITION THAT THE RESOURCE REVENUES ARE FINITE AND ARE NON-RECURRING. IN MY VIEW, THE VOTERS RECOGNIZED THIS IN STATING THAT THERE MUST BE A RESIDIUM OF CASH ASSETS AVAILABLE FOR FUTURE GENERATIONS WHEN NORTH SLOPE OIL IS EXHAUSTED. ALASKA'S ECONOMIC AND POLITICAL SITUATION IS UNIQUE SINCE WE COMBINE A STATE WHICH IS PREDOMINANTLY DEPENDENT UPON GOVERNMENTAL ACTIVITIES, AS WELL AS OIL AND GAS RESOURCES FOR THE FORESEEABLE FUTURE. THUS, ALASKANS FEEL SOMEHOW THAT OUR ECONOMIC BASE MUST BE BROADENED AND THAT THE FUND MAY PRESENT AN INVESTMENT VEHICLE FOR THIS PURPOSE.

IN LIGHT OF THESE PROPOSITIONS, IF THEY ARE ACCEPTED, THE QUALITY OF THE PROCESS OF DEVELOPING PUBLIC VIEWS AS TO

THE GOALS AND USES OF THE PERMANENT FUND BECOMES IMMENSELY IMPORTANT IF WE ARE TO EXPECT A RATIONAL RESULT. AS YOU KNOW, THE INVESTMENT ADVISORY COMMITTEE WAS THE INITIAL EXECUTIVE EFFORT IN CONSIDERATION OF USES OF THE PERMANENT FUND. THIS EFFORT WAS PREDOMINANTLY EDUCATIONAL TO THE COMMITTEE. ADVISORS WERE CONSULTED TO EDUCATE THE COMMITTEE ON DEVELOPMENT LOAN AND PERMANENT FUND SYSTEMS IN PLACE ELSEWHERE. THE EFFORT DID NOT INTENSIVELY INVOLVE THE PUBLIC BUT BASICALLY WAS DESIGNED TO DEVELOP A KNOWLEDGE BASE AS TO WHAT HAS HAPPENED ELSEWHERE. CURRENTLY, THE TWO LEGISLATIVE COMMITTEES ARE APPARENTLY HOLDING PUBLIC HEARINGS ON THE SUBJECT MATTER THROUGHOUT THE STATE. AT THE MOMENT, I DO NOT SEE THE BRIDGE BETWEEN THE EDUCATIONAL EFFORTS OF THE INVESTMENT COMMITTEE WITH THEIR ADVISORS AND THE PUBLIC HEARINGS BEING HELD BY THE LEGISLATIVE COMMITTEES. IN MY VIEW, PUBLIC EDUCATION AS TO THE PARAMETERS OF THE ISSUES OF DEVELOPMENT LOAN BANKING IS NECESSARY TO EVOKE AN INTELLIGENT PUBLIC RESPONSE. FAILING THIS, I BELIEVE THAT PUBLIC RESPONSE WILL CONSIST OF REQUESTS FOR NEW LOAN PROGRAMS BY SECTORS OF THE ALASKA ECONOMY IN THE NATURE OF SPECIAL INTEREST PLEADING OR RELATIVELY REPETITIVE TESTIMONY FROM

INDIVIDUAL MEMBERS OF THE PUBLIC. IN FACT, THE WHOLE ENDEAVOR TO ESTABLISH GOALS FOR THE PERMANENT FUND COULD BE MADE THE SUBJECT OF A BROAD BASED EDUCATIONAL EFFORT THROUGH THE SCHOOL AND UNIVERSITY SYSTEMS. IT PRESENTS A FINITE PROBLEM IN ECONOMICS AND FINANCE WHICH COULD STIMULATE THE DEVELOPMENT OF SPECIFIC COURSES IN SECONDARY, UNIVERSITY AND ADULT EDUCATION. THE COURSES WOULD BE TOPICAL AND INTERESTING BECAUSE THEY INVOLVE PROBLEM SOLVING IN THE IMMEDIATE CONTEXT OF THE ALASKA ECONOMY AND ITS PROSPECTS FOR THE FUTURE. SURELY, SUCH A COURSE OF STUDY WOULD BE OF INTEREST TO ALASKANS SINCE IT INVOLVES THEIR MONEY AND FUTURE.

PERHAPS FORMULATION OF SUCH A PROGRAM IS UNREALISTIC GIVEN THE EXISTING FORMAT OF PUBLIC HEARINGS ALREADY ESTABLISHED AND THE APPARENT INTENTION TO DEVELOP LEGISLATION FOR THE PERMANENT FUND DURING THE NEXT LEGISLATIVE SESSION. IF THIS IS FELT TO BE SO, I WOULD SAY THAT MINIMALLY THE COMMITTEES SHOULD COMPILE A DIGEST OF THE EXPERT TESTIMONY ALREADY RECEIVED AND THAT OTHERWISE AVAILABLE TO IT AS TO WHAT HAS HAPPENED ELSEWHERE WITH PERMANENT FUNDS CREATED WITH NON-RENEWABLE RESOURCE REVENUES AND WITH PUBLIC DEVELOPMENT BANKING. I FURTHER SUGGEST THAT SUCH A DIGEST BE MADE

BROADLY AVAILABLE IN ALASKA TO CONSTITUTE A KNOWLEDGE BASE FOR PUBLIC HEARINGS. IN ADDITION, I THINK IMMEDIATE WORK SHOULD GO FORWARD ON AN ECONOMIC ANALYSIS OF THE EFFECT OF STATE LOAN PROGRAMS TO DATE. WE DO HAVE A KNOWLEDGE BASE IN ALASKA, BOTH WITH THE STATE LOAN PROGRAMS WHICH HAVE EXPANDED IN SIZE SINCE 1970, AS WELL AS IN THE HISTORY OF NATIVE CORPORATION INVESTMENTS IN THE STATE. TO THE EXTENT CASE HISTORIES OF SUCCESSES AND FAILURES IN NATIVE CORPORATION INVESTMENTS ARE AVAILABLE, THERE SHOULD BE AN ANALYSIS OF THIS ACTIVITY AND DISSEMINATION OF THE RESULTS.

AS TO SUBSTANTIVE MATTERS AS OPPOSED TO PROCEDURE, I HAVE SEVERAL OBSERVATIONS. FIRST, AN EARLIER STUDY OF DEVELOPMENT LOAN BANKING OPPORTUNITY CARRIED OUT BY THE STATE IN THE EARLY 1970'S, ELICITED THE FIRM RECOMMENDATION OF A REPRESENTATIVE OF THE WORLD BANK THAT STRUCTURING OF ANY DEVELOPMENT LOAN PROGRAM BE PRECEDED FIRST BY AN INTENSIVE INVESTIGATION OF DEVELOPMENT LOAN OPPORTUNITIES IN THE AREA TO BE SERVED. DEVELOPMENT LOAN BANKS ELSEWHERE IN THE WORLD HAVE BEEN STRUCTURED FOLLOWING AN INITIAL EFFORT TO ASCERTAIN THE SCOPE AND MAGNITUDE OF INVESTMENT OPPORTUNITIES. IN OTHER SITUATIONS, A COMMISSION OR COMMITTEE OF BUSINESSMEN,

ENTREPRENEURS AND INVESTORS IN VARIOUS SEGMENTS OF THE ECONOMY HAVE BEEN FORMED TO MAKE THE STUDY AND HAVE PRESENTED INSIGHTS WHICH HAVE SHAPED THE STRUCTURE AND GOALS OF THE DEVELOPMENT FINANCING INSTITUTIONS BEFORE THEY ARE CREATED. THIS IS A NEEDS ASSESSMENT PROCEDURE WHICH I THINK IT IS VITAL TO BE UNDERTAKEN IN ALASKA BEFORE A DEVELOPMENT FINANCING STRUCTURE IS LEGISLATED INTO LAW. AGAIN, I THINK THE NEEDS ASSESSMENT CANNOT BE ADEQUATELY ACCOMPLISHED THROUGH THE HEARING PROCESS, BUT MUST INVOLVE A BROAD SECTION OF THE BUSINESS, ENTREPRENEURIAL AND INVESTMENT COMMUNITY IN MAKING AVAILABLE KNOWLEDGE OF THE CONFIGURATION OF VARIOUS FINANCING OPPORTUNITIES IN THIS STATE. THIS EFFORT IS PARTICULARLY IMPORTANT IN VIEW OF THE FACT THAT THE DEVELOPMENT LOAN ASPECT OF THE PERMANENT FUND IS NOT STATED IN THE CONSTITUTIONAL AMENDMENT BUT IS ONLY ASSUMED TO BE A COMPONENT.

SECONDLY, I FEEL THAT PERMANENT FUND MONIES DEVOTED TO PUBLIC SECTOR FINANCING SHOULD BE USED ON A "LEVERAGED" BASIS. PUBLIC SECTOR LOAN USE OF THE FUND INVOLVES SOME ESTABLISHED ALASKA PRECEDENT. ESTABLISHMENT OF RESERVE FUNDS WHICH WOULD CONSTITUTE SUBORDINATED LOANS FROM THE

FUND IN SUPPORT OF LOCAL GOVERNMENT BORROWING OR STATE AGENCY BORROWING FOR CAPITAL IMPROVEMENT PURPOSES IS PREFERABLE IN ALL CASES TO DIRECT LOANS TO MUNICIPALITIES. A REASON FOR THIS VIEW IS THE FACT THAT LOCAL GOVERNMENT BONDS ARE TAX EXEMPT. IN ADDITION, THE TEST OF THE MARKET IS A VALUABLE BRAKE ON VARIOUS TYPES OF PUBLIC IMPROVEMENTS WHICH WOULD NOT EXIST IF LOAN FUNDS WERE DIRECTLY AVAILABLE THROUGH AN AGENCY CREATED TO MANAGE THE PERMANENT FUND. RESERVE FUND SUPPORT OF LOCAL GOVERNMENT BORROWING FOR PURPOSES WHICH CAN BE FINANCED IN THE PUBLIC MARKET SHOULD LOWER INTEREST RATES FOR THIS FINANCING AND IS IN ANY EVENT ECONOMICALLY EFFICIENT IF THE DEBTOR ENTITY CAN BORROW PUBLICLY AT TAX EXEMPT RATES. SATISFACTORY PRECEDENT FOR THIS PROCEDURE NOW EXISTS WITH VARIOUS STATE BORROWING ENTITIES AND I COMMEND IT TO THE LEGISLATIVE COMMITTEES IN FORMULATING THE STRUCTURE OF THE PERMANENT FUND MANAGEMENT VEHICLE.

THE EXAMPLE OF WHAT HAPPENED WITH FORMULATION OF PLANS FOR THE \$900 MILLION BONUS SALE PROCEEDS OF SEPTEMBER, 1969, SHOULD BE STUDIED. IMMEDIATELY AFTER THE BONUS LEASE SALE, BROOKINGS INSTITUTE SEMINARS WERE HELD THROUGHOUT THE STATE

TO RECEIVE PUBLIC INPUT AS TO USE OF MONEYS IN DEVELOPMENT OF THE STATE OVER THE NEXT TEN-YEAR PERIOD. SOMEHOW, THE RESULTS OF THE BROOKINGS INSTITUTE MEETINGS WERE NOT PROPERLY TRANSLATED INTO THE LEGISLATIVE PROCESS. INSTEAD, WITH THE CONVENING OF THE 1970 SESSION OF THE LEGISLATURE, HEARINGS ON THE CONFIGURATION OF THE STATE'S INVESTMENT OF THE LEASE SALE PROCEEDS BROUGHT FORTH AN ARMY OF INVESTMENT BANKERS AND FUND MANAGERS TO CONVINCING THE STATE THAT INVESTMENT IN THE STOCK MARKET WAS THE ONLY SURE PROTECTION AGAINST EROSION OF THE FUND THROUGH INFLATION. THE FORD FOUNDATION'S REPORT PREPARED BY MCGEORGE BUNDY IN 1970 HEAVILY INFLUENCED THE DISCUSSIONS AND PERCEPTIONS OF STATE OFFICIALS. THIS WAS AN ACADEMIC FORMALIZATION OF THE TOTAL RETURN THEORY OF INVESTMENT IN COMMON STOCKS. THE BEST THING ABOUT THE REPORT WAS ONE OF THE DISSENTS IN WHICH IT WAS STATED THAT IT IS POSSIBLE THAT THE EXPERIENCE OF THE PAST SEVERAL DECADES WAS A SPECIAL SITUATION IN THAT THE VAST UPWARD MOVEMENT OF EQUITY MARKETS MAY BE NEARING ITS CULMINATION. THE LEGISLATURE AFTER MANY MONTHS OF INPUT BY INVESTMENT BANKERS AND OTHERS FINALLY IN JUNE, 1970, ENACTED AN INVESTMENT STATUTE WHICH PERMITTED THE STATE TO INVEST UP TO 1/3 OF THE GENERAL FUND IN THE

STOCK MARKET AND CONTAINED EVERY OTHER CONCEIVABLE INVESTMENT PERMISSION. THE ACT WAS A MIXTURE OF GOALS, MANY OF WHICH WERE CONTRADICTIONARY.

THIS IS NOT TO BE CRITICAL OF THE LEGISLATURE, BUT TO SUGGEST THAT AT LEAST PART OF THE PROBLEM AND THE CONFUSED INVESTMENT ACT WHICH RESULTED, MAY HAVE BEEN BASED ON FAILURE OF COMMUNICATION BETWEEN THE PUBLIC SECTOR THROUGH THE HEARING PROCESS WHICH PROCEEDED THE SESSION AND THE LEGISLATIVE HEARING PROCESS WHICH WAS SO HEAVILY DOMINATED BY INVESTMENT BANKER ADVOCATES. THE EXAMPLE IS GIVEN TO SHOW HOW ACUTELY IMPORTANT THE PROCESS OF PUBLIC EDUCATION, PUBLIC HEARING AND COMMUNICATION CAN BE IN THE FORMULATION OF A PUBLIC POLICY RESPECTING STATE INVESTMENT.

FINALLY, I FEEL IT IS NOT UNDEMOCRATIC TO DOUBT THAT A MAGIC FORMULA FOR PERMANENT FUND MANAGEMENT CAN EMERGE FROM PUBLIC HEARINGS. THE CONCEPT IS UNIQUE AND FURNISHES LITTLE, IF ANY, ANALOGY IN AMERICAN LOCAL GOVERNMENTAL EXPERIENCE. THE ONLY HOPE WE HAVE FOR NOT REPEATING SOME OF THE MISTAKES OR HALF SUCCESSES OF THE PAST IS INTENSIVE STUDY AND PUBLIC EDUCATION WITH EFFICIENT DISSEMINATION OF THE RESULTS TO THE PUBLIC. TO THE EXTENT THIS PHILOSOPHY IS NOT REFLECTED IN

CURRENT EFFORTS, I ADVISE THE LEGISLATORS INVOLVED TO BACK UP AND EXAMINE THE PRODUCTIVITY OF THEIR EFFORTS TO DATE. IF WE LOSE SIX MONTHS ON A STUDY FORMULATION PROCESS, IT IS A SIX MONTHS EASILY LOST IN VIEW OF THE FACT THAT THE PERMANENT FUND WILL NOT ACHIEVE ANY SIZABLE VOLUME UNTIL TWO OR MORE YEARS FROM DATE. IF WE FAIL TO STUDY OUR EXISTING LOAN PROGRAMS, THE FOUR YEARS OF NATIVE CORPORATION INVESTMENT EXPERIENCE, AS WELL AS WHAT HAS HAPPENED ELSEWHERE THROUGHOUT THE WORLD, WE ARE CONDEMNING OURSELVES TO REPEATING PAST MISTAKES AND MISSING THE OPPORTUNITY OF ENHANCING THE ECONOMY OF THE STATE OF ALASKA TO THE BETTERMENT OF ALL THE CITIZENS.

* * * * *