

SCOMM

#44: 7

Amended
1980

For an Act entitled: "An Act establishing the Prudhoe Bay Oil and Gas Royalty Trust of ~~1981~~ 1980; and providing for an effective date.

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

Section 1. AS 13 is amended by adding a new chapter to read:

CHAPTER 37 PRUDHOE BAY OIL AND GAS ROYALTY TRUST OF 1980

ARTICLE 1. POLICY, PURPOSES, FINDINGS AND
FORMATION OF TRUST

Sec. 13.37.010. POLICY, PURPOSES AND FINDINGS.

(a) It is the duty and policy of the state with respect to the natural resources belonging to it and the income derived from them to provide for their utilization, development, and conservation for the maximum benefit of its people.

(b) The purposes of this chapter are:

(1) to transfer part of Alaska's petroleum wealth to its people in the form of income-producing assets;

(2) to encourage increased awareness and involvement by the people of Alaska in the management of natural resource production and development.

(c) The legislature finds

(1) that it is in the public interest and in the furtherance of a public purpose to distribute a portion

*difference between
increasing wealth as opposed to income*

*vs. income
? or just
receive
income*

*to increase
personal wealth
equitable*

of Alaska's energy wealth to the people of Alaska in the form of income producing assets in order to increase their involvement and awareness regarding the management of the state's natural resources;

(2) that a mechanism by which the state distributes a portion of its resource royalties will best promote the state's interests in producing a more personal and direct stake in the impact of decisions involving the state's natural resource production and development.

at Rev. Sec. 13.37.020. CREATION OF TRUST. The commissioner shall create by trust indenture a trust in accordance with the provisions of this chapter. The trust shall be known as the Prudhoe Bay Oil and Gas Royalty Trust of 1980 and the trustee may transact its affairs in that name.

Sec. 13.37.030. TRUST INDENTURE. (a) The Commissioner of Natural Resources shall execute the trust indenture on behalf of the State. The trustee shall also execute the trust indenture as trustee for the trust. After execution, the trustee shall register the trust in accordance with AS 13.36.

(b) The trust indenture shall include:

- (1) the name and purpose of the trust;
- (2) powers and duties of the trustee;
- (3) the nature and rights of the holders of the beneficial interests;
- (4) accounting and distribution methods and procedures;
- (5) liability of trustee;
- (6) duration, revocation and termination of

*Which actual
leases*

to the trust a portion of the state's royalty interest in leases or properties of the state as authorized by law.

(b) The deed must indicate that the conveyance is only of the state's royalty interest and not the entire mineral interest which will be retained by the state. The conveyance of the royalty interest must be for so long as there is production in paying quantities from the leases or properties described in (a) of this section. After production in paying quantities has ceased, the royalty interest must revert to the state.

(c) The conveyance to the trust is subject to the prior obligations of the state to make payments from the royalty interest to the Alaska Permanent Fund under art. IX, sec. 15 of the Alaska State Constitution and AS 37.13.010, the Alaska Renewable Resources Development Fund under AS 37.10.011, [and the Alaska Native Fund under sec. 9(b) of the Alaska Native Claims Settlement Act (Public Law 92-203 43 U.S.C. 1601 et seq.)] The conveyance is also subject to the rights and obligations of the lessor and lessee of the leases and properties described in (a) of this section including the right to a reduction in royalty as authorized by AS 38.05.180(j), the right to enter into storage or exchange agreements concerning royalty under AS 38.05.180(1), the right to elect to take royalty in kind or in value as authorized by AS 38.05.182 and any future sales, exchanges or other disposal or encumbrance which the Commissioner of Natural Resources is presently authorized by law or may be authorized by law in the future to make or place upon the royalty interest.

50% of income
of x leases

income
not interest

(d) If at the time of conveyance the royalty interest is subject to contracts of sale, the conveyance must expressly identify the contracts and state that the conveyance is subject to them and does not limit the state's rights, duties, and obligations under them.

(e) The royalty interest conveyed under this section includes the interest of the state in the net proceeds from a sale, exchange or other disposition of royalty oil and gas taken in kind from the properties described in (a) of this section.

ARTICLE 2. TRUSTEE.

Sec. 13.37.080. SELECTION OF TRUSTEE (a) The commissioner shall be the trustee for the trust. The commissioner may, however, appoint other persons to act as its agent in administering the trust including a bank or trust company licensed under AS 09.

Sec. 13.37.090. POWERS AND DUTIES OF TRUSTEE. The trustee shall have the duties of preserving the trust estate, the collection of the income from the trust estate, the payment of expenses, and the distributions of the net proceeds of the trust estate to the certificate holders. The powers of the trustee shall not extend beyond those necessary and incidental to carrying out of these duties and shall be restricted to:

(1) the power to manage, conserve and protect the royalties that it would have if it were the absolute owner of the royalties;

(2) the power to temporarily accumulate cash as a reserve for liabilities or for distribution at the next

distribution date and to invest those reserves in accordance with sec. 130 of this chapter;

(3) the power to prosecute or defend, and to settle by arbitration or otherwise any claim of or against the trust, to waive or release rights of any kind and to pay or satisfy any debt, tax or claim upon evidence considered sufficient;

(4) the power to employ oil and gas consultants, accountants, attorneys and other professional and expert persons and to employ or contract for clerical and other administrative assistance and to make payments of all fees for services or expenses in any manner thus incurred out of the trust;

(5) the power to use all money received by it in the payment of all liabilities and obligations incurred by it in connection with the trust including all expenses, taxes, liabilities, compensation to it and compensation to persons employed by it.

Sec. 13.37.100. NO POWER TO ENGAGE IN BUSINESS OR MAKE INVESTMENTS. The trustee may not, in its capacity as trustee under the trust acquire any oil and gas lease, mineral interest, or royalty other than the royalties conveyed under sec. 70 of this chapter or except as provided in sec. 1³/₂₀ of this chapter acquire any other asset or engage in any business or investment activity of any kind.

Sec. 13.37.110. LIABILITY OF TRUSTEE. The trustee's standard of care and liability shall be determined in accordance with AS 13.36.

Sec. 13.37.120. COMPENSATION OF TRUSTEE. The

trustee shall be compensated for its expenses in administering the trust but shall receive no other compensation for its services.

Sec. 13.37.130. INVESTMENT OF CASH RESERVES. (a)

The trustee shall invest the temporary cash reserves established under secs. 140 and 260 of this chapter in:

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

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

(3) certificates of deposits issued by the United States domestic banks which are members of the Federal Deposit Insurance Corporation and secured as to the payment of principal and interest in accordance with Alaska law.

Sec. 13.37.140. PAYMENT OF LIABILITIES. (a) The trustee may use all money received by it in the payment of all liabilities of the trust, including but not limited to, all expenses, taxes, liabilities incurred of all kinds, compensation to it for its expenses, and compensation to persons employed by it. If a liability is contingent or uncertain in amount or is not currently due and payable, the trustee may establish a temporary cash reserve for its payment. The trustee may not pay any liability of the trust with funds set aside under sec. 250 of this chapter for the payment of a monthly distribution amount unless there are no other

available funds in the trust estate and the trustee is satisfied that on the distribution date there will be sufficient funds to pay the monthly distribution amount. If funds set aside under sec. 240 of this chapter are used, the amount used shall be treated as a liability of the trust and shall bear interest at the rate of funds invested under sec. 130 of this chapter.

(b) If at any time the cash on hand and to be received by the trustee is not, or will not, in the judgment of the trustee, be sufficient to pay liabilities of the trust as they become due, the trustee is authorized to borrow the funds required to pay those liabilities. If the trustee borrows funds under this subsection, no further distributions will be made to the certificate holders except previously determined monthly distribution amounts, until the indebtedness created by the borrowings has been paid in full. To secure payment of the indebtedness, the trustee is authorized to mortgage, pledge, grant security interests in or otherwise encumber and to include any and all terms, powers, remedies, covenants, and provisions considered necessary including without limitation the power of sale with or without judicial proceedings the trust estate, or any portion of the trust estate including all or any part of the royalties.

ARTICLE 3. TERMINATION OF TRUST AND LIQUIDATION.

Sec. 13.37.150. DURATION, REVOCATION AND TERMINATION OF TRUST. (a) The trust shall be irrevocable. The trust shall be terminable only as provided in this section and shall continue until so terminated.

(b) The Trust shall terminate upon the first to occur of the following events or times:

(1) at the time as its net revenues for each of two successive years are less than \$1,000,000;

(2) the termination of production from the properties for which the royalties are due;

(3) a vote in favor of termination by the certificate holders present or represented at a meeting held in accordance with sec. 280 of this chapter.

Sec. 13.37.160. LIQUIDATION. (a) Upon termination of the trust, the trustee shall proceed to liquidate and wind up the affairs of the trust. For the purpose of liquidating and winding up the affairs of the trust at its termination, the trustee shall continue to act and exercise each power until its duties have been fully performed and the trust estate has been finally distributed. Upon the termination of the trust, the trustee shall sell for cash in one or more sales all the properties other than cash then constituting the trust estate. The trustee shall, as promptly as possible, distribute the proceeds of any such sales and any other cash in the trust estate according to the respective interests and rights of the certificate holders, after paying, satisfying and discharging all of the liabilities of the trust; or, when necessary, setting up reserves in amounts as trustee in its discretion considers appropriate for contingent liabilities. Upon making final distribution to the certificate holders, the trustee shall be under no further liability except as provided in sec. 110 of this chapter.

ARTICLE 4. BENEFICIAL INTERESTS.

Sec. 13.37.170. CREATION OF BENEFICIAL SHARES AND CERTIFICATES. (a) The entire beneficial interest in the trust shall be divided into a total number of units represented by the value of the royalties conveyed to the trust divided by \$50. The ownership of the units shall be evidenced by certificates in substantially the following form.

CERTIFICATE OF BENEFICIAL INTEREST

IN

THE PRUDHOE BAY OIL AND GAS ROYALTY TRUST OF 1980

Created by, Issued under, and subject to the Prudhoe Bay Oil and Gas Royalty Trust of 1980 Indenture dated as of _____

THIS CERTIFIES THAT _____ is the owner of _____ Units of Beneficial Interest ("Units") in that certain Trust known and designated as the Prudhoe Bay Oil and Gas Royalty Trust of 1980, created and established under the terms of the above-referenced Indenture by and between the State of Alaska, as Trustor, and _____, as Trustee, a duplicate original of which Indenture is, for the information of all concerned, held by said Trustee at its office. The Indenture is hereby referred to and made a part of this Certificate for all purposes, and the owner of this Certificate by accepting the same consents to, and becomes bound by, all the terms and provisions of the Indenture. The Units represented by this Certificate are transferable on the books of the trustee by the holder in person, or by duly authorized attorney, upon surrender of this Certificate, properly endorsed, to

the trustee.

WITNESS the seal of the Trustee and the signature of its duly authorized officer.

DATED _____

_____, TRUSTEE

By _____

Authorized Officer

By _____

Authorized Officer

(b) Initially, the state shall own all of the units and the trustee shall issue a certificate in name of the state for those units. However, the commissioner shall distribute the units in accordance with sec. 180 of this chapter. Upon that distribution, the trustee shall forthwith issue certificates to those persons evidencing the number of units distributed to him or her, and a certificate in the name of the state for those units remaining.

Sec. 13.37.180. DISTRIBUTION OF UNITS. (a) After the conveyance of the royalties to the trust under sec. 70 of the chapter, the commissioner shall determine the value of royalties conveyed in accordance with AS 43.17.080 and divide that total value by \$50 to determine the total number of units in the trust. The number of units determined under this section shall fix the total number of units in the trust and no additional units in the trust may be created. The trustee shall then issue a certificate as described in

sec. 170 of this chapter in the name of the State of Alaska representing the ownership of all the units in the trust.

(b) The commissioner shall then distribute 10 percent of the total units to eligible individuals in accordance with AS 43.17.090. After the distribution under this section, the trustee shall issue certificates as described in sec. 70 of this chapter to the eligible individuals representing the units distributed to them and then issue a new certificate as described in sec. 70 of this chapter in the name of the State of Alaska for the remainder of the units which have not been distributed.

(c) After the distribution under (b) of this section, the commissioner shall distribute the remaining units in accordance with AS 43.17.100, 43.17.110, and 43.17.130. After the distribution under this section, the trustee shall issue certificates as described in sec. 70 of this chapter to the eligible individuals representing the units distributed to them, and then issue a new certificate in the name of the State of Alaska for the remainder of the units which have not been distributed.

(d) The commissioner may not distribute units of the trust under AS 43.17.120 and the commissioner shall hold units not distributed under this section in the name of the state.

Sec. 13.37.190. OWNERSHIP AND TRANSFERABILITY OF UNITS. (a) An eligible individual who has received a unit in the trust under this chapter may not be required to return, sell, or otherwise relinquish that unit as a result of ceasing to be a resident. A unit may not be sold,

given, assigned, transferred, or otherwise conveyed except by inheritance to an individual who is not a resident, and the trustee may cancel any certificates representing units sold, given, assigned, transferred, or otherwise conveyed, except by inheritance, to persons other than an individual who is a resident.

(b) An individual may not own directly or indirectly more than 5 percent of the total units in the trust, and the trustee may not distribute to any person directly or indirectly payments under the trust in excess of that amount attributable to 5 percent of the total units in the trust. For purposes of this subsection, the rules prescribed by section 318 of the Internal Revenue Code (26 U.S.C. §318) for determining the ownership of stock shall apply for determining the ownership of units of the trust.

Sec. 13.37.200 RIGHTS OF CERTIFICATE HOLDERS.

(a) The certificate holders shall own pro rata the beneficial interest in the trust, and shall be entitled to participate pro rata in the rights and benefits of the certificate holders under this chapter. A certificate holder, by assignment or otherwise, takes and holds the same subject to all the terms and provisions of this chapter, which shall be binding upon and inure to the benefit of the successors, assigns, legatees, heirs and personal representatives of the certificate holder. By an assignment or transfer of one or more units represented by a certificate, the assignor shall part with, all of his or her beneficial interest attributable to it, all his rights in, to and under such certificate and all interests, rights and benefits

active
holders
vs.
passive
trust

under this trust of a certificate holder which are attributable to that unit or units as against all other certificate holders and the trustee.

(b) The certificates, units, and the rights, benefits and interests evidenced by either or both including the entire beneficial interest are and shall be held and construed to be in all respects as intangible personal property, and the units and certificates evidenced by them shall be bequeathed, assigned, disposed of and distributed as intangible personal property.

(c) A certificate holder does not have any legal or equitable interest in or to any real property interest which is a part of the trust estate, including, without limitation the royalties or any part of it, but the sole interest of each certificate holder shall be his beneficial interest and the obligation of the trustee to hold, manage and dispose of the trust estate and to account for the trust estate as provided in this chapter. A certificate holder may not call for or demand or secure any partition during the continuance of the trust or during the period of liquidation and winding up under sec. 160 of this chapter.

Sec. 13.37.210. EXECUTION OF CERTIFICATES. All certificates shall be signed by the trustee or a duly authorized agent of the trustee.

Sec. 13.37.220. REGISTRATION AND TRANSFER OF UNITS. The units may be transferred by the certificate holders in accordance with sec. 190 of this chapter and this section. The units shall be transferrable as against the trustee only on the records of the trustee upon the surrender

of certificates and compliance with such reasonable regulations as it may prescribe. A service charge may not be made for a transfer of a unit. Until a transfer, the trustee may treat the owner of any certificate as shown by its records as the owner of the units evidenced by them and is not charged with notice of any claim or demand respecting a certificate or the interest represented by any other party. A transfer of a unit shall, as to the trustee, transfer to the transferee as of the close of business on the date of transfer all of the right, title and interest of the transferor in and to the beneficial interest. The death of any certificate holder shall not entitle the transferee to an account or valuation for any purpose, but such transferee shall succeed to all rights of the deceased certificate holder under this chapter upon proper proof of title, satisfactory to the trustee.

Sec. 13.37.230. DETERMINATION OF OWNERSHIP OF CERTIFICATES. In the event of any disagreement between persons claiming to be transferee of any certificate holder, the trustee shall be entitled at its option to refuse to recognize the claims so long as the disagreement continues. In so refusing, the trustee may elect to make no delivery or other disposition of the interest represented by the certificate involved, or any part of it, or of any sum or sums of money accrued or accruing under it, and, in so doing, the trustee shall not be or become liable to any person for the failure or refusal of the trustee to comply with such conflicting claim and the trustee shall be entitled to continue so to refuse to so act, until:

(1) the rights of the adverse claimants have been adjudicated by a final judgment of a court assuming and having jurisdiction of the parties and the interest and money involved; or

(2) all differences have been adjusted by valid agreement between said parties and the trustee shall have been notified in writing signed by all of the interested parties.

ARTICLE 5. ACCOUNTING AND DISTRIBUTION.

Sec. 13.37.240. FISCAL YEAR AND ACCOUNTING METHOD. The trustee may adopt any fiscal year and may change its fiscal year from time to time as it elects, and shall maintain its books in accordance with generally accepted accounting principles.

Sec. 13.37.250. DISTRIBUTIONS. (a) The trustee shall determine the monthly distribution amount for each month and on the monthly record date for that month shall establish a cash reserve equal to that amount. During the months of January, April, July and October of each year, the trustee shall for each of the immediate preceding three months, distribute pro rata the monthly distribution amount for that month, together with interest earned on that amount from the monthly record date for that month to the payment date, to the certificate holder on the monthly record date for that month.

(b) The monthly distribution amount shall be the amount determined by the trustee equal to the excess, if any, of:

(1) the cash received during a calendar

month which is attributable to the royalties plus any decrease in a cash reserve established by the trustee for the payment of any liabilities of the trust plus any other cash receipts of the trust during the month other than interest earned on the monthly distribution amount for any other month; over

(2) the liabilities of the trust paid during that month plus the amount of any cash reserve established or increased by the trustee for the payment of any future or contingent liabilities of the trust.

(c) The monthly record date for each shall be the close of business on the last business day of the month.

Sec. 13.37.260. TAX REPORTING. For tax purposes, the trustee shall file returns and statements as in its judgment are required to comply with applicable provisions of law and to permit each certificate holder to correctly report his share of the income and deductions of the trust.

Sec. 13.37.270. REPORTS TO CERTIFICATE HOLDERS. At the end of each calendar quarter, the trustee shall mail to each person who was a certificate holder of record on a monthly record date during that quarter a report which shall show, in reasonable detail, the assets, liabilities, receipts and disbursements of the trust for the quarter and for each month in the quarter. Within 90 days following the end of each fiscal year, the trustee shall mail to each person who was a certificate holder of record for a date to be selected by the trustee, an annual report containing financial statements audited by a nationally recognized firm of independent public accountants selected by the trustee.

ARTICLE 6. MEETINGS

Sec. 13.37.280. MEETINGS OF CERTIFICATE HOLDERS.

(a) A meeting of the certificate holders may be called for purposes of terminating the trust under sec. 150 of this chapter or for amending the trust indenture under sec. 40 of this chapter.

(b) A meeting of the certificate holders may be called for the purposes specified in (a) of this section by the trustee or by certificate holders owning not less than 5 percent in number of the units represented by the then outstanding certificates. All meetings shall be held at a time and at a place in the state as the notice may designate.

(c) The notice of every meeting of the certificate holders shall be in writing, be signed by the trustee or the certificate holders calling the meeting, set forth the time and place of the meeting, and matters proposed to be acted upon at the meeting. The notice shall be given in person or by mail not more than 60 days or less than 30 days before the meeting is to be held to all of the certificate holders of record not more than 60 days before the date of the meeting.

(d) If the notice is given to certificate holders by mail, it shall be directed to him or her at the last address as shown on the records of the trustee and shall be considered duly given when so addressed and deposited in the United States mail, postage prepaid. No matter other than that stated in the notice shall be acted upon at any meeting.

Sec. 13.37.290. VOTING. At a meeting of the certificate holders, the presence in person or by proxy of

certificate holders holding a majority of the units outstanding as of the record date for determining the right to receive notice of the meeting, shall constitute a quorum. Any matter shall be considered to have been approved by the certificate holders if it is approved by the vote of a majority in interest of such certificate holders constituting a quorum, although less than a majority of all of the units at the time outstanding. A certificate holder shall be entitled to one vote for each unit owned by him or her and certificate holder may vote in person or by a duly executed written proxy.

Sec. 13.37.300. CONDUCT OF MEETINGS. The trustee may make reasonable regulations as it may consider necessary for any meeting of the certificate holders, for the appointment of proxies, the appointment and duties of inspectors of votes, the submission and examination of proxies, certificates or other evidence of the right to vote, the preparation and use at the meeting of a list authenticated by or on behalf of the trustee of the certificate holders entitled to vote at the meeting and other matters concerning the conduct of the meeting as it shall consider necessary.

ARTICLE 7. GENERAL PROVISIONS

Sec. 13.37.310. INSPECTION OF TRUSTEE'S BOOKS. A certificate holder and his authorized agents, attorneys, and auditors shall have the right during reasonable business hours to examine, inspect and make audits of the Trust and the records of the trustee in reference to the trust.

Sec. 13.37.320. RULE AGAINST PERPETUITIES. The conveyance of royalties to the trust, the transfer of the

beneficial interests in the trust, or the duration of the trust itself shall not be considered as violating the so-called rule against perpetuities or any law restricting or limiting the duration of trusts, and the trust to be created under this chapter may continue for that time as may be necessary to accomplish the purposes for which it was created.

Sec. 13.37.330. WAIVER. The provisions of AS 38.05.125, 38.05.183 and AS 38.06 shall not apply to a conveyance under this chapter.

Sec. 13.37.340. DEFINITIONS. In this chapter:

- (1) "beneficial interest" means an equitable interest in cash of the trust estate including without limitation the proceeds from the conversion of the royalties to cash, and in the right to cash from such conversion of royalties, but does not include any legal or equitable title in or to the royalties as any part of the royalties;
- (2) "certificate" means a certificate issued by the trustee evidencing ownership of one or more units;
- (3) "certificate holder" means the owner of a certificate as reflected on the books of the trustee;
- (4) "commissioner" means the Commissioner of Revenue;
- (5) "conveyance" means the transfer of royalties to the trust by the state;
- (6) "eligible individual" means an individual who is a resident as of an eligibility date determined by the commissioner.
- (7) "individual" means a natural person;
- (8) "resident" means an individual who

maintains a permanent place of abode in the state with the intention of making the state his permanent place of residence and who resides in the state continuously except for temporary purposes only and with the intent of returning; a person may not be considered to have gained a residence solely by reason of his presence and he may not lose it solely by reason of his absence while in the civil or military service of this state or of the United States or by reason of his absence because of marriage to a person engaged in the civil or military service of this state or the United States; a person may not be considered to lose his residence while a student at an education institution, while in an institution at public expense, while confined in prison, while engaged in the navigation of waters of this state, of the United States, or of the high seas, or while residing upon an Indian or military reservation; a minor takes the residence of his parent or of his legal guardian; a married woman may establish her own residence and does not presumptively take the residence of her husband;

(9) "royalties" means the royalties conveyed to the trust pursuant to this chapter.

(10) "trust" means the trust created by and administered under the terms of this chapter and the trust indenture;

(11) "trustee" means the entity serving as trustee of the trust and includes any successor trustee;

(12) "trust estate" means the assets held by trustee under the trust and shall include both income and principal;

(13) "trust indenture" means the trust indenture originally executed by the Commissioner of Revenue and the trustee under this chapter, or if amended or supplemented, as so amended or supplemented;

(14) "unit" means an undivided fractional interest in the beneficial interest.

Sec. 2. The enactment of this Act shall constitute approval of a plan under AS 43.17.040. After enactment, the Commissioner of Revenue shall implement the plan in accordance with this Act and AS 43.17, subject to necessary appropriation. Notwithstanding the approval under this section, the Commissioner of Revenue may submit to the legislature by the thirtieth day of First Session of Twelfth Legislature a revised plan if in his judgment a revised plan is necessary to fully accomplish the policy, purposes and findings under this Act and AS 43.17, or if in his judgment a revised plan is necessary to provide complete information concerning the plan. A revised plan submitted under this section is subject to legislative approval under AS 43.17.040.

Sec. 3. This Act takes effect immediately in accordance with AS 01.10.070(c).

JUNEAU

"The Voice of Ala

VOL. 74 NO. 64

JUNEAU, ALASKA, MC

New oil revenue plan s

By **ROXINNE ERVASTI**
Associated Press Writer

A new proposal for sharing the state's oil revenues with citizens is making the rounds of the State Capitol and will probably be introduced as legislation soon.

The idea is to give everyone a small share of the royalty income that now flows to the state treasury and to sell shares in the balance at a low price.

In addition, the state would turn over to citizen-investors large-scale projects, such as a conditioning plant for North Slope natural gas, after they are constructed. And, the state would establish mutual funds and real estate trusts for citizen-investors.

In order to allow those who do not have money to invest, citizens could pledge their permanent fund dividends and state income tax refunds and credits, or take out loans, toward the long-term purchase of the shares.

"A lot of people would like to pass this to counter the Alaska

General Stock Ownership Corporation initiative," said House Speaker Terry Gardiner. "This idea hasn't been subject to a rigorous review, so we'll have it introduced as a bill for review, and public input."

The AGSOC initiative has been certified for the November election ballot. Under it, a private corporation, but with all citizens as stockholders, would be set up. Some legislators who first endorsed the proposal of Sen. Mike Gravel are now having second thoughts about it, particularly because the electorate and shareholders would be the same.

As for investment in the state's oil through the proposed "energy resource trusts," Gardiner said: "Now, if you want to invest in Alaska oil, you have to buy stock in Exxon. This would give people a chance to invest directly in Alaska."

Dr. Arlon Tussing, a consultant, wrote the proposal at the request of Gov. Jay Hammond. He briefed the governor and a group of House members on it Friday.

★ ★ ★ ★ ★ ★ EMPIRE

Alaska's Capital City"

MONDAY, MARCH 31, 1980

12 PAGES 25¢

surfaces in Legislature

Tussing said the royalty trusts are probably the only parts of the proposal that could be put into effect this year. He suggests one for Prudhoe Bay revenues, in which shares of 5 to 15 percent of the revenues would be given free to Alaskans, and the rest sold at a conservative price with a limit of 5 percent ownership of any individual or group. A separate trust is suggested for revenues from Beaufort Sea leases.

Tussing told the seven House members at the briefing that the state's economic base, excluding oil production, is the same now as it was in the mid-1960s — fishing, tourism, timber. After the oil industry winds down, and the natural gas pipeline is built, he said, "how are the people going to be supported?"

Tussing quoted other economists who have said that Alaska would have to produce 5½ times the United States' entire coal production to replace the revenues from Prudhoe Bay, or equal the entire world catch of fish if fisheries were to replace those revenues.

"There's little chance the state can fill the gap" he said. "A lot of

people are going to have to leave, so you might as well give them a nest egg."

Here are some of the various proposals:

--Prudhoe Bay Oil and Gas Royalty Trust: The state would set aside certain tracts under lease and royalties in excess of current levels would be conveyed to shareholders. Revenues would therefore increase rapidly with the decontrol of oil, with \$100 to \$200 distributed the first year, but then fall off as production declines.

--Beaufort Sea Oil and Gas Royalty Trust: Royalties from 1979 leases would be set aside for distribution and there would be some speculation on the part of those who want to buy shares since the field is not yet in production. The state's right to take royalty in-kind, for refinery or petrochemical uses, would not be impaired, and citizens would be less inclined to allow discounts or give-aways of the state's royalty.

--Industrial Development Projects: When the state invests more than \$100 million in an industrial project.

Arlan

3/27

- original - H Finance Report

Alternatives to AGSOL

+ BCR Corp

- Synthesize alternatives in draft legislative form

Dept of Revenue

- Royalty pass through

- financing of conditioning plant, distribution of equity interest
v.a shares

- mutual fund, REIT's, GSP
existing businesses

- provide financing for purchase of extra shares
distribution - 5-15% free
rest - financed by subscribers
10% down payment
easy terms

comply charges are less than earnings

Royalty Trust
needs only to eligible Alaska

Value of Prudhoe = world's seabed catch
= $5\frac{1}{2} \times$ US Coal Production

Mandates Administration Proposals

Royalty Trust proposals



STATE OF ALASKA

JAY S. HAMMOND, Governor

OFFICE OF THE GOVERNOR
DIVISION OF POLICY DEVELOPMENT AND PLANNING

Phone 465-3512
Pouch AD - Juneau 99811

ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM

A Brief Summary

1. What is the purpose?
 - transfer wealth to people;
 - means for direct participation by individuals in newly organized enterprises;
 - greater resident control over existing Alaskan industries; and
 - wider participation in and understanding of capitalist system through wider ownership.
2. Who organizes or runs the Program?
 - the program is housed in the Department of Revenue;
 - the Commissioner must propose at least one wealth distribution plan but not more than three to the Legislature each session;
 - the Legislature may approve or amend the plan and appropriate any sums required for its implementation;
 - some plans may require the creation of new private organizations, such as GSOC's or mutual funds.
3. What types of assets could be distributed under the Program?
 - Energy Resource Trusts, which pass on a portion of the State's oil and gas royalties directly to holders of certificates in the trust;
 - Industrial Development Projects, which are major projects involving State financial participation which would be distributed by the State to residents;
 - General Stock Ownership Corporations, which are widely held corporations organized under sub-chapter U of the Internal Revenue Code;

- Investment Funds, which are regulated investment companies (mutual funds) holding securities of corporations doing business in Alaska;
 - Real Estate Trusts, which invest in Alaska real estate developments; and
 - Existing Private Enterprises, large blocks of shares of which could be purchased by the State and distributed to residents.
4. Who is eligible for participation in the program?
 - all Alaska residents as defined in the bill;
 - eligibility for each Plan is established by dates included in the Plan.
 5. What State appropriations would be required?
 - an appropriation of the assets to be distributed under the plan; and
 - amounts required to administer the Program.
 6. What actions would be mandatory?
 - only that the Commissioner of Revenue prepare and present at least one Plan and not more than three Plans for each legislative session.
 7. What actions would be elective?
 - legislative adoption of a Plan and appropriations necessary to implement it; and
 - individual participation in a Plan.
 8. What would individual residents receive?
 - free distribution of a minor portion of the assets included in a Plan;
 - an option to purchase additional shares or securities in the remaining assets; and
 - the assets distributed under the Program would be the unencumbered private property of the beneficiaries except as otherwise provided by law.

MEMORANDUM

TO: T. Gardiner
FROM: J. Sund
DATE: March 12, 1981
RE: Proposed Committee Substitute for HB 33.

General Comments:

The proposed CS for HB 33 is nine (9) pages long versus the original bill which is fourteen (14) pages long. The major reason for the shortening of the bill was a decision to delete the sections in the original HB 33 starting on page 7, with section 43.17.080 - page 10, 43.17.110. Those sections detailed out the method for distributing units in a proposed plan.

The proposed CS adopts the policy that the proposal for a distribution plan to the Legislature shall contain the details regarding the distribution of the units. Different methods of distribution are more acceptable for different types of enterprises. The proposed CSHB 33 on Page 6, line 14, section 43.17.110 deal with distribution. The title of the paragraph should probably be just "Distribution" and the word "Free" should be deleted. That section mandates that the Commissioner should propose a method of distribution with each plan submitted to the Legislature.

The major addition to HB 33 involves the setting up of a public process for the origination for distribution plans. In CSHB 33, page 2, line 19, an Investement Advisory Council is created to advise the Commissioner of Revenue regarding potential proposals for a portfolio plan. Page 4, line 23, establishes a provision for hearings to be held throughout the State regarding proposed plans is set out.

There are specific work drafting changes made at the following locations in the bill. Examining HB 33 as follows:

Page 1, line 14-15. Redrafted.

Page 1, line 19-20. Deleted.

Page 1, line 22. "by residents" changed to "by State residents".

Page 1, line 26. Add, "business enterprise and local industry".

Page 1, line 27-Page 2, line 1. Delete, it has been incorporated in sub-section 5.

Page 2, line 5. After "their", add "income and their".

Page 2, line 12. After "mechanism", delete "allowing the State to distribute a part of its ownership interests". Replace with, "to provide a means for direct participation by state residents".

Page 2, line 13. After "enterprises", delete "to residents".

Page 2, line 24. Add a new section, titled Investment Advisory Counsel, found in the CSHB 33 at Page 2, line 19-28.

Page 3, line 5. Delete (c)"a state general stock ownership corporation".

Page 4, line 17. Add a new subsection (c)"a portfolio plan developed by the department shall be submitted to the Investment Advisory Council". That's found in the CS, Page 4, line 21.

Page 4, line 17. Add new section entitled "Hearings". It is found in the CS at Page 4, line 23-Page 5, line 1.

Page 4, line 18. After "portfolio plans", delete "to the second session of the twelfth legislature and to both regular sessions of the thirteenth legislature. This submission shall be made". Replace the deleted line with "to the legislature".

Page 4, line 21. Add a new sentence, "a portfolio plan shall include a report containing public comments on the plan and identifying recommendations submitted by the public which are included in the plan".

New line is found in the CS at, Page 5, line 4-7.

Page 5, line 4. After the word "require" add a period and delete all language from Page 5, line 5-22.

Page 5, line 27. After the work "sold" insert "."; delete the rest of line 27 and all of line 28.

Page 6, line 5. After "project", delete "a State general stock ownership corporation".

Page 6, line 14. After "methods", insert ".".
Delete the remainder of Page 6, line 14-25.

Page 6, line 28. Insert a new section, entitled Disposition of proceeds. "the Commissioner shall deposit net proceeds for sale of units under this chapter into the general fund." That's found in the CS, Page 6, line 11-13.

Page 7, line 2. After "them", delete the remainder line 2-4. Replace with "the Commissioner shall establish a methods for distribution of units under this section". A technical note, the CS at Page 6, line 14 the title should probably delete the word "free", so that it just states "distribution".

Page 7, line 5. Delete all material from Page 7, line 5-Page 11, line 1.

Page 11, line 3. Delete the entire section through line 9 and replace with the following "a portfolio plan may include restrictions on the transfer or disposition of units". That can be found in the CS at Page 6, line 20 and 21.

Page 11, line 10. Delete the entire section, lines 10-17.

Page 12, line 28. Delete line 28-29.

Page 13, line 2. Delete line 2-6.

Page 14, line 1. Delete line 1-4.

Page 14, line 17. Delete line 17-18.

Page 14, line 22. Section 3 , "We may reconsider the effective date clause on this act in light of the royalty trust bill which is being written. The royalty trust bill date should be prior to the effective date of this bill.

MEMORANDUM

TO: CHAIRMAN GARDNER
FROM: JOHN SUND
DATE: MARCH 24, 1981
RE: CONCEPTUAL OUTLINE OF ROYALTY TRUST BILL

The proposed Royalty Trust of 1981 is distributed today in very rough draft condition. The cleaned up version should be available shortly.

THE BILL ORGANIZATION

The purpose is to establish a mechanism to distribute a portion of the states income directly to the residents of the state. Basically the bill does the following:

- 1.0 Article 1. Establishment of a Trust. pages 2-5
- 2.0 Article 2. The Trust Estate. pages 5-7
- 3.0 Article 3. Beneficiary Certificates. pages 8-10
- 4.0 Article 4. Eligibility. page 11
- 5.0 Article 5. Distribution of Units. page 11-14
- 6.0 Article 6. General. pages 14-15
- 7.0 Article 7. Definitions. pages 15-17

The difficult parts of this bill are;

Article 2. The manner in which the asset which will be the trust principle is conveyed from the state to the trust.

Article 5. The manner in which the trust principle is distributed.

There are several crucial policy decisions that must be considered by the committee. Most of the issues have been raised in material that has been distributed to the committee at the last meeting.

THE CONCEPT

The asset. It is assumed that the asset will have an annual income level of about \$200,000,000.

The Trust. The trust will be merely a conduit for the purposes of distributing the annual income accruing to the trust.

Acquisition. The trust will acquire the trust principle by a negotiated purchase from the state. The terms of payment will allow for the payment from future revenues.

Eligibility. All residents of the state as of January 1, 1982 would be eligible to.

Distribution of Certificates. Twenty-five percent (25%) of the beneficiary certificates will be distributed free. Seventy-five percent (75%) would be purchased at a fixed option price at the time of the initial distribution. A purchase warrant would be issued for the purchase of the 75% at the time of the initial distribution.

Distribution of trust income. The income to the trust would first be used to pay for the purchase of the asset. The remainder would be distributed to the certificates.

Issued and unissued certificates. 25% of the certificates are issued immediately and 75% remain unissued until the purchase warrants are exercised. POLICY DECISION. What happens to the revenue accumulating to the unissued certificates? This proposed draft provides that the accumulated amount be distributed with the certificates as the purchase warrants are exercised.

There are many unanswered questions that must be resolved. Primarily the issues deal with the numbers. What size of asset, what will it cost, what would remain for distribution, what effect on the certificate holders, various other financial and tax matters. It is my recommendation that the committee consider contracting for assistance on these matters.

Sund

3/18/81

Original sponsors: Gardiner etc.

IN THE HOUSE

BY GARDINER ETC

HOUSE BILL NO. ____.

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWELFTH LEGISLATURE - FIRST SESSION

A BILL

For an Act entitled: "An Act establishing the Alaska Royalty Trust of 1981.

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

* Section 1. DECLARATION OF POLICY, PURPOSES AND FINDINGS. (a)

It is the policy of the state to provide for the use, development, and conservation of the state's natural resources and the income derived from them for the maximum benefit of its people.

(b) The purposes of this Act are to

(1) increase the income of state residents by transferring part of the wealth derived from the natural resources of the state to them;

(2) provide a means for the direct participation of state residents in the financing of business enterprises which benefit the state, and to provide residents with the opportunity to share in potential profits;

(3) encourage greater participation in and understanding of the capitalist system by state residents through a wider distribution of economic interests in state business enterprises;

(c) The legislature finds that

(1) it is in the public interest and furthers a public purpose to distribute a part of Alaska's wealth derived from natural resources to state residents to increase their income and their involvement and awareness regarding the management of the state's natural resources, development of its local industry, and the capitalist system;

(2) a mechanism allowing the state to distribute a part of its resource wealth to residents will best promote the state's interest in creating direct involvement by residents in the decisions concerning the state's natural resource management.

(d) Except as otherwise required by law, it is intended that distributions to residents under this Act shall be unencumbered property.

* Sec. 2. AS 43 is amended by adding a new chapter to read:

CHAPTER 90. ALASKA ROYALTY TRUST OF 1981.

ARTICLE 1. ESTABLISHMENT OF A TRUST.

Sec. 43.90.010. ESTABLISHMENT OF A TRUST. There is established in the Department of Revenue the Alaska Royalty Trust of 1981 to carry out the purposes of this chapter.

Sec. 43.90.020. TRUSTEE. The commissioner of revenue or his agent or designee is the trustee of the trust fund established in this chapter and shall:

(1) act as the official custodian of the securities and cash belonging to the trust;

(2) receive transfers and appropriations of cash and securities to the trust;

(3) invest and reinvest the principal of the trust in accordance with AS 37.10.070;

(4) collect interest, dividends and royalties earned on assets, securities and investments of the trust;

(5) provide for the distribution and sale of share certificates in the trust to eligible beneficiaries; and

(6) determine and make distributions of trust income to the beneficiaries of the trust.

Sec. 43.90.030. TRUST PURPOSE. The purpose of the trust is to provide an efficient and practical means of permitting each certificate holder to receive his pro rata share of the proceeds attributable to the royalties conveyed to the trust. This purpose is realized by retaining and collecting the cash proceeds of royalties and to distribute that cash, net of expenses and liabilities of the trust, to the certificate holders pro rata on a quarterly basis.

Sec. 43.90.040. COMPENSATION OF TRUSTEE. The trustee shall be compensated for its expenses in administering the trust but shall receive no other compensation for its services.

Sec. 43.90.050. PAYMENT OF LIABILITIES. The trustee may use all money received by it in the payment of all liabilities of the trust, including but not limited to, all expenses, taxes, liabilities incurred of all kinds, compensation to it for its expenses, and compensation to persons employed by it, If a liability is contingent or uncertain in

amount or is not currently due and payable, the trustee may establish a temporary cash reserve for its payment. The trustee may not pay any liability of the trust with funds set aside under sec. ___ of this chapter for the payment of quarterly distributions unless there are no other available funds in the trust estate and the trustee is satisfied that on the distribution date there will be sufficient funds to pay the quarterly distribution amount. If funds set aside under sec. ___ of this chapter are used the amount used shall be treated as a liability of the trust and shall bear interest at the rate of funds invested under sec. ___ of this chapter.

Sec. 43.90.060. DURATION, REVOCATION AND TERMINATION OF TRUST. (a) The trust shall be irrevocable. The trust shall be terminable only as provided in this section and shall continue until so terminated.

(b) The trust shall terminate at such time as the termination of production from the properties for which the royalties are due.

Sec. 43.90.070. LIQUIDATION. (a) Upon termination of the trust, the trustee shall proceed to liquidate and wind up the affairs of the trust. For the purpose of liquidation and winding up the affairs of the trust at its termination, the trustee shall continue to act and exercise each power until its duties have been fully performed and the trust estate has been finally distributed. The trustee shall, as promptly as possible, distribute the cash in the trust estate according to the respective interests and rights of the certificate holders, after paying, satisfying and discharging all of the liabilities of the trust; or, when necessary, setting up reserves in amounts as trustee in its discretion considers appropriate for contingent liabilities. Upon

making final distribution to the certificate holders, the trustee shall be under no further liability except as provided in sec. ___ of this chapter.

Sec. 43.90.080. FISCAL YEAR AND ACCOUNTING METHOD. The trustee shall adopt the fiscal year of the state and shall maintain its books in accordance with generally accepted accounting principles.

Sec. 43.90.090. REPORTS TO CERTIFICATE HOLDERS. At the end of each fiscal year the trustee shall mail to each person who was a certificate holder of record during the prior year a report which shall show, in reasonable detail, the assets, liabilities, receipts and disbursements of the trust for the year. The report shall contain financial statements audited by a nationally recognized firm of independent public accountants selected by the trustee.

Sec. 43.90.100. REPORT. The trustee shall annually file with governor and the legislature no later than the 30th day after the convening of the legislature each year a report of the activities of the trust for the preceding year.

Sec. 43.90.110. INSPECTION OF TRUSTEE'S BOOKS. A certificate holder and his authorized agents, attorneys, and auditors shall have the right during reasonable business hours to examine, inspect and make audits of the Trust and records of the trustee in reference to the trust.

ARTICLE 2. THE TRUST ESTATE.

Sec. 43.90.120. TRUST ESTATE. The assets of the trust shall consist of the royalties conveyed to the trust under sec. .650 of this chapter.

Sec. 43.90.130. CONVEYANCE OF ROYALTIES. (a) The state through the commissioner of natural resources shall negotiate and sell to the trust a portion of the state's royalty interest in leases or properties of the state as authorized by law.

(b) The conveyance is only of the state's royalty interest and not the entire mineral interest which will be retained by the state. The conveyance of the royalty interest must be for so long as there is production in paying quantities from the leases or properties described in (a) of this section. After production in paying quantities has ceased, the royalty interest must revert to the state.

(c) The conveyance to the trust is subject to the prior obligations of the state to make payments from the royalty interest to the Alaska Permanent Fund under art. IX, sec. 15 of the Alaska State Constitution and AS 37.13.010, the Alaska Renewable Resources Development Fund under AS 37.10.011, and the Alaska Native Fund under sec. 9(b) of the Alaska Native Claims Settlement Act (Public Law 92-203 43 U.S.C. 1601 et seq.). The conveyance is also subject to the rights and obligations of the lessor and lessee of the leases and properties described in (a) of this section including the right to a reduction in royalty as authorized by AS 38.05.180(j), the right to enter into storage or exchange agreements concerning royalty under AS 38.05.180(1), the right to elect to take royalty in kind or in value as authorized by AS 38.05.182 and any future sales, exchanges or other disposal or encumbrance which the Commissioner of Natural Resources is presently authorized by law or may be authorized by law in the future to make or place upon the royalty interest.

(d) If at the time of conveyance the royalty interest is subject to contracts of sale, the conveyance must expressly identify the contracts and state that the conveyance is subject to them and does not limit the state's rights, duties, and obligations under them.

(e) The royalty interest conveyed under this section includes the interest of the state in the net proceeds from a sale, exchange or other disposition of royalty oil and gas taken in kind from the properties described in (a) of this section.

Sec. 43.90.140. VALUE OF ASSETS CONVEYED TO THE ALASKA ROYALTY TRUST OF 1981. The value of assets contributed to a Alaska Royalty Trust of 1981 is the conservatively appraised value of the assets. A conservatively appraised value for assets is a value determined by generally accepted appraisal methods and shall be calculated using

(1) estimates of resource production volumes having an accuracy confidence level of 75 percent or greater;

(2) an assumed rate of increase in future world prices for resources not exceeding the general rate of price inflation in the United States; and

(3) a discount rate reflecting the judgment of private investors as to the expected rate of return before payment of taxes required to justify incremental investment in the exploration and development of resources comparable to those committed to the Alaska Royalty Trust of 1981.

ARTICLE 3. BENEFICIARY CERTIFICATES.

Sec. 43.90.150. CREATION OF BENEFICIAL SHARES AND CERTIFICATES. The ownership of the units shall be evidenced by certificates in substantially the following form.

CERTIFICATE OF BENEFICIAL INTEREST

IN

ALASKA ROYALTY TRUST OF 1981

Created by, Issued under, and subject to the Alaska Royalty Trust of 1981 Indenture dated as of _____.

THIS CERTIFIES THAT _____ is the owner of _____ Units of Beneficial Interest ("Units") in that certain Trust known and designated as the Alaska Royalty Trust of 1981, created and established under the terms of the above-referenced Indenture by and between the State of Alaska, as Trustor, and the Commissioner of Revenue, as Trustee, a duplicate original of which Indenture is, for the information of all concerned, held by said Trustee at its office. The Indenture is hereby referred to and made a part of this Certificate for all purposes, and the owner of this Certificate by accepting the same consents to, and becomes bound by, all the terms and provisions of the Indenture. The Units represented by this Certificate are transferable on the books of the trustee by the holder in person, or by duly authorized attorney, upon surrender of this Certificate, properly endorsed, to the Trustee.

WITNESS the seal of the Trustee and the signature of its duly authorized officer.

DATED _____

_____, TRUSTEE

By _____

Sec. 43.90.160. EXECUTION OF CERTIFICATES. All certificates shall be signed by the trustee or a duly authorized agent of the trustee.

Sec. 43.90.170. OWNERSHIP AND TRANSFERABILITY OF UNITS. (a) An eligible individual who has received a unit in the trust under this chapter may not be required to return, sell, or otherwise relinquish that unit as a result of ceasing to be a resident. A unit may not be sold, given, assigned, transferred, or otherwise conveyed except by inheritance to an individual who is not a resident, and the trustee may cancel any certificates representing units sold, given, assigned, transferred, or otherwise conveyed, except by inheritance, to persons other than an individual who is a resident.

(b) An individual may not own directly or indirectly more than 100 units in the trust, and the trustee may not distribute to any person directly or indirectly payments under the trust in excess of that amount attributable to 100 units in the trust. For purposes of this subsection, the rules prescribed by section 318 of the Internal Revenue Code (26 U.S.C. 318) for determining the ownership of stock shall apply for determining the ownership units of the trust.

Sec. 43.90.180. REGISTRATION AND TRANSFER OF UNITS. The units may be transferred by the certificate holders in accordance with sec. ___ of this chapter and this section. The units shall be transferable as against the trustee only on the records of the trustee upon the surrender of certificates and compliance with such reasonable regulations as it may prescribe. A service charge may not be made for a transfer of a unit. Until a transfer, the trustee may treat the owner of any certificate as shown by its records as the owner of the units

evidenced by them and is not charged with notice of any claim or demand respecting a certificate or the interest represented by any other party. A transfer of a unit shall, as to the trustee, transfer to the transferee as of the close of business on the date of transfer all of the right, title and interest of the transferor in and to the beneficial interest. The death of any certificate holder shall not entitle the transferee to an account or valuation for any purpose, but such transferee shall succeed to all rights of the deceased certificate holder under this chapter upon proper proof of title, satisfactory to the trustee.

Sec. 43.90.190. DETERMINATION OF OWNERSHIP OF CERTIFICATES.

In the event of any disagreement between persons claiming to be transferee of any certificate holder, the trustee shall be entitled at its option to refuse to recognize the claims so long as the disagreement continues. In so refusing, the trustee may elect to make no delivery or other disposition of the interest represented by the certificate involved, or any part of it, or of any sum or sums of money accrued or accruing under it. and, in so doing, the trustee shall not be or become liable to any person for the failure or refusal of the trustee to comply with such conflicting claim and the trustee shall be entitled to continue so to refuse to so act, until:

(1) the rights of the adverse claimants have been adjudicated by a final judgment of a court assuming and having jurisdiction of the parties and the interest and money involved; or

(2) all differences have been adjusted by valid agreement between said parties and the trustee shall have been notified in writing signed by all of the interested parties.

ARTICLE 4. ELIGIBILITY.

Sec. 43.90.200. ELIGIBILITY. To be eligible to receive a unit distributed by the trustee under this chapter an individual must

- (1) be a resident of the state on January 1, 1982;
- (2) apply to the department; and
- (3) submit with the application a signed, sworn certification

that he was a resident of the state on the eligibility date and other proof of residency as the commissioner may require.

(b) The department shall prescribe and furnish a form for applications and for certification of residency.

ARTICLE 5. DISTRIBUTION OF UNITS

Sec. 43.90.210. NUMBER AND PURCHASE PRICE OF UNITS. The price for each unit shall be \$50.00. The commissioner shall determine the total number of units to be distributed by dividing the value of the assets contributed to the trust by \$50.00.

Sec. 43.90.220. DISTRIBUTION AND SALE OF BENEFICIAL CERTIFICATES. The Trustee shall determine the total number of units each eligible individual is entitled to obtain from the Trust by dividing the entire number of units as established in sec. ~~.120~~ by the total number of eligible individuals as established in sec. _____. The trustee shall distribute twenty-five per cent (25%) of the number of the units to the eligible individuals free without charge. Each eligible individual shall also receive, along with the free units, six purchase warrants. Each purchase warrant shall entitle the holder to purchase the additional seventy-five percent (75%) of the units from the Trust which the individual is entitled.

Sec. 43.90.230. PURCHASE WARRANTS. (a) A purchase warrant entitles an eligible individual to purchase three-quarters of the number of units the individual is entitled according to the following schedule:

(1) one-eighth of the units not later than one year after the purchase warrant was issued;

(2) one-eighth of the units not later than two years after the purchase warrant was issued;

(3) one-eighth of the units not later than three years after the purchase warrant was issued;

(4) one-eighth of the units not later than four years after the purchase warrant was issued;

(5) one-eighth of the units not later than five years after the purchase warrant was issued;

(6) one-eighth of the units not later than six years after the purchase warrant was issued;

(b) Payment for units purchased using a purchase warrant may be made by cash, check, or money order.

(c) A purchase warrant is void if transferred. A purchase warrant may not be used except by an individual who is a resident of the state.

Sec. 43.90.240. DISTRIBUTIONS. (a) The trustee shall determine the quarterly distribution amount for each quarter and on the quarterly record date for that quarter establish a cash reserve equal to that amount. During the months of January, April, July and October of each year, the trustee shall for each of the immediate preceding three months, distribute pro rata the quarterly distribution amount for that quarter, together with interest earned on that amount from the quarter

record date for that quarter to the payment date, to the certificate holder on the quarterly record date for that quarter.

(b) The quarterly distribution amount shall be the amount determined by the trustee equal to the excess, if any, of:

(1) the cash received during a calendar quarter which is attributable to the royalties plus any decrease in a cash reserve established by the trustee for the payment of any liabilities of the trust plus any other cash receipts of the trust during the quarter other than interest earned on the quarterly distribution amount for any other quarterly over;

(2) the liabilities of the trust paid during that quarter plus the amount of any cash reserve established or increased by the trustee for the payment of any future or contingent liabilities of the trust.

(c) The quarterly record date for each quarter shall be the close of business on the last business day of the quarter.

Sec. 43.90.250. CALCULATION OF THE INDIVIDUAL CERTIFICATE DISTRIBUTION. The individual certificate distribution amount shall be determined by dividing the total quarterly distribution amount by the total certificates as determined in sec. ____, both issued and unissued. The dividend shall be paid to each individual certificate of an issued certificate holder. The remainder shall be retained by the trustee and credited to the unissued certificates. At such time as a purchase warrant is exercised and a certificate is issued the total amount attributable to the certificate to that date shall be paid with the first quarterly dividend to be paid to the certificate holder.

Sec. 43.90.260. PROCEEDS OF THE SALE OF CERTIFICATES. The proceeds from the sale of share certificates shall be placed in the trust account and become part of the trust principle and available for paying the purchase price of the trust asset.

ARTICLE 6. GENERAL.

Sec. 43.90.270. NO POWER TO ENGAGE IN BUSINESS. The trustee may not, in its capacity as trustee under the trust acquire any oil and gas leases, mineral interest, or royalty other than the royalties conveyed under sec. .050 of this chapter or acquire any other asset or engage in any business.

Sec. 43.90.280. LIABILITY OF TRUSTEE. The trustee's standard of care and liability shall be determined in accordance with AS 13.36.

Sec. 43.90.290. TAX REPORTING. For tax purposes, the trustee shall file returns and statements as in its judgment are required to comply with applicable provisions of law and to permit each certificate holder to correctly report his share of the income and deductions of the trust.

Sec. 43.90.300. AUTHORITY TO PARTICIPATE IN MARKET. (a) If the commissioner determines that an efficient public market does not exist for the sale of units, he may buy, sell, and trade in units for the purpose of establishing a market.

(b) If the commissioner trades in units as authorized in (a) of this section, he shall maintain an average markup sufficient to compensate the state for the administrative costs of his trading

activity and shall publish regularly the bid and asking prices for units traded.

(c) In this section, "efficient public market" means a market in which the units distributed under this chapter have a readily ascertainable market value and in which they may be bought or sold readily without unnecessary or unreasonable transaction costs.

Sec. 43.90.310. WAIVER. The provisions of AS 38.05.125, 38.05.183 and AS 38.06 shall not apply to a conveyance under this chapter.

ARTICLE 7. DEFINITIONS.

Sec. 43.90.320. DEFINITIONS. In this chapter:

(1) "beneficial interest" means an equitable interest in cash of the trust estate including without limitation the proceeds from the conversion of the royalties to cash, and in right to cash from such conversion of royalties, but does not include any legal or equitable title in or to the royalties as any part of the royalties;

(2) "certificate" means a certificate issued by the trustee evidencing ownership of one or more units;

(3) "certificate holder" means the owner of a certificate as reflected on the books of the trustee;

(4) "commissioner" means the Commissioner of Revenue;

(5) "conveyance" means the transfer of royalties to the trust by the state;

(6) "eligible individual" means an individual who is a resident as of an eligibility date determined by the commissioner;

(7) "individual" means a natural person;

(8) "resident" means an individual who maintains a permanent place of abode in the state with the intention of making the state his permanent place of residence and who resides in the state continuously except for temporary purposes only and with the intent of returning; a person may not be considered to have gained a residence solely by reason of his presence and he may not lose it solely by reason of his absence while in the civil or military service of this state or of the United States or by reason of his absence because of marriage to a person engaged in the civil or military service of this state or the United States; a person may not be considered to lose his residence while a student at an educational institution, while in an institution at public expense, while confined in prison, while engaged in the navigation of waters of this state, of the United States, or of the high seas, or while residing upon an Indian or military reservation; a minor takes the residence of his parent or of his legal guardian; a married person may establish his or her own residence and does not presumptively take the residence of the other spouse;

(9) "royalties" means the royalties conveyed to the trust pursuant to this chapter;

(10) "trust" means the trust created by and administered under the terms of this chapter and the trust indenture;

(11) "trustee" means the entity serving as trustee of the trust and includes any successor trustee;

(12) "trust estate" means the assets held by the trustee under the trust and shall include both income and principal;

(13) "trust indenture" means the trust indenture originally executed by the Commissioner of Revenue and the trustee under this chapter, or if amended or supplemented, as so amended or supplemented;

(14) "unit" means an undivided fractional interest in the beneficial interest.

~~Sec. 2~~ Sec. 2 This Act takes effect immediately in accordance with AS 01.10.070(c).

Cook ✓

Original sponsors: Gardiner and Rogers

1 IN THE HOUSE

BY THE SPECIAL GAS
PIPELINE COMMITTEE

2 CS FOR HOUSE BILL NO. 33 (Gas Pipeline)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

5 A BILL

6 For an Act entitled: "An Act establishing the portfolio of Alaska citizen
7 enterprises; and providing for an effective date."

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

9 * Section 1. DECLARATION OF POLICY, PURPOSES AND FINDINGS. (a) It is
10 the policy of the state to provide for the use, development, and conserva-
11 tion of the state's natural resources and the income derived from them for
12 the maximum benefit of its people.

13 (b) The purposes of this Act are to

14 (1) increase the income of state residents by transferring part of
15 the wealth derived from the natural resources of the state to them;

16 (2) provide a means for the direct participation of state resi-
17 dents in the financing of business enterprises which benefit the state, and
18 to provide residents with the opportunity to share in potential profits;

19 (3) encourage greater participation in and understanding of the
20 capitalist system by state residents through a wider distribution of economic
21 interests in state business enterprises;

22 (4) encourage increased awareness and involvement by state resi-
23 dents in the management of state natural resource production and develop-
24 ment, in state participation in business enterprises, and in the development
25 of local industry.

26 (c) The legislature finds that

27 (1) it is in the public interest and furthers a public purpose to
28 distribute a part of Alaska's wealth derived from natural resources to state
29 residents to increase their income and their involvement and awareness

1 regarding the management of the state's natural resources, the development
2 of its local industry, and the capitalist system;

3 (2) a mechanism allowing the state to distribute a part of its
4 resource wealth to residents will best promote the state's interest in
5 creating direct involvement by residents in the decisions concerning the
6 state's natural resource management; and

7 (3) a mechanism to provide a means for direct participation by
8 state residents in business enterprises will best promote the state's inter-
9 est in creating involvement by residents in the decisions concerning state
10 investments and development of local industry.

11 (d) Except as otherwise required by law, it is intended that distribu-
12 tions to residents under this Act shall be unencumbered property.

13 * Sec. 2. AS 43 is amended by adding a new chapter to read:

14 CHAPTER 17. PORTFOLIO OF ALASKA CITIZEN ENTERPRISES.

15 ARTICLE 1. PORTFOLIO OF ALASKA CITIZEN ENTERPRISES PROGRAM.

16 Sec. 43.17.010. ESTABLISHMENT OF PROGRAM. The portfolio of
17 Alaska citizen enterprises is established in the department to provide
18 for distribution of state assets to state residents.

19 Sec. 43.17.020. INVESTMENT ADVISORY COUNCIL. (a) The Investment
20 Advisory Council is established composed of the commissioner and six
21 members [with training and experience in investment] who are appointed by
22 the governor. Appointed members shall serve two-year terms, except
23 that three of the initial members shall be appointed for one-year
24 terms.

25 (b) The council shall develop proposals for portfolio plans for
26 distribution of state assets which meet the objectives of this chapter.
27 Proposals shall be submitted to the department for detailed study and
28 recommendations in accordance with AS 43.17.030.

29 Sec. 43.17.030. PORTFOLIO PLANS. (a) The department shall study

1 proposals for portfolio plans and develop portfolio plans for distribu-
2 tion of state assets. A portfolio plan must

3 (1) provide for contribution or transfer of assets owned by
4 the state or to be acquired by the state;

5 (2) provide for distribution of interests in the assets
6 owned by the state or to be acquired by the state to eligible residents
7 by issuing certificates representing units of

8 (A) a state energy resource trust;

9 (B) a state industrial development project;

10 (C) a state investment fund;

11 (D) a state real estate trust;

12 (E) a business enterprise.

13 (3) specify the assets to be distributed;

14 (4) specify how the assets not then owned by the state will
15 be acquired by the state;

16 (5) specify the date on which an individual must be a state
17 resident to be eligible to participate in the distribution of units
18 under AS 43.17.060 - 43.17.090;

19 (6) specify how an individual applies for a unit;

20 (7) specify the types of assets involved, an appraisal of
21 their value, the number of units to be distributed, and the manner in
22 which the units will be distributed;

23 (8) specify the terms of payment for units to be sold and
24 the number of units to be distributed without charge;

25 (9) specify restrictions on the transfer or encumbrance by
26 the state of a distributed unit;

27 (10) provide a financial assessment of the portfolio plan
28 including

29 (A) administrative costs;

- 1 (B) initial costs;
- 2 (C) a projection of future costs;
- 3 (D) contingent costs or liabilities;
- 4 (E) a projection of future earnings;
- 5 (F) value of the units in the plan;
- 6 (G) probable financial and tax consequences for pur-
- 7 chasers and recipients of units;
- 8 (11) list and evaluate state and federal laws and regulations
- 9 affecting the portfolio plan;
- 10 (12) propose legislation needed to implement the portfolio
- 11 plan; and
- 12 (13) include other information considered necessary by the
- 13 commissioner.
- 14 (b) If a corporation or trust is needed to implement the port-
- 15 folio plan, the plan must include
- 16 (1) the proposed articles of incorporation and bylaws of the
- 17 corporation or the proposed trust indenture of the trust;
- 18 (2) the names of the incorporators and directors of the
- 19 corporation or the trustees of the trust or the method of selecting
- 20 those individuals.
- 21 (c) A portfolio plan developed by the department shall be sub-
- 22 mitted to the Investment Advisory Council.
- 23 Sec. 43.17.040. HEARINGS. (a) The Investment Advisory Council
- 24 shall hold public hearings on a portfolio plan. The council shall
- 25 report recommendations and observations of the public concerning the
- 26 plan to the commissioner.
- 27 (b) After reviewing the report submitted by the Investment
- 28 Advisory Council and considering public comments, the commissioner may
- 29 adopt recommended changes to the portfolio plan before submitting it to

*leg may request plan
by resolution*

1 the legislature for consideration.

2 Sec. 43.17.050. PORTFOLIO PLANS SUBMITTED TO LEGISLATURE. (a)
3 The commissioner shall submit one or more portfolio plans to the legis-
4 lature on or before the 30th day of each legislative session. A port-
5 folio plan shall include a report containing public comments on the
6 plan and identifying recommendations submitted by the public which are
7 included in the plan.

8 (b) A portfolio plan may not be implemented until it has been
9 approved by law.

10 ARTICLE 2. DISTRIBUTION OF UNITS.

11 Sec. 43.17.080. ELIGIBILITY. (a) To be eligible to receive a
12 unit distributed under AS 43.17.110, an individual must

13 (1) be a resident of the state on the eligibility date
14 established in the portfolio plan under which the unit is distributed;

15 (2) apply to the department; and

16 (3) submit with the application a signed, sworn certifica-
17 tion that he was a resident of the state on the eligibility date and
18 other proof of residency as the commissioner may require.

19 (b) The department shall prescribe and furnish a form for ap-
20 plications and for certification of residency.

21 Sec. 43.17.090. NUMBER AND PURCHASE PRICE OF UNITS ISSUED. (a)
22 For each portfolio plan the commissioner shall establish a purchase
23 price for each unit to be sold.

24 (b) The commissioner shall determine the total number of units to
25 be distributed under a portfolio plan by dividing the value of the
26 assets contributed under the plan by the purchase price for a unit
27 established under (a) of this section.

28 (c) The value of assets contributed to a state industrial develop-
29 ment project, a state investment fund, a state real estate trust, or a

1 business enterprise, is equal to the cost to the state of the assets
2 contributed to the portfolio plan, plus an amount that compensates the
3 state for the administrative costs of acquiring, holding, and dis-
4 tributing those assets.

5 (d) The value of assets contributed to a state energy resource
6 trust is the conservatively appraised value of the assets. A con-
7 servatively appraised value for assets in a state energy resource trust
8 is a value determined by generally accepted appraisal methods.

9 (e) Before a sale of units, the commissioner shall publish notice
10 of the purchase price.

11 Sec. 43.17.100. DISPOSITION OF PROCEEDS. The commissioner shall
12 deposit net proceeds from the sale of units under this chapter into the
13 general fund.

14 Sec. 43.17.110. FREE DISTRIBUTION. A part of the units to be
15 distributed in accordance with AS 43.17.090(b) shall be distributed
16 equally without charge to all eligible individuals who apply to receive
17 them. The commissioner shall establish a method for distribution of
18 units under this section.

19 ARTICLE 3. GENERAL PROVISIONS.

20 Sec. 43.17.150. DISPOSITION OF UNITS. A portfolio plan may
21 include restrictions on the transfer or disposition of units.

22 Sec. 43.17.160. AUTHORITY TO PARTICIPATE IN MARKET. (a) If the
23 commissioner determines that an efficient public market does not exist
24 for the sale of units, he may buy, sell, and trade in units for the
25 purpose of establishing a market.

26 (b) If the commissioner trades in units as authorized in (a) of
27 this section, he shall maintain an average markup sufficient to compen-
28 sate the state for the administrative costs of his trading activity and
29 shall publish regularly the bid and asking prices for units traded.

1 (c) In this section, "efficient public market" means a market in
2 which the units distributed under this chapter have a readily ascer-
3 tainable market value and in which they may be bought or sold readily
4 without unnecessary or unreasonable transaction costs.

5 Sec. 43.17.170. WAIVER OF RESTRICTIONS. AS 37.10.085 does not
6 apply to the acquisition of assets under this chapter.

7 Sec. 43.17.180. REGULATIONS. The department may adopt regula-
8 tions necessary to administer this chapter.

9 Sec. 43.17.190. PENALTIES. In addition to any criminal penalties
10 imposed, if an individual is convicted of perjury or unsworn falsifica-
11 tion on the basis of a certification made under AS 43.17.080 and the
12 conviction is not reversed, he is not eligible for a distribution of
13 units under this chapter.

14 Sec. 43.17.200. DEFINITIONS. In this chapter,

15 (1) "assets" means shares of stock, debentures or other debt
16 obligations, royalties or other interests in minerals, or other inter-
17 ests in business enterprises or natural resources;

18 (2) "business enterprise" means a private corporation en-
19 gaging or about to engage in the state in manufacturing, transporta-
20 tion, communication, trade, services, natural resource extraction, or
21 natural resource processing, whose securities the commissioner has
22 purchased under AS 37.10, or has proposed to purchase under the terms
23 of a portfolio plan established under this chapter;

24 (3) "commissioner" means the commissioner of revenue;

25 (4) "department" means the Department of Revenue;

26 (5) "eligibility date" means a date established by the
27 commissioner for a distribution of units under a portfolio plan estab-
28 lished under this chapter;

29 (6) "individual" means a natural person;

1 (7) "resident" means an individual who maintains a permanent
2 place of abode in the state with the intention of making the state his
3 permanent residence and who stays in the state continuously except for
4 temporary absences taken with the intent of returning; an individual is
5 not a resident solely by reason of his presence and does not cease to
6 be a resident solely by reason of his absence because of marriage to a
7 person engaged in the civil or military service of this state or the
8 United States; an individual does not cease to be a resident while a
9 student at an educational institution, while in an institution at
10 public expense, while confined in prison, while engaged in the naviga-
11 tion of waters of this state, of the United States, or of the high
12 seas, or while residing in an Indian or military reservation; a minor
13 takes the residence of his parent or of his legal guardian; a married
14 woman may establish her own residence and does not presumptively take
15 the residence of her husband;

16 (8) "state energy resource trust" means a trust established
17 under this chapter the assets of which consist of a right to receive
18 income equal to a specified part of the rentals, royalties, or net
19 profits belonging to the state under specified leases of state land for
20 the extraction of oil, gas, coal, oil shale, or other minerals or a
21 specified part of the revenue from the sale of oil, gas, coal, oil
22 shale, or other minerals taken by the state as in kind royalties under
23 those leases;

24 (9) "state industrial development project" means a business
25 enterprise engaged or about to engage in the state in manufacturing,
26 transportation, communications, natural resource extraction, or natural
27 resource processing, and to which the state or an agency or subdivision
28 of the state contributes an investment of equity or debt exceeding
29 \$100,000,000;

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29

(10) "state investment fund" means a regulated investment company organized in accordance with subchapter M, Chapter 1 of the Internal Revenue Code of 1954 as amended (26 U.S.C. secs. 851 - 855);

(11) "state real estate trust" means a real estate investment trust organized in accordance with subchapter M, Chapter 1 of the Internal Revenue Code of 1954 as amended (26 U.S.C. secs. 856 - 858);

(12) "unit" means an undivided fractional ownership right or interest in a trust, corporation, fund, project or enterprise established under this chapter.

* Sec. 3. This Act takes effect immediately in accordance with AS 01.10.-070(c).



UNIVERSITY OF ALASKA
JUSTICE CENTER
3211 Providence Drive
Anchorage, Alaska 99504

December 10, 1980

Representative Hugh Malone
P. O. Box 9
Kenai, Alaska 99611


Dear Mr. ^{Hugh} Malone:

As a person who has given special thought to some of these issues, you may find some of this analysis helpful in formulating your own thinking.

The articles were not intended to provide answers so much as to stimulate others, closer to the action, to formulate their own.

Best wishes for the holiday season.

Sincerely,


John E. Havelock

JEH:pb

ALASKAN WEALTH MANAGEMENT

BY

JOHN E. HAVELOCK

THIS SERIES OF ARTICLES APPEARED IN THE ANCHORAGE TIMES
OCTOBER 26 THROUGH NOVEMBER 1, 1980

ALASKAN WEALTH MANAGEMENT

PART I

The Midas Touch

The embarrassment of wealth is a legendary topic in every culture. Few children are not familiar with the misfortune of King Midas, who transformed the flowers in his garden and even his precious daughter into inanimate gold. Who has not savored the story of the man given three magic wishes? The tale requires him to use the last one to restore himself to his previous condition after avaricious commands in the exercise of the first two produced unexpected and unwanted results. The parent telling this tale will often hear from the child, "Well, Daddy, what if he had asked that only one finger would turn things to gold?" or some alternative choice of wishes which could have lead to a more pleasant and successful result.

The child's point is a good one and the principal moral of the story is threefold: not that wealth or power inevitably brings disaster but that it can bring disaster, that impulsive choices (particularly if based on greed) are often wrong and that once made, a choice often has irrevocable consequences.

RELATION TO d-2. Alaskans can find much to agree with in these folk tales as they address the issue of wealth management for the 1980's. It is a matter of considerable disappointment as we enter the second phase of election 80 that few of those who offer themselves as candidates for Alaskan office seem to have considered the magnitude and scope of the premier issue of this

time and place.

In part, the dramatic pyrotechnics of the d-2 battle may be credited with overshadowing this area of public policy. For some individuals, the perception of threat to a lifestyle understandably brings out high passion. But the dollar value of the difference between the wealth development potentials in the most recent competing versions of the land settlement do not come close to matching the magnitude of the responsibility involved in managing the billions of dollars which are already in firm prospect from Prudhoe Bay.

While value estimates are inherently volatile as a result of the political control of the price of oil, it is not unreasonable to use numbers in the forty billion dollar-plus range to describe revenue to accrue between now and the year two thousand. Unlike the value of various proposed economic development projects, this is a net return figure, accruing to the state without any more work than it takes to carefully count it. As a people, we Alaskans are to be, for a time, the richest the earth has ever seen but whether this wealth may be the Midas touch is still an open question.

THE MAGIC OF MAGNITUDE. If we have done badly so far both in addressing and failing to address this wealth opportunity which is also a problem, it may be because of the magical aspect of it. The magnitude of the oil revenue is well beyond any ordinary experience of windfall. Thus the earliest public policy reaction was to put a little away for a rainy day by creating a "permanent fund" as if the selection of such a title could resolve

the hard investment questions which accompany the stewardship of great wealth. To this "permanent fund" the state dedicated a minor fraction of the income flow, no policy formation attending the management of the remaining bulk of the income.

STRANGENESS OF PUBLIC WEALTH. The other unfamiliar aspect of this wealth is its collective nature. We are at least familiar on a vicarious basis with the private, unanticipated inheritance - the Irish sweepstakes winner or the nephew of humble means who becomes a millionaire when a never-seen uncle dies in Australia.

In the end these models of private wealth management are likely to play a major part in the development of a philosophic policy for the state; but, they are different. For whether these fortunes are squandered in riotous living and fruitless speculative schemes or husbanded for the ultimate benefit of philanthropy, as in the case of Carnegie, Rockefeller and some other great fortunes of the turn of the century, it is still a private matter. The Alaskan return is a subject of public trust.

American history found no room for the accumulation of public wealth. The revenue function of government was to collect no more than was essential to an established minimum of collective needs. To tax beyond the requirements of an operating budget was unthinkable. While state and local governments did experience revenue from the disposition of public resources, notably land, seldom if ever did these revenues rise above the requirements of budget maintenance. In fact, much of America's public land was sold to keep taxes down. It is not surprising then if, after

-4-

a rainy day gesture, the next response of the Alaska public was to abolish non-oil taxes on a wholesale basis.

PART II

Limitations on Income

The regular session of the legislature is likely to pick up with the same subject as the special session: tax relief. A multibillion dollar state surplus certainly invites the question: What do we collect taxes for?

We can expect a number of lesser taxes to blow away with the wind. The focus of attention is likely to be on property taxes and oil taxes.

ARE OIL TAXES TOO HIGH? In most respects oil can make the most plausible case for tax reduction. The usual justification for taxes is their necessity to meet the ordinary expenses of government services. There is enough money in royalty payments alone to meet all current state expenses. Since the surplus is in large measure a product of the taxation of oil, does not fairness require the repeal of oil taxes?

This argument, which has a firm foundation in the history of state taxation, is not likely fully to carry the day, if only for political reasons. A more limited objective has been outlined by at least one influential leader: to reduce oil taxes to the level pertaining in the average of other states. This may be a pragmatic middle ground but the logic of this position on the purpose of taxation allows total repeal.

PURPOSE OF OIL TAXES. Those who will argue for the existing rate of taxation must argue a more expanded function for tax

policy: that resource taxes are intended to recoup part of the value of the oil for the general public. This is certainly the tax philosophy of all major oil producing countries outside of the United States. To some extent it can be said to be the tax position of the federal government with respect to, for example, the "windfall profits" tax.

But is a "fair share" philosophy the right tax position for a state? Maybe the value of the oil should be shared with the rest of the United States through enhanced oil company profits invested in energy investment or reduced prices via the operation of the free market. The industry may also renew their argument that oil taxation is an unfair adjustment of the contract bargained for and entered by them initially in bonus bidding on north slope leases.

EARLY HARVEST OR EXCESS TAXATION? Those resisting the oil tax reduction will argue, as they did in the years that the taxes were raised, that the possibility of increased taxes was part of the original bargain. Variable taxes on resource wealth produced from state land are a reasonable way to assure a reasonable return to the people from that resource. It is not the same thing as a tax on the productivity of labor.

Further, they may point out, this year's large tax and royalty income is a result of the imperatives of pipeline flow requirements and national energy policy, not state interest. State interest alone would dictate drawing on the oil a little at a time as income was needed to supplement state taxes in meeting frugally budgeted state expenditures. These years, the State of Alaska is not just

raising money for annual expenditures but taking an early income harvest thrust upon it which will be needed in 10 - 25 years.

DEFERRING INCOME. A major alternative to "giving it back to the oil companies" may be deferred income, an effort to reduce income now in favor of receipt at the time perhaps ten years hence when the oil flow and government revenue are in sharp decline.

LEAVE IN THE GROUND? The likelihood of producing another Prudhoe Bay on state land (including tide and submerged lands) as distinct from federal lands which now hold the most promise, is too small to provide a planning hypothesis for the economy of the state government. Statements from various public optimists notwithstanding, the numbers and planning data from those who are in a position to know in the oil industry do not support the idea of other Prudhoes around the corner. Thus, though bonus bids derived from further oil leasing on state land will exaggerate and prolong the income bubble of the 80's, it will not do so in a substantial way.

On the other hand, one might ask, where do we start in spreading income into the future? What on earth is the state doing in pursuing an active leasing schedule when we have more money than we can use for a decade? Even when, as in the most recent lease offering, the bonus values are a paltry \$12,000,000, it would help a little if the state could leave it in the ground a few more years. Investments as good as oil are hard to find. Its

value will increase faster in the ground than above. On the other hand, the lead time in developing a field may be long enough that today's leases will mean income more than a decade hence when we will need it again.

TRADING PRESENT OIL FOR FUTURE OIL. A greater impact on revenue flow would result from the enactment or negotiation of deferred income arrangements with the owners of the non-royalty oil. For example, instead of taking one eighth of the oil now, we could agree to take a more limited fraction now in favor of a larger percentage of ownership of oil produced after 1990. Arrangements of this kind might help to keep the state out of ventures in the oil business. On the other hand, since oil is politically priced, as good as the future looks, is oil a commodity which the state should keep as its nest egg?

PART III

Limiting Income: Other than Oil

The flood of income from royalty and taxation on oil wealth quickly washed away the ground under all other forms of taxation. Suddenly we are in a topsy-turvy world in which the functional tension of government is sprung. No longer is the state to squeeze taxes out of those with income to provide services of common demand with (perhaps) a greater emphasis on the call of those least able to help themselves.

The principal functions of government are now distributive. The benefits appear to be painless. Governor Hammond, arguing that at least the concept of payment for services be preserved for the generation of the 90's, finds his pleas swept aside by the deluge in a 24 hour special session of the State House.

The normal status of state government is an equilibrium, after combat, between demands for service and the resistance of the taxpayer. Released, the demand side mushrooms, often in glaring examples of conspicuous consumption or waste. While expenditures climb, all vestiges of counterbalancing revenue from taxation are repealed with little debate except, of course, those on oil.

PRECIPITOUS DECLINE IN REVENUE. Though they receive little attention now, there are justifications of taxations beyond the need to raise general revenue. First, since the revenue is non-recurring, maybe we should be thinking about spreading the income

over decades to come. The tax necessities of the future are greatly exaggerated by discharge of the present tax burden. By repealing all taxes, we abandon hope of returning to the normal equilibrium short of the public and private anguish of decades of reimposed and sharply escalating taxes accompanied by sharply declining services. The down curve on the far side of the state wealth bubble has become a precipice.

NEW CLAIMANTS ON THE STATE TREASURY. Since money is plentiful, the argument that a particular state expenditure benefits that part of society that least needs it is lost. The tenuous distributional fairness of governmental activity is jeopardized. Since the money is no longer extracted from the people, expenditures can provide a greater benefit to those that are already well off. If there is no resistance to expenditure from those who must pay, if the pie is not a limited pie, then there is no protest when large portions are sliced out by interests with little traditional claim for need.

If the tourist industry will benefit from expanded national advertising then advertise; if the fisheries will benefit from increased attention to the conservation of the fisheries then add conservation programs and officers; if the construction industry will benefit from public works then build. As well as providing sewers to hard-pressed urban areas, let's use public funds for sewers wherever people live. Suddenly every successful industry in Alaska wants the benefits which are normally

distributed for hard fought reasons to distressed industry or to people of generally acknowledged deserving need.

TAXES FOR COMMON COSTS. Ordinarily, government collects taxes not only for general income, but as a service so that all those who benefit from a collective expenditure are compelled to meet their share of the cost. There is no redistributive effect.

When we abandon the principle that taxation shall be required for service that the beneficiary is able to pay, we may be distributing a subsidy not for any social or economic purpose, but because the money is there. The elimination of a tax which goes to pay for a particular service has the same effect as an expenditure for a subsidy. Is this kind of income transfer arrangement justifiable or should the oil companies have their tax dollars back?

This problem becomes more acute when the subsidy is not only in the form of free public services but in direct assistance to private enterprise via subsidized interest rates.

THE THREAT TO FREE ENTERPRISE. Unjustifiable subsidy works like excess calories on the human body. A subsidized industry is not exercised by the free enterprise system but spoons in the dollars. When the subsidy is cut off (as will inevitably be the case), the industry will be uncompetitive and collapse, corrupted by bad economic habits. The inefficient and uncompetitive American shipbuilding industry leads the list of examples of this principle.

From a broader historical perspective, grim predictions of

the impact of running out of money on both the public and private sectors may be overdrawn. There are parallels. All America may now be going through a similar crisis as we prepare our appetite for high cost alternative fuels after a generation of super-cheap gasoline. But the nation wonders how we could have read the numbers without realizing that a policy must be available to meet the coming drought in oil. The current national economic gloom is in many respects a consequence of the improvident policies of the 60's and 70's.

Would America be in better shape if we had recognized in our national policies that cheap oil was on the way out and that the country's reserves of this non-renewable resource would inevitably dwindle? The parallel between America a decade ago and Alaska today poses a challenge. But if Alaskans are not prepared to debate the question, it should not be surprising if the results are ultimately sour.

PART IV

Controlling State Expenditure: Demands of the Private Sector

One of the ironies of the present call for limitations on state expenditures is that some of the strongest calls come from those who have been the beneficiaries of the most recent government expansion. A recent estimate gauged that a thousand dollars per capita was appropriated in 1980 to special loan programs while only half that amount went to tax refund distribution.

While long standing government programs enjoyed relatively modest budget increases (considering current inflation rates) last year, major increases in expenditure have been made in direct and indirect support of the business community and private economic enterprise.

Many of the more conservative voices in the state who, one might think, would stand firm against government involvement in the private economy have been heard to urge that all of the Alaska's new wealth be reinvested in private industry in the state without apparent reservation concerning the political and economic consequences of such action.

ROAD TO SOCIALISM. A recent economist visiting the state pronounced his concern that Alaska's wealth would tempt the state to expand service programs thereby pushing the Alaskan people along the road to socialism. Socialism is defined by conventional economists of left and right as government ownership of the means of production.

Alaska is surely one of the most conservative

states in a conservative country. If a single voice has been raised in the legislature calling for a massive increase in government programs in the social sector, it has not received much attention. The outcry is all for investment and capital projects.

RIDING THE TIGER. On this trend to government expansion, the itinerant economist could have made his point. If the state does indeed invest its multibillion surpluses annually in businesses within the state, it will own all the non-oil business in the state very quickly. Nor is the legislature likely to avoid supervision of its interest in business because some equity is reserved in private hands if ninety percent of the value consists of invested state wealth. The entrepreneurial community that wishes to ride the state tiger for the advantage of her economic power may end up inside her.

There is a limited market for new capital in Alaska. It is simply not true that billions of dollars worth of economic activity await only the availability of funds to take off. Every touted industry, on close examination (the bottom fishery is a more recent example) reveals that other major efficiency hurdles in management, transportation, communication and labor impede development.

INFLUENCE OF WORLD MARKETS. The final parameter controlling such developments is the world market price as set by international competition. You cannot make a submarginal economic prospect profitable by throwing money at it. Alaskans are in some danger of spending billions of dollars in subsidies to prove that

principle.

If a big project is, in fact, economically feasible, money experts such as the Inter-American Development Bank's John Elac say there is not likely to be a lack of investment capital to support it. The lesson for Alaskans may be that by investing in projects no one else will buy, we end up with what Belden Daniels has called "lemon socialism" - state ownership of unprofitable industry.

A distinction can be made, however, between major enterprise and small business. Despite the need for great caution in state investment policy, there may be gaps in the supply of money for small scale enterprise, gaps which the state can address - carefully and with a relatively small proportion of its annual revenue. But such programs must use clear loan criteria of general application. One of the greater risks in funny loan programs is corruption.

Before going into the loan business, the question must be asked: to what extent may this need be met by the existing banking structure? There is an old saying that "bad money will chase out good". Private investment will leave Alaska wherever public dollars are made available at interest costs below market.

STATE VENTURE CAPITAL. The kind of capital for which demand is likely to be greatest is venture capital, money for the higher class of risk. Normally, sound investment policy requires that the venture capital investor take a piece of the equity as a way of guaranteeing a reasonable, average return considering the

higher proportion of outright losses that will be involved. Again the question arises, may this involve us in socialism? If the state does end up with stock interests, how is it to vote this stock when points of policy are involved?

THE STATE IN THE PRIVATE ECONOMY. There are many possible answers to the overall question asked: what is the proper role of the state in the private economy? Indirect support such as carefully scrutinized communications and transportation facilities, community development, marketing development studies, manpower development, and research avoid some of the problems of excessive involvement cited. But public debate is not helped by impassioned cries that Alaska's money be invested in Alaska.

FACING HARD QUESTIONS. Who would argue against such a proposition - to a point? The real questions are not being asked or answered: how much is enough? How is it delivered? Should there be other policy objectives involved? - a regional distribution preference, for example? Who are the beneficiaries? Is this trickle down socialism with an unseemly slice of benefit going to those who need it least? Are we creating an unaccountable bureaucracy of state employed bankers?

Whatever it may do, the economic power of the state today is so great that any role we permit the state to play in the economy could easily slip into a dominant role.

A MINI-FED: Recognizing that fact, it may be that the state, which has already established a series of new banking institutions should limit itself to one more model, the federal reserve system.

IV - 5

The state might exercise a moderating role in the ups and downs of the state's economy through a policy-oriented, deposit and bank interest policy, without pushing us into a state-run state. But in the end, most of our surplus must be invested outside the state to keep the state from taking over the private economy.

PART V

Privatization

It is strange in many respects that the state's citizens, while they have wandered to Norway, Venezuela and even Kuwait to gather experience in wealth management, have paid almost no attention to the single most appropriate example in their own backyard: The Alaska Native Claims Settlement Act. Both in what was intended and in the results (about which much is knowable but far too little known) the Settlement is a forerunner to contemporary state experience.

In 1971, the Congress found itself faced with the prospect of developing a plan of distribution for what then seemed an enormous sum - over \$900 million in state and federal revenue to be delivered over more than ten years. In part the Congress was settling a legal claim. But the Congress had a larger objective: to create an economy to support the Alaskan Native people, while preserving the patrimony and without expanding the people's already dangerous dependence on handouts.

The experience with personal distributions in the past settlements of Indian claims had not been good. The money or property quickly seemed to pass through the hands of those intended to be benefited. Lasting improvements were rare. Examples of profligacy were all too common.

Yet it was recognized that there would be an immediate outcry if something was not realized immediately from adoption of the Act. Accordingly, a provision was included for a ten percent

cash pass through to every beneficiary under it. One wonders here that distribution went. It would be worth having a comprehensive answer, but not all would care to hear.

STATE DISTRIBUTIONS. The State of Alaska is now facing a somewhat similar dilemma. We have a very large amount of money in which, some say, each Alaskan has a pro rata property interest. Others assert that, as a one time yield of the bounty of the earth, it is vested with a trust which includes Alaska generations as yet unborn.

Many hope that in the long run these funds can be used to provide the state with a stable and prosperous economy and a government which provides adequate service on a tolerable tax load. The Statehood Act required that the state reserve an interest in its subsurface resource precisely because the Congress did not believe that taxation alone would be enough to sustain the cost of government services in the new state.

Because there is so much, there is a considerable demand that some of the money be handed out in cash distributions - some would have it all so handed out. The term used is "privatize" - turn the public wealth into private wealth.

Governor Hammond proposed and the legislature has adopted a scheme to distribute cash according to a plan meeting several other policy objectives - notably encouraging of savings in the Permanent Fund. His draftsmen, like any who prepare actual programs of distributions, must answer other tough policy questions too. Just who is eligible for a distribution; should entitlements be differentiated based on some other policy criteria? Perhaps

inevitably, the answers to these questions have met constitutional objections. The outcome, as of this writing, is unknown.

CASH OR CAPITAL? Whether or not this particular plan survives constitutional challenge, pressure to distribute funds directly to the people will remain, as it has with public lands. This pressure will balance against concern that some of the wealth be preserved in capital form (as was the intent, for example, of the scheme of the Settlement Act).

The effort to preserve capital could take the form of non-cash distributions. By distributing stock or by having the State or a State-created institution or series of State-sponsored institutions hold stock and invest it for the account of individuals, capital will be preserved. The beneficiary may be entitled to freely transfer that entitlement or not but some capital preservation is involved. In a sense this is why the Permanent Fund disbursement program is characterized as a "dividend" program. The Settlement Act allowed for the establishment of a series of government sponsored corporations to preserve the capital appropriated by the Congress.

ELITISM VS. POPULISM. There is at least a whiff of populism vs. elitism in the contending arguments. The populists will say that the people know best how to use "their" cash. The elitists (who will say they are just more worldly-wise populists) will point out that history does not sustain this position.

SURGE IN CONSUMER SPENDING. In our consumer-oriented society it is unlikely that much of any cash distribution will end up as capital investment. It would be interesting to see what has

become of the state tax refund by January 1. Is it disputed that almost all of it will be spent on consumer goods? It would be useful to know just what is occurring. This stimulation of consumer spending does stimulate the economy. The sellers of such goods will reap a profit. But since consumer goods are virtually all manufactured outside this state, there is a very low secondary benefit from the consumer purchase dollar turnover.

On the minus side, a splurge of spending on consumer goods may encourage the unwise expansion of the merchandising sector of the economy - unless this form of handout is to become a regular feature of the economy. Lastly, this kind of distribution is subject to a big federal tax bite and unforeseeable consequences in the reaction of the national public. On the other hand cash handouts are hard to argue with, particularly just before Christmas. The issue is only one of degree.

INVESTMENT TRUSTS. Such objections to cash distribution will not prevent their happening but may temper their amount and frequency. Middle ground positions are likely to prevail. Several schemes are under discussion in government circles involving the distribution of a property interest which is capital in form but which can be alienated for cash. In any case, only a part of the state's surplus will be given over to privatization schemes.

According to one school of thought, distribution of a power of investment may prevent raids on the treasury for big project financing. People tend to push projects, even if unfeasible, if they see some spinoff benefit to themselves. The public will be less inclined to push money into doubtful development schemes in

the hope of getting some spinoff benefits from the process, if the citizen can direct that investment himself and sees his main benefit as return on investment rather than spinoff.

Capital distributions certainly operate more equitably than state loan programs which give the benefit to those whose superior financial position allows them to borrow. By letting the citizen be the lender, capital distribution gives every citizen a direct stake in state investment policy.

TOO COMPLICATED? Apart from the populist argument, capital distribution schemes are challenged as too complicated to be understood or appreciated by the people. This may be so but the Alaska Native community soon grasped a very complex version of this concept. At the time of the Settlement Act, the Alaska Native community debated many complex issues such as having one big investment trust or a series of regional arrangements and non-profit vs. profit. The latter positions prevailed.

The final challenge to capital distribution may be a philosophical one: do we want to make every Alaskan a capitalist? Thus in the end, optional conversion features will likely be included in any kind of capital distribution program adopted.

PART VI

Limiting Public Sector Growth

While not a popular position today, some privately ask whether the State is now doing all it should to meet public service needs, particularly in rural Alaska. The point is a sore one because costs of delivery, as well as past deficits, make service distributions in rural Alaska something other than equal per capita in comparison with urban areas.

Apparent examples of abuse of service programs in rural Alaska, such as unused school houses, feed the illusion that needs are fully met. Those who have occasion to travel in rural Alaska know that serious deficiencies still exist, the kind of deficiencies that have usually pricked the conscience of the more fortunate into giving something up - it used to be taxes - in favor of the more needy. The urban areas also have a continuing demand for improved public services. The state park system is nowhere near as extensively developed as the U. S. Forest Service, for example. Does limiting public sector growth mean we will never address those needs?

Underlying the division of urban prosperity and rural want lie also some serious unanswered policy questions. What is the minimum level of service that the State should provide to everyone regardless of where he lives? The Molly Hootch case which gave a tentative and hesitant answer to this question in the area of secondary education has potential equivalents, whether or not they rise to the level of a constitutional question, in health,

housing, justice administration and many other categorical topics in which the State is involved in providing service.

DISTRIBUTIONAL EQUITY. The question of distributional equity also comes up with the shoe on the other foot. For example, a village which doesn't want the roads which are distributed to urban areas and whose citizens may not benefit from subsidized hydroelectric power projects, should they get payment in lieu of this benefit? If the poor village with high cost of service is in proximity to one of the wells which is the source of wealth, should it get a specially enhanced share? If so, how much? Service equalization needs to go hand in hand with tax equalization.

The measurement of categorical entitlement can also get the State involved in unintended interference with local plans and priorities. This kind of problem has produced a trend nationally towards general revenue sharing instead of categorical support.

Many of the same people who worry whether the needs of the region are being met are also antagonistic to the further expansion of state government. After tax repeal, limitation on state expenditure is the most popular rallying cry for any politician this year. Some very serious problems support the need for a state spending lid.

LOG ROLLING. When the taxpayer no longer stands as an obstacle to raised expenditure, it is easy for those who have or want to acquire an interest in state expenditure to scratch each other's backs in the time-honored tradition of log rolling. It should not be overlooked that those interested in sharing in State largesse through "investment" stand shoulder to shoulder with the

interested in direct appropriation.

THE LIMITED PIE. Though the current climate and situation seem to call out for control, little attention has been given so far to the consequences of various styles of limitations on expenditures. State expenditure patterns are fluid. An expanding state role has let new interests in without pushing others out. If a real, blanket lid is imposed, a great many interests will find that they are displaced. Ironically, in a limited pie, it is the commercial interests which may find themselves the first displaced as social service need sectors flex political muscle.

To avoid such a result, some large holes are being carved in the proposed lid for capital costs and bonding so that the construction industry, for example, which is a leading beneficiary of the state spending process, will not suffer. This is a hole that takes nonsense out of the restriction. Every capital project has program costs and maintenance associated with it.

LOCAL GOVERNMENT IMPACT. Another major feature of limitations on state expenditure is its effect in throwing costs back on local government, so another hole is proposed to allow unlimited revenue sharing. This may have the desirable effect of decentralizing government but it will not limit increases in government expenditure.

Some desirable policy results may emerge from the examination of this rather overrated policy solution. The state may come up with an acceptable estimate of just what this often talked of deficit in services is. The legislature may move towards a comprehensive program of revenue sharing bearing some relationship to categorical needs.

At its simplest reduction, there may be a major increase in per capita based distribution to local or regional government, including a regionalized cost-of-living formula, and a devolution of responsibility for traditional governmental service concerns.

The public may be let back in on the budget process via annual voting on the capital budget, or the larger elements in it as was the case earlier when the capital budget was largely funded by bonds.

However, not just an appropriation lid but the full range of necessary policy responses to Alaskan wealth management issues is required by burgeoning oil revenue. The policy issues should be faced directly. While it may provide a small part of the answer, a call for limitations on State spending is simplistic. We cannot adopt such schemes and go home, pronouncing our problem solved.

PART VII

Privatizing the Public Sector

A lid on state government expenditures is just one of the policy options open to the state in addressing special issues posed by the state's oil wealth. The issue of how we decide how money is to be spent is also an issue. Categorical formula funding could result in a massive shift to regional government, in theory government closer to the people.

While at the moment investment of state oil money in the state's private sector is a very popular concept, the full range of choices has not been presented. In a free market the people of the state would not be investment oriented but purchase oriented. Given the choice of a cash or loan program, the distribution would be preferred.

While the first splurge would undoubtedly be in consumer goods, in the longer run the average family would be likely to choose to spend a significant portion of their money on more of the things the State already has provided or could provide in some way. Recreational opportunity, medical benefits, education or other forms of self-improvement, a retirement fund, a night out at a sports or civic center, a broader or more current television entertainment spectrum are some of the examples. But the public will be averse to such needs if it means "more government."

The commitment of the average citizen to the expansion of the economic base of the state through enlarging the number of jobs

available and other supposed objectives of state economic policy is theoretical rather than arising from direct interest. Granted many Alaskans feel at least a little uneasy about chronic unemployment in some regional sectors of the economy; granted also that many, if not all, Alaskans can look at past boom times as period of improved income and maybe enhanced lifestyle.

But the majority of Alaskans who have been in Alaska for some time are not unemployed, nor facing likely unemployment nor desirous of changing what they are now doing to work in a petrochemical plant: they are interested in expanded benefits and the right to pick those benefits themselves. And this is what they hope to get out of the state's oil wealth. They just don't want the State to expand to provide them.

BENEFIT DRAWING RIGHTS. Among the possible initiatives which Alaska might explore to meet this demand are the distribution of benefit drawing rights. This approach has been discussed at some length in the education field but it could be expanded to cover other areas of categorical benefit.

As applied in education, instead of supporting a public school system with a practical monopoly on education, each person with school age children would get a certain value of education credits which would be donated to a school of the parent's choice. These credits may be cashed by the providing institution.

Thus a private or mixed economy of education would be created bringing the benefits of the competitive market to the education process, allowing the parent/child maximum freedom of selection and reducing the risk of self-serving expansion in one of the

great public bureaucracies.

Secondary education where this concept has received the most extensive discussion may be one of the worst places to try out such a system. A near century of tradition in developing a public school system and the public schools' role as the provider of a unifying experience for a pluralistic America may make an entirely new, privatized delivery system unfeasible and most certainly unpopular with the educational community.

The national food stamp program is another style of benefit entitlement. It is plagued by problems of definition of the benefit class that would not carry over to a universal program. Whatever its demerits it is a program in place. Food is an unlikely candidate for a state supplementary program.

MEDICAL INSURANCE. The benefit drawing right concept might be transferred to other areas where public bureaucracy and the structure of public policies are not considered such a threat. The purchase of medical insurance may be a ripe example.

An insurance benefit drawing right could assure the continued privatization of service management and delivery while relieving the State of the huge financial headaches which result from the failure of large numbers of Americans (whether from their own fault or poverty) to obtain such insurance.

THE CASE AGAINST CASH. In the dilemma created by the failure of private choice to prefer public rationality lies the reason to disfavor cash distributions. Yes, cash distribution will maximize individual choice, at least to a point. But individual choice will not result in some types of benefits such as roads,

parks and clean water which must be purchased collectively. Freeloaders should be forced to pay a share. There is also a larger objection to the free choice, cash distribution. If the money is just handed out many people will spend it most foolishly. If such people would then go away and die quietly that would be an appropriate solution. But they will not. They will clamour for more to meet the consequences of their failure to meet practical needs and those that have saved their money will end up picking up a double tab.

For this reason, the State should conserve from any hand-outs, except a benefit drawing right, enough to insure the minimum need which the society says we will end up providing on the demand of the improvident or unlucky.

TAX AVOIDANCE. Expenditures on behalf of our citizens to meet collective needs in established areas of public concern can have the additional major benefit of avoidance of federal taxation. The flaw in most distributions under active public discussion as well as in the 1980 tax refund of 1979 taxes.

Benefit drawing rights should be tax free if devoted to the traditional functions of government. Further, by transferring his benefit drawing right to another entity which may be a private provider, the citizen can show his dissatisfaction with a service in a manner, modeled on the free market system, which is practically forbidden to him under contemporary tax-service systems.

RETIREMENT NEEDS. Similar concern might be given to funding the needs of citizens of the state with respect to retirement

needs. The State is actively and directly involved in one retirement program now, the unique and praiseworthy Pioneer Home system. Fortunately, resident pioneers are not taxed on the attributable income that results from such residence.

One would think that before distributing cash as federally taxable income, or paying off low interest bonds issued in a different inflation climate, the surplus might be dedicated to tax sheltered systems for supporting Alaskan citizens in the lower earning years of later life in or out of a Pioneer Home. There is ample additional social justification if required. If we don't dedicate the distribution, the provident will end up paying for the improvident later anyway.

Localization, regionalization, privatization - these and other options for reorganizing the public sector should be considered. We are a bold frontier people and should not be timid or unimaginative in exploring and adopting bold approaches to the management of our extraordinary wealth. But in our enthusiasm for individualistic ends, we should not forget that many of our needs and desires will require collective action.

PART VIII

Required: A Long Term View

One of the overriding problems with the response of the Alaskan public to Alaska's wealth management has been its failure to recognize the long established distinction between public and private sectors of activity. The State money is seen, extraordinarily, by quite conservative people as the driving force in the state's economy without any assessment of the result that this might have in shifting power among the institutions of the state.

Part of our difficulty arises from the semantic confusion of "the state" meaning the state government, "the state," meaning the economic engine of the state, private and public sector, and the "state" meaning the collective will of the people of the state. Because of this confusion, people who might think differently on reflection are embracing quite unsettling concepts, confusion between private and public endeavor.

A second problem in overall approach arises from the semantic confusion which equates investment savings policy with growth policy.

THE MEANING OF GROWTH. Each of us has a vested interest in personal and community growth. I have a vision of where I want to be twenty years from now and what I hope my community will be like - happy people, engaged in satisfying work with ample recreational and personal development opportunity, leading full lives and me a part of that.

Given an inheritance which could be used to bring this about, each of us is forced to think what steps each of us in the community may take to move in the right direction. First let us recognize that just spending money will not bring about healthy change. Growth is a process in which we all engage, building a pattern out of individual long term plans and in which capital utilization is only one element. Some expenditure may be involved, but it is measured and focuses on concrete objectives leading one step at a time to that hoped for future.

THE MUSIC MAN. Music men will come to town to tell me what they can do for me, building a fine place, a great industry. But to follow them is to play to their tune surrendering freedom of choice; nor does the music man care about our dream for the future.

INVESTMENT POLICY. So hopefully we will avoid buying pie in the sky and follow our own prudent plan. Since the money is not to be spent as it comes in, for the bulk of the income we adopt an investment policy. This policy is intended to conserve and enhance assets until they are needed. Investment policy is socially neutral - to get the maximum return consistent with prudence.

It is not invested in new houses for our citizens or a power plant. We should have already scheduled such objectives into our plan for the future. Whether it is called spending or investment, putting more money into the community will most likely disrupt a carefully conceived plan. Our excess cash should be

invested for return and safety alone, somewhere where it will not mess up the community.

CONFUSION OF ACCOUNTABILITY. When social investments aimed at long term community goals are mixed with savings investments there is a confusion of accountability from which both ends will suffer. The social goals are compromised because we are losing money. Social benefits are hard to measure in the mix. The investment goal is compromised because we are handing out unearned and unaccounted benefit.

LESSONS OF THE SETTLEMENT ACT. We should gather and apply the lessons of the Native Claims Settlement in the management of these present funds given to all Alaskans. Most of the Settlement Act corporations soon learned the dangers of mixing social policy with savings investment policy. For example, at least one non-profit corporation has been independently established in each region to address social concerns.

The Native Corporations learned, sometimes the hard way, that there are not a lot of great opportunities in Alaska just waiting for investment capital. They also learned that it may be a better investment policy to go outside your region and even Alaska with most of your funds rather than force investment in local business.

They are also learning that economic activity is not an end in itself. Perhaps investing in steel mills or other heavy industry may make sense from the perspective of the national

als of India or other undeveloped nations. But most Alaskans
 me from a post-industrial age. Their lifestyle expectations
 a rightfully higher. They come to get away from the steel
 ls and assembly lines which employed their fathers. If a steel
 ll is economically feasible and can be operated consistently
 th environmental safety, fine, let someone build it. It is
 rt of the free enterprise way. But it is a part of someone
 e's plan, not ours, so we don't have to spend our own money to
 ke it happen.

THE SUBSISTENCE WAY. Other Alaskans, though they are not by
 ucation and experience post-industrial, value a way of life con-
 stent with subsistence hunting and fishing. That is not com-
 ible with every form of expanded economic activity. Planning
 owth for such people is unlikely to include conventional industry.

So it is that we should define our goals as a people and
 nd our wealth to achieve those goals where we can, investing
 e balance according to contemporary standards of prudence.

No, it won't hurt to have a little party once in a while,
 we should not accustom ourselves to handouts in support of
 lic luxury or private endeavor, either in cash or in subsidized
 ns to those of us who are capable of operating as entrepreneurs.

Nor will it hurt for us to give a little thought now and then
 the larger purposes of mankind. Alaskans do tend to become
 rly involved with the collective Alaskan navel. We might
 arge our horizons by asking whether any other frontier - of
 wledge, of human aspiration on a world scale, or of dire
 rivation - might be addressed by a tithing of our wealth.

A GREAT DEBATE. Above all it is important that we discuss among ourselves the policies of our wealth management. A major debate is in order. Much more public give-and-take is required among those who aspire to lead us and between them and the people. Nor should we rush to make decisions which may have lasting consequences. Time and attention may give Alaskans a special destiny. Many people before us have wasted great birthrights; none have had such an opportunity to demonstrate wise management of great resources for the general good and individual freedom. The challenge is breathtaking.

for Malone

Frances A. Ulmer
Director
Division of Policy Development
and Planning

November 14, 1980

Tom Singer
Policy Program Specialist
Division of Policy Development
and Planning

Royalty Trusts

Attached you will find the following documents:

1. Revised PACE memo focusing on royalty trusts;
2. Original October 1, 1979 BCRIC memo which served as the basis for the Governor's interest in privatization;
3. The March 27, 1980 Tussing final report on PACE (emphasis added for royalty trust sections); and
4. The March 26, 1980 Messenger legal memorandum on remaining legal questions with PACE.

These documents provide a good summary of previous PACE work efforts which can serve as the basis for future ground breaking on royalty trusts. Please note that a draft royalty trust bill was prepared by the Department of Law in preparation for last session and is on file. It is entitled "An Act Establishing the Prudhoe Bay Oil and Gas Royalty Trust of 1980."

Attachments

cc: Governor Jay Hammond

TS/dg

Where there's \$'s . . .

Probe finds Massachusetts was up 'for sale'

^{1/81}
The Associated Press

BOSTON—Massachusetts government has been so riddled with corruption that "among those who had money and the influence to strike the bargain, the state was for sale," according to the report of a special commission investigating building contracts.

The panel's report, ending a two-year investigation, outlined a pattern of political bribes and payoffs and concluded that "corruption has been a way of life" in state government.

"It was not a matter of a few crooks," said the report by the Special Commission on State and County Buildings. "The pattern is too broad and pervasive for that easy excuse."

The panel today released a summary of its 2,500-page findings. Parts of it were published earlier today in the Boston Globe and Boston Herald-American.

"In the award of contracts for construction of state and county buildings, corruption has been a way of life," the report said. "For a decade at least, across Republican and Democratic administrations alike, the way to get architectural contracts was to buy them."

The panel said that since Jan. 1, 1968, the state has appropriated more than \$17 billion for construction projects. Results of a study of the buildings by the commission "stagger belief," the report said.

"In the sample of buildings

which we examined, 76 percent have significant defects, that is, a structural flaw that threatens the safety of the building and results from incompetent design or inferior construction."

The commission estimated the cost for repairing defects in all public buildings at more than \$2 billion.

The report said the criterion for getting a state building contract was "whether one pays, not whether one can do the best job. Over time, political influence, not professional performance, comes to be taken for granted as the criterion for doing state work."

The panel said the money took the form of "bonus checks to employees who negotiate them and return the cash; false invoices from suppliers which appear as a deductible business expense even while the dollars come back; honoraria for consulting services never performed; fictional business entities through which money is channeled."

The commission traced bribery and kickbacks in public construc-

tion projects by investigating thousands of contracts dating back to the early 1960s.

The panel was created in 1978 by Gov. Michael S. Dukakis and reformers in the Legislature after a scandal involving construction at the University of Massachusetts.

Public hearings this year disclosed the link between political contributions and contract awards. Witnesses at those hearings also linked the award of contracts with pressure from gubernatorial money-raisers.

(Among those investigated by the commission was former Massachusetts Lt. Gov. Donald R. Dwight, now publisher of The Minneapolis Star and the Minneapolis Tribune.

(In testimony before the commission in May, William V. Masiello told the commission that he had

given Dwight a \$2,000 bribe in 1974 to secure a design contract for a proposed state mental health treatment center. Dwight denied the allegations, calling Masiello a professional liar and admitted extortionist.

(Dwight was lieutenant governor from 1971 to 1975. While it was not his job to select architects for state projects, a former aide to Dwight testified that he did so.)

Among those figuring in the report were the administrations of former Govs. John A. Volpe and Endicott Peabody in the 1960s and Francis W. Sargent in the early 1970s.

A commission source said Tuesday that names of more than 100 people have been referred to state and federal law enforcement agencies for possible prosecution. Those names will not be disclosed.

THE DODGE TWINS

HOPKINS DODGE

DE

Grace
Baptist Ch-

E. 38th St. "

Where there's \$'s . . .

Probe finds Massachusetts was up 'for sale'

1/81

The Associated Press

BOSTON—Massachusetts government has been so riddled with corruption that "among those who had money and the influence to strike the bargain, the state was for sale," according to the report of a special commission investigating building contracts.

The panel's report, ending a two-year investigation, outlined a pattern of political bribes and payoffs and concluded that "corruption has been a way of life" in state government.

"It was not a matter of a few crooks," said the report by the Special Commission on State and County Buildings. "The pattern is too broad and pervasive for that easy excuse."

The panel today released a summary of its 2,500-page findings. Parts of it were published earlier today in the Boston Globe and Boston Herald-American.

"In the award of contracts for construction of state and county buildings, corruption has been a way of life," the report said. "For a decade at least, across Republican and Democratic administrations alike, the way to get architectural contracts was to buy them."

The panel said that since Jan. 1, 1968, the state has appropriated more than \$17 billion for construction projects. Results of a study of the buildings by the commission "stagger belief," the report said.

"In the sample of buildings

which we examined, 76 percent have significant defects, that is, a structural flaw that threatens the safety of the building and results from incompetent design or inferior construction."

The commission estimated the cost for repairing defects in all public buildings at more than \$2 billion.

The report said the criterion for getting a state building contract was "whether one pays, not whether one can do the best job. Over time, political influence, not professional performance, comes to be taken for granted as the criterion for doing state work."

The panel said the money took the form of "bonus checks to employees who negotiate them and return the cash; false invoices from suppliers which appear as a deductible business expense even while the dollars come back; honoraria for consulting services never performed; fictional business entities through which money is channeled."

The commission traced bribery and kickbacks in public construc-

tion projects by investigating thousands of contracts dating back to the early 1960s.

The panel was created in 1978 by Gov. Michael S. Dukakis and reformers in the Legislature after a scandal involving construction at the University of Massachusetts.

Public hearings this year disclosed the link between political contributions and contract awards. Witnesses at those hearings also linked the award of contracts with pressure from gubernatorial money-raisers.

(Among those investigated by the commission was former Massachusetts Lt. Gov. Donald R. Dwight, now publisher of The Minneapolis Star and the Minneapolis Tribune.)

(In testimony before the commission in May, William V. Masiello told the commission that he had

given Dwight a \$2,000 bribe in 1974 to secure a design contract for a proposed state mental health treatment center. Dwight denied the allegations, calling Masiello a professional liar and admitted extortionist.

(Dwight was lieutenant governor from 1971 to 1975. While it was not his job to select architects for state projects, a former aide to Dwight testified that he did so.)

Among those figuring in the report were the administrations of former Govs. John A. Volpe and Endicott Peabody in the 1960s and Francis W. Sargent in the early 1970s.

A commission source said Tuesday that names of more than 100 people have been referred to state and federal law enforcement agencies for possible prosecution. Those names will not be disclosed.

THE DODGE TWINS

HOPKINS

AL

Grace
Baptist Ch.
E. 38th St.

MEMORANDUM

TO: Governor Jay Hammond
VIA: Frances Ulmer, Director
Division of Policy Development and Planning
FROM: Arlon R. Tussing
DATE: December 9, 1980
RE: AFTERTHOUGHTS ON PACE

1. The most important lesson from BCRIC is, "ignore the political wise men, the financial experts and the bureaucrats --- DO IT!" There was no significant popular constituency for BCRIC; at the same time, the legal and financial experts gave a million reasons why it couldn't be done or wouldn't work. Once Bill Bennett pushed it through the legislature, however, BCRIC was immensely popular, and everyone around the BC government or legislature wanted to take part of the credit.

2. Another source of BCRIC's spectacular success was its combination of a free distribution with a purchase option. Every resident got something, which guaranteed universal interest, and any resident had the right to buy enough BCRIC stock to make a difference. There are other advantages to combining a free distribution with a purchase option; see point 8 below.

3. The first PACE distribution must be a sure winner. BCRIC distributed stock in profitable, established provincial enterprises, plus some mineral rights. Alaska doesn't have any profitable state-owned business other than oil & gas leasing, however. A royalty trust therefore seems to be the only really suitable asset for the first PACE distribution.

4. The surest asset value for distribution would be an interest in Prudhoe Bay royalties. The experts and state officials generally don't like the idea of a Prudhoe Bay royalty trust, however. I suspect that many of them will always find reasons to oppose any plan that gives up government control over assets of proved value with a significant current revenue stream. Nevertheless, some real problems seem to exist:

a. Statehood Act. Will Condon, Susan Burke, and Tom Williams seem to worry most about a conflict with the Statehood Act, which prohibits the state from alienating the mineral rights on lands selected under the Act. I'm not a lawyer and I don't propose to go into the question in detail here, but I from a practical standpoint, I don't think conflict with the Statehood Act is an insuperable problem.

b. Public purpose. At least one of the state's lawyers was concerned about reconciling PACE generally and the royalty trust in particular with the state constitution's provision that appropriations be for a "public purpose."

To my imperfect recollection, neither the adverse Supreme Court majority on the resident income tax exemption nor the adverse minority on the permanent fund dividend made the public purpose question central to their objections. In any event, we have both a specific response to this problem [See point 8 below, and a general remedy for any STATE constitutionality problem. [See point 9 below.]

c. Windfall Profits Tax. A more serious problem with a Prudhoe Bay royalty trust may be the treatment of its income under the Windfall Profits Tax (WPT): Crude oil "owned by" a State or local government or a Native corporation is exempt from the WPT, but other Prudhoe Bay oil is subject to a 30 percent marginal rate.

It is not obvious from the law's language that the exemption is waived when income from the sale of State royalty oil is passed directly through a royalty trust to private citizens. I have thought about ways the trust and the distribution might be structured to reduce the likelihood that distributed royalties would be subject to WPT. Whatever the arrangement, and whatever the ultimate outcome in the courts, however, IRS is sure to challenge the exemption, and a final decision might be many years off. Prudhoe Bay natural gas revenues are not subject to WPT.

d. Federal Income Tax. An interest in proved, producing reserves at Prudhoe Bay has an obvious, assessable value. A free distribution of Prudhoe Bay royalty trust shares would surely create a troublesome tax liability for citizens who receive them. IRS is also likely to insist on taxing any really attractive royalty trust purchase plan on the basis of the difference between the market value of the shares and the amount the purchaser actually pays.

I can think of ways to reduce the federal tax burden on a Prudhoe Bay royalty trust distribution, but I doubt whether there is any way to keep it from being substantial.

5. A distribution of Beaufort Sea royalty rights offers no immediate income and its asset value is less certain, but it avoids or mitigates some of the problems listed under point 3 above.

a. Statehood Act. Mineral rights on state submerged lands were not obtained by land selection under the Statehood Act, and are not subject to the Act's ban on alienating the mineral estate. Most of the 1979 Beaufort Sea lease sale area meets this test. [I wonder, are any of the leases in the Prudhoe Bay unit on submerged rather than Statehood Act lands?]

b. Windfall profits tax. Crude oil production from Arctic Alaska, other than Prudhoe Bay production, is exempt from WPT.

c. Federal income tax. So long as there are no proved reserves on the Beaufort Sea leases, their value for tax purposes is very speculative. A free distribution of royalty trust shares would nevertheless be taxable as income to the extent of that value.

If the state assigned a low nominal price to shares in a Beaufort Sea royalty trust, however, the IRS would have a difficult time establishing any other price. The tax liability on recipients of a free share distribution would probably be much lighter than on recipients of rights at Prudhoe Bay, and there is a good chance that purchasers of Beaufort Sea royalty trust certificates would avoid the tax entirely.

6. Structuring the royalty trust so that its revenues are very sensitive to wellhead prices or total royalties will make the Alaska public very sensitive to oil and gas management and disposal policy. Consider, for example, a royalty trust that distributed only the Prudhoe Bay oil royalties in excess of \$20.00 per barrel, and only the Prudhoe Bay natural gas revenues in excess of 75 percent of the federal ceiling price. Then consider how much sympathy there would be for discounts on royalty oil, gas, or NGLs for the sake of "industrial development."

7. The federal courts are very unlikely to approve any distribution scheme that gives credit for the duration of PAST residency, but a plan that implicitly ties benefits to the length of FUTURE residency has a better prospect. In last year's PACE proposal we suggested distribution of "serial purchase warrants" --- options to buy shares in the future at the initial year's price plus a nominal interest charge --- that can be exercised only by residents. The concept is a bit complicated, but people will figure it out quickly enough once they receive the warrants.

8. A royalty trust purchase option has many advantages over a free distribution: Sale at some nominal, low, but defensible price can avoid, mitigate, or dilute the federal income tax liability, public purpose, equal protection, and "right-to-travel" objections to PACE.

Essentially, eligible residents will get exactly what they pay for. Thus, the receipt of shares is not taxable income and persons excluded from the closed class (residents as of a certain date) are not deprived of any right that has demonstrable value. Nevertheless, we can structure a purchase option that is so attractive that every eligible person will want to take advantage of it.

The other merit of a purchase option is, of course, that people value most what they have to make some decision and some sacrifice to obtain. (If we want to educate everybody in the workings and ethic of free enterprise, let's begin with the lesson that "there is no free lunch." A bargain lunch is another matter . . .)

MEMORANDUM
December 9, 1980
Page Five

9. Any STATE constitutional objection to PACE is easily overcome. Simply provide in the PACE legislation that any final Supreme Court decision disapproving any provision of the plan on state constitutional grounds automatically triggers a referendum on a constitutional amendment that would correct the problem.

This device may be TOO clever. It would almost certainly work, but let's think a bit whether we want to unleash such a weapon. What other momentarily fashionable causes might be railroaded into the constitution in the same way once we established the precedent in the PACE bill?

for
ROYALTY TRUST IMPLEMENTATION
through
P.A.C.E.

DRAFT

Program Elements

Detailed Components

Assets to be distributed

free dist. vs.
Sale would
affect

- select principal amount required based on estimated number of shares and value per share, and desired annual earnings per share level.

\$2 Billion
200 million / yr.
↓
\$500 per capita

- identify leases whose value or portion thereof equals principal amount and yields royalty cash flow at desired levels for per share value and earnings per share.

- identify fine-tuning options for structuring Trust so earnings per share are sensitive to wellhead prices or royalty revenues.

- identify appropriations options and requirements for transferring royalty interest to trust.

- specify details of existing Royalty Trusts (see attachment).

- identify desired Trust attributes, develop draft Trust indentures and corporate organization.

- specify options for Trustee, e.g., Commissioner, private trust company, etc.

Trustee -
no stock
management
powers
no voting
rights
for
shareholders

Corporate Mechanism
for administration of
Royalty Trust

check Kuparuk production
→ small royalty exemption / see Williams

Comm. could
~~have~~ - just not
designate
zip

- specify Trust duties, e.g., maintain principal, pass through income, administer dispersal of share certificates, [limitations on lease negotiation involvement,] etc.

Exec. Budget Act

- identify funding source for Trust operating costs. *Rev. operating budget*

Here on application
date (1/1/82)
not retroactive
include children,
managed by
two

Eligibility to
and/or receive free and/or
to purchase additional
shares

- identify status of durational - or other residency requirements.
- specify eligibility requirements for participation in Trust.

Disposition of Shares
by either gift or sale
or both

- select per capita allocation of either free shares or shares for sale or both.

serial
warrant
options

- identify installment sale options, i.e., terms and conditions, duration of State sale, other financing details and limitations.

50/50?
slgs?

- select free share distribution mechanism.
- select share sale mechanism.
- identify and select limitations on transferability of shares.

TS/dg

Timing of distribution

investment powers up to a year?

Frances A. Ulmer
Director
Division of Policy Development
and Planning

November 14, 1980

Tom Singer
Policy & Program Specialist
Division of Policy Development
and Planning

Royalty Trusts

OUTLINE SUMMARY:

1. What is the purpose?
 - to transfer part of Alaska's petroleum wealth to its people in the form of income-producing assets;
 - to encourage increased awareness and involvement by the people of Alaska in the management of natural resource production and development; and
 - to encourage wider participation in and understanding of the capitalist system through wider ownership.
2. Who organizes or runs a Royalty Trust?
 - a Trust is created by the Legislature and approved by the Governor;
 - the Trustee could be a Commissioner and/or such trust agents as a bank or Trust Company; and
 - the Trustee would receive royalty revenues for the owners of the Trust, and would distribute such revenues directly to the owners in proportion to their ownership interest.
3. What types of assets could be placed in a Royalty Trust?
 - rights to or interest in a specified portion of the income from lease rentals, royalties, net profit shares, and/or mineral sale revenues of the State, such as oil and gas leases, coal leases, etc.
4. Who is eligible for participation?
 - all Alaska residents as defined in a bill; and
 - eligibility for participation in each Trust is established by dates included in a bill.

5. What State appropriations would be required?
 - an appropriation of the assets (royalty interest in lease holding) to be distributed under the Trust; and
 - amounts required to administer the Trust, unless provided directly from Trust income.
6. What actions would be elective?
 - legislative adoption of a Royalty Trust and appropriations necessary to implement it; and
 - individual participation in a Trust.
7. What would individual residents receive?
 - free distribution of a minor portion of the assets included in a Trust;
 - an option to purchase additional shares or securities in the remaining shares of a Trust; and
 - the certificates distributed as evidence of ownership in the Trust would be the unencumbered private property of the beneficiaries except as otherwise provided by law.

INTRODUCTION:

The concept of a Royalty Trust was one of the mechanisms by which State-owned assets could be distributed directly to residents under the Governor's Portfolio of Alaska Citizen Enterprise (PACE). For several reasons, the Governor has determined that Royalty Trusts are the most attractive mechanisms included in PACE. These reasons include the relative certainty of the market values of the asset, the absence of need for State management or business expertise to implement a Royalty Trust, and the simplicity of the concept. The following sections introduce the essentials of the concept as presently understood. Attached memoranda document the work performed to date on Royalty Trusts and can serve as a starting point for future efforts.

PURPOSE:

The overall purpose of a Royalty Trust is to transfer part of the wealth derived from the natural resources of the State directly to its residents. Additional purposes include increased awareness and involvement by residents in the management of State natural resource production and development, and wider participation in, and understanding of the capitalist system through wider ownership (and the ownership of financial securities). An additional purpose is to increase the actual wealth of residents rather than simply their income (as with Permanent Fund dividends). Such increased wealth can be used to offset certain current State activities in the lending arena by providing an asset which an

individual can pledge as security, thus increasing the credit worthiness of all Alaskans. This approach was recommended by Coffman and Fry in their study "Capital Shortage in Rural Alaska," prepared for the Governor's Office and the Department of Revenue.

ASSETS:

Basically, the assets which could be distributed to residents through a Royalty Trust include any right to, or interest in a specified portion of the income from any State lease rentals, royalties, net profit shares, and/or mineral sale revenues. The State would identify one or more lease tracts to be included (this could be structured to a target per capita asset value or income stream) and convey the rights to the income from that tract to the Trust. Thus the asset would only be a portion of the State's royalty interest and not the entire mineral interest. This royalty interest must be appropriated by the Legislature to the Trust. The asset would have value and produce income as long as mineral production continues.

MANAGEMENT:

A Trust is a very conventional and well-known financial organization. A Commissioner, and/or such trust agents as a bank or trust company, would be responsible for carrying out the duties of Trustee. Such duties include preserving the Trust estate, collecting income from the Trust estate, paying administrative expenses, and distributing net proceeds to the certificate holders. The Trustee may not engage in any business activities or make investments. Thus the many problems created by other wealth distribution plans are avoided -- there is no requirement for managerial or entrepreneurial activities by the State and no interference with private business activities.

DISTRIBUTION:

Any Alaska resident as defined in the Act would be eligible to receive any free shares in the Trust which may be distributed by the State. An eligible resident would also have the right to purchase additional shares up to some specified limit established to avoid concentration of ownership. Ownership shares would be evidenced by Trust certificates. The value of a Trust share unit could be set at any level deemed appropriate to encourage wide participation, such as \$25, \$50, or \$100.

With respect to the terms and conditions governing the sale of Trust units and the market which will exist for them, a number of options are available. Decisions will be necessary regarding how much of the Trust is distributed free and how much is offered for sale. The financial terms of share sales is also open to discussion, such as whether Permanent Fund dividends can be applied or whether installment sales will be permitted. Sales at attractive terms (perhaps involving subsidies) may also be considered. The ability of non-residents to purchase shares and other aspects of the market for Trust shares needs to be considered. These and other similar issues are addressed in the Tussing report (p. 11 - 22), where one set of options is offered.

CONCLUSION:

Many financial, organizational, and legal details require further refinement. The Tussing report, the Messenger memo, and the draft bill offer some tentative options and raise additional questions. These documents should be reviewed and important policy issues should receive further consideration. Once decisions can be reached, the technicians can proceed to develop a more detailed proposal.

cc: Governor Jay Hammond

TS/dg

Governor Hammond

October 1, 1979

Fran Ulmer

by: Tom Singer
Policy Analyst

The British Columbia
Resources Investment
Corporation - How Does
It Relate to the Development
and Distribution Options
Facing Alaska?

- You have asked us for a briefing paper on the British Columbia Resources Investment Corporation (BCRIC) as a result of your meeting with Premier W. P. Bennett. The following outlines the BCRIC concept and its relation to AGSOC and the Permanent Fund.

BCRIC

BCRIC is a mechanism designed to achieve the goal of transferring or returning to the private sector, via the corporate structure, assets which are owned by the public sector. A companion goal is the creation of individual stock ownership among residents of a political jurisdiction. More specifically, in British Columbia the present administration of Premier Bennett found itself owner of a number of formerly private firms which had been socialized by the previous socialist government. In keeping with the principle of private ownership, the Bennett Administration devised BCRIC as a way to return these firms and some other public assets to the private sector, not by sale to large organizations but by gift and sale to the general public in British Columbia.

In 1977, the British Columbia Legislature created BCRIC and handed over the following government-owned assets to it:

- Oil and gas exploration rights to some 2.3 million acres of crown land in northeastern British Columbia.
- 81 percent of the common shares of Canadian Cellulose Company Limited, a large-scale forest products firm.
- 100 percent of the common shares of Kootenay Forest Products Limited, a medium-sized lumber and plywood manufacturer.
- 100 percent of the common shares of Plateau Mills Limited, a mid-sized lumber producer.
- About 10 percent of the shares of Westcoast Transmission Company, which operates a major pipeline in B.C. and is also a partner in the Alaska Highway gas pipeline project.

This past summer eighty percent of the government-owned stock in BCRIC, 12 million shares, was distributed to the public, five shares per resident. The government retained the remaining twenty percent. BCRIC also offered its treasury stock for sale to residents in an attempt to provide additional shares and to raise additional cash. Any resident may own up to 5000 shares. Future residents will have to purchase shares on the open market if they wish to own BCRIC stock. Thus, BCRIC is now eighty percent privately-held.

Although the government retains twenty percent ownership, there are no government representatives on the Board or in management. There are also no guarantees or other government assistance, although Premier Bennett's support and the twenty percent government ownership do strengthen the firm's financial position. There are many other details (see attachments); nevertheless these are the major characteristics. The share offering is reported to have been extremely successful.

BCRIC and AGSOC

As you have probably concluded by this point, BCRIC bears a striking resemblance to AGSOC. Indeed, in many respects, BCRIC is identical to AGSOC. Share distributions are limited to residents. Ownership is limited to avoid concentration. The firm is totally private; Board members are elected by the shareholders; a majority of the Board must also be residents of B.C. and so on. Some differences are that BCRIC does not receive a federal tax break in Canada, nor does the Corporation have to pay out 90% of its earnings annually as would AGSOC.

The critical difference, which of course makes all the difference, is that BCRIC has tangible assets while AGSOC has none. BCRIC is a holding company with a portfolio of existing, profitable firms and (formerly) public assets (oil and gas exploration rights). AGSOC is simply a corporate structure with some hefty front-end expenses (current estimated start-up costs - \$5M). This corporate structure, upon creation by the state, is supposed to perform an acquisition or investment analysis, identify its "best deal" and then proceed to borrow in the capital markets to finance the venture and acquire its assets. Contrary to Mr. Kelso's theoretical reliance on the collective credit strength of AGSOC's shareholders (i.e. state government), Senator Gravel insists that AGSOC will be able to 100 percent debt finance on the strength of the venture itself. BCRIC has few of the financial and economic risks inherent in AGSOC.

In the political arena, BCRIC does share the potential political conflicts perceived with AGSOC. In the areas of oil and gas and forest products taxation and regulation, BCRIC can be expected to become a political force (like AGSOC), as it too represents "all of the people" just like government. It is not clear whether, by being a holding company with several different and somewhat smaller assets, BCRIC will be less politically formidable than a monolithic AGSOC with one major resource development project as its asset. While the House State Affairs Committee has amended the AGSOC bill to limit such political activities as lobbying or candidate endorsements, the effectiveness and constitutionality of such limitations are uncertain.

If you are attracted to the underlying philosophy of AGSOC but balk at its risks, BCRIC offers a proven alternative based on private ownership

by residents of in-state wealth-producing assets. A brief discussion of options follows.

BCPIC and the Permanent Fund

The relationship between BCPIC and the Permanent Fund is the relationship between a tool for "privatization" of a public asset and a public asset. For British Columbia, the assets were several firms and oil and gas exploration rights. For Alaska, it could be:

- The Permanent fund (financial assets),
- Land,
- Our loan program portfolio,
- Part of our general fund surplus (in the form of financial securities or as cash for the acquisition of profitable foreign-held Alaskan corporations),
- Our oil and gas holdings or exploration rights, etc., or
- Any other publicly-held asset (such as an equity share in the gasline, a gas conditioning plant, part of a petrochemical complex, fish hatcheries, a utility like Susitna, etc.).

BCPIC could serve as a model for Alaska to pass any of these wealth-producing assets into private hands via a corporation whose stockholders would be all Alaskan residents. The major drawbacks to such a program would be the transfer of direct control over these assets to the corporation's managers (the state would retain "police power" and taxation controls) and the political conflicts of interest inherent in these ideas. The major benefits would be direct financial benefit in the form of dividends and the more general benefit of broadened capital ownership among Alaskans. This scheme may also avoid some of the legal pitfalls facing the Energy Tax Credit concept, because a private firm faces different legal constraints than state government. Finally, this idea offers an opportunity for Alaskans generally to benefit from the downstream development of our resources which is the province of the private sector. It could provide, for example, stock ownership in a land development corporation or oil and gas exploration or development firms or acquisition of foreign-held fisheries companies. Representative Gardiner is presently interested in using the AGSOC/BCPIC framework to acquire foreign-owned, profit-exporting business for Alaskans. The alternative in which the state could hand out part of the Permanent Fund to Alaskans and admonish them to buy stock in Alaskan businesses with the money does not afford the same opportunity to reduce foreign ownership in Alaska.

Your Permanent Fund bill currently before the Legislature divides the fund into two components, a 25% trust and a 50% development bank. Basically, the entire fund would be managed by an independent state corporation with a Board of Directors appointed by the Governor. The first twenty-five percent contribution would be invested as a trust in safe, secure financial securities. The next fifty-percent contribution would also be invested as a trust unless the Board found there were prudent development banking-type investments to make (amendment to the statute would be required for additional investment categories). Income would be divided, half to the general fund and half for distribution.

The goals inherent in this legislation are, first, safe, secure investments; second, a certain income stream for distribution and the operating budget; and third, prudent in-state economic development.

Applying the BCRIC model to the Permanent Fund would require a reordering of goals. The first goal of the BCRIC model is to put public assets into private hands (direct, non-governmental benefit). A secondary goal is to broaden capital ownership. Under this model, all or part of the Permanent Fund could be transferred to a private corporation set up to manage this asset. The corporation could be modeled after any number of private sector financial management institutions, such as investment banks, pension funds, or mutual funds. Use of the AGSOC framework or a public corporation should also be considered for the added benefits of tax exemption and, in the public corporation case, continued state involvement. The corporation would issue shares to all Alaskans (perhaps based on durational residency) who would then become the owners of the firm and would receive its profits in the form of dividends. A version of this approach, the "AGSOC-ing of the Permanent Fund," has been introduced in the Legislature by Senator Sumner as SD122. While this scheme would provide direct, equitable benefits to Alaskans, it would preclude use of Permanent Fund income for operating budgets, unless only part of the fund was allocated to this program.

This memo serves as an introduction to the concept of "privatization" of public assets. BCRIC, AGSOC, and public corporations offer fertile ground for innovation in distributing the benefits of publicly-held assets. If this memo appears "fuzzy," it is because the breadth of opportunity is so great. If you are interested in pursuing these ideas, we can provide a more complete analysis based on the most appropriate asset for experimentation (Permanent Fund, general fund surplus, land, oil and gas holdings, etc.) and the most appropriate organizational form (BCRIC, AGSOC, public corporation).

FAU:TE/cw

BCRIC

MEMORANDUM

TO: Governor Jay Hammond
VIA: Frances Ulmer, Director
Division of Policy Development and Planning
FROM: Arlon R. Tussing
DATE: December 9, 1980
RE: AFTERTHOUGHTS ON PACE

1. The most important lesson from BCRIC is, "ignore the political wise men, the financial experts and the bureaucrats --- DO IT!" There was no significant popular constituency for BCRIC; at the same time, the legal and financial experts gave a million reasons why it couldn't be done or wouldn't work. Once Bill Bennett pushed it through the legislature, however, BCRIC was immensely popular, and everyone around the BC government or legislature wanted to take part of the credit.

2. Another source of BCRIC's spectacular success was its combination of a free distribution with a purchase option. Every resident got something, which guaranteed universal interest, and any resident had the right to buy enough BCRIC stock to make a difference. There are other advantages to combining a free distribution with a purchase option; see point 8 below.

3. The first PACE distribution must be a sure winner. BCRIC distributed stock in profitable, established provincial enterprises, plus some mineral rights. Alaska doesn't have any profitable state-owned business other than oil & gas leasing, however. A royalty trust therefore seems to be the only really suitable asset for the first PACE distribution.

4. The surest asset value for distribution would be an interest in Prudhoe Bay royalties. The experts and state officials generally don't like the idea of a Prudhoe Bay royalty trust, however. I suspect that many of them will always find reasons to oppose any plan that gives up government control over assets of proved value with a significant current revenue stream. Nevertheless, some real problems seem to exist:

a. Statehood Act. Will Condon, Susan Burke, and Tom Williams seem to worry most about a conflict with the Statehood Act, which prohibits the state from alienating the mineral rights on lands selected under the Act. I'm not a lawyer and I don't propose to go into the question in detail here, but I from a practical standpoint, I don't think conflict with the Statehood Act is an insuperable problem.

b. Public purpose. At least one of the state's lawyers was concerned about reconciling PACE generally and the royalty trust in particular with the state constitution's provision that appropriations be for a "public purpose."

To my imperfect recollection, neither the adverse Supreme Court majority on the resident income tax exemption nor the adverse minority on the permanent fund dividend made the public purpose question central to their objections. In any event, we have both a specific response to this problem [See point 8 below, and a general remedy for any STATE constitutionality problem. [See point 9 below.]

c. Windfall Profits Tax. A more serious problem with a Prudhoe Bay royalty trust may be the treatment of its income under the Windfall Profits Tax (WPT): Crude oil "owned by" a State or local government or a Native corporation is exempt from the WPT, but other Prudhoe Bay oil is subject to a 30 percent marginal rate.

It is not obvious from the law's language that the exemption is waived when income from the sale of State royalty oil is passed directly through a royalty trust to private citizens. I have thought about ways the trust and the distribution might be structured to reduce the likelihood that distributed royalties would be subject to WPT. Whatever the arrangement, and whatever the ultimate outcome in the courts, however, IRS is sure to challenge the exemption, and a final decision might be many years off. Prudhoe Bay natural gas revenues are not subject to WPT.

d. Federal Income Tax. An interest in proved, producing reserves at Prudhoe Bay has an obvious, assessable value. A free distribution of Prudhoe Bay royalty trust shares would surely create a troublesome tax liability for citizens who receive them. IRS is also likely to insist on taxing any really attractive royalty trust purchase plan on the basis of the difference between the market value of the shares and the amount the purchaser actually pays.

I can think of ways to reduce the federal tax burden on a Prudhoe Bay royalty trust distribution, but I doubt whether there is any way to keep it from being substantial.

5. A distribution of Beaufort Sea royalty rights offers no immediate income and its asset value is less certain, but it avoids or mitigates some of the problems listed under point 3 above.

a. Statehood Act. Mineral rights on state submerged lands were not obtained by land selection under the Statehood Act, and are not subject to the Act's ban on alienating the mineral estate. Most of the 1979 Beaufort Sea lease sale area meets this test. [I wonder, are any of the leases in the Prudhoe Bay unit on submerged rather than Statehood Act lands?]

b. Windfall profits tax. Crude oil production from Arctic Alaska, other than Prudhoe Bay production, is exempt from WPT.

c. Federal income tax. So long as there are no proved reserves on the Beaufort Sea leases, their value for tax purposes is very speculative. A free distribution of royalty trust shares would nevertheless be taxable as income to the extent of that value.

If the state assigned a low nominal price to shares in a Beaufort Sea royalty trust, however, the IRS would have a difficult time establishing any other price. The tax liability on recipients of a free share distribution would probably be much lighter than on recipients of rights at Prudhoe Bay, and there is a good chance that purchasers of Beaufort Sea royalty trust certificates would avoid the tax entirely.

6. Structuring the royalty trust so that its revenues are very sensitive to wellhead prices or total royalties will make the Alaska public very sensitive to oil and gas management and disposal policy. Consider, for example, a royalty trust that distributed only the Prudhoe Bay oil royalties in excess of \$20.00 per barrel, and only the Prudhoe Bay natural gas revenues in excess of 75 percent of the federal ceiling price. Then consider how much sympathy there would be for discounts on royalty oil, gas, or NGLs for the sake of "industrial development."

7. The federal courts are very unlikely to approve any distribution scheme that gives credit for the duration of PAST residency, but a plan that implicitly ties benefits to the length of FUTURE residency has a better prospect. In last year's PACE proposal we suggested distribution of "serial purchase warrants" --- options to buy shares in the future at the initial year's price plus a nominal interest charge --- that can be exercised only by residents. The concept is a bit complicated, but people will figure it out quickly enough once they receive the warrants.

8. A royalty trust purchase option has many advantages over a free distribution: Sale at some nominal, low, but defensible price can avoid, mitigate, or dilute the federal income tax liability, public purpose, equal protection, and "right-to-travel" objections to PACE.

Essentially, eligible residents will get exactly what they pay for. Thus, the receipt of shares is not taxable income and persons excluded from the closed class (residents as of a certain date) are not deprived of any right that has demonstrable value. Nevertheless, we can structure a purchase option that is so attractive that every eligible person will want to take advantage of it.

The other merit of a purchase option is, of course, that people value most what they have to make some decision and some sacrifice to obtain. (If we want to educate everybody in the workings and ethic of free enterprise, let's begin with the lesson that "there is no free lunch." A bargain lunch is another matter . . .)

MEMORANDUM
December 9, 1980
Page Five

9. Any STATE constitutional objection to PACE is easily overcome. Simply provide in the PACE legislation that any final Supreme Court decision disapproving any provision of the plan on state constitutional grounds automatically triggers a referendum on a constitutional amendment that would correct the problem.

This device may be TOO clever. It would almost certainly work, but let's think a bit whether we want to unleash such a weapon. What other momentarily fashionable causes might be railroaded into the constitution in the same way once we established the precedent in the PACE bill?

R.T. → appears in margin to
mark sections applicable to
Royalty Trusts.

DRAFT LEGISLATION FOR AN
ALASKA CITIZENS WEALTH OWNERSHIP PLAN

Prepared for the
OFFICE OF THE GOVERNOR
STATE OF ALASKA

By
ARLON R. TUSSING & ASSOCIATES, INC.
and
PRESTON, THORGRMISON, HOLMAN & ELLIS

27 March, 1980

ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM

INTRODUCTION AND EXPLANATION OF MARCH 27 DRAFT

There are three main parts to the draft legislation: Chapter 1 establishes a general procedure for distributing any of several kinds of securities to Alaska residents; Chapters 2 through 7 describe the different kinds of securities; and Chapters 8 and 9 provide for a distribution that could be put into effect this year and which would put securities of unquestionable value into the hands of Alaskans (as opposed to some of the more speculative alternatives, such as AGSOC or a share in the gas conditioning plant).

Article 1 of Chapter 1 sets out the purposes of the Program — these are self-explanatory. It houses the Program in the Department of Revenue, and requires the Commissioner to submit at least one and as many as three wealth distribution plans to the legislature each year. Each plan must be accompanied by a financial and legal analysis, and will not go into effect unless enacted as a law or joint resolution.

Article 2 defines residency for the purpose of obtaining benefits under the program. Beneficiaries of any plan are limited to Alaska residents as of an eligibility date specified for that plan. The legislation also sets out the evidence a person must submit to establish a presumption of residency, and certain actions that establish a presumption of non-residency.

Article 3 spells out the general procedures for distributing securities to eligible residents. A small part (5 to 15 percent) of the securities distributed under each plan will be distributed free, in equal portions to each resident who applies for them. This provision assures that everybody gets something, and serves as advertisement for the program. Most of the assets distributed (85 to 95 percent), however, are to be sold to residents at their nominal value. There are at least three major reasons for selling, rather than giving away, the bulk of the assets:

(a) Sale at value is far more likely to survive constitutional challenge than free distribution. [The legislation will be written so that the sales procedures will survive even if the courts disallow free grants.]

(b) Sale at value is unlikely to create any federal tax liability for the recipient, while the IRS may rule that assets received free of charge are taxable income in the year they are received.

(c) People are likely to place a higher value on things they have to pay for than on free gifts.

There are at least three reasons Alaskans would want to buy assets distributed under the program:

(a) We assume that some kind of tax credit scheme will be adopted, and Alaska taxpayers will be allowed to apply any tax credit or refund to the purchase of securities under the plan. Thus, although they will have to make a real choice (between investments and cash), many and probably most Alaskans will be able to avoid any cash outlay.

(b) Most assets will be sold at a "cost" or "conservatively appraised value" intended to satisfy constitutional and federal tax requirements, but they can be expected to earn exceptionally high rates of return in relation to that "cost".

(c) Residents will be able to buy the securities on time, over a ten year period at a carrying cost far less than their expected rate of return.

Alaskans who want to buy securities on time will be issued non-transferable warrants — certificates that allow them to buy a specified number of units each year at a fixed price. While Alaskans who move away will be able to keep the securities they have actually bought, and (with certain important exceptions) to sell them freely, their unused warrants will become invalid.

Article 4 sets out the rights of securities holders. Except for the non-transferable warrants described above, shares in a natural resource trust (which can be transferred or sold only to other resident Alaskans, except by inheritance), and AGSOC shares (whose ownership is restricted by federal law), the assets distributed under the program will be the unrestricted property of the recipients, and can be disposed of as they wish.

Article 5 states that receipt of securities under the program, whether by grant or by purchase, is not taxable income under Alaska law, but that income from those securities, and proceeds from their resale, will be treated like any other income or capital gains. It also provides that if the IRS rules receipt of these securities to be taxable income under federal law, any additional federal tax the recipient is required to pay may be credited against Alaska income taxes.

Article 6 provides for the Commissioner of Revenue to buy and sell securities distributed under the program in order to create an orderly market for them, if an effective private market for those securities did not otherwise develop.

Article 7 (not yet drafted) will define various terms used in the legislation; provide penalties for persons who falsely claim residency or make false statements in order to obtain benefits under the program; and specifies what parts of the legislation will remain valid if other parts are declared unconstitutional.

Chapters 2 through 7 describe the various kinds of assets that can be distributed under the Program. For each kind of asset, the Commissioner of Revenue would have to present a specific plan to be acted on by the legislature.

Alaska Energy Resource Trusts are royalty trusts — devices for passing on a portion of the state's oil and gas royalties directly to holders of certificates in the trust. (See the attached clipping from Fortune magazine. [pp ix-x])

Alaska Industrial Development Projects are major new investments, like the gas pipeline or conditioning plant, in which the state might decide to participate financially. Chapter 3 provides that if the state does make such an investment, the state's ownership and management role should be temporary — through the development phase only — and that the state's shares in the project should ultimately be distributed to Alaskans under this program.

Alaska General Stock Ownership Corporations (AGSOCs) are the familiar Kelso-Gravel idea. Chapter 4 would incorporate the major provisions of the bill reported by the House State Affairs Committee, but (in contrast to the current initiative) would require the legislature to act upon a complete financing plan before creating any AGSOC.

Alaska Investment Funds are regulated investment companies (mutual funds) empowered to invest in the securities of corporations doing business in Alaska, and Alaska Real Estate Trusts are real estate investment trusts (REITs) empowered to invest in Alaska real estate developments. Both kinds of enterprise are essentially passive investments and are in themselves exempt from federal income taxes (like AGSOCs); they are a way of increasing resident Alaskan ownership in major Alaska industry without the state's having to register as a securities underwriter.

Chapter 7 provides for the distribution of securities in existing private enterprises. This provision would allow the State to buy blocks of shares in major Alaska businesses (fish processing plants, airline and communications companies, and the like), and to sell them to residents on easy terms in order to increase resident Alaskan ownership and control in important industries.

Chapters 8 and 9 set out specific wealth distribution programs that could be put into effect by the current legislature. Both are Alaska Energy Resource Trusts.

R.T.



We believe that the effectiveness and credibility of the program demands that there be an early distribution of assets that have a certain, positive value. The first distribution must be one that neither requires a large front-end appropriation of money nor presents any risks to the citizens who receive the assets. Shares in oil and gas royalties --- specifically, royalties from the proved reserves at Prudhoe Bay --- seem to be the only kind of asset that can play this pioneering role.

The Prudhoe Bay Oil and Gas Royalty Trust of 1980 would commit royalties from only some of the leases at Prudhoe Bay, and only those royalties in excess of current levels. Thus, the revenues conveyed to the trust would increase very rapidly with the decontrol of crude oil prices, and then fall off very rapidly as Prudhoe Bay production declined. We suggest the leases be chosen so that the average distribution per capita in the first year is in the \$100 to \$200 range --- large enough that people will have to take it seriously, but (in this first distribution) not enough to make a large dent in available revenues.

The Beaufort Sea Oil and Gas Royalty Trust of 1980 would commit royalties from Beaufort Sea leases sold in 1979. Any revenues produced from those leases would be distributed much later than the Prudhoe Bay royalties, and while the value of the certificates would probably be much greater, they would be a far more speculative property. Conceivably, the two plans could be combined into one plan that provided some certain near-term income, and some less certain but possibly far greater income, say, seven to ten years in the future.

The certificate holders would not have any voice in management of the oil and gas resource itself, and the trust indenture specifically makes the conveyance subject to any existing commitments of royalties. It also preserves the state's option to take royalty in kind --- it therefore creates no obstacles, for example, to fulfilling the Alpetco

contract or to exchanging royalty gas for gas liquids to be used in Alaska petrochemical development. But the plans will certainly create a greater citizen identification with the North Slope oil and gas resource, and a more intense and informed interest in state and federal policies affecting those resources. - -

These plans would probably make Alaskans more receptive, for example, to state financial participation in the gas line, especially if state involvement can reasonably be expected to accelerate its completion — and thereby the flow of gas royalties. The plans would also create a broadly-based Alaska constituency pressing to maximize the wellhead value of the state's oil and gas, and resisting proposals to give away or discount the state's royalty for any purpose. (After all, the people will recognize, as they may not fully appreciate now, that these decisions involve their own money.)

ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM
DRAFT LEGISLATION

CONTENTS

TITLE	
CHAPTER 1. ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM	1
ARTICLE 1. GENERAL PROVISIONS	1
Section 100 Findings	1
Section 110. Purposes (a)	1
(b) to (e)	2
Section 115. Alaska Citizens Wealth Distribution Plans	
(a) to (c)	3
Section 120. Plans submitted to Legislature (a) and (b)	4
(c) and (d)	5
(d) [continued] and (e)	6
ARTICLE 2. ELIGIBILITY FOR BENEFITS	
Section 210. Eligibility for benefits (a) to (d)	7
Section 215. Alaska residency defined (a) to (c)	8
Section 220. Evidence of residency (a) and (b)	9
Section 225. List of persons claiming residency	10
ARTICLE 3. DISTRIBUTION OF ASSETS	11
Section 310. Basic purchase price (a)	11
(b) and (c)	12
Section 315. Free distribution	13
Section 320. First restricted sale (a) to (d)	13
(e) and (f)	14
Section 325. Second restricted sale (a) to (c)	15
(d) and (e)	16
Section 330. Unrestricted sale	17
Section 335. Stock-purchase warrants (a)	18
(b)	19
(c) and (d)	20
Section 340. Use of income tax credits (a) and (b)	21
(c) and (d)	22
ARTICLE 4. OWNERSHIP RIGHTS	23
Section 410. Transfer of assets	23
Section 415. Voting rights	23
ARTICLE 5. TAX TREATMENT	24
Section 510. Receipt of assets not taxable	24
Section 515. Credit for federal taxes paid	24
Section 520. Income not tax-exempt	24
ARTICLE 6. SECURITIES MARKETS	25
ARTICLE 7 MISCELLANEOUS PROVISIONS	26*
Section 700. Definitions	26*
Section 710. Penalties for false statements	26*
Section 720. Savings clauses	26*

CHAPTER 2.	ALASKA ENERGY RESOURCE TRUSTS	27
Section 110.	Alaska Energy Resource Trust defined	27
Section 120.	Distribution of certificates	27
Section 140.	Ownership and transferability	28
CHAPTER 3.	ALASKA INDUSTRIAL DEVELOPMENT PROJECTS	29
Section 110.	Alaska Industrial Development Project defined	29
Section 120.	Intent	29
Section 130.	Alaska Natural Gas Transportation System	30
CHAPTER 4.	ALASKA GENERAL STOCK OWNERSHIP CORPORATIONS	31
ARTICLE 1.	GENERAL PROVISIONS	31
Section 110.	Alaska General Stock Ownership Corporation defined	31
ARTICLE 2		*
CHAPTER 5.	ALASKA INVESTMENT FUNDS	32
Section 110.	Alaska Investment Fund defined	32
		*
CHAPTER 6.	ALASKA REAL ESTATE TRUSTS	33
Section 110.	Alaska Real Estate Trust defined	33
		*
CHAPTER 7.	EXISTING PRIVATE ENTERPRISES	34
Section 110.	Existing private enterprise defined	34
CHAPTER 8.	PRUDHOE BAY OIL AND GAS ROYALTY TRUST PLAN OF 1980	35
ARTICLE 1.	FORMATION OF TRUST	
Section 110.	Creation of trust	35
Section 120.	Trust indenture	35
Section 130.	Amendments to trust indenture	35
Section 140.	Purpose	36
Section 150.	The trust estate	36
Section 155.	Conveyance of royalties (a) through (c)	36
	(c) [continued] through (d)	37
Section 160.	Rule against perpetuities	37
ARTICLE 2.	TRUSTEE	38
Section 210.	Selection of trustee and successor trustees (a) to (d)	38
Section 220.	Powers and duties of trustee	39
Section 230.	No power to engage in business or make investments	40
Section 240.	Liability of trustee	40
Section 250.	Compensation of trustee	40
Section 260.	Investment of cash reserves	40
Section 270.	Payment of liabilities (a)	40
	(b)	41
Section 280.	Resignation and termination of trustee (a)	41
	(b)	42

* Drafting incomplete as of 27 March, 1980.

-viii-(B2)

DRAFT OF 27 MARCH, 1980 (A.T.)
Supersedes all previous drafts

ARTICLE 3. TERMINATION OF TRUST AND LIQUIDATION	42
Section 310. Duration, revocation, and termination of trust	42
Section 320. Liquidation	42
ARTICLE 4 BENEFICIAL INTERESTS	43
Section 410. Creation of beneficial shares and certificates	43
Section 420. Rights of certificate holders (a)	44
(b) and (c)	45
Section 430. Execution of certificates	45
Section 440. Registration and transfer of units	45
Section 450. Determination and ownership of certificates	46
ARTICLE 5. ACCOUNTING AND DISTRIBUTION	47
Section 510. Fiscal year and accounting method (a) and (b)	47
Section 520. Distributions (a) and (b)	47
Section 530. Tax reporting	48
Section 540. Reports to certificate holders	48
ARTICLE 6. MEETINGS	48
Section 610. Meetings of certificate holders (a) to (c)	48
(d)	49
Section 620. Voting	49
Section 630. Conduct of meetings	49
ARTICLE 7. GENERAL PROVISIONS	50
Section 710. Inspection of trustee's books	50
Section 720. Definitions	50
CHAPTER 8. BEAUFORT SEA OIL AND GAS ROYALTY TRUST OF 1980	51
[The article and section titles will be the same as for Chapter 7]	

R.T.

Personal Investing

Trusts That Rake Royalties Off the Top by Aimée L. Morner

Inflation hedgers flocking into natural-resource investments have been eyeing the unusual vehicles known as royalty trusts. These trusts, a few of which have been around since the early 1950's, are unincorporated enterprises that act as conduits for distributing royalty income to investors. Four of the five large publicly traded trusts (see table) derive their income from royalties on sales of oil and gas; the other, Mesabi Trust, gets its royalties from iron ore. Not surprisingly, the oil and gas trusts have risen the most in the last few years, and in mid-March a big new one—Houston Oil Royalty Trust—was about to come to market.

All of the royalty trusts share some common characteristics. None of them owns real property; instead, they hold interests in royalties from properties owned or leased to, one or more operating companies. The royalties, figured as a certain percentage of sales, are paid "off the top"—i.e., before the operator makes any deductions for expenses or taxes. The trusts bear none of the risks or costs of drilling or mining. In fact, they are required by the Internal Revenue Service to remain "passive" and, in addition, to pay out virtually all their earnings.

In return, IRS rulings allow the trusts, and investors in their "units of beneficial interest," some tax breaks. The trusts themselves pay no federal income taxes, and the IRS takes the view that investors have a stake in the assets that produce income for the trust. Consequently, part of the cash payout is regarded as depletion, a return of capital, so shareholders pay income tax on that portion.

Bookkeeping is tough

The yields on most of the trusts are fair-ly generous. The highest—11.4 percent for Mesabi Trust—is more than twice the yield on the stock of Cleveland-Cliffs Iron, the nation's largest iron-ore producer. Estimated yields on the other trusts range between 6.7 percent for North European Oil Roy-

alty Trust to 8.1 percent for Mesa Royalty Trust. By comparison, the yield on the S.&P. index of nine domestic oil companies is a slim 3.3 percent.

Figuring the taxes on the trusts' yields is nettlesome, but the bookkeeping is worth the trouble. Investors who have bought into oil and gas trusts in the last few years take "cost depletion," which involves using a depletion rate that is determined annually for each trust by independent engineers. The rates vary—from about 4 percent (an estimate) for Mesa to between 7 and 8 percent for the other three in the table.

The taxpayer applies the depletion rate to the cost of his units. If the rate is 7 percent, for example, and the units have a cost basis of \$40, then \$2.80 is considered a return of capital, and the cost of the units is reduced by that amount. Most of the time the depletion calculation will yield a figure lower than the payout; the rest of the cash distribution is taxed as ordinary income. (The treatment of this excess is dif-

ferent for Mesabi unit-holders. Once its units have been held for a period of time—it varies depending on when they were bought—the excess payout is taxed as a capital gain.)

Even though the underlying assets are being used up, the few analysts who follow the oil and gas trusts expect cash distributions to increase. Frederick A. Lynn, president of F.A.L. Capital Management, has been buying these trusts because he expects oil and gas prices to keep rising, which will not only lift royalties but also cause operators to press harder for more production.

Investors trying to figure out how much production is ultimately possible will be frustrated. While the Securities and Exchange Commission requires most publicly traded companies to report information about the size of their hydrocarbon reserves, some royalty trusts can duck the requirement if the data are either unavailable or too costly to get.

And that's the case with three of the four

THE PAYOUTS KEEP GROWING

	CASH DISTRIBUTION				YIELD	
	1979	1980 estimate	1981 estimate	Rate of growth, compounded 1975-1979	1975	Recent (based on est. 1980 distribution)
North European Oil Royalty Trust	\$4.07	\$5.00	\$7.50	37.2%	6.9%	5.6%
Marine Petroleum Trust	\$2.25	\$2.80	\$3.30	45.7%	8.0%	7.8%
Tidelands Royalty Trust B	\$1.9	\$2.80	\$3.60	N.A.	N.A.	6.7%
Mesa Royalty Trust	N.A.	\$3.05	\$3.30	N.A.	N.A.	8.1%
Mesabi Trust	\$1.39	\$1.65	\$1.80	4.8%	15.9%	11.4%

Two of the four oil and gas royalty trusts shown here—North European and Marine—have boosted cash distributions to investors at a heady pace since 1975. Of the remaining two, Mesa is a newcomer that sprang up last year, and Tidelands, which first began to distribute its royalty income in 1977, has nearly quadrupled its payout in the past two years. The other trust in the group, Mesabi, gets its income from royalties on shipments of iron-

ore pellets, and its performance has been lead- ing. All the estimates for 1980 and 1981 were compiled from forecasts by various analysts and portfolio managers. Though the prices of trust units have risen significantly, the yields, based on the 1980 estimates, have not changed all that radically. A portion of the payouts of all the trusts, with the possible exception of Mesa, can be treated for tax purposes as a return of capital rather than income.

oil and gas trusts. North European Oil derives royalties from properties in West Germany that are leased to Mobil, Royal Dutch, and Exxon, which never whisper a word about the size of those reserves. Gulf Oil is just as tight-lipped about the reserves in fields it operates partly for Marine Petroleum Trust and partly for Tidelands Royalty Trust B.

Investors know a lot more about the reserves associated with Mesa Royalty Trust because of estimates in a prospectus issued last November, when the trust was spun off to shareholders of Mesa Petroleum. Independent petroleum engineers estimated proven oil and gas reserves and calculated their present value, discounting the expected income at an annual rate of 10 percent. This worked out to \$27.75 per unit, but the assumptions about the future price of oil and gas that go into such calculations are considered to be very conservative. Consequently, the units sold for about \$30 once they began trading. They subsequently rose as high as \$42, and were recently selling for about \$35.

Real-world expectations about price increases, particularly for gas, are quite bullish, for good reason. Under the Natural Gas Policy Act of 1978, prices of newly discovered gas—now about \$3 per 1,000 cubic feet (mcf)—may rise 10 percent a year until 1985. At that time controls will be lifted, and some analysts expect new gas to sell at a parity with oil. If they are right, even if oil were to sell at only \$30 a barrel, the price of gas will rise some 65 percent, to \$5 per mcf, in five years, since that quantity of natural gas has one-sixth as much heating power as a barrel of oil.

Life in new leases?

Buyers of Marine Petroleum Trust are betting primarily on the higher gas prices. Marine's royalties—a low 0.75 percent of sales—are derived solely from the trust's interest in 500,000 acres leased to Gulf Oil in the Gulf of Mexico. Half of that acreage now produces oil and gas, much of it coming from "mature" fields. While Gulf could yet find oil or gas in the other half, investors are primarily intrigued that some 70



In the last two years, the standout in this group has been North European, whose units have doubled in price. But over the period shown, Tidelands' shares have gone up even more—from only about \$1 in 1975, to \$42 recently. Shares of Marine (which owns a third of Tidelands' units) have retreated somewhat since reaching a record level last year. With the exception of Mesa and Mesabi, the trusts have relatively few units outstanding, and their prices tend to be quite volatile.

percent of Marine's royalties come from "old" natural gas with an average price of only \$1.20 per mcf. As contracts expire, or if new gas is discovered, that figure will inevitably go a lot higher. And the kicker in Marine is its 32.6 percent equity interest in Tidelands Royalty Trust B.

Tidelands is primarily a speculative bet on an increase in production. The Tidelands trust agreement with Gulf Oil covers 1.3 million acres offshore, and Gulf has so far leased only 40,000 of them. Analysts expect Gulf to seek new leases in the area and to spend freely on wildcat drilling. Tidelands will also benefit, though not as much as Marine, from rising prices: the Tidelands gas sells at an average price of around \$1.80 per mcf.

The price on much of the gas in which Mesa Royalty Trust has an interest is strictly bargain-basement. Close to 80 percent of the gas in its largest field sells under contract at a paltry 25 cents per mcf. The contract won't expire until 1989, but new gas from the same field would, of course, sell for a lot more.

Mesa investors are buying units in the face of an unusual risk: the IRS hasn't yet ruled that it can be treated as a trust. Regardless of how this issue is resolved, a hefty portion of the payout will almost certainly be taxed as ordinary income because Mesa's depletion rate this year is expected to be so low.

The new trust in the wings, an offspring of Houston Oil & Minerals, also lacks an IRS ruling on its tax status. The properties in which Houston Oil Royalty Trust has an interest include a substantial amount of unexplored acreage that would be worth a lot if Houston Oil & Minerals made dis-

coveries there. The company's success in finding new reserves, however, has recently been only fair.

The hottest trust in the market lately has been North European. Unit holders have benefited from the rise in the value of the D-mark because the operating companies involved sell what they produce in West Germany, where the fields are. In the last three years, the trust's royalty income, in dollars, has more than doubled. Carey E. Tharp Jr., an analyst at Stillman, Maynard & Co., is convinced the payout will continue to spurt ahead. He points out that more and more of the gas sold in Germany is coming from a field that produces royalties at a rate 7.5 times higher than the rate on sales from the field that is currently producing much of the trust's income.

A direct link to inflation

The iron trust, Mesabi, hasn't been particularly popular with investors lately. Its royalties come from properties in Minnesota's Mesabi range—the nation's largest iron-ore reserve. They are mined by Reserve Mining, which ships pellets made from the ore to the two steelmakers—Armco and Republic—who jointly own the company. Reserve pays Mesabi a base royalty that depends on the volume of pellets shipped, which means the trust's income is sensitive to the demand for steel. The base is also adjusted by a factor that reflects the annual change in the producer price index. That inflation hedge hasn't swayed investors, who are aware that Reserve's pellet factory could be struck this August when a labor contract expires. After the workers went out three years ago, Mesabi's cash distributions were slashed.

DRAFT: ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM

A BILL

For an Act entitled: "An Act establishing the Alaska Citizens Wealth Ownership Program, and providing for an effective date.

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

Section 1. AS AA is amended by adding a new chapter to read:

CHAPTER 1. ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM

ARTICLE 1. GENERAL PROVISIONS

§AA.BB.100 FINDINGS. The Legislature hereby finds —

R.T. → (1) that it is in the public interest and in the furtherance of a public purpose to distribute a portion of Alaska's energy wealth to the people of Alaska in the form of income-producing assets in order to increase their involvement and awareness regarding the management of the state's natural resources, in the development of its local industry, and in the capitalist system;

R.T. → (2) that a mechanism by which the state distributes a portion of its resource royalties will best promote the state's interest in producing a more personal and direct stake in the impact of decisions involving the state's natural resource production and development; and

(3) that a mechanism by which the state distributes a portion of its ownership interests in business enterprises will best promote the state's interest in providing a more personal and direct stake in the impact of decisions involving state investments, development of local industry, as well as a more personal and direct stake in the capitalist system.

§AA.BB.110. PURPOSES. (a) The Alaska Citizens Wealth Ownership Program (hereinafter the Program) is hereby established in the Department of Revenue.

DRAFT LEGISLATION FOR AN
ALASKA CITIZENS WEALTH OWNERSHIP PLAN

Prepared for the
OFFICE OF THE GOVERNOR
STATE OF ALASKA

By
ARLON R. TUSSING & ASSOCIATES, INC.
and
PRESTON, THORGRMISON, HOLMAN & ELLIS

27 March, 1980

ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM

INTRODUCTION AND EXPLANATION OF MARCH 27 DRAFT

There are three main parts to the draft legislation: Chapter 1 establishes a general procedure for distributing any of several kinds of securities to Alaska residents; Chapters 2 through 7 describe the different kinds of securities; and Chapters 8 and 9 provide for a distribution that could be put into effect this year and which would put securities of unquestionable value into the hands of Alaskans (as opposed to some of the more speculative alternatives, such as AGSOC or a share in the gas conditioning plant).

Article 1 of Chapter 1 sets out the purposes of the Program -- these are self-explanatory. It houses the Program in the Department of Revenue, and requires the Commissioner to submit at least one and as many as three wealth distribution plans to the legislature each year. Each plan must be accompanied by a financial and legal analysis, and will not go into effect unless enacted as a law or joint resolution.

Article 2 defines residency for the purpose of obtaining benefits under the program. Beneficiaries of any plan are limited to Alaska residents as of an eligibility date specified for that plan. The legislation also sets out the evidence a person must submit to establish a presumption of residency, and certain actions that establish a presumption of non-residency.

Article 3 spells out the general procedures for distributing securities to eligible residents. A small part (5 to 15 percent) of the securities distributed under each plan will be distributed free, in equal portions to each resident who applies for them. This provision assures that everybody gets something, and serves as advertisement for the program. Most of the assets distributed (85 to 95 percent), however, are to be sold to residents at their nominal value. There are at least three major reasons for selling, rather than giving away, the bulk of the assets:

(a) Sale at value is far more likely to survive constitutional challenge than free distribution. [The legislation will be written so that the sales procedures will survive even if the courts disallow free grants.]

(b) Sale at value is unlikely to create any federal tax liability for the recipient, while the IRS may rule that assets received free of charge are taxable income in the year they are received.

(c) People are likely to place a higher value on things they have to pay for than on free gifts.

There are at least three reasons Alaskans would want to buy assets distributed under the program:

(a) We assume that some kind of tax credit scheme will be adopted, and Alaska taxpayers will be allowed to apply any tax credit or refund to the purchase of securities under the plan. Thus, although they will have to make a real choice (between investments and cash), many and probably most Alaskans will be able to avoid any cash outlay.

(b) Most assets will be sold at a "cost" or "conservatively appraised value" intended to satisfy constitutional and federal tax requirements, but they can be expected to earn exceptionally high rates of return in relation to that "cost".

(c) Residents will be able to buy the securities on time, over a ten year period at a carrying cost far less than their expected rate of return.

Alaskans who want to buy securities on time will be issued non-transferable warrants --- certificates that allow them to buy a specified number of units each year at a fixed price. While Alaskans who move away will be able to keep the securities they have actually bought, and (with certain important exceptions) to sell them freely, their unused warrants will become invalid.

Article 4 sets out the rights of securities holders. Except for the non-transferable warrants described above, shares in a natural resource trust (which can be transferred or sold only to other resident Alaskans, except by inheritance), and AGSOC shares (whose ownership is restricted by federal law), the assets distributed under the program will be the unrestricted property of the recipients, and can be disposed of as they wish.

Article 5 states that receipt of securities under the program, whether by grant or by purchase, is not taxable income under Alaska law, but that income from those securities, and proceeds from their resale, will be treated like any other income or capital gains. It also provides that if the IRS rules receipt of these securities to be taxable income under federal law, any additional federal tax the recipient is required to pay may be credited against Alaska income taxes.

Article 6 provides for the Commissioner of Revenue to buy and sell securities distributed under the program in order to create an orderly market for them, if an effective private market for those securities did not otherwise develop.

Article 7 (not yet drafted) will define various terms used in the legislation; provide penalties for persons who falsely claim residency or make false statements in order to obtain benefits under the program; and specifies what parts of the legislation will remain valid if other parts are declared unconstitutional.

Chapters 2 through 7 describe the various kinds of assets that can be distributed under the Program. For each kind of asset, the Commissioner of Revenue would have to present a specific plan to be acted on by the legislature.

Alaska Energy Resource Trusts are royalty trusts — devices for passing on a portion of the state's oil and gas royalties directly to holders of certificates in the trust. (See the attached clipping from Fortune magazine. [pp ix-x])

Alaska Industrial Development Projects are major new investments, like the gas pipeline or conditioning plant, in which the state might decide to participate financially. Chapter 3 provides that if the state does make such an investment, the state's ownership and management role should be temporary — through the development phase only — and that the state's shares in the project should ultimately be distributed to Alaskans under this program.

Alaska General Stock Ownership Corporations (AGSOCs) are the familiar Kelso-Gravel idea. Chapter 4 would incorporate the major provisions of the bill reported by the House State Affairs Committee, but (in contrast to the current initiative) would require the legislature to act upon a complete financing plan before creating any AGSOC.

Alaska Investment Funds are regulated investment companies (mutual funds) empowered to invest in the securities of corporations doing business in Alaska, and Alaska Real Estate Trusts are real estate investment trusts (REITs) empowered to invest in Alaska real estate developments. Both kinds of enterprise are essentially passive investments and are in themselves exempt from federal income taxes (like AGSOCs); they are a way of increasing resident Alaskan ownership in major Alaska industry without the state's having to register as a securities underwriter.

Chapter 7 provides for the distribution of securities in existing private enterprises. This provision would allow the State to buy blocks of shares in major Alaska businesses (fish processing plants, airline and communications companies, and the like), and to sell them to residents on easy terms in order to increase resident Alaskan ownership and control in important industries.

Chapters 8 and 9 set out specific wealth distribution programs that could be put into effect by the current legislature. Both are Alaska Energy Resource Trusts.

We believe that the effectiveness and credibility of the program demands that there be an early distribution of assets that have a certain, positive value. The first distribution must be one that neither requires a large front-end appropriation of money nor presents any risks to the citizens who receive the assets. Shares in oil and gas royalties --- specifically, royalties from the proved reserves at Prudhoe Bay --- seem to be the only kind of asset that can play this pioneering role.

The Prudhoe Bay Oil and Gas Royalty Trust of 1980 would commit royalties from only some of the leases at Prudhoe Bay, and only those royalties in excess of current levels. Thus, the revenues conveyed to the trust would increase very rapidly with the decontrol of crude oil prices, and then fall off very rapidly as Prudhoe Bay production declined. We suggest the leases be chosen so that the average distribution per capita in the first year is in the \$100 to \$200 range --- large enough that people will have to take it seriously, but (in this first distribution) not enough to make a large dent in available revenues.

The Beaufort Sea Oil and Gas Royalty Trust of 1980 would commit royalties from Beaufort Sea leases sold in 1979. Any revenues produced from those leases would be distributed much later than the Prudhoe Bay royalties, and while the value of the certificates would probably be much greater, they would be a far more speculative property. Conceivably, the two plans could be combined into one plan that provided some certain near-term income, and some less certain but possibly far greater income, say, seven to ten years in the future.

The certificate holders would not have any voice in management of the oil and gas resource itself, and the trust indenture specifically makes the conveyance subject to any existing commitments of royalties. It also preserves the state's option to take royalty in kind --- it therefore creates no obstacles, for example, to fulfilling the Alpetco

contract or to exchanging royalty gas for gas liquids to be used in Alaska petrochemical development. But the plans will certainly create a greater citizen identification with the North Slope oil and gas resource, and a more intense and informed interest in state and federal policies affecting those resources. --

These plans would probably make Alaskans more receptive, for example, to state financial participation in the gas line, especially if state involvement can reasonably be expected to accelerate its completion — and thereby the flow of gas royalties. The plans would also create a broadly-based Alaska constituency pressing to maximize the wellhead value of the state's oil and gas, and resisting proposals to give away or discount the state's royalty for any purpose. (After all, the people will recognize, as they may not fully appreciate now, that these decisions involve their own money.)

ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM
DRAFT LEGISLATION

CONTENTS

TITLE	1
CHAPTER 1. ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM	1
ARTICLE 1. GENERAL PROVISIONS	1
Section 100 Findings	1
Section 110. Purposes (a)	1
(b) to (e)	2
Section 115. Alaska Citizens Wealth Distribution-Plans	
(a) to (c)	3
Section 120. Plans submitted to Legislature (a) and (b)	4
(c) and (d)	5
(d) [continued] and (e)	6
ARTICLE 2. ELIGIBILITY FOR BENEFITS	
Section 210. Eligibility for benefits (a) to (d)	7
Section 215. Alaska residency defined (a) to (c)	8
Section 220. Evidence of residency (a) and (b)	9
Section 225. List of persons claiming residency	10
ARTICLE 3. DISTRIBUTION OF ASSETS	11
Section 310. Basic purchase price (a)	11
(b) and (c)	12
Section 315. Free distribution	13
Section 320. First restricted sale (a) to (d)	13
(e) and (f)	14
Section 325. Second restricted sale (a) to (c)	15
(d) and (e)	16
Section 330. Unrestricted sale	17
Section 335. Stock-purchase warrants (a)	18
(b)	19
(c) and (d)	20
Section 340. Use of income tax credits (a) and (b)	21
(c) and (d)	22
ARTICLE 4. OWNERSHIP RIGHTS	23
Section 410. Transfer of assets	23
Section 415. Voting rights	23
ARTICLE 5. TAX TREATMENT	24
Section 510. Receipt of assets not taxable	24
Section 515. Credit for federal taxes paid	24
Section 520. Income not tax-exempt	24
ARTICLE 6. SECURITIES MARKETS	25
ARTICLE 7 MISCELLANEOUS PROVISIONS	26*
Section 700. Definitions	26*
Section 710. Penalties for false statements	26*
Section 720. Savings clauses	26*

CHAPTER 2.	ALASKA ENERGY RESOURCE TRUSTS	27
Section 110.	Alaska Energy Resource Trust defined	27
Section 120.	Distribution of certificates	27
Section 140.	Ownership and transferability	28
CHAPTER 3.	ALASKA INDUSTRIAL DEVELOPMENT PROJECTS	29
Section 110.	Alaska Industrial Development Project defined	29
Section 120.	Intent	29
Section 130.	Alaska Natural Gas Transportation System	30
CHAPTER 4.	ALASKA GENERAL STOCK OWNERSHIP CORPORATIONS	31
ARTICLE 1.	GENERAL PROVISIONS	31
Section 110.	Alaska General Stock Ownership Corporation defined	31
ARTICLE 2		*
CHAPTER 5.	ALASKA INVESTMENT FUNDS	32
Section 110.	Alaska Investment Fund defined	32
		*
CHAPTER 6.	ALASKA REAL ESTATE TRUSTS	33
Section 110.	Alaska Real Estate Trust defined	33
		*
CHAPTER 7.	EXISTING PRIVATE ENTERPRISES	34
Section 110.	Existing private enterprise defined	34
CHAPTER 8.	PRUDHOE BAY OIL AND GAS ROYALTY TRUST PLAN OF 1980	35
ARTICLE 1.	FORMATION OF TRUST	
Section 110.	Creation of trust	35
Section 120.	Trust indenture	35
Section 130.	Amendments to trust indenture	35
Section 140.	Purpose	36
Section 150.	The trust estate	36
Section 155.	Conveyance of royalties (a) through (c)	36
	(c)[continued] through (d)	37
Section 160.	Rule against perpetuities	37
ARTICLE 2.	TRUSTEE	38
Section 210.	Selection of trustee and successor trustees (a) to (d)	38
Section 220.	Powers and duties of trustee	39
Section 230.	No power to engage in business or make investments	40
Section 240.	Liability of trustee	40
Section 250.	Compensation of trustee	40
Section 260.	Investment of cash reserves	40
Section 270.	Payment of liabilities (a)	40
	(b)	41
Section 280.	Resignation and termination of trustee (a)	41
	(b)	42

* Drafting incomplete as of 27 March, 1980.

-viii-(B2)

DRAFT OF 27 MARCH, 1980 (A.T.)
Supersedes all previous drafts

ARTICLE 3. TERMINATION OF TRUST AND LIQUIDATION	42
Section 310. Duration, revocation, and termination of trust	42
Section 320. Liquidation	42
ARTICLE 4. BENEFICIAL INTERESTS	43
Section 410. Creation of beneficial shares and certificates	43
Section 420. Rights of certificate holders (a)	44
(b) and (c)	45
Section 430. Execution of certificates	45
Section 440. Registration and transfer of units	45
Section 450. Determination and ownership of certificates	46
ARTICLE 5. ACCOUNTING AND DISTRIBUTION	47
Section 510. Fiscal year and accounting method (a) and (b)	47
Section 520. Distributions (a) and (b)	47
Section 530. Tax reporting	48
Section 540. Reports to certificate holders	48
ARTICLE 6. MEETINGS	48
Section 610. Meetings of certificate holders (a) to (c)	48
(d)	49
Section 620. Voting	49
Section 630. Conduct of meetings	49
ARTICLE 7. GENERAL PROVISIONS	50
Section 710. Inspection of trustee's books	50
Section 720. Definitions	50
CHAPTER 8. BEAUFORT SEA OIL AND GAS ROYALTY TRUST OF 1980	51
[The article and section titles will be the same as for Chapter 7]	

Personal Investing

Trusts That Rake Royalties Off the Top by Aimée L. Morner

Inflation hedgers flocking into natural-resource investments have been eyeing some unusual vehicles known as royalty trusts. These trusts, a few of which have been around since the early 1950's, are unincorporated enterprises that act as conduits for distributing royalty income to investors. Four of the five large publicly traded trusts (see table) derive their income from royalties on sales of oil and gas; the other, Mesabi Trust, gets its royalties from iron ore. Not surprisingly, the oil and gas trusts have risen the most in the last few years, and in mid-March a big new one—Houston Oil Royalty Trust—was about to come to market.

All of the royalty trusts share some common characteristics. None of them owns any real property; instead, they hold interests in royalties from properties owned by, or leased to, one or more operating companies. The royalties, figured as a certain percentage of sales, are paid "off the top"—i.e., before the operator makes any deductions for expenses or taxes. The trusts thus bear none of the risks or costs of drilling or mining. In fact, they are required by the Internal Revenue Service to remain "passive" and, in addition, to pay out virtually all their earnings.

In return, IRS rulings allow the trusts, and investors in their "units of beneficial interest," some tax breaks. The trusts themselves pay no federal income taxes, and the IRS takes the view that investors have a stake in the assets that produce income for the trust. Consequently, part of the cash payout is regarded as depletion, i.e., a return of capital, so shareholders pay no income tax on that portion.

The bookkeeping is tough

The yields on most of the trusts are fairly generous. The highest—11.4 percent for Mesabi Trust—is more than twice the yield on the stock of Cleveland-Cliffs Iron, the nation's largest iron-ore producer. Estimated yields on the other trusts range between 5.6 percent for North European Oil Roy-

alty Trust to 8.1 percent for Mesa Royalty Trust. By comparison, the yield on the S.&P. index of nine domestic oil companies is a slim 3.3 percent.

Figuring the taxes on the trusts' yields is nettlesome, but the bookkeeping is worth the trouble. Investors who have bought into oil and gas trusts in the last few years take "cost depletion," which involves using a depletion rate that is determined annually for each trust by independent engineers. The rates vary—from about 4 percent (an estimate) for Mesa to between 7 and 8 percent for the other three in the table.

The taxpayer applies the depletion rate to the cost of his units. If the rate is 7 percent, for example, and the units have a cost basis of \$40, then \$2.80 is considered a return of capital, and the cost of the units is reduced by that amount. Most of the time the depletion calculation will yield a figure lower than the payout; the rest of the cash distribution is taxed as ordinary income. (The treatment of this excess is dif-

ferent for Mesabi unit-holders. Once its units have been held for a period of time—it varies depending on when they were bought—the excess payout is taxed as a capital gain.)

Even though the underlying assets are being used up, the few analysts who follow the oil and gas trusts expect cash distributions to increase. Frederick A. Lynn, president of F.A.L. Capital Management, has been buying these trusts because he expects oil and gas prices to keep rising, which will not only lift royalties but also cause operators to press harder for more production.

Investors trying to figure out how much production is ultimately possible will be frustrated. While the Securities and Exchange Commission requires most publicly traded companies to report information about the size of their hydrocarbon reserves, some royalty trusts can duck the requirement if the data are either unavailable or too costly to get.

And that's the case with three of the four

THE PAYOUTS KEEP GROWING

	CASH DISTRIBUTION				YIELD	
	1979	1980 estimate	1981 estimate	Rate of growth, compounded 1975-1979	1975	Recent (based on est. 1980 distribution)
North European Oil Royalty Trust	\$4.07	\$5.00	\$7.50	37.2%	6.9%	5.6%
Marine Petroleum Trust	\$2.25	\$2.80	\$3.30	45.7%	8.0%	7.8%
Tidelands Royalty Trust B	\$1.94	\$2.80	\$3.60	N.A.	N.A.	6.7%
Mesa Royalty Trust	N.A.	\$3.05	\$3.30	N.A.	N.A.	8.1%
Mesabi Trust	\$1.39	\$1.65	\$1.80	4.8%	15.9%	11.4%

Two of the four oil and gas royalty trusts shown here—North European and Marine—have boosted cash distributions to investors at a heady pace since 1975. Of the remaining two, Mesa is a newcomer that sprang up last year, and Tidelands, which first began to distribute its royalty income in 1977, has nearly quadrupled its payout in the past two years. The other trust in the group, Mesabi, gets its income from royalties on shipments of iron-

ore pellets, and its performance has been leaden. All the estimates for 1980 and 1981 were compiled from forecasts by various analysts and portfolio managers. Though the prices of trust units have risen significantly, the yields, based on the 1980 estimates, have not changed all that radically. A portion of the payouts of all the trusts, with the possible exception of Mesa, can be treated for tax purposes as a return of capital rather than income.

oil and gas trusts. North European Oil derives royalties from properties in West Germany that are leased to Mobil, Royal Dutch, and Exxon, which never whisper a word about the size of those reserves. Gulf Oil is just as tight-lipped about the reserves in fields it operates partly for Marine Petroleum Trust and partly for Tidelands Royalty Trust B.

Investors know a lot more about the reserves associated with Mesa Royalty Trust because of estimates in a prospectus issued last November, when the trust was spun off to shareholders of Mesa Petroleum. Independent petroleum engineers estimated proven oil and gas reserves and calculated their present value, discounting the expected income at an annual rate of 10 percent. This worked out to \$27.75 per unit, but the assumptions about the future price of oil and gas that go into such calculations are considered to be very conservative. Consequently, the units sold for about \$30 once they began trading. They subsequently rose as high as \$42, and were recently selling for about \$35.

Real-world expectations about price increases, particularly for gas, are quite bullish, for good reason. Under the Natural Gas Policy Act of 1978, prices of newly discovered gas—now about \$3 per 1,000 cubic feet (mcf)—may rise 10 percent a year until 1985. At that time controls will be lifted, and some analysts expect new gas to sell at a parity with oil. If they are right, even if oil were to sell at only \$30 a barrel, the price of gas will rise some 65 percent, to \$5 per mcf, in five years, since that quantity of natural gas has one-sixth as much heating power as a barrel of oil.

Life in new leases?

Buyers of Marine Petroleum Trust are betting primarily on the higher gas prices. Marine's royalties—a low 0.75 percent of sales—are derived solely from the trust's interest in 500,000 acres leased to Gulf Oil in the Gulf of Mexico. Half of that acreage now produces oil and gas, much of it coming from "mature" fields. While Gulf could yet find oil or gas in the other half, investors are primarily intrigued that some 70



In the last two years, the standout in this group has been North European, whose units have doubled in price. But over the period shown, Tidelands' shares have gone up even more—from only about \$1 in 1975, to \$42 recently. Shares of Marine (which owns a third of Tidelands' units) have retreated somewhat since reaching a record level last year. With the exception of Mesa and Mesabi, the trusts have relatively few units outstanding, and their prices tend to be quite volatile.

percent of Marine's royalties come from "old" natural gas with an average price of only \$1.20 per mcf. As contracts expire, or if new gas is discovered, that figure will inevitably go a lot higher. And the kicker in Marine is its 32.6 percent equity interest in Tidelands Royalty Trust B.

Tidelands is primarily a speculative bet on an increase in production. The Tidelands trust agreement with Gulf Oil covers 1.3 million acres offshore, and Gulf has so far leased only 40,000 of them. Analysts expect Gulf to seek new leases in the area and to spend freely on wildcat drilling. Tidelands will also benefit, though not as much as Marine, from rising prices: the Tidelands gas sells at an average price of around \$1.80 per mcf.

The price on much of the gas in which Mesa Royalty Trust has an interest is strictly bargain-basement. Close to 80 percent of the gas in its largest field sells under contract at a paltry 25 cents per mcf. The contract won't expire until 1989, but new gas from the same field would, of course, sell for a lot more.

Mesa investors are buying units in the face of an unusual risk: the IRS hasn't yet ruled that it can be treated as a trust. Regardless of how this issue is resolved, a hefty portion of the payout will almost certainly be taxed as ordinary income because Mesa's depletion rate this year is expected to be so low.

The new trust in the wings, an offspring of Houston Oil & Minerals, also lacks an IRS ruling on its tax status. The properties in which Houston Oil Royalty Trust has an interest include a substantial amount of unexplored acreage that would be worth a lot if Houston Oil & Minerals made dis-

coveries there. The company's success in finding new reserves, however, has recently been only fair.

The hottest trust in the market lately has been North European. Unit holders have benefited from the rise in the value of the D-mark because the operating companies involved sell what they produce in West Germany, where the fields are. In the last three years, the trust's royalty income, in dollars, has more than doubled. Carey E. Tharp Jr., an analyst at Stillman, Maynard & Co., is convinced the payout will continue to spurt ahead. He points out that more and more of the gas sold in Germany is coming from a field that produces royalties at a rate 7.5 times higher than the rate on sales from the field that is currently producing much of the trust's income.

A direct link to inflation

The iron trust, Mesabi, hasn't been particularly popular with investors lately. Its royalties come from properties in Minnesota's Mesabi range—the nation's largest iron-ore reserve. They are mined by Reserve Mining, which ships pellets made from the ore to the two steelmakers—Armco and Republic—who jointly own the company. Reserve pays Mesabi a base royalty that depends on the volume of pellets shipped, which means the trust's income is sensitive to the demand for steel. The base is also adjusted by a factor that reflects the annual change in the producer price index. That inflation hedge hasn't swayed investors, who are aware that Reserve's pellet factory could be struck this August when a labor contract expires. After the workers went out three years ago, Mesabi's cash distributions were slashed. F

DRAFT: ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM

A BILL

For an Act entitled: "An Act establishing the Alaska Citizens Wealth Ownership Program, and providing for an effective date.

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

Section 1. AS AA is amended by adding a new chapter to read:

CHAPTER 1. ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM

ARTICLE 1. GENERAL PROVISIONS

§AA.BB.100 FINDINGS. The Legislature hereby finds —

(1) that it is in the public interest and in the furtherance of a public purpose to distribute a portion of Alaska's energy wealth to the people of Alaska in the form of income-producing assets in order to increase their involvement and awareness regarding the management of the state's natural resources, in the development of its local industry, and in the capitalist system;

(2) that a mechanism by which the state distributes a portion of its resource royalties will best promote the state's interest in producing a more personal and direct stake in the impact of decisions involving the state's natural resource production and development; and

(3) that a mechanism by which the state distributes a portion of its ownership interests in business enterprises will best promote the state's interest in providing a more personal and direct stake in the impact of decisions involving state investments, development of local industry, as well as a more personal and direct stake in the capitalist system.

§AA.BB.110. PURPOSES. (a) The Alaska Citizens Wealth Ownership Program (hereinafter the Program) is hereby established in the Department of Revenue.

(b) The Program's purposes are:

(1) to transfer part of Alaska's petroleum wealth to its people in the form of income-producing assets;

(2) to provide a means for the direct participation of individual Alaskans in the financing of, and profits from, newly organized enterprises of general benefit to the state [such as the Alaska Natural Gas Transportation System (ANGIS)];

(3) to promote greater resident Alaskan control, and to reduce absentee ownership and control, of existing Alaska industries;

(4) to encourage wider citizen participation in and understanding of the capitalist system through a wider distribution of ownership in Alaska business enterprise;

(5) to encourage increased awareness and involvement by the people of Alaska in the management of natural resource production and development;

(6) to encourage increased awareness and involvement by the people of Alaska in the state's participation in business enterprise; and

(7) to encourage increased awareness and involvement by the people of Alaska in the development of local industry.

(c) Except as expressly required or authorized by this Act, or otherwise required by United States or Alaska laws, the assets distributed under the Program shall be the unencumbered private property of its beneficiaries, and the beneficiaries shall not be in any way impaired in their enjoyment of the earnings of those assets, the proceeds of their sale, or any other advantage of their use or disposition.

(d) The Program is not intended to create or result in the creation of any new governmental agency, corporation, or enterprise.

(e) Except as expressly provided in this Act, the Program is not intended to be part of, duplicate, enlarge or diminish, conflict with, substitute for, or alter in any way —

(1) any existing service or function of State government;

(2) any State business loan or industrial development program;

(3) any plan for the elimination, refund, or reduction of any State personal or business tax; or

(4) the investment of State revenues in, or the disposition of earnings from, the Permanent Fund.

§ AA.BB.115. ALASKA CITIZENS WEALTH DISTRIBUTION PLANS. (a) An Alaska Citizens Wealth Distribution Plan (hereinafter a Plan) is a plan under which the Commissioner of Revenue (hereinafter the Commissioner)

(1) contributes, transfers, commits, or dedicates to the Program securities, rights to resource revenues, or other assets, either already owned by the State or acquired expressly for the Program; and

(2) distributes those assets to individual Alaskans by grant and/or sale under the terms of this Act.

(b) Each Plan shall provide for the distribution of assets to individual Alaskans in the form of shares, certificates, debentures, warrants, options, or other securities or instruments that establish their ownership, right, or interest in one (and only one) of the following:

(1) An Alaska Energy Resource Trust, as provided in CHAPTER 2 of this Act.

(2) An Alaska Industrial Development Project, as provided in CHAPTER 3 of this Act.

(3) An Alaska General Stock Ownership Corporation, as provided in CHAPTER 4 of this Act.

(4) An Alaska Investment Fund, as provided in CHAPTER 5 of this Act.

(5) An Alaska Real Estate Trust, as provided in CHAPTER 6 of this Act.

(6) Shares in one or more existing private enterprises doing business in Alaska, as provided in CHAPTER 7 of this Act.

(c) Each Plan shall provide for a single distribution of such shares, certificates, debentures, warrants, options, or other securities or instruments, only to persons who were residents of Alaska as of an eligibility date to be specified in the Plan.

§ AA.BB.120. PLANS SUBMITTED TO LEGISLATURE. (a) The Commissioner shall, on or before the thirtieth legislative day of each Session of the Legislature beginning with the 1981 Session, submit to the Legislature for its consideration and approval, at least one Plan, and not more than three Plans.

(b) Each Plan submitted to the legislature under this section shall be in the form of a Bill or Joint Resolution that —,

(1) specifies the assets to be made available for distribution;

(2) authorizes their purchase or other acquisition by the State, if necessary, and their appropriation, transfer, commitment, or dedication to the Plan;

(3) specifies the eligibility date for persons receiving benefits under the Plan;

(4) specifies the manner in which eligible persons must apply for a grant of assets, or subscribe to purchase assets, distributed under the Plan, and the earliest and latest dates on which they may make such an application or subscription;

(5) specifies the type and number of shares, certificates, debentures, warrants, options, or other securities or instruments to be distributed, and the manner in which they are to be distributed;

(6) specifies the terms and manner of payment for any shares, certificates, debentures, warrants, options, or other securities or instruments to be sold under the Plan;

(7) directs and authorizes the disposition of any assets appropriated, transferred, committed, or dedicated to the Plan, and of any authorized or issued shares, certificates, debentures, warrants, options, or other securities or instruments, which are not actually distributed under the Plan;

(8) specifies the restrictions, if any, on the sale, assignment, hypothecation, or other transfers of or encumbrances upon the shares, certificates, debentures, warrants, options, or other securities or instruments distributed under the Plan, consistent with this Act; and

(9) authorizes the appropriation and expenditure of such funds as may be necessary to administer the Plan.

(c) Each Plan submitted to the Legislature under this section shall be accompanied by ---

(1) such draft legislation in the form of a Bill or Bills amending the general laws of Alaska, as may be necessary, to implement the Plan. [An example might be enactment of an Alaska regulated investment company (mutual fund) law, in order to establish an Alaska Investment Fund under CHAPTER 6 of this Act.]

(2) the proposed articles of incorporation and by-laws of any corporate entity, or the proposed indentures of any trust, whose creation is necessary to implement the Plan;

(3) the names of, or a statement of the manner of selecting, the incorporators and initial directors of any such corporate entity, or trustee(s) of any such trust; and

(d) CHAPTERS 8 and 9 of this Act shall be deemed to be Plans for the purposes of this section.

(4) a statement that contains —

(A) a description of the assets to be distributed under the Plan, and an appraisal of their value, with due attention to any uncertainty that may attach to the appraisal;

(B) a tabulation of the initial fiscal cost of the Plan to the State, and a projection of probable future fiscal costs, with due attention to any contingent fiscal costs, liabilities, or risks that may attach to the Plan;

(C) projections of the probable earnings and appreciation (or decline) in the value of those assets, and of their probable impact on income and wealth of the Plan's intended beneficiaries, with due attention to any uncertainty that may attach to those projections;

(D) a statement of any federal or state tax liability that might be incurred by beneficiaries of the Plan in connection with the initial distribution of shares, certificates, debentures, warrants, options, or other securities or instruments, earnings derived from them, or their ultimate sale or other disposal, with due attention to any uncertainty that may exist with respect to that tax liability [for example, regarding future IRS rulings];

(E) an assessment of any other costs, liabilities, or risks that may attach to the receipt or ownership of assets distributed under the Plan; and

(F) such other kinds of information as the United States and Alaska securities laws might require to be included in a registration statement or prospectus in an ordinary public offering or sale of the kinds of shares, certificates, debentures, warrants, options, or other securities or instruments to be distributed under the Plan.

(f) The Legislature may study, debate, amend, and enact or reject a Plan in the same manner as other Acts or joint resolutions, as provided by the Alaska Constitution and the rules of the Legislature.

ARTICLE 2. ELIGIBILITY FOR BENEFITS

§AA.BB.210. ELIGIBILITY FOR BENEFITS. (a) No person other than a natural person who is a resident of Alaska as defined in AS AA.BB.215 on the eligibility date established for any Plan may receive a free grant under that Plan of shares, certificates, debentures, warrants, options, or other securities or instruments as described in AS AA.BB.315, or purchase such assets under that Plan on the First or Second Restricted Sales as described in AS AA.BB.320-325.

(b) No person who has been granted, without consideration, any non-transferable warrant or option to purchase shares, certificates, debentures, or other assets distributed under this Program, and who has ceased to be a resident of Alaska, may exercise any such warrant or option or portion thereof remaining unexercised on the date on which said person ceased to be a citizen of [a resident of, domiciled in?] Alaska, and any said unexercised warrant or option or portion thereof shall become null and void as of that date.

(c) (1) No person who has purchased, for consideration, any non-transferable warrant or option to purchase shares, certificates, debentures, or other assets distributed under this Program, and who has ceased to be a resident of Alaska, may exercise any such warrant or option or portion thereof that remains unexercised on the date on which said person ceased to be a resident of Alaska, but (2) any such person may offer any such unexercised and otherwise valid warrant or option or portion thereof for repurchase by the State, and upon such an offer the Commissioner shall repurchase said asset at its issue price, plus interest accrued from the date of issue to the date on which the offeror ceased to be a resident Alaska.

(d) Any installment contract or other loan made or held by the State of Alaska or any agency thereof for the purchase of shares, certificates, debentures, warrants, options, or other securities or instruments distributed under this Program, or secured by such assets, shall become due and payable as of the date the beneficiary ceases to be a resident of Alaska.

(4) a statement that contains —

(A) a description of the assets to be distributed under the Plan, and an appraisal of their value, with due attention to any uncertainty that may attach to the appraisal;

(B) a tabulation of the initial fiscal cost of the Plan to the State, and a projection of probable future fiscal costs, with due attention to any contingent fiscal costs, liabilities, or risks that may attach to the Plan;

(C) projections of the probable earnings and appreciation (or decline) in the value of those assets, and of their probable impact on income and wealth of the Plan's intended beneficiaries, with due attention to any uncertainty that may attach to those projections;

(D) a statement of any federal or state tax liability that might be incurred by beneficiaries of the Plan in connection with the initial distribution of shares, certificates, debentures, warrants, options, or other securities or instruments, earnings derived from them, or their ultimate sale or other disposal, with due attention to any uncertainty that may exist with respect to that tax liability [for example, regarding future IRS rulings];

(E) an assessment of any other costs, liabilities, or risks that may attach to the receipt or ownership of assets distributed under the Plan; and

(F) such other kinds of information as the United States and Alaska securities laws might require to be included in a registration statement or prospectus in an ordinary public offering or sale of the kinds of shares, certificates, debentures, warrants, options, or other securities or instruments to be distributed under the Plan.

(f) The Legislature may study, debate, amend, and enact or reject a Plan in the same manner as other Acts or joint resolutions, as provided by the Alaska Constitution and the rules of the Legislature.

§AA.BB.215. ALASKA RESIDENCY DEFINED. (a) For the purposes of this Act, "resident" means a natural person who maintains a permanent place of abode in the state with the intention of making the state his or her permanent place of residence and who resides in the state continuously except for temporary purposes only and with the intent of returning.

(b) A person may not be considered to have gained a residence solely by reason of his or her presence and may not lose it solely by reason of his or her absence while in the civil or military service of this state or of the United States or by reason of his or her absence because of marriage to a person engaged in the civil or military service of this state or of the United States, or for attendance as a student or visiting scholar at an educational institution, or while in an institution at public expense, while confined in prison, while engaged in the navigation of the waters of the state, the United States, or the high seas, or while residing upon an Indian or military reservation within the state.

(c) A minor's residence shall be deemed to be the same as that of his or her parent or guardian; a married person may establish his or her own residence, and does not presumptively lose residency if his or her spouse is not a resident.

§AA.BB.220 EVIDENCE OF RESIDENCY. (a) A person shall be presumed to be a resident of Alaska on a specified date, as defined in AS AA.BB.215, if he or she offers at least two of the following:

(1) evidence that he or she was registered to vote in Alaska on that date, and actually voted in the last statewide general election prior to that date;

(2) a copy of the individual's Alaska resident personal income tax return for the tax year which includes that date, or for the previous tax year;

(3) an Alaska driver's license, or resident hunting, fishing, or trapping license, purchased prior to that date, and valid on that date;

(4) evidence that he or she had a telephone or electric utility connection listed in his or her name, or in the name of a spouse, or (in the case of a minor) in the name of a parent or guardian, at a private residence in Alaska on that date; and

(5) a notarized affidavit from two or more Alaska residents who can themselves present at least two of the items listed in paragraphs (1) through (4) of this subsection.

(b) A presumption of residency established under subsection (a) of this section may be rebutted, and a person shall be presumed not to be a resident on a given date if, within thirty days prior to or one year following that date, he or she —

(1) voted in an election, or stood for election or served in public office, in another state or nation; or

(2) declared himself or herself to be a resident of any other state or nation for any purpose, or took advantage of any right or privilege reserved to residents of another state or nation.

§AA.BB.225 LIST OF PERSONS CLAIMING RESIDENCE. At least sixty days prior to the distribution of any shares, certificates, debentures, warrants, options, or other securities or instruments under any Plan, the Commissioner shall make available for public inspection in at least five locations around the state, a list of the names, addresses, and type of residency evidence submitted, of all persons claiming to be residents for the purpose of receiving benefits under the Plan.

ARTICLE 3. DISTRIBUTION OF ASSETS

§AA.BB.310. BASIC PURCHASE PRICE. (a) The Commissioner shall establish a basic purchase price for any shares, certificates, or debentures to be distributed to individual Alaskans under each Plan, as follows:

(1) The basic purchase price for shares or debentures of an Alaska Industrial Development Project, an Alaska General Stock Ownership Corporation, an Alaska Investment Fund, an Alaska Real Estate Trust, or existing private enterprises, authorized to be distributed to individual Alaskans under any Plan, shall be equal to the average original cost to the State of Alaska of those shares or debentures, or of the other assets contributed, transferred, committed, or dedicated to the Program and represented by those shares or debentures, plus an amount that, in the judgement of the Commissioner, compensates the State for the administrative costs of acquiring, holding, and distributing those shares, debentures, or assets; and

(2) The basic purchase price for the certificates of an Alaska Energy Resource Trust, authorized to be distributed to individual Alaskans under any Plan shall be the conservatively appraised value of those certificates, as defined in subsection (b) of this section.

(b) A "conservatively appraised value" for certificates of an Alaska Energy Resources Trust is a value determined by generally accepted appraisal methods, with the following stipulations:

(1) estimates of resource or production volumes shall have a confidence level of seventy-five percent (75%) or greater — that is, the appraiser must believe that there is at least a seventy-five percent probability that the actual resource or production volume will equal or exceed the estimated value;

(2) the assumed rate of increase in future world prices for energy commodities (as represented, for example, by the price of Saudi Arabian "marker" crude oil) shall not exceed the general rate of price inflation in the United States; and

(3) the discount rate used to reduce future income and costs to present value shall reflect the judgment of private investors as to the expected pre-tax rate of return required to justify incremental investments in the exploration and development of resources comparable to those from which income has been committed to the Plan.

(c) The shares, certificates, or debentures distributed under any Plan must be divided, or must be subdivisible at the option of the holder, into units whose basic purchase price does not exceed fifty dollars (\$50) per unit.

§AA.BB.315 FREE DISTRIBUTION. Under each Plan, a fraction to be specified in the Plan, but not less than five percent (5%) and not more than fifteen percent (15%), of the total number of shares, certificates, debentures or other assets to be distributed under the Plan shall be granted in equal portions, without consideration, to eligible Alaskans who apply to receive said assets;

§AA.BB.320 FIRST RESTRICTED SALE. (a) All shares, certificates, debentures, or other assets authorized to be distributed to individual Alaskans under each Plan, other than those distributed as a grant without consideration under AS AA.BB.310, shall be offered for sale to eligible Alaskans in a first restricted sale.

(b) In the first restricted sale under each Plan, each eligible Alaskan shall have the right to subscribe for any number of units of the assets to be distributed, by depositing with his or her subscription application and evidence of eligibility, a deposit in the form of —

- (1) cash, check, or money order,
- (2) an assignment of any unpaid Alaska personal income tax credit or refund for the past, current, or next tax year, or
- (3) a combination of the above

— in a total amount equal to ten percent (10%) of the basic purchase price of the assets subscribed for.

(c) The applicant shall indicate on his or her subscription application whether he or she wishes to purchase the assets (1) for cash, or (2), on an extended purchase plan as provided in subsection (f) of this section.

(d) If the first restricted sale is oversubscribed (that is, if the total number of units of the assets subscribed for exceeds the number of units available for sale), each eligible applicant shall have the right to complete the purchase of the lesser of —

- (1) the number of units subscribed for, and
- (2) the number of units which, if established as the maximum number of units that any one eligible applicant may purchase, would result in the sale of all the units authorized for sale.

(e) The Commissioner shall notify each subscriber who elects to purchase for cash as provided in subsection (c) of this section of the total number of units of shares, certificates, debentures, or other assets he or she is entitled to purchase in the first restricted sale, and of the cash balance required, after crediting his or her deposit, to complete the purchase of those units:

(1) On receipt of cash, check, or money order equal to the balance owing, the Commissioner shall, subject to the limitation in AS AA.BB.340, convey to such subscriber the shares, certificates, debentures, or other assets so purchased; but

(2) If the subscriber fails to complete the purchase as provided in paragraph (1) of this subsection within sixty days, the Commissioner shall convey to such subscriber, subject to the limitation in AS AA.BB.340, the largest number of whole units whose basic purchase price does not exceed the amount of the subscriber's deposit, and refund any balance remaining from the subscriber's deposit.

(f) The Commissioner shall notify each subscriber who elects to purchase on an extended payment plan as provided in subsection (c) of this section of the total number of units of shares, certificates, debentures, or other assets he or she is entitled to purchase in the first restricted sale, and convey to such subscriber:

(1) The largest number of whole units that does not exceed one-tenth of the total number of units the subscriber is entitled to purchase;

(2) A refund of the difference, if any, between the subscriber's deposit and the basic purchase price for the number of units conveyed under paragraph (1) of this subsection; and

(3) Stock-purchase warrants described in AS AA.BB.335, for the balance of the total number of units the subscriber is entitled to purchase.

§AA.BB.325. SECOND RESTRICTED SALE. (a) If the first restricted sale of shares, certificates, debentures, or other assets under any Plan is undersubscribed (that is, if the total number of units available for sale exceeds the number of units subscribed for in the first restricted sale), and if the Plan authorizes a second restricted sale in such an event, the Commissioner shall conduct such a sale under this section.

(b) In the second restricted sale under any Plan, each eligible Alaskan may submit one or more sealed bid(s) each of which shall specify the number of units the bidder wishes to purchase at a bid price specified by the him or her (which price must be equal to or exceed a minimum bid price specified by the Commissioner, but which may otherwise be less than, equal to, or more than the basic purchase price).

(c) The sealed bids described in subsection (b) of this section must be accompanied by evidence of the bidder's eligibility, and a deposit in the form of —

- (1) cash, check, or money order,
- (2) an assignment of any unpaid Alaska personal income tax credit or refund for the past, current, or following tax year (not already encumbered in the first restricted sale), or

(3) a combination of the above
— in a total amount equal to ten percent (10%) of the bid price for the number of units subscribed for.

(d) The Commissioner shall tally the bids in descending order of bid price, until (1) the total number of units bid for equals the number of units to be sold, or (2) all bids at or above the minimum bid price have been tallied, whichever occurs sooner; and the Commissioner shall award to each bidder whose bid has been included in this tally, sale of the number of units for which he or she bid, at an actual sales price equal to his or her bid price for those units [ALTERNATE PROVISION: to the bid price for lowest bid so tallied], until (1) all such bids have been satisfied, or (2) all units have been sold, whichever occurs sooner.

(e) If the number of units for which valid bids are received at a bid price equal to or greater than the actual sales price as described in subsection (d) of this section, exceeds the number of units available for sale, the Commissioner shall award sale of the number of units bid for to each such bidder whose bid price exceeded the actual sales price, and shall award sale of the remaining units to those bidders whose bid price was exactly equal to the actual sales price, in proportion to the number of units for which they bid at that price.

(f) All sales of shares, debentures, or other securities in any second unrestricted sale shall be cash sales; the Commissioner shall notify each successful bidder of the total number of units he or she is entitled to purchase in the second restricted sale, and of the cash balance required, after crediting his or her deposit, to complete the purchase of those units:

(1) On receipt of cash, check, or money order equal to the balance owing, the Commissioner shall, subject to the limitation in AS AA.BB.340, convey to such bidder the shares, debentures, or other assets so purchased; but

(2) If the bidder fails to complete the purchase as provided in paragraph (1) of this subsection within sixty days, the Commissioner shall convey to such bidder, subject to the limitation in AS AA.BB.340, the largest number of whole units for which the actual sales price does not exceed the amount of the subscriber's deposit, and refund any balance remaining from the subscriber's deposit.

§AA.BB.330. UNRESTRICTED SALE. Except as expressly provided in this Act or the terms of a Plan, or otherwise prohibited by law, the Commissioner is authorized to hold as investments or to sell for maximum revenue, or otherwise for the the benefit of the State, any shares, certificates, debentures, or other assets authorized to be distributed under a Plan, but which (1) remain undistributed after completion of the free distribution, the first restricted sale, and (where required) the second restricted sale, and (2) are not reserved for sale according the terms of a stock-purchase warrant.

§AA.BB.335. STOCK-PURCHASE WARRANTS. (a) Stock-purchase warrants distributed under AS AA.BB.320(f) shall grant an eligible holder the right to purchase, over a period of nine years from their date of issue, the number of shares, certificates, debentures, or other assets that equals nine-tenths (90.%) of the total number of units which the holder was entitled to purchase in a first restricted sale under this chapter, on the following schedule:

(1) The largest number of whole units that does not exceed one-ninth of the total number of units that the holder is entitled to purchase after receipt of the units distributed under AS AA.BB.320(f) (1), not later than one year after the issue date;

(2) The largest number of whole units that does not exceed one-eighth of the units that the holder is entitled to purchase after receipt of the units distributed under AS AA.BB.320(f)(1), less the number of units he was entitled to purchase under paragraph (1) of this subsection, not later than two years after the issue date;

(3) The largest number of whole units that does not exceed one-seventh of the units that the holder is entitled to purchase after receipt of the units distributed under AS AA.BB.320(f)(1), less the number of units he was entitled to purchase under paragraphs (1) and (2) of this subsection, not later than three years after the issue date;

(4) The largest number of whole units that does not exceed one-sixth of the units that the holder was entitled to purchase after receipt of the units distributed under AS AA.BB.320(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (3) of this subsection, not later than six years after the issue date;

(5) The largest number of whole units that does not exceed one-fifth of the units that the holder was entitled to purchase after receipt of the units distributed under AS AA.BB.320(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (4) of this subsection, not later than seven years after the issue date;

(6) The largest number of whole units that does not exceed one-fourth of the units that the holder was entitled to purchase after receipt of the units distributed under AS AA.BB.320(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (5) of this subsection, not later than six years after the issue date;

(7) The largest number of whole units that does not exceed one-third of the units that the holder was entitled to purchase after receipt of the units distributed under AS AA.BB.320(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (6) of this subsection, not later than seven years after the issue date;

(8) The largest number of whole units that does not exceed one-half of the units that the holder was entitled to purchase after receipt of the units distributed under AS AA.BB.320(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (7) of this subsection, not later than eight years after the issue date;

(9) The largest number of whole units that does not exceed the number of units that the holder was entitled to purchase after receipt of the units distributed under AS AA.BB.320(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (8) of this subsection, not later than nine years after the issue date;

(b) The actual purchase price for any asset purchased by exercising a stock-purchase warrant under this section shall be ---

(1) the basic purchase price of the asset, plus

(2) a carrying charge, calculated as interest on the basic purchase price, compounded from the stock-purchase warrant's date of issue to the date of actual purchase of the asset, at the weighted average cost of borrowing to the State of Alaska during the fiscal year previous to the date of issue, less

(3) any dividends, interest, royalties, or profits received by the State from holding the asset between the stock-purchase warrant's date of issue and the date of actual purchase. Provided, however, that the actual purchase price shall in no case be less than one-half the basic purchase price.

(c) Payment for shares, certificates, debentures, or other assets purchased by exercising a stock-purchase warrant under this chapter may be by ---

(1) cash, check, or money order,

(2) an assignment of any unpaid Alaska personal income tax credit or refund, from the past, current, or following tax year, or

(3) a combination of the above.

(d) All stock-purchase warrants distributed under AS AA.BB. 320(f) shall be non-transferable, except by inheritance, and no purchase right granted by such a warrant shall be exercised except by a natural person who is a resident of Alaska at the time said purchase right is exercised.

§AA.BB.340. USE OF INCOME TAX CREDITS. (a) The Commissioner shall not convey to a purchaser any share, certificate, debenture, or other asset to be distributed under this Program, and purchased under AS AA.BB.320(b), 325(c), or 335(c) in whole or in part by means of an assignment of an Alaska personal income-tax credit or refund for any year, until the purchaser's individual income tax return for that year has been filed and processed by the Department of Revenue, and the Commissioner has determined that the purchaser in fact appears to be entitled to a personal income tax credit or refund sufficient to satisfy the balance owing for his or her purchase of the shares, certificates, debentures, or other assets, or until that balance has been otherwise paid as provided in subsection (b) of this section.

(b) If after the purchaser has filed, and the Department has processed, the purchaser's Alaska personal income tax return as provided in subsection (a) of this section, the Commissioner determines that the purchaser does not appear to be entitled to a personal income tax credit or refund sufficient to pay the balance owing for his or her purchase, the Commissioner shall notify the purchaser of the balance owing after crediting any refund or credit to which the purchaser may be entitled:

(1) On receipt of cash, check, or money order equal to the balance owing, the Commissioner shall convey to the purchaser all shares, certificates, debentures, or other assets so purchased; but

(2) If the bidder fails to complete the purchase as provided in paragraph (1) of this subsection within sixty days, the Commissioner shall convey to such purchaser the largest number of whole units for which the actual sales price does not exceed the sum of (a) any applicable cash payment and (b) any tax refund or credit which in the judgment of the Commissioner may properly be applied to the purchase, and the Commissioner shall refund, or credit to the purchaser's Alaska personal tax payments, any balance that remains owing to the purchaser.

§ AA.BB.115. ALASKA CITIZENS WEALTH DISTRIBUTION PLANS. (a) An Alaska Citizens Wealth Distribution Plan (hereinafter a Plan) is a plan under which the Commissioner of Revenue (hereinafter the Commissioner)

(1) contributes, transfers, commits, or dedicates to the Program securities, rights to resource revenues, or other assets, either already owned by the State or acquired expressly for the Program; and

(2) distributes those assets to individual Alaskans by grant and/or sale under the terms of this Act.

(b) Each Plan shall provide for the distribution of assets to individual Alaskans in the form of shares, certificates, debentures, warrants, options, or other securities or instruments that establish their ownership, right, or interest in one (and only one) of the following:

(1) An Alaska Energy Resource Trust, as provided in CHAPTER 2 of this Act.

(2) An Alaska Industrial Development Project, as provided in CHAPTER 3 of this Act.

(3) An Alaska General Stock Ownership Corporation, as provided in CHAPTER 4 of this Act.

(4) An Alaska Investment Fund, as provided in CHAPTER 5 of this Act.

(5) An Alaska Real Estate Trust, as provided in CHAPTER 6 of this Act.

(6) Shares in one or more existing private enterprises doing business in Alaska, as provided in CHAPTER 7 of this Act.

(c) Each Plan shall provide for a single distribution of such shares, certificates, debentures, warrants, options, or other securities or instruments, only to persons who were residents of Alaska as of an eligibility date to be specified in the Plan.

(c) In the event a disagreement exists between any purchaser and the Commissioner regarding the purchaser's entitlement to apply Alaska personal income tax refunds or credits to the purchase of shares, certificates, debentures, or other assets under this section, the determination of the Commissioner shall, if not amended by him, become final sixty days after the notice provided for in subsection (b) of this section (or if amended by him, sixty days after his notice to the purchaser of such amendment). (That is, the purchaser's only recourse in case the Commissioner is in error, and does not correct the error within sixty days, is to pay off the balance owing on the purchase of assets under the Program, and to pursue whatever administrative or legal remedies may otherwise be available, in order to obtain a cash refund or tax credit; the purchaser's remedies do not include any right to compel the Commissioner to complete the sale of any shares, certificates, debentures, or other assets to which the disputed sum would have been applied.)

(d) The provisions of subsection (c) of this section shall not in any way alter any person's Alaska personal income tax liability, entitlement to any tax refund or credit, or any recourse or remedy he or she may have in respect to any disagreement with the State of Alaska regarding such liability or entitlement.

§AA.BB.350. DISPOSITION OF PROCEEDS. The Commissioner shall deposit all net proceeds from the sale of shares, certificates, debentures, or other assets under this Program into the Permanent Fund.

ARTICLE 4. OWNERSHIP RIGHTS

§AA.BB.410. TRANSFER OF ASSETS. Except as expressly provided (with respect to non-transferable stock-purchase warrants in AS AA.BB. 210(b) and (c), and 335(d); the certificates of an Alaska Energy Resource Trust in AS AA.BC.140); and shares in an Alaska General Stock Ownership Corporation in AS AA.BE.140, nothing in this Act shall restrict the right of a recipient or holder of any shares, certificates, debentures, or other assets distributed under the Program to sell, transfer, devise, bequeath, pledge, hypothecate, or otherwise dispose of any such asset, or interest in or earnings from that asset.

§AA.BB.415. VOTING RIGHTS. (a) The voting rights attached to ownership any security distributed under this Program shall be conveyed unrestricted to the individual Alaskans receiving that security, and the Commissioner shall not reserve, or require as a condition of distribution of any such security that the recipient waive any such right, grant any proxy, or adhere to any voting trust, unless the security were subject to such a stipulation or covenant at the time it was acquired by the State.

(b) Subsection (a) of this section shall not be interpreted to prohibit the Commissioner from exercising any voting rights attached to any security owned, held in trust, or reserved by the State for future distribution under the Program, or from issuing or distributing convertible debentures or non-voting securities under the terms of a Plan.

ARTICLE 5. TAX TREATMENT

§AA.BB.510. RECEIPT OF ASSETS NOT TAXABLE. The receipt by an eligible individual of shares, certificates, debentures, warrants, options, or other securities or instruments distributed by the State of Alaska under the Program, whether by grant or purchase, shall not be considered as taxable income or capital gains for purposes of the Alaska individual income tax.

§AA.BB.515. CREDIT FOR FEDERAL TAXES PAID. (a) If the receipt by any eligible individual of shares, certificates, debentures, warrants, options, or other securities or instruments distributed by the State of Alaska under the Program, whether by grant or purchase, should be treated as taxable income or capital gains under the United States federal income tax, and that individual is thereby required to pay an additional federal income tax, the amount of such additional tax shall be creditable against the individual's Alaska individual income tax for the tax year in which the additional federal income tax is paid.

(b) The Alaska personal income tax credit provided by subsection (a) of this section shall not be limited to the taxpayer's Alaska individual income tax liability absent the credit, but shall be creditable in the tax year in which it occurs even if its net effect is a "negative tax" to be paid to the individual by the State, for that tax year.

(c) Any Alaska personal income tax credit taken to offset an additional federal income tax payment that is subsequently refunded or credited to the taxpayer, shall be treated for purposes of the Alaska personal income tax as a negative tax credit in the tax year in which the refund or credit is taken.

§AA.BB.520. INCOME NOT TAX-EXEMPT. Nothing in this article shall be construed to exempt from state or federal taxes any dividends, interest, profits, or other income received from the shares, debentures or other assets distributed under the Program, or the proceeds from their sale.

ARTICLE 6. SECURITIES MARKETS

§AA.BB.610. INTENT. It is the intent of this Act that the shares, certificates, debentures, or other assets distributed to Alaskans under the Program have a market value that is readily ascertainable, and that the people of Alaska be able to buy or sell such assets readily and without unnecessary or unreasonable transactions costs. |

§AA.BB.620 AUTHORITY OF COMMISSIONER TO MAKE MARKET. (a) If the Commissioner finds that an efficient public market does not exist for any issue of shares, certificates, debentures, or other assets distributed under the Program, he is authorized to buy, sell, and trade in such securities for the purpose of establishing such a market, and to publish regularly the "bid" and "ask" prices for those securities.

(b) If the Commissioner makes a market in any asset as authorized in subsection (a) of this section, he shall maintain an average markup (or spread between bid and ask prices) just sufficient, in his judgment, to compensate the State for the administrative costs of his trading activity.

ARTICLE 6. MISCELLANEOUS PROVISIONS

TO BE DRAFTED:

§AA.BB.700. DEFINITIONS. Defines terms used in this Act.

§AA.BB.710 PENALTIES. Provides criminal penalties and forfeiture of distributed assets, whether granted or purchased, for fraudulently claiming residence and for making false statements for the purpose of receiving benefits under the program.

§AA.BB.720. SAVINGS CLAUSES. Include provisions that preserve the intent and body of the Program if specific provisions are found unconstitutional: e.g., if definition of residency, or standards for determining residency, are invalidated, allows Commissioner to proceed on strictest definition of residency allowed by courts; if free grants of securities are prohibited, allows sale of assets, etc.

CHAPTER 2 ALASKA ENERGY RESOURCE TRUSTS.

§AA.BC.110. ALASKA ENERGY RESOURCE TRUST DEFINED. An Alaska Energy Resource Trust is a trust established by the Commissioner under authority of an Act of the Legislature under AS AA.BB.120, as part of the Alaska Citizens Wealth Ownership Program; its assets are a right or interest in, or a right to receive income equal to a specified portion of, the lease rentals, royalties, net profit shares, and/or mineral sale revenues from the production of oil and gas, coal, oil shale, tar sands, or uranium, from specified areas, tracts, or leases of state onshore or submerged lands.

§AA.BC.120. DISTRIBUTION OF CERTIFICATES (a) The certificates of any Alaska Energy Resource Trust established under this Act shall be distributed to eligible Alaskans according to the provisions of AS AA.BB.315-325, and the basic purchase price for such certificates shall be determined as provided in AS AA.BB.310(a)(2) and 310(b).

(b) There shall be no unrestricted sale of the certificates of any Alaska Energy Resource Trust; and the Commissioner shall hold as an investment for the State any certificates that (1) remain undistributed after completion of the free distribution, the first restricted sale, and (where required) the second restricted sale, and (2) are not reserved for sale according the terms of a stock-purchase warrant, including those certificates that were previously so reserved, but for which the outstanding warrants have expired or been cancelled or invalidated.

§AA.BC.140. OWNERSHIP AND TRANSFERABILITY. (a) An individual who has received certificates of an Alaska Energy Resources Trust in a distribution under this Act shall not be required to return, sell, or otherwise relinquish those certificates as a result of ceasing to be a resident, but no certificates of such a Trust may be sold, given, assigned, transferred, or otherwise conveyed, except by inheritance, to any person who is not a resident of Alaska as defined in AS AA.BB.215; and the trustee may cancel any certificates sold, given, assigned, transferred, or otherwise conveyed, except by inheritance, to other than a resident, and provide compensation for such shares at no more than the basic purchase price.

(b) No person or affiliated group may obtain or hold, by grant or purchase, whether from the State or otherwise, or by any other means, title to or a beneficial interest in, more than one-twentieth (5%) of the total authorized, issued, or outstanding certificates (whichever is the least) of any Alaska Energy Resource Trust authorized, issued, or outstanding (whichever is the least), and the trustee of such a Trust may not distributed to any person or affiliated group, and such person or group may not receive, any dividends, royalties, profits, or other payments from the income of such a Trust in excess of those attributable to one-twentieth (5%) of the total shares.

CHAPTER 3 ALASKA INDUSTRIAL DEVELOPMENT PROJECTS

§AA.BC.110. ALASKA INDUSTRIAL DEVELOPMENT PROJECT DEFINED. An Alaska Industrial Development Project (hereinafer a Project) is a nominally private enterprise engaged or intending to engage in the business of natural resource extraction or processing, or manufacturing, transportation, or communications, wholly or partly in the state of Alaska, and to which the State of Alaska or an agency or subdivision of the State, contributes capital or assists in financing, thorough an investment of equity or debt capital in the form of money or rights in land or natural resources, or by loan guarantees, with a value exceeding \$100 million.

§AA.BC.120. INTENT. It is the intent of this Act that, whenever the State of Alaska participates in the financing of large-scale basic industrial enterprise in or of major importance to the state, whenever and to the extent feasible —

(1) the State's direct participation be temporary and limited to the promotional, organizational, design and construction phases (or, in the case of natural resource extractive enterprises, to the promotional, organizational, exploration, and development phases);

(2) any state ownership and management role in such enterprises be relinquished to private persons once those enterprises become established and viable; and

(3) ownership and management roles relinquished by the state in such enterprises be transferred to resident Alaskans through the Program established by this Act.

§AA.BC.130. ALASKA NATURAL GAS TRANSPORTATION SYSTEM. If the Commissioner, under his existing authority, should invest any funds of State of Alaska in equity or convertible debentures of the Alaska Natural Gas Transportation System (also known as the Alaska Highway Gas Pipeline; hereinafter ANGTS), or a portion thereof, or in a natural gas conditioning plant associated with ANGTS, or if the Governor or any official of the Executive Branch of the State should submit to the Legislature any proposal for State participation in the financing of ANGTS, or a portion thereof, or of a natural gas conditioning plant associated with ANGTS, by contribution of equity or purchase of convertible debentures, the Commissioner shall, within 30 legislative days, submit a Plan for eventual distribution of the State's ownership interest to individual Alaskans through the Program established by this Act.

CHAPTER 4 ALASKA GENERAL STOCK OWNERSHIP CORPORATIONS

ARTICLE 1. GENERAL PROVISIONS

§AA.BE.110. ALASKA GENERAL STOCK OWNERSHIP CORPORATION DEFINED. An Alaska General Stock Ownership Corporation (hereinafter an AGSOC) is a corporation formed in accordance with subchapter U, chapter 1 of the Internal Revenue Code of 1954, as amended (26 U.S.C. 1391-1397) and this chapter.

TO BE DRAFTED: An adaptation of HB 240 as reported by the House State Affairs Committee, to make it permissive rather than mandatory.

CHAPTER 5 ALASKA INVESTMENT FUNDS

§AA.BF.110. ALASKA INVESTMENT FUND DEFINED. An Alaska Investment Fund (hereinafter a Fund) is a regulated investment company (also known as a mutual fund) organized or caused to be organized by the Commissioner in accordance with subchapter M, chapter 1 of the Internal Revenue Code of 1954, as amended (26 U.S.C. 851-855) and this chapter. !

TO BE DRAFTED: an Alaska Regulated Investment Company Act (adaptation of the Maryland statute) or direction to the Commissioner of Commerce to submit a draft of such an Act; authorization for an Alaska Investment Fund organized under the program to issue more than one class of shares, and for the Commissioner to invest General Fund or Permanent Fund balances in the preferred shares in order to leverage the income of the shares distributed to citizens under the Program.

CHAPTER 6. ALASKA REAL ESTATE TRUSTS

§AA.BG.110. ALASKA REAL ESTATE TRUST DEFINED. An Alaska Real Estate Trust (hereinafter a ARET) is a real estate investment trust (REIT) organized or caused to be organized by the Commissioner in accordance with subchapter M, chapter 1 of the Internal Revenue Code of 1954, as amended (26 U.S.C. 856-858) and this chapter.

TO BE DRAFTED: authorization for an Alaska Real Estate Trust organized under the Program to issue more than one class of shares, and for the Commissioner to invest General Fund or Permanent Fund balances in the preferred shares in order to leverage the income of the shares distributed to citizens under the Program.

CHAPTER 7. EXISTING PRIVATE ENTERPRISES

§AA.BH.110. EXISTING PRIVATE ENTERPRISE DEFINED. For the purposes of this Act, an existing private enterprise is an existing private corporation engages in or intending to engage in natural resource extraction or processing; manufacturing, transportation, communications, trade, or services in Alaska, whose securities the Commissioner has purchased under his existing authority, or proposes to purchase under the terms of a Plan, for distribution through this Program.

CHAPTER 8. PRUDHOE BAY OIL AND GAS ROYALTY TRUST PLAN OF 1980

§AA.YY.110 CREATION OF TRUST. The Commissioner shall create by trust indenture an Alaska Energy Resource Trust in accordance with the provisions of this Chapter and other provisions of this Act, to be known as the Prudhoe Bay Oil and Gas Royalty Trust of 1980, and its trustee may transact affairs in that name.

§AA.YY.120. TRUST INDENTURE. (a) The Commissioner shall prepare a trust indenture and execute it on behalf of the State. The trustee shall also execute the trust indenture as trustee for the trust, and register the trust in accordance with AS 13.36.

(b) The trust indenture shall include:

- (1) the name and purpose of the trust;
- (2) powers and duties of the trustee;
- (3) the nature and rights of the beneficial shares and certificates;
- (4) accounting and distribution methods and procedures;
- (5) liability of trustee and method of succession;
- (6) meetings and rights of certificate holders;
- (7) duration, revocation, and termination of the trust;
- (8) limitations on the powers and rights of the trustee and the certificate holders; and
- (9) such other matters as the Commissioner considers necessary, not inconsistent with this Chapter.

§AA.YY.130. AMENDMENTS TO TRUST INDENTURE. (a) Amendments may be made to the trust indenture by a vote of the certificate holders present and represented at a meeting held in accordance with Article 6 of this Chapter, except that no amendment shall be effective without the express written approval of the trustee.

(b) An amendment may not be made to the trust indenture that would increase the power of the trustee to engage in business or investment activities or alter the rights of the certificate holders in relation to one another.

§AA.YY.140. PURPOSE. The purpose of the trust is to provide an efficient and practical means of permitting each certificate holder to receive his or her pro rata share of the proceeds attributable to the royalties conveyed to the trust. This purpose is realized by retaining and collecting the cash proceeds of royalties until production has ceased or the royalties have otherwise terminated; and to distribute that cash, net of expenses and liabilities of the trust, to the holders pro rata.

§AA.YY.150. THE TRUST ESTATE. The assets of the trust shall consist of the royalties conveyed to the trust under section 050 of this Chapter.

§AA.YY.155. CONVEYANCE OF ROYALTIES. (a) The Commissioner shall convey by deed to the trust, all royalties exceeding the average daily royalties accrued during the first three calendar months of 1980, from the State's reserved royalty interest in the following leases:

[INSERT PROPERTY DESCRIPTION]

(b) The deed shall indicate that the conveyance is only of a specified portion of the State's royalty interest and not the entire mineral interest, which shall be retained by the State. The conveyance of the royalty interest shall be for so long as there is production in paying quantities from the leases or properties specified in subsection (a) of this section. Five years after production in paying quantities has ceased, the royalty interest shall revert to the State.

(c) The conveyance to the trust shall be subject to the prior obligations of the State to make payments from the royalty interest to the Alaska Permanent Fund under Article IX, Section 11 of the Alaska Constitution, the Alaska Renewable Resources Development Fund under _____, and the Alaska Native Fund under _____. The conveyance shall also be subject to the rights and obligations of the lessor and lessee of the leases in properties described in subsection (a) of this section, including --

(1) the authority of the Commissioner of Natural Resources to reduce royalties as authorized by AS 38.05.180(j);

(2) the authority of the Commissioner of Natural Resources to enter into storage or exchange agreements concerning royalties under AS 38.05.180(1);

(3) the authority of the Commissioner of Natural Resources to elect to take royalty in kind or in value under AS 38.05.182; and

(4) any future sales, exchanges, or other disposal or encumbrance that the Commissioner of Natural Resources is presently authorized by law or may be authorized by law in the future to make or place upon the royalty interest.

(d) For the purposes of this section, the net proceeds to the State from any sale of royalty oil and gas taken in kind from the leases specified in subsection (a) of this section, or of oil and gas or other property exchanged for royalties from those leases, or from any other disposal under clauses (2) through (4) of subsection (c) of this section, shall be regarded as royalty subject to conveyance.

(e) The conveyance shall not constitute a sale, exchange or disposal of a mineral for purposes of AS 38.05.183 or AS 38.06, and none of the requirements of these sections need be satisfied as a condition of the conveyance.

§AA.YY.160. RULE AGAINST PERPETUITIES. The conveyance of royalties to the trust, or the transfer of beneficial interests in the trust, or the duration of the trust itself shall not be considered as violating the so-called rule against perpetuities, or any law restricting or limiting the duration of trusts; and the trust to be created under this Chapter may continue for such time as may be necessary to accomplish the purposes for which it was created.

ARTICLE 2. TRUSTEE

§AA.YY.210. SELECTION OF TRUSTEE AND SUCCESSOR TRUSTEES. (a) The Commissioner shall select as a trustee for the Trust a bank or trust company licensed under AS 09, which has its principal offices in the state; has capital, surplus, and undivided profits of at least \$_____ ; and accepts the powers and duties of the trustee under this Chapter.

(b) In the event of a vacancy in the office of trustee or if a trustee has given notice of its intention to resign, the certificate holders present or represented at a meeting in accordance with Article 6 of this Chapter may appoint a successor trustee.

(c) If a vacancy in the position of trustee continues for 60 days, a successor may be appointed by the court, in accordance with its powers under AS 13.36.035, upon the application of any certificate holder. The court may appoint a temporary trustee at any time after the application is filed with it and, pending the final appointment of a trustee, the temporary trustee shall have the powers and duties as the court appointing the temporary trustee shall provide in its order of appointment, consistent with the provisions of this Chapter and the trust indenture registered in accordance with it.

(d) Immediately upon the appointment of any successor trustee, all rights, titles, duties, powers and authority of the succeeding trustee shall be vested in and undertaken by the successor trustee and shall be entitled to receive from the trustee which it succeeds all of the Trust Estate held by it and all records and files in connection with it.

§AA.YY.220. POWERS AND DUTIES OF TRUSTEE. The trustee shall have the duties of preserving the Trust Estate, the collection of the income from the Trust Estate, the payment of expenses, and the distributions of the net proceeds of the Trust Estate to the certificate holders. The powers of the trustee shall not extend beyond those necessary and incidental to carrying out of these duties and shall be restricted to:

(1) the power to manage, conserve and protect the royalties that it would have if it were the absolute owner of the royalties, including the power to agree to any modification of the royalties, or to settle any dispute with respect to the royalties;

(2) the power to sell any part of the royalties for cash as it considers in the best interests of the certificate holders, but only after approval by all certificate holders under Article 6 of this Chapter;

(3) the power to accumulate cash temporarily as a reserve for liabilities or for distribution at the next distribution date and to invest those reserves in accordance with section _____ of this Chapter;

(4) the power to prosecute or defend, and to settle by arbitration or otherwise any claim of or against the trust, to waive or release rights of any kind and to pay or satisfy any debt, tax or claim upon evidence considered sufficient;

(5) the power to employ oil and gas consultants, accountants, attorneys and other professional and expert persons and to employ or contract for clerical and other administrative assistance and to make payments of all fees for services or expenses in any manner thus incurred out of the Trust; and

(6) the power to use all money received by it in the payment of all liabilities and obligations incurred by it in connection with the trust including all expenses, taxes, liabilities incurred of all kinds, compensation to it for its services hereunder, and compensation to parties employed by it.

§AA.YY.230. NO POWER TO ENGAGE IN BUSINESS OR MAKE INVESTMENTS. The trustee shall not, in its capacity as trustee under the trust acquire any oil and gas lease, mineral interest, or royalty other than the royalties conveyed under Section 155 of this Chapter or, except as provided in _____, acquire any other asset or engage in any business or investment activity of any kind. --

§AA.YY.240. LIABILITY OF TRUSTEE. The trustee's standard of care and liability shall be determined in accordance with the provisions of AS 13.36.

§AA.YY.250. COMPENSATION OF TRUSTEE. The trustee's compensation for its services shall be determined initially by the commissioner. The compensation of the trustee may be changed by a vote of the certificate holders in accordance with _____.

§AA.YY.260. INVESTMENT OF CASH RESERVES. (a) The trustee shall invest temporary cash reserves established under _____ of this Chapter in:

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

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

(3) certificates of deposit issued by the United States domestic banks which are members of the Federal Deposit Insurance Corporation and secured as to the payment of principal and interest in accordance with Alaska law.

§AA.YY.270. PAYMENT OF LIABILITIES. (a) The trustee may use all money received by it in the payment of all liabilities of the trust,

including but not limited to, all expenses, taxes, liabilities incurred of all kinds, compensation to it for its services, compensation to persons employed by it. If any liability is contingent or uncertain in amount or is not currently due and payable, the trustee may establish a temporary cash reserve for its payment. The trustee shall not pay any liability of the trust with funds set aside under _____ for the payment of a monthly distribution amount unless there are no other available funds in the Trust Estate and the trustee is satisfied that on the distribution date there will be sufficient funds to pay the monthly distribution amount. If the funds set aside under _____ are used, the amount used shall be treated as a liability of the trust and shall bear interest at the rate of funds invested under _____.

(b) If at any time the cash on hand and to be received by the trustee is not, or will not, in the judgment of the trustee, be sufficient to pay liability of the trust as they become due, the trustee is authorized to borrow the funds required to pay those liabilities. If the trustee borrows funds under this subsection, no further distributions will be made to the certificate holders except previously determined monthly distribution amounts, until the indebtedness created by the borrowings has been paid in full. To secure payment of the indebtedness, the trustee is authorized to mortgage, pledge, grant security interest in or otherwise encumber and to include any and all items, remedies, covenants, and provisions considered necessary including without limitation the power of sale with or without judicial proceedings the Trust Estate, or any portion of the Trust Estate including all or any part of the royalties, and to carve out and convey production payments.

§AA.YY.280. RESIGNATION AND TERMINATION OF TRUSTEE. (a) The trustee may resign, with or without cause, at any time by written notice to each of the then certificate holders, given by registered mail addressed to those certificate holders at his or her last known post office address as shown by the records of the trustee at the time

the notice is given. The notice shall specify a date when the resignation shall take effect, but shall not be a date less than 60 days after the notice is mailed.

(b) The trustee may be removed by the affirmative vote of the certificate holders present or represented at a meeting held in accordance with the requirements of _____.

ARTICLE 3. TERMINATION OF TRUST AND LIQUIDATION

§AA.YY.310. DURATION, REVOCATION, AND TERMINATION OF TRUST. (a) The trust shall be irrevocable. The trust shall be terminable only as provided in this Section and shall continue until so terminated.

(b) The Trust shall terminate upon the first to occur of the following events or times:

(1) At the time as its net revenues for each of two successive years are less than \$_____.

(2) A cessation for five years of production from the properties for which the royalties are due.

(3) A vote in favor of termination by the certificate holders present or represented at a meeting held in accordance with _____

§AA.YY.320. LIQUIDATION. Upon termination of the Trust, the trustee shall proceed to liquidate and wind up the affairs of the trust. For the purpose of liquidating and winding up the affairs of the Trust at its termination, the trustee shall continue to act and exercise each power until its duties have been fully performed and the Trust Estate has been finally distributed. Upon the termination of the Trust, the trustee shall sell for cash in one or more sales all the properties other than cash then constituting the Trust Estate. The trustee shall, as promptly as possible, distribute the proceeds of any such sales and any other cash in the Trust Estate according to the respective interests and rights of the certificate holders, after paying, satisfying and discharging all of the liabilities of the Trust; or, when necessary,

setting up reserves in amounts as trustee in its discretion considers appropriate for contingent liabilities. If any property which the trustee is required to sell is not sold by the trustee within _____ years after the termination of the Trust, the trustee shall sell the property at public auction to the highest cash bidder. Notice of the sale by auction shall be mailed at least thirty days prior to the sale to each certificate holder at his or her address as it appears upon the books of the trustee. The trustee shall not be required to obtain approval of the certificate holders prior to selling property pursuant to this section. Upon making final distribution to the certificate holders, the trustee shall be under no further liability except as provided in _____.

ARTICLE 4. BENEFICIAL INTERESTS

§AA.YY.410. CREATION OF BENEFICIAL SHARES AND CERTIFICATES. (a) The entire beneficial interest in the Trust shall be divided into _____ units. The ownership of the units shall be evidenced by certificates in substantially the following form.

CERTIFICATE OF BENEFICIAL INTEREST

IN

THE PRUDHOE BAY OIL AND GAS ROYALTY TRUST OF 1980

Created by, Issued under, and subject to the Prudhoe Bay Oil and Gas Royalty Trust Indenture dated as of _____

THIS CERTIFIES THAT _____ is the owner of _____ Units of Beneficial Interest ("Units") in that certain Trust known and designated as the Prushoe Bay Oil and Gas Royalty Trust of 1980, created and established under the terms of the above-referenced Indenture by and between the State of Alaska, as Trustor, and _____, as Trustee, a duplicate original of which Indenture is, for the information of all concerned, held by said Trustee at its office. Said Indenture is hereby

referred to and made a part of this Certificate for all purposes, and the owner of this Certificate by accepting the same consents to, and becomes, bound by, all the terms and provisions of said Indenture and the provision herein. The Units represented by this Certificate are transferable on the books of the Trustee by the holder hereof in person, or by duly authorized attorney, upon surrender of this Certificate, properly endorsed, to the Trustee.

WITNESS the seal of the Trustee and the signature of its duly authorized officer.

DATED _____

_____, Trustee

By _____
Authorized Officer

By _____
Authorized Officer

(b) Initially, the state shall own all of the units. However, the state intends to distribute the units as of a date selected by the commissioner in accordance with _____. Upon that distribution, the trustee shall forthwith issue Certificates to those persons evidencing the number of units distributed to him or her.

§AA.44.420. RIGHTS OF CERTIFICATE HOLDERS. (a) The certificate holders shall own pro rata the beneficial interest in the Trust, and shall be entitled to participate pro rata in the rights and benefits of the certificates holders under this Chapter. A certificate holder, by assignment or otherwise takes and holds the same subject to all the terms and provisions of this Chapter, which shall be binding upon and inure to the benefit of the successors, assigns, legatees, heirs and personal representatives of the certificate holders. By an assignment or transfer of one or more units represented by a certificate, the

assignor shall part with, all of his or her beneficial interest attributable to it, all his rights in, to and under such certificate and all interests rights and benefits under this Trust of a certificate holder which are attributable to such unit or units as against all other certificate holders and the trustee.

(b) The certificates, units, and the rights, benefits and interest evidenced by either or both (including without limiting the foregoing, the entire beneficial interest) are and shall be held and construed to be in all respects intangible personal property, and the certificates and units evidenced by them shall be bequeathed, assigned, disposed of and distributed as intangible personal property.

(c) A certificate holder shall not have any legal or equitable interest in or to any real property interest which is a part of the Trust Estate, including, without limitation the royalties or any part of it, but the sole interest of each certificate holder shall be his or her beneficial interest and the obligation of the trustee to hold, manage and dispose of the Trust Estate and to account for the Trust Estate as provided in this chapter. A certificate holder shall not have the right to call for or demand or secure any partition during the continuance of the trust or during the period of liquidation and winding-up under _____

§AA.YY.430. EXECUTION OF CERTIFICATES. All certificates shall be signed by the trustee or a duly authorized officer of the trustee. Certificates may be signed and sealed on behalf of the trustee by such persons as at the actual date of the signing and sealing of such certificates shall be the proper officer of the trustee, although at the nominal date of such certificates any such person shall not have been such officer of the trustee. Any such signature may be the manual or facsimile signature of such officer and may be affixed, imprinted or otherwise reproduced on the certificate.

§AA.YY.440. REGISTRATION AND TRANSFER OF UNITS. The units may be transferred by the certificate holders in accordance with _____. The

units shall be transferable as against the trustee only on the records of the trustee upon the surrender of certificates and compliance with such reasonable regulations as it may prescribe. No service charge shall be made to the transferor or transferee for any transfer of a unit but the trustee may require payment of a sum sufficient to cover any tax or other governmental charge that may be imposed in relation to the transfer. Until any transfer, the trustee may treat the owner of any certificate as shown by its records as the owner of the units evidenced by them and shall not be charged with notice of any claim or demand respecting such certificate or the interest represented by any other party. A transfer of a unit shall, as to the trustee, transfer to the transferee as of the close of business on the date of transfer all of the right, title and interest of the transferor in and to the beneficial interest. The death of any certificate holder shall not entitle the transferee to an account or valuation for any purpose, but such transferee shall succeed to all rights of the deceased certificate holder under this Chapter upon proper proof of title, satisfactory to the trustee.

§AA.YY.450. DETERMINATION OF OWNERSHIP OF CERTIFICATES. In the event of any disagreement between persons claiming to be transferee of any certificate holder, the trustee shall be entitled at its option to refuse to recognize any such claim so long as such disagreement shall continue. In so refusing, the trustee may elect to make no delivery or other disposition of the interest represented by the certificate involved, or any part of it, or of any sum or sums of money accrued or accruing under it, and, in so doing, the trustee shall not be or become liable to any person for the failure or refusal of the trustee to comply with such conflicting claim and the trustee shall be entitled to continue so to refrain and refuse to so act, until:

(1) the rights of the adverse claimants have been adjudicated by a final judgment of a court assuming and having jurisdiction of the parties and the interest and money involved; or

(2) all differences have been adjusted by valid agreement between said parties and the trustee shall have been notified in writing signed by all of the interested parties.

ARTICLE 5. ACCOUNTING AND DISTRIBUTION

§AA.YY.510. FISCAL YEAR AND ACCOUNTING METHOD. The trustee may adopt any fiscal year and may change its fiscal year from time to time as it elects, and shall maintain its books in accordance with generally accepted accounting principles.

§AA.YY.520. DISTRIBUTIONS. (a) The trustee shall determine the monthly distribution amount for each month and on the monthly record date for such month shall establish a cash reserve equal to such amount. During the months of January, April, July and October of each year, the trustee shall for each of the immediate preceding three months, distribute pro rata the monthly distribution amount for each such month, together with interest earned on each such amount from the monthly record date for such month to the payment date, to the certificate holder on the monthly record date for each such month.

(b) The monthly distribution amount shall be the amount determined by the trustee equal to the excess, if any, of:

(1) the cash received during a calendar month which is attributable to the royalties plus any decrease in any cash reserve established by the trustee for the payment of any liabilities of the trust plus any other cash receipts of the trust during the month other than interest earned on the monthly distribution amount for any other month; or

(2) the liabilities of the trust paid during that month plus the amount of any cash reserve established or increased by the trustee for the payment of any future or contingent liabilities of the trust.

(c) The monthly record date for each shall be the close of business on the last business day of the month.

§AA.YY.530 TAX REPORTING. For tax purposes, the trustee shall file such returns and statements as in its judgment are required to comply with applicable provisions of law and to permit each certificate holder to report correctly his or her share of the income and deductions of the Trust.

§AA.YY.540. REPORTS TO CERTIFICATE HOLDERS. At the end of each calendar quarter, the trustee shall mail to each person who was a certificate holder of record on a monthly record date during that quarter a report which shall show, in reasonable detail, the assets, liabilities, receipts and disbursements of the Trust for the quarter and for each month in the quarter. Within 90 days following the end of each fiscal year, the trustee shall mail to each person who was a certificate holder of record for a date to be selected by the trustee, an annual report containing financial statements audited by a nationally recognized firm of independent public accountants selected by the trustee.

ARTICLE 6. MEETINGS

§AA.YY.610. MEETINGS OF CERTIFICATE HOLDERS. (a) A meeting of the certificate holders may be called at any time and from time to time pursuant to the provisions of this section to transact any matter that the certificate holders may be authorized to transact.

(b) A meeting of the certificate holders may be called by the trustee or by certificate holders owning not less than _____ percent of the units represented by the then outstanding certificates. All meetings shall be held at a time and at a place in Alaska as the notice may designate.

(c) The notice of every meeting of the certificate holders shall be in writing, be signed by the trustee or the certificate holders

calling the meeting, set forth the time and place of the meeting and, in general terms, the matters proposed to be acted upon at the meeting. The notice shall be given in person or by mail not more than 60 days or less than 30 days before the meeting is to be held to all of the certificate holders of record not more than 60 days before the date of such meeting.

(d) If the notice is given to any certificate holder by mail, it shall be directed to him or her at the last address shown on the records of the trustee and shall be considered duly given when so addressed and deposited in the United States mail, postage prepaid. No matter other than that stated in the notice shall be acted upon at any meeting.

§AA.YY.620. VOTING. At a meeting of the certificate holders, the presence in person or by proxy of certificate holders holding a majority of the units outstanding as of the record date for determining the right to receive notice of the meeting, shall constitute a quorum. Any matter shall be considered to have been approved by the certificate holders if it is approved by the vote of a majority in interest of such certificate holders constituting a quorum, although less than a majority of all of the units at the time outstanding. A certificate holder shall be entitled to one vote for each unit owned by him or her and certificate holder may vote in person or by a duly executed written proxy.

§AA.YY.630. CONDUCT OF MEETINGS. The trustee may make reasonable regulations as it may deem advisable for any meeting of the certificate holders, for the appointment of proxies, the appointment and duties of inspectors of votes, the submission and examination of proxies, certificates or other evidence of the right to vote, the preparation and use at the meeting of a list authenticated by or on behalf of the trustee of the certificate holders entitled to vote at the meeting and other matters concerning the conduct of the meeting as it shall consider advisable.

ARTICLE 7. GENERAL PROVISIONS

§AA.YY.710. INSPECTION OF TRUSTEE'S BOOKS. A certificate holder and his or her authorized agents, attorneys, and auditors shall have the right during reasonable business hours to examine, inspect and make audits of the Trust and the records of the trustee in reference to the Trust.

§AA.YY.720. DEFINITIONS. In this chapter, ...

- (1) "beneficial interest" means an equitable interest in the cash of the Trust Estate including without limitation the proceeds from the conversion of the royalties to cash, and in the right to cash from such conversion of royalties, but does not include any legal or equitable title in or to the royalties as any part of the royalties;
- (2) "certificate" means a certificate issued by the trustee evidencing the ownership of one or more units;
- (3) "certificate holder" means the owner of a certificate as reflected on the books of the trustee;
- (4) "commissioner" means the Commissioner of Revenue;
- (5) "conveyance" means the transfer of royalties to the trust by the State;
- (6) "trust" means the trust created by and administered under the terms of this Chapter and the trust indenture;
- (7) "trustee" means the entity serving as trustee of the trust and includes any successor trustee;
- (8) "Trust Estate" means the assets held by trustee under the trust and shall include both income and principal;
- (9) "trust indenture" means the trust indenture originally executed by the Commissioner of Revenue and the trustee under this Chapter, or if amended or supplemented, as so amended or supplemented;
- (10) "royalties" means the royalties conveyed to the trustee pursuant to the conveyance;
- (11) "unit" means an undivided fractional interest in the beneficial interest.

CHAPTER 9. BEAUFORT SEA OIL AND GAS ROYALTY TRUST PLAN OF 1980

§AA.ZZ.110 CREATION OF TRUST. The Commissioner shall create by trust indenture an Alaska Energy Resource Trust in accordance with the provisions of this Chapter and other provisions of this Act, to be known as the Beaufort Sea Oil and Gas Royalty Trust of 1980, and its trustee may transact affairs in that name.

§AA.ZZ.120-150. [SAME AS CORRESPONDING SECTIONS OF CHAPTER 8]

§AA.ZZ.155. CONVEYANCE OF ROYALTIES. (a) The Commissioner shall convey by deed to the trust, 30 percent of the first "\$X" million, 50 percent of any amount exceeding "\$X" million but less than "\$Y" million, and 70 percent of any amount exceeding "\$Y" million in any calendar month, from the State's reserved royalty interest in the following leases:

[INSERT PROPERTY DESCRIPTION]

[INTERVENING LANGUAGE SAME AS CORRESPONDING SECTIONS OF CHAPTER 8]

§AA.ZZ.410. CREATION OF BENEFICIAL SHARES AND CERTIFICATES. (a) The entire beneficial interest in the Trust shall be divided into _____ units. The ownership of the units shall be evidenced by certificates in substantially the following form.

CERTIFICATE OF BENEFICIAL INTEREST
IN
THE BEAUFORT SEA OIL AND GAS ROYALTY TRUST OF 1980

Created by, Issued under, and subject to the Beaufort Sea Oil and Gas Royalty Trust Indenture dated as of _____

THIS CERTIFIES THAT _____ is the owner of _____ Units of Beneficial Interest ("Units") in that certain Trust known and designated as the Beaufort Sea Oil and Gas Royalty Trust of 1980 . . .

[REMAINING LANGUAGE SAME AS CORRESPONDING SECTIONS OF CHAPTER 8]

DRAFT LEGISLATION FOR A
PORTFOLIO OF ALASKA CITIZEN ENTERPRISES
(PACE)

Prepared for the
OFFICE OF THE GOVERNOR
STATE OF ALASKA

By
ARLON R TUSSING & ASSOCIATES, INC.
and
PRESTON, THORGRIMSON, ELLIS & HOLMAN

10 April, 1980

*Check Dole
amendment
on small royalty owners*

loan
portfolio

PORTFOLIO OF ALASKA CITIZEN ENTERPRISES

INTRODUCTION AND EXPLANATION OF FINAL DRAFT

This draft is a synthesis of the plan for an Alaska Citizens Wealth Ownership Program that Arlon R. Tussing submitted to the office of the Governor on March 27, 1980, and the April 10, 1980 redraft of that plan in bill form by Preston, Thorgrimson, Ellis and Holman. The redraft made some unintended substantive changes in the plan: the current version corrects these changes and is intended as a further improvement in the legislative language.

Both the March 27 and April 10 drafts included (1) legislation establishing the general procedures for distributing any of several kinds of assets to Alaska residents, plus (2) plans in bill form for a "Prudhoe Bay Oil and Gas Royalty Trust", and a "Beaufort Sea Oil and Gas Royalty Trust." These plans provided for the one kind of asset distribution that could conceivably be put into effect in 1980 and which would put securities of unquestionable value into the hands of Alaskans (as opposed to some of the more speculative alternatives, such as AGSOC or a share in the gas conditioning plant).

Article 1 sets out the purposes of the portfolio --- these are self-explanatory. It houses the portfolio in the Department of Revenue, and requires the Commissioner to submit at least one and as many as three wealth distribution plans to the legislature each year. Each plan must be accompanied by a financial and legal analysis, and will not go into effect unless enacted as a law.

Article 2 limits benefits of the portfolio to Alaska residents as of an eligibility date specified for that plan. The legislation also sets out the evidence a

person must submit to establish a presumption of residency, and certain actions that establish a presumption of non-residency.

Article 3 spells out the general procedures for distributing securities to eligible residents. A small part (5 to 15 percent) of the securities distributed under each plan will be distributed free, in equal portions to each resident who applies for them. This provision assures that everybody gets something, and serves as advertisement for the program. Most of the assets distributed (85 to 95 percent), however, are to be sold to residents at their nominal value. There are at least three major reasons for selling, rather than giving away, the bulk of the assets:

(a) Sale at value is far more likely to survive constitutional challenge than free distribution. [The legislation will be written so that the sales procedures will survive even if the courts disallow free grants.]

(b) Sale at value is unlikely to create any federal tax liability for the recipient, while the IRS may rule that assets received free of charge are taxable income in the year they are received.

(c) People are likely to place a higher value on things they have to pay for than on free gifts.

There are at least three reasons Alaskans would want to buy assets distributed under the program:

(a) We assumed that some kind of tax credit or refund scheme will be adopted by the 1980 Legislature; Alaska taxpayers will be allowed to apply any tax credit or refund to the purchase of securities under the portfolio. Thus, although they will have to make a real choice (between investments and cash), many and probably most Alaskans will be able to avoid any cash outlay

(b) Most assets distributed under the portfolio will be sold at a "cost" or "conservatively appraised

intended to satisfy constitutional and federal tax requirements, but they can be expected to earn exceptionally high rates of return in relation to that "cost".

(c) Residents will be able to buy the securities on time, over a ten year period at a carrying cost far less than their expected rate of return.

Alaskans who want to buy securities on time will be issued non-transferable warrants --- certificates that allow them to buy a specified number of units each year at a fixed price. While Alaskans who move away will be able to keep the securities they have actually bought, and (with certain important exceptions) to sell them freely, their unused warrants will become invalid.

Article 4 contains a number of general provisions related to the program. Section 160 sets out the rights of securities holders. Except for the non-transferable warrants described above, shares in a natural resource trust (which can be transferred or sold only to other resident Alaskans, except by inheritance), and AGSOC shares (whose ownership is restricted by federal law), the assets distributed under the program will be the unrestricted property of the recipients, and can be disposed of as they wish.

Section 180 states that receipt of securities under the program, whether by grant or by purchase, is not taxable income under Alaska law, but that income from those securities, and proceeds from their resale, will be treated like any other income or capital gains. It also provides that if the IRS rules receipt of these securities to be taxable income under federal law, any additional federal tax the recipient is required to pay may be credited against Alaska income taxes.

Section 200 provides for the Commissioner of Revenue to buy and sell securities distributed under the program in order to create an orderly market for them, if an effective

private market for those securities did not otherwise develop.

Section 230 provides penalties for persons who falsely claim residency or make false statements in order to obtain benefits under the program.

Section 240 defines various terms used in the legislation, including residency.

The kinds of assets that may be distributed under the Program include the following. For distribution of each type of asset, the Commissioner of Revenue would have to present a specific plan to be acted on by the legislature.

Alaska Energy Resource Trusts are royalty trusts --- devices for passing on a portion of the state's oil and gas royalties directly to holders of certificates in the trust. (See the attached clipping from Fortune magazine. [pp ix-x])

Alaska Industrial Development Projects are major new investments, like the gas pipeline or conditioning plant, in which the state might decide to participate financially. Article 6 provides that if the state does make such an investment, the state's ownership and management role should be temporary --- through the development phase only --- and that the state's shares in the project should ultimately be distributed to Alaskans under this program.

Alaska General Stock Ownership Corporations (AGSOCs) are the familiar Kelso-Gravel idea. An article in the proposed legislation (not included here) would incorporate the major provisions of the bill reported by the House State Affairs Committee, but (in contrast to the current initiative) would require the legislature to act upon a complete financing plan before creating any AGSOC.

Alaska Investment Funds are regulated investment companies (mutual funds) empowered to invest in the securities of corporations doing business in Alaska, and Alaska Real Estate Trusts are real estate investment trusts (REITs) empowered to invest in Alaska real estate developments. Both kinds of enterprise are essentially passive investments and are in themselves exempt from federal income taxes (like AGSOCs); they are a way of increasing resident Alaskan ownership in major Alaska industry without the state's having to register as a securities underwriter.

The draft legislation also provides for distribution of securities in existing private enterprises. This provision would allow the State to buy blocks of shares in major Alaska businesses (fish processing plants, airline and communications companies, and the like), and to sell them to residents on easy terms in order to increase resident Alaskan ownership and control of important industries.

Natural resource trusts. The only wealth distribution plans that could be put to into effect under this program by the current legislature are probably Alaska Energy Resource Trusts. We believe that the effectiveness and credibility of the program demands that there be an early distribution of assets that have a certain, positive value. The first distribution must be one that neither requires a large front-end appropriation of money nor presents any risks to the citizens who receive the assets. Shares in oil and gas royalties --- specifically, royalties from the proved reserves at Prudhoe Bay --- seem to be the only kind of asset that can play this pioneering role.

The Prudhoe Bay Oil and Gas Royalty Trust of 1980 would commit royalties from only some of the leases at Prudhoe Bay, and only those royalties in excess of current

levels. Thus, the revenues conveyed to the trust would increase very rapidly with the decontrol of crude oil prices, and then fall off very rapidly as Prudhoe Bay production declined. We suggest the leases be chosen so that the average distribution per capita in the first year is in the \$100 to \$200 range --- large enough that people will have to take it seriously, but (in this first distribution) not enough to make a large dent in available revenues.

The Beaufort Sea Oil and Gas Royalty Trust of 1980 would commit royalties from Beaufort Sea leases sold in 1979. Any revenues produced from those leases would be distributed much later than the Prudhoe Bay royalties, and while the value of the certificates would probably be much greater, they would be a far more speculative property. Conceivably, the two plans could be combined into one plan that provided some certain near-term income, and some less certain but possibly far greater income, say, seven to ten years in the future.

The certificate holders would not have any voice in management of the oil and gas resource itself, and the trust indenture specifically makes the conveyance subject to any existing commitments of royalties. It also preserves the state's option to take royalty in kind --- it therefore creates no obstacles, for example, to fulfilling the Alpetco contract or to exchanging royalty gas for gas liquids to be used in Alaska petrochemical development. But the plans will certainly create a greater citizen identification with the North Slope oil and gas resource, and a more intense and informed interest in state and federal policies affecting those resources.

These plans would probably make Alaskans more receptive, for example, to state financial participation in the

gas line, especially if state involvement can reasonably be expected to accelerate its completion --- and thereby the flow of gas royalties. The plans would also create a broadly-based Alaska constituency pressing to maximize the wellhead value of the state's oil and gas, and resisting proposals to give away or discount the state's royalty for any purpose. (After all, the people will recognize, as they may not fully appreciate now, that these decisions involve their own money.)

PORTFOLIO OF ALASKA CITIZEN ENTERPRISES
DRAFT LEGISLATION

CONTENTS

<u>Section 1.</u>	1
CHAPTER 17. PORTFOLIO OF ALASKA CITIZEN ENTERPRISES	1
ARTICLE 1. GENERAL PROVISIONS	1
Section 10. Policy, purposes, and findings	1
Section 20. Establishment of portfolio	2
Section 30. Portfolio plans	3
Section 40. Portfolio plans submitted to legislature	4
Section 50. Legislative approval	7
ARTICLE 2. ELIGIBILITY FOR BENEFITS	7
Section 60. Eligibility for benefits	7
Section 70. Determination of eligibility	8
Section 75. List of persons claiming residence	10
ARTICLE 3. DISTRIBUTION OF ASSETS	10
Section 080. Basic purchase price (a)	10
Section 090. Free distribution	11
Section 100. First restricted sale	12
Section 110. Second restricted sale	14
Section 120. Unrestricted sale	15
Section 130. Purchase warrants	16
Section 140. Use of income tax refunds	18
Section 150. Disposition of proceeds	20
ARTICLE 4. GENERAL PROVISIONS	20
Section 160. Transfer of assets	20
Section 170. Voting rights	20
Section 180. Tax treatment	21
Section 200. Authority of commissioner to make a market	21
Section 210. Waiver of AS 37.10.085.	22
Section 220. Regulations	22
Section 230. Penalties	22
Section 240. Definitions	22
ARTICLE 5. ALASKA ENERGY RESOURCE TRUSTS	25
Section 250. Distribution of units	25
ARTICLE 6. ALASKA INDUSTRIAL DEVELOPMENT PROJECTS	26
Section 270. Intent	26
Section 280. Alaska Natural Gas Transportation System,	27
<u>Section 2.</u>	27
<u>Section 3.</u>	28
<u>APPENDIX:</u> HOUSE BILL NO. 1006	

PACE: Alaska's next plan to spread out the wealth

By ROXINNE ERVASTI
Associated Press Writer

JUNEAU, Alaska (AP) — Alaskans savoring the state's commitment to give them cash from its oil wealth and all but wipe out state income taxes now have an encore to consider — shares in state-owned assets.

It's called PACE — Portfolio of Alaska Citizens Enterprises.

The proposal introduced as legislation Thursday by Gov. Jay Hammond and House Speaker Terry Gardiner would sell stock in some state-owned assets to Alaskans at market value. Fifteen percent of the stock in the assets would be distributed free to all Alaskans.

Chief among the assets are oil, coal and natural gas. But the legislation provides that anything built with state money, be it offices, airports or pipelines, could be turned over to citizens.

The state could even buy shares in private companies, such as airlines, manufacturers or businesses, to sell and give away.

The money for PACE would divert funds from Alaska's burgeoning state treasury — now swelling so quickly from oil revenues that analysts last week upped their three-month-old estimate of its value in mid-1981 by \$319 million — to \$4.5 billion.

"Distributing a portion of Alaska's energy wealth to the people of Alaska in the form of income-producing assets would increase their involvement and awareness of the management of the state's natural resources, the development of its local industries and in the capitalist system overall," Hammond said. "All Alaskans, including the little guy, would have a piece of the action."

This proposal follows a "share-the-state-wealth" plan Hammond signed into law Tuesday that will put \$405 million into the pockets of 400,000 Alaskans this year alone.

Under that law, people who have filed a state income tax return for any three years since statehood in 1959 will be exempt from future taxes and get refunds on 1979 taxes. The state this year will pay residents \$50 in oil wealth "dividends" for each year they have lived in Alaska since 1959.

The "dividends" are to be an annual payment tied to a kind of oil revenues "state savings account" which is building and will give thousands annually to longtime Alaskans in the 1990s.

Under PACE, residents wouldn't get cash. They would get stock.

"Right now, if you want to invest in Alaska's oil, you have to buy shares in Exxon," said Gardiner, 29, a college-educated fisherman born in Ketchikan. "This would give

people a chance to invest directly in Alaska."

Alaskans have a longstanding dislike for "Outsiders" — people who came here years ago and nearly depleted the salmon, those who are absentee owners of fish processing and other facilities and those who came for oil pipeline construction money and left.

"This proposal will enable Alaskans to invest in Alaskan enterprises," says Hammond.

The state also shares its wealth through low-interest business and home loans. But Hammond has sought ways to benefit a broader base of residents, saying the programs give money that belongs to all the people to only a few.

The low-interest loan program in Alaska makes even federal aid pale by contrast.

For example, the Carter administration announced last week it would make \$160 million available to builders for unsold houses and to help low-income buyers. Since January, Alaska has appropriated \$140 million for home mortgage and consumer loans, \$75 million for business loans and \$15 million for fishing and farming loans. Legislators expect to allocate \$300 million more loans this year.

Rep. Russ Meekins, a 30-year-old Democrat and chairman of the House Finance Committee, shrugs his shoulders about the state's wealth and the envy it may bring, saying: "People hate the Rockefellers, too."

About 80 percent of state revenues come from oil through taxes, royalties and other payments from the oil companies to the state.

The oil won't last forever, and backers of the wealth-sharing plans say it makes no sense for the state to spend all the money on public works or other government programs, especially since they expect a mass exodus from Alaska once the oil runs out.

When that will happen is uncertain. But federal estimates indicate the amount of oil available from the state's primary known source — Prudhoe Bay — will decline significantly by the year 2000.

Dr. Arlon Tussing, an economist who worked on the PACE proposal, told legislators that after the oil industry winds down Alaska will be back to a fishing, tourism and timber economy.

"After that, how are the people going to be supported?" he asks.

Tussing estimates Alaska would have to produce 5½ times the United States' total coal production to replace Prudhoe Bay oil revenues, or equal the entire world catch of fish.

"There's little chance the state can fill the gap," he says. "A lot of people are going to have to leave, so you might as well give them a nest egg."

Personal Investing

Trusts That Rake Royalties Off the Top by Aimée L. Morner

Inflation hedgers flocking into natural-resource investments have been eyeing some unusual vehicles known as royalty trusts. These trusts, a few of which have been around since the early 1950's, are unincorporated enterprises that act as conduits for distributing royalty income to investors. Four of the five large publicly traded trusts (see table) derive their income from royalties on sales of oil and gas; the other, Mesabi Trust, gets its royalties from iron ore. Not surprisingly, the oil and gas trusts have risen the most in the last few years, and in mid-March a big new one—Houston Oil Royalty Trust—was about to come to market.

All of the royalty trusts share some common characteristics. None of them owns any real property; instead, they hold interests in royalties from properties owned by, or leased to, one or more operating companies. The royalties, figured as a certain percentage of sales, are paid "off the top"—i.e., before the operator makes any deductions for expenses or taxes. The trusts thus bear none of the risks or costs of drilling or mining. In fact, they are required by the Internal Revenue Service to remain "passive" and, in addition, to pay out virtually all their earnings.

In return, IRS rulings allow the trusts, and investors in their "units of beneficial interest," some tax breaks. The trusts themselves pay no federal income taxes, and the IRS takes the view that investors have a stake in the assets that produce income for the trust. Consequently, part of the cash payout is regarded as depletion, i.e., a return of capital, so shareholders pay no income tax on that portion.

The bookkeeping is tough

The yields on most of the trusts are fairly generous. The highest—11.4 percent for Mesabi Trust—is more than twice the yield on the stock of Cleveland-Cliffs Iron, the nation's largest iron-ore producer. Estimated yields on the other trusts range between 5.6 percent for North European Oil Roy-

alty Trust to 8.1 percent for Mesa Royalty Trust. By comparison, the yield on the S.&P. index of nine domestic oil companies is a slim 3.3 percent.

Figuring the taxes on the trusts' yields is nettlesome, but the bookkeeping is worth the trouble. Investors who have bought into oil and gas trusts in the last few years take "cost depletion," which involves using a depletion rate that is determined annually for each trust by independent engineers. The rates vary—from about 4 percent (an estimate) for Mesa to between 7 and 8 percent for the other three in the table.

The taxpayer applies the depletion rate to the cost of his units. If the rate is 7 percent, for example, and the units have a cost basis of \$40, then \$2.80 is considered a return of capital, and the cost of the units is reduced by that amount. Most of the time the depletion calculation will yield a figure lower than the payout; the rest of the cash distribution is taxed as ordinary income. (The treatment of this excess is dif-

ferent for Mesabi unit-holders. Once its units have been held for a period of time—it varies depending on when they were bought—the excess payout is taxed as a capital gain.)

Even though the underlying assets are being used up, the few analysts who follow the oil and gas trusts expect cash distributions to increase. Frederick A. Lynn, president of F.A.L. Capital Management, has been buying these trusts because he expects oil and gas prices to keep rising, which will not only lift royalties but also cause operators to press harder for more production.

Investors trying to figure out how much production is ultimately possible will be frustrated. While the Securities and Exchange Commission requires most publicly traded companies to report information about the size of their hydrocarbon reserves, some royalty trusts can duck the requirement if the data are either unavailable or too costly to get.

And that's the case with three of the four

THE PAYOUTS KEEP GROWING

	CASH DISTRIBUTION				YIELD	
	1979	1980 estimate	1981 estimate	Rate of growth, compounded 1975-1979	1975	Recent (based on est. 1980 distribution)
North European Oil Royalty Trust	\$4.07	\$5.00	\$7.50	37.2%	6.9%	5.6%
Marine Petroleum Trust	\$2.25	\$2.80	\$3.30	45.7%	8.0%	7.8%
Tidelands Royalty Trust B	\$1.94	\$2.80	\$3.60	N.A.	N.A.	6.7%
Mesa Royalty Trust	N.A.	\$3.05	\$3.30	N.A.	N.A.	8.1%
Mesabi Trust	\$1.39	\$1.65	\$1.80	4.8%	15.9%	11.4%

Two of the four oil and gas royalty trusts shown here—North European and Marine—have boosted cash distributions to investors at a heady pace since 1975. Of the remaining two, Mesa is a newcomer that sprang up last year, and Tidelands, which first began to distribute its royalty income in 1977, has nearly quadrupled its payout in the past two years. The other trust in the group, Mesabi, gets its income from royalties on shipments of iron-

ore pellets, and its performance has been lead-
ing. All the estimates for 1980 and 1981 were compiled from forecasts by various analysts and portfolio managers. Though the prices of trust units have risen significantly, the yields, based on the 1980 estimates, have not changed all that radically. A portion of the payouts of all the trusts, with the possible exception of Mesa, can be treated for tax purposes as a return of capital rather than income.

oil and gas trusts. North European Oil derives royalties from properties in West Germany that are leased to Mobil, Royal Dutch, and Exxon, which never whisper a word about the size of those reserves. Gulf Oil is just as tight-lipped about the reserves in fields it operates partly for Marine Petroleum Trust and partly for Tidelands Royalty Trust B.

Investors know a lot more about the reserves associated with Mesa Royalty Trust because of estimates in a prospectus issued last November, when the trust was spun off to shareholders of Mesa Petroleum. Independent petroleum engineers estimated proven oil and gas reserves and calculated their present value, discounting the expected income at an annual rate of 10 percent. This worked out to \$27.75 per unit, but the assumptions about the future price of oil and gas that go into such calculations are considered to be very conservative. Consequently, the units sold for about \$30 once they began trading. They subsequently rose as high as \$42, and were recently selling for about \$35.

Real-world expectations about price increases, particularly for gas, are quite bullish, for good reason. Under the Natural Gas Policy Act of 1978, prices of newly discovered gas—now about \$3 per 1,000 cubic feet (mcf)—may rise 10 percent a year until 1985. At that time controls will be lifted, and some analysts expect new gas to sell at a parity with oil. If they are right, even if oil were to sell at only \$30 a barrel, the price of gas will rise some 65 percent, to \$5 per mcf, in five years, since that quantity of natural gas has one-sixth as much heating power as a barrel of oil.

Life in new leases?

Buyers of Marine Petroleum Trust are betting primarily on the higher gas prices. Marine's royalties—a low 0.75 percent of sales—are derived solely from the trust's interest in 500,000 acres leased to Gulf Oil in the Gulf of Mexico. Half of that acreage now produces oil and gas, much of it coming from "mature" fields. While Gulf could yet find oil or gas in the other half, investors are primarily intrigued that some 70



In the last two years, the standout in this group has been North European, whose units have doubled in price. But over the period shown, Tidelands' shares have gone up even more—from only about \$1 in 1975, to \$42 recently. Shares of Marine (which owns a third of Tidelands' units) have retreated somewhat since reaching a record level last year. With the exception of Mesa and Mesabi, the trusts have relatively few units outstanding, and their prices tend to be quite volatile.

percent of Marine's royalties come from "old" natural gas with an average price of only \$1.20 per mcf. As contracts expire, or if new gas is discovered, that figure will inevitably go a lot higher. And the kicker in Marine is its 32.6 percent equity interest in Tidelands Royalty Trust B.

Tidelands is primarily a speculative bet on an increase in production. The Tidelands trust agreement with Gulf Oil covers 1.3 million acres offshore, and Gulf has so far leased only 40,000 of them. Analysts expect Gulf to seek new leases in the area and to spend freely on wildcat drilling. Tidelands will also benefit, though not as much as Marine, from rising prices: the Tidelands gas sells at an average price of around \$1.80 per mcf.

The price on much of the gas in which Mesa Royalty Trust has an interest is strictly bargain-basement. Close to 80 percent of the gas in its largest field sells under contract at a paltry 25 cents per mcf. The contract won't expire until 1989, but new gas from the same field would, of course, sell for a lot more.

Mesa investors are buying units in the face of an unusual risk: the IRS hasn't yet ruled that it can be treated as a trust. Regardless of how this issue is resolved, a hefty portion of the payout will almost certainly be taxed as ordinary income because Mesa's depletion rate this year is expected to be so low.

The new trust in the wings, an offspring of Houston Oil & Minerals, also lacks an IRS ruling on its tax status. The properties in which Houston Oil Royalty Trust has an interest include a substantial amount of unexplored acreage that would be worth a lot if Houston Oil & Minerals made dis-

coveries there. The company's success in finding new reserves, however, has recently been only fair.

The hottest trust in the market lately has been North European. Unit holders have benefited from the rise in the value of the D-mark because the operating companies involved sell what they produce in West Germany, where the fields are. In the last three years, the trust's royalty income, in dollars, has more than doubled. Carey E. Tharp Jr., an analyst at Stillman, Maynard & Co., is convinced the payout will continue to spurt ahead. He points out that more and more of the gas sold in Germany is coming from a field that produces royalties at a rate 7.5 times higher than the rate on sales from the field that is currently producing much of the trust's income.

A direct link to inflation

The iron trust, Mesabi, hasn't been particularly popular with investors lately. Its royalties come from properties in Minnesota's Mesabi range—the nation's largest iron-ore reserve. They are mined by Reserve Mining, which ships pellets made from the ore to the two steelmakers—Armco and Republic—who jointly own the company. Reserve pays Mesabi a base royalty that depends on the volume of pellets shipped, which means the trust's income is sensitive to the demand for steel. The base is also adjusted by a factor that reflects the annual change in the producer price index. That inflation hedge hasn't swayed investors, who are aware that Reserve's pellet factory could be struck this August when a labor contract expires. After the workers went out three years ago, Mesabi's cash distributions were slashed.

DRAFT: PORTFOLIO OF ALASKA CITIZEN ENTERPRISES (PACE)

A BILL

For an Act entitled: "An Act establishing the Portfolio of Alaska Citizen Enterprises, and providing for an effective date.

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

Section 1. AS 43 is amended by adding a new chapter to read:

CHAPTER 17. PORTFOLIO OF ALASKA CITIZEN ENTERPRISES

ARTICLE 1. GENERAL PROVISIONS

§43.17.010 POLICY, PURPOSES, AND FINDINGS

(a) It is the duty and policy of the State with respect to the natural resources belonging to it and the income derived from them to provide for their utilization, development, and conservation for the maximum benefit of its people.

(b) The purposes of this chapter are:

(1) to transfer part of Alaska's petroleum wealth to its people in the form of income-producing assets;

(2) to provide a means for the direct participation of individual Alaskans in the financing of, and profits from, newly organized enterprises of general benefit to the state [such as the Alaska Natural Gas Transportation System (ANGTS)];

(3) to promote greater resident Alaskan control, and to reduce absentee ownership and control, of existing Alaska industries;

(4) to encourage wider citizen participation in and understanding of the capitalist system through wider distribution of ownership in Alaska business enterprise;

(5) to encourage increased awareness and involvement by the people of Alaska in the management of natural resource production and development;

(6) to encourage increased awareness and involvement by the people of Alaska in the state's participation in business enterprise; and

(7) to encourage increased awareness and involvement by the people of Alaska in the development of local industry.

(c) The legislature hereby finds ---

(1) that it is in the public interest and in the furtherance of a public purpose to distribute a portion of Alaska's energy wealth to the people of Alaska in the form of income-producing assets in order to increase their involvement and awareness regarding the management of the state's natural resources, in the development of its local industry, and in the capitalist system;

(2) that a mechanism by which the state distributes a portion of its resource royalties will best promote the state's interest in producing a more personal and direct stake in the impact of decisions involving the state's natural resource production and development; and

(3) that a mechanism by which the state distributes a portion of its ownership interests in business enterprises will best promote the state's interest in providing a more personal and direct stake in the impact of decisions involving state investments, development of local industry, as well as a more personal and direct stake in the capitalist system.

§43.17.020. ESTABLISHMENT OF PORTFOLIO. The Portfolio of Alaska Citizen Enterprises is hereby established in the Department of Revenue as program for citizen wealth ownership and consists of one or more portfolio plans established according to §30 of this chapter.

(d) Except as required or authorized by this Act, or otherwise required by law, the assets distributed under the portfolio shall be the unencumbered private property of its beneficiaries, and the beneficiaries shall not be in any way impaired in their enjoyment of the earnings of those assets, the proceeds of their sale, or any other advantage of their use or disposition.

(e) The portfolio is not intended to create or result in the creation of any new governmental agency, corporation, or enterprise.

(f) Except as provided in this Act, the portfolio is not intended to be part of, duplicate, enlarge or diminish, conflict with, substitute for, or alter in any way ---

(1) any existing service or function of state government;

(2) any state business loan or industrial development program;

(3) any plan for the elimination, refund, or reduction of any state personal or business tax; or

(4) the investment of state revenues in, or the disposition of earnings from, the Permanent Fund.

§ 43.17.030. PORTFOLIO PLANS. (a) A portfolio plan under §20 of this chapter is a plan under which the Commissioner---

(1) contributes, transfers, commits, or dedicates to the Program securities, rights to resource revenues, or other assets, either already owned by the State or acquired expressly for the portfolio; and

(2) distributes those assets to individual Alaskans by grant and/or sale under the terms of this Act.

(b) Each portfolio plan shall provide for the distribution of assets to eligible individuals in the form of certificates that establish their ownership, right, or interest in one (and only one) of the following:

- (1) An Alaska Energy Resource Trust,
- (2) An Alaska Industrial Development Project,
- (3) An Alaska General Stock Ownership Corporation,
- (4) An Alaska Investment Fund,
- (5) An Alaska Real Estate Trust, or
- (6) Shares in one or more existing private enterprises doing business in Alaska.

(c) Each portfolio plan shall provide for a single distribution of such certificates only to persons who were residents on an eligibility date to be specified in the plan.

§ 43.17.040. PORTFOLIO PLANS SUBMITTED TO LEGISLATURE.

(a) The Commissioner shall, on or before the thirtieth legislative day of each Session of the legislature beginning with the First Session of the Twelfth Legislature, submit to the legislature for its consideration and approval, at least one portfolio plan, and not more than three such plans.

(b) Each portfolio plan submitted to the legislature under this section shall be in the form of a report that ---

(1) specifies the assets to be made available for distribution;

(2) authorizes their purchase or other acquisition by the State, if necessary, and their appropriation, transfer, commitment, or dedication to the plan;

(3) specifies the eligibility date for persons receiving benefits under the plan;

(4) specifies the manner in which eligible persons must apply for a grant of assets, or subscribe to purchase assets, distributed under the plan, and the earliest and latest dates on which they may make such an application or subscription;

(5) specifies the type and number of shares, certificates, debentures, warrants, options, or other securities or instruments to be distributed, and the manner in which they are to be distributed;

(6) specifies the terms and manner of payment for any assets to be sold under the plan;

(7) directs and authorizes the disposition of any assets appropriated, transferred, committed, or dedicated to the, and of any authorized or issued certificates that are not actually distributed under the plan;

(8) specifies the restrictions, if any, on the sale, assignment, hypothecation, or other transfers of or encumbrances upon the assets distributed under the portfolio plan, consistent with this chapter; and

(9) authorizes the appropriation and expenditure of such funds as may be necessary to administer the plan.

(c) Each portfolio plan submitted to the legislature under this section shall be accompanied by ---

(1) such draft legislation in the form of a Bill or Bills amending the general laws of Alaska, as may be necessary to implement the plan. [An example might be enactment of an Alaska regulated investment company (mutual fund) law, in order to establish an Alaska Investment Fund]

(2) the proposed articles of incorporation and by-laws of any corporate entity, or the proposed indentures of any trust, whose creation is necessary to implement the plan;

(3) the names of, or a statement of the manner of selecting, the incorporators and initial directors of any such corporate entity, or trustee(s) of any such trust; and

(4) a statement that contains ---

(A) a description of the assets to be distributed under the plan, and an appraisal of their value, with due attention to any uncertainty that may attach to the appraisal;

(B) a tabulation of the initial fiscal cost of the plan to the State, and a projection of probable future fiscal costs, with due attention to any contingent fiscal costs, liabilities, or risks that may attach to the plan;

(C) projections of the probable earnings and appreciation (or decline) in the value of those assets, and of their probable impact on income and wealth of the plan's intended beneficiaries, with due attention to any uncertainty that may attach to those projections;

(D) a statement of any federal or state tax liability that might be incurred by beneficiaries of the plan in connection with the initial distribution of shares, certificates, debentures, warrants, options, or other securities or instruments, earnings derived from them, or their ultimate sale or other disposal, with due attention to any uncertainty that may exist with respect to that tax liability;

(E) an assessment of any other costs, liabilities, or risks that may attach to the receipt or ownership of assets distributed under the plan; and

(F) such other kinds of information as the United States and Alaska securities laws might require to be included in a registration statement or prospectus in an ordinary public offering or sale of the kinds of shares, certificates, debentures, warrants, options, or other securities or instruments to be distributed under the plan.

§43.17.050. LEGISLATIVE APPROVAL. A portfolio plan may not be implemented until it has been enacted by law.

ARTICLE 2. ELIGIBILITY FOR BENEFITS

§43.17.060. ELIGIBILITY FOR BENEFITS. (a) No person other than an individual who was a resident on the eligibility date established for a portfolio plan may receive a free grant under §90 of this chapter, or purchase under §100-110, any asset distributed under that plan.

(b) No person who has been granted, without consideration, any purchase warrant distributed under this chapter, and who has ceased to be a a resident, may exercise any such warrant or portion thereof remaining unexercised on the date on which said person ceased to be a resident, and any said unexercised warrant or option or portion thereof shall become null and void as of that date.

(c) (1) No person who has purchased, for consideration, any purchase warrant distributed under this chapter, and who has ceased to be a resident, may exercise any such warrant or portion thereof that remains unexercised on the date on which said person ceased to be a resident of Alaska, but

(2) any such person may offer any such unexercised and otherwise valid warrant or option or portion thereof for repurchase by the State, and upon such an offer the Commissioner shall repurchase said asset at its issue price, plus interest accrued from the date of issue to the date on which the offeror ceased to be a resident Alaska.

(d) Any installment contract or other loan made or held by the State of Alaska or any agency thereof for the purchase of assets distributed under this chapter, or secured by such assets, shall become due and payable as of the date the beneficiary ceases to be a resident.

§43.17.070. DETERMINATION OF ELIGIBILITY. (a) An individual who claims a distribution of units under §§90-110 of this chapter must file an application and statement of eligibility verified by him or her under penalty of perjury.

(b) In the application and statement of eligibility, the commissioner may require the individual to include one or more of the following:

(1) evidence that he or she was registered to vote in Alaska on that date, and actually voted in the last statewide general election prior to that date;

(2) a copy of the individual's Alaska resident personal income tax return for the tax year which includes that date, or for the previous tax year;

(3) an Alaska driver's license, or resident hunting, fishing, or trapping license, purchased prior to that date, and valid on that date;

(4) evidence that he or she had a telephone or electric utility connection listed in his or her name, or in the name of a spouse, or (in the case of a minor) in the name of a parent or guardian, at a private residence in Alaska on that date; and

(5) a notarized affidavit from two or more Alaska residents who can themselves present at least two of the items listed in paragraphs (1) through (4) of this subsection.

(c) An individual shall be presumed eligible if he or she provides at least two of the items specified in subsection (b) of this section.

(d) Any presumption of residency established under subsection (c) of this section may be rebutted, and a person shall be presumed not to be a resident on a given date if, within thirty days prior to or one year following that date, he or she ---

(1) voted in any election, or stood for election or served in any public office, in another state or nation; or

(2) declared himself or herself to be a resident of any other state or nation for any purpose, or took advantage of any right or privilege reserved to residents of another state or nation.

(e) The department shall prescribe and furnish a form for application and statement of eligibility, which must include a certification of residency in substantially the following form:

Under penalty of perjury, I hereby certify that

(1) I was a resident of the state of Alaska within the meaning of the law (AS 43.17.230(16), which is attached) on [date] , and

(2) I understand that my claim for a distribution of assets is based upon that residency, and that the law (AS 43.17.220, which is attached) provides that I will forfeit those assets and be required to repay any income I have received from them, in addition to any criminal penalties for which I may be liable, if I

should be convicted of perjury or unsworn falsification for making a false claim of residency.

Signature of applicant

§43.17.075 LIST OF PERSONS CLAIMING RESIDENCE. At least sixty days prior to the distribution of any units under any portfolio plan, the commissioner shall make available for public inspection in at least five locations around the state, a list of the names, addresses, and type of residency evidence submitted, of all persons claiming to be residents for the purpose of receiving benefits under the portfolio plan.

ARTICLE 3. DISTRIBUTION OF ASSETS

§43.17.080. BASIC PURCHASE PRICE. (a) The commissioner shall establish a basic purchase price for a unit of any asset to be sold to eligible individuals under §§100-110 of this chapter.

(b) The basic purchase price for units in an Alaska Industrial Development Project, an Alaska General Stock Ownership Corporation, an Alaska Investment Fund, an Alaska Real Estate Trust, or existing private enterprises, shall be equal to the average original cost to the State of Alaska of those units, or of the assets contributed, transferred, committed, or dedicated to the portfolio and represented by those units, plus an amount that, in the judgement of the commissioner, compensates the state for the administrative costs of acquiring, holding, and distributing those units.

(c) The basic purchase price for units in an Alaska Energy Resource Trust, authorized to be distributed to individual Alaskans under any portfolio plan shall be the conservatively appraised value of those units, as defined in subsection (d) of this section.

(d) A conservatively appraised value for units in an Alaska Energy Resource Trust is a value determined by generally accepted appraisal methods, with the following stipulations:

(1) Estimates of resource or production volumes shall have a confidence level of seventy-five percent (75%) or greater --- that is, the appraiser must believe that there is at least a seventy-five percent probability that the actual resource or production volume will equal or exceed the estimated value;

(2) the assumed rate of increase in future world prices for energy commodities (as represented, for example, by the price of Saudi Arabian "marker" crude oil) shall not exceed the general rate of price inflation in the United States; and

(3) the discount rate used to reduce future income and costs to present value shall reflect the judgment of private investors as to the expected pre-tax rate of return required to justify incremental investments in the exploration and development of resources comparable to those from which income has been committed to the portfolio plan.

(e) The assets distributed under any portfolio plan must be divided, or must be subdivisible at the option of the holder, into units whose basic purchase price does not exceed fifty dollars (\$50) per unit.

(f) Prior to sale of any asset under any portfolio plan, the commissioner shall notify prospective purchasers of the basic purchase price determined by him under this section for the units to be sold.

§43.17.090 FREE DISTRIBUTION. Unless otherwise required by law, a fraction to be specified in each portfolio plan, but not less than five percent (5%) nor more than fifteen percent (15%), of the total number of units

to be distributed under each plan shall be granted in equal portions, without consideration, to all eligible individuals Alaskans who apply to receive said assets;

§43.17.100 FIRST RESTRICTED SALE. (a) All units authorized to distributed to eligible individuals under each portfolio plan, other than those distributed as a grant without consideration under §90 of this chapter, shall be offered for sale to eligible individuals in a first restricted sale.

(b) In each sale under this section, each eligible individual shall have the right to subscribe for any number of units of the assets to be distributed, by submitting an application and statement of eligibility under §70 of this chapter together with a deposit equal to ten percent of the basic purchase price of the subscribed units. The deposit shall be in the form of cash, check, money order, or an assignment of any unpaid Alaska income tax refund for a past or current tax year.

(c) The applicant shall indicate on his or her subscription application whether he or she wishes to purchase the assets (1) for cash, or (2), on an extended purchase plan as provided in subsection (f) of this section.

(d) If the first restricted sale is oversubscribed, each eligible applicant shall have the right to complete the purchase of the lesser of ---

(1) the number of units subscribed for,
or

(2) the number of units which, if established as the maximum number of units that any one eligible applicant may purchase, would result in the sale of all the units authorized for sale.

(e) The commissioner shall notify each subscriber who elects to purchase assets for cash as provided in subsection (c) of this section of the total number of units he or she is entitled to purchase in the first restricted sale, and of the cash balance required, after crediting his or her deposit, to complete the purchase of those units. On receipt of cash, check, or money order equal to the balance owing, the commissioner shall, subject to the limitation in §140 of this chapter, convey to such subscriber the shares, certificates, debentures, or other assets so purchased. If the subscriber fails to complete the purchase as provided in paragraph (1) of this subsection within sixty days, the commissioner shall convey to such subscriber, subject to the limitation in §140, the largest number of whole units whose basic purchase price does not exceed the amount of the subscriber's deposit, and refund any balance remaining from the subscriber's deposit.

(f) The commissioner shall notify each subscriber who elects to purchase on an extended payment plan as provided in subsection (c) of this section of the total number of units he or she is entitled to purchase in the first restricted sale, and convey to such subscriber:

(1) The largest number of whole units that does not exceed one-tenth of the total number of units the subscriber is entitled to purchase;

(2) A refund of the difference, if any, between the subscriber's deposit and the basic purchase price for the number of units conveyed under paragraph (1) of this subsection; and

(3) Purchase warrants described in §130 of this section, for the balance of the total number of units the subscriber is entitled to purchase.

§43.17.110. SECOND RESTRICTED SALE. (a) If the first restricted sale under any portfolio plan is undersubscribed, and if the plan authorizes a second restricted sale in such an event, the commissioner shall conduct such a sale under this section.

(b) In a sale under this section, each eligible individual may submit one or more sealed bid(s) each of which shall specify the number of units the bidder wishes to purchase at a bid price specified by him or her, which price must be equal to or exceed a minimum bid price specified by the commissioner, but which may otherwise be less than, equal to, or more than the basic purchase price.

(c) The sealed bids described in subsection (b) of this section must be accompanied by an application and statement of eligibility under §70 of this chapter, and a deposit equal to ten percent of the bid price for the number of units subscribed. The deposit may be in the form of cash, check, or money order, or an assignment of any unpaid Alaska personal income tax credit or refund for the past or current tax year not already encumbered in the first restricted sale.

(d) The commissioner shall tally the bids in descending order of bid price, until (1) the total number of units bid for equals the number of units to be sold, or (2) all bids at or above the minimum bid price have been tallied, whichever occurs sooner; and the commissioner shall award to each bidder whose bid has been included in this tally, sale of the number of units for which he or she bid, at an actual sales price equal to his or her bid price for those units [ALTERNATE PROVISION: to the bid price for lowest bid so tallied], until (1) all such bids have been satisfied, or (2) all units have been sold, whichever occurs sooner.

(e) If the number of units for which valid bids are received at a bid price equal to or greater than the actual sales price as described in subsection (d) of this section, exceeds the number of units available for sale, the Commissioner shall award sale of the number of units bid for to each such bidder whose bid price exceeded the actual sales price, and shall award sale of the remaining units to those bidders whose bid price was exactly equal to the actual sales price, in proportion to the number of units for which they bid at that price.

(f) All sales of units shall be cash sales. The commissioner shall notify each successful bidder of the total number of units he or she is entitled to purchase in the second restricted sale, and of the cash balance required, after crediting his or her deposit, to complete the purchase of those units. On receipt of cash, check, or money order equal to the balance owing, the commissioner shall, subject to the limitation in §140 of this chapter, convey to such bidder the units so purchased. If the bidder fails to complete the purchase as provided in this subsection within sixty days, the commissioner shall convey to such bidder, subject to the limitation in §140, the largest number of whole units for which the actual sales price does not exceed the amount of the subscriber's deposit, and refund any balance remaining from the deposit.

§43.17.120. UNRESTRICTED SALE. Except as expressly provided in this Act or the terms of a portfolio plan, or otherwise prohibited by law, the Commissioner is authorized to hold as investments or to sell for maximum revenue, or otherwise for the the benefit of the state, any units authorized to be distributed under a plan, but which (1) remain undistributed after completion of the free distribution under §90 of this chapter, the first restricted sale under §100, and (where authorized) the second restricted sale under §110, and (2) are not reserved for sale under the terms of a purchase warrant.

§43.17.130. PURCHASE WARRANTS. (a) Purchase warrants distributed under §100(f) shall grant an eligible holder the right to purchase, over a period of nine years from their date of issue, the number of units that equals nine-tenths (90%) of the total number of units that the holder was entitled to purchase in a first restricted sale under this chapter, on the following schedule:

(1) The largest number of whole units that does not exceed one-ninth of the total number of units that the holder is entitled to purchase after receipt of the units distributed under §100(f)(1), not later than one year after the issue date;

(2) The largest number of whole units that does not exceed one-eighth of the units that the holder is entitled to purchase after receipt of the units distributed under §100(f)(1), less the number of units he was entitled to purchase under paragraph (1) of this subsection, not later than two years after the issue date;

(3) The largest number of whole units that does not exceed one-seventh of the units that the holder is entitled to purchase after receipt of the units distributed under §100(f)(1), less the number of units he was entitled to purchase under paragraphs (1) and (2) of this subsection, not later than three years after the issue date;

(4) The largest number of whole units that does not exceed one-sixth of the units that the holder was entitled to purchase after receipt of the units distributed under §100(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (3) of this subsection, not later than six years after the issue date;

(5) The largest number of whole units that does not exceed one-fifth of the units that the holder was entitled to purchase after receipt of the units distributed

under §100(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (4) of this subsection, not later than seven years after the issue date;

(6) The largest number of whole units that does not exceed one-fourth of the units that the holder was entitled to purchase after receipt of the units distributed under §100(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (5) of this subsection, not later than six years after the issue date;

(7) The largest number of whole units that does not exceed one-third of the units that the holder was entitled to purchase after receipt of the units distributed under §100(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (6) of this subsection, not later than seven years after the issue date;

(8) The largest number of whole units that does not exceed one-half of the units that the holder was entitled to purchase after receipt of the units distributed under §100(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (7) of this subsection, not later than eight years after the issue date;

(9) The largest number of whole units that does not exceed the number of units that the holder was entitled to purchase after receipt of the units distributed under §100(f)(1), less the number of units he or she was entitled to purchase under paragraphs (1) through (8) of this subsection, not later than nine years after the issue date;

(b) The actual purchase price for any asset purchased by exercising a purchase warrant under this

section shall be the basic purchase price of the unit as defined in §80 of this chapter, as adjusted according to subsection (c) of this section.

(c) The basic purchase price shall be increased by a carrying charge calculated at a rate equal to the weighted average cost of borrowing to the State of Alaska during the fiscal year previous to the date of issue, compounded from the purchase warrant's date of issue to the date of actual purchase of the issue, less any dividends, interest, royalties, or profits received by the State from holding the unit between the stock-purchase warrant's date of issue and the date of actual purchase, but in no event may the actual purchase price be less than one-half the basic purchase price.

(c) Payment for units purchased by exercising a purchase warrant under this chapter may be by cash, check, or money order, or by an assignment of any unpaid Alaska personal income tax credit or refund from the past or current tax year.

(d) All stock-purchase warrants distributed under §80 of this chapter 320(f) shall be non-transferable, except by inheritance, and no purchase right granted by such a warrant shall be exercised except by an individual who is a resident at the time said purchase right is exercised.

§43.17.140. USE OF INCOME TAX REFUNDS. (a) The commissioner may not convey to a purchaser a unit to be distributed under this program, and purchased under §§110-120 of this chapter in whole or in part by means of an assignment of an Alaska personal income tax refund for any year, until the purchaser's personal income tax return for that year has been filed and processed by the Department of Revenue, and the commissioner has determined that the purchaser appears to be entitled to a tax refund sufficient to satisfy the balance owing for his or her purchase of under the portfolio.

(b) If after the purchaser has filed, and the Department has processed, the purchaser's Alaska personal income tax return as provided in subsection (a) of this section, the commissioner determines that the purchaser does not appear to be entitled to a personal income tax credit or refund sufficient to pay the balance owing for his or her purchase, the commissioner shall notify the purchaser of the balance owing after crediting any refund or credit to which the purchaser may be entitled. On receipt of cash, check, or money order equal to the balance owing, the commissioner shall convey to the purchaser the units so purchased. If the purchaser fails to complete the purchase as provided by this subsection within sixty days, the commissioner shall convey to such purchaser the largest number of whole units for which the actual sales price does not exceed the sum of (a) any applicable cash payment and (b) any tax refund or credit which in the judgment of the commissioner may properly be applied to the purchase, and the commissioner shall refund or credit to the purchaser's Alaska tax payments any balance that remains owing to the purchaser.

(c) If a disagreement exists between any purchaser and the commissioner regarding the purchaser's entitlement to apply Alaska personal income tax refunds to the purchase of units under this section, the determination of the commissioner shall, if not amended by him, become final sixty days after the notice provided for in subsection (b) of this section, or if amended by him, sixty days after his notice to the purchaser of such amendment. The purchaser's only remedy against the determination of the commissioner in this section is to pay the balance owing on the purchase of units under the portfolio, and to pursue whatever remedies exist at law to obtain a refund. The purchaser's remedies

do not include any right to compel the commissioner to complete the sale of any units to which the disputed sum would have been applied.

(d) The provisions of subsection (c) of this section shall not in any way alter any person's Alaska personal income tax liability, entitlement to any tax refund or credit, or any remedy he or she may have in respect to any disagreement with the State of Alaska regarding such liability or entitlement.

§43.17.150. DISPOSITION OF PROCEEDS. The commissioner shall deposit all net proceeds from the sale of units under this chapter into the Alaska Permanent Fund established in IX §15 of the Alaska State Constitution and AS 37.13.010.

ARTICLE 4. GENERAL PROVISIONS

§43.17.160. TRANSFER OF ASSETS. Except as expressly provided with respect to purchase warrants in §30 of this chapter, or units in an Alaska Energy Resource Trust or in an Alaska General Stock Ownership Corporation, a recipient or holder of any units distributed under this chapter shall have an unrestricted right to sell, transfer, devise, bequeath, pledge, hypothecate, or otherwise dispose of any such units, or interest in or earnings from those units.

§43.17.170. VOTING RIGHTS. (a) The commissioner may exercise any voting rights owned, held in trust, or reserved for future distribution under the program.

(b) The voting rights attached to ownership of any unit distributed under this chapter shall be conveyed unrestricted to the eligible individual receiving that security, and the commissioner may not reserve, or require as a condition of distribution of any such security that the

recipient waive any such right, grant any proxy, or adhere to any voting trust, unless the security were subject to such a stipulation or covenant at the time it was acquired by the State.

§43.17.180. TAX TREATMENT. (a) The receipt by an eligible individual of units distributed under this chapter is not taxable under AS 43.20.

(b) If the receipt by any eligible individual of units distributed by the State under this program should be treated as income or capital gains under the Internal Revenue Code and, as a result, that individual is required to pay an additional federal income tax, the amount of that additional tax shall be creditable against the individual's Alaska individual income tax for the tax year in which the additional federal income tax is paid.

(c) If the amount of the credit to which an eligible individual is entitled under (a) of this section exceeds his or her net tax liability, if any, under AS 43.20, the individual is entitled to receive a payment for the excess and that payment for the excess shall not be taxable under AS 43.20.

(d) Nothing in this article shall be construed to exempt from state or federal taxes any dividends, interest, profits, or other income received from any units distributed under the program, or the proceeds from their sale.

§47.17.200. AUTHORITY OF COMMISSIONER TO MAKE A MARKET. (a) If the commissioner finds that an efficient public market does not exist for any issue of units distributed under the program, he is authorized to buy, sell, and trade in those units for the purpose of establishing such a market, and to publish regularly the "bid" and "ask" prices for those units.

(b) If the commissioner makes a market in units as authorized in subsection (a) of this section, he shall

as authorized in subsection (a) of this section, he shall maintain an average markup (or spread between bid and ask prices) just sufficient, in his judgment, to compensate the State for the administrative costs of his trading activity.

(c) An efficient public market for purposes of this section means a market in which the units distributed the program have at all times a readily ascertainable market value, and that they may be bought and sold readily and without unnecessary or unreasonable transactions costs.

§43.17.210. WAIVER. The provisions of AS 37.10.085 shall not apply to the acquisition of assets under this chapter.

§43.17.220. REGULATIONS. The department may adopt regulations necessary to administer the program.

§43.17.230. PENALTIES. Any person convicted of perjury or unsworn falsification on the basis of a statement made under §70 of this chapter may never, if that conviction is not reversed, become eligible for the distribution of units under this program, and shall forfeit all units distributed to him or her.

§43.17.240. DEFINITIONS. In this chapter

(1) "Alaska Energy Resource Trust" means a trust established by the commissioner as part of a plan enacted under this chapter, the assets of which trust are a right to receive income equal to a specified portion of the rentals, royalties, net profits, or mineral sale revenues from the production of oil, gas, coal, oil, or other resources from specified leases or properties of the state;

(2) "Alaska Industrial Development Project" means a private enterprise engaged or intending to engage in the business of natural resource extraction or processing, or manufacturing, transportation, or communications, wholly or partly within the state, and to which the State or an

agency or subdivision of the State, contributes capital or assists in financing, thorough an investment of equity or debt capital in the form of money or rights in land or natural resources, or by loan guarantees, having a value exceeding \$100 million;

(3) "Alaska General Stock Ownership Corporation" means a corporation formed in accordance with subchapter U, chapter 1 of the Internal Revenue Code of 1954, as amended (26 U.S.C. 1391-1397);

(4) "Alaska Investment Fund" means a regulated investment company (also known as a mutual fund) organized or caused to be organized by the commissioner in accordance with subchapter M, chapter 1 of the Internal Revenue Code of 1954, as amended (26 U.S.C. 851-855);

(5) "Alaska Real Estate Trust" means a real estate investment trust organized or caused to be organized by the commissioner in accordance with subchapter M, chapter 1 of the Internal Revenue Code of 1954, as amended (26 U.S.C. 856-858);

(6) "assets" means shares of stock, debentures or other debt obligations, royalties or other interests in minerals, or other interests in minerals or other business enterprises or natural resources;

(7) "certificate" means an instrument evidencing ownership of one or more units and includes stock certificates, debentures or other debt instruments and trust certificates;

(8) "commissioner" means the Commissioner of Revenue;

(9) "department" means the Department of Revenue;

(10) "eligible individual" means an individual who is a resident as of an eligibility date set out in a portfolio plan.

(11) "eligibility date" means a date established by the commissioner, on which an individual must have been a resident in order to receive units distributed under §90-110 of this chapter;

(12) "existing private enterprise" means an existing private corporation engaged in or intending to engage in natural resource extraction or processing; manufacturing, transportation, communications, trade, or services in Alaska, whose securities the commissioner has purchased under his existing authority, or proposes to purchase under the terms of a portfolio plan for distribution under this chapter;

(13) "extended purchase plan" means the purchase of units over time through the exercise of purchase warrants;

(14) "individual" means a natural person;

(15) "issue date" means the date on which the commissioner issues a purchase warrant or other certificate to an eligible individual;

(16) "oversubscribed" means a sale in which the total number of units subscribed for exceeds the total number of units offered for sale;

(17) "plan" means a portfolio plan as described in §40 of this chapter.

(18) "portfolio" means the Portfolio of Alaska Citizen Enterprises established by this chapter.

(19) "resident" means an individual who maintains a permanent place of abode in the state with the intention of making the state his or her permanent place of residence and who resides in the state continuously except for temporary purposes only and with the intent of returning; a person may not be considered to have gained a residence solely by reason of his or her presence and may not lose it solely by reason of his or her absence while in the

civil or military service of this state or of the United States or by reason of his or her absence because of marriage to a person engaged in the civil or military service of this state or of the United States, or for attendance as a student or visiting scholar at an educational institution, or while in an institution at public expense, while confined in prison, while engaged in the navigation of the waters of the state, the United States, or the high seas, or while residing upon an Indian or military reservation within the state; a minor's residence shall be deemed to be the same as that of his or her parent or guardian; a married person may establish his or her own residence, and does not presumptively lose residency if his or her spouse is not a resident.

(20) "unit" means the smallest fractional interest in an asset distributed under this chapter; and

(21) "warrant" means an instrument authorizing the purchase of units under this chapter.

ARTICLE 5. ALASKA ENERGY RESOURCE TRUSTS.

§43.17.250. DISTRIBUTION OF UNITS. (a) Units in any Alaska Energy Resource Trust established under this chapter shall be distributed to eligible individuals according to the provisions of §90-110 of this chapter, and the basic purchase price for such certificates shall be determined as provided in §80(c) of this chapter.

(b) There shall be no unrestricted sale under §120 of this chapter, of the units of any Alaska Energy Resource Trust; and the commissioner shall hold as an investment for the State any certificates that (1) remain undistributed after completion of the free distribution under §90 of this chapter, the first restricted sale under §100, and (where authorized) the second restricted sale

under §110, and (2) are not reserved for sale according the terms of a purchase warrant, including those units that were previously so reserved, but for which the outstanding purchase warrants have expired or been invalidated.

§43.17.260. OWNERSHIP AND TRANSFERABILITY. (a) An individual who has received units in an Alaska Energy Resources Trust in a distribution under this chapter shall not be required to return, sell, or otherwise relinquish those certificates as a result of ceasing to be a resident, but no certificates of such a Trust may be sold, given, assigned, transferred, or otherwise conveyed, except by inheritance, to any person who is not a a resident of Alaska; and the trustee may cancel any certificates sold, given, assigned, tranferred, or otherwise conveyed, except by inheritance, to other than a resident, and provide compensation for such shares at no more than the basic purchase price.

(b) No person or affiliated group may obtain or hold, by grant or purchase, whether from the State or otherwise, or by any other means, title to or a beneficial interest in, more than one-twentieth (5%) of the total authorized, issued, or outstanding units (whichever is the least) of any Alaska Energy Resource Trust authorized, issued, or outstanding (whichever is the least), and the trustee of such a Trust may not distribute to any person or affiliated group, and such person or group may not receive, any dividends, royalties, profits, or other payments from the income of such a Trust in excess of those attributable to one-twentieth (5%) of the total shares.

ARTICLE 6. ALASKA INDUSTRIAL DEVELOPMENT PROJECTS

§43.17.270. INTENT. It is the intent of this chapter that, to the extent it is feasible, whenever the State participates in the financing of any enterprise that is an Alaska Industrial Development Project as defined in §240(2) of this chapter,

ARRL

(1) the state's direct participation be temporary and limited to the promotional, organizational, design and construction phases (or, in the case of natural resource extractive enterprises, to the promotional, organizational, exploration, and development phases);

(2) any state ownership and management role in such enterprises be relinquished to private parties once those enterprises become established and viable; and

(3) ownership and management roles relinquished by the state in such enterprises be transferred to eligible individuals through the portfolio established by this chapter.

§43.17.280. ALASKA NATURAL GAS TRANSPORTATION SYSTEM. If the commissioner under his existing authority should invest any funds of the state in equity or convertible debentures of the Alaska Natural Gas Transportation System, also known as the Alaska Highway Gas Pipeline (hereinafter ANGTS), or a portion thereof, or in a natural gas conditioning plant or natural gas liquids transportation system associated with ANGTS, or if the governor or any official of the executive branch of the state should submit to the legislature any proposal for state participation in the financing of ANGTS or a portion thereof, or of a natural gas conditioning plant or natural gas liquids pipeline associated with ANGTS, by contribution of equity or purchase of convertible debentures, the commissioner shall, within 30 legislative days of such an investment or the submission of such a proposal, submit a plan for eventual distribution of the state's ownership interest to eligible individuals through the portfolio established by this chapter.

Section 2. The enactment of a version of SB 170 or HB 240 [Eleventh Legislature] relating to general stock ownership corporations and creating an Alaska General Stock

Ownership Corporation shall constitute approval of a portfolio plan under AS 43.17.040. After enactment, the Commissioner of Revenue shall implement the plan in accordance with this Act and a version of SB 170 or HB 240 relating to general stock ownership corporations and creating an Alaska General Stock Ownership Corporation, whichever may be enacted, subject to necessary appropriation. Notwithstanding the approval under this section, the Commissioner of Revenue may submit to the legislature by the thirtieth legislative day of the Twelfth Legislature a revised plan if in his judgment a revised plan is necessary to implement fully the policy, purposes, and findings of this Act and of the version of SB 170 or HB 240 relating to general stock ownership corporations and creating an Alaska General Stock Ownership Corporation, whichever may be enacted, or if in his judgment a revised plan is necessary to provide complete information concerning the plan. A revised plan submitted under this section is subject to legislative approval under AS 43.17.040.

Section 3. This Act takes effect immediately in accordance with AS 01.10.070(c).

$\frac{\$50m/yr}{0.0001} = 500,000,000$ (7.2%)
 Loan portfolio of

$\frac{\$60,000,000}{0.0001} = 600,000,000$
 @ 7.5%
 Interest

~~Warrant~~

$\frac{547,500}{0.0001}$

365

$\frac{182,500}{0.0001}$

15

325

$\frac{15,000}{0.0001}$

524

009

$\frac{15,000}{0.0001} = 150,000,000$
 18 81 2
 7500 100

$\frac{12}{15} = 0.8$
 $\frac{0.0001}{0.0001} = 1$

~~Handwritten scribble~~

Handwritten scribble

~~Handwritten scribble~~

THE PROPOSED ALASKA GENERAL STOCK
OWNERSHIP CORPORATION (AGSOC)

PREPARED BY ARLON R. TUSSING & ASSOCIATES, INC.

For the House Finance Committee

ALASKA STATE LEGISLATURE

February 5, 1980

CONTENTS

	Page No.
PREFACE AND SUMMARY.....	i.
PART I: THE GENERAL STOCK OWNERSHIP CORPORATION (GSOC): TAX ADVANTAGES.....	1
Dividend and total earnings after taxes: GSOC vs. an ordinary business corporation.....	4
GSOC's vs. tax shelters for ordinary corporate earnings.....	5
GSOC's vs. small business organization.....	8
REINVESTMENT OF GSOC EARNINGS.....	11
THE DANGER OF CASH DEFICIENCIES.....	14
PART II: AGSOC FINANCING AND INVESTMENT STRATEGY HOW IS AGSOC TO BE FINANCED?.....	19
PRINCIPLES OF FINANCING.....	22
PROJECT FINANCING: ELEVEN CASES.....	24
Case 1: Commercial real estate.....	24
Case 2: Commercial real estate.....	24
Case 3: Oil Pipeline.....	25
Case 4: Electrical generating plant.....	25
Case 5: Electrical generating plant.....	26
Case 6: LNG terminal.....	27
Case 7: Ship Construction.....	27
Case 8: Ship Construction.....	28
Case 9: Public works.....	28
Case 10: Public works.....	29
Case 11: Housing.....	29
. . . AND THEIR IMPLICATIONS.....	30

(continued on next page)

PUBLIC UTILITY INVESTMENTS.....	32
Implications of GSOC's tax exemptions.....	33
Allowed earnings of regulated utilities.....	36
Treatment of IIC.....	37
BRITISH PETROLEUM'S INTEREST IN TAPS.....	39
Financing the purchase.....	40
Purchase price.....	41
Tariff conditions.....	41
Risk.....	43
Summary.....	44
SOME AGSOC INVESTMENT POSSIBILITIES.....	45
The gas conditioning plant.....	45
Coal mining.....	47
Shipping.....	48
In general.....	48
STATE APPROPRIATIONS, DIRECT LOANS, AND LOAN GUARANTEES.....	50
State equity contributions.....	50
Direct loans.....	51
Loan guarantees.....	52
Assumption of risk and creation of risk.....	53
The adverse impacts of soft credit.....	54
Shareholder tax liability.....	54
Today's Alaskans and future Alaskans.....	55
Summary.....	56
PART III: AGSOC SHAREOWNERSHIP AND MANAGEMENT.....	58
Kelso's ideology.....	58
Restrictions on shareownership, transfers and voting.....	58
Will the example of a new, broadly-based form of business enterprise revolutionize the economic system or the social order?.....	59
The experience of the cooperative movement.....	60
Management incentives.....	61

PREFACE AND SUMMARY

The geological accident at Prudhoe Bay has given the government of Alaska, and through it the state's four hundred thousand people, a source of income that will far exceed anyone's notions of the funds needed for ordinary public services. The expected cash surplus also surpasses the capital requirements for all but the most far-fetched state economic development schemes.

Most Alaskans give some support to the idea of saving part of this treasure against the day that current oil revenues no longer can provide the citizens with a high level of government services, lavish transfer payments and generous promotional programs for favored industries at practically no cost in personal or business taxes. But savings plans that will benefit mostly strangers ten, twenty, or more years in the future, probably can not match the attraction of programs that will, one way or another, get money into the state's economy now.¹

For many decades, moreover, residents of Alaska have deplored or resented the fact that outside capital dominated its major industries --- mining, fisheries, and now petroleum. In the 1980's, Alaskans have a chance to dilute this outside control, if they wish to use part of the state's oil wealth for such a purpose.

1) As I have commented elsewhere, some proposals that are purportedly aimed at diversifying Alaska's economic base are best understood as disguised programs to "privatize" a part of the oil revenues. [See Arlon R. Tussing, "Investing in Economic Development." Statement at Workshop of Alaska Growth Policy Council, Anchorage, October 20, 1979.]

Thus, it is not surprising that the state's citizens should consider ways in which to turn at least part of the current government windfall directly into private income or wealth. Some current proposals, such as Governor Hammond's energy credit plan and his "people's portfolio" are openly intended to serve this aim.

AGSOC resembles these plans in some respects, and not in others. Like them, it intends to distribute privately-owned wealth broadly among individual Alaskans. But, according to the inventor of the concept, San Francisco financial consultant Louis Kelso, and its most prominent Alaska advocate, Senator Mike Gravel, the Corporation's capital will come from borrowing in private financial markets. Thus, the sponsors assert, any wealth distributed to Alaska residents in the form of AGSOC shares will neither come from, nor depend upon, the state's oil wealth.

Notwithstanding these claims, our report treats AGSOC as one option for managing Alaska's oil and gas wealth, for four reasons: First, until about one year ago, even Mr. Kelso and Senator Gravel presented AGSOC as a wealth-distribution plan. Second, most legislators and concerned members of the public regard it as such a plan. Third, and more important, we can evaluate the General Stock Ownership Corporation (GSOC) as a form of business organization quite separately from the way in which it is originally capitalized. Finally and most significantly, our investigation concludes that there is almost no hope that an Alaska GSOC could be financed entirely with "non-recourse" borrowing --- that is, without a direct state appropriation or loan guarantee.

The Kelso-Gravel program for AGSOC, which is reflected in the variants on H. B. 240 and S. B. 170, has three elements that we can consider separately:

1. The Alaska legislature would charter AGSOC as a private corporation entitled to certain federal tax benefits under Subchapter U of the Internal Revenue Code, and distribute one share in the Corporation free of charge to each Alaska resident.
2. AGSOC would purchase one or more existing profit-making enterprises: AGSOC sponsors have devoted the greatest attention to British Petroleum's interest in the Trans Alaska oil pipeline (TAPS).
3. AGSOC would finance these purchases with borrowed money, using its profits to pay off the debt.

Part I of this report examines the tax treatment of general stock ownership corporations (GSOCs) under Subchapter U and finds that:

1. A GSOC can create significant tax savings for shareholders, compared to an ordinary business corporation, if all of the latter corporation's earnings are exposed to the highest federal tax rates; but
2. Ordinary business corporations can be (and usually are) organized so as to shelter much of their income from the corporate income tax by their scheduling of depreciation, for example, or by converting profits to deferred capital gains and interest;
3. GSOCs are not the only kind of business organization that avoids double taxation of profits: cooperatives, mutual funds, and small businesses (proprietorships, partnerships and Subchapter U corporations), for example, are treated similarly. All other things being equal, the three principal types of small-business organizations are at least equal to, and are usually more efficient than, GSOCs as producers of after-tax earnings;
4. Any tax savings for shareholders that result from organizing a business as a GSOC are greatest in the lowest tax brackets, and may be insignificant for upper-income taxpayers; and that

5. The need to pay dividends every year sufficient to offset the personal tax liability that GSOC ownership creates for individual shareholders severely restricts the kinds of investments that GSOCs may safely make, and the ways in which those investments can be financed.

Thus, the ability to shelter benefits from the federal tax collector is obviously an important consideration in choosing the instruments by which Alaska tries to distribute capital ownership more widely among the state's residents, but it is by no means the only consideration and may not always be the dominant one. And, as we have seen, a GSOC is not even the most effective tax shelter in every instance.

The AGSOC idea may remain an enticing one even if its tax treatment is not an important advantage, because it seems to offer individual Alaskans stock in a profitable business at no cost to them or to state government for the Corporation's initial equity. Any promise of something-for-nothing depends, however, on the success of an unusual financing plan, whereby AGSOC would pay for its plant and equipment entirely by "non-recourse" borrowing. Part II of our report finds that the outlook for any such financing plan is extremely dim.

The only kinds of business that a GSOC would have much hope of financing with even 75 percent non-recourse debt (not to mention 100 percent debt) is one that has a guaranteed market at a guaranteed price. The industries that meet this test are mostly regulated utilities or facilities serving regulated utilities. But utility property as such is not a particularly promising investment for a GSOC, because the ratemaking process does not let tax-exempt businesses retain the benefits of their tax exemption.

The inability to profit from a GSOC's special tax treatment is the most serious of several flaws in the proposal that AGSOC buy an interest in the Trans Alaska

oil pipeline (TAPS). The most appealing investment opportunities are probably non-utility ventures whose product or services can be marketed on long-term cost-of-service contracts. Examples of such enterprises are the North Slope natural gas conditioning plant, a coal mining venture serving out-of-state electric utilities, or specialized ships built for chartering to oil companies or utilities.

As AGSOC is not likely to finance any major acquisition or investment entirely without state government aid, the form which that aid takes is of considerable importance. We conclude that a direct appropriation of equity is a more efficient and less risky way of arranging a GSOC's initial funding than state loans or loan guarantees.

Part III briefly reviews some of the provisions of the AGSOC legislation concerning shareholding and corporate governance. AGSOC is not a something-for-nothing money machine, as Senator Gravel and the AGSOC Educational Committee seem to imply. Nor is it the gateway to a radical reform of capitalism that Louis Kelso proclaims. And despite the fears of some, an Alaska GSOC is not likely to become a parallel government or a powerful political lobby, or otherwise subvert the integrity of democratic government. Even if GSOCs came to hold a significant block of capital assets in Alaska, their impact on the distribution of wealth and political power would be imperceptible.

A GSOC is one rather arcane form of business organization defined in the Internal Revenue Code, nothing more and nothing less. For each of AGSOC's purported objectives --- avoiding or reducing federal tax liabilities, broadening the ownership of corporate capital, redistributing wealth, privatizing a part of Alaska's oil wealth, or whatever --- there are several alternative measures, some of which may be more familiar, less complex, and more efficient.

AGSOC's enthusiasts have their priorities backward. Alaska's citizens, through their elected representatives, first need to decide what existing industries they want to Alaskanize, what new industries they want to promote, whether or not they want a state investment in the gas pipeline or the conditioning plant, and what balance they want between private and governmental management of the state's resource wealth.

It is only in connection with these decisions that it makes sense to choose a kind of business organization or a financing plan. A GSOC may make sense for some investments --- for many others it surely will not. An approach that calls on the state to set up a very specialized corporate organization, and then to let it loose looking for something to do, is simply topsy-turvy.

PART I. THE GENERAL STOCK OWNERSHIP CORPORATION (GSOC):

TAX ADVANTAGES

The General Stock Ownership Corporation (GSOC) is a creature of United States tax law. Its singular advantage, indeed its only advantage, over an ordinary business corporation is the fact that Subchapter U of the Internal Revenue Code exempts the profits of a GSOC from being taxed twice, first as corporate income and once more as dividends to its shareholders.

With a top rate of 46 percent, the federal corporate tax can leave as little as 54 cents out of each profit dollar earned by an ordinary corporation to be reinvested or distributed as dividends. (State corporate and personal income taxes will of course reduce the shareholder's after-tax benefits even further.) A shareholder who is subject to a 30 percent marginal tax rate on his personal income could thus end with after-tax benefits of only about 38 cents per dollar of earnings:

$$\begin{array}{rcl} & - \text{\$.46 corporate tax (46\%)} & \\ \text{\$1.00 profits} < & = \text{\$.54 after-tax profit (54\%)} < & - \text{\$.162 personal income tax (30\%)} \\ & & & = \text{\$.378 net personal income (70\%)} \end{array}$$

The ability to avoid double taxation under federal law can give AGSOC shareholders a real advantage over shareholders of other corporations that do not qualify under Subchapter U. The earnings of a GSOC, in contrast to ordinary corporate profits, are taxed only once at the federal level --- as personal income to the shareholder. Thus, a GSOC shareholder in the 30 percent federal income tax bracket might be able to benefit from as much as 70 percent of his GSOC profit dollar:

$$\begin{array}{rcl} & & - \text{\$.30 personal income tax (30\%)} \\ \text{\$1.00 GSOC profits} & \text{-----} & \text{\$1.00 dividend (100\%)} < & = \text{\$.70 net personal income (70\%)} \end{array}$$

The GSOC is not the only form of business organization that can avoid having its earnings taxed twice. This ability is shared by proprietorships (single-owner businesses), partnerships, small business corporations under Subchapter S of the Internal Revenue Code, regulated investment companies (mutual funds), cooperatives, and thrift institutions.² The previous comparison, moreover, tends to exaggerate the tax advantage of GSOCs over ordinary business corporations, because:

1. Most corporations can arrange their affairs so that they do not in fact pay the maximum rate of the corporate income tax;

2. The larger part of shareholders' earnings on common stock is not made up of dividends but of capital gains that are taxed only when the stock is sold, and even then at rates that are (at most) one-half of the rates that apply to ordinary income; and

3. Subchapter U creates tax disadvantages as well as advantages:

- a) GSOC dividends do not receive the \$100 exclusion that applies to ordinary dividend income:

- b) A GSOC may not benefit from the investment tax credit (IIC) --- IIC benefits, if any, have to be claimed by shareholders on their personal income tax returns;

- 2) In this context, we cannot ignore the alternative of state- or municipally-owned enterprises, whose earnings are tax free, and which can, in addition, borrow in the tax-exempt bond market. Some government enterprises (like the Alaska Marine Highway and the Alaska Power Authority) exist to provide services to the citizens at a low cost, and others (like the Anchorage Telephone Utility or the Washington State Liquor Board), are operated primarily as sources of revenue. New forms of state enterprise conceivably could be designed to channel income and wealth directly to individual citizens.

c) GSOC shareholders are liable for personal income taxes on their share of GSOC earnings, whether or not the GSOC distributes sufficient dividends to cover this added tax liability;

d) While GSOC shareholders are liable for taxes on their share of its earnings, they may not claim GSOC losses as deductions on their personal income tax returns; and

e) A GSOC that distributes less than 90 percent of its taxable income in any year is subject to an additional 20 percent tax penalty.

One way to consider all these factors together may be to look at the total tax burden on the profits from an identical investment under various forms of business organization. The actual burden in any real-world instance depends upon a large number of factors, and the reader should realize that the figures in this report are only illustrations, and not predictions about the performance of any particular enterprise.

The chief assumptions of the calculations of tables 1 through 7 are that:

1. A company is formed with a net investment of \$1,000 per shareholder;
2. The company is capable of earning 25 percent before taxes on that investment, and also on any funds that it may reinvest;
3. Each year's depreciation is 10 percent of the previous year's cumulative net investment, and all depreciation allowances are reinvested; and
4. The company or its shareholders earn a 10 percent investment tax credit (ITC) on its initial investment and on all reinvested funds.

The tax rate on corporate profits is assumed to be 45 percent, and after-tax benefits to shareholders are calculated for taxpayers at 20 and 50 percent marginal tax rate brackets, with capital gains taxed at half the rate on ordinary income.

Dividend and total earnings after taxes: GSOC vs. an ordinary business corporation. Our first comparison is between a GSOC and an ordinary business corporation, both of which distribute 90 percent of their net earnings as dividends. I have chosen this assumption because the tax law penalizes a GSOC that distributes less than 90 percent of its earnings directly to shareholders.

Table 1 shows the after-tax benefits to a taxpayer in the 20 percent income tax bracket. In year 5, the GSOC pays dividends worth \$207 after taxes, while the ordinary corporation's dividends are worth only \$140 --- a difference of 48 percent. This difference is due to the GSOC's shareholder's avoidance of double taxation.

Table 1. Dividend Earnings After Taxes--
20 Percent Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>ordinary corporation</u>	<u>ratio</u>
5	\$207	\$140	148%
20	\$297	\$197	151%

The total benefits of share ownership reflect total company earnings, which include appreciation in the value of the shares, as well as dividend payments. Again, the GSOC shareholder enjoys a substantial advantage. In the fifth year, GSOC dividends plus book value appreciation are worth \$232, while the corresponding total for the ordinary corporation is only \$168, a difference of 38 percent.

Table 2. Total Earnings After Taxes--
20 Percent Marginal Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>ordinary corporation</u>	<u>ratio</u>
5	\$232	\$168	138%
20	\$336	\$238	141%

As we go up the income scale, however, the picture changes. To a taxpayer in the 50 percent marginal income tax bracket, the advantage of a GSOC over an ordinary corporation is much weaker. Until about the eighth year, after-tax performance favors the ordinary corporation. Even in the twentieth year, GSOC after-tax dividends are only 15 percent higher than those of the ordinary company, and total earnings are 1 percent less.

Table 3. Dividend Earnings After Taxes--
50 Percent Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>ordinary corporation</u>	<u>ratio</u>
5	\$124	\$125	99%
20	\$184	\$160	115%

Table 4. Total Earnings After Taxes

<u>year</u>	<u>GSOC</u>	<u>ordinary corporation</u>	<u>ratio</u>
5	\$145	\$160	91%
20	\$210	\$212	101%

The main reason the ordinary corporation is relatively more attractive to higher-bracket taxpayers is that the personal income tax is a greater part of their total tax burden. Here, the exclusion of the first \$100 of ordinary corporate income (an exclusion not available for GSOC dividends) makes a noticeable difference, as does the fact that capital gains are taxed at a much lower rate than ordinary income.

GSOCs vs. tax shelters for ordinary corporate earnings.

The comparisons above probably overstate the tax advantage of GSOCs over ordinary corporations, because the framework of corporate accounting and the tax laws offer many ways to

reduce the burden of double taxation. Thus the previous cases tend to be "worst-case" examples --- cases of companies without clever managers or tax advisors. The following illustrates the effect of just one simple corporate tax-avoidance device --- but it is one that might well be used by an Alaska state-sponsored enterprise taking a conventional corporate form.

One way to shelter corporate earnings from double taxation is to treat them as interest rather than profits. In the case of the "leveraged" business corporation whose performance we summarize below, the shareholder's original \$1000 in common shares is replaced by \$100 in common shares, plus \$900 in "junior debt" --- in effect a second mortgage on the corporation's assets. This debt is more risky than the company's regular bonds, because it would be the last to be serviced if earnings were insufficient to meet all the firm's obligations. Hence it is reasonable that this junior debt earn a higher rate of return than ordinary corporate bonds --- say 20 percent. In place of dividends alone, the shareholder now receives a combination of dividends and interest.

Interest, like the profits of a GSOC, is not subject to the corporate profits tax, but is taxed only as income to the ultimate recipient. Thus, under our "leveraging" plan, the same corporate revenues suffer a substantially lower tax burden before they reach the investor.

Compare the after-tax dividends plus interest, and the total earnings, of the leveraged corporation with those of the GSOC. In the lowest tax bracket, according to Table 5, the GSOC retains some dividend advantage, but its edge is very much diminished: In the fifth year, GSOC payments are worth \$207 after taxes, while the leveraged corporation produces 97 percent of that figure, or \$200.

Table 5. Dividends and Interest After Taxes--
20 Percent Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>leveraged corporation</u>	<u>ratio</u>
5	\$207	\$200	104%
20	\$297	\$244	122%

Total earnings including the increase in book value are \$232 and \$217 respectively, a difference of only 6 percent between the GSOC and the leveraged corporation. The GSOC's advantage increases somewhat over the years, but is still substantially less than it was in our earlier comparison with a conventional business corporation.

Table 6. Total Earnings After Taxes--
20 Percent Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>leveraged corporation</u>	<u>ratio</u>
5	\$232	\$217	107%
20	\$336	\$270	124%

At higher incomes, the GSOC's advantage in after-tax earnings disappears, and a taxpayer in the 50 percent bracket may receive more dividends after taxes by holding an interest in a leveraged corporation than by owning GSOC shares.

Table 7. Dividends and Interest After Taxes--
50 Percent Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>leveraged corporation</u>	<u>ratio</u>
5	\$124	\$146	85%
20	\$184	\$190	97%

The increase in after-tax total earnings shows a similar picture:

Table 8. Total Earnings After Taxes--
50 Percent Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>leveraged corporation</u>	<u>ratio</u>
5	\$145	\$160	91%
20	\$210	\$212	99%

GSOC's versus small business organization. As noted earlier, a GSOC is not the only kind of business organization that can avoid double-taxation of its earnings. Proprietorships, partnerships, and Subchapter S small business corporations (which are taxed essentially as if they were partnerships), are also permitted to flow their profits through to their owners untaxed.

The Internal Revenue Code provides similar treatment for these three kinds of business organizations, and here we can lump them all together under the heading small business. One essential difference in accounting and tax treatment between GSOCs and small businesses does concern us here: Subchapter U does not permit a GSOC to benefit from investment tax credits (ITC); any tax credits generated by the GSOC investment must be claimed by the GSOC shareholders on their individual income tax returns.

While the owners of small businesses may (and often do) use the ITC as a tax-shelter for income from other sources, there is nothing in the tax code that prevents them from plowing it back into their businesses; and this is by far their most common use for the ITC. The tables assume therefore that small businesses reinvest any ITC they

earn, (together with their depreciation allowances and 10 percent of their taxable income). Any IIC the GSOC earned, however, is treated as an offset to shareholder tax liability --- that is, as part of shareholder after-tax earnings.

As a result, tables 9 through 12 show that a given investment in a small business will yield at least as much current after-tax income and at least as much after-tax total earnings from a given investment as will a GSOC, in all tax brackets. In most cases, the small business form of organization is substantially more effective in sheltering earnings from the federal tax collector.

The fifth-year figures in table 9 show, for example, that a small business can give a low-income taxpayer 9 percent more current after-tax income than a GSOC; the advantage is 29 percent in the 20th year. (In this case, the heading "current income" may cover proprietor's income or partnership income.) The small business has a 16 percent edge in total after-tax earnings in year 5, and a 38 percent edge in year 20.

Table 9. Current Income After Taxes-- 20 Percent Marginal Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>small business</u>	<u>ratio</u>
5	\$207	\$226	92%
20	\$297	\$384	77%

Tables 10 through 12 show similar patterns for after-tax current income in the 50 percent tax bracket, and for total income in both the 20 and 50 percent brackets.

Table 10. Current Income After Taxes--50 Percent Marginal Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>small business</u>	<u>ratio</u>
5	\$145	\$166	87%
20	\$210	\$276	76%

Table 11. Total Income After Taxes--20 Percent Marginal Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>small business</u>	<u>ratio</u>
5	\$207	\$226	92%
20	\$297	\$384	77%

Table 12. Total Income After Taxes--50 Percent Marginal Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>small business</u>	<u>ratio</u>
5	\$124	\$124	100%
20	\$145	\$166	87%

REINVESTMENT OF GSOC EARNINGS

A business corporation normally does not distribute the bulk of its net earnings as dividends, but keeps them inside the firm to finance new investment. This arrangement is in the interest of both the company and its shareholders: On the one hand, internally-generated funds are usually the cheapest source of new equity capital for the firm. On the other hand, the shareholders are able to take most of their profits in the form of long-term capital gains, which are taxed at lower rates than dividend income --- if at all.

Many highly profitable corporations pay at most token dividends. Indeed, the more profitable the company and, especially, the greater its opportunities for growth, the more its shareholders tend to benefit from a policy of keeping dividend payments to a minimum.

Congress, when it enacted Subchapter U, clearly intended that GSOCs not reinvest the bulk of their earnings. Indeed the chief rationale for exempting GSOCs from corporate income taxes was the idea that they would be direct conduits for earnings like mutual funds, and not accumulators of capital.

Despite this explicit intent, the penalty in tax code on a GSOC that accumulates internal capital is remarkably mild: a 20 percent tax on undistributed earnings exceeding 10 percent of taxable income in any one year. This penalty is still less than half the top tax rate --- 46 percent --- on the income of ordinary corporations, whether that income is distributed or retained. Thus, the frequent assertion that Subsection U prohibits GSOCs from reinvesting their earnings is inaccurate, and we shall see in the following tables what happens to the after-tax dividends and total after-tax earnings of a GSOC that reinvests a substantial part of its profits.

Tables 13 through 16 compare the after-tax earnings on a \$1000 net investment by (1) a GSOC; (2) an ordinary business corporation, all of whose income is exposed to the top rates of the corporate tax; (3) an ordinary business corporation in which the owners each contribute \$100 as common equity and \$900 as junior debt at an interest rate of 20 percent in lieu of \$1000 equity; and (4) a small business taxed as a proprietorship, a partnership, or a Subchapter S corporation. In each case, a firm reinvests 50 percent of its net earnings, in addition to its depreciation allowances and (except for the GSOC) its IIC.

In most respects the results are just what we would expect from Tables 1 through 10. In general, GSOCs produce more after-tax income and grow faster on the same initial investment than ordinary business corporations, and small businesses earn more and grow faster than GSOCs. The contrasts between the figures in Tables 11 through 14 and those of Tables 1 through 10 reflect the general principle that reinvesting means sacrificing current income for future income or capital gains. Comparing Table 11 with Table 1, for example, it is not surprising that reinvesting 50 percent of earnings yields a lower after-tax dividend in year 5 than reinvesting only 10 percent, except in the case of the "leveraged" corporation.

Table 13. Current Income After Taxes, Fifth Year--
20 Percent Marginal Tax Bracket

<u>Reinvestment of percent earnings</u>	<u>GSOC</u>	<u>ordinary business corporation</u>	<u>"leveraged" corporation</u>	<u>small business</u>
10%	\$207	\$140	\$200	\$226
50%	\$119	\$103	\$200	\$139

The contrast in year 20 dividends per share between a corporation which always reinvests half of its income and one that invests only 10 percent is a dramatic illustration of the power of compounding. The reason the leveraged corporation shows its best dividend performance relative to a GSOC in its early years and the poorest comparison in the later years is its large fixed payout (\$180 per share) in the form of interest, and thus the relatively lower proportion of the leveraged corporation's total earnings (profit plus interest) that is reinvested.

Table 14. Current Income After Taxes, Twentieth Year--
20 Percent Marginal Tax Bracket

<u>reinvestment</u> <u>(percentage of</u> <u>taxable income)</u>	<u>GSOC</u>	<u>ordinary</u> <u>business</u> <u>corporation</u>	<u>"leveraged"</u> <u>corporation</u>	<u>small</u> <u>business</u>
10%	\$297	\$197	\$244	\$ 384
50%	\$698	\$306	\$247	\$1,083

The impact on after-tax total earnings of a high reinvestment rate is even greater than its effect on after-tax dividends. In the 20 percent tax bracket the difference is notable even in year 5.

Table 15. Total Earnings After Taxes, Fifth Year--
20 Percent Marginal Tax Bracket

<u>reinvestment</u> <u>(percentage of</u> <u>taxable income)</u>	<u>GSOC</u>	<u>ordinary</u> <u>business</u> <u>corporation</u>	<u>"leveraged"</u> <u>corporation</u>	<u>small</u> <u>business</u>
10%	\$238	\$168	\$217	\$270
50%	\$299	\$220	\$250	\$383

The higher reinvestment rate of course has an even more dramatic impact on total earnings in the 20th year.

Table 16. Total Earnings After Taxes, Twentieth Year--
20 Percent Marginal Tax Bracket

<u>reinvestment (percentage of taxable income)</u>	<u>GSOC</u>	<u>ordinary business corporation</u>	<u>"leveraged" corporation</u>	<u>small business</u>
10%	\$ 336	\$238	\$270	\$ 462
50%	\$1,658	\$708	\$466	\$2,990

THE DANGER OF CASH DEFICIENCIES

Table 17 shows one especially striking implication of choosing to operate a company under Subchapter U of the tax code. A GSOC or a small business that invests 50 percent of its earnings generates no after-tax income at all for a shareholder in the 50 percent tax bracket. In a sense this situation is equivalent to that of an ordinary corporation that retains and reinvests 100 percent of its net income.

In contrast to owners of ordinary common stock, however, GSOC shareholders are liable for personal income taxes on their share of the GSOC's earnings whether or not the GSOC distributes dividends, and totally without respect to any dividends that the GSOC does distribute.

Table 17. Current Income After Taxes, 50 Percent Reinvestment--
50 Percent Marginal Tax Bracket

<u>year</u>	<u>GSOC</u>	<u>ordinary corporation</u>	<u>"leveraged" corporation</u>	<u>small business</u>
5	-1	79	102	0
20	-3	288	212	0

In table 17, therefore, we see a major danger to shareholders arising from the very aspect of the GSOC that makes it an attractive form of business organization --- "tax integration" --- together with a serious limitation on the GSOC's management and investment flexibility.

In at least one plausible combination of circumstances, therefore, the sum of GSOC dividends and ITC are barely enough --- or not quite enough --- to cover the additional personal tax liability that the GSOC's earnings have created for its shareholders. This situation can be expected to arise, under the assumptions used in this analysis, any time reinvestment of earnings approaches 50 percent.

Actually, Table 17 understates the seriousness of this potential problem because:

1. The table assumes that the GSOC passes on to its shareholders substantial ITC benefits every year, which can be used to offset additional tax liabilities. It is quite probable, however, that a large part of GSOC investment will be in assets such as land, existing plant and equipment, and working capital which do not generate any ITC.

2. The table assumes there are no claims against GSOC earnings other than reinvestment and payment of dividends --- specifically that depreciation allowances will always generate enough cash to amortize any outstanding debt.

3. There is nothing in the GSOC scheme that rules out a situation in which the corporation earns a taxable income --- and thus creates a tax liability for its shareholders --- and yet is unable to pay them sufficient dividends to offset that tax liability.

It will be intolerable if any group of shareholders is put into a negative cash position as a result of owning GSOC stock. Such a situation clearly can come about, however,

with reinvestment rates considerably less than 50 percent, and there are plausible circumstances in which it might arise even if there were no reinvestment at all.

Consider, for example, a GSOC that had to pay off initial borrowings of \$1,000 per share out of its earnings over a period of ten years. Assume that it earns only 15 percent, or \$150 per share, instead of the 25 percent projected by its organizers (which would have permitted the GSOC to pay sufficient dividends to cover the additional tax liabilities for all classes of shareholders). Only \$50 per share thus remains for distribution as dividends --- and to pay the 20 percent added tax Subsection U imposes on undistributed earnings in excess of 10 percent of taxable income. The maximum dividend payment would therefore be \$28.75 per share.

Table 18. GSOC Income Available for Distribution (per share)

<u>Taxable income</u>	\$150.00
(Less) amortization	100.00
(Less) penalty tax	<u>21.15*</u>
 <u>Available for Distribution</u>	 \$ 28.75

*[20% x (90% x \$150.00 - \$28.75)]

The shareholders' tax liability does not depend upon the dividends they actually receive, however, but upon their portion of the corporation's taxable income, which is \$150 per share. Thus, owning a GSOC share will increase each shareholder's tax bill. A taxpayer in the 20 percent bracket will have to pay an additional \$30.00 per share in personal income taxes, while a taxpayer in the 50 percent bracket will have to pay \$75.00. Both of these figures exceed cash flow available to the GSOC for payment of dividends.

Table 19. GSOC Dividends and Shareholder Tax Liability

<u>marginal tax bracket</u>	<u>dividends</u>	<u>increased tax liability</u>	<u>income deficiency</u>
20%	\$28.75	\$30.00	\$(1.25)
50%	28.75	75.00	(46.25)

In this quite plausible instance, therefore, ownership of GSOC shares has put taxpayers of every bracket into a negative cash position. This scenario is not the worst possible one; the reader can surely conceive of even more troublesome situations.

There is little doubt that a GSOC can theoretically be capitalized and operated so as to avoid any danger that the personal tax liabilities of any shareholder group would ever exceed its dividend distributions. To be quite safe, however, such a GSOC probably must ---

1. Limit its borrowing, both for its initial capitalization and for expansion, to levels at which the GSOC can meet its debt service obligations out of depreciation allowances alone in all events, without ever having to rely on taxable income;
2. Begin with and keep a substantial equity cushion in the form of initial paid-in capital and surplus, or retained depreciation allowances and profits; the GSOC will have to maintain such a reserve in order to cover any short-term losses and to pay sufficient dividends in every year to cover each shareholder's tax liabilities if, for any reason whatsoever, there is not sufficient cash flow from current operations; and
3. Give up any notion of financing its expansion out of retained earnings.

A GSOC's tax advantages, in brief, comes at a high price to the corporation in flexibility regarding the kind of business it can operate, in the range of prudent capital-

ization plans available to it, and in the ability to respond to new investment opportunities. In many instances, surely, these costs will more than offset the benefits of operating under the provisions of Subchapter U. Indeed, we cannot be certain that there is any kind of investment in Alaska, or any strategy for distributing private wealth more broadly among individual Alaskans, for which a GSOC is clearly the most suitable form of business organization.

PART II. AGSOC FINANCING AND INVESTMENT STRATEGY

HOW IS AGSOC TO BE FINANCED?

AGSOC's advocates intend that individual Alaskans will each receive at least one share of stock at no charge to them. Whether the AGSOC financing plan requires the use of state government revenues is not so easy to determine.

Until recently, state loan guarantees were clearly a crucial part of the AGSOC concept. For example, Senator Gravel's press release of March 29, 1978 stated:

What [Mr. Kelso] has proposed, basically, is this: the people of Alaska could, through the offices of the state, form a corporation which would finance and own a portion of the new pipeline. The state would assist in securing the money which would establish the corporation, and the money would be paid back to the lenders out of the profits generated by the pipeline. [emphasis added]

Senator Gravel, in his April 10, 1978, Response to Several Questions Concerning the Alaska General Stock Ownership Plan, answered one question as follows:

Up front cash, a question also raised, need not be required. The only State appropriation required would be for the study, so that the Alaskan GSOP could be properly launched. Any operating or investment monies that it needs could be borrowed. The loans in question, at the beginning, would have to have a State government guarantee, but not an appropriation. In fact, the Alaskan GSOP could even repay the moneys expended by the State in setting it up. The guarantee, if the investment is sound, need pose little risk . . . [emphasis added]

Louis Kelso, et al., in a February 1979 report, Design of an Alaskan General Stock Ownership Plan, included a proposed "Act Establishing Alaska General Stock Ownership

Corporation." Section 11 of the draft provided for special sessions of the legislature and special elections to approve state treasury backing for AGSOC projects:

Section 11. SPECIAL SESSION TO APPROVE FINANCING. It is the intent of the legislature that at such time as AGSOC comes forward with a request for project financing that the Governor shall call a special session of the legislature to consider such request. . . . In the event that the legislature shall determine that financing or the guaranty of financing for an AGSOC project is necessary or desirable, the legislature shall at the earliest convenient time call a special election . . . for voting on the approval of the extension of credit to AGSOC by the State of Alaska, or the guarantying [sic] by the State of Alaska or by any agency or instrumentality thereof of the credit of AGSOC.

In support of the bill, the Kelso report offered the following "Analysis Recommended for Inclusion in the Legislative Financial Committee Report to Accompany the AGSOC Bill:"

The average citizen does not have effective access to credit for capital formation because he does not have existing wealth to guarantee the lender's risk. However, joined together with his fellow citizens through his State government he has tremendous borrowing power. The security of a State guarantee can perform the same guarantee function for the average citizen which existing capital does for the wealthy. Through the power of State government the typical citizen can leverage himself into a capital asset which will pay for itself and throw off income to him and his neighbors and his children. [emphasis added]

Recently, however, publicity efforts in favor of AGSOC have begun to downplay or disavow any notion that a GSOC would require state financial support (other than for its initial organizing expenses). At a hearing of the House Finance Committee on November 2, 1979, for example, Senator Gravel argued at length that AGSOC had nothing in common with Governor Hammond's proposed energy credits or Alaska, Inc., because AGSOC was not a plan to distribute benefits of

the state's oil wealth among private citizens. AGSOC, Senator Gravel insisted, did not depend on state revenues in any way, and he specifically objected to the assumption that AGSOC would require state loan guarantees for its initial capitalization: "It is a concept just as valid for Chad as for Alaska."

The AGSOC Educational Committee's recent campaign brochure, "It's Time to Take Stock in Alaska", is categorical on this point:

Once AGSOC was formed, it would operate independently of the state.

AGSOC would borrow money from banks, insurance companies and other large institutional investors. These lenders would loan their money on the strength of investments proposed by AGSOC and eventually on the financial strength of AGSOC itself.

If any AGSOC investment should fail, the lenders would not be able to recover any money from the shareholders. They could only look to the AGSOC itself for AGSOC debts. [emphasis in original]

Senator Gravel's current campaign for AGSOC and the propaganda of the AGSOC Educational Committee thus clearly reject the notion that the Corporation's financing will depend upon a state equity contribution or state loan guarantees. But the question is not thereby laid to rest. In the following pages, we shall examine whether or not 100 percent non-recourse debt financing is a realistic hope for AGSOC under any circumstance, and if so, for what kinds of investments. To the extent that AGSOC can not be capitalized without a direct appropriation or guarantees from the state, however, we shall consider the implications of such assistance, both for the state budget and for AGSOC's shareholders.

PRINCIPLES OF FINANCING

All investments are risky, and some are riskier than others. Business risks include market setbacks that can be unique to a particular firm or reflect general economic conditions; increased costs for labor, materials or services; accidents, strikes, and disasters; management mistakes, incompetence or dishonesty; unpleasant surprises from new technologies or unfamiliar environments; cost overruns or delays in plant construction or in delivery of equipment; and changes in laws, regulations, or taxes.

The first principle of debt financing is that lenders do not voluntarily assume any of these risks. Of course, some borrowers do become delinquent or default on loans; the spread in interest rates charged to different borrowers reflects this experience. In order to minimize risk, however, business lenders invariably require one, and usually both, of the following assurances:

1. The venture's projected cash flow from current operations must be sufficient to make all scheduled payments of principal and interest on time --- even under the worst plausible circumstances, and with some margin to spare; and

2. The borrower or a creditworthy third party must pledge sufficient collateral in the form of saleable assets or unrelated income to pay off the entire loan plus accumulated interest, even if the venture in question fails totally, i.e., generates no cash flow.

These requirements are normally met by the borrower's equity in the venture. Investors expect the return of and on equity to provide the business with a substantial margin of cash flow in excess of its fixed costs, which include repayment of principal and interest on debt. Hence, profits

may fall drastically, or the business may even run considerable losses for a long time, before it can no longer cover its debt service obligations out of current revenues. The shareholders' equity itself provides collateral that lenders can attach and liquidate if necessary, should the business fail to generate enough cash to meet its obligations.

It follows, therefore, that the more equity there is in a company's capital structure, the less likely it is that revenues will fail to cover operating expenses and debt service. Conversely, the more leveraged a firm's capital structure, that is, the higher the percentage of debt, the greater the danger that, for some reason, revenues will not be adequate.

For this reason, the financing of business ventures with anything approaching 100 percent debt (as Senator Gravel now proposes for AGSOC acquisitions) is extremely rare. Most firms have a capital structure about evenly divided between equity and debt. The 1978 debt of the top 50 manufacturing companies in the Fortune 500, for example, was 51 percent of their total assets; only 7 of the 50 had debt ratios greater than 60 percent. Even for the 50 top utility companies, debt was only 62 percent of total assets, and among them there were just two that had debt ratios exceeding 75 percent.

In support of their claim that AGSOC could finance its acquisition of business plant and equipment entirely with non-recourse borrowing, Senator Gravel and other AGSOC advocates have cited examples of several kinds of financing that seem to contradict the principles we have outlined, but it is important to look carefully at such examples. The following cases illustrate most of the circumstances in

which individuals, firms, or governmental entities are able to make highly leveraged investments. In very few of the examples is the borrower truly exempt both from contributing substantial equity to the venture, and from pledging some other kind of security in place of equity.

PROJECT FINANCING: ELEVEN CASES

Case 1: Commercial real estate. An Anchorage businessman buys an office building for \$1 million --- and a friendly local banker assigns the property a value of \$1.4 million in order to lend the buyer \$1.15 million. The building is fully leased, so that its cash flow can easily cover payments on a mortgage of this amount. Our businessman not only acquires an income-generating asset with no down payment, but walks away from the closing with \$150,000 in cash!

Can the buyer truly finance such a purchase without any equity investment? Is the bank really assuming the risk that the building may be half-empty next year and thus fail to bring in enough cash to cover the mortgage payments? Not really, because the buyer, who has a net worth of \$3.5 million, personally signed the note. The bank's security for its \$1.15 million is, therefore, not a building worth \$1 million, but \$4.5 million --- the value of the building plus the owner's net interest in other properties.

Case 2: Commercial real estate. A Texas oil billionaire buys and finances an Anchorage commercial building on the same terms as the local businessman in Case 1, but in this instance the Texan does not personally sign the note.

Is this a case of 100 (or 115) percent debt financing? Not quite, because the oilman's total income and assets are implicit security for the loan, at least as good as the borrower's signature in Case 1. The bank has no reason to doubt the borrower's ability or his motivation to pay, even if the investment in question turned out to be a bad one: For him to renege on this relatively small loan would be a near scandal, and would cost the oilman more in damage to his business reputation and credit standing than he would save by defaulting on the debt.

Case 3: Oil pipeline. The oil companies that built the IAPS oil pipeline each financed its own share of the project with 90 to 100 percent borrowed funds.

Are the owner companies' equity contributions really less than 10 percent of the pipeline's total cost? This case is just like Case 1: Each of the companies put its entire worldwide assets at stake, so the 40 to 60 percent debt ratios of the parent companies are the real capital structure, not the apparent 90 to 100 percent debt covered on the books of their pipeline subsidiaries.

Case 4: Electrical generating plant. An electric utility builds a new generating plant, and sells bonds that pay the entire cost of the facility.

Is this a 100 percent debt financing? Once more, not really, because the debt is secured by the utility's other assets and its total income. The willingness of lenders to fund the new plant will not depend on the income from that facility alone, but rather on the projected coverage ratio for the utility's entire operations. Each future year's cash flow available for debt service must be some multiple of --- usually at least twice --- its anticipated debt service requirement.

Case 5: Electrical generating plant. A consortium of electric utilities has formed a joint venture to build a new generating plant. The plant is project-financed: The utilities establish a new corporate entity financially independent of all the sponsoring companies. The new corporation then borrows 100 percent of its long-term capital needs on a non-recourse basis, meaning that the parent companies do not guarantee the debt.

Surely this is a true 100 percent debt financing? Yes and no. Lenders have no direct recourse against the sponsoring utilities' other assets in event of default, but project financing is possible only because the utilities have signed all-events, minimum-bill contracts to buy the project's electrical output.

In some instances, lenders prefer this form of project financing to conventional balance-sheet financing, because regulatory commissions and bankruptcy courts will allow the parent utility to continue paying its operating costs which include current costs for the purchase of electricity even if the parent utility's own bonds are in default. This arrangement in effect makes the cash outlay serving the project's bonds senior to all debt instruments previously issued by the sponsoring utilities.

An absolute prerequisite for this form of non-recourse project financing of gas or electric utility investments is perfect tracking --- arrangements guaranteeing that no regulatory commission will ever prevent the utilities who sign all-events, minimum-bill service agreements from passing these charges on to final consumers, no matter how many separate transactions and regulatory jurisdictions may be involved.

Case 6: LNG terminal. A group of gas utilities are jointly building a terminal to receive liquefied natural gas (LNG) by tanker and to regasify it for delivery into their gas distribution networks. Long-term financing will be 25 percent equity and 75 percent non-recourse debt, secured by full-cost-of-service-contracts signed by the sponsoring utilities and approved by the state and federal regulatory commissions that have jurisdiction over the utilities.

The commissions have turned down sponsors' requests to begin customer billing for servicing debt during the construction phase. Instead of putting construction work in progress (CWIP) into their present rate base the companies must capitalize the allowance for funds used during construction (AFUDC) --- the return to debt and equity accrued during the construction period --- and begin billing consumers only after the plant goes into service. Thus the lenders can be expected to insist upon external loan guarantees during the construction phase, though they may be willing to accept non-recourse financing terms once operations begin.

Case 7: Ship construction. A group of investors has formed a limited partnership to build and charter an oil-industry service vessel (a heavy-duty ocean-going tug for moving and servicing offshore drilling rigs). Financing for the \$2 million vessel will consist of a conventional 12 year bank loan for 65 percent of the cost and a 5 year second mortgage from a finance company for 25 percent. Taking the 10 percent investment tax credit (IIC) into account, the investors will not have to make any long-term equity contribution, and they might even recover all of their organizational and promotional expenses out of the loan proceeds.

How can these investors manage without equity? Collateral for a 65 percent conventional loan is the value of the vessel itself. Since the ship's value is insufficient to serve as collateral on the second mortgage as well, a boat charter to a major oil company assures the necessary cash flow for a period of three years to cover payments on both loans. The holder of the second mortgage insists, however, on some security for the fourth and fifth year payments on his loan; to accomplish this, he requires the owners (during the three year charter period) to set aside a certain part of their profits in a sinking fund which can meet the fourth and fifth year payments if necessary.

Case 8: Ship construction. A transportation company built a \$50 million U.S. flag tanker with an equity contribution of only \$2.5 million, without a charter and indeed without any clear idea of where the tanker will be used.

How? Seventy-five percent of the total price was borrowed from financial institutions on the strength of a U.S. Maritime Administration (Marad) loan guarantee under Title XI of the Merchant Marine Act. Another 10 percent was a direct loan by another federal agency that was trying to preserve shipyard jobs in a community with high unemployment rates. Addition of the 10 percent Investment Tax Credit left the owners with a need to supply only five percent of the project cost from their own resources.

Case 9: Public works. A school district plans to sell bonds for a construction program and to finance the construction entirely out of the bond proceeds.

Is this 100 percent debt financing? Once more, yes and no. Because the bonds are "general obligation" bonds, they are backed by the school district's taxing authority. The marketability of the bonds depends upon the lenders' assess-

ment of the district's tax base, its other debt service obligations, and its legal and political capacity to levy whatever taxes are necessary to service the debt.

Case 10: Public works. A state toll road authority sells bonds to finance turnpike construction, and pays for that construction entirely out of loan proceeds.

Is this 100 percent debt financing? Maybe. The bonds are revenue bonds, secured completely by tolls without recourse to the state's general fund. The ability of the authority to sell these bonds, however, depends upon convincing lenders that tolls from the project will be sufficient to cover all debt service obligations with some margin of safety and that the authority is legally and politically capable of increasing tolls on this project or on others in order to make up any deficit.

Case 11: Housing.

(a) In the late 1960's and early 1970's some prominent banks formed real estate investment trusts (REITs) to develop rental housing and condominiums. The REITs were 80 to 100 percent capitalized by loans from a variety of financial institutions and individuals. In the mid-1970's, however, cost overruns, construction delays, and high vacancy rates caused a number of REITs to fail, costing the lenders hundreds of millions of dollars.

(b) The government of an eastern state formed a public corporation to build middle-income housing. Construction was funded entirely by sale of bonds that were to be serviced from rent receipts. Here again, cost overruns, construction delays, high vacancy rates, and tenant resistance caused the housing corporation to become delinquent in its debt service payments, creating substantial losses for the bondholders.

Why did the lenders make such poorly-secured loans? In each case, they thought that the debt carried an implicit guarantee from a creditworthy sponsor as in Case 2. In the first instance, the association of prominent banks with the REITs led lenders into assuming these banks would take responsibility for REIT debts. In the case of the state housing corporation, the governor (who was himself a financier of sorts) had styled the corporation's debt as "moral obligation bonds," despite the fact that the bonds themselves provided no explicit recourse against the "full faith and credit" of the state. Ironically, some of the same banks that walked away from the debts incurred by their REITs were fooled into believing that the state government would stand behind its own housing subsidiary.

. . . AND THEIR IMPLICATIONS

The preceding examples show that it is indeed possible to borrow all or almost all the funds needed for a business venture, but only if:

(1) The debt is secured by recourse against other assets or income of the borrower, either express (cases 1 and 3) or implied (cases 2 and 11), or by a guarantee from a creditworthy third party (such as the federal government in case 8);

(2) The debt service is assured by a contract that commits creditworthy purchasers to pay the venture's full cost of service, or at least to pay a minimum bill that covers its fixed costs "in all events," or "come hell or high water" (cases 5 and 6); or

(3) The borrower is (a) a regulated utility, fully assured that the regulatory authorities will allow it whatever rates may be necessary to service its debt (case 4), or (b) an unregulated monopoly or a governmental body with the power to set its prices or levy taxes, at whatever level may be necessary to service its debt (cases 9 and 10).

While these three conditions do not absolutely rule out any possibility of financing AGSOC ventures without either a state appropriation or a state loan guarantee, they do stringently narrow the investment options for any state-sponsored enterprise that starts without equity and without the ability to pledge the state's credit.

Our cases illustrate at least two more principles relevant to the outlook for financing AGSOC investments:

(1) With a governmental loan guarantee, it is possible to borrow even on a patently unsound business enterprise, like the shipbuilding venture in case 8 (or the Chrysler Corporation's 1981 model year). The state's credit is thus capable of making almost any AGSOC enterprise financible, but it does not thereby make it a sound venture.

2) It is sometimes possible to persuade lenders that an implicit loan guarantee from government exists for bonds that are really only revenue bonds, or that an implicit guarantee from a creditworthy entity attaches to loans that on their face are non-recourse debt.

Conceivably, therefore, AGSOC could borrow more money for one of its business ventures than would normally be prudent for either AGSOC or the lenders, but only on the condition the loan were guaranteed by the state treasury, or where the lenders believed that AGSOC's political influence (or the state government's fear of damage to its own credit standing) would force the state to cover AGSOC's debts even in the absence of a legal obligation to do so.

Notwithstanding the possibility that AGSOC's initial investments could be financed with 100 percent non-recourse debt on the strength of the state's "moral obligation" alone, the probability is very small --- because of recent experiences like those of case 11, because of the capital market's unfamiliarity with GSOCs as a form of business

enterprise, and because of the political controversy in which an Alaska GSOC would likely be born, and the controversy that would certainly surround it if it got into financial trouble.

PUBLIC UTILITY INVESTMENTS

The preceding discussion leads toward one strong conclusion about AGSOC financing: The only kind of business that a GSOC has much hope of financing with a capital structure containing even 75 percent (not to mention 100 percent) non-recourse debt, is one with a guaranteed market at a guaranteed price. This probably means either regulated utility property, or facilities serving regulated utilities through long-term, cost-of-service contracts.

The fact that almost every urban transit company and most of the major railroads in the United States have gone into bankruptcy at one time or another is ample evidence that regulated industries are not necessarily riskless enterprises. Electric, gas, and telephone utilities have tended to be relatively safe investments, however, because (until recently) they have enjoyed the lucky combination of rapidly expanding demand and falling real costs. Nevertheless, risks do exist even in these industries. While new project-financed gas or electric ventures secured by all-events, minimum bill service agreements have managed to obtain financing based on only 25 percent equity, the typical utility company has had to maintain about 40 percent equity in its overall capital structure. The various segments of the Alaska Highway gas transportation system, all to be owned by newly-created entities of utilities and others, plan ratios in the vicinity of 75/25.

Where a project's revenues are effectively guaranteed by regulation or by a long-term contract with a regulated utility, lenders are much less concerned about the project's capital structure. Instead, they scrutinize its coverage ratio --- the cash flow available for debt service as a multiple of the total debt service obligation. Here, a GSOC might appear to have a distinct advantage over a conventional firm; the following discussion will show why.

Implications of GSOC's tax exemptions. As we noted in Part I of this report, the singular advantage of a GSOC over an ordinary business corporation is the fact that Subchapter U of the Internal Revenue Code exempts the GSOC's profits from being taxed twice, first as corporate income and once more as dividends to shareholders. To the extent AGSOC does not pay federal income taxes, more cash should be available out of a given stream of revenues to service debt than would be the case for a fully taxable company.

Consider, for example, a project-financed investment with a cost of \$1 billion undertaken by a conventional corporation and a GSOC respectively. Assume that:

- (1) Either venture would produce a contractually-guaranteed net operating income (revenues less operating costs) of \$250 million;
- (2) Interest is 10 percent annually, and debt is amortized on a straight-line 20 year schedule; and
- (3) The GSOC pays no corporate income taxes, while the ordinary corporation's earnings are taxed at 45 percent.

Suppose that lenders demand a coverage ratio (a ratio of current cash flow to debt service requirements) of 1.9 or higher on this kind of project. The table below shows that

an ordinary corporation would be able to borrow about 75 percent of its capital requirements and a GSOC about 85 percent, without bringing their respective coverage ratios below 1.9.

Table 20. Cash Flow: GSOC Versus An Ordinary Corporation
(millions of dollars)

		<u>ordinary corporation</u>	<u>GSOC</u>
a	Equity	\$250	\$150
b	Debt	\$750	\$850
c	Net operating income	\$250	\$250
d	(Less) depreciation	100	100
e	(Less) interest	75	85
f	Taxable income (c - d - e)	<u>\$ 75</u>	<u>\$ 65</u>
g	(Less) corporate tax 45% of f	33.75	0
h	Net income (f - g)	<u>\$ 41.75</u>	<u>\$ 65</u>
i	Debt amortization	\$ 37.50	\$ 42.50
e	Plus interest	75.	85.
j	Total debt service (i + e)	<u>\$112.50</u>	<u>\$127.50</u>
d	Depreciation	\$100	\$100
e	Plus interest	75.	85
h	Plus net income (f - g)	41.75	65
k	Available cash flow (d + e + h)	<u>\$216.75</u>	<u>\$250</u>
l	Coverage ratio (k/j)	1.92	1.96
m	Return on equity (h/a)	16.5%	43.3%

Note that the GSOC's preferential corporate tax treatment results in an after-tax rate of return to shareholder equity almost three times that of the conventional corporation, but that the GSOC is still unable to get by completely without equity of its own. In the real world, a GSOC's advantage would probably be much less than the illustration above suggests, because:

1) As noted in Part I, few conventional corporations are actually taxed at the maximum rates of the corporate income tax.

2) A conventional corporation can benefit directly from the investment tax credit (ITC), while a GSOC can not. (Any ITC earned by a GSOC must be claimed by its shareholders on their personal tax returns.) This feature alone may completely negate the apparent advantage the GSOC's corporate tax exemption gives it in financing!

3) The GSOC's apparent advantages in Table 20 both in financing and in return to equity, depend entirely upon the questionable assumption that the state or federal regulatory commission having jurisdiction over a GSOC-owned utility project would permit it to retain its tax savings rather than requiring them to "flow-through" for the ratepayers' benefit.

Considering only the role of the ITC, the effective sources of investment funds for the two firms described previously will be changed to the following:

Table 21. Financial Requirements, GSOC Versus Ordinary Corporation

	<u>ordinary corporation</u>	<u>GSOC</u>
a Equity	\$150 Mil.	\$150 Mil.
a' Investment tax credit	100	0
b Debt	750	850

All other figures on the two income statements would remain the same except the bottom line. The GSOC's financial advantage has disappeared, but it still has an edge in rate of return to shareholder equity (though considerably reduced):

h Net income	(f-g)	\$ 41.75	\$ 65
m Return to equity	(h/a)	27.8%	43.3%

Allowed earnings of regulated utilities. The reasoning and behavior of regulatory commissions are neither wholly uniform nor wholly predictable, and the various state and federal regulatory commissions differ greatly in their treatment of tax issues, for example accelerated depreciation. But it is quite unlikely that any commission having authority over a utility investment in Alaska would leave AGSOC's federal tax savings intact.

Most commissions (including the Federal Energy Regulatory Commission [FERC] in its jurisdiction over wholesale electricity transactions and the interstate transportation of natural gas, and the Alaska Public Utilities Commission [APUC], in its jurisdiction over the distribution of locally-produced gas and electricity in Alaska) treat income tax liabilities as a specific component of the utility's cost of service. Thus, if the utility's tax liability is reduced or eliminated, its rates will be reduced by exactly the same amount.

Suppose, for example, AGSOC were to own a major hydroelectric or coal-fired generating plant in Alaska. The Alaska Power Administration (federal), the Alaska Power Authority (state), the Anchorage and Fairbanks municipal utilities, or the Golden Valley and Chugach Electric Associations (cooperatives) are also tax-exempt. None of these utilities charges its ratepayers for non-existent corporate taxes. None of them computes the interest on its tax-exempt bonds or low interest loans from the United States Treasury at the rates they would have had to pay private lenders in the taxable corporate bond market. How then, could APUC justify allowing an AGSOC-owned utility project to add taxes that it does not pay to the bills it sends Alaska consumers?

Consider, alternatively, a project whose ultimate ratepayers are mainly consumers outside Alaska, as would

be the case with an AGSOC investment in TAPS or the Alaska Highway gas pipeline. Once again, FERC builds up a regulated firm's allowable rates out of specific cost elements, including corporate income taxes.

Treatment of ITC. While regulatory commissions normally require a flow-through of any tax exemption to the ratepayers, the Internal Revenue Code virtually prohibits a flow-through of the investment tax credit. The law denies ITC to any utility if the regulators reduce either the size of its rate base or the rate of return to that rate base on account of the ITC. In the incentive rate of return (IROR) proceeding for the Alaska natural gas transportation system, for example, FERC interpreted the tax law as compelling it to ignore the ITC totally in setting the pipeline tariff. Thus, the joint effect of utilities law (flow-through of tax exemptions) and the tax code (no flow-through of ITC) may be fatal to AGSOC as a vehicle for investment in regulated industries.

Assume, for example, that FERC or APUC allowed an AGSOC-owned project to collect the only same 16.5 percent rate of return to equity it found fair and reasonable for the conventional private utility whose accounts are summarized in Table 20 and repeated in the first column of Table 22 below. The second column shows that the GSOC could not actually borrow 85 percent of its capital requirement as we assumed in Table 20, because its resulting debt service coverage ratio would be only 1.65. Thus, the GSOC's borrowing capacity would be only 75 percent of its total investment, just like that of the ordinary corporation.

But, as we can see in the third column below, the GSOC's effective loss of the corporate tax advantage with respect to utility investment would leave it with an earnings capability even less than that of an ordinary corporation.

TABLE 22. Effect of Flow-Through and Investment Tax Credit on GSOC and Ordinary Utility Cash Flow

(millions of dollars)

		ordinary corporation	GSOC 85% debt	GSOC 75% debt
a	Equity	\$150	\$150	\$250
a'	Investment tax credit	100	0	0
b	Debt	750	850	750
c	Net operating income	\$250	\$209.75	\$216.75
d	(Less) depreciation	\$100	100	100
e	(Less) interest	10% of debt	75	75
f	Taxable income	(c - d - e)	\$ 75	\$ 41.75
g	(Less) corporate tax	45% of f	33.75	0
h	Net income	(f - g)	\$ 41.75	\$ 41.75
i	Debt amortization	5% of debt	\$ 37.50	\$ 37.50
e	Plus interest	10% of debt	75	75
j	Total debt service	(i + e)	\$112.50	\$112.50
d	Depreciation	\$100	\$100	\$100
e	Plus interest	10% of debt	75	75
h	Plus net income	(f - g)	41.75	41.75
k	Available cash flow	(d + e + h)	\$216.75	\$216.75
l	Coverage ratio	(k/j)	1.93	1.93
m	Return on equity	(h/a)	27.8%	16.5%

To summarize the preceding pages, it appears that:

- 1) The chance of AGSOC financing major investments with 100 percent non-recourse debt is virtually non-existent.
- 2) The only investments AGSOC is likely to finance with a high proportion (75 percent or more) of non-recourse debt are projects with a contractually-guaranteed market and price over the life of the debt;

3) Non-recourse financing will be available even under these circumstances only for completed projects, projects that have virtually no risk of prolonged delay, non-completion or premature abandonment, or projects in which the customers accept these risks; and

4) A GSOC's special tax treatment does not give it any advantage, and may in fact be a handicap, in financing regulated utility projects.

The preceding pages examined the opportunities and limitations for a GSOC with respect to general classes of investments and financing schemes. Now we shall look at the prospects for making specific investments, including those that have been proposed by the most prominent sponsors of the AGSOC concept.

BRITISH PETROLEUM'S INTEREST IN TAPS

The investment most often suggested by Senator Gravel and other advocates of AGSOC is the British Petroleum (BP) interest in the Trans Alaska pipeline system (TAPS). BP retains a 15.84 percent undivided interest in the pipeline, despite the fact that it has transferred its operating interest in the Prudhoe Bay field, and a 33.34 percent interest in TAPS to its affiliate, Sohio. BP officers have hinted that the company would be willing to sell its interest if the terms were right, and have held preliminary discussions with Senator Gravel, Alaska state officials, members of the legislature, and investment advisors regarding possible terms.

TAPS is an undivided interest pipeline, which is (curiously) the term for a joint-venture pipeline in which each of the several owners arranges its own financing, keeps

separate books, files its own tariffs, and accepts separate "tenders" (proposals to ship oil) from shippers, as if it owned and operated a physically separate pipeline. Alyeska Pipeline Service Company does not own IAPS, but is only a non-profit service corporation that schedules shipments, operates and maintains the system, and sends monthly bills to each of the eight IAPS owners for its proportion of the pipeline's operating costs.

If IAPS were a single corporate entity in which each oil company was a shareholder, rather than an undivided-interest venture, there would be no reason even to consider an AGSOC purchase of the BP share, as Subchapter U denies its special tax exemption to any dividends a GSOC might receive from another corporation. (It also forbids a GSOC to own more than 20 percent of any other corporation, but this provision is not at issue here, as BP's interest in IAPS is less than 20 percent.)

Financing the purchase. Senator Gravel and Louis Kelso [in Kelso & Co.'s December 7, 1978, memorandum to the state] assume that AGSOC's purchase of the pipeline share would be 100 percent debt-financed. AGSOC could either (1) buy the property for cash and arrange its own bond issue, or (2) assume BP's debt and issue new debt in AGSOC's name only to pay for BP's equity interest in the pipeline.

Either course would require the state to guarantee AGSOC's bonds: BP's present creditors would surely refuse to exchange the liens they now hold against the worldwide interests of British Petroleum for a practically worthless claim on AGSOC assets. The bondholders might be willing to accept the state of Alaska as a substitute guarantor in place of BP, but it would be unreasonable to expect BP to maintain its existing billion-dollar-plus guarantee on a pipeline that it no longer owned --- unless the state were willing to backstop this liability.

Assuming, however, that AGSOC could somehow refinance the pipeline, the proposed AGSOC purchase invokes some more fundamental problems:

Purchase price. What will the purchase price be? Kelso & Co. seem to assume that the price will be the pipeline's book value at the time of sale. This assumption, however, begs the question of what "book value" really means in this context. Is it the ICC valuation (which was used in fixing the initial tariffs), or BP's net pipeline assets according to generally accepted accounting practices (GAAP)? There is no reason, in fact, to assume that BP would be willing to sell at either price, or at any price that is even remotely related to either of them.

Tariff conditions. Moreover, until FERC decides what ratemaking methodology it will require oil pipelines to use in the future, it is impossible to estimate the pipeline's real worth to either party with much confidence. The Commission may retain the old ICC concept of valuation, under which pipeline rates can be expected to increase with inflation, as FERC's Chairman, Charles Curtis, has repeatedly suggested.

Under the latter method (whose advocates in the ICC and FERC proceedings included the U.S. Justice Department, FERC staff, and the state of Alaska), a 100 percent debt-financed pipeline would not be entitled to any profit at all, because it would have no equity in its rate base on which to earn a profit. Until FERC finally defines its oil pipeline ratemaking methodology, therefore, any estimate of the value of a share in TAPS is quite conjectural and, further, poses the danger that a highly-leveraged investment might all but destroy its profitability.

Only after this proceeding is completed can one even begin to calculate the pipeline property's value to AGSOC or any prospective purchaser. This value is, of course, based upon the stream of net income the owner would expect to receive, discounted to the present. But, as we explained previously, it is extremely unlikely that FERC would allow a GSOC-owned pipeline to add non-existent corporate income taxes to its rates, regardless of which of the two basic ratemaking principles it finally adopts. Thus, in the most probable circumstance, there would be no real advantage to a GSOC investment in the line, and further inquiries into its worth from the buyer's standpoint would be futile.

If by chance, FERC did permit AGSOC to extract a larger net income from the pipeline tariff each year than BP, because of the Subchapter U tax exemption, the property would be worth more to AGSOC than to BP. Both companies could, therefore, benefit from the sale of the TAPS interest at any price less than its worth to AGSOC and more than its worth to BP. (That price must of course compensate BP for any capital gains taxes it has to pay as a result of the sale, as well as for the present value of future pipeline earnings.)

But where, within this range of prices will the deal be cut? There is no confident way to answer such a question: it is a matter for bargaining. BP, however, would tend to have the stronger hand because it has no compelling need to sell its interest in the pipeline, while AGSOC's management would be under pressure to buy something if only in order to justify its own existence. In any case, the final price is likely to be substantially higher than the pipeline's current worth as seen by BP: the bargaining process will surely enable BP to extract from AGSOC some part of whatever added worth the latter's tax-exempt status might convey to the pipeline property.

Risk. Thus, the BP pipeline purchase is at best a wild gamble for AGSOC. Granted, deals are in fact made in the face of great uncertainty --- oil and gas lease sales, for example --- but for this one, every omen is unfavorable. Kelso & Co.'s own cash flow scenarios [loc. cit.] make unreasonably optimistic assumptions regarding the purchase price and FERC's treatment of AGSOC's tax exemption, plus an additional unsupportable assumption that pipeline throughput will remain steady for 20 years at either 1.2 or 1.6 million barrels per day.³ Despite these biases, many of Kelso's own scenarios show only trivial payouts to AGSOC shareholders, and others even show losses.

The purely financial risks to AGSOC in such a purchase are monumental, particularly if a large fixed debt-service obligation caused by 100 percent debt financing reduces the margin for error to the barest minimum. Senator Gravel has himself identified another notable risk, yet dismisses it with a most unusual argument:

The guarantee, if the investment is sound, need pose little risk particularly so for the purchase of an interest in the TAPS line, since we are already dependent upon the oil line for our prosperity and for substantial State revenues. Whatever is at risk in the guarantee of the purchase of an interest in the TAPS line is very little risk indeed, since we are already at risk as a State on the economic success of that line. In the unlikely event that the TAPS line should fail, the State will suffer severe economic dislocation because of the loss of jobs and our inability to transport royalty oil. An Alaskan GSOP ownership interest in the line would not substantially compound the economic crisis resulting from a failure. ["Response to Several Questions Concerning the Alaska General Stock Ownership Plan," April 10, 1978.]

3) Our projections show a probability of only 50 percent that total Arctic Slope oil production --- including production from new fields --- will exceed 1 million barrels per day in 1995, or 600 thousand barrels per day in 2000. See Arlon R. Tussing & Associates, Inc., Alaska North Slope Production Forecasts, 1980-2000 [October 8, 1979].

The illogic of this argument is so obvious that further comment would seem unnecessary. Senator Gravel appears to say that a failure of the Prudhoe Bay field or of the TAPS system would be so devastating to the state's economy that Alaskans would be indifferent to further disasters such as the loss of all value in their AGSOC shares and the drain of hundreds of millions of dollars on an already depleted state treasury in order to make good on pipeline loan guarantees. Most of our eggs are already in one basket. Therefore, he tells us, it is no matter if we put the rest of our eggs there!

Summary. BP's share of TAPS looks like an exceedingly questionable first investment for AGSOC:

Nobody knows what method FERC will ultimately use to set the TAPS tariff;

Until FERC does finalize its ratemaking methodology, moreover, the value of TAPS ownership will be pure conjecture, and bargaining will take place in the dark;

Whatever ratemaking method FERC adopts, it is unlikely to allow AGSOC to profit from its Subchapter U tax exemption; and

Even if AGSOC's tax position did make ownership of the pipeline more valuable to AGSOC than to BP, the latter would be able to bargain away some, and possibly the major part, of this additional value.

SOME AGSOC INVESTMENT POSSIBILITIES

The factors reviewed in this report --- both the tax and accounting considerations examined in Part I and the financial and regulatory principles reviewed just now --- drastically narrow the range of projects and investment strategies for which a GSOC has a decisive advantage over other forms of business organization. They do not, however, entirely eliminate AGSOC as a vehicle for citizen participation in the ownership of Alaska business, provided the legislature is willing to appropriate equity for AGSOC or to provide state guarantees for its financing.

The most promising opportunities for (1) financing AGSOC investments with a relatively high proportion of non-recourse debt, and (2) turning the provisions of Subchapter U to an advantage for the shareholders rather than a handicap or a hazard, are ventures that can operate under long term cost-of-service contracts to utilities or other large purchasers, but which are not themselves regulated utilities. The following pages examine three such ventures, their prospects for securing highly leveraged financing, and their ability to make effective use of a GSOC's special tax status.

The gas conditioning plant. One investment that may meet these standards is the Prudhoe Bay gas conditioning plant. This facility is an ideal subject for a highly leveraged project-financing (a debt ratio of 75 percent or more), because it will operate under long-term cost-of-service contracts either to the gas producers or to the shippers of gas through the Alaska Highway pipeline. But the conditioning plant will not itself be a regulated utility, and probably will not carry the severe disabilities for GSOC ownership that utility status creates.

FERC interprets the relevant laws (the Natural Gas Act [NGA], the Alaska Natural Gas Transportation Act [ANGTA], and the Natural Gas Policy Act of 1978 [NGPA]) to mean that the conditioning plant is not a gas transportation facility subject to FERC's direct regulatory jurisdiction, but is rather a part of the production process. Thus, the return to equity, the treatment of corporate and ad valorem property taxes paid or not paid, and other components of the conditioning charges need not conform strictly to utility law or to FERC's accounting practices.

The Commission does believe, however, that NGPA gives it the authority to decide what part of the gas conditioning costs may be passed along to gas consumers, and what part must be absorbed by the producers. Thus far, FERC has insisted that the producers bear all of the conditioning costs, but may modify this ruling during the current negotiations over pipeline financing. In any event, both FERC and the producers are likely to view the reasonableness of conditioning charges quite broadly. To the extent the alternative to AGSOC ownership is a conventional, taxable private corporation, neither the producers nor FERC is likely to insist that conditioning charges be reduced by the amount of AGSOC's tax exemption, as would be required by strict public utility rate-making principles.

A conventional, taxable private corporation is not necessarily the only feasible alternative to a GSOC for financing and operating the conditioning plant, however. For example, the state of Alaska, which is also exempt from corporate income taxes, and which in addition might be able to obtain capital for the project (at least indirectly) from the tax-exempt bond market, might build and operate the plant, taking advantage of its own favorable tax position to earn after-tax profits equal to a conventional corporation's taxable profits.

Still another possibility is that the producers themselves establish such a non-profit (and effectively tax-exempt) 100-percent-debt financed entity. Whatever entity ultimately owns and operates the gas conditioning plant, however, it can be project-financed only on the basis of guarantees from some party or group of parties that the plant and the entire Alaska gas transportation system will be completed and go into operation within a certain time and within a certain cost. It is still quite unclear who will provide these guarantees. Thus, we can not accurately assess the feasibility, or the magnitude and distribution of benefits, of AGSOC ownership --- or of any other arrangement for financing, building, and operating the conditioning plant --- except as part of an overall agreement regarding financing of the entire gas transportation system.

Coal mining. Another kind of enterprise that might capitalize on AGSOC's tax advantages, and thereby enable financing with a high proportion of non-recourse debt, is a coal mining venture under contract to an electric utility company, in (say) California or Japan. Like the gas conditioning plant, such a venture would not be subject to strict utility-type regulation. The California Public Utilities Commission (CPUC), for example, would scrutinize any service agreement for the sale of Alaska coal to a California utility, but would bar the utility from executing a contract only if it seemed "imprudent" --- that is, if the terms were patently inferior to those obtainable from some alternative source of supply.

As was the case for the gas conditioning plant, the alternatives are likely to involve production of the coal by fully taxable private corporations. If the delivered price of coal from an Alaska GSOC were competitive, the CPUC probably would not veto a contract that let AGSOC capture all or most of its tax advantages.

Shipping. A GSOC might build or buy and operate tankers or offshore service vessels under charter to oil companies, or coal carriers under charter to a utility. Ships can easily be moved from one market to another, and though their resale prices are volatile, they can readily be sold or chartered to other parties. Ships also have much lower risks of prolonged construction delay, non-completion, or unserviceability than specialized, fixed installations such as Arctic pipelines, refineries, and electrical generating plants.

As a result, ships can often be conventionally financed with very low down payments, even during the design and construction periods. Title XI of the U.S. Merchant Marine Act provides federal loan guarantees of 75 percent for most kinds of U.S. ships, and up to 85 percent for ocean-going tugs and LNG tankers. Thus, it is not unknown for ships to be privately financed 100 percent (or more) with non-recourse debt.

In general. As we have seen, there are many factors that determine whether a particular business enterprise organized as a GSOC would actually produce more after-tax income for its owners than some other kind of business organization, and whether Subchapter U of the Internal Revenue Code would be an advantage or a handicap. Likewise, uncertainties plague any judgment about whether an otherwise sound GSOC financing plan might actually require some shareholders to pay out more in additional income taxes than they receive in GSOC dividends.

While other equally worthwhile investments surely exist, the three specific cases examined here (the gas conditioning plant, a coal mining venture under contract to an outside utility, and ships built or bought for charter to outside companies) offer the best prospects for GSOC success. Nevertheless, even these ventures may not turn out to be

particularly prudent, profitable, or otherwise appropriate GSOC investments. Among them, only the shipping venture offers more than the slimmest possibility of 100 percent debt-financing without state loan guarantees.

Finally, no matter how compatible with the GSOC form of organization and highly-leveraged financing a class of projects seems to be, the state government should not encourage the purchase or construction of any kind of facility until the prospective cash flow and risks of a particular project have been carefully scrutinized.

STATE APPROPRIATIONS, DIRECT LOANS, AND LOAN GUARANTEES

Promoters of the AGSOC concept originally described it as a means to transfer the state's oil wealth to private citizens (through a state government equity contribution or guarantee for borrowed money). Interestingly, they have now abandoned that rationale, and seem to imply that AGSOC is a means of creating wealth virtually out of thin air, solely by capitalizing on a GSOC's federal tax exemption.

We have seen, however, that there is little chance a major GSOC investment can be financed 100 percent with non-recourse debt. If a GSOC is to become a reality in Alaska, it must therefore get its initial funding and its ability to attract additional private capital from some infusion of surplus state revenues. And, if the state's treasury or credit is involved, it is only prudent for the legislature to weigh the merits of AGSOC against other vehicles for transferring state oil wealth to individual Alaskans. Whatever organizational vehicle may be chosen, the three methods by which this transfer can be accomplished are state equity contributions, direct loans, or loan guarantees.

State equity contributions. The most straightforward and efficient way to transfer wealth from the state government to individuals is by direct appropriation. If the legislature wants to capitalize the excess revenues of state government and distribute them as income-earning shares in a GSOC or some other kind of state-sponsored enterprise, the most straightforward and efficient, and the safest method is to grant it a direct appropriation of equity capital.

With an equity appropriation, the citizens and the legislature will know just how much they are putting at risk. They will also have a clear standard for comparing

alternative investment opportunities: what rates of return do they expect to earn on each project? Finally, they will have a clear measure by which to judge the results of actual investments and to assess the performance of a project's managers: what rate of return has the equity in fact earned?

An appropriation of state equity, coupled with debt furnished by financial institutions and other private lenders under market terms without a state guarantee, is also the most prudent capitalization strategy for a state-sponsored enterprise. The private capital market can thereby be expected to serve as a check against over-leveraged capitalization schemes --- capital structures in which the debt service burden can exceed the venture's cash flow if something goes wrong.

Direct loans. There is, however, little point for state government to lend money to AGSOC or any other state-sponsored business enterprise at market rates and terms. Such loans only displace outside private capital that the enterprise otherwise would be able to borrow. After all, the market rate is simply the rate at which money is actually available for a certain purpose, and subject to a certain level of risk. A direct loan from the state can, however, be tailored to create more favorable business prospects for a GSOC than would a conventional private loan:

- 1 The state may charge AGSOC a lower interest rate than private lenders would demand for investments of similar risk. The reduced service obligation might make an otherwise submarginal venture competitive, or leave a greater part of a profitable venture's total cash flow in the form of earnings that can be distributed as dividends.

Like a state appropriation of equity capital, an interest subsidy in a direct state loan allows citizens and the legislature to know exactly how much they are contributing to AGSOC. The cost-effectiveness of an interest subsidy is much harder to judge, however, than that of an equity appropriation. And "soft loans" often tend to make bad investments and bad management look much better than they really are.

2. The state might lend AGSOC a greater proportion of the capital it needs than private lenders would deem prudent --- as much as 100 percent. State loans would thus reduce AGSOC's need for equity and permit it to earn a higher rate of return on that reduced equity commitment --- provided, of course, that everything goes well.
3. The state might grant AGSOC a direct loan, subordinated to loans from private parties, and in doing so allow AGSOC to begin with a highly leveraged capital structure that it would otherwise be unable to attain.

In both of these cases, it would be impossible to measure the true size of the subsidy. Instead of a clearly discernible interest rate discount relative to private market rates, the state's contribution would be to assume part or all of the risk that is normally borne by equity capital. No direct cost to the state will appear until something goes wrong, but at that time, the cost can be far greater than any interest discount ever would have been.

Loan guarantees. A state loan guarantee can serve the same function in capitalizing a GSOC as a direct state loan:

1. State credit backing may allow the GSOC to obtain lower interest rates in the private capital market than would otherwise be available. Again, the reduced debt service obligation may make an other-

wise submarginal venture competitive or leave a greater part of a profitable venture's total cash flow in the form of earnings that can be distributed as dividends.

2. A state loan guarantee can induce financial institutions to lend AGSOC a greater proportion of its needed capital than they would normally deem prudent --- even as much as 100 percent. Such loans will thus reduce AGSOC's need for equity and permit it to earn a higher rate of return on the reduced equity commitment.

In either case, the state's contribution to AGSOC would be to assume all or a part of the risks that are normally borne by equity capital. Here the citizens and the legislature would have no way whatsoever to measure their contribution to AGSOC, because no burden will become apparent until something goes wrong. Once more, the cost to the state in case of trouble might be far greater than if it had simply granted the GSOC a direct equity contribution or an interest subsidy. What may not be readily apparent, however, is that the use of state loans or loan guarantees to create a highly leveraged capital structure for AGSOC makes trouble more likely. The following pages explain why this is so.

Assumption of risk and creation of risk. Government loans or loan guarantees are needed in an Alaska GSOC's capital structure only to the extent that private lenders are not convinced that its cash flow will cover its debt service under every plausible circumstance, or that the value of the GSOC's assets would offset its debts should it become insolvent. Thus, state credit or credit backing to a venture that otherwise could not be financed bears an equity risk --- it consists of funds that in fact may not earn their specified return or be repaid. But it also carries a debt service burden --- the return of and return on debt capital is a fixed cost that must be paid in good times and bad if the business is to remain solvent.

The adverse impacts of soft credit. It is a truism that direct state loans or loan guarantees can make even the poorest business venture financible by reducing or eliminating the risks to private lenders. It is not so widely realized that they can also make the most promising venture unsafe by encouraging over-leveraging.

If financial institutions refuse to supply as much debt capital as AGSOC seeks unless the state backs the loans, they are saying that AGSOC's proposed capital structure is over-leveraged, undercapitalized, and therefore unsafe. A capital structure that is unsafe for private lenders will also be unsafe for the state as a lender or guarantor.

It is, moreover, unsafe for AGSOC's shareholders, because it carries the danger that their equity could be wiped out by a relatively small business setback. When private lenders insist that each project have enough paid-in equity that its debt service obligations will never exceed the cash available to meet those obligations, they are guarding not only their own investment from default but that of the shareholders from insolvency and liquidation. Alaskans should not ignore this free advice and protection, except for the most compelling reasons.

Shareholder tax liability. In addition to the dangers of insolvency, the extension of state credit or guarantees in order to create an over-leveraged capital structure poses another risk to AGSOC shareholders. Under Subchapter U of the Internal Revenue Code, the income of a GSOC is taxable to its shareholders in proportion to their ownership, without regard to the dividends the GSOC actually pays.

Part I of this report showed that there were a number of plausible circumstances in which ownership of GSOC shares would create personal tax liabilities that exceeded the

shareholder's dividend receipts. The likelihood of such a situation increases with the amount of debt in the GSOC's capital structure and its resulting need to use net earnings to retire debt rather than to pay dividends. The danger is thus an additional reason to avoid using the state's credit strength for the purpose of arranging a highly leveraged AGSOC capitalization.

Today's Alaskans and future Alaskans. The various measures for capitalizing AGSOC affect present and future Alaskans quite differently.

Subchapter U of the Internal Revenue Code and the AGSOC bills before the legislature require AGSOC to be a closed corporation, in which the only Alaskans to receive shares without charge will be those who reside in the state at a specific time. While these initial shareholders may not transfer their shares to nonresidents, they would be allowed to take their shares with them if they moved out of Alaska. Any person who moved to Alaska after the distribution date and wished to own AGSOC shares would have to buy the shares either from an out-migrant or (after five years) from another resident shareholder. Individual Alaska residents could each accumulate up to ten shares from the original distribution or by inheritance, gift or purchase.

As of the time of initial distribution, therefore, the ownership of AGSOC shares would be almost identical with the state's population. But as time passed, the distribution of stock ownership in any one GSOC would diverge substantially from the state's population at that time.

An appropriation of current funds by today's legislature, which represents today's Alaskans, for the purpose of funding a private corporation that benefits all of today's Alaskans is one thing: The population making the appro-

priation, the population whose revenues are appropriated, and the beneficiary population are identical. Once the legislature makes such an equity grant, moreover, the state treasury will bear no further obligation to the GSOC or because of it.

Direct loans and guarantees for AGSOC are quite another matter: Once again it would be today's Alaska population that commits the state's credit and receives an equal distribution of whatever benefits it conveys. But the risk of default on loans or loan guarantees granted by a past legislature will be borne by a quite different group of people. That is, the GSOC formed today, will in the future be owned much less equally by a group composed of some (but not all) Alaska residents together with some non-residents. The propriety, fairness, and legality of such an arrangement is certainly worth questioning.

Summary. The outlook for financing AGSOC's initial investments entirely by borrowing as described by Senator Gravel and the AGSOC Educational Committee is extremely slim unless the state of Alaska lends or guarantees some or all of the debt. Direct loans from the state or state loan guarantees for this purpose, however, have little to recommend them:

1. The true cost of direct loans or loan guarantees is impossible to measure accurately;

2. The cost-effectiveness of a state financed contribution to AGSOC in the form of direct loans or loan guarantees cannot be estimated with any confidence;

3. Soft loans or state-guaranteed loans make it harder to monitor the quality of AGSOC investments or the performance of management;

4. Loans or loan guarantees that one used to increase the leverage of a GSOC's capital structure also increase the likelihood of insolvency and business failure;

5. Loans or loan guarantees that increase a GSOC's debt ratio increase the danger that the shareholders' personal tax liability on GSOC earnings would exceed their dividend receipts; and

6. The Alaskans who will bear the costs of state loans or loan guarantees for AGSOC will be a quite different population from those who benefit from the state's financial aid.

State loans and loan guarantees are thus an undesirable means of capitalizing AGSOC. An Alaska GSOC should carry no more debt in its capital structure than financial institutions would regard as prudent for a conventional private corporation in similar circumstances.

To the extent the legislature wants to provide financial assistance to an Alaska GSOC, state participation should take the form of an appropriation of equity capital. This route is straightforward; its costs and risks are measurable, it preserves the ability to judge the quality of investments and AGSOC management, and the people who bear its costs are the same as those who benefit. An equity appropriation is, in short, the honest, direct, and efficient way of financing AGSOC.

PART III: AGSOC SHAREOWNERSHIP AND MANAGEMENT

Kelso's ideology. Louis Kelso, originator of the GSOC concept, is the leading spokesman for a distinctive, radical social philosophy whose details need not concern us here. In general, however, Kelso's ideology combines an emphasis on capital (as opposed to labor) as the principal source of prosperity, with a deep hostility to the private enterprise system as it actually exists. The chief evil of contemporary capitalism, according to Kelso and his followers, is the concentration of wealth and economic power in the hands of a few wealthy individuals. This concentration, he believes, results in:

" . . . endemic poverty . . . misuse of technology, resource waste, despoilation of the environment, declining personal freedom, increasing lawlessness and civil disorder, the waning of liberal education, the civil rights impasse, the youth revolt, urban concentration, rising public and private debt, public loss of confidence in leadership and the seemingly irreversible advance toward a totalitarian society." [Kelso, et al, "Design of an Alaskan General Stock Ownership Plan" Volume I, p.16.(February 15, 1979)]

Restrictions on shareownership, transfer, and voting.

Instead of welfare measures or state socialism, however, Kelso advocates an equal or more nearly equal distribution of capital in the form of shares in new kinds of corporate enterprise, one of which is the General Stock Ownership Corporation (GSOC). The special restrictions on share ownership, transfer, and voting rights incorporated in Subchapter U of the federal tax law, and in the proposed Alaska GSOC legislation, stem directly from Kelso's theories and social philosophy. These restrictions include the following:.

1. The original distribution of shares is limited to residents of the state, and no shareholder may transfer stock to a non-resident (even by inheritance);

2. Only natural persons (not corporations or associations) may own GSOC stock;
3. No resident shareholder may transfer his stock (except by inheritance) for 5 years after its issue;
4. No person may acquire more than ten shares in total through original distribution, inheritance, purchase, or otherwise; and
5. Proxy and cumulative voting are prohibited.

The first four provisions are required by Subchapter U, and the last is a feature of the proposed Alaska legislation. The purpose of these restrictions is to preserve the identification of the GSOC with its home state, to prevent the concentration of control in the hands of a few large shareholders, and to deter "speculation" in GSOC stock (as opposed to its retention for income). These are elements of the new economic order that Mr. Kelso and Senator Gravel would create.

Will the example of a new, broadly-based form of business enterprise revolutionize the economic system or the social order?

If state-sponsored GSOCs were to acquire substantial productive assets, they would indeed have some impact on the overall distribution of wealth. But that influence, for good or evil, is not likely to be profound, and in many cases its direction will be quite different from that envisioned by Kelso or other GSOC boosters. On the other hand, fears that AGSOC could become a "rival government" or a pernicious economic and political power, are probably unjustified. The following pages review a few of the implications of existing federal and proposed state legislation governing GSOC shareholding and management.

The experience of the cooperative movement. It is useful to consider another form of broadly-based business enterprise with which we have already had extensive experience. Cooperatives on the Rochdale model have existed in Western Europe and the United States for more than 140 years, and have deep cultural roots in the farmer, labor, and socialist movements. In our judgment, at least, their philosophical bases are more respectable intellectually, and they are certainly more acceptable to more people than Mr. Kelso's "two-factor" theory.

The federal tax treatment of cooperatives is, interestingly, much more liberal than that which applies to GSOCs, and the legal restrictions on their membership and their investment strategy are considerably less onerous. A cooperative does not need a special state charter, for example; any group of citizens (or non-citizens, for that matter) may establish one. A large body of experience with successful (and unsuccessful) cooperatives in different economic sectors exists to guide those who would set up a new enterprise. Successful cooperatives exist in retailing, in the marketing of agricultural and fishery products, in finance (credit unions), and in health (HMOs). Cooperatives predominate in the electric utility business in Alaska, for example.

Yet despite successful precedents in all these fields, despite the tax advantages of corporations over ordinary corporate enterprise, despite the attractiveness of economic democracy and broad-based shareholder participation, the cooperative movement has not swept the nation, nor has it perceptibly changed the distribution of economic or political power.

Mutual savings banks and savings and loan associations are also successful vehicles for widening the ownership of financial capital. The thrift institutions are theoretically owned and governed by their depositors, just as mutual insurance companies are theoretically owned and governed by the policyholders. Federal and state laws grant such collectivist enterprises certain tax and other advantages over commercial banks and stock insurance companies, respectively, but their impact on the distribution of wealth and power is no more evident than that of the cooperatives.

Despite their origins in radical or reform movements, cooperatives and mutual enterprises are really specialized parts of a highly pluralistic capitalist economy, distinguished from other corporations by somewhat different rules regarding their financial structure, government, and accounting systems. In practice, they neither reform nor subvert the economic and social system. There is little reason to believe that the influence of GSOCs --- if they ever managed to overcome the handicaps we have enumerated --- would be any more profound.

Management incentives. Viewed from the standpoint of the business enterprise itself, the Kelso formula for economic democracy probably does not lend itself to effective management and business performance. Broadly-based enterprises like cooperatives and mutual aid societies have been most often successful where they are specialized, single-purpose ventures with relatively standardized operations and in which the shareholder-member can easily measure management performance: How do the premiums and benefits of a specific mutual insurance company compare with its competitors? What interest rate does this credit union charge, and what does it pay as dividends on share deposits? How long is the wait to see a doctor at the Group Health Association? Etc.

Though important exceptions do exist, the most successful cooperatives and related organizations are not usually those with an active and involved membership --- but rather those with a competent and usually self-perpetuating professional business management. The coop member's most effective remedy for poor performance is to shop or bank, or sell his crop elsewhere. Thus, those associations that fill an appropriate niche in the economy and are well-managed thrive, while those who do not meet both specifications flounder and disappear.

These are exactly the means by which customers and shareholders alike exact performance from ordinary business corporations. Very few customers or shareholders want to become involved in the governance of the enterprises that serve them, or in which they invest, and very few take advantage of the opportunity to participate in management even when it is offered to them. The dissatisfied customer goes elsewhere, and the small investor sells his stock.

This option on the part of shareholders is the ultimate discipline on corporate management and the most fundamental incentive for economic efficiency, and against sloth, gold-plating, pyramid building, and management self-dealing. The net worth of efficient and profitable corporations appreciates (whether or not they pay dividends) --- these are the corporations whose management have access to both the internal and external funds needed for rapid growth.

In addition to the ability of the shareholders to "vote" on management in the stock market, the most important protection that small shareholders have is the large shareholder.

One or one hundred shares in a company usually does not make it worthwhile for a shareholder to learn much about a corporation or become active in its affairs. The fact that there are wealthy individuals, banks, or other large institutions for whom business is a profession, and for which the corporation's efficiency and profitability makes a difference of millions --- means that someone is almost always looking out for the interests of the "little guy" and of the legendary "widows and orphans."

In their naive hostility toward the capitalist system as it operates today, and in their idealistic desire to protect the little guy, AGSOC advocates like Mr. Kelso and Senator Gravel would substantially dilute forces that create efficiency incentives, and the value of shareownership:

1. By requiring a GSOC to flow-through as dividends at least 90 percent of its taxable income, Subchapter U limits the GSOCs ability to generate capital gains --- which in the long run constitutes the largest benefit from owning common stock;
2. By restricting the sale of shares in various ways, the federal and state GSOC legislation limits the growth of a market for GSOC shares, and further reduces the shareholders' ability to benefit from appreciation of stock values;
3. By restricting shareholders to natural persons, the law effectively prevents individual shareholders from borrowing money on their stock, and thus from using their GSOC wealth as a foundation for additional investments. (This is a particularly ironic restriction, in light of Kelso's belief that it is the access of the wealthy to credit that is the root of their economic power);
4. By limiting an individual to ten shares, the law guarantees that no shareholder will have a sufficiently large stake in the GSOC to make it worthwhile for him or her to pay careful attention to the quality, conduct, or performance of the directors or management.

We can not predict with any confidence what the net impact of the dispersal of AGSOC ownership and voting rights on business performance would actually be.

1. As we noted earlier, some broadly-based organizations --- specialized cooperatives, thrift institutions, and insurance companies, perform as well as their conventional corporate rivals. In most successful instances, however, the membership seems to be apathetic (or just content?) and the management is more-or-less permanent.

2. In other cases, including, for example, many non-profit hospitals and nursing homes, some labor unions or professional organizations and their welfare funds, a large and inactive membership coexists with an incompetent, indifferent, or corrupt management.

3. Finally, there are still other instances where broad-based economic organizations have a relatively large group of active members, but where the organization is constantly convulsed by turmoil and factional warfare, a situation that is hardly conducive to achieving the organization's economic objectives.

All three models and all gradations between them, are visible among Alaska Native corporations today. Of all the types of organizations with which Alaskans are familiar, the Native corporations are probably the most similar in objectives and structure to a GSOC, and their history and performance are probably good predictors of the outcome of a GSOC experiment in Alaska. It is anybody's guess, however, which kind of Native Corporation AGSOC would most closely resemble.

STATE OF ALASKA

JAY S. HAMMOND, Governor

OFFICE OF THE GOVERNOR

Phone 465-3512

DIVISION OF POLICY DEVELOPMENT AND PLANNING

Pouch AD - Juneau 99811

ALASKA CITIZENS WEALTH OWNERSHIP PROGRAM

A Brief Summary

1. What is the purpose?

- transfer wealth to people;
- means for direct participation by individuals in newly organized enterprises;
- greater resident control over existing Alaskan industries; and
- wider participation in and understanding of capitalist system through wider ownership.

2. Who organizes or runs the Program?

- the program is housed in the Department of Revenue;
- the Commissioner must propose at least one wealth distribution plan but not more than three to the Legislature each session;
- the Legislature may approve or amend the plan and appropriate any sums required for its implementation;
- some plans may require the creation of new private organizations, such as GSOC's or mutual funds.

3. What types of assets could be distributed under the Program?

- Energy Resource Trusts, which pass on a portion of the State's oil and gas royalties directly to holders of certificates in the trust;
- Industrial Development Projects, which are major projects involving State financial participation which would be distributed by the State to residents;
- General Stock Ownership Corporations, which are widely held corporations organized under sub-chapter U of the Internal Revenue Code;

- Investment Funds, which are regulated investment companies (mutual funds) holding securities of corporations doing business in Alaska;
 - Real Estate Trusts, which invest in Alaska real estate developments; and
 - Existing Private Enterprises, large blocks of shares of which could be purchased by the State and distributed to residents.
4. Who is eligible for participation in the program?
- all Alaska residents as defined in the bill;
 - eligibility for each Plan is established by dates included in the Plan.
5. What State appropriations would be required?
- an appropriation of the assets to be distributed under the plan; and
 - amounts required to administer the Program.
6. What actions would be mandatory?
- only that the Commissioner of Revenue prepare and present at least one Plan and not more than three Plans for each legislative session.
7. What actions would be elective?
- legislative adoption of a Plan and appropriations necessary to implement it; and
 - individual participation in a Plan.
8. What would individual residents receive?
- free distribution of a minor portion of the assets included in a Plan;
 - an option to purchase additional shares or securities in the remaining assets; and
 - the assets distributed under the Program would be the unencumbered private property of the beneficiaries except as otherwise provided by law.

CHAPTER 9. BEAUFORT SEA OIL AND GAS ROYALTY TRUST PLAN OF 1980

§AA.ZZ.110 CREATION OF TRUST. The Commissioner shall create by trust indenture an Alaska Energy Resource Trust in accordance with the provisions of this Chapter and other provisions of this Act, to be known as the Beaufort Sea Oil and Gas Royalty Trust of 1980, and its trustee may transact affairs in that name.

§AA.ZZ.120-150. [SAME AS CORRESPONDING SECTIONS OF CHAPTER 8]

§AA.ZZ.155. CONVEYANCE OF ROYALTIES. (a) The Commissioner shall convey by deed to the trust, 30 percent of the first "\$X" million, 50 percent of any amount exceeding "\$X" million but less than "\$Y" million, and 70 percent of any amount exceeding "\$Y" million in any calendar month, from the State's reserved royalty interest in the following leases:

[INSERT PROPERTY DESCRIPTION]

[INTERVENING LANGUAGE SAME AS CORRESPONDING SECTIONS OF CHAPTER 8]

§AA.ZZ.410. CREATION OF BENEFICIAL SHARES AND CERTIFICATES. (a) The entire beneficial interest in the Trust shall be divided into _____ units. The ownership of the units shall be evidenced by certificates in substantially the following form.

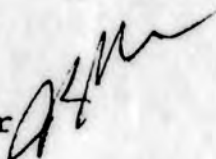
CERTIFICATE OF BENEFICIAL INTEREST
IN
THE BEAUFORT SEA OIL AND GAS ROYALTY TRUST OF 1980

Created by, Issued under, and subject to the Beaufort Sea Oil and Gas Royalty Trust Indenture dated as of _____

THIS CERTIFIES THAT _____ is the owner of _____ Units of Beneficial Interest ("Units") in that certain Trust known and designated as the Beaufort Sea Oil and Gas Royalty Trust of 1980 . . .

[REMAINING LANGUAGE SAME AS CORRESPONDING SECTIONS OF CHAPTER 8]

MEMORANDUM

To: Arlon Tussing
From: John R. Messenger 
Date: March 26, 1980
Re: Legal Issues relating to the establishment
of the Alaska Citizens Wealth Ownership
Program

In the course of drafting legislation for the Alaska Citizens Wealth Ownership Program, it has been necessary to consider numerous legal issues which are not immediately apparent from a reading of the proposed legislation. The purpose of this memorandum is to identify those issues, indicate how they have been dealt with in the proposed legislation and indicate what issues remain unresolved at this time. This final point is particularly important because in the time available, it has not been possible to undertake a complete analysis of all the legal issues.

Perhaps because of the novel and ambitious nature of the project, the legal questions are numerous and wide ranging. For example, it has been necessary to address several federal and state constitutional issues, including: a) whether the program serves a public purpose as required by Art. IX, §6 of the Alaska Constitution, b) whether the conveyance to a trust of the state's oil and gas royalty interests results in a dedication of revenues in violation of Art. IX, §7 of the Alaska Constitution, c) whether the restrictions on eligibility for ownership and/or the restrictions on alienation of the ownership interests runs afoul either of federal and state equal protection clauses, the due process clauses or the federal privileges and immunities clause of the United States Constitution, and d) whether enactment of the proposed legislation is sufficiently similar to the AGSOC initiative certified by the Lt. Governor so as to void the initiative petition as provided for in Art. XI §4 of the Alaska Constitution. In addition to these constitutional matters, we have had to consider federal statutory and regulatory questions in the area of federal securities law, federal income

tax, and federal restrictions on the alienation of the state's minerals. The discussion which follows is intended only to provide a brief, general review of these issues.

EQUAL PROTECTION, DUE PROCESS, AND PRIVILEGES
AND IMMUNITY CLAUSES OF THE FEDERAL AND STATE
CONSTITUTIONS

Restricting the benefits of the wealth ownership program to residents, creating a closed class of eligible participants, prohibiting the transfer of beneficial rights to nonresidents, each raise serious questions under the federal and state equal protection clauses, due process clauses, and under the federal privileges and immunities clause of the U. S. Constitution and State of Alaska Constitution.

Without reviewing in detail the specific standards state and federal courts might use in reviewing this legislation, we can say that a court will look to the purposes of legislation and the nature of the governmental interests involved, the nature of the interests affected, and how carefully the legislation is tailored to meet the purposes of the legislation.

Because the court will carefully scrutinize the public purposes addressed by the legislation, substantial care must be exercised in stating these purposes and structuring the classifications and restrictions in legislation as closely as possible to accomplish these purposes and not any improper purposes. Each restriction must be examined to determine if it is necessary and whether it is the best, or perhaps only, way to accomplish the desired objective.

There are several legitimate state purposes which can be advanced for an Alaska Citizens Wealth Ownership program and which are set out in the proposed legislation. To the extent possible, the restrictions appear to have been drawn to meet these objectives.

Notwithstanding the care in the legislative drafting, serious constitutional questions remain. At this point, it is difficult to predict how a court will resolve these issues I believe additional analysis should be done before any plan is implemented.

PUBLIC PURPOSE

An investment of state funds in business enterprises or the transfer of public property at less than its full value, raises the question whether those investments or

transfers have a public purpose as required by Art. IX, §6 of the Alaska Constitution. In order to satisfy this provision of the State Constitution, a court must be able to conclude that the state funds expended under the Alaska Citizens Wealth Program are being used for a public purpose.

Many older court cases hold that state and local governments may only tax sufficiently to pay for the basic functions of government such as education, police protection, and maintaining public works and may not use public funds for investing in or aiding private individuals or business. In fact, some of those early cases struck down aid given to, and subscription of stock in, private business. Modern case law has given states much more latitude to venture into the private economy to relieve economic stress and unemployment, to encourage industrial development, and to promote local industry. These purposes have been achieved and sustained through the use of loans, loan guarantees, revenue bonds, and tax credits.

Because the courts will not set aside a legislative finding of public purpose unless it appears that the finding is arbitrary and without any reasonable basis in fact; the proposed legislation has been structured to state the legitimate public purposes that would be served by the program. I believe these findings, buttressed by a record of public hearings and debate should allow the legislation to withstand a public purpose challenge.

DEDICATION OF REVENUES

The transfer of the state's royalties, especially if made at less than full value, might be interpreted as a dedication of revenues in violation of Art. IX, §7 of the Alaska Constitution. Although a plain reading of section 7 would seem to say that only the dedication of taxes and license fees is prohibited, the Attorney General has ruled that the constitutional prohibition applies to all revenues including royalties from minerals produced from State-owned lands.

If we accept the Attorney General's conclusion that the dedication of royalties is proscribed, there is a significant possibility that the transfer of royalties to the trust is in violation of section 7 of Article IX. This possibility is increased to the extent, that the royalty interest is sold for less than its full market value and/or is stripped of many of its property ownership attributes.

* public purpose in
democratic distribution
of wealth to accomplish
same purposes.

The legislation has attempted to deal with this problem by structuring the transfer as a sale of the royalty at its fair market value. We believe a fair market sale, where the proceeds from the sale go to the general fund, may overcome the dedication of revenue problems. We also note that, notwithstanding the ruling of the Attorney General, there is a possibility that royalty revenues are not subject to the constitutional prohibition against dedication.

SUBSTANTIALLY SIMILAR LEGISLATION

It is difficult to say whether or not the proposed legislation is sufficient to void the initiative petition creating a general stock ownership corporation.

The Alaska Supreme Court has held that the legislature has wide discretion when enacting legislation and has, therefore, found legislation to be substantially similar, if in general the legislative act achieves the same general purpose as a proposed initiative by comparable means. The court, however, was closely divided over the question. A minority of the court concluded that the legislature has considerably less discretion and that the legislature must almost duplicate the initiative in order to remove it from the ballot.

With respect to the proposed legislation, there are reasons for concluding that the Alaska Citizens Wealth Ownership Program achieves the same general purposes as the initiative. However, there are also reasons for concluding that not all the purposes of the GSOC approach are met by the proposed legislation. If we assume the Supreme Court will adhere to the test established earlier, the outcome is uncertain. On the other hand, if the court should move closer to the minority position, then it is likely that this legislation does not void the GSOC initiative since the means used to reach the public purposes are different.

RESTRICTIONS ON THE ALIENATION OF THE STATE'S MINERALS

Under section 6(i) of the Alaska Statehood Act, the state is required to retain all minerals in mineral lands conveyed to the state by the federal government pursuant to section 6(a) and (b) of the Statehood Act. If the State attempts to convey the mineral estate, the Attorney General of the United States may bring an action for the forfeiture of the lands affected by the purported conveyance.

Although there is room for debate on the matter, I believe a conveyance of only the royalty interest to the trust would not be a violation of section 6(i). The proposed

legislation attempts to assure this outcome by requiring the Commissioner expressly to retain the mineral estate. I must note, however, that the oil and gas law of other states treats the royalty interest in many different ways, and in the absence of Alaskan case law on the subject, it is not possible to predict how an Alaskan state or federal court might treat the conveyance of a royalty interest.

It is possible to avoid the 6(i) prohibition by conveying to the trust only those leases or portions of leases on lands received by the state by operation of the Submerged Lands Act of 1953. Since there is no restriction on the alienation of the state's mineral interest in lands received under the Submerged Lands Act, the state can convey the royalty interest from such lands without fear of the 6(i) forfeiture.

A cautious approach would dictate that only submerged lands be conveyed to the trust.

FEDERAL TAX QUESTIONS

There are several tax questions which must be analyzed further before any of the ownership plans are implemented. Indeed, since the federal tax consequences to both the state and individual citizens are of great importance, I suggest the state request a ruling from the Internal Revenue Service prior to final implementation.*

Some of these questions are:

- (1) Must the state pay federal taxes on the income received from the earnings on and sale of assets purchased by the state under each of the plans;
- (2) Must citizens who receive (or purchase) ownership rights pay federal taxes on the rights received (or purchased);
- (3) Must the trust or other entity pay federal taxes on the earnings of the assets held by them.

* The IRS has refused to issue a ruling on the tax status of two recently created royalty trusts of the type included in the proposed legislation.

Although a state is not generally taxed on the income received from its investment of surplus funds, the issue is not free from doubt when the state owns and operates a business enterprise. To avoid this problem, the legislation is structured so that the state's role is limited to that of making short term investments and subsequent sale of those investments.

Any sale or distribution of ownership rights at less than full value might be the basis for an IRS contention that the individual Alaskan has realized income from the transfer.

On the other hand, purchase of an asset which will produce income in the future does not necessarily result in taxable income to the purchaser in the year of purchase simply because the asset is valuable. The draft legislation contains provisions which require assigning a value to the ownership rights and further requires that the participants pay that value. To the extent, however, that this value is below full market value, it is possible, and perhaps even probable that the IRS will treat the difference between the purchase price and the true value as taxable income to the participant at the time he receives his ownership rights.

Whether the entities to be created under the program will be subject to federal taxation will depend upon the nature of the entity created. Some of the entities contemplated under the program are vehicles which, if properly implemented, should avoid taxation at the corporate or trust level.

In the case of the Energy Resource Trust, the legislation has been drafted to avoid the trust being taxable and to provide that the income and allowable deductions flow through to the individual certificate holders. It should be noted, however, that there are only a few trusts of this type and a dearth of precedent on their taxable status. Whether the trust established under the proposed legislation would be nontaxable is not absolutely free from doubt. If the state decides to implement the trust, it should press the IRS for a ruling.

SECURITIES LAW

The distribution of ownership rights to Alaskans, raise several securities law questions.

For example, the proposed distribution of trust participation certificates under the Energy Resource Trust involves certain federal and state securities law issues. The key issue is

whether the distribution of trust participation certificates will be exempt from the registration requirements of the Securities Act of 1933 ("the 1933 Act") and the Alaska Securities Act of 1959 ("the 1959 Act"). In this regard, the Trust may be deemed to be a "public instrumentality" of the state, exempt from registration under Section 3(a)(2) of the 1933 Act and Section 45.55.140(1) of the 1959 Act may be available. In addition, it is possible that the distribution of trust participation certificates could be exempt from registration under the 1933 Act if the distribution complies with the requirements of Section 3(a)(11) of the 1933 Act regarding securities offered and sold to residents of a single state. The state, in any event, should obtain a "no action" letter from the Securities Exchange Commission before proceeding with the offering. As part of the distribution, the state must comply with the disclosure requirements of the 1933 Act, the 1959 Act and the Securities and Exchange Act of 1934, through the preparation and distribution of a prospectus containing detailed information about the trust and the trust participation units.

If the state elects to sell the trust participation units on an installment basis, it should seek a determination by the Federal Reserve Board that the margin requirements do not apply to such sales. While it appears that the margin regulations do not apply, clearance from the Federal Reserve Board should be sought before any distribution of the trust participation certificates. Similarly, in regard to the other plans being reviewed by the Commissioner, the extension of credit by the state in connection with sales of stock or other participation units raises the issue of compliance with the Federal Reserve margin regulations. Each plan may present differing problems and require separate analysis. A possible planning method would be the issuance of serial warrants to purchase the stock or participation units which could then be exercised by the citizen recipients over a period of time.

PACE

1/22

Kay
Singer
to Ulmer
Gardner
Sund
M. Miller
Morgan
Tom Cook

General bill or specific proposal?

[Loyalty Trust - on Beantest, could also be "net profit share" trust]

DPZ - have Messenger draft of Prudhoe Bay royalty trust

many technical details - need professional advice

lek - concerned about effect of trust on OIR management
" that Beantest income ^{might} will be needed when it comes due - don't know what state's fiscal situation will be - don't know what the benefits will be

Problems: public purpose

Severance Tax distribution via credit

process for Dept. of Revenue determination

section 43~~8~~.17.060(d) - hazy (eliminate?)

.160. voting rights - depends on method of transferring assets

+ all issues brought up in PF dividend program - problem w/ treating state residents different from US citizens

assets v. appropriati-

income tax -

WPT -

federal tax liability, gift (?) etc.

applicability of securities law

GIVE BRIAN PACE MEMOS

CONCEPTUAL OUTLINE
for
ROYALTY TRUST IMPLEMENTATION
through
P.A.C.E.

DRAFT

Program Elements

Detailed Components

Assets to be
distributed

- select principal amount required based on estimated number of shares and value per share, and desired annual earnings per share level.
- identify leases whose value or portion thereof equals principal amount and yields royalty cash flow at desired levels for per share value and earnings per share.
- identify fine-tuning options for structuring Trust so earnings per share are sensitive to *wellhead* prices or royalty revenues.
- identify appropriations options and requirements for transferring royalty interest to trust.

Corporate Mechanism
for administration of
Royalty Trust

- specify details of existing Royalty Trusts (see attachment).
- identify desired Trust attributes, develop draft Trust indentures and corporate organization.
- specify options for Trustee, e.g., Commissioner, private trust company, etc.

- specify Trust duties, e.g., maintain principal, pass through income, administer dispersal of share certificates, limitations on lease negotiation involvement, etc.

- identify funding source for Trust operating costs.

Eligibility to
~~and/or~~ receive free *and/or*
to purchase additional
shares

- identify status of durational or other residency requirements.

- specify eligibility requirements for participation in Trust.

Disposition of Shares
by either gift or sale
or both

- select per capita allocation of either free shares or shares for sale or both.

- identify installment sale options, i.e., terms and conditions, duration of State sale, other financing details and limitations.

- select free share distribution mechanism.

- select share sale mechanism.

- identify and select limitations on transferability of shares.

TS/dg

R.T.

Personal Investing

MSOP
NY

Trusts That Rake Royalties Off the Top by Aimée L. Morner

Inflation hedgers flocking into natural-resource investments have been eyeing some unusual vehicles known as royalty trusts. These trusts, a few of which have been around since the early 1950's, are unincorporated enterprises that act as conduits for distributing royalty income to investors. Four of the five large publicly traded trusts (see table) derive their income from royalties on sales of oil and gas; the other, Mesabi Trust, gets its royalties from iron ore. Not surprisingly, the oil and gas trusts have risen the most in the last few years, and in mid-March a big new one—Houston Oil Royalty Trust—was about to come to market.

All of the royalty trusts share some common characteristics. None of them owns any real property; instead, they hold interests in royalties from properties owned by, or leased to, one or more operating companies. The royalties, figured as a certain percentage of sales, are paid "off the top"—i.e., before the operator makes any deductions for expenses or taxes. The trusts thus bear none of the risks or costs of drilling or mining. In fact, they are required by the Internal Revenue Service to remain "passive" and, in addition, to pay out virtually all their earnings.

In return, IRS rulings allow the trusts, and investors in their "units of beneficial interest," some tax breaks. The trusts themselves pay no federal income taxes, and the IRS takes the view that investors have a stake in the assets that produce income for the trust. Consequently, part of the cash payout is regarded as depletion, a return of capital, so shareholders pay income tax on that portion.

The bookkeeping is tough. The yields on most of the trusts are fair-ly generous. The highest—11.4 percent for Mesabi Trust—is more than twice the yield on the stock of Cleveland-Cliffs, Iron, the world's largest iron-ore producer. Estimated yields on the other trusts range between 6.7 percent for North European Oil Roy-

alty Trust to 8.1 percent for Mesa Royalty Trust. By comparison, the yield on the S.&P. index of nine domestic oil companies is a slim 3.3 percent.

Figuring the taxes on the trusts' yields is nettlesome, but the bookkeeping is worth the trouble. Investors who have bought into oil and gas trusts in the last few years take "cost depletion," which involves using a depletion rate that is determined annually for each trust by independent engineers. The rates vary—from about 4 percent (an estimate) for Mesa to between 7 and 8 percent for the other three in the table.

The taxpayer applies the depletion rate to the cost of his units. If the rate is 7 percent, for example, and the units have a cost basis of \$40, then \$2.80 is considered a return of capital, and the cost of the units is reduced by that amount. Most of the time the depletion calculation will yield a figure lower than the payout; the rest of the cash distribution is taxed as ordinary income. (The treatment of this excess is dif-

ferent for Mesabi unit-holders. Once its units have been held for a period of time—it varies depending on when they were bought—the excess payout is taxed as a capital gain.)

Even though the underlying assets are being used up, the few analysts who follow the oil and gas trusts expect cash distributions to increase. Frederick A. Lynn, president of F.A.L. Capital Management, has been buying these trusts because he expects oil and gas prices to keep rising, which will not only lift royalties but also cause operators to press harder for more production.

Investors trying to figure out how much production is ultimately possible will be frustrated. While the Securities and Exchange Commission requires most publicly traded companies to report information about the size of their hydrocarbon reserves, some royalty trusts can duck the requirement if the data are either unavailable or too costly to get.

And that's the case with three of the four

THE PAYOUTS KEEP GROWING

	CASH DISTRIBUTION				YIELD	
	1979	1980 estimate	1981 estimate	Rate of growth, compounded 1975-1979	1975	Recent (based on est. 1980 distribution)
North European Oil Royalty Trust	\$4.07	\$5.00	\$7.50	37.2%	6.9%	5.6%
Marine Petroleum Trust	\$2.25	\$2.80	\$3.30	45.7%	8.0%	7.8%
Tidelands Royalty Trust B	\$1.94	\$2.80	\$3.60	N.A.	N.A.	6.7%
Mesa Royalty Trust	N.A.	\$3.05	\$3.30	N.A.	N.A.	8.1%
Mesabi Trust	\$1.39	\$1.65	\$1.80	4.8%	15.9%	11.4%

Two of the four oil and gas royalty trusts shown here—North European and Marine—have boosted cash distributions to investors at a heady pace since 1975. Of the remaining two, Mesa is a newcomer that sprang up last year, and Tidelands, which first began to distribute its royalty income in 1977, has nearly quadrupled its payout in the past two years. The other trust in the group, Mesabi, gets its income from royalties on shipments of iron-

ore pellets, and its performance has been lead- ing. All the estimates for 1980 and 1981 were compiled from forecasts by various analysts and portfolio managers. Though the prices of trust units have risen significantly, the yields, based on the 1980 estimates, have not changed all that radically. A portion of the payouts of all the trusts, with the possible exception of Mesa, can be treated for tax purposes as a return of capital rather than income.

oil and gas trusts. North European Oil derives royalties from properties in West Germany that are leased to Mobil, Royal Dutch, and Exxon, which never whisper a word about the size of those reserves. Gulf Oil is just as tight-lipped about the reserves in fields it operates partly for Marine Petroleum Trust and partly for Tidelands Royalty Trust B.

Investors know a lot more about the reserves associated with Mesa Royalty Trust because of estimates in a prospectus issued last November, when the trust was spun off to shareholders of Mesa Petroleum. Independent petroleum engineers estimated proven oil and gas reserves and calculated their present value, discounting the expected income at an annual rate of 10 percent. This worked out to \$27.75 per unit, but the assumptions about the future price of oil and gas that go into such calculations are considered to be very conservative. Consequently, the units sold for about \$30 once they began trading. They subsequently rose as high as \$42, and were recently selling for about \$35.

Real-world expectations about price increases, particularly for gas, are quite bullish, for good reason. Under the Natural Gas Policy Act of 1978, prices of newly discovered gas—now about \$3 per 1,000 cubic feet (mcf)—may rise 10 percent a year until 1985. At that time controls will be lifted, and some analysts expect new gas to sell at a parity with oil. If they are right, even if oil were to sell at only \$30 a barrel, the price of gas will rise some 65 percent, to \$5 per mcf, in five years, since that quantity of natural gas has one-sixth as much heating power as a barrel of oil.

Life in new leases?

Buyers of Marine Petroleum Trust are betting primarily on the higher gas prices. Marine's royalties—a low 0.75 percent of sales—are derived solely from the trust's interest in 500,000 acres leased to Gulf Oil in the Gulf of Mexico. Half of that acreage now produces oil and gas, much of it coming from "mature" fields. While Gulf could yet find oil or gas in the other half, investors are primarily intrigued that some 70



In the last two years, the standout in this group has been North European, whose units have doubled in price. But over the period shown, Tidelands' shares have gone up even more—from only about \$1 in 1975, to \$42 recently. Shares of Marine (which owns a third of Tidelands' units) have retreated somewhat since reaching a record level last year. With the exception of Mesa and Mesabi, the trusts have relatively few units outstanding, and their prices tend to be quite volatile.

percent of Marine's royalties come from "old" natural gas with an average price of only \$1.20 per mcf. As contracts expire, or if new gas is discovered, that figure will inevitably go a lot higher. And the kicker in Marine is its 32.6 percent equity interest in Tidelands Royalty Trust B.

Tidelands is primarily a speculative bet on an increase in production. The Tidelands trust agreement with Gulf Oil covers 1.3 million acres offshore, and Gulf has so far leased only 40,000 of them. Analysts expect Gulf to seek new leases in the area and to spend freely on wildcat drilling. Tidelands will also benefit, though not as much as Marine, from rising prices: the Tidelands gas sells at an average price of around \$1.80 per mcf.

The price on much of the gas in which Mesa Royalty Trust has an interest is strictly bargain-basement. Close to 80 percent of the gas in its largest field sells under contract at a paltry 25 cents per mcf. The contract won't expire until 1989, but new gas from the same field would, of course, sell for a lot more.

Mesa investors are buying units in the face of an unusual risk: the IRS hasn't yet ruled that it can be treated as a trust. Regardless of how this issue is resolved, a hefty portion of the payout will almost certainly be taxed as ordinary income because Mesa's depletion rate this year is expected to be so low.

The new trust in the wings, an offspring of Houston Oil & Minerals, also lacks an IRS ruling on its tax status. The properties in which Houston Oil Royalty Trust has an interest include a substantial amount of unexplored acreage that would be worth a lot if Houston Oil & Minerals made dis-

coveries there. The company's success in finding new reserves, however, has recently been only fair.

The hottest trust in the market lately has been North European. Unit holders have benefited from the rise in the value of the D-mark because the operating companies involved sell what they produce in West Germany, where the fields are. In the last three years, the trust's royalty income, in dollars, has more than doubled. Carey E. Tharp Jr., an analyst at Stillman, Maynard & Co., is convinced the payout will continue to spurt ahead. He points out that more and more of the gas sold in Germany is coming from a field that produces royalties at a rate 7.5 times higher than the rate on sales from the field that is currently producing much of the trust's income.

A direct link to inflation

The iron trust, Mesabi, hasn't been particularly popular with investors lately. Its royalties come from properties in Minnesota's Mesabi range—the nation's largest iron-ore reserve. They are mined by Reserve Mining, which ships pellets made from the ore to the two steelmakers—Armco and Republic—who jointly own the company. Reserve pays Mesabi a base royalty that depends on the volume of pellets shipped, which means the trust's income is sensitive to the demand for steel. The base is also adjusted by a factor that reflects the annual change in the producer price index. That inflation hedge hasn't swayed investors, who are aware that Reserve's pellet factory could be struck this August when labor contract expires. After the workers went out three years ago, Mesabi's cash distributions were slashed.

Question (iv), about newly discovered oil in a reservoir underlying producing formations, raises a ticklish issue. The Regs require that in such cases, the fact that the new reservoir constitutes a separate source of oil must be supported by a written finding by the "appropriate governmental agency", which is either the state regulatory agency or the U.S. Geological Survey. There is probably an exception, if the old production is from a unit limited to a specified depth which is less than the newly discovered formation. If you do not have such certification, it is advisable to get it before audit.

The requirements for furnishing data on twenty day notice (obviously for audit) includes a lot of things you are bound to have, but also:

Copies of the original lease, farm-out assignments, and all other legal instruments which affect the right to produce.

supporting documentation for any subdivisions, geographically or by formation.

Production records, including the dates the initial well was commenced or reworking began, and the date of completion or recompletion; the date of installation of production facilities (tanks, gathering system, etc.); and the identity of the first purchaser of any oil, and of oil in commercial quantities.

So much for certification. Now for some good news:

PL 96-499

Congress passed the \$1,000 credit for royalty owners (only individuals or "farm corporations") but not for working interests. A credit can be taken on their tax returns for all WPT withheld, up to \$1,000. Since the returns are already printed, just where this is to be inserted on the form is not yet clear.

WPT inflation adjustment factors for use in the first quarter of 1981 have been declared to be 1.1187 for Tiers 1 and 2, and 1.1469 for Tier 3.

Extensions have been granted for various filings of WPT data. The revised timetable is as follows:

First purchasers must notify producers as to WPT withheld during 1980 by 1/31/81. This is the amount you can deduct as a business expense in your 1980 return. You may find this figure on your Form 1099 from the pipeline. Producers who redistribute to other producers, and partnerships, have another 15 days to pass this data on.

First purchasers must file Form 6248, which is the official annual WPT information return, by 3/31/81. This includes data on all WPT withheld on oil purchased in 1980 (including that paid for in 1981). One Form 6248 is filed for each producer, covering all leases from which the first purchaser makes payment to such producer. If he redistributes, the producer similarly issues a single Form 6248 for each party to whom he redistributes. There appears to be no way in which anyone will ever be able to make any sense out of these reports; but a copy must be attached to any claim for refund, so don't throw it away. Copies of these Form 6248's must be filed with IRS (including those from redistributors) by 4/30/81.

Underpayment of WPT must be corrected by payment accompanied by Form 6249 (which is not yet available in final form) by 5/31/81. After that date, interest and penalties will be charged.

continued ...

First purchasers may make corrections in tax withheld at any time before they file their Form 6248. Since it will be simpler to have them correct mistakes than to file with IRS (and also less likely to inspire audits), keep after the pipelines to make corrections as soon as possible.

Now, about the happier subject of refunds of WPT: There will be more than IRS had dreamed. They may be claimed as credits in your 1980 return; but it seems unlikely that the data to compute them will be fully available by the time you file (due in no small part to the fact that Regs promised in October have not yet appeared).

The alternative procedure for handling refunds, which will be used in most cases, is to file Form 843. This form, designed to handle overpayments of excise taxes, does not really fit WPT, and will probably be supported by both Forms 6248 and 6249, neither of which is available in final form. Forms 843 have heretofore been processed by the dozen, and are expected to be filed by the thousands for WPT refunds. In other words, refunds will be some time in materializing.

Calculation of some aspects of Net Income Limitation (NIL) remain swathed in mystery, until the missing Regs are published. However, some progress has been made in how to determine which leases may qualify.

All Tier 1 leases (both old and new oil) will qualify for 15% or more refund, without regard to operating expenses or "as-if" cost depletion. This means that even royalty owners with Tier 1 interests will be entitled to a refund - although the cost of preparing the claims may exceed the refunds. Operators should notify them, and also start computing expenses, depletion, etc.

Only "high-cost" Tier 2 and Tier 3 leases will qualify. How high is "high-cost" has been dodged in most WPT seminars. However, IOPA calculations, based on Tri-State prices and severance tax rates (which, by changing the "windfall", affect the calculation) indicate that for 40 gravity oil, a lease will qualify (before "as-if" depletion or depreciation) if its lifting cost per barrel exceeds:

	<u>Tier 2</u>	<u>Tier 3</u>
Illinois	\$14.85	\$16.90
Indiana	15.10	17.10
Kentucky	15.70	17.60

This limit is increased by about one cent for each point of gravity below 40. If the lifting costs exceed these figures by any substantial amount, a full-scale calculation may produce enough refund to make it worth while. YOU SAW THIS HERE FIRST!!

Claims for NIL refunds can (if they tell us how) before filed after 2/28/81 by calendar year taxpayers. Fiscal year taxpayers can file on the portion of their fiscal year between 3/1/80 and the end of the fiscal year after 2/28/81, on the portion between the end of their fiscal year and 12/31/81 in their 1980-81 return, and on the rest of their fiscal year after 2/28/82. Fiscal years are becoming less fun.

HAPPY NEW YEAR!! It can't be any more confusing than 1980!!

press: Carpenter AT
Kizer AP
Capital 81(?)
PGinzburg APRN

(left)
Gordian Malone Royce, Hayes, Vasco, Halford, Randolph
& Fanning (left)

HB 33 - PACE

2/17
full committee present

Gordian

7⁰⁰ to 7²⁰ pm

- alt. to PF dividend program
similar goals

boom & bust economy / extraction

All one of richest political jurisdictions in world
\$17,000 per capita - modern economy - unlike LDC's.

but bad social problems - alcoholism

rich, but rich, educated populace

how long will bubble last - will cartel fall apart?

feds take it?

models:

/ European socialism / Venezuela

— Do we want to be controlled exclusively by corporations
owned by outsiders?

Royalty trust will be introduced — next week (?)

AGSOC different - outside the govt

State investment → project → one time distribution of assets
Not just cash, but asset that produces cash

Various combinations of free & preferred shares are
possible (BRIC example)

Malone - Public Purpose question (CAA 2/12 memorandum)

(725) Fran Ulmer

Gov Hammond enthusiastic about concept
want, to be involved

PACE general idea -

Gov supports HB 33

specific ~~parts~~ proposals need further evaluation

Gov -
early brainstorming w/ Bennett, BC premier

PACE emerged as substitute for AGSOL

prudent management includes 4

- save (PF)
- invest (loans, pf investments, development)
- spend (budget)
- share (pf dividends)

Solution lies in raising wealth, not debt of Alaskans

Avoid quasi-public organization w/ management prerogatives
Decisions should pass through budget process

PACE very different from PF program - would not
jeopardize PF suit.

735 Arlan Tussing

H. Finance - analysis of AGSOC - pointed out # of difficulties

Wanted to rescue what was good in AGSOC

BC experience - new govt had promised to de-socialize industries like, timber
auto insurance

experts - you couldn't do it yourselves

ministers - didn't want to give away good businesses

BC established holding company - for socialized businesses,
plus added mineral rights

each resident - 5 shares for free

could buy several thousand additional shares

at a fixed price

sold \$400 million worth of shares

Tussig, cont.

AGSOX - idea of direct participation in energy good
Gardner - buying out foreign ownership

745 pm

+ state intervention necessary for building pipeline
- state would pass out ownership interest
Success of BC - had profitable assets to distribute
AK owns no other assets but oil leases
ARRL could be privatized
don't start w/ turkey & lemons; Chrysler & lemons
biggest difficulty w/ PB - WPT
royalty oil must be used for "public purposes"
to be exempt
PB ng would be workable, Kuparuk oil

750

- distribution possibilities - gift or sale
HD 33 - BC model
bank through sale - often people would have hard time refuelling
marol - some sacrifice to obtain

755

less exposure to IRS liabilities less legal problems
serial warrants
people can take shares out of the state

800 pm

Dick Randolph - profit or no profit
AT - not a corporation. Trust is pass-through
depends on enterprise

Randolph - fed tax liabilities

AT - (explanation) see tax specialists

805 Halford - IRS has charged interest on no-interest loan if intent & benefit recipient is present
AT different - for public

Vasca - free shares v. purchased?
how many can one individual purchase?

AT - proxy voting - w/o it, no check on management

815 Randolph - qs, comments

820 Rogers - public purpose
assets directly & resident,
would least problem

Any oil co. which gives overriding royalty & royalty trust can deduct it from royalty payments (from tax payments)

AT - Const. Amendment solution

Gardiner - should let voters decide - amendment

830 - Art

1 IN THE HOUSE

BY GARDINER

2 HOUSE BILL NO. 33

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

5 A BILL

6 For an Act entitled: "An Act establishing the portfolio of Alaska citizen
7 enterprises; and providing for an effective date."

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

9 * Section 1. DECLARATION OF POLICY, PURPOSES AND FINDINGS. (a) It is
10 the policy of the state to provide for the use, development, and conserva-
11 tion of the state's natural resources and the income derived from them for
12 the maximum benefit of its people.

13 (b) The purposes of this Act are to

14 (1) transfer part of the wealth derived from the natural re-
15 sources of the state to its residents;

16 (2) provide a means for the direct participation of state resi-
17 dents in the financing of business enterprises which benefit the state, and
18 to provide residents with the opportunity to share in potential profits;

19 (3) reduce ownership and control of industries in the state by
20 nonresidents;

21 (4) encourage greater participation in and understanding of the
22 capitalist system by residents through a wider distribution of economic
23 interests in state business enterprises;

24 (5) encourage increased awareness and involvement by state resi-
25 dents in the management of state natural resource production and develop-
26 ment;

27 (6) encourage increased awareness and involvement by state resi-
28 dents in state participation in business enterprises; and

29 (7) encourage increased awareness and involvement by state resi-

1 dents in the development of local industry.

2 (c) The legislature finds that

3 (1) it is in the public interest and furthers a public purpose to
4 distribute a part of Alaska's wealth derived from natural resources to state
5 residents to increase their involvement and awareness regarding the manage-
6 ment of the state's natural resources, the development of its local industry,
7 and the capitalist system;

8 (2) a mechanism allowing the state to distribute a part of its
9 resource wealth to residents will best promote the state's interest in
10 creating direct involvement by residents in the decisions concerning the
11 state's natural resource management; and

12 (3) a mechanism allowing the state to distribute a part of its
13 ownership interests in business enterprises to residents will best promote
14 the state's interest in creating direct involvement by residents in the
15 decisions concerning state investments and development of local industry.

16 (d) Except as otherwise required by law, it is intended that distribu-
17 tions to residents under this Act shall be unencumbered property.

18 * Sec. 2. AS 43 is amended by adding a new chapter to read:

19 CHAPTER 17. PORTFOLIO OF ALASKA CITIZEN ENTERPRISES.

20 ARTICLE 1. PORTFOLIO OF ALASKA CITIZEN ENTERPRISES PROGRAM.

21 Sec. 43.17.010. ESTABLISHMENT OF PROGRAM. The portfolio of
22 Alaska citizen enterprises is established in the department to provide
23 for distribution of state assets to state residents.

24 Sec. 43.17.020. PORTFOLIO PLANS. (a) The department shall de-
25 velop portfolio plans for distribution of state assets. A portfolio
26 plan must

27 (1) provide for contribution or transfer of assets owned by
28 the state or to be acquired by the state;

29 (2) provide for distribution of interests in the assets

1 owned by the state or to be acquired by the state to eligible residents
2 by issuing certificates representing units of

3 (A) a state energy resource trust;

4 (B) a state industrial development project;

5 (C) a state general stock ownership corporation;

6 (D) a state investment fund;

7 (E) a state real estate trust;

8 (F) a business enterprise.

9 (3) specify the assets to be distributed;

10 (4) specify how the assets not then owned by the state will
11 be acquired by the state;

12 (5) specify the date on which an individual must be a state
13 resident to be eligible to participate in the distribution of units
14 under AS 43.17.060 - 43.17.090;

15 (6) specify how an individual applies for a unit;

16 (7) specify the types of assets involved, an appraisal of
17 their value, the number of units to be distributed, and the manner in
18 which the units will be distributed;

19 (8) specify the terms of payment for units to be sold and
20 the number of units to be distributed without charge;

21 (9) specify restrictions on the transfer or encumbrance by
22 the state of a distributed unit;

23 (10) provide a financial assessment of the portfolio plan
24 including

25 (A) administrative costs;

26 (B) initial costs;

27 (C) a projection of future costs;

28 (D) contingent costs or liabilities;

29 (E) a projection of future earnings;

1 (F) value of the units in the plan;

2 (G) probable financial and tax consequences for pur-
3 chasers and recipients of units;

4 (11) list and evaluate state and federal laws and regulations
5 affecting the portfolio plan;

6 (12) propose legislation needed to implement the portfolio
7 plan; and

8 (13) include other information considered necessary by the
9 commissioner.

10 (b) If a corporation or trust is needed to implement the port-
11 folio plan, the plan must include

12 (1) the proposed articles of incorporation and bylaws of the
13 corporation or the proposed trust indenture of the trust;

14 (2) the names of the incorporators and directors of the
15 corporation or the trustees of the trust or the method of selecting
16 those individuals.

17 Sec. 43.17.030. PORTFOLIO PLANS SUBMITTED TO LEGISLATURE. (a)
18 The commissioner shall submit one or more portfolio plans to the Second
19 Session of the Twelfth Legislature and to both regular sessions of the
20 Thirteenth Legislature. This submission shall be made on or before the
21 30th day of each legislative session.

22 (b) A portfolio plan may not be implemented until it has been
23 approved by law.

24 ARTICLE 2. DISTRIBUTION OF UNITS.

25 Sec. 43.17.050. ELIGIBILITY. (a) To be eligible to purchase a
26 unit under AS 43.17.080 - 43.17.090 or to receive a unit distributed
27 under AS 43.17.070, an individual must

28 (1) be a resident of the state on the eligibility date
29 established in the portfolio plan under which the unit is distributed;

1 (2) apply to the department; and

2 (3) submit with the application a signed, sworn certifica-
3 tion that he was a resident of the state on the eligibility date and
4 other proof of residency as the commissioner may require, including

5 (A) evidence that he was registered to vote in Alaska
6 on the eligibility date, and actually voted in the last statewide
7 general election before that date;

8 (B) an Alaska driver's license, or a resident hunting,
9 fishing, or trapping license, issued on or before the eligibility
10 date, and valid on the eligibility date;

11 (C) evidence that, on the eligibility date, he had
12 telephone or utility service at a residence in the state listed in
13 his name or in the name of a spouse, or, if the individual is a
14 minor, in the name of a parent or guardian;

15 (D) an affidavit of one or more individuals having
16 personal knowledge concerning his residency on the eligibility
17 date; and

18 (E) other documentary evidence of residency acceptable
19 to the commissioner.

20 (b) An individual is presumed to be a resident of the state on
21 the eligibility date if he provides at least two items specified in
22 (a)(3) of this section.

23 (c) The department shall prescribe and furnish a form for ap-
24 plications and for certification of residency.

25 Sec. 43.17.060. NUMBER AND PURCHASE PRICE OF UNITS ISSUED. (a)
26 For each portfolio plan the commissioner shall establish a purchase
27 price for each unit to be sold under AS 43.17.080 - 43.17.090. The
28 price for each unit may not exceed \$50.

29 (b) The commissioner shall determine the total number of units to

1 be distributed under a portfolio plan by dividing the value of the
2 assets contributed under the plan by the purchase price for a unit
3 established under (a) of this section.

4 (c) The value of assets contributed to a state industrial develop-
5 ment project, a state general stock ownership corporation, a state
6 investment fund, a state real estate trust, or a business enterprise,
7 is equal to the cost to the state of the assets contributed to the
8 portfolio plan, plus an amount that compensates the state for the
9 administrative costs of acquiring, holding, and distributing those
10 assets.

11 (d) The value of assets contributed to a state energy resource
12 trust is the conservatively appraised value of the assets. A con-
13 servatively appraised value for assets in a state energy resource trust
14 is a value determined by generally accepted appraisal methods and shall
15 be calculated using

16 (1) estimates of resource production volumes having an accu-
17 racy confidence level of 75 percent or greater;

18 (2) an assumed rate of increase in future world prices for
19 resources not exceeding the general rate of price inflation in the
20 United States; and

21 (3) a discount rate reflecting the judgment of private in-
22 vestors as to the expected rate of return before payment of taxes re-
23 quired to justify incremental investments in the exploration and de-
24 velopment of resources comparable to those committed under a portfolio
25 plan.

26 (e) Before a sale of units, the commissioner shall publish notice
27 of the purchase price..

28 Sec. 43.17.070. FREE DISTRIBUTION. A part of the units to be
29 distributed in accordance with AS 43.17.060(b) shall be distributed

HAZY
↓

1 equally without charge to all eligible individuals who apply to receive
2 them. The number of the units to be distributed under this section
3 shall total at least five percent, but not more than 15 percent, of all
4 units to be distributed.

5 Sec. 43.17.080. FIRST RESTRICTED SALE. (a) The commissioner
6 shall offer for sale in a first restricted sale all units authorized to
7 be distributed under a portfolio plan, other than those distributed
8 without charge under AS 43.17.070.

9 (b) In a first restricted sale, an individual may subscribe for
10 any number of units by submitting an application and certificate of
11 residency under AS 43.17.050 and a deposit equal to 10 percent of the
12 purchase price of the units. The deposit must be in the form of cash,
13 check, or money order. The individual shall indicate on his applica-
14 tion whether he wishes to pay for the units at one time or under an
15 extended purchase plan.

16 (c) If a sale is oversubscribed, each eligible individual apply-
17 ing under this section may purchase the lesser of

18 (1) the number of units he applied for; or

19 (2) the number of units which allows for an equal distribu-
20 tion among all applicants of the units authorized for sale.

21 (d) The commissioner shall notify each subscriber who elects to
22 pay for units at one time of the total number of units he is entitled
23 to purchase and the balance due. On receipt of cash, check, or money
24 order equal to the balance due, the commissioner shall issue to the
25 subscriber a certificate for each unit purchased. If the subscriber
26 fails to complete the purchase within 60 days of notification, the
27 commissioner shall issue to him the number of units paid for by the
28 deposit, and refund any balance remaining from the deposit.

29 (e) The commissioner shall notify each subscriber who elects to

1 pay for units under an extended payment plan of the total number of
2 units that he is entitled to purchase in the first restricted sale, and
3 issue to him

4 (1) certificates for one-tenth of the units;

5 (2) a refund of the difference, if any, between the deposit
6 and the purchase price for the number of units represented by certifi-
7 cates issued; and

8 (3) purchase warrants in accordance with AS 43.17.110 for
9 nine-tenths of the units.

10 Sec. 43.17.090. SECOND RESTRICTED SALE. (a) If the first re-
11 stricted sale under a portfolio plan is undersubscribed and if the plan
12 authorizes a second restricted sale, the commissioner shall conduct a
13 second restricted sale.

14 (b) At a second restricted sale an individual may submit one or
15 more sealed bids, each of which must specify the number of units that
16 he wishes to purchase and a bid price for each unit. The bid price
17 must equal or exceed a minimum bid price specified by the commissioner,
18 which may be less than, equal to, or more than the purchase price at
19 the first restricted sale.

20 (c) The sealed bid must be accompanied by an application and
21 certificate of residency under AS 43.17.050 and by a deposit equal to
22 10 percent of the total bid price. The deposit must be in the form of
23 cash, check, or money order.

24 (d) The commissioner shall tally the bids in descending order of
25 bid price, until the total number of units bid for equals the number of
26 units to be sold. If the number of units to be sold exceeds the number
27 of units bid for, the commissioner shall accept the bids that have been
28 tallied. If the number of units to be sold is less than the number of
29 units bid for, the commissioner shall accept all bids equal to or

1 greater than the specified minimum bid price.

2 (e) Units sold at a second unrestricted sale must be paid for at
3 one time. The commissioner shall notify a successful bidder of the
4 total number of units he is entitled to purchase and of the balance
5 due. On receipt of cash, check, or money order the commissioner shall
6 issue to the bidder certificates representing the units purchased. If
7 the bidder fails to complete the purchase within 60 days, the commis-
8 sioner shall issue to him certificates representing the number of units
9 paid for by the deposit and refund any balance remaining from the de-
10 posit.

11 Sec. 43.17.100. UNRESTRICTED SALE. Except as expressly pro-
12 hibited by this chapter or under the terms of a portfolio plan, the
13 commissioner may hold as investments or may sell those units authorized
14 to be distributed under a portfolio plan which remain undistributed
15 after completion of the free distribution, the first restricted sale,
16 and the second restricted sale, and which are not reserved under pur-
17 chase warrants.

18 Sec. 43.17.110. PURCHASE WARRANTS. (a) A purchase warrant
19 entitles a subscriber to purchase nine-tenths of the number of units he
20 was entitled to purchase in a first restricted sale according to the
21 following schedule:

22 (1) one-tenth of the units not later than one year after the
23 purchase warrant was issued;

24 (2) one-tenth of the units not later than two years after
25 the purchase warrant was issued;

26 (3) one-tenth of the units not later than three years after
27 the purchase warrant was issued;

28 (4) one-tenth of the units not later than four years after
29 the purchase warrant was issued;

1 (5) one-tenth of the units not later than five years after
2 the purchase warrant was issued;

3 (6) one-tenth of the units not later than six years after
4 the purchase warrant was issued;

5 (7) one-tenth of the units not later than seven years after
6 the purchase warrant was issued;

7 (8) one-tenth of the units not later than eight years after
8 the purchase warrant was issued;

9 (9) one-tenth of the units not later than nine years after
10 the purchase warrant was issued.

11 (b) The total price for a unit purchased with a purchase warrant
12 is the purchase price of the unit at the time of the first restricted
13 sale increased by an amount equal to the weighted average rate of
14 interest paid by the state on bonds issued after the first restricted
15 sale and before the time the purchase warrant is used compounded from
16 the date the purchase warrant was issued to the date of payment for the
17 units. The purchase price shall be decreased by the amount of divi-
18 dends, interest, royalties, or profits received by the state from
19 holding the units between the date the purchase warrant was issued and
20 the date of payment for the units, except that the price may not be
21 reduced below 50 percent of the purchase price for a unit at the time
22 of the first restricted sale.

23 (c) Payment for units purchased using a purchase warrant may be
24 made by cash, check, or money order.

25 (d) A purchase warrant is void if transferred. A purchase warrant
26 may not be used except by an individual who is a resident of the state.

27 Sec. 43.17.120. DISPOSITION OF PROCEEDS. The commissioner shall
28 deposit net proceeds from the sale of units under this chapter into the
29 Alaska permanent fund established in art. IX, sec. 15 of the state

1 constitution and AS 37.13.010.

2 ARTICLE 3. GENERAL PROVISIONS.

3 Sec. 43.17.150. DISPOSITION OF UNITS. (a) Except as provided in
4 (b) of this section, an individual has an unrestricted right to sell,
5 transfer, devise, pledge or dispose of a unit, an interest in a unit,
6 or earnings from a unit which is his.

7 (b) A portfolio plan for a state general stock ownership corpora-
8 tion or for a state energy resource trust may include restrictions on
9 the transfer or disposition of units in the corporation or trust.

10 Sec. 43.17.160. VOTING RIGHTS. (a) The commissioner may exer-
11 cise the voting rights attached to a unit that the state owns, holds in
12 trust, or reserves for future distribution.

13 (b) The voting rights attached to ownership of a unit distributed
14 under a portfolio plan must be conveyed unrestricted to the individual
15 receiving the unit. The commissioner may not reserve a voting right or
16 require as a condition of the distribution that the recipient waive a
17 voting right, grant a proxy, or adhere to a voting trust.

18 Sec. 43.17.170. AUTHORITY TO PARTICIPATE IN MARKET. (a) If the
19 commissioner determines that an efficient public market does not exist
20 for the sale of units, he may buy, sell, and trade in units for the
21 purpose of establishing a market.

22 (b) If the commissioner trades in units as authorized in (a) of
23 this section, he shall maintain an average markup sufficient to compen-
24 sate the state for the administrative costs of his trading activity and
25 shall publish regularly the bid and asking prices for units traded.

26 (c) In this section, "efficient public market" means a market in
27 which the units distributed under this chapter have a readily ascer-
28 tainable market value and in which they may be bought or sold readily
29 without unnecessary or unreasonable transaction costs.

*What
a plan
necessary
include
voting
rights*

1 Sec. 43.17.180. WAIVER OF RESTRICTIONS. AS 37.10.085 does not
2 apply to the acquisition of assets under this chapter.

3 Sec. 43.17.190. REGULATIONS. The department may adopt regula-
4 tions necessary to administer this chapter.

5 Sec. 43.17.200. PENALTIES. In addition to any criminal penalties
6 imposed, if an individual is convicted of perjury or unsworn falsifica-
7 tion on the basis of a certification made under AS 43.17.050 and the
8 conviction is not reversed, he is not eligible for a distribution of
9 units under this chapter.

10 Sec. 43.17.210. DEFINITIONS. In this chapter,

11 (1) "assets" means shares of stock, debentures or other debt
12 obligations, royalties or other interests in minerals, or other inter-
13 ests in business enterprises or natural resources;

14 (2) "business enterprise" means a private corporation en-
15 gaging or about to engage in the state in manufacturing, transportation,
16 communication, trade, services, natural resource extraction, or natural
17 resource processing, whose securities the commissioner has purchased
18 under AS 37.10, or has proposed to purchase under the terms of a port-
19 folio plan established under this chapter;

20 (3) "certificate" means an instrument evidencing ownership
21 of one or more units and includes stock certificates, debentures or
22 other debt instruments and trust certificates;

23 (4) "commissioner" means the commissioner of revenue;

24 (5) "department" means the Department of Revenue;

25 (6) "eligibility date" means a date established by the
26 commissioner for a distribution of units under a portfolio plan estab-
27 lished under this chapter;

28 (7) "extended purchase plan" means the purchase of units
29 over a period of time through the exercise of purchase warrants;

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29

(8) "individual" means a natural person;

(9) "oversubscribed" means a sale in which the total number of units subscribed for exceeds the total number of units available for sale;

(10) "purchase warrant" means an instrument authorizing the purchase of units under this chapter;

(11) "resident" means an individual who maintains a permanent place of abode in the state with the intention of making the state his permanent residence and who stays in the state continuously except for temporary absences taken with the intent of returning; an individual is not a resident solely by reason of his presence and does not cease to be a resident solely by reason of his absence because of marriage to a person engaged in the civil or military service of this state or the United States; an individual does not cease to be a resident while a student at an educational institution, while in an institution at public expense, while confined in prison, while engaged in the navigation of waters of this state, of the United States, or of the high seas, or while residing in an Indian or military reservation; a minor takes the residence of his parent or of his legal guardian; a married woman may establish her own residence and does not presumptively take the residence of her husband;

(12) "state energy resource trust" means a trust established under this chapter the assets of which consist of a right to receive income equal to a specified part of the rentals, royalties, or net profits belonging to the state under specified leases of state land for the extraction of oil, gas, coal, oil shale, or other minerals or a specified part of the revenue from the sale of oil, gas, coal, oil shale, or other minerals taken by the state as in kind royalties under those leases;

1 (13) "state general stock ownership corporation" means a
2 corporation formed in accordance with subchapter U, Chapter 1 of the
3 Internal Revenue Code of 1954, as amended (26 U.S.C. secs. 1391 -
4 1397);

5 (14) "state industrial development project" means a business
6 enterprise engaged or about to engage in the state in manufacturing,
7 transportation, communications, natural resource extraction, or natural
8 resource processing, and to which the state or an agency or subdivision
9 of the state contributes an investment of equity or debt exceeding
10 \$100,000,000;

11 (15) "state investment fund" means a regulated investment
12 company organized in accordance with subchapter M, Chapter 1 of the
13 Internal Revenue Code of 1954 as amended (26 U.S.C. secs. 851 - 855);

14 (16) "state real estate trust" means a real estate investment
15 trust organized in accordance with subchapter M, Chapter 1 of the
16 Internal Revenue Code of 1954 as amended (26 U.S.C. secs. 856 - 858);

17 (17) "undersubscribed" means a sale in which the total number
18 of units available for sale exceed the number of units subscribed;

19 (18) "unit" means an undivided fractional ownership right or
20 interest in a trust, corporation, fund, project or enterprise estab-
21 lished under this chapter.

22 * Sec. 3. This Act takes effect immediately in accordance with AS 01.10.-
23 070(c).

Introduced: 4/15/80
Referred: Finance

1 IN THE HOUSE

BY THE RULES COMMITTEE

2 HOUSE BILL NO. 1006

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 ELEVENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act establishing the portfolio of Alaska citizen
7 enterprises; and providing for an effective date."

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

9 * Section 1. DECLARATION OF POLICY, PURPOSES AND FINDINGS. (a) It is
10 the policy of the state to provide for the utilization, development and
11 conservation of the state's natural resources and the income derived from
12 them for the maximum benefit of its people.

13 (b) The purposes of this Act are to

14 (1) transfer part of the wealth derived from the natural resources
15 of the state to its residents;

16 (2) provide a means for the direct participation of state resi-
17 dents in the financing of business enterprises which benefit the state, and
18 to provide residents with the opportunity to share in potential profits;

19 (3) reduce ownership and control of industries in the state by
20 nonresidents;

21 (4) encourage greater participation in and understanding of the
22 capitalist system by residents through a wider distribution of economic
23 interests in state business enterprises;

24 (5) encourage increased awareness and involvement by state resi-
25 dents in the management of state natural resource production and development;

26 (6) encourage increased awareness and involvement by state resi-
27 dents in state participation in business enterprises; and

28 (7) encourage increased awareness and involvement by state resi-
29 dents in the development of local industry.

1 (c) The legislature finds that

2 (1) it is in the public interest and furthers a public purpose to
3 distribute a part of Alaska's wealth derived from natural resources to state
4 residents to increase their involvement and awareness regarding the management
5 of the state's natural resources, the development of its local industry, and
6 the capitalist system;

7 (2) a mechanism allowing the state to distribute a part of its
8 resource wealth to residents will best promote the state's interest in creat-
9 ing direct involvement by residents in the decisions concerning the state's
10 natural resource management; and

11 (3) a mechanism allowing the state to distribute a part of its
12 ownership interests in business enterprises to residents will best promote
13 the state's interest in creating direct involvement by residents in the
14 decisions concerning state investments and development of local industry.

15 (d) Except as otherwise required by law, it is intended that distribu-
16 tions to residents under this Act shall be unencumbered property.

17 * Sec. 2. AS 43 is amended by adding a new chapter to read:

18 CHAPTER 17. PORTFOLIO OF ALASKA CITIZEN ENTERPRISES.

19 ARTICLE 1. PORTFOLIO OF ALASKA CITIZEN ENTERPRISES PROGRAM.

20 Sec. 43.17.010. ESTABLISHMENT OF PROGRAM. The portfolio of Alaska
21 citizen enterprises is established in the Department of Revenue to
22 provide for distribution of state assets to state residents.

23 Sec. 43.17.020. PORTFOLIO PLANS. The department shall develop
24 portfolio plans for distribution of state assets. A portfolio plan must
25 provide for

26 (1) contribution or transfer of assets owned by the state or
27 to be acquired by the state;

28 (2) distribution of interests in the assets to eligible
29 residents by issuing certificates representing units of

- 1 (A) a state energy resource trust;
- 2 (B) a state industrial development project;
- 3 (C) a state general stock ownership corporation;
- 4 (D) a state investment fund;
- 5 (E) a state real estate trust;
- 6 (F) business enterprises.

7 Sec. 43.17.030. PORTFOLIO PLANS SUBMITTED TO LEGISLATURE. (a)
8 Beginning with the First Session of the Twelfth Legislature and ending
9 with the First Session of the Thirteenth Legislature, the commissioner
10 shall submit to the legislature, on or before the 30th day of each
11 legislative session, one or more portfolio plans.

12 (b) A portfolio plan submitted to the legislature under this
13 section must

- 14 (1) specify the assets to be distributed;
- 15 (2) specify the manner in which the assets not then owned by
16 the state will be acquired by the state;
- 17 (3) specify the date on which a person must be a state resi-
18 dent to be eligible to participate in the distribution of units under
19 AS 43.17.060 - 43.17.090;
- 20 (4) specify the manner in which a person must apply to pur-
21 chase or receive a unit;
- 22 (5) specify the types of assets involved, an appraisal of
23 their value, the number of units to be distributed, and the manner in
24 which they are to be distributed;
- 25 (6) specify the terms of payment for units to be sold and the
26 number of units to be distributed free;
- 27 (7) specify restrictions on the transfer or encumbrance of a
28 unit distributed by the state;
- 29 (8) propose needed legislation;

1 (9) include proposed articles of incorporation and bylaws of
2 a corporation or the proposed trust indenture of a trust needed to
3 implement the plan;

4 (10) if a corporation or trust is needed to implement the
5 plan, include a method of selection or the names of the incorporators
6 and initial directors of a corporation and trustees of a trust;

7 (11) provide a financial assessment of the plan including

8 (A) administrative costs;

9 (B) initial costs;

10 (C) a projection of future costs;

11 (D) contingent costs or liabilities;

12 (E) a projection of future earnings;

13 (F) value of units;

14 (G) probable financial and tax consequences for pur-
15 chasers and recipients of units;

16 (12) assess applicable state or federal laws or regulations;

17 and

18 (13) provide other information considered necessary by the
19 commissioner.

20 Sec. 43.17.040. LEGISLATIVE APPROVAL. (a) A portfolio plan may
21 not be implemented until it has been approved by the legislature by law.

22 ARTICLE 2. DISTRIBUTION OF UNITS.

23 Sec. 43.17.050. ELIGIBILITY. (a) To be eligible to purchase a
24 unit under AS 43.17.080 - 43.17.090 or to receive a unit distributed
25 under AS 43.17.070, a person must

26 (1) be a resident of the state on the eligibility date estab-
27 lished in the portfolio plan under which the unit is distributed;

28 (2) file an application; and

29 (3) submit with the application a signed, sworn certification

1 that the person was a resident on the eligibility date and other proof
2 of residency as the commissioner may require.

3 (b) Other proof of residency under (a)(3) of this section may
4 include

5 (1) evidence that the person was registered to vote in Alaska
6 on the eligibility date, and actually voted in the last statewide general
7 election before that date;

8 (2) a copy of the person's Alaska resident income tax return
9 for the tax year which includes the eligibility date, or for the previous
10 tax year;

11 (3) an Alaska driver's license, or a resident hunting, fish-
12 ing, or trapping license, issued before the eligibility date, and valid
13 on that date;

14 (4) evidence that the person had telephone or utility service
15 at a private residence in the state on the eligibility date listed in
16 his name or in the name of a spouse, or in the name of a parent or
17 guardian if the person is a minor;

18 (5) an affidavit of one or more individuals having personal
19 knowledge concerning the person's residency on the eligibility date; and

20 (6) other documentary evidence of residency acceptable to the
21 commissioner.

22 (c) A person is presumed to be a resident on the eligibility date
23 if he provides at least two items specified in (b) of this section.

24 (d) The department shall prescribe and furnish a form for ap-
25 plications and for certification of residency.

26 Sec. 43.17.060. NUMBER AND PURCHASE PRICE OF UNITS ISSUED. (a)
27 For each portfolio plan the commissioner shall establish a purchase
28 price for each unit to be sold under AS 43.17.080 - 43.17.090. The
29 price for each unit may not exceed \$50.

1 (b) The commissioner shall determine the number of units to be
2 distributed and sold by dividing the value of the assets contributed
3 under the portfolio plan by the purchase price of a unit established
4 under (a) of this section.

5 (c) The value of assets contributed to a state industrial develop-
6 ment project, a state general stock ownership corporation, a state
7 investment fund, a state real estate trust, or a business enterprise, is
8 equal to the cost to the state of the assets contributed to the portfolio
9 plan, plus an amount that compensates the state for the administrative
10 costs of acquiring, holding, and distributing those assets.

11 (d) The value of assets contributed to a state energy resource
12 trust is the conservatively appraised value of the assets contributed to
13 the trust. A conservatively appraised value for assets in a state
14 energy resource trust is a value determined by generally accepted apprai-
15 sal methods and shall be calculated using

16 (1) estimates of resource production volumes having an accu-
17 racy confidence level of 75 percent or greater;

18 (2) an assumed rate of increase in future world prices for
19 resource commodities not exceeding the general rate of price inflation
20 in the United States; and

21 (3) a discount rate reflecting the judgment of private in-
22 vestors as to the expected rate of return before payment of taxes re-
23 quired to justify incremental investments in the exploration and develop-
24 ment of resources comparable to those committed under a portfolio plan.

25 (e) Before a sale of units, the commissioner shall publish notice
26 of the purchase price.

27 Sec. 43.17.070. FREE DISTRIBUTION. A part of the total number of
28 units to be distributed under a portfolio plan shall be granted in equal
29 parts without consideration to all eligible persons who apply to receive

1 them. The part of the units to be distributed under this section shall
2 be at least five percent, but not more than 15 percent, of the total
3 number of units to be distributed unless otherwise required by law.

4 Sec. 43.17.080. FIRST RESTRICTED SALE. (a) The commissioner
5 shall offer for sale in a first restricted sale all units authorized to
6 be distributed under a portfolio plan, other than those distributed
7 under AS 43.17.070.

8 (b) In a first restricted sale, a person may subscribe for any
9 number of units by submitting an application and certificate of resi-
10 dency under AS 43.17.050 and a deposit equal to 10 percent of the pur-
11 chase price of the subscribed units. The deposit must be in the form of
12 cash, check, or money order.

13 (c) The person shall indicate on his application whether he wishes
14 to pay for the units at one time or under an extended purchase plan.

15 (d) If the sale is oversubscribed, each person subscribing under
16 this section may complete the purchase of the lesser of

17 (1) the number of units he subscribed for; or

18 (2) the number of units which allows for an equal distribu-
19 tion of all the units authorized for sale among all the subscribers.

20 (e) The commissioner shall notify each subscriber who elects to
21 pay for units at one time of the total number of units he is entitled to
22 purchase and of the balance due, after crediting his deposit, to complete
23 the purchase. On receipt of cash, check, or money order equal to the
24 balance due, the commissioner shall issue to the subscriber a certificate
25 for each unit purchased. If the subscriber fails to complete the pur-
26 chase as provided in this subsection within 60 days of notification, the
27 commissioner shall issue to him the number of whole units paid for by
28 the deposit, and refund any balance remaining from the deposit.

29 (f) The commissioner shall notify each subscriber who elects to

1 pay for units under an extended payment plan of the total number of
2 units that he is entitled to purchase in the first restricted sale, and
3 issue to him

4 (1) certificates for one-tenth of the units;

5 (2) a refund of the difference, if any, between the deposit
6 and the purchase price for the number of units represented by certifi-
7 cates issued; and

8 (3) purchase warrants under AS 43.17.110 for nine-tenths of
9 the units.

10 Sec. 43.17.090. SECOND RESTRICTED SALE. (a) If the first re-
11 stricted sale under a portfolio plan is undersubscribed and if the plan
12 authorizes a second restricted sale, the commissioner shall conduct a
13 second restricted sale.

14 (b) A person may submit one or more sealed bids, each of which
15 must specify the number of units that he wishes to purchase and a bid
16 price for each unit. The bid price must be equal to or exceed a minimum
17 bid price specified by the commissioner, which may be less than, equal
18 to, or more than the purchase price at the first restricted sale.

19 (c) A sealed bid must be accompanied by an application and certifi-
20 cate of residency under AS 43.17.050 and by a deposit equal to 10 percent
21 of the total bid price. The deposit must be in the form of cash, check,
22 or money order.

23 (d) The commissioner shall tally the bids in descending order of
24 bid price, until the total number of units bid for equals the number of
25 units to be sold. If the number of units to be sold exceeds the number
26 of units bid for, the commissioner shall tally all bids at or above the
27 minimum bid price. The commissioner shall accept each bid that has been
28 tallied.

29 (e) Units sold in a second unrestricted sale may not be paid for

1 under an extended payment plan. The commissioner shall notify a success-
2 ful bidder of the total number of units he is entitled to purchase and
3 of the balance due, after crediting his deposit, to complete the pur-
4 chase. On receipt of cash, check or money order the commissioner shall
5 issue to the bidder certificates representing the units purchased. If
6 the bidder fails to complete the purchase within 60 days, the commis-
7 sioner shall issue to him certificates representing the number of whole
8 units paid for by the deposit, and refund any balance remaining from the
9 deposit.

10 Sec. 43.17.100. UNRESTRICTED SALE. Except as expressly prohibited
11 by this chapter or under the terms of a portfolio plan, the commissioner
12 may hold as investments or may sell for maximum revenue any units autho-
13 rized to be distributed under a portfolio plan which remain undistributed
14 after completion of the free distribution, the first restricted sale,
15 and the second restricted sale, and which are not reserved under issued
16 purchase warrants.

17 Sec. 43.17.110. PURCHASE WARRANTS. (a) Purchase warrants issued
18 under AS 43.17.080(f) entitle a subscriber to purchase under an extended
19 payment plan nine-tenths of the number of units which the subscriber was
20 entitled to purchase in a first restricted sale on the following
21 schedule:

22 (1) one-tenth not later than one year after the purchase
23 warrant was issued;

24 (2) one-tenth not later than two years after the purchase
25 warrant was issued;

26 (3) one-tenth not later than three years after the purchase
27 warrant was issued;

28 (4) one-tenth not later than four years after the purchase
29 warrant was issued;

1 (5) one-tenth not later than five years after the purchase
2 warrant was issued;

3 (6) one-tenth not later than six years after the purchase
4 warrant was issued;

5 (7) one-tenth not later than seven years after the purchase
6 warrant was issued;

7 (8) one-tenth not later than eight years after the purchase
8 warrant was issued;

9 (9) one-tenth not later than nine years after the purchase
10 warrant was issued.

11 (b) The total price for a unit purchased under this section shall
12 be the purchase price of the unit at the time of the first restricted
13 sale under AS 43.17.080 increased by an amount equal to the weighted
14 average rate of interest to be paid by the state on bonds issued during
15 the prior fiscal year compounded from the date the purchase warrant was
16 issued to the date of payment for the units. The purchase price shall
17 be decreased by the amount of dividends, interest, royalties, or profits
18 received by the state from holding the units between the date the pur-
19 chase warrant was issued and the date of payment for the units, but the
20 price may not be reduced below 50 percent of the purchase price for the
21 units at the time of the first restricted sale.

22 (c) Payment for units purchased by exercising a purchase warrant
23 may be made by cash, check or money order.

24 (d) A purchase warrant may not be transferred, and may not be
25 exercised except by a person who is a resident at the time the purchase
26 warrant is exercised. A purchase warrant is void if transferred.

27 Sec. 43.17.120. DISPOSITION OF PROCEEDS. The commissioner shall
28 deposit net proceeds from the sale of units under this chapter into the
29 Alaska permanent fund established in art. IX, sec. 15 of the state

1 constitution and AS 37.13.010.

2 ARTICLE 3. GENERAL PROVISIONS.

3 Sec. 43.17.130. DISPOSITION OF UNITS. (a) Except as provided in
4 (b) of this section, a person has an unrestricted right to sell, trans-
5 fer, devise, pledge or dispose of a unit, an interest in a unit, or
6 earnings from a unit.

7 (b) A portfolio plan for a state general stock ownership corpora-
8 tion or for a state energy resource trust may include restrictions on
9 the transfer or disposition of units in the corporation or trust.

10 Sec. 43.17.140. VOTING RIGHTS. (a) The commissioner may exercise
11 the voting rights attached to a unit that the state owns, holds in
12 trust, or reserves for future distribution.

13 (b) The voting rights attached to ownership of a unit distributed
14 under a portfolio plan must be conveyed unrestricted to the person
15 receiving the unit. The commissioner may not reserve a voting right or
16 require as a condition of the distribution that the recipient waive a
17 voting right, grant a proxy, or adhere to a voting trust.

18 Sec. 43.17.150. TAX TREATMENT. (a) The receipt by a person of a
19 unit distributed under AS 43.17.070 - 43.17.090 is not taxable under
20 AS 43.20. Earnings from a unit and from a sale or transfer of a unit
21 are taxable under AS 43.20.

22 Sec. 43.17.160. CREDIT FOR FEDERAL TAXES PAID. If the receipt by
23 a person of a unit distributed under AS 43.17.070 - 43.17.090 is treated
24 as income under the Internal Revenue Code and if, as a result, the
25 person is required to pay additional federal income tax, the amount of
26 additional tax attributable to that income may be applied as a credit
27 against the person's Alaska individual income tax for the tax year in
28 which the additional federal income tax is paid.

29 Sec. 43.17.170. AUTHORITY TO PARTICIPATE IN MARKET. (a) If the

1 commissioner determines that an efficient public market does not exist
2 for the sale of units held by persons, he may buy, sell, and trade in
3 those units for the purpose of establishing that market. The commis-
4 sioner shall publish regularly the bid and ask prices for those units.

5 (b) If the commissioner trades in units as authorized in (a) of
6 this section, he shall maintain an average markup sufficient, in his
7 judgment, to compensate the state for the administrative costs of his
8 trading activity.

9 (c) In this section, "efficient public market" means a market in
10 which the units distributed under this chapter have a readily ascer-
11 tained market value and in which they may be bought or sold readily and
12 without unnecessary or unreasonable transaction costs.

13 Sec. 43.17.180. WAIVER OF RESTRICTIONS. AS 37.10.085 does not
14 apply to the acquisition of assets under this chapter.

15 Sec. 43.17.190. REGULATIONS. The department may adopt regulations
16 necessary to administer this chapter.

17 Sec. 43.17.200. PENALTIES. In addition to any criminal penalties
18 imposed, if a person is convicted of perjury or unsworn falsification on
19 the basis of a certification made under AS 43.17.050 and the conviction
20 is not reversed, that person is not eligible for a distribution of units
21 under this chapter.

22 Sec. 43.17.210. DEFINITIONS. In this chapter,

23 (1) "assets" means shares of stock, debentures or other debt
24 obligations, royalties or other interests in minerals, or other inter-
25 ests in business enterprises or natural resources;

26 (2) "business enterprise" means a private corporation engaging
27 in or about to engage in natural resource extraction or processing, or
28 in manufacturing, transportation, communication, trade or services in
29 the state, whose securities the commissioner has purchased under his

1 existing investment authority under AS 37.10, or has proposed to purchase
2 under the terms of a portfolio plan established under this chapter;

3 (3) "certificate" means an instrument evidencing ownership of
4 one or more units and includes stock certificates, debentures or other
5 debt instruments and trust certificates;

6 (4) "commissioner" means the commissioner of revenue;

7 (5) "department" means the Department of Revenue;

8 (6) "eligibility date" means a date established by the commis-
9 sioner for a distribution of units under a portfolio plan established
10 under this chapter;

11 (7) "extended purchase plan" means the purchase of units over
12 a period of time through the exercise of purchase warrants;

13 (8) "oversubscribed" means a sale in which the total number
14 of units subscribed for exceeds the total number of units available for
15 sale;

16 (9) "person" means a natural person;

17 (10) "purchase warrant" means an instrument authorizing the
18 purchase of units under this chapter;

19 (11) "resident" means a person who maintains a permanent place
20 of abode in the state with the intention of making the state his per-
21 manent place of residence and who resides in the state continuously
22 except for temporary purposes only and with the intent of returning; a
23 person may not be considered to have gained a residence solely by reason
24 of his presence and he may not lose it solely by reason of his absence
25 because of marriage to a person engaged in the civil or military service
26 of this state or the United States; a person may not be considered to
27 lose his residence while a student at an educational institution, while
28 in an institution at public expense, while confined in prison, while
29 engaged in the navigation of waters of this state, of the United States,

1 or of the high seas, or while residing upon an Indian or military reser-
2 vation; a minor takes the residence of his parent or of his legal guar-
3 dian; a married woman may establish her own residence and does not
4 presumptively take the residence of her husband;

5 (12) "state energy resource trust" means a trust established
6 under this chapter the assets of which are a right to receive income
7 equal to a specified part of the rentals, royalties, or net profits
8 belonging to the state under specified leases of state land for the
9 extraction of oil, gas, coal, oil shale, or other minerals or a speci-
10 fied part of the revenue from the sale of oil, gas, coal, oil shale, or
11 other minerals taken by the state as in kind royalties under those
12 leases;

13 (13) "state general stock ownership corporation" means a
14 corporation formed in accordance with subchapter U, Chapter 1 of the
15 Internal Revenue Code of 1954, as amended (26 U.S.C. secs. 1391 - 1397);

16 (14) "state industrial development project" means a business
17 enterprise engaged in or about to engage in natural resource extraction
18 or processing, or in manufacturing, transportation, or communications in
19 the state, and to which the state or an agency or subdivision of the
20 state contributes an investment of equity or debt exceeding \$100,000,000;

21 (15) "state investment fund" means a regulated investment
22 company organized in accordance with subchapter M, Chapter 1 of the
23 Internal Revenue Code of 1954 as amended (26 U.S.C. secs. 851 - 855);

24 (16) "state real estate trust" means a real estate investment
25 trust organized in accordance with subchapter M, Chapter 1 of the
26 Internal Revenue Code of 1954 as amended (26 U.S.C. secs. 856 - 858);

27 (17) "undersubscribed" means a sale in which the total number
28 of units available for sale exceed the number of units subscribed;

29 (18) "unit" means an undivided fractional ownership right or

1 interest in a trust, corporation, fund, project or enterprise established
2 under this chapter.

3 * Sec. 3. The enactment of a version of Senate Bill No. 170 or House Bill
4 No. 240 relating to general stock ownership corporations and creating the
5 Alaska General Stock Ownership Corporation constitutes approval of a portfolio
6 plan under AS 43.17.030 enacted by sec. 2 of this Act. After enactment of
7 either, the commissioner of revenue shall implement the portfolio plan in
8 accordance with this Act, subject to necessary appropriation. If the port-
9 folio plan is approved under this section, the commissioner of revenue may,
10 notwithstanding the approval, submit to the legislature by the 30th day of
11 the First Session of the Twelfth Legislature a revised portfolio plan if in
12 his judgment a revised plan is necessary to accomplish the policy, purposes
13 and findings under this Act or to provide complete information concerning the
14 plan. A revised portfolio plan submitted under this section is subject to
15 legislative approval under AS 43.17.030.

16 * Sec. 4. This Act takes effect immediately in accordance with AS 01.10.-
17 070(c).

18
19
20
21
22
23
24
25
26
27
28
29