

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 8672

1573 SCOMM 59: JNT. COMMITTEE ON ECONOMIC RECOVERY, 1988

1370

Recommendations

The Department of Commerce and Economic Development, the Department of Community and Regional Affairs, the University of Alaska, the Division of Tourism, etc. to identify a few, should jointly budget and develop a comprehensive program to promote royalty-based product development investments that create permanent jobs at the least cost.

The Legislature should establish a broad-based economic index, written in law, which will enable the Legislature and the Governor to determine objectively the performance of the economy and its outlook and which will become the basis for formulating the state's fiscal policy.

This Alaska Economic Index should include indicators such as:

Consumer spending, savings and investments, public and private sector employment, wage and salary rates, housing starts, retail and wholesale sales, value on contract construction, personal income, gross state products and state revenues.

The Legislature should also:

Support passage of CSHB 430 (Labor and Commerce) - Neighborhood Business Development Fund

Support passage of HB 431 - Appropriation: Neighborhood Business Development Fund.

Support passage of HB 219 - Appropriation: Alaska Center/International Business

Support passage of HB 352/SB322 - Worker's Compensation

Note: Small Business Subcommittee received more correspondence and comments from small businesses on this subject than on any other piece of legislation.

Support passage of SB 166 - Regulations that Affect Small Businesses and Municipalities.

Support passage of CSHB 310 (Labor and Commerce) - Relating to Public Works and Public Construction.

Support passage of CSHB 45 - Relating to Alaska Business Bidder Preference.

Burt

SENATE JOINT COMMITTEE ON ECONOMIC RECOVERY
Agenda items for Meeting of March 14, 1988

Pat Steward wife (Marilyn Steward)

1. SB 484 - restructuring the debt of certain dairy farmers.
2. Willow Park Demolition Resolution.
3. SB 471 - establishing a program in the Alaska Industrial Development and Export Authority to guarantee business loans and to refinance debt.
4. Update on bridge-bank concepts. *check w/ Jim Kelly*
5. FDIC status report.
6. *7 digit liability resolution*

Handwritten signatures and initials:
Kodlen
Tuttle
Zharovsk 0/16
Dyghin
Jones
Arlin
Coughlin
Helford
Handwritten signature: [unclear]

SENATE JOINT COMMITTEE ON ECONOMIC RECOVERY

DATE: March 7, 1988

RE: Committee Endorsement of Legislation

The Senate Joint Committee on Economic Recovery has reviewed the following legislation and recommends passage by the Fifteenth Alaska Legislature.

SCR32 - by Senator Paul Fischer - "Urging the state's financial institutions to adopt more flexible lending and collection policies."

Status: House Labor & Commerce Committee.

This legislation urges banks, the Alaska Building Authority, the Alaska Industrial Development and Export Authority and other financial institutions to adopt a flexible position when servicing loans by amending procedures to allow for collection moratoriums and flexible payment schedules to allow for realistic and practical loan workouts.

SB333 - by Senator Rick Halford - "An Act relating to wage, salary and benefit claims having priority in certain bank liquidations and to certain bank reports required by the Department of Commerce and Economic Development; and providing for an effective date."

Status: House Labor & Commerce Committee

This bill provides for quarterly reporting by a bank of the financial condition of that bank. It also assigns a high priority to wage, salary and benefit claims in cases of certain bank liquidations.

SB392 - by Senator Rick Halford - "An Act relating to delinquent loans of the Alaska Industrial Development Authority; and providing for an effective date."

Status: House Labor & Commerce Committee

This bill allows the Authority the flexibility of adopting regulations defining under what circumstances AIDEA will discontinue purchasing loans from a financial institution because of the institution's loan default rate. Statute currently causes AIDEA to discontinue purchasing loans from an institution with a default rate of 2% or more.

SENATE COMMITTEE OF JOINT COMMITTEE ON ECONOMIC RECOVERY
March 16, 1988
5:00 P.M.

MEMBERS PRESENT

Senator Arliss Sturgulewski, Co-Chair
Senator Lloyd Jones, Co-Chair
Senator Jan Faiks
Senator Rick Halford
Senator Joe Josephson
Senator Jack Coghill
Senator Pat Rodey

MEMBERS ABSENT

Senator Dick Eliason
Senator Fred Zharoff

WITNESS REGISTER

Tony Gambiner, Chairman
The Hallwood Group
767 Third Avenue
New York, New York 10017
(212) 319-2360

Frank Cox, District Director
Small Business Administration
701 "C" Street
Anchorage, Alaska
(907) 271-4022

Nancy Gross, City Manager
City of Unalaska
P. O. Box 89
Unalaska, Alaska 99685

Gary Daily, Port Director
City of Unalaska
P. O. Box 89
Unalaska, Alaska 99685

Dennis Robinson
Ounalashka Corporation
Unalaska, Alaska 99685

ACTION NARRATIVE

Tape One, Side One
Number 002

Senator Sturgulewski, Senate Co-Chair, called the meeting to order at 5:10 p.m. Senator Tim Kelly was also in attendance.

Tony Gambiner, Hallwood Group, addressed the committee on the Hallwood Alaskan Real Estate Stabilization Trust (trust), or bridge bank, proposal. He said that Jim Cairns previously discussed the risk to Alaska's banking system

Senate Committee of
Joint Committee
on Economic Recovery

that would be caused if Alliance Bank would fail and the resulting decline of real estate values. They feel the state should take action to alleviate the problem. When they made the original proposal, they asked for an equity investment from the state of \$15 million with allowance for further borrowings. They are now asking for an appropriation limited to \$15 million, but it will only allow them to run the trust for one year. If, during that year, they are able to generate sufficient income from sales of the trust, without collapsing the local market, they will come back with a progress report. Then, if necessary, they will request the state to lend money to the trust.

They feel any action by the state should be conditional upon the FDIC agreeing to participate in the program. Otherwise, the FDIC might be expecting other opportunities for it to sell to third parties, which will be funded by some state agency. In responding to expressed concern that Hallwood, after its 18 month trust commitment, might put its shares in Alliance Bank back to the FDIC, Mr. Gambiner said Hallwood would be contractually obligated to run the trust for the ten year life of the trust. It is in their interest to run the trust because of their large investment in Alliance Bank. If they no longer have that investment, they would propose they pay a fee based on the negotiated pricing structure laid down between FDIC and the 27 beneficiary banks in the 27th Trust. They would then be compensated for the work they were doing, and would continue with their contractual obligation, unless it was felt they should be replaced.

Number 136

Senator Sturgulewski asked about their interest in Alaska Housing Finance Corporation (AHFC). Mr. Gambiner said they were not suggesting that the proposal be conditional upon AHFC joining in, since the state controls AHFC through its own authority. They have talked with Commissioner Tony Smith, Department of Commerce and Economic Development (DCED), and Mr. Gambiner thought the Commissioner was in favor of the project and he is to advise the Governor of his recommendation.

Number 158

Senator Josephson commented he had drafts of CSSB 408 () and CSSB 409 () for committee review. Mr. Gambiner had proposed amendments to the drafts as follows: CSSB 408 (), page 1, line 27, delete "corporations that have interests in" which would give them the power to take over failing banks rather than real estate portfolios.

They discussed whether the appropriation amount should be \$15 million or \$45 million in CSSB 409 () page 1, line 10.

Mr. Gambiner said the cost of the operation will depend on how much property is managed in the trust. If they assume the trust is limited to Alliance Bank, FDIC and AHFC's portfolios, they think the cost will be \$15 million a year to run it. Until such time as the marketing efforts in the trust have produced an income stream that takes up the slack, they would look to the state to fund it. They intend to come back to the legislature after the first year, provide a status report, advise how much money will be needed for the following year, and make application to borrow that money in a manner similar to that laid down in the original proposal. The \$45 million is their best worst guess of how much money they would need: \$15 million equity investment and a drawdown facility of up to \$30 million. Senator Josephson referred to page 1, lines 10-11, and said the source is not referenced because it will be a judgment call as to what it will be.

Number 226

Senator Josephson asked about reimbursement to the state. Mr. Gambiner said the \$15 million would be invested in equity, the same way as any other participant (i.e., Alliance Bank or FDIC) will contribute property. That property will be valued at current market value and they will receive units or shares or partnership interest in the trust, which entitle them for distributions as these units are sold in the liquidations process. They are asking the state to provide liquidity in the form of cash and asking the beneficiary participants to put in their various properties. The state's money will be used to pay operating costs (management expenses) until such time as income is generated from marketing the assets. He explained the method by which the state would get reimbursed.

Number 275

Senator Sturgulewski commented that U.S. Senator Frank Murkowski informed her that they have requested the Federal Home Loan Bank Board in Seattle, Washington, to take an independent look at our situation and the report will be sent to his office on March 14, 1988.

Number 295

Frank Cox, Small Business Administration (SBA), came to the table. Senator Halford said the bill, SSSB 471, represents the re-write of the original bill with input from AIDEA and Mr. Cox. The bill establishes a program in AIDEA to guarantee business loans and to refinance debt. In response to a question from Senator Coghill, Senator Halford said the business assistance fund will be established with the existing funds in AIDEA.

Mr. Cox said that the legislature may be seeing a little paranoia on the part of AIDEA and they are being careful because they are afraid the banks will rip them off. He has been doing loans for 18 years and the SBA guarantees 90%.

Number 336

Senator Sturgulewski commented that it has been mentioned that this is a bank bailout approach and asked him to answer several questions pertaining the SBA loans. Mr. Cox said there would not be any advantage to a person, who qualifies for his program, to use AIDEA. SBA would guarantee 85%; and get an answer in five days whereas it takes the state 5-6 months to respond. Concerning SBA's delinquency rates, he stated the matter is difficult to address as FDIC has possession of approximately 35% of his portfolio. Before FDIC took some loans, the delinquency rate was 12% (60 plus days); his charge-off rate is 3.2% (loan losses on ten year continuum). AIDEA's 75-80% rule would not change.

Senator Halford said a question was raised about whether they should apply to new loans as well as refinanced. AIDEA was interested that they not apply to refinance. Mr. Cox favored the inclusion of the refinance, not to allow people to pull all the equity from the loans and run, but to help someone by restructuring their payments. Those are the loans, limited to 20 years, that help residents; new loans help those that stepped off the plane last year. SBA does refinance, but only to the benefit of the borrower and not to the bank. Many SBA loans are not real estate based; but working capital. It's much easier to collateralize real estate than working capital.

Number 407

Senator Jones asked whether the banks will take advantage of AIDEA. Mr. Cox responded that it is up to AIDEA to say "we're not interested in doing this deal." If they are credit-worthy, AIDEA should be helping them. Senator Halford explained why it is to the advantage of the bank to refinance good loans: they can take the AIDEA guarantee and sell the loan to someone else, which gives them the capital to operate and make loans.

In response to Senator Coghill's comment about the need to refinance soft assets (working capital, inventory), Mr. Cox said AIDEA could only make loans on hard assets in the past. Senator Halford outlined the method for which AIDEA expands its capital base.

Number 454

Senator Faiks made two points: (1) the bill expands the number of players that can go to outside markets to bring money into the state; and (2) recommended language inserted, if the committee agreed, to include consideration of what's been called soft assets. Would this expand AIDEA's statutory authority and create a major re-write of the bill. Senator Rodey said those actions would expand its authority. Mr. Cox added it could be addressed on a percentage level such as ability to withdraw 10% (or whatever) of equity to be used as working capital.

Senator Halford said the reason AIDEA doesn't allow loans on soft assets is they are dealing with the bond market; it doesn't make sense to go through the bonding process for a short-term working capital loan. Likewise, it doesn't make sense to go through the guarantee process for a loan that is based on short-term asset. He raised the question of what happens during foreclosure: AIDEA felt that during foreclosure, the principal should be paid first. The banks disagree with it and said, essentially, the attorneys' fees and cost of the foreclosure should be paid first, and then the principal. Mr. Cox said SBA gives the bank 90 days, and if they choose, SBA will buy it. At that point, SBA gives the bank the choice to liquidate; if not, SBA will do it. If the bank liquidates, SBA takes some responsibility for controlling the attorneys' fees and other cost. They have not had trouble in telling the bank that SBA will allow \$10,000 in attorneys' fees and that's it. SBA's regulations address the process.

Number 494

Senator Josephson said the 90% figure has been criticized on the basis of it being a bank bailout and the state would be better to reduce the percentage. Mr. Cox said it depends on who is running the program and what type of credit judgments are being made. SBA is dropping its percentage from 90% to 85%.

Senator Coghill asked what percentage of SBA loans are for inventory and accounts receivables. Mr. Cox answered about 30% of loans are specifically for operating capital.

Senator Faiks asked, if possible, could Mr. Cox address the differences in their working relationship with banks than that of AIDEA. Mr. Cox said they assume the banks will act legally with them and normally everything is handled in the documentation.

Number 540

Senator Rodey addressed the inclusion of soft assets for purposes of AIDEA loans. He stated AIDEA was set up as a secondary market, not to deal directly with anyone, due to

the state's delinquency rate (about 40%). When you move into the area of relatively unsecured loans, it has to be carefully considered, as AIDEA was not set up for that purpose. Responding to a question from Senator Coghill, Senator Rodey said the AIDEA bond program does have a restriction on soft asset loans. Mr. Cox added there is equity there that can be recaptured for working capital.

Senator Sturgulewski asked if the SBA had a debt ceiling. Mr. Cox said there was a national limit, maybe \$6.5 billion, that has only been reached twice. She asked if there was any flexibility for SBA to service the market rather than our creation of a loan program. Mr. Cox said the SBA is responding; part of the problem is that AIDEA has much of the collateral, which leaves little collateral for anyone to base a loan. Senator Rodey added that bond covenants are involved.

Number 580

In responding to a inquiry from Senator Sturgulewski about appropriating funds for capital reserves, Mr. Cox stated AIDEA has about \$300 million, with profits of almost \$20 million last year and \$30 million the year before, maybe they should use that.

In discussing SBA's strict guidelines, Mr. Cox said their decline rate is about 5-6 times as high; it used to be less than 1%, and they have had months where they have declined up to 30%.

Senator Sturgulewski said they've heard charges the state program has been subject to political pressure and asked if that was a problem in SBA. Mr. Cox stated it is only a problem if the person that is running the program responds to it.

Number 600

Senator Josephson said, in a situation where the originating bank fails, does it create special problems. Mr. Cox answered that it does if FDIC takes the loans. They have several hundred loans now in the hands of FDIC and they know they are current; but the FDIC, as trustee for the debtor, has them in an account. Because they are in the secondary market, SBA will end up repurchasing the loans. In particular, if you send a payment on a loan, the FDIC puts it into a holding account and doesn't remit the payment to the purchaser in the secondary market. The secondary market wants to get payment on the guarantee. The FDIC doesn't care if they fail; they want money.

Senator Halford recommended the committee support the bill as part of its legislative package.

Tape One, Side Two
Number 652

The committee generally discussed the shifting of responsibilities from banks to AIDEA. Senator Rodey commented that banks are only servicing agencies; they get a fee from AIDEA. The bill does not shift the burden; it remains on AIDEA.

Senator Halford said the banks would probably like to shift the burden to AIDEA, if they could. The major benefit is drawing capital into the state. The bank may sell some of its good loans which they would not have been able to sell without the guarantee; then take the money from the sale and make more good loans. The banks are trying to bail out their bad loans with their good loans and good business. If we can expand their capacity on the positive side, we can help them carry their negative side.

The committee discussed Senator Coghill's concerns about inclusion of soft assets in the bill. Senator Faiks recommended that the bill be considered part of the package as is, since she has another bill which allows AIDEA to take up to 25% equity in refinancing loans. That bill would be a better vehicle for this issue.

Senator Rodey moved and asked unanimous consent that the bill be considered as part of the package. Hearing no objections, it was so ordered.

Number 820

At the request of Senator Zharoff, the committee heard from Nancy Gross, City Manager; Gary Daily, Port Director; and Dennis Robinson, City Council Member and Ounalashka Corporation Board member, of Unalaska, Alaska, concerning a fisheries proposal.

Mr. Daily explained home porting for the American factory troller, the Alaskanization of this industry and what it means to the state and residents. Currently, there are 41 Alaska factory trollers, mostly from Seattle. A factory troller is a vessel approximately 200-300 plus feet in length, the retrofits and costs range from \$17-35 million. To show the significance of the value in terms of jobs and income, the Port of Seattle recently appropriated \$200 million to upgrade its maritime moorage facilities to ensure they retain the factory trollers there. The 41 factory trollers give 240 persons/per troller with jobs which equates to just over 9,800 jobs. In 3-4 years, they are going to double the amount of trollers, resulting in excess of 22,400 jobs.

He continued to provide a history of the bottomfish industry in the state, and explained the chart detailing the fisheries' resources. U.S. Customs and Immigration are located in Dutch Harbor. He then noted the values of state and international fisheries, specifically 1.2 million metric tons of bottomfish, per exvessel value, exceeds \$2 billion; and the impact the industry has on jobs and support services. He felt the key to unlocking the Seattle monopoly was to provide a shore-based facility; they have \$60 million worth of business in a 10,000 foot area in Dutch Harbor which involves relations with 14 nations.

Number 988

Senator Sturgulewski asked about the monetary request. Ms. Gross pointed out that fisheries of the Bering Sea, particularly the bottomfish, per every 5% of revenue from the industry, can attract \$100 million into the state.

Senator Faiks asked how that money arrives in the state. Mr. Daily responded it includes shops, cold storage, processing, cargo, trans-shipment, jobs, fueling, etc. Cold storage in Japan is eight times as expensive than Alaska, and there are three requests for construction for facilities in Unalaska. He said fishing crews are hired out of Anchorage.

Senator Faiks commented if the state could capture 5% of the market, there would be a spin-off of \$100 million in both capital and salary investments, but it would not be every year.

Number 072

Senator Josephson referred to the proposal and commented it did not include the specifics for project description #2, and asked what is necessary to make Anchorage the service center they discussed. Ms. Gross answered that that section of the proposal represents the research Anchorage needs to do to get marketing plans.

Senator Halford asked the total budget of Unalaska and how much is spent on debt service. Ms. Gross said the total general fund budget is about \$4.0-4.5 million annually; they are maximized out on bonds which is one of their problems. They have been carrying, on the books, a population of 1,922 for several years, and this year, C&RA decided their population was 1,331. The Bond Bank will not talk to her; and she looked at an assessment district and was told that 35% of the land is not assessable because it is undeveloped land granted to the village corporation under the ANCSA.

In response to a question from Senator Halford about using revenue bonds for the dock, Ms. Gross responded the problem is the users have said when the city gets the facility, they will sign long-term leases for use; however, the city can't get the revenue bonds until they have the agreements.

Number 123

Senator Jones referred to the renewable resource aspect of fishing and asked how a sustained yield could be guaranteed. Ms. Gross said federal enforcement was necessary, such as the Coast Guard patrolling the area. However, the biological aspects of the waters make it so nutrient rich along the coast and shelf that the Japanese, who have fished the area for 20 years, have not impacted the yield.

Senator Sturgulewski compared the ports of Southeast (120-122 tourship stops/year) and this port which gets over five times that amount. She said the committee would not be able to take any action on the request.

Ms. Gross said there was a House Bill that addresses the request. In response to a question from Senator Halford, Ms. Gross commented their annual budget does not include the school budget; simply operating the electric, water, sewer, utility, port, airport and terminal, etc. that are general operations.

Number 163

The committee decided the next meeting would be a work session on bills and proposals already presented for discussion. There being no further business to come before the committee, Senator Sturgulewski adjourned the meeting at 6:31 p.m.

5-1863B

Cook

3/16/88

MAR 16 1988

Revised

Original sponsors: Kelly and Sturgulewski

1 IN THE SENATE

2 CS FOR SENATE BILL NO. 408 ()

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FIFTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act relating to the Alaska stabilization assis-
7 tance program; and providing for an effective date."

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

9 * Section 1. ALASKA STABILIZATION ASSISTANCE PROGRAM. (a) The purpose
10 of the Alaska stabilization assistance program is to promote the stabi-
11 lization of real property values in the state.

12 (b) The Alaska stabilization assistance fund is established in the
13 Alaska Industrial Development and Export Authority. The authority may use
14 money appropriated to the fund to make loans or investments to carry out
15 the purposes of this section. An appropriation to the Alaska stabilization
16 assistance fund lapses to the fund from which it was appropriated July 1,
17 1998, unless specified otherwise in the appropriation act. Other receipts
18 shall be separately accounted for and deposited into the general fund.
19 Each year the authority shall notify the legislature of the amount of these
20 receipts and the legislature may appropriate that amount into the _____.

21 (c) To encourage institutional lenders, state or federal agencies,
22 and other institutions not to attempt to dispose of real property in the
23 state until the real estate market becomes more stable, the authority may

24 (1) enter into contracts to provide for the management of real
25 property in the state that has been or could be foreclosed upon or other-
26 wise acquired through actions taken on defaulted loans;

27 (2) acquire interests in

28 (A) part-performing or nonperforming loans secured by real
29 property in the state; or

1 (B) loans acquired by an institution or federal or state
2 agency as a result of a bank failure in the state.

3 (d) Contracts entered into by the authority under (c) of this section
4 may provide for the management of property only through June 30, 1998.

5 * Sec. 2. This Act is repealed July 1, 1998.

6 * Sec. 3. This Act takes effect immediately under AS 01.10.070(c).
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29

STATE PROPERTY EXEMPTIONS IN BANKRUPTCY

	<u>1962</u>	<u>1971</u>	<u>1972</u>	<u>1974</u>	<u>1976</u>	<u>1982</u>	<u>1986</u>	<u>FEDERAL EXEMPTION</u>
<u>LIMITED VALUE EXEMPTION</u>								
Books Pictures Musical Instruments	300					1,500 ²	1,650 ²	4,000 ⁸
Wearing Apparel *								4,000 ⁸
Watches & Jewelry	200					500	550	500
Articles for Trade/Profession	1,800	2,500				1,400	1,540	750
Household Goods Furniture	1,200					1,500 ²	1,650 ²	4,000 ⁸
Pets						500	550	4,000 ⁸
Automobile	(Exempt under Trade/Profession)					1,500 ³	1,650 ⁶	1,200
Heirlooms						1,500 ²	1,650 ²	
Earnings (within 30 days)	350 (Head of Household) 200 (Single Man)							
Weekly Net Earnings Cash & Other Liquid Assets				25%/114 ¹		175 700	193 770	25%/ ¹⁰
Weekly Disposable Income Increased Cash & Liquid Assets						275 1,100	303 1,210	Not Specified
<u>HOMESTEAD EXEMPTION</u>								
Debtor's Dwelling (Realty)	8,000		12,000		19,000	27,000 ⁴	29,700	7,500
Debtor's Dwelling (Mobile Home)			8,000		12,000			
<u>PROPERTY EXEMPTION W/O LIMITATION</u>								
Unmatured Life Insurance & Annuity Contracts						5,000 ⁵	5,500 ⁷	4,000 ⁹

TONY
SMITH

MEMORANDUM

Sen. Sturgulewski
State of Alaska

TO: See Distribution

DATE: March 7, 1988

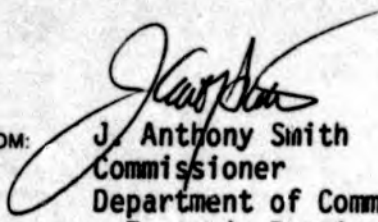
FILE NO:

TELEPHONE NO:

THRU:

SUBJECT: Comments on Various
Economic Recovery
Proposals

FROM:


J. Anthony Smith
Commissioner
Department of Commerce and
Economic Development

Due to the number of issues being discussed relative to legislative suggestions for possible actions to address our economic troubles, we are providing the following comments on a number of various issues/bills.

1. SB 392 & HB 402 -- AIDEA -- These bills address the issue of bank participation with AIDEA and the current statutory withholding of such participation because of the "2% rule." The Governor's bill, HB 402, also addresses a number of other issues which the Board of AIDEA has identified as limitations on AIDEA's ability to be responsive to the current economic conditions. The Department of Commerce and Economic Development supports both of these bills, and strongly supports passage of the entire package of proposals contained in HB 402.
2. SB 471 -- AIDEA Loan Guarantees and Refinancing -- Both of these issues have been the subject of considerable discussion among the board members of AIDEA. There is not at this time a consensus of opinion on the board on the relative merits or structure of either proposal. All members of the board are most concerned about preserving AIDEA's current bonding ability and ratings. Hence, close scrutiny must be utilized when incorporating any new financial service into AIDEA's powers.

The Department of Commerce and Economic Development is conceptually supportive of both proposals. With respect to the guarantee program, we believe it is most appropriate to fund the reserve for such a program by new appropriation to AIDEA. For consideration, we suggest that a portion of the current unappropriated portfolio of DCED's Division of Investments be appropriated to fund a reserve for the insurance program. The funded reserve will be the only asset offered to insure against losses, e.g., neither AIDEA nor the state

pledge any additional assets or responsibility. There will be losses in the program irrespective of the quality of the underwriting standards, but these losses will appear at least a year or two in the future. We also recommend that there be a 1-to-4 ratio of reserves to program commitment at the start with the Board of AIDEA having the flexibility to adjust reserves to reflect actual experience. This means that there needs to be an appropriation of loans which will generate \$25 million if we are to do \$100 million in guarantees for the program to have the impact desired. We recommend a \$100 million program at the start.

3. HB 422 -- Payment for Purchases by Various Public Entities -- DCED supports this expansion of current law.
4. HB 429 -- Optional Exemption from Property Taxes on Vacated Land -- The Department is supportive of this concept and would suggest elimination of the limitation of its applications by removing the 30-year-old requirement on improvements currently included in the bill. So long as this proposal does not directly affect the revenues of the state, and is optimal for local governments, it should be considered.
5. HB 430 - 431 -- Neighborhood Business Development Programs and Appropriation -- The Department is conceptually supportive of these bills. We understand the difficulties associated with balancing the state's budget and do not represent that this is an essential \$3 million item. Hence, a threshold question is identifying a source of funding.

In addition to HB 429, 430, and 431, it is our perception that an appropriate public sector response to the supply/demand problem is public acquisition of developments for purposes of parks, neighborhood upgrade and to eliminate obsolete or nonconforming properties. Thus, special appropriations to entities such as the Heritage Land Bank and local governments would allow local governments and the state to take advantage of present price levels to improve the quality of life while beneficially impacting the supply/demand problem.

6. HB 432 -- AHFC Trades -- We are conceptually supportive of this bill; although by this time the Labor and Commerce Committee is fully cognizant of the limitations on AHFC's ability to unilaterally achieve the ends sought in this bill. The approach currently undertaken by the Labor and Commerce Committee seems to reasonably address this issue.

There are other changes in AHFC which would allow the agency to manage its revenues to be part of the solution rather than part of the problem. For example, AS 18.56.098 needs to be altered so that the interest rate formula is more flexible. Some recommended changes are:

Financial Provisions Changes - Currently, many AHFC financial provisions are "hard-wired." For instance, the interest rate formula as specified in AS 18.56.098 permits no flexibility in interest rate calculation, even though at times adding some flexibility could significantly help the market at little or no additional cost to AHFC.

One way to add some flexibility would be to develop a mechanism whereby the maximum amount of assistance that AHFC can provide for any individual loan is set, but the specific way in which it was applied would be flexible. Another possible change would be to permit more flexibility in the amount of assistance if the whole market was in bad shape. For instance, if the delinquency rate in a particular market exceeded, say, 10%. Additional assistance would have to be targeted at certain groups to achieve specified outcomes, or very quickly AHFC could use up its available resources.

For instance, assume AHFC wanted to target the condo market, either for trade ups to mid-high range condos, or to encourage the purchase of some of the many low end condos. Many of the current condo loans were based on a loan amount of \$75-80,000, with an interest rate of 10-12%. Consider the following figures:

<u>Loan Amount</u>	<u>Interest Rate</u>	<u>Payment</u>
\$ 80,000	10%	\$702
125,000	6%	749
50,000	6%	300

In one case, a borrower can buy much more "house" for approximately the same payment, whereas in the other case, a borrower could buy a \$50,000 condo (which was likely originally an \$80,000 condo) for a payment of less than half of the original. Properly targeted this could help stabilize price and reduce the inventory of foreclosed properties. It is our belief that the "equity underwater" problem could be stabilized in targeted projects by offering financing opportunities for full prices sales.

Other changes would deal with AHFC's role in disposing of its real estate portfolio. For instance, if current plans are successful, AHFC could well own entire condo projects. These projects could eventually be sold as condos, but they might also be sold as apartment buildings. If AHFC were able to manage the building (via a contract) and perhaps provide financing to the ultimate buyer, the total loss might be much less. Possibly other types of nonowner-occupied financings to help in disposal of foreclosed properties should be added.

More flexibility would be most helpful in workout situations. HOAP will be sufficient for a great number of troubled borrowers, others will need far more assistance. AHFC, in conjunction with the applicable insurance companies, should be able to provide assistance to these borrowers in a variety of ways -- much lower interest rate, deferral of principal payments, etc. To hold down the ultimate cost of the program and to provide more assistance than is needed, AHFC should be able to design various approaches to recapturing some of this assistance if the property ever appreciates in value beyond its original loan amount.

We have discussed with various individuals the thought of establishing a subsidiary corporation of AHFC which would be granted broader powers to address critical issues in Alaska's current housing market. Such a subsidiary may be charged with acquisitions and/or eminent domain powers to achieve public purposes. Further, it could facilitate the consolidation of condominium owners to allow for the conversion of other condominium projects to other uses, including apartment complexes and public sector housing. We believe all such ideas should be explored in detail and are appropriate items to try to adopt this legislative session.

Lastly, AHFC should be given broader investment powers so that it could participate in acquisitions such as Hollywood Vista and Willow Park when it makes economic sense for the agency.

7. HB 433 -- Moratoriums on Judicial and Nonjudicial Foreclosures -- This is intended as a parochial attempt to preserve for Alaskans a greater opportunity to preserve their residence at the expense of lenders, a good portion of whom are nonresident. Similiar legislation was adopted in two mid-western states as responses to the farm crisis. Their experience should be studied in detail before passage of this legislation.

While the approach has appeal on its surface, it appears to also generate considerable technical questions, especially with respect to bonded indebtedness of various Alaska debt issuers. Further, as probably the largest financier of Alaska real estate, various state entities, including the retirement funds, may be injured by this approach. We are also concerned about the potential ramifications if "outside" lenders respond to passage of this legislation by further restricting access of Alaskans to secondary money markets.

We are also confused by the language which suggests that a non-judicial foreclosure entitles the mortgagor to a right of redemption. This appears to be antithetical to the main purpose of nonjudicial foreclosures.

March 7, 1988

8. SCR xx -- Loan Approval Withheld for New Construction -- The Department has been asked to comment on a draft of this resolution. We do not agree with this approach. We do agree that financing agencies must be sensitive to the oversupply of several categories of real estate and should coordinate their financing policies to assure that they do not inadvertently exacerbate a serious problem. We also believe that the inventory of some classes of property may require additional construction to meet a growing demand in the near term. It would be much more appropriate, from our perspective, to allow market forces and coordinated state policy development, such as through the Alaska Housing Marketing Council, to address the concerns expressed in this draft resolution. For example, there are market segments which would be severely paralyzed by a generalized moratorium. It is more appropriate to add private sector representatives to the Housing Market Council.

We feel any response of this nature should be in the manner in which municipalities issue building permits and carry out inspections. As Chairman of AHFC, it seems indisputable that many of AHFC's problem projects were not inspected.

Other

Bridge Bank and Hallwood Trust - we conceptually support these, as well as other initiatives to have assets held by the FDIC or banks managed to minimize the adverse impact on the economy. There needs to be consideration given to both the management difficulties and the carrying costs which will be incurred. In addition, we need to recognize that any state guarantee or stand-by letter of credit could most likely be used.

There are three possible options at this time. Any one, or a combination of these, may work. They are the Anchorage Economic Development Corp., the Sealaska REIT group, and the Hallwood Trust. Should the state choose to participate in one of these structures, it should be prepared to contribute cash as well as properties. Cash flows to fund such an entity will not likely, in the short run, be sufficient to meet expenses. Hence, initial capitalization will be important to help assure success -- understanding that success includes the avoidance of increases of property liquidations.

Distribution

Garrey Peska, Chief of Staff, Office of the Governor
Bob Evans, Legislative Liaison, Office of the Governor
The Honorable Jan Faiks
The Honorable Max Gruenberg
The Honorable David Donley
Gregg Erickson, Office of Management & Budget,

JAS/sh5144M
3488c

MAR 16 1988

5-1864B
Cook
3/16/88

Original sponsors: Kelly and Sturgulewski

*BA*Funding Information

General Fund \$

Other Funds \$

1 IN THE SENATE

2 CS FOR SENATE BILL NO. 409 ()

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FIFTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act making a special appropriation to the Alaska
7 stabilization assistance fund; and providing for an
8 effective date."

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

10 * Section 1. The sum of \$15,000,000 is appropriated from the _____
11 _____ to the Alaska stabilization assistance fund.

12 * Sec. 2. The appropriation made by sec. 1 of this Act lapses into the
13 _____ on July 1, 1998.

14 * Sec. 3. This Act takes effect on the effective date of a version of
15 an Act enacted by the Fifteenth Alaska State Legislature establishing the
16 Alaska stabilization assistance fund.

17

18

19

20

21

22

23

24

25

MISCELLANEOUS INFORMATION

FILE 2

MASTER

Alaska State Legislature

SENATOR
ARLISS STURGULEWSKI

Chairman, Senate Community and Regional Affairs Committee
Vice-Chairman, Senate Judiciary Committee
Member, Senate Resources Committee



2957 SHELDON JACKSON STREET
ANCHORAGE, ALASKA 99508

While in Juneau
P. O. BOX V
JUNEAU, ALASKA 99811
(907) 465-1818

Senate

MEMORANDUM

March 21, 1988

* Revisen MARCH 28, 1988

TO: All Members
Senate Joint Committee on Economic Recovery

FROM: Senator Arliss Sturgulewski *AS*

RE: Existing and proposed legislation

I have reviewed the existing and proposed legislation before the Senate Committee on Economic Recovery and would suggest that we concentrate on those specific pieces outlined in this memo.

I have used the following guidelines in the selection of this legislation.

1. The December 1, 1987 Briefing Paper by the Institute of Social and Economic Research (ISER) suggests several important considerations.

A. That state spending is part of the current economic problem because of high state budgets in the early 1980's. They stated, "Unless it [state spending] can be sustained [it] will have a destabilizing impact on the economy." We know now that we cannot sustain those high budgets with our present income.

B. That "the recession is progressively dissipating and is likely to end over the course of the coming year." If this view is correct, the state must be cautious in its response to the economic recovery to avoid disrupting the natural market forces and simply prolonging the adjustment period.

C. That "an increase in state spending will not hasten an enduring economic recovery unless the increased spending can be sustained or the state's basic industries increase their economic output to match a future decline in state spending." The state has a limited ability to sustain increased spending, however, all basic industry (oil, fish, timber, and mining) in the state show healthy signs of increased growth in the near future and will aide the economic recovery. This, of course, is the typical economic stimulus in most economies not government spending.

2. State financial programs such as AHFC, AIDEA and the various state loan programs have significant impact on the financial health of the economy because of the large dollar contribution that they represent. They should exercise maximum flexibility in their response to distressed borrowers without the state simply providing more funding which it has only a limited ability to do.

3. Because of the limited funding available from the state, it should encourage private sector financial institutions to respond to the economic recovery. This can be accomplished in two ways, one would be to assist private financial institutions in the refinancing of troubled loans; and two, to encourage new loans in businesses that will aide the economic recovery through job creation and economic growth in the state.

4. The distribution of cash into the economy has an immediate effect on the economy. The jobs bill that was recently passed will soon be having a positive impact throughout the state. Another source of cash is the permanent fund dividend distribution.

I would recommend that we endorse the following specific legislation and concepts for appropriate standing committee review:

A. The concept of a "Bridge Bank" is contained in SB 408. This legislation offers a potential for relieving the pressure of property management for private financial institutions and some state agencies. However, it should be structured to encourage private sector management, limited state contributions and provisions for eventual repayment of the contributions, to the state.

* STATUS: ENDORSED BY COMMITTEE 3/22/88

B. SB 471, which the committee endorsed previously, has several elements that I feel are beneficial to the economic recovery process. It will need further refinement in the Senate Finance Committee and I would recommend that they review setting a cap or maximum limit to the total amount of loan funds that can be guaranteed by AIDEA. This will prevent uncontrollable liability at some future date. I would also recommend that AIDEA develop guidelines for allowing private financial institutions to offer refinanced debt packages as well as guidelines for new business loans that will stimulate economic growth. Finally, in order to evaluate its progress, I would suggest a sunset date on the AIDEA loan guarantee program.

* STATUS: ENDORSED BY COMMITTEE 3/22/88

C. SJR , Urging a change under the IRS Code. This resolution petitions the IRS to review its policy of taxing forgiven negative equity in cases of foreclosure.

* D. HJR 72 , Relating to residential real estate. This resolution specifically petitions state loan programs and lending agencies to use the maximum flexibility at their disposal in order to keep their portfolios as active as possible.

* SUBCOMMITTEE RECOMMENDATION: (NOT FORMALLY INTRODUCED)

E. ~~HJR~~ , Willow Park Demolition. Calls for the demolition of the substandard Willow Parking Housing Project with funding for the demolition spelled out in an agreement between the state and municipality. It further

calls upon the federal government to fund and carry out the relocation of the involved dislocated families. This project, in addition to being substandard, poses serious health concerns because of asbestos insulation.

F. HB 432, Authorizing the AHFC to accept trades in certain cases. This legislation would allow individuals to trade into mortgages of greater/lesser obligation with AHFC. This would allow borrowers with greater resources to purchase homes with larger mortgages making those loan packages active and those borrowing on the margin to trade into more affordable housing, once again reactivating those loans. The Labor and Commerce amended version includes a provision for reducing negative equity that should be reviewed in the committee hearing process.

* G. HB 550, "Authorizing the Department of Community and Regional Affairs to modify the terms of its mortgage loans; and providing for an effective date." Allows the Housing Assistance Section to modify home loans in certain cases.

* H. HB 549, Notice requirements on a Deed of Trust." Requires lender to inform the borrower in the note securing the loan of all methods of recourse in the event of default.

I. Investigate early dividend and/or increased dividend. Request the Alaska Permanent Fund managers to present the opportunity to provide an early dividend or a substantially higher dividend than currently projected for the year 1988.

1 IN THE SENATE

BY KELLY AND STURGULEWSKI

2

SENATE BILL NO. 408

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

4

FIFTEENTH LEGISLATURE - SECOND SESSION

5

A BILL

6 For an Act entitled: "An Act relating to the Alaska stabilization assis-
7 tance program; and providing for an effective date."

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

9 * Section 1. ALASKA STABILIZATION ASSISTANCE PROGRAM. (a) The purpose
10 of the Alaska stabilization assistance program is to promote the stabi-
11 lization of real property values in the state.

12 (b) The Alaska stabilization assistance fund is established in the
13 Alaska Industrial Development and Export Authority. The authority may use
14 money appropriated to the fund to carry out the purposes of this section.
15 An appropriation to the Alaska stabilization assistance fund lapses to the
16 fund from which it was appropriated July 1, 1992, unless specified other-
17 wise in the appropriation act. Other receipts shall be separately
18 accounted for and deposited into the general fund. Each year the authority
19 shall notify the legislature of the amount of these receipts and the legis-
20 lature may appropriate that amount into the Railbelt energy fund
21 established under AS 37.05.153.

22 (c) To encourage lenders not to attempt to dispose of real property
23 in the state that has been foreclosed upon or otherwise acquired through
24 actions taken on defaulted loans until the real estate market in the state
25 becomes more stable, the authority may enter into contracts to provide for
26 the management of the property. However, the authority may provide for the
27 management of property only through June 30, 1992.

28 * Sec. 2. This Act is repealed July 1, 1992.

29 * Sec. 3. This Act takes effect immediately under AS 01.10.070(c).

Funding Information
General Fund \$15,000,000
Other Funds -0-
\$15,000,000

1 IN THE SENATE

BY KELLY AND STURGULEWSKI

2

SENATE BILL NO. 409

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

4

FIFTEENTH LEGISLATURE - SECOND SESSION

5

A BILL

6 For an Act entitled: "An Act making a special appropriation to the Alaska
7 stabilization assistance fund; and providing for an
8 effective date."

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

10 * Section 1. The sum of \$15,000,000 is appropriated from the Railbelt
11 energy fund (AS 37.05.153) to the Alaska stabilization assistance fund.

12 * Sec. 2. The appropriation made by sec. 1 of this Act lapses into the
13 Railbelt energy fund (AS 37.05.153) on July 1, 1992.

14 * Sec. 3. This Act takes effect on the effective date of a version of
15 an Act enacted by the Fifteenth Alaska State Legislature establishing the
16 Alaska stabilization assistance fund.

IN THE SENATE

BY HALFORD, FAIKS, UEHLING,
JOSEPHSON, STURGULEWSKI AND
ABOOD

SENATE BILL NO. 471

IN THE LEGISLATURE OF THE STATE OF ALASKA

FIFTEENTH LEGISLATURE - SECOND SESSION

A BILL

For an Act entitled: "An Act establishing a program in the
Alaska Industrial Development and Export
Authority to guarantee business loans and
to refinance debt; and providing for an
effective date."

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

* Section 1. AS 44.88 is amended by adding new sections
to read:

ARTICLE 6A. BUSINESS ASSISTANCE PROGRAM.

* Sec. 44.88.500. BUSINESS ASSISTANCE FUND. The business
assistance fund is established in the authority from
appropriations for the purpose. Subject to the requirements of
AS 44.88.500 - 44.88.599, the authority may use money in the
fund to guarantee loans, including loans made to refinance
existing loans, to business that qualify under AS 44.88.510 and
apply under AS 44.88.520.

* Sec. 44.88.510. APPLICANT QUALIFICATIONS. A business
enterprise may apply for a loan guarantee under AS 44.88.500 -

44.88.599. The authority may establish additional applicant qualifications by regulation and these qualifications may vary depending upon the type of business the applicant is engaged in.

* Sec. 44.88.520. APPLICATION. An applicant for a loan guarantee shall provide information required by regulation of the authority, which may include an economic benefit analysis prepared by a person acceptable to the authority together with other information.

* Sec. 44.88.530. POWERS RELATING TO LOAN GUARANTEES.
The authority may

(1) designate agents and delegate powers necessary to implement AS 44.88.500 - 44.88.599;

(2) adopt regulations to implement AS 44.88.500 - 44.88.599;

(3) establish terms and conditions for loan guarantees subject to the requirements of AS 44.88.500 - 44.88.599;

(4) make and execute contracts and other instruments to implement AS 44.88.500 - 44.88.599;

(5) acquire real or personal property by purchase, transfer, or foreclosure when the acquisition is necessary to protect an interest in the fund; and

(6) exercise any other power necessary to implement AS 44.88.500 - 44.88.599.

* Sec. 44.88.540. CONDITIONS OF LOAN GUARANTEES. (a) The authority may guarantee a loan under AS 44.88.500 - 44.88.599 if the

(1) loan is commercially reasonable, contains amortization provisions satisfactory to the authority, and is secured by adequate collateral, and if the net cash flow from the borrower provides adequate coverage for the debt service on the loan;

(2) term of the loan does not exceed 20 years;

(3) loan is originated with and serviced by a state chartered or federally chartered financial institution;

(4) portion of the loan not guaranteed by the authority is held by the originating financial institution or another financial institution approved by the authority; and

(5) loan is made to a business with a majority interest held by state residents.

(b) The authority may provide a guarantee from the fund for up to 90 percent of a loan that qualifies under AS 44.88.500 - 44.88.599. The ratio of the guarantee to the outstanding principal of the loan shall not increase over the term of the loan.

(c) The authority may not guarantee

(1) the payment of interest on the guaranteed portion of a loan; or

(2) more than \$1,000,000 per loan.

* Sec. 44.88.550. INTEREST. The maximum interest rate on a loan guaranteed by the authority is

(1) for a guarantee of 80 percent or more of the loan, one and one-half percentage points above the prime rate, as determined by the authority, on the day the loan guarantee is made; and

(2) for a guarantee of less than 80 percent of the loan, two and three-quarters percentage points above the prime rate, as determined by the authority, on the day the loan guarantee is made.

* Sec. 44.88.560. DEFAULT OR FORECLOSURE. (a) Amounts received toward satisfaction of a default on a loan guaranteed under AS 44.88.500 - 44.88.599 shall only be applied to pay principal of the loan until the entire principal balance of the loan has been repaid.

(b) The authority shall dispose of property acquired through default or foreclosure of a loan guaranteed under AS 44.88.500 - 44.88.599. Disposal shall be in a manner that serves the best interest of the state and may include the amortization of payments over a period of years.

* Sec. 44.88.570. SPECIAL ACCOUNT ESTABLISHED. (a) There is established as a special account within the fund the foreclosure expense account.

(b) The authority may expend money credited to the foreclosure expense account when necessary to protect the state's security interest in collateral on loans guaranteed or refinanced under AS 44.88.500 - 44.88.599 or to defray expenses incurred during a foreclosure proceeding after a default.

* Sec. 44.88.580. PREREQUISITE FOR OTHER LOANS.

Notwithstanding other provisions of law, a business enterprise that qualifies under AS 44.88.510 to apply for a loan guarantee under AS 44.88.500 - AS 44.88.599 shall apply for a loan guarantee before it may apply for a direct loan of state money under any other state loan program. Only after an application for the guarantee of a loan to be used for a particular purpose is rejected under AS 44.88.500 - 44.88.599 may a business enterprise apply for a direct state loan for that purpose.

* Sec. 44.88.599. DEFINITIONS. In AS 44.88.500 - AS 44.88.599.

(1) "fund" means the business assistance fund established under AS 44.88.500;

(2) "prime rate" means the lowest money center prime rate of interest that is published in the Wall Street Journal.

* Sec. 2. This Act takes effect immediately under AS
01.10.070(c).

1 IN THE SENATE

2 SENATE JOINT RESOLUTION NO.

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FIFTEENTH LEGISLATURE - SECOND SESSION

5 Urging a change under the Internal
6 Revenue Code in the tax treatment of the
7 transfer of a residence subject to a
8 mortgage that is a recourse loan when
9 the indebtedness on the residence is
10 discharged through foreclosure, repos-
11 session, or surrender of the property.

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

13 WHEREAS, under current provisions of the Internal Revenue Code and
14 pertinent regulations defining "gross income," a voluntary foreclosure,
15 repossession of real property, or surrender of property that serves as
16 collateral for an indebtedness is treated as a disposition similar to the
17 sale or exchange of real property; and

18 WHEREAS, if real property is transferred through foreclosure or repos-
19 session to satisfy a debt secured by the property or the property is sur-
20 rendered, the property owner may realize a gain or loss; and

21 WHEREAS in a foreclosure, repossession, or surrender, the difference
22 between the mortgage debt discharged and the fair market value of the
23 property given up is called "discharge of indebtedness" income; and

24 WHEREAS "discharge of indebtedness" income is taxable to the real
25 property owner as ordinary income if the loan discharged is a "recourse
26 loan," in which the owner is personally liable for repayment of the loan,
27 if the fair market value of the property foreclosed, repossessed, or
28 surrendered is less than the amount of the debt discharged, and if the
29 lending institution forgives payment of the balance of the underlying debt;

1 and

2 WHEREAS many Alaska homeowners have mortgages that are recourse loans
3 and

4 WHEREAS, having only a small equity in their residences and unable to
5 make current monthly mortgage payments in a declining economy, a number of
6 these homeowners have had their residences foreclosed on or repossessed;
7 and

8 WHEREAS, as an alternative to foreclosure or repossession, other
9 homeowners in similar circumstances have surrendered the mortgaged property
10 to the lending institution; and

11 WHEREAS, in a substantial number of the loans of these homeowners, the
12 fair market value of the property foreclosed on, repossessed, or surren-
13 dered is substantially less than the amount of the indebtedness discharged,
14 giving rise to a "discharge of indebtedness" income; and

15 WHEREAS, even after these homeowners lose their residences through
16 foreclosure, repossession, or surrender, the Internal Revenue Code and its
17 regulations may apply to impose substantial liability for taxation on the
18 homeowner's discharge of indebtedness income; and

19 WHEREAS the Alaska Legislature believes that the loss of a residence
20 through foreclosure, repossession, or surrender due to the homeowner's
21 financial problems in a time of economic uncertainty combined with incur-
22 rence of tax liability for that loss is inequitable and works a substantial
23 hardship on these families;

24 BE IT RESOLVED by the Alaska State Legislature that the Congress is
25 urged to amend the applicable Internal Revenue Code provisions to except
26 from treatment as income the liability of taxpayers incurring "discharge of
27 indebtedness" income tax liability under a recourse loan on foreclosed,
28 repossessed, or surrendered residential property in these circumstances.

29 COPIES of this resolution shall be sent to Lawrence B. Gibbs.

1 Commissioner of the Internal Revenue Service; and to the Honorable Te
2 Stevens and the Honorable Frank Murkowski, U.S. Senators, and the Honorable
3 Don Young, U.S. Representative, members of the Alaska delegation in
4 Congress.
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

BY THE RULES COMMITTEE BY
REQUEST OF THE HOUSE MEMBERS
OF THE JOINT COMMITTEE ON
ECONOMIC RECOVERY

1 IN THE HOUSE

2

HOUSE JOINT RESOLUTION NO. 72

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

4

FIFTEENTH LEGISLATURE - SECOND SESSION

5

Relating to the residential real estate

6

market.

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

8

WHEREAS some areas of the state are experiencing a severe economic
9 crisis as evidenced by bankruptcies, foreclosures, business failures, and
10 the loss of homes and property values; and

11 WHEREAS the state is experiencing a difficult economic period, espe-
12 cially in the residential real estate market, and many persons are finding
13 it difficult to meet their financial obligations during these times; and

14 WHEREAS keeping people in their homes and facilitating the purchase
15 and sale of homes serves an important public purpose and is financially
16 beneficial to both the borrower and the lender; and

17 WHEREAS borrowers are anxious to continue to meet their financial
18 obligations, but there is a significant number of individuals who are under
19 severe risk of being unable to do so; and

20 WHEREAS many borrowers would be able to meet their financial obliga-
21 tions if various forms of debt restructuring were made possible; and

22 WHEREAS debt restructuring requires the cooperation of the various
23 parties to each real estate loan, including the borrower, the loan origina-
24 tor, the Alaska Housing Finance Corporation or other loan packager, the
25 secondary purchasers of the loans, and the various loan insurers; and

26 WHEREAS the state's economy would be greatly helped if the financial
27 institutions of the state would adjust their lending and collection pol-
28 icies to the present needs and abilities of their customers by using more
29 flexible approaches to stabilize and improve the economy of the state; and

1 WHEREAS present financing packages available to residential real
2 estate borrowers do not provide adequate market liquidity or ability to
3 buy, sell, or trade properties in today's economic circumstances in which
4 debt balances on the properties are nearly equal to or greater than the
5 values of the property; and

6 WHEREAS, in order for residents of the state to meet their financial
7 obligations, the parties to residential loans in the state must be willing
8 to negotiate more creative financing terms and conditions for the benefit
9 of all concerned; and

10 WHEREAS to some extent state agencies and the financial institutions
11 in the state have not yet developed a coherent policy that addresses the
12 current economic crises; and

13 WHEREAS the likelihood of loss or default is lessened if a market is
14 made more liquid, something that will benefit all participants in real
15 estate loans; and

16 WHEREAS the ability to buy, sell, and trade properties in a market
17 that has very high loan-to-value ratios can only be accomplished through
18 innovation and cooperation of the various parties to a real estate loan;
19 and

20 WHEREAS the Alaska Housing Finance Corporation is presently working
21 with the legislature, lending institutions, federal governmental agencies,
22 and private mortgage insurers to find creative ways of refinancing existing
23 mortgages and managing recent acquisitions in the residential real estate
24 market;

25 BE IT RESOLVED by the Alaska State Legislature that the various finan-
26 cial participants in the Alaska real estate market, including the Alaska
27 Housing Finance Corporation, the Department of Commerce and Economic Devel-
28 opment, the Department of Community and Regional Affairs, the Department of
29 Revenue, the Alaska Permanent Fund Corporation, and the various loan

1 servicers, guarantors, and insurers are urged to cooperate in developing
2 innovative ways to restructure debt and to buy, sell, and trade properties
3 for their collective benefit; and be it

4 FURTHER RESOLVED that economic stabilization of the residential real
5 estate market be accomplished with the joint cooperation of the Alaska
6 Housing Finance Corporation, the Department of Commerce and Economic Devel-
7 opment, the Department of Community and Regional Affairs, the Department of
8 Revenue, and the Alaska Permanent Fund Corporation and other agencies of
9 the state and of lending institutions in the state as well as the Federal
10 Housing Administration, the U.S. Department of Housing and Urban Develop-
11 ment, the Veterans Administration, the Federal National Mortgage Asso-
12 ciation, the Government National Mortgage Association, the Federal Home
13 Loan Mortgage Corporation, and private mortgage insurers; and be it

14 FURTHER RESOLVED that the legislature fully supports efforts on the
15 part of the Alaska Housing Finance Corporation, the Department of Commerce
16 and Economic Development, the Department of Community and Regional Affairs,
17 the Department of Revenue, and the Alaska Permanent Fund Corporation to
18 hold foreclosed-upon residential properties off the market in instances
19 where such action makes long-term economic sense.

20 COPIES of this resolution shall be sent to the Honorable Steve Cowper,
21 Governor; the Honorable J. Anthony Smith, commissioner of commerce and
22 economic development; the Honorable David Hoffman, commissioner of com-
23 munity and regional affairs; the Honorable Hugh Malone, commissioner of
24 revenue; Ron Lehr, executive director, Alaska Housing Finance Corporation;
25 Dave Rose, executive director, Alaska Permanent Fund Corporation; the
26 Federal Housing Administration; the U.S. Department of Housing and Urban
27 Development; the Veterans Administration; the Federal National Mortgage
28 Administration; the Government National Mortgage Association; the Federal
29 Home Loan Mortgage Corporation; and to the Honorable Ted Stevens and the

- 1 Honorable Frank Murkowski, U.S. Senators, and the Honorable Don Young, U.S.
- 2 Representative, members of the Alaska delegation in Congress.



Official Business

Alaska State Legislature

House

P.O. BOX V
State Capitol
Juneau, Alaska 99801

BY THE JOINT COMMITTEE ON ECONOMIC RECOVERY

March 2, 1988

COMMITTEE RESOLUTION

Relating to the Residential Real Estate Market

WHEREAS the Alaska State Building Authority, (ASBA), has proposed a comprehensive plan to relocate the tenants, and then demolish Willow Park, a 150-unit, low-rent housing project; and

WHEREAS ASBA is seeking funding for this project from federal, state and local sources; and

WHEREAS the existing structures are 35 years old and in need of extensive renovation to remedy safety code violations, and renovation would cost more than the structures are worth; and

WHEREAS removing substandard units and replacing them with available public and privately owned housing units will help to stabilize the current housing market and help bring substantial new federal funds into a local Alaskan economy; and

WHEREAS relocation would provide an improved quality of life for the current residents of Willow Park; and

WHEREAS the complexes are functionally obsolete and a blight on the community; and

WHEREAS the Committee recognizes the value of the Willow Park demolition project and recognizes a responsibility for asbestos abatement of this state-owned facility; and

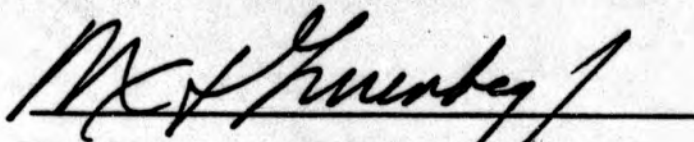
WHEREAS federal funding for relocation of the Willow Park tenants is directly related to garnering state or local funding of other costs, including asbestos abatement, demolition and site restoration.

BE IT RESOLVED that the Committee supports all efforts to obtain state, federal and local funds to complete this relocation and demolition project.

BE IT FURTHER RESOLVED that the Committee recommends that finding appropriate and sufficient state and local funding sources remain both a state legislative and municipal government priority, and that further analysis for consideration by the Legislature in upcoming appropriation actions be completed as soon as possible. The Committee further recommends that final

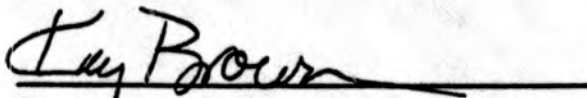
project costs exclusive of federal relocation assistance funds, once verified and funded, be spelled out in a memorandum of understanding between the state and local government by the Alaska State Building Authority subject to the conditions for appropriation the Legislature deems advisable.

Signed this 2nd day of March, 1988



Representative Max Gruenberg

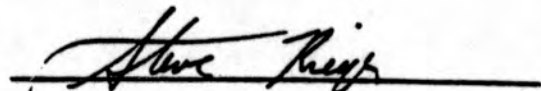
Chairman, House Joint Economic Recovery Committee



Representative Kay Brown

Co-Chairperson

Housing & Banking Subcommittee



Representative Steve Rieger

Co-Chairperson

Housing & Banking Subcommittee

Original sponsors: Donley, Ellis,
Boucher, et al.

BY THE LABOR AND
COMMERCE COMMITTEE

1 IN THE HOUSE

2

CS FOR HOUSE BILL NO. 432 (L&C)

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

4

FIFTEENTH LEGISLATURE - SECOND SESSION

5

A BILL

6 For an Act entitled: "An Act authorizing the Alaska Housing Finance Corpo-
7 ration to accept trades in certain cases; and provid-
8 ing for an effective date."

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

10 * Section 1. PURPOSE AND AUTHORIZATION. (a) The legislature finds
11 that a sizeable proportion of the residents of the state have mortgages
12 that exceed both the present value of the property and the present ability
13 of the mortgagors of the property to make the payments agreed to in the
14 past. The purpose of this Act is to direct the Alaska Housing Finance
15 Corporation to use creative solutions to the present crisis in the housing
16 market and, at the same time, to permit the corporation to seek the dis-
17 posal of surplus residences within the corporation's inventory.

18 (b) The Alaska Housing Finance Corporation may permit mortgagors who
19 are experiencing difficulty in meeting their mortgage payments to return
20 the residence and its mortgage to the Alaska Housing Finance Corporation
21 and to enter into a new mortgage for different residential property subject
22 to the control of the corporation at rates that are more within the ability
23 of the mortgagors.

24 (c) The Alaska Housing Finance Corporation may also permit a mortga-
25 gor who is willing to accept the responsibility for a larger mortgage to
26 offer an existing residence and its mortgage to the corporation and enter
27 into a new mortgage for different residential property subject to the
28 control of the corporation.

29 (d) The Alaska Housing Finance Corporation, the mortgage insurers,

1 and the mortgagor shall, in each case, work together to reduce the negative
2 equity that may be present in individual cases.

3 (e) Subject to appropriations, the Alaska Housing Finance Corporation
4 may use up to 1 percent of its total fund equity to achieve the purposes of
5 this section.

6 (f) In this section, "residence" includes mobile homes.

7 * Sec. 2. This Act is repealed July 1, 1991.

8 * Sec. 3. This Act takes effect immediately under AS 01.10.070(c).

STATE OF ALASKA
1988 LEGISLATIVE SESSION

BILL VERSION: CSHB 432(L&C)
PUBLISH DATE: HOUSE 3/4/88

FISCAL NOTE

REQUEST:

Revision Date: _____
Title: "An Act authorizing AhFC to
accept trades in certain cases."
Sponsor: Labor and Commerce
Requestor: House Labor & Commerce

Agency Affected: RevenueBkU: AhFC

Components: _____

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 86	FY 87	FY 88	FY 89	FY 90	FY 91	FY 92	FY 93
OPERATING								
PERSONAL SERVICES	-	-	-	-	-	-	-	-
TRAVEL	-	-	-	-	-	-	-	-
CONTRACTUAL	-	-	-	-	-	-	-	-
SUPPLIES	-	-	-	-	-	-	-	-
EQUIPMENT	-	-	-	-	-	-	-	-
LANDS & STRUCTURES	-	-	-	-	-	-	-	-
GRANTS, CLAIMS	-	-	-	-	-	-	-	-
MISCELLANEOUS	-	-	-	-	-	-	-	-
TOTAL OPERATING	-	-	-	-	-	-	-	-
CAPITAL	-	-	-	-	-	-	-	-
REVENUE	-	-	-	-	-	-	-	-

FUNDING: (Thousands of Dollars)

GENERAL FUND	-	-	-	-	-	-	-	-
FEDERAL FUNDS	-	-	-	-	-	-	-	-
OTHER	15,210	-	-	-	-	-	-	-
TOTAL	15,210	-	-	-	-	-	-	-

POSITIONS:

FULL-TIME	-	-	-	-	-	-	-	-
PART-TIME	-	-	-	-	-	-	-	-
TEMPORARY	-	-	-	-	-	-	-	-

ANALYSIS: (Attach a separate page if necessary)

It is unclear at this time what the total volume of the program would be under this bill. The maximum amount would be 1% of \$1.521 billion or \$15,210,000.

Prepared By: Ron Lehr, Executive Director
Division: Alaska Housing Finance Corporation

Phone: 276-5595Date: 03/03/88

Approved by Commissioner: Hugh Malone
Agency: Department of Revenue

Date: 03/03/88

Distribution (by preparer):

Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)

H.C+RA
L+C
FIN

5-2052X
Chenoweth

3/23/88
* 3/29/88

* By the Rules Committee at
the request of
BY THE JOINT COMMITTEE ON ECONOMIC
RECOVERY (For the Subcommittee on
Housing and Banking)

1 IN THE HOUSE

2 HOUSE BILL NO. 550

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FIFTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act authorizing the Department of Community and
7 Regional Affairs to modify the terms of its mortgage
8 loans; and providing for an effective date."

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

10 * Section 1. FINDINGS. The legislature finds that

11 (1) some residents of the state who have obtained mortgage loans
12 from the Department of Community and Regional Affairs have mortgages with
13 payment obligations that exceed their present ability to make the required
14 payments;

15 (2) the Department of Community and Regional Affairs does not
16 have statutory authority to reduce interest rates;

17 (3) the costs of foreclosure and resale, including legal ex-
18 penses, publication costs, maintenance costs, repair and renovation costs,
19 sales expenses, closing costs, and costs due to sale in a distressed mar-
20 ket, may be very substantial;

21 (4) it may be in the department's and state's best direct finan-
22 cial interest to avoid foreclosure by modifying loan terms including
23 rescheduling principal payments, reducing interest rates and payment
24 amounts, and adjusting maturity dates to induce existing owners to remain
25 in title to the property and maintain active management of the property.

26 * Sec. 2. AS 44.47 is amended by adding a new section to read:

27 Sec. 44.47.525. MODIFICATION OF LOANS. (a) Notwithstanding
28 AS 44.47.410(a) and (b) and 44.47.520(b), on mortgages that it has
29 financed under AS 44.47.360 - 44.47.560 the department may, by loan

1 modification, reschedule principal payments or reduce interest rates,
2 or both, if the department finds that

3 (1) a loan modification would result in the likelihood that
4 the loan would pay to maturity and induce the borrower to remain in
5 active management and ownership of the property; and

6 (2) the loan modification would be

7 (A) in the best financial interest of the department
8 and the state; and

9 (B) considered prudent by private lending standards
10 taking into account the financial circumstances of the borrower
11 and other costly alternatives such as foreclosure.

12 (b) Rescheduling of the borrower's repayment of principal under
13 (a) of this section provides an interim payment adjustment and is not
14 intended to affect the obligation of the borrower to repay the princi-
15 pal amount on the mortgage loan.

16 (c) The department may reduce the interest rate payable on a
17 mortgage under (a) of this section only if the modification contains
18 an interest rate reopener clause. The interest rate reopener clause
19 must

20 (1) require that, if the interest rate is reduced, the
21 borrower and the department shall renegotiate the rate of interest on
22 the mortgage within five years of the date of an interest rate reduc-
23 tion approved by the department under this section;

24 (2) specify the date by which the borrower and the depart-
25 ment are to renegotiate the rate of interest under (1) of this sub-
26 section;

27 (3) incorporate a call feature reserving to the department
28 the right to demand repayment of the entire principal amount due if
29 the borrower and the department are unable to conclude renegotiation

1 of the rate of interest under (1) of this subsection; the department
2 may not use the call feature incorporated under this paragraph to
3 demand repayment of the entire principal amount due before the date
4 determined under (2) of this subsection.

5 (d) An interest rate reduction approved by the department under
6 this section cancels the borrower's obligation to pay the amount due
7 that is attributable to the difference between the original interest
8 rate and the interest rate reduction for the period of the rate re-
9 duction.

10 (e) When an interest rate is renegotiated under (c) of this
11 section, the renegotiated rate may not exceed the interest rate orig-
12 inally charged on the loan.

13 (f) The department shall adopt regulations prescribing the terms
14 and conditions of and the procedures applicable to loan modifications
15 made under this section.

16 * Sec. 3. This Act takes effect July 1, 1988.
17
18
19
20
21
22
23
24
25
26
27
28
29

H L+C
JUD

5-2066A
Bradley
3/14/88
* 3/29/88

* By the Rules Committee at
the request of
BY THE JOINT COMMITTEE ON ECONOMIC
RECOVERY (For the Subcommittee on
Housing and Banking)

1 IN THE HOUSE

2 HOUSE BILL NO. 549

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FIFTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act relating to notice requirements on the use of
7 a deed of trust; and providing for an effective
8 date."

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

10 * Section 1. AS 34.20 is amended by adding a new section to read:

11 Sec. 34.20.132. NOTICE OF OTHER REMEDIES. When a lender uses a
12 note as evidence of an obligation secured by a deed of trust, the note
13 must affirmatively advise the trustor and any other party bound by the
14 note, in writing within the note, of the security, recourse, and other
15 remedies, if any, available to the beneficiary. If it is intended to
16 permit the beneficiary to bring suit to collect an amount owing on the
17 obligation without foreclosing the deed of trust, this intent must be
18 stated in writing in the note. A beneficiary may not use a remedy not
19 specifically and clearly stated on a note executed after the effective
20 date of this Act. If a note executed after the effective date of this
21 Act fails to contain the notice required by this section, the debt
22 secured by the deed of trust may be foreclosed only under AS 34.20.-
23 070 - 34.20.135, a deficiency judgment may not be entered, and no
24 other action may be taken nor judgment entered against the trustor,
25 surety, or guarantor on the obligation secured by the note.

26 * Sec. 2. This Act takes effect immediately under AS 01.10.070(c).
27
28
29

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

Steve
STEVE COWPER, GOVERNOR

P.O. BOX 5
JUNEAU, ALASKA 99811-0400
PHONE: (907) 465-2300

February 19, 1988

The Honorable Max F. Gruenberg, Jr.
Chairman, Joint Committee on Economic Recovery
Alaska State Legislature
P.O. Box V
Juneau, AK 99811

Dear Representative Gruenberg:

At the meeting of the Joint Economic Recovery Committee Thursday February 18, you asked whether I believed the legislature should consider social responsibilities as opposed to only considering what to do about the contraction that has occurred in the Alaska economy.

My answer was that I thought of the word "economic" as encompassing both the financial issues and the social and political issues.

I realize that may have been a confusing answer. Perhaps this will make it more clear.

State spending was the driving force behind the recent "oil boom." If we had spent at lower levels, and had much more moderate growth, then the adjustment would have been much easier. Hundreds of condos would not have been built, and would not stand empty today.

As pointed out by Erickson, and other economists, letting the real estate decline (or market correction) settle out will result in lower costs, and a quick growth rate because of that.

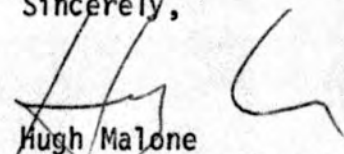
If the state intervenes, we will bias normal investment decisions, and make private dollars less productive than they otherwise would be. Economic recovery will be slowed, and the uncertainty and hardship will be prolonged. (Of course, if we could return spending to the per capita level of a few years ago, and keep it there, we will still be in fat city. But we can not - although we can squander our limited revenue).

Therefore, I think the most socially, politically responsible, and useful, thing we can do is to let the market correct itself.

The Honorable Max F. Gruenberg, Jr.
February 19, 1988
Page

Intervening is not social responsibility. At best, it is tinkering. At worst, it will waste what money we have and create an enormous sense of unfairness. I am not suggesting we let anyone starve, or freeze in the dark. I am suggesting we foster a private economy.

Sincerely,



Hugh Malone
Commissioner of Revenue

HM:m11
88-46

cc: Members, Joint Committee on Economic Recovery

MEMORANDUM

State of Alaska

TO: Milt Barker
Deputy Commissioner, Treasury
Department of Revenue

DATE: February 12, 1988

FILE NO:

TELEPHONE NO:

THRU: Vincent Wright *VW*
Chief of Research
Department of Revenue

SUBJECT: Commercial Real Estate
Subsidy

FROM: Alfred G. Zangri *AGZ*
Economist

Conclusion: Recent proposals to have the State purchase existing 'excess supply' of commercial real estate will likely have the following impacts:

1. Could cost the State something in the neighborhood of \$115 million to \$165 million if all current nonperforming and foreclosed property is covered;
2. Force rents higher than would have been in the absence of such a program which in turn will;
3.
 - decrease the level of business activity,
 - increase layoffs,
 - decrease aggregate demand and
 - decrease aggregate income

more they would have been in the absence of such a program while at the same time sending signals to the market which will;

4. Provide incentives for additional investment in commercial real estate in the face of existing excess supply;
5. Create an additional source of uncertainty in the economy as other interest groups exert pressure on the system to fashion their own bail out program which will in turn;
6. Further delay the adjustment process and delay the process of economic recovery;
7. Bail out a few banks rather than nonperforming building owners;
8. Result in a tax leakage to the federal government if commercial real estate investors tend to have a higher than average income;
9. Subsidize owners of commercial real estate and banks at the expense of the economy and the rest of the citizens of the state;

10. Result in leakage to out-of-state owners who will also benefit from the subsidy;

11. Result in additional leakage as the funds used in the program are unlikely to be reinvested in the state due to excess capacity;

12. Replace the market price with a state bureaucracy in making commercial real estate investment and allocation decisions with the resulting fallibility, inefficiency and opportunity for unequal treatment.

Discussion: This memo discusses the impact that the recently proposed commercial real estate excess capacity purchase program will have on the State economy. The primary focus of the discussion will be whether the economy is likely to be helped or hurt by the program. As a part of this discussion it is necessary to examine the distribution of gains and losses throughout the economy resulting from such a program. However, the central question is not the equity of the distribution. Instead, the question is whether the overall net impact of the program is to help or hurt the State economy.

Before assessing the impact of these proposals we must first examine the way the commercial real estate market works.

There are two types of operators in the market for commercial real estate:

1. The Users - these are businesses or professionals that rent or own commercial space for their use in day-to-day business activities.
2. The Investor - these are individuals or businesses that own commercial real estate for the revenue stream (rents and/or capital gains) the space yields.

The level of aggregate demand for goods and services determines the rental value and in turn the market value of commercial real estate. Investors' demand for commercial real estate is derived from the future stream of rents that the owner expects to receive. Users demand is derived from the profits they expect to receive from its use which are in turn derived from consumers' demand for the product or service offered by the business occupying the commercial space.

The problem that has occurred in the Alaskan economy is that the overall level of aggregate demand has fallen below the level anticipated during the building boom because there are fewer people than anticipated and those people are spending less. The result of this fall in aggregate demand is that business profitability has fallen, increasing both business failures and the number of marginal businesses. This in turn has reduced the level of demand for commercial space and created 'excess supply' in the commercial real estate market (as well as most, if not all, other markets).

We should realize, however, that 'excess supply' is a price dependent concept. This means that as aggregate demand falls and the general level of business activity declines users of commercial space have a demand for less space because some have gone out of business while others have found it necessary to reduce costs in order to stay in business. Part of this reduction in costs will be accomplished by reducing the rent they are willing to pay. This will cause these businesses to seek rent reductions from their existing landlords and/or move to less expensive or smaller quarters. Rents for all commercial space will begin to fall as owners of commercial space try to bring vacancy factors back to prior levels. Even businesses that are not feeling pinched will find that they can now rent larger and/or higher quality space at reduced rates.

Simply stated, excess capacity exists when prices are too high to clear the market. As prices fall the excess capacity will tend to be absorbed back into the economy. Two factors must be noted about this reabsorption: First, as rents fall and businesses tend to move up to higher quality space, vacancy factors in lower quality (older, less luxurious) space will tend to be higher than in higher quality (newer, more luxurious) commercial space. This occurs because the more marginal or risky or newer businesses will tend to locate in this cheaper space thus creating a higher turnover. This will in turn tend to increase the rent differential between lower quality and higher quality space. This process will be reversed as the economy recovers -- a fact that any investor in lower quality properties realizes.

The second factor to note about the eventual reabsorption of 'excess capacity' is that the adjustment period will not be fast. It may well take a number of years. There are some indications that the adjustment is well under way (see for example the Anchorage Office Space Market Analysis Summary - midyear 1987 which shows an increasing vacancy factor for lower quality space and a slowing vacancy factor for higher quality space).

On the other hand, as rents fall it is likely that leveraged commercial space investors will be unable to avoid increasingly negative cash flows which may cause additional buildings to be sold at losses. It is possible that the capitalized value of some commercial real estate has not only fallen below the level of existing financing but also below current replacement cost.

From the above discussion we can identify which people will benefit and which will lose from a general decline in commercial real estate rents. Those that stand to gain from decreased rents are

- businesses that use rented commercial space;
- customers of businesses that use rented commercial space;
- employees of businesses that use rented commercial space;
- investors in businesses that use rented commercial space.

Those that stand to lose from falling commercial space rents are

- owners of commercial space for rent;
- businesses that operate from owned commercial space;
- employees of businesses operating from owned commercial space;
- investors in businesses operating from owned commercial space;
- investors in banks that have inadequate reserves to cover nonperforming commercial real estate loans.

It is also possible to examine the likely impact of proposed solutions to the 'excess capacity' problem. First, if the State buys distressed properties at market prices and rents these properties at market prices there is no effect on the market. Rents will be driven down to the same level they would have reached in the absence of the State purchase. However, since this does nothing to relieve the perceived 'excess capacity' problem, the proposals put forward have been to purchase these properties and withhold them from the market either temporarily, by keeping them vacant, or permanently by bulldozing them. In either case this action on the part of the State will result in a subsidy to the owners of non-State owned buildings. This subsidy will occur because rents will be kept higher than they would have been in the absence of the State program. The result remains unchanged even if aggregate demand falls so far that some buildings cannot be sold at any price: the ghost town effect. Even in this case, purchase for land value or any other price by the State represents a subsidy to other building owners. Purchase and subsequent bulldozing by the State represents destruction of wealth.

This subsidy is directly paid for by:

- businesses that use rented commercial space;
- customers of businesses that use rented commercial space;
- employees of businesses that use rented commercial space;
- investors in businesses that use rented commercial space;

through higher rents, higher prices and/or fewer products available, fewer jobs available and decreased returns on their investments.

The subsidy is also indirectly paid for by all the citizens of the state through the opportunity cost of the program. This cost is the value of the lost benefits of the other programs that could have been funded with the revenues spent on the purchase of commercial real estate. Opportunity costs arise because the State has a limited amount of money to spend. Any money spent to purchase commercial real estate reduces the amount available to spend on other programs. The foregone benefits of these lost or reduced programs are, therefore a cost associated with the proposal.

One estimate of the potential size of this opportunity cost is 25% to 35% of the \$292.3 million in past due & non-accruing commercial

real estate loans plus the 165.2 million in foreclosed real estate owned by banks identified by the Governor's Office of Management and Budget (1/4/88)¹. To place these numbers into perspective consider that this \$115 million to \$165 million represents two to three times the FY88 authorization to the Municipal Assistance program². State purchase of these nonperforming loans will actually result in a bail out of the banks holding these loans not the current building owners. In fact the nonperforming owners will likely not only lose the building but also be hit with a taxable gain on the amount of the loan the bank has written off plus the accumulated interest, fees and charges associated with the foreclosure.

Both the direct and indirect costs will be imposed upon the State economy even if it is the lowest quality space that is taken off the market since this will keep rents higher than necessary and could well keep many start-up businesses from ever making it. Actual estimation of the net costs and benefits of higher rents for commercial space would require a difficult and, due to data availability problems, perhaps impossible, empirical study. It is likely, however, that since the proportion of businesses that rent space is greater than the proportion that own space, the losses of the losers from higher rents will more than offset any gains to the gainers.

Further if, as is likely, the income of commercial real estate investors is higher than the average income of the rest of the population of the state then the leakage to Federal income taxes will be greater than if the funds were used in alternative ways. It may also be more likely that commercial real estate owners will spend incremental income on out-of-state travel and other out-of-state goods and services. Additionally, to the extent that buildings are owned by out-of-state individuals or corporations, this leakage from the economy is increased.

It has been argued that the owners of other buildings will be unable to compete with buildings sold at distress sales. It is true that market conditions are causing building owners to accept reduced returns on their buildings as rents fall. On the other hand, if current owners believe that prices at any potential distress sale will be so low that they will be unable to compete, they have the option of purchasing the distress priced buildings themselves. This option will allow the owners of other buildings to minimize the reduction in their revenue.

In summary, the outcome of a State program to reduce excess capacity in commercial real estate will be to keep rents higher than they would have been in the absence of such a program which will, in turn, drive business, employment, aggregate demand, and aggregate income lower than they would be in the absence of such a program. Furthermore, implementation of this type of program will create an additional source of uncertainty in the economy as other interest groups exert pressure on the system to fashion their own 'bail out' program. This will further prolong the adjustment

period and delay the process of economic recovery. Banks and owners of commercial real estate will be the beneficiaries of this program while the costs will be borne by all the other citizens of the State.

FOOTNOTES

1. Memorandum to Mary Holloran. "Commercial Real Estate Background Report", R.A. Fineberg and Joan Kasso, Table 1, Jan. 28, 1988.

2. "Special Report Governor's FY89 Spending Plan", Legislative Finance Division, January 14, 1988.

U

OPTIONS
TO IMPROVE THE
ALASKAN ECONOMY

DAR/JAN 88

This paper summarizes the present economic situation within Alaska; discusses fundamental economic principles which must be adhered to in order to create a lasting and positive change for improvement; and sets forth a series of detailed options for implementation.

Alaska's Economic Situation

Alaska's present plight can be summed up in two simple words -- "Excess Capacity".

Alaska currently has:

- Excess residential housing to include condominiums
and mobile home units
- Excess strip malls
- Excess shopping mall space
- Excess office space
- Excess industrial and warehouse space
- Excess (high) retail inventories
- Excess work force as manifested by unemployment rates

True, there are some sectors of our economy which are doing well -- fishing, timber and tourism. These should continue to prosper as long as the dollar retains its low valuation relationship to the yen and other currencies. Some of Alaska's hard-core base industries (not always appreciated during the oil boom but now winning long-deserved recognition) include the military and Federal government sectors which offer high prospect of growth.

This paper will primarily concern itself with real estate because it is clear that the excess capacity referred to above relates predominantly to real estate and its support industry of: banking and mortgage institutions; private mortgage insurance companies; highly leveraged investors and mortgagees; real estate sales firms; and governmental institutions which now hold ownership in: loans secured by real estate; defaulted or delinquent real estate loans; and foreclosed upon property.

Fundamental Economic Principles

It should be clear to any student of basic economics that the supply curves of certain elements of the Alaskan economy are out of

desired equilibrium with demand. Conversely, demand curves are out of desired equilibrium with supply.

In short, the long-term solution to our problem can be found in:

- (1) Decreasing available supply.
- (2) Increasing business and consumer demand.
- (3) A blend of the two.

Unless our actions result in a permanent movement of either the supply or demand curve, or both, any benefit will be fleeting, costly and of no long-term consequence.

We do not require the implementation of actions which can be termed as "political", "placebo", "quick fix", or "bailout".

What we do need are well-thought-out approaches that effectively reduce (and certainly not increase!) supply. Increasing demand is a tougher venture because in almost all cases it falls outside of effective unilateral action.

Programs and Actions

The following options are submitted for consideration. Some programs are dependent on others; some stand alone. The adoption of any, all or a portion of a single option may be beneficial. The rejection of a particular option should not negatively affect viewpoints on others. Many of these options are not new; some are simply being set forth in writing for the first time. All are in the public domain.

1. Move Supply Curve (decrease supply) Permanently

Create an entity or a subsidiary of an existing entity such as AIDA.

Vest that entity with funds on a loan or grant basis from the General Fund of the State.

Entity purchases developed property held as "real estate owned" by financial institutions, mortgage companies, mortgage insurance companies, and governmental agencies such as FDIC, AHFC, AIDA, Permanent Fund. Purchase is for land value only.

Following acquisition, entity removes improvements thus reducing supply but retains underground utilities.

Entity holds what is now vacant land for the long term and eventually sells at acquisition value or (hopefully) appreciated value.

Proceeds of sales are returned to the State which has bankrolled the operation. Or vacant land is returned to the State and appropriated to a long-term trust. (Mental Health, Public Education, Permanent Fund, etc.)

2. Move Supply Curve (decrease supply) Permanently

Demolish and do not replace old and deteriorating low-income development housing, such as Hollywood Vista and Willow Park.

Aggressive action on the joint State-Federal level must be taken. If the Federal government will not act, the State must be prepared to take quick and decisive unilateral action -- at its expense.

Occupants of demised developments are placed in AIDA-or AHFC-owned multi-family or condominium units. To the degree necessary, condo owners will be given the opportunity to trade their units for other AHFC-owned property.

AIDA/AHFC will be reimbursed for their housing assets used by this program. Funds utilized are from Federal and/or State sources. The program should be coordinated by the Alaska State Building Authority.

3. Move Supply Curve (decrease supply) Permanently

We must step back and review the thought process involved in continually spending huge sums of money on maintaining mobile homes. There is a huge excess and no demand. Clearly, since there is no demand for the foreseeable future, this must be recognized and acted upon. Spend a few dollars for some full-page advertising in active construction areas around the world, find a buyer, load them on a barge and remove them from the state. Funds saved on maintenance and ground rent could be channeled toward work outs or rescheduling loans on quality assets.

4. Move Supply Curve (decrease supply) Five Years

Create a financial entity empowered to act like a bank -- except for receipt of consumer deposits -- under State regulation.

Regulation is important to assure that the entity does not become a super bank in competition with existing Alaskan financial institutions.

The entity is capitalized with stock or debentures or a combination thereof.

Stock is issued in exchange for real estate owned, defaulted loans and delinquent loans held by: FDIC; banks; mortgage companies; mortgage insurance companies; and state governmental agencies. Non-producing assets are exchanged for preferred stock which provides a minimal (but better than non-producing) return.

The entity is permitted to buy, sell and trade real estate. It is to service and collect on loans; to work out loans; and to reschedule debt. It may invest in financial assets.

It must do everything necessary to convert illiquid assets into cash and into income-producing cash assets while covering expenses and eventually making a profit.

The entity would sell off assets over the long term with major emphasis on stabilization.

As the entity becomes profitable and liquid, it distributes paid-in-capital and dividends.

NOTE: In the event that the entity cannot be capitalized entirely with problem assets, consideration may have to be given to an initial State grant or loan to partly fund the capitalization.

5. Stabilize Supply Curve (keep increases in supply to a minimum)
Five Years

The board of directors of AIDA (Alaska Industrial Development Authority) should place a moratorium on the financing of construction of new commercial or industrial facilities.

This moratorium is designed to curtail new supply, and supports and acts in concert with other actions directed toward stabilization of the economy. Supply problems cannot be met by some programs and exacerbated by others. AIDA would continue to finance existing structures with changing ownership.

Obviously, the curtailment of new activity assists local government in that controls on new supply create value in existing supply and thus stabilize or raise assessed valuation used in the computation of ad valorem taxes.

Curtailement of new activity can have a chilling effect on economic development in communities where there is no excess capacity in commercial or industrial facilities or in communities where a special purpose facility is required. It is envisioned that a moratorium would remain in effect unless the local governmental unit which is intended to be the beneficiary of the moratorium formally requests its waiver by the action of its local city council or borough assembly.

6. Stabilize Supply Curve (keep increases in supply to a minimum)
Five Years

This is similar to the proposal for AIDA except it applies to residential housing financed by AHFC, PERS, TRS, Permanent Fund and any other State line organization or agency.

Place by board, commissioner or trustee action, a moratorium on the financing of construction of new residential housing units to include single and multi-family residences, including condominiums and mobile homes. The moratorium is designed to curtail new supply, and supports and acts in concert with other actions directed toward stabilization of the economy. Supply problems cannot be met by some programs and exacerbated by others.

Existing housing stock which is changing ownership would continue to be financed by the respective agencies and organizations.

The curtailment of new supply will create value in existing supply and thus stabilize or raise assessed valuations used by local governments in the computation of ad valorem taxes.

This program, similar to its complimenting commercial and industrial program, contemplates that the moratorium can be lifted at the request of the local government governing body.

7. Stabilize Supply Curve (keep increase in supply to a minimum)
Three Years

The State of Alaska is planning to construct an addition to its court complex in downtown Anchorage. This facility is important to the Court System and to the Municipality of Anchorage as it centralizes expanded court activity and anchors downtown economic activity against mid-town drift. Also, the project is important in that it does produce a substantial number of construction jobs.

Unfortunately, the creation of new office space supply at the same time that huge excess exists is self-defeating from a macroeconomic perspective. If this project is to be completed within the concept of stabilizing supply, it can be done in such a way that it meets immediate Court System needs on one hand and defers meeting other needs for a three-year period.

Here, the building would be constructed as planned. However, only essentially needed courtroom space would be finished. Other space -- office space available through existing supply -- would not be finished in the initial phase. A subsequent construction phase, perhaps three years after completion of phase I, would provide the needed office space.

Absent this kind of compromise which curtails the wrong kind of supply (offices) and permits the right kind of supply (courtrooms), the project should be deferred.

8. Stabilize Supply Curve (keep increases in supply to a minimum) Three Years

Local governments have a strong, vested interest in the stabilization of supply. To the degree that new supply can be curtailed, value to existing supply increases as does assessed valuation and the local tax base.

Expansion in many communities has required the rapid extension of utilities. In some cases this extension has been imprudent in that it has leap-frogged undeveloped areas to reach new residential or commercial subdivisions.

The expansion has been imprudent -- in an economic sense -- because the rate base of the new development does not always carry the operation, maintenance or debt service costs of the extension.

Local governments should be encouraged to place moratoriums on utility expansions, rezonings and replats to discourage the new construction of the types of developed real estate now in excess. Flat moratoriums in this area offer a better prospect than selective ones because of inherent fairness and equal treatment to all.

9. Move Demand Curve (increase demand)

To the degree that demand can be stimulated to reduce or eliminate excess capacity, such stimulation should be encouraged.

If major financial institutions such as pension funds, endowments, foundations, the Permanent Fund, etc. -- who are long-term buyers and holders of commercial and industrial property -- can be induced to take major, institutional-grade buildings off the market for a long period of time, such action could remove upwards of \$50 million from the current real estate marketplace.

The absorption of this "high end" sector of the market has the impact of channeling investment capital of other (smaller) investors toward the distressed portfolio of loans.

The importation of investment capital through the formation of investment pools would increase the demand for ownership of Alaskan real estate and fundamentally move the ownership demand curve.

This proposal, however, would not move the demand curve for office space occupancy since investors only bring their money and not new tenants to the table. However, any ownership diversification outside of Alaska brings with it a degree of outreach, new contacts and beneficial exposure.

10. Move Demand Curve (increase demand)

Alaska has been the beneficiary of "settlement waves" in the past such as the gold rush, building of the railroad, construction of military bases, statehood, and pipeline construction.

Each new wave of Alaskans has contributed to the economy and stimulation of the next wave can create some of the demand needed to reduce excess capacity and stimulate economic activity across many business sectors.

Perhaps Alaska's best opportunity lies with the military. Restructuring of some domestic and overseas forces with Alaska as the beneficiary would have a dramatic impact.

Navy homeporting is on everyone's lips. But it can only occur in the context of a well-thought-out plan, positive naval interest and the actual execution of long-term leases and agreements which are clearly advantageous to Alaska and its people. It is strongly urged that Alaska not embark on a program which provides for construction of infrastructure in hopes of "luring" the navy. Secure the firm, documented commitment and then as part of the agreement, utilize State resources as necessary.

The Army, Air Force, and Coast Guard have been mainstays of our economy for many years. Recently, these institutions have taken a back seat to the glitter of black gold and its overwhelming economic power. It's time to return to a full appreciation of these military institutions and to actively pursue a greater presence in the state. As the balance of trade continues to falter, some consideration may have to be given to a restructure of some foreign-based units (Korea, Germany). Alaska should open initiative's to welcome shifts should they occur.

11. No Fundamental Change to Supply or Demand

The easiest measure -- but one with virtually no positive long-term impact -- is a capital projects appropriation.

Elements of the construction industry have been hit hard and it is apparent that we will not need new residential, commercial, industrial, office and strip mall construction for many years to come. This sector cannot and should not be propped up lest we either provide wasted subsidy or create false expectation. Jobs must be centered around preventative and actual maintenance of existing roads, ports, airports and governmental facilities rather than new construction which creates a need for increased operation and maintenance costs.

It is suggested that rather than expend a huge amount of funds on a placebo, some should be diverted toward activity which will fundamentally affect supply and demand, some of which is set forth in this paper.

12. A Caution

Both AIDA and AHFC have some unencumbered capital. This has been eyed -- covetously -- by those who feel that these "pots of money" are available for appropriation for "quick fix" programs or for funding additional programs or functions assigned to these two agencies. This capital should be viewed as reserves critically required by the agencies to support existing programs in this time of stress. Before consumption of these funds is seriously considered, inquiry should be made to respective agency boards of directors.

In Summary

- * Raze uneconomic residential and commercial buildings
- * Raze deteriorating low-income residential units
- * Sell excess AHFC-owned mobile homes
- * Create a work-out bank emphasizing stabilization
- * Moratorium on new construction of residential and commercial properties, subject to local government waivers

- * Construct the Anchorage Court complex addition in phases
- * Moratoriums on local government utility expansions, rezonings and replats
- * Encourage institutional purchases of quality commercial and industrial properties
- * Seek agreement regarding Navy homeporting before initiating construction of infrastructure
- * Regarding construction projects, emphasize preventative and actual maintenance rather than new construction
- * Leave existing capital reserves in AHFC or AIDA

Comment Draft 2/18/88

Comments should be addressed to: Gregg Erickson, senior economist, Division of Policy, P.O. Box AD, Juneau, AK 99811-0164 phone (907) 465-3568

The Recession, The Real Estate Crash, and Alaska's Economic Prospects

Introduction

Many Alaskans have been surprised by the severity of the current recession, and the speed with which it engulfed the state's economy. The collapse of the real estate market has been a shock, particularly in Anchorage. As long as anyone there can remember, investment in Anchorage real estate has been about as sure a thing as one could hope to find in this uncertain world. Granted, there have been ups and downs, but Anchorage real estate always held its value when the economy was doing poorly. When the economy was expanding -- during the Korean War, again after statehood, after the \$900 million North Slope lease sale in 1969, during the pipeline boom, and in the biggest boom of all in the early 1980s -- an investor could achieve extraordinary returns. In the intervals when the economy was stagnant, a real estate investor in Anchorage felt protected. "You never sold a piece of property for less than you paid for it," recalls John Rader, Anchorage lawyer and investor whose experience in Anchorage dates to the early 1950s. "It was almost a religious statement."

The benefits of real estate appreciation weren't just restricted to the very rich. Anyone wealthy enough to buy a home was able to play the game. The more a family borrowed to buy a home and the less of their own cash they used in the purchase, the faster their home equity would compound. Over the years, ordinary folks and major investors alike came to believe that there some rules of investing were better ignored. In Alaska, it always paid to be highly leveraged. In Alaska, the more an individual borrowed, the more an individual stood to make. And in Anchorage, one would never need to sell a piece of real estate for less than one paid for it.

No single event swept away this folklore, but it vanished nonetheless. In January 1986 Anchorage taxable real estate had an assessed value of \$13.9 billion, up 38 percent from two years earlier. In January 1988 municipal assessors estimated it at \$8.3 billion, down 41 percent in two years. Because a half billion in new construction was added to the tax rolls over the '86-'88

period, the average property in Anchorage took an even bigger beating.

This kind of collapse would spell trauma in any community, but because of Anchorage's demographics, growth pattern, and the policies of an activist state government, the distress has touched an especially large number of households. Anchorage's population is relatively young, and the town has been growing fast. In any other state most of the young families that dominate Anchorage's demographics would still be renting; a crash in real estate values would then be to their advantage since it would mean falling rents. In Alaska, though, the state has actively encouraged home ownership by providing mortgage credit at subsidized rates. The booming market made it look foolish not to participate, and in Anchorage about 29,000 households now owe about \$2.5 billion on subsidized residential mortgages.

According to Anchorage real estate broker Brooke Marston, these subsidized mortgages are now virtually all "underwater," e.g., the principal owed on the mortgage exceeds the market value of the home. The average family's equity in its home is one of its major repositories of savings. In Alaska, for most urban households, the value of that asset has been erased or become a net liability. The probability is that many now have negative net worth.

The purpose of this analysis is to examine these painful events in the broader context of Alaska's overall economic performance, addressing five questions: What caused the recession? When will it end? What sort of recovery can we expect? How will the real estate crash affect the recovery? And what are the economic policy options for state government?

The Inevitable Recession

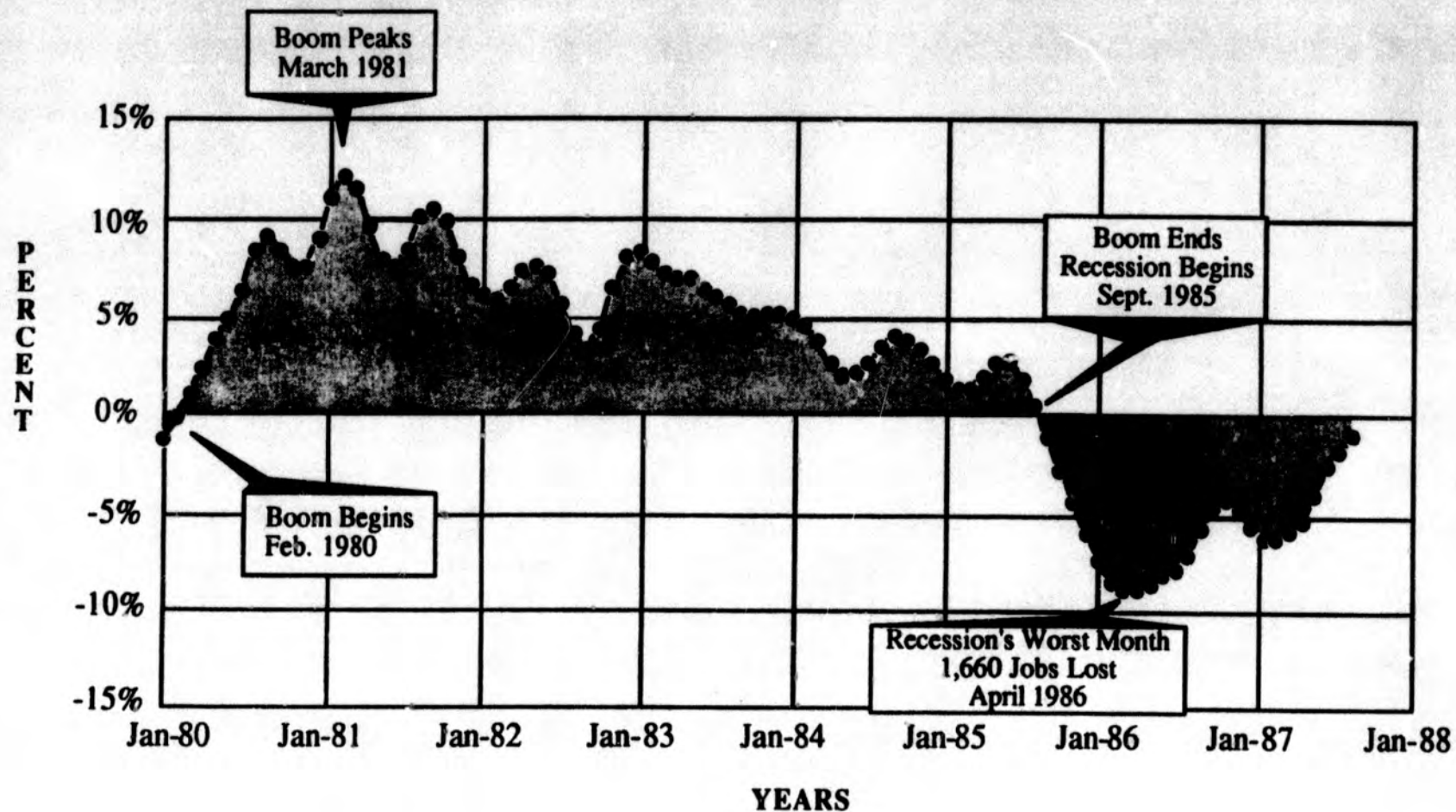
Alaska's recession had its roots in the extraordinary boom that began in early 1980s. *When the state government doubled its real per capita spending between 1980-81, a recession became virtually inevitable.* Using the rate of job creation and job loss (shown in Figure 1) as his yardstick, Scott Goldsmith, economics professor at the University of Alaska's Institute of Social and Economic Research, measures the peak of the boom in early 1981, when jobs were being added at the phenomenal 12 percent annual rate.¹ The rate tapered off slowly after that, but since growth was still occurring the economy continued to get bigger. The economy stopped growing in September 1985, which is the date ISER's Goldsmith identifies as the beginning of the recession. The first phase of the recession was exceptionally sharp, but it was also short: the economy hit bottom in April 1986, just 6 months after the recession started; at that point

¹ Economists who keep track of the business cycle on a national basis generally define a recession as two consecutive quarters of falling gross national product. Because figures for gross *regional* product are more difficult to determine, regional economists generally use falling employment as their measure. Economists recognize that there is much more to the evaluation of economic performance than is told by either GNP or employment.

Figure 1

Rates of Growth and Decline in Alaska Employment

Seasonally Adjusted Annual Rate



Source: Scott Goldsmith, ISER

Office of the Governor
Division of Policy
2/8/88

jobs were being lost at an 8.5 percent annual rate. Thereafter things improved, with the data from late 1987 showing jobs being lost at a 1 percent annual rate.²

The Alaska recession has not been typical. Regional recessions usually result from regional specialization, as in the manufacture of airplanes or the production of corn, combined with declining worldwide demand for the specialized product or service. The Seattle area specialized in large commercial jet transport aircraft. When demand for that product ebbed in the 1960s, Seattle lost 70,000 jobs in the space of a year. In the mid-1980s declining agricultural prices triggered a regional recession encompassing much of the Midwest. Here is the way the Scott Goldsmith, of the University of Alaska's Institute of Social and Economic Research (ISER) put it:

It is critically important to recognize that we brought this recession on ourselves, and that it was not primarily the result of weakness in the markets for the goods and services which Alaska sells to the rest of the world. This fact distinguishes our recession from those that have occurred in other regional economies.

The dramatic growth in state spending in the first years of this decade guaranteed that there would be an explosion of demand, and that private capital and labor would mobilize to meet that demand. Since much of this demand was from new public and private investment, demand was especially strong in the area of investment goods -- especially construction services and housing. Just to keep up with the growth in population and business required a Herculean effort. Few communities ever find themselves needing to add housing at a rate that would double the number of units in seven years. Since much of the growth was itself the result of new investment, there was a feedback loop. Economists call it an investment accelerator -- the expansion called forth investment which in turn accelerated the expansion. Unfortunately, the process also works in reverse. When growth stopped (notice we didn't say "reversed"), the Herculean effort would no longer be needed. And once a downturn was started, the feedback loop would cause it to feed on itself, to accelerate.

The only thing that could have prevented an eventual demand collapse was for state spending to keep growing. This would have required state revenue to keep growing. Some thought this a likely future, but it wasn't. When state spending stopped going up, the balloon would be punctured and the Alaska economy would deflate. The only questions remaining were when the recession would occur and how severe it would be.

This logic leads to an important conclusion. *The oil price collapse was not an important cause of the recession.* The oil price slide started in December 1985, three months *after* the recession began and two

² Some economists are less sanguine in their interpretation of the employment data, but most conclude that the recession, if not yet over, is in its final stages.

years *after* job losses started in the Alaska construction industry. Real (inflation adjusted) state spending stayed constant at \$6,800 per capita in FY 1983 and 1984, then increased to \$7,400 in FY 1985. The construction recession began in December 1984 (mid-FY 1985), notwithstanding the spending increase. With the beginning of FY 1986 spending fell to \$5,400 per capita.³

The FY 86 spending cut hurried along the recession which started three months later and made it more intense, but didn't cause it. The cause was that in 1981 the state of Alaska increased its spending at growth rates it could not reasonably hope to sustain, and adopted policies that encouraged private investment in housing, where the needs were only a temporary response to the inflated spending. *When state spending stopped growing, a recession resulted from falling demand for investment goods.* The collapse had its most severe consequences in construction and housing, precisely those areas where the state had the most success in its efforts to stimulate the economy.

The recession did not take Alaska's economists by surprise. Ten years ago, in March 1978, economist David Reaume and Goldsmith independently analyzed the effects of state spending growth expected with the beginning of Prudhoe oil production. Their analyses were contained in separate papers delivered to the annual meeting of the Western Economic Association. Both authors used the concept of "sustainable" spending (Reaume called it "sustainable revenue"). Both papers concluded that spending growth above the sustainable level would culminate in a self-inflicted regional recession.

Over the following decade this central conclusion was refined and reiterated by virtually every Alaska economist who wrote or spoke on the subject. Sometimes the conclusions were cloaked in mathematics or couched in eco-speak, but the warning was clear from the beginning. Here is how Dr. Reaume, phrased it ten years ago:

[I]ndependence from non-renewable resource revenue can be achieved ...if real state spending grows by no more than 2.5 percent per year...and if short term budget surpluses are carefully invested. A parallel conclusion is that ...the state faces a financial crisis by 1990 if it does not immediately restrict spending.

Despite the warnings, between fiscal 1979 and 1985, real (inflation adjusted) state spending rose at a compounded annual rate of 13.9 percent.⁴

³ The average U.S. state spends about \$1,700 per capita. All figures are unrestricted general funds expressed in constant 1987 dollars.

⁴ The annual real per capita growth rate over the whole fiscal 1979-88 period was 3.7 percent.

Recovery

If the economists are right, the end of Alaska's recession is imminent and doesn't depend on outside events like a rise in the price of zinc or corn or a change in the demand for Boeing airplanes. Alaska's recession will end when the decline in state spending ends and the excess capacity in areas like construction has, in the words of ISER director Lee Gorsuch, "been fully wrung out." Since most economists believe that both have already happened or are due soon, most also believe the job losses will end soon as well.

Precisely when will the recession end? Some economists believe it may already be over. A simple-minded extrapolation of Goldsmith's data (Figure 1) would suggest that employment actually started to grow between December and January. Chuck Caldwell, the state's chief labor economist, thinks this is possible: "I'm not going to make any predictions now, but when [the final seasonally adjusted numbers are in] we may well see that the economy started growing again around the first of the year." A Dittman Research Corporation survey of Railbelt business owners and managers conducted in January 1988 seems to provide some confirming evidence. Twenty-one percent of those responding said they planned to increase the number of employees in 1988, while only 12 percent said they planned to cut. Goldsmith himself predicts that the recession will end in the second half of 1988, a view shared by Reaume.

The pace of the recovery thereafter will be affected by any structural changes that occur in the Alaska economy, by changes in state spending, and by demand for Alaska's exports -- energy, fisheries products, wood products, visitor services, and defense services. The outlook for the state's export industries is generally favorable. Virtually all international economic experts foresee a protracted period -- perhaps 15 years -- during which foreigners will find U.S. dollars cheaper than at any time in recent history. For Alaska the change will mean growth. Consider tourism. The weakening dollar has reduced the cost in Japanese yen of an Alaska vacation, making it more affordable to the Japanese tourist. Moreover, Americans tourists will also be more likely to come to Alaska since the dollar cost of visiting foreign destinations, Alaska's competitors for tourist spending, will have increased. The same altered incentive structure will increase demand for Alaska minerals, wood and fisheries products.

In fishing, development of an on-shore bottomfish processing industry, discussed for years, has finally shown up this winter as real growth in employment. With one mine preparing for production and others well along in development, this time it appears that metal mining has finally started to grow. Federal spending is under pressure everywhere, but new military deployments to Alaska and increased federal park and wilderness management responsibilities in the state may mean an increasing overall federal presence in the economy. Petroleum employment is growing now,

reflecting the extraordinary profits available from further investments in already producing fields. The oil companies and state forecasters expect long-term increases in the real price of Alaska oil, but even if this doesn't materialize, labor required to produce existing fields will increase due to technical factors common to all declining fields even as production declines. The consensus among Alaska economists is that demand for the goods and services Alaska produces will grow, and that this growth will add new jobs to the Alaska economy at a rate of 1 percent or so annually, starting in 1988 or 1989 at the latest.

Recession's Dividends

Scholars of economic development have noted that the great economic "leaps" recorded in history often come as the result of a crisis of one sort or another. The crisis brought about a reordering of society that was key to releasing suppressed opportunities and efficiencies. Alaska's recession isn't likely to spawn an economic miracle, but it is eroding two longtime barriers to Alaska's development -- high wages and inflated prices. Whatever one may feel about these changes -- and there are many who are hurt by them -- "[t]he bonus ...is an increase of competitiveness of our economy both in the production of basic commodities, and in the local production of support services," states Goldsmith.

The most immediate economic impact of falling real estate values is the boost it gives to the purchasing power of people that rent. Mike Breedlove, chief demographer for the Municipality of Anchorage, estimates that 31,000 Anchorage households live in rented quarters.⁵ Assuming 2.4 persons per household, and if the average rental cost two years ago was \$200 per month per person, the roughly 40 percent drop in rents has added an average \$960 to the annual spendable incomes of these 75,000 people. This "renter's dividend" has thus increased Anchorage's spendable income by about \$72 million, and has had about the same economic impact as would result from hiring 1,400 new state employees in Anchorage.⁶

The recession hasn't been all bad for businesses either. Anchorage has about 7.8 million square feet of net rentable office space, and 5.4 million square feet of retail space. Assuming that 70 percent percent of that space is renter occupied and that monthly costs have declined by \$0.75 per square foot from their levels three years ago, the business renter dividend in Anchorage is over \$80 million per year, the equivalent of another 1,600 additional jobs in the Anchorage economy.

Declining real wages have hurt household purchasing power, but they've provided business with a powerful competitive boost, and many have taken

⁵ The figures do not include renters living on military bases.

⁶ The calculation assumes an average annual salary of \$35,000, and a personal income multiplier of 1.30.

advantage of it. Oil companies can now make money in fields like Kuparuk with wellhead prices as low as \$3.50 per barrel, and Alaska petroleum construction contractors are starting to bid fabrication work away from competitors in Oregon or Korea. Space rental and labor are the biggest cost items in many service and support sector businesses, so declines in these costs are particularly important to holding on to the recent growth in these sectors. Alaska retailers have also been helped by declining transportation charges. According to Greg Carr, of Carr's Quality Centers, these factors together contributed to narrowing the differential between grocery costs in Alaska and Seattle, a differential which he believes is now only about 3 percent. This has also produced a "dividend" for all residents.

The full ramifications of these changes cannot be predicted, but they suggest structural resilience and adaptability in the Alaska economy. These are good attributes for any economy, and especially valuable traits in a period of economic uncertainty.

The Real Estate Crash

The economists haven't completely ignored the \$8 billion or so in Alaska real estate values lost over the past two years.⁷ ISER economists recently studied the Anchorage housing market for the Alaska Housing Finance Corporation; they said to expect further declines in values, especially in Anchorage. Nevertheless, there is wide agreement among Alaska economists: *The real estate crash will tend to stimulate economic growth in Alaska.*

The reason is jobs. A bankrupt real estate investor has minimal impact on employment, but a bankrupt hardware store may signify a real loss in jobs. The real estate crash makes it hard for real estate investors, but it makes it easier on hardware store by lowering its costs. This mean the store is more competitive, which means more business and more jobs, so the real estate crash means employment is likely to grow. What if the investor also owns the hardware store? No problem -- the investor sells the business to cover his losses. The new owner pays more attention to the business, and with lower occupancy costs becomes more competitive. Because it means more jobs, the real estate crash is good for the Alaska economy, however difficult it may be for individuals.

Given this view, economists tend to be skeptical of schemes to rescue the economy by spending public money on real estate. Indeed, they express considerable skepticism about any *economic* justification for trying to prop up the real estate market. Part of this skepticism arises from growing doubts

⁷ The loss in Anchorage private real property values has already been \$5 billion; making allowances for the losses elsewhere in the state, the likelihood of further losses, and losses of "going concern" values, \$8 to \$10 billion is a reasonable guess for the toll the recession has taken on the value of Alaska assets. Outside investors, mortgage insurance companies, and the federal deposit insurers have absorbed a major part of this, however.

concerning state government's institutional suitability for managing economic change in general. "It seems very clear to me now that politics and the kind of hard objective decision-making needed...will never be reconciled," writes Dr. Reaume, formerly chief economist in the state Department of Commerce and Economic Development and formerly a leading advocate of aggressive government action to achieve development. Professor Hayden Green's skepticism is more concrete: "Some of the same people who recommended we spend ourselves into this nightmare are now telling us that they can get us out by using the same concoction that made us sick as medicine to heal us...."

The Dissenters

One expert who disagrees with this generally upbeat view of the economy is Scott Hawkins, formerly chief economist with Alaska Pacific Bank and now executive director of the Anchorage Economic Development Corporation. He believes that the real estate collapse and repercussions in the banking sector have "given Alaska a bad name" among outside banks that had been providing loans for Alaska development or were thinking of coming in. "It will be ten years before some of those [institutions] consider coming back to Alaska," Hawkins predicts. He argues that the resulting lack of capital is likely to cause retarded development.

Some economists are concerned that mergers will increase the share of the state's banking business controlled by the two or three largest institutions, possibly causing reduced competition in credit markets. Nevertheless economists apart from Hawkins discount "capital shortage" as a significant drag on development. Less money is flowing to the state now than two years ago, just as Hawkins suggests, and outside banks that thought they saw opportunities here, now probably see the issue differently. But it is important not to confuse cause and effect. Less money is being invested in Alaska because there are fewer opportunities for profitable investment, not the other way around. It is a situation that is not likely to change for several years, at least as far as the kind of lending that outside banks did during the boom. Their loans went largely to build shopping malls, offices, and homes, all of which are now in oversupply in urban Alaska. Meanwhile, deposits in Alaska banks have declined by less than 3 percent during the recession. Opportunities to make profitable loans, on the other hand, have declined much more significantly. The result is that *Alaska bankers are scrambling to find creditworthy loan customers*. "If someone with a serious business proposition comes through my door, I can assure you that person will have no difficulty in getting what he needs," said one Anchorage banker. Juneau economist and business consultant Eric McDowell agrees: "If I had a money-making idea that required capital, I could get it in an instant. The problem is that there aren't that many opportunities out there right

now."

Hayden Green, professor of real estate at the University of Alaska at Anchorage, is the other notable dissenter from the consensus view, though not on the capital shortage issue. Green argues that the collapse in property values will cause Alaskans to feel less wealthy, and this will cause them to reduce their consumption of goods and services, including goods and services provided by other Alaskans. Declining demand will mean more layoffs, thus propagating and prolonging the recession.

In eco-speak this is a "wealth effect." It will have some impact, but economists don't generally expect it to be significant. Goldsmith notes that the stock market crash wiped out \$1 trillion in wealth overnight and has had little apparent effect on consumption. In interviews with Anchorage retailers, Seattle consultant Dr. Bill Mundy found that "stores...that sell non-discretionary items (such as groceries) indicate that sales [in the first half of 1987] are just about the same as a year ago or off some, but not dramatically as one might expect." Mundy also notes that employment in stores selling general merchandise didn't decrease at all from March 1986 to March 1987, and that food store employment actually increased. According to Professor Lee Huskey, co-author of ISER's recent study of the housing market, if people do respond with reduced consumption, items foregone will be heavily weighted toward items with low "Alaskan" content such as Hawaiian vacations and Cadillacs. "The effect will be very marginal."

What about the arguments that a state funded entity, a so-called vulture fund, is needed to buy up distressed properties and keep them off the market? The "Phoenix Fund" proposed by Hawkins would be designed to prevent...

an unnecessary acceleration of small business bankruptcies [and] the additional failure of Alaska financial institutions, which would set off another cycle of falling real estate values, rising foreclosures, business bankruptcies, job losses, population outflow, etc.

The fund would be run by Hawkins' Anchorage Economic Development Corporation.

Fundamental to this line of thinking is the assumption that Alaska economic development will be hurt by falling property values. Economists, as noted earlier, simply don't buy this idea because they think falling property values will on balance increase jobs. "The real estate collapse is tough on those who invested in property," says McDowell, "but for the economy at large it is of little consequence." According to Reaume, "the current real estate situation may have major positive ramifications on the economy. A 'buy out,' on the other hand, could induce mistakes in the future. It's a bad idea." Department of Revenue economist Al Zangri is specific:

" [a] state program to reduce excess capacity in commercial real estate...will

... drive business, employment, aggregate demand, and aggregate income lower than they would be in the absence of such a program. Furthermore, this will create an additional source of uncertainty in the economy as other interest groups exert pressure on the system to fashion their own 'bail out' program. This will further prolong the adjustment period and delay the process of economic recovery."

Connie Yoshimura, an Anchorage real estate broker, points out the shaky technical assumption underlying the vulture/Phoenix fund idea -- that purchasing distressed properties will stabilize the market for holders of other properties. The Anchorage market has seen a "distinct flight to quality." She argues that the demand for mid- and high quality property is largely independent of the demand for the low quality properties that constitute virtually all the distressed assets. According to Yoshimura, removing those assets by demolition might make sense as an urban renewal strategy, but will have no effect on prices or demand for anything except the the very lowest quality properties, most of which are already in foreclosure. Professor Green expresses similar concerns.

Loss of Confidence

Despite economists belief that the direct economic effects of the real estate crash will be positive, the regional recession in Alaska is at least partly beyond the range of economic experience. It is a reason for caution.

An event this encompassing could conceivably have non-economic effects that could feed back into the economic system in unanticipated ways. Anchorage real estate broker Chris Stephens has suggested that most severe effect of the market crash could be the loss of entrepreneurial talent. Most economists scoff at this idea. "Heck," ISER's Lee Huskey remarks, "lower costs are going to make it *more* likely entrepreneurs will succeed."

Arlon Tussing, a Seattle economist and frequent visitor, thinks the odds are good that the loss of confidence won't last very long or extend very deep into the fabric of Alaska society. So far, the evidence seems to favor this view. Anchorage's municipal demographer Michael Breedlove estimates that 59 percent of the households lost in Anchorage since 1985 have been male headed, non-family households, a category that accounts for only 18 percent of total households. Moreover, 80 percent of the population loss has been in 20-30 age group, and two-thirds of the loss is accounted for by males. These numbers don't suggest a broad-based exodus.

But what about the attitudes and intentions of those who remain? Population movements tend to lag changes in the economy, so a collapse of confidence could have already happened, with the resulting wave of out-migration only now beginning. As far as attitudes are concerned, the answers given by Dittman's Railbelt respondents don't reflect any sense of crisis: 44 percent say the economy will get better over the next two years,

compared with 16 percent who see things getting worse.

What about the 18 percent of Dittman's respondents who reported they were "very likely" or "quite likely" to leave Alaska within two years? For some observers the number was "shocking." Gregg Williams, the state's chief demographer, doesn't see it that way. "Every year, in good times and bad, about 15 percent of the people in Alaska leave. The [poll] results are about what I'd have expected." According to Dr. Williams, the number of people coming to Alaska is much more variable than the number leaving, and much more sensitive to economic conditions. Unfortunately, surveys of people already in Alaska, whether the results are "shocking" or "expected," tell nothing about the intentions of those not yet here. The guessing among experts like Breedlove and Williams is that population isn't in for any collapse in Anchorage, and certainly not in the balance of the state.

Alaska's Policy Options

Many of the experts who are saying there is no economic justification for using public money to prop up the real estate market are also owners of homes and other real estate. A few of them suggest that there may be some *moral* justification for state government involvement. "After all," one asked rhetorically, "doesn't everyone agree that the state government was responsible for getting us into this?" But even those who see a moral basis for state intervention sense that whatever state government's guilt, indemnification of those who have taken losses would be beyond its means. And proposals to assist only a segment of the market, say the commercial real estate market, are hard to take seriously when so many others have also been hurt. Indemnifying all Alaskans hurt by the real estate collapse would simply cost more than the state could afford.

Besides, excess capacity in investment goods and services (like construction) has dissipated, and it seems likely that the state will arrest the decline in public spending. If this happens, the recovery will occur regardless of what else the state does or does not do. That doesn't mean that prompt, informed government action would not save a lot of pain. Unfortunately, what the government should do, apart from not trying to corner the real estate market, is not nearly so clear. It would make sense to allow people to carry their negative equity along with them to a different house. Whether the public and private bureaucracies involved are able to handle these transactions remains to be seen. It doesn't make sense to have a moratorium on foreclosures. The rights of condominium associations may need to be strengthened. The policies and role of the state's lending agencies -- especially AHFC, need review. Millett Keller, an Anchorage business consultant, suggests that the real estate collapse provides Alaska communities with "opportunities to accomplish ... public sector projects at bargain rates," including acquisition of property for parks, greenbelts and rights-of-way for

future transportation facilities, assuming government can avoid carelessly mixing in subsidies and economic recovery. That may be an optimistic assumption, but Commerce and Economic Development Commissioner Tony Smith was surely on target when he testified that "we can't spend ourselves out of this one, we have to manage ourselves out of it."

Borrowed Time

With management -- and a little luck -- the real estate crash will do no lasting damage to Alaska's economy. Years hence Alaskans may look back at the recession and post-recession period as a time of renewal and opportunity. If so, it will probably be because Alaskans learned the lessons that this self-inflicted recession had to teach.

On this point, however, the returns are still to be counted. Alaska did cut its spending in FY 1985-88, but not enough to erase the fundamental imbalance that Drs. Goldsmith and Reaume first described ten years ago. In a speech early this year Goldsmith described the imbalance as a problem

which always takes a back seat to concerns which are more immediate or pressing, but it is the most pervasive issue we will face in the next decade. *In the long run the economy is still living on borrowed time.* We continue to artificially stimulate the economy by selling off the assets of the state -- our petroleum wealth. How we adjust to a sustainable level of government will affect us all as surely as this recession. [emphasis added]

Unless Alaska controls its public spending, the state will be buying a ticket to a rerun of its present recession. Showtime will be within the decade, and probably sooner.

Another old imbalance also remains. Alaska has developed a mature economy, but parts of rural Alaska have increasingly been left behind. Disparities in income, employment, educational success, health, and a host of other measures all are all widening. Some economists say that this is the kind of problem that economics shouldn't have much say in solving, but all agree that the growing disparities are already a drag on economic development *throughout* Alaska, and that these disparities will become an even greater burden in the future. Economic solutions that might work seem unacceptable on other grounds, and solutions acceptable on other grounds clearly don't work economically. It is a tough issue that won't be ignored.

Alaska's economist emeritus George Rogers wrote in 1962 of how many Alaskans subscribe to the view that economic forecasting "should be a projection of present hopes, that prediction should bolster self assurance. Forecasting in this view is only valid if it agrees with a popularly held dream of the future and makes its realization appear likely."

Today, economists' believe that the real estate collapse will not produce dangerous consequences for the economy as a whole. This view runs counter not to a popular hope, but to a popular fear. A lesson from the recession and

real estate crash may be that hopes and fears, like dreams, are better servants when they are firmly founded on a hardheaded respect for history.

Reference Notes (Incomplete)

If not otherwise cited, quotations are from personal conversations with the author.

Taxable Anchorage real estate values are from Phil Webber, municipal assessor's office, Municipality of Anchorage. Data on the number of Anchorage AHFC mortgages are from AHFC. State spending data are Division of Policy figures.

Goldsmith's seasonally adjusted employment figures have not been published, but are available from him or the author. Goldsmith's statement on the cause of the recession is from "Remarks to the Alaska Policy Forum," January 7, 1988.

The papers presented ten years ago to the Western Economic Association are "Fiscal Planning and the Long-run Growth Pattern of Resource Based Open Economies," by Goldsmith, and "Alaska Financial Planning and the Permanent Fund," by Reaume, both dated March 1978.

For more on Caldwell's and his Department of Labor research staff's view on the end of the recession, see Edward Eboch, "Alaska's Employment Scene," *Alaska Economic Trends* January 1988. Reaume's recovery estimate is found in his article, "One More Year of Employment Decline," *Alaska Construction and Oil Report*, January 1988. He thinks despite the expected upturn in late 1988, average employment figures for the year will be down. Goldsmith's predictions are found in his Alaska Policy Forum remarks. Also see "Can State Spending Speed Alaska's Economic Recovery, December 8, 1988, by Goldsmith and Gorsuch, research memorandum prepared for Governor Cow

The Dittman survey data is found in *Railbelt Economic Assessment Survey*, January 1988, by Dittman Research Corp. The Anchorage demographic information is from the *1987 Anchorage Population Profile*, December 1987, prepared by Breedlove, *et al*, in the Community Planning Department, Municipality of Anchorage. It is an extraordinarily useful document.

Figures on total available office space figures are from Norman Rokeberg, Jack White Realty. Retail space figures are from Alaska Valuation Services, Fred Ferrara, president, as provided by Connie Yoshimura in testimony to the trustees of the Alaska Permanent Fund, February 10, 1988.

The Greg Carr quotation is from an Associated Press story datelined Fairbanks, December 2, 1987.

It's time to take economic action

Picture this scene: a very ill patient is laying in a hospital bed. His original case of influenza is nearly gone, but it was so severe that it left him susceptible to pneumonia, which is now threatening his recovery. His vital signs are deteriorating and his prognosis is uncertain.

But oddly, the doctors can't decide what to do! They're huddled in another room, locked in heated debate. Should they do anything, or should they just let nature take its course? If they do "do something," what should it be? Who should do it? Who should get the credit if it works? Who might get blamed if it fails?

Does this scene sound preposterous? It is, but it could happen right here in Alaska. In case you haven't already guessed, the pneumonia patient is the Alaska economy, and the doctors are its elected officials, business leaders, journalists and economists.

As the debate drags on, Alaska is entering its third year of recession. But in recent months, the relevance of the debate has increased. We now have more of an opportunity to stop the deterioration than we had before. The reason is that the nature of our problem has changed.

Two years ago, a large drop in oil prices left a hole in our economy that couldn't be filled. Period. But after losing nearly 10 percent of our jobs and people since then, we have completed most of the necessary downsizing. Our new problem is controlling the financial aftermath of such a sudden and severe adjustment.

That, however, is doable. Financial damage control is much more realistic than trying to immediately replace billions of dollars in lost oil revenue. Yet, the payoff could be enormous.

Indeed, one should not underestimate the damage further financial deterioration could cause and the corresponding benefits of preventing it.

There was nothing about the 1929 stock market crash and ensuing recession that, in themselves, forced the U.S. into a decade-long depression. Rather, it was excessive adherence by policymakers to the "let nature take its course" doctrine during the following five years. That moral doctrine is what led Congress and the central bank to stand idly by while the financial aftermath snow-balled and wiped out nearly



By Scott Hawkins

one-third of the nation's banks, crushed its real estate and business asset values and perpetuated the economic downturn.

Sound familiar? Those that see no parallel between the U.S. in the early 1930s and Alaska in the late 1980s should look again. Four of Alaska's 14 banks have failed in the past year, and they were four of its largest seven. Two are in FDIC receivership and two more were merged with each other and given reprieve through an infusion of capital. Business and real estate assets have plunged in value. Longtime, well-established Alaskans have gone bankrupt.

The potential for yet another cycle of foreclosures, bankruptcies, liquidations, falling asset values, failing financial institutions, job losses, etc., is very real. The FDIC has yet to dispose of the loans and real estate that it is already holding in receivership. Several other banks and thrifts are considered vulnerable, and the newly merged bank has yet to come to grips with the massive portfolio of real estate and troubled loans.

The manner in which these troubled assets are managed will be crucial. If the various managers put short-term cash recovery as their highest priority, they will deal with debtors rigidly and market the foreclosed properties and business assets aggressively.

Obviously, this would further depress asset values and prolong Alaska's financial deterioration. Yet, how can individual managers be expected not to strive for short-term cash recovery, especially in today's business environment?

Several ideas have surfaced in recent weeks. Permanent Fund director Dave Rose has suggested that the state establish a "bridge bank" that would swap stock for real estate with the FDIC and other financial institutions, and then hold those properties off the market or manage them with the intention of stabilizing the market.

When the properties are liquidated gradually over period of years, the proceeds — minus expenses — would be returned to the stockholders.

Sealaska and the state Commissioner of Commerce and Economic Development, Tony Smith, are investigating a real estate investment trust (REIT) that would buy up properties, hold them for a period of time, and sell them gradually. It would be funded by native corporations, wealthy Alaskans, not-so-wealthy Alaskans and perhaps even the state.

The organization I represent, the Anchorage Economic Development Corporation (AEDC), has proposed something very similar to Dave Rose's "bridge bank." We would establish a statewide non-profit, non-governmental affiliate to purchase the FDIC's portfolio of loans and properties and manage both with a long-term view toward economic stabilization. Our purchase would be funded by the proceeds of a long-term bond issuance that, depending on how it is structured, may require a "moral backing" or capitalization loan from the state.

Once the FDIC purchase is complete, our concept can be expanded so that some of the troubled assets of other banks and thrifts can be purchased as well. Any surplus revenues that this non-profit corporation realized (in excess of expenses and debt service) would be returned to state and local governments for distribution as economic development block grants.

All of the above proposals are compatible and mutually reinforcing and all seek to stop Alaska's financial deterioration by marketing troubled assets less aggressively. They would stop the deterioration of real estate and business asset values by easing the aggressive competition among sellers. The economy would "hit bottom" sooner, values would begin to recover sooner, and virtually everyone would benefit. A public purpose would be served.

But this is not an issue that can wait a year. If nothing significant is done soon, nature will take its course. And we may or may not like the results.

Economist Scott Hawkins is president of the Anchorage Economic Development Corporation.

Legislature Must Intervene