

ALASKA LEGISLATURE SPECIAL COMMITTEE/SUBJECT FILE 8672
2176 SCOMM 83: HOUSE SPECIAL COMM. INTL. TRADE & TOURISM, 1991-92

SOVIET BUSINESS JOURNAL

Volume III, Number 1

January 1992

PRICE INCREASES

In anticipation of price liberalization the consumer market is panicked. In November, price increases in commercial trade amounted to about 22% in the average, while prices for goods in great demand rose by 120%, in comparison with October.

State prices for food have increased by 15% a month, while for some kinds of meat and bread they have increased by four times. As a result, prices at farmers' markets have also increased by 100-200%.

The growth of the cost of living in major cities was 24%. The rate of inflation grew by 35%.

Experts predict that in December the average growth of the cost of living will be at least 25%.

This data clearly shows that prices became free long before the official date of their liberalization.

In spite of sharp price increases, there are practically no goods to buy - there are just prices. Stores are even emptier than before. People standing in lines for food for hours say that it is time for Yeltsin to come out of his study and have a look at what is actually going on. Prices are already so high that many people can afford only bread. The consumption of bread has significantly increased and the longest lines are those for bread. What will happen next when prices are freed? Officials seem to believe that liberalization of prices is the last possible remedy that will immediately

solve all the problems. But prices are already sky-rocketing, and nevertheless the situation shows no signs of improvement. (*Kommersant*, No. 48)

COMMONWEALTH OF INDEPENDENT STATES

On December 8, the leaders of the three Slavic republics - Yeltsin (Russia), Kravchuk (the Ukraine) and Shushkevich (Byelorussia) - signed an agreement on the Commonwealth of Independent States. The three leaders managed to reach an agreement on a unified monetary policy for the period of economic stabilization and the openness of their borders. The Ukraine and Byelorussia confirmed their obligations to supply more food in order to prevent emergency situation in Russia and especially in Moscow. The Ukraine and Byelorussia also agreed to liberalize prices in order to support the same in Russia but insisted that the date will be changed from December 16, 1991 to January 2, 1992. The agreement also stipulates that its member-countries will ensure unified control over the nuclear potential of the country.

As a result, Yeltsin again appeared a great politician who managed to turn the coming confrontation with the Ukraine into a hearted consent. But the hardest job of

working out concrete details of the pact is still ahead.

President Gorbachev seemed offended. In a talk with a Ukrainian TV correspondent he said: "I started this process and I stand for it. But I do object to an extremist approach to the problem of achieving national independence and sovereignty. The consequences may be very severe. I agree, that I bear the responsibility for the fact that the process of disintegration of the USSR was not stopped in time. We are now on the brink of chaos and anarchy."

On December 9, President Gorbachev made a statement. "For me, the president of this country, the main criterion of the document in question is how far it meets the interests of the security of its citizens

(Continued on Page 5)

IN THIS ISSUE. . .

Feature Articles 1 & 5-8

News From The Republics 2-5

News In Brief 4-7

Produced by the Center for US/USSR Economic Cooperation, Moscow, U.S.S.R., in conjunction with the Foundation for Soviet/American Economic Cooperation. Produced and distributed monthly, the Soviet Business Journal is Moscow's most objective reading service for foreign businesspeople. This state-independent organization compiles information from 130 dailies, periodicals, magazines, independent publications and Soviet Television. For more information, please call one of our U.S. representatives, Svyatoslav Raikov or Katy Rusho at (206) 443-1935. Editorial Staff: Founder and Publisher: Svyatoslav Raikov, Chairman of the Center for US/USSR Economic Cooperation; Managing Editor: Katy Rusho, Foundation for Soviet/American Economic Cooperation; Contributing Editors: Kevin Horst and Natasha Lozitskaya; Stylists: Janna Gross, Kelly Lanpher.

News From The Republics

RUSSIA

■ Aeroflot opens its international operations with a flight from Moscow to Paris. Before the end of the year, its airplanes will fly also to Tokyo, London and Rome. Tickets are sold for hard currency only. (*Komsomolskaya Pravda*, 11/12)

■ Russian Interior Ministry officials do not believe that the introduction of coupons for food staples in Moscow will play any significant role in the lives of Muscovites. Most of the food products are now bought by dealers from the Caucasus with the help of corrupt shop employees and sold for astronomical prices in the provinces. This concerns sugar and vodka which were rationed a couple of years ago. (*Trud*, 11/14)

■ The unemployment benefit (272 rubles a month) is much lower than the minimum survival level (521 rubles) according to the estimation of the Moscow Federation of Trade Unions. (*Trud*, 11/15)

■ The chairman of the Peasant's Party, Yury Chernichenko, who is also a prominent public figure and writer, has accused the Moscow administration of putting their power ambitions before the well-being of Muscovites. To back up the charge, Chernichenko says that on November 10 he wrote to Mayor Gavril Popov and Vice Mayor Yury Luzhkov asking them to offer the Farm Manager cooperative 15 vacant food stores so that it could provide muscovites with meat, sausage, pickles, fresh fruit and vegetables. Besides homegrown produce, the cooperative said its groceries would offer a wide choice of imported food from Hungary, Switzerland and other countries whose firms agreed to sell it for rubles. The author blames red tape for the matter remaining still unresolved. Worse still,

it has been learnt that his letters were handed down to deputy mayors, then further down to their clerks, and on to the bottom of the bureaucratic hierarchy where the Farm Manager was told to forget the idea altogether. (*Vechernaya Moskva*, 11/23)

■ The mayor of Moscow, Gavril Popov, has signed an instruction on the privatization of government-owned and municipal housing. As of today all contracts on the transfer of housing to Muscovites for private use are to be drawn up by district and neighborhood housing offices. To have their flats privatized its occupants are to submit an application and pay 250 rubles for the operation. A law on real estate taxes is expected to be drafted before January 1st. (*Radio "Echo of Moscow,"* 11/25)

■ By the beginning of next year, the Russian labor market will number close to 15 million people. Over 2 million will have the official status of unemployed persons. Only 8 to 10 percent of those registered with employment agencies can hope to receive unemployment benefits. (*Trud*, 11/26)

■ Eighty percent of all the icons that were in the territory of the USSR during the 80's have been smuggled out of the country. Now there seems to be more Russian icons abroad than in the USSR. (*Vesti*, 11/27)

■ It was announced that the Russian Republic is going to undertake the obligation of paying the salaries of all workers in the Union Ministries and officers in the Soviet Army. By doing this, Russia retains the right to cut down its contribution to the Union budget by several billion rubles. It looks as though the army and the Union structures are being peacefully transferred under the control of the RSFSR. (*Vesti* 12/2)

■ The mayor of Moscow, Gavril Popov, apart from his main job as the mayor of the capital, holds the following positions and titles: editor-in-chief of the *Voprosy Ekonomiki* (economic questions) journal, a member of the High Consultative Council of the Chairman of the Russian Supreme Soviet, a member of the Political Consultative Council of the USSR President, head of the City Assembly, a USSR people's deputy, President of the USSR Baseball and Softball Federation, and a Moscow University professor. Popov has made several unsuccessful attempts to become a member of the USSR Academy of Sciences. (*Syn Otechestva*, No. 46)

BYELORUS

■ Second-hand clothes which used to be worn by citizens of the USA are being sold in a shop in Minsk. The prices are quite reasonable. There is a proposal to export used clothing from Byelorussia to the USA and sell it there as souvenirs. (*Komsomolskaya Pravda*, 11/30)

■ Deputies representing the National Front of Byelorussia demanded the resignation of the Byelorussian government at a session of the republican Supreme Soviet. They accused the Prime Minister and his team of passivity, incriminating them for the fact that they have not taken any steps to form a national financial and bank system and have failed to organize any preparation for the introduction of a national currency. (*Radio "Echo of Moscow,"* 11/13)

News From The Republics

ARMENIA

■ In early November, Armenia was cut off from gas supplies. The pipeline delivering gas from Russia was blocked in Azerbaidjani territory. As a result of this action, Armenian industry is at a standstill and hospitals, schools and kindergartens receive no heat. There is no gas in apartment houses. The Azerbaidjan side has set the terms for reopening the gas pipeline, the main one of which is the creation of a 10 kilometer wide buffer zone between the two republics controlled by Interior Forces. For Armenia, this would mean another blockade ring and, the main thing, complete isolation from Nagorny Kabarakh, which is quite unacceptable. (*TV News Service, 11/13*)

■ Ever since the establishment of a blockade on November 4th, the Armenian industry has lost over 600 million rubles. Around 85% of the Republic's manufacturing enterprises have stopped operation because of fuel shortages. (*TV Inform, 12/02*)

■ The Armenian delegation made a statement that they are not going to continue negotiating with the Azerbaidjan Republic. When the gas trunk pipeline was cut off on the territory of Azerbaidjan, leaving Armenia without energy, Armenia regarded this hostile action as an attempt to ruin its economy and exert pressure on its people. (*TV Inform, 11/22*)

SOVIET CENTRAL ASIA

KAZAKHSTAN

■ The Kazakh leadership is pursuing negotiations with Chevron Corporation for joint exploitation of oil fields in the Tengiz region. The plan is to begin operations before the end of the year, and a joint venture is being formed, to be named the Tengiz-Chevron Oil Company. Certain details have not yet been worked out concerning exactly how the profits will be divided between the partners, and this matter is delaying the signing of the contract. The Kazakh side apparently does not agree to the terms that Chevron Oil Corporation is offering, but it is hoped that this most important matter will be ironed out in the very near future. (*EXPRESS, a Kazakh Independent Youth Daily, No. 192.*)

■ Kazakhstan has begun to close down uranium mining enterprises located within its territory. The Shagly and Tasbulak mines have stopped operation altogether. At the same time, the Caspian mining and metal smelting plant cut down the output of substances used in the production of fissionable materials. (*TV Inform, 12/2*)

■ A center for refugees and migrants has been formed in the Kazakh capital of Alma-Ata and is the first of its kind in the Soviet Union. Many former Kazakhs and Russians are returning to the republic. The opinion prevails that this is the result of the growing stability in Kazakhstan. Refugees in the new center will be able to go through a course of adaptation to new conditions and to polish up their languages. It is planned to house the center in one of the former luxurious rest homes of the Kazakh Communist Party's Central Committee in the outskirts of Alma-Ata. (*Kazakhstanskaya Pravda No. 237*)

UZBEKISTAN

■ The Uzbek Republic has introduced stringent customs regulations on its borders. Only goods exchanged on a barter basis are allowed to be exported. As people leave Uzbekistan, they can only take with them two kilograms of vegetables and fruit per person. (*Vechernaya Moskva, 11/11*)

KIRGHIZIA

■ Kirghizia's state inspectorate has imposed a freeze on bank deposits of more than 100 small businesses in Bishkek, pending the revision of the tax legislation which has been ordered by President Akayev. (*Kuranty, 12/10*)

MOLDOVA

■ Moldova's ex-Premier Mircha Druk, who leads the Popular Front faction in the republican parliament, has declared that Moldova is going to integrate with Romania next July. He was speaking in Kishinev at a public meeting organized by the December 16th National Alliance. About a thousand people came to the city to celebrate the 73rd anniversary of the "reintegration of all Romanian lands." (*Izvestia, 12/2*)

■ On December 1st, in Kishinev the supporters on the Moldavian Popular Front formed a council for the unification of Moldova and Romania. (*TV Inform, 12/2*)

News from The Republics

THE BALTICS

LITHUANIA

■ The Deputy Director-General of the Lithuanian Statistics Department, P. Adlis, writes that exports remain at the same level: 46% fuel, minerals, iron and steel; 18% products of the chemical industries and fertilizers; 14% industrial raw materials; 10% consumer goods; 5% food products; 2% building materials. A large part of these exports go to Germany (22%), Belgium (20%) and Poland (9%). Imports comprise mainly consumer goods (46%), raw materials for food processing (27%), food products (6%), machinery, equipment and transport means (7%). Of this, 15% comes from the United States, 12% from France and 10% each from India, Poland and Germany. So far exports to Latvia comprise only 7% and to Estonia 3%, and imports from these republics are around 4%. (*Lietuvos Rytas*, a Lithuanian weekly No. 41)

■ Prime Minister of Lithuania Vagnoris is not in any hurry to introduce the Lithuanian national currency. He plans first to discuss the situation and

sign a corresponding agreement with the USSR on currency policy. (*Kuranty*, 11/15)

■ The Law Department of the Lithuanian Foreign Ministry confirmed the fact that famous ballerina Maya Plisetskaya and her husband, composer Rodion Shedrin, received Lithuanian citizenship. Plisetskaya's mother was born in Lithuania. The famous family has built a beautiful villa in Trakai and Maya keeps saying that "she is charmed by the way of life in Lithuania and hopes that she will soon forget about the disgusting life in Moscow." (*Trud*, 11/22)

LATVIA

■ The mother of a young girl, a Riga resident, who was killed in a road accident was shocked to find in the morgue that her daughter's head and body were all crisscrossed with scars. The woman thought there could not be so many, considering the way the girl had died. Research which was done later by a Zemlya newspaper reporter revealed that

the brain and some bones of the deceased had been taken away as "biological materials" used for the preparation of some medicine. It turns out that operations of this sort have been sanctioned by the Health Ministry of the Latvian Republic. It was further discovered that these "biological materials" are also exported to the West, specifically Germany, for hard currency. (*Izvestia*, 12/2)

■ The Vice President of the Latvian Bank, Alfred Bergmanis, refuted information that Latvia had put into circulation a limited amount of the new currency, Lats. According to Latvian officials, the new currency will be introduced in the republic no earlier than September 1992. (*Radio "Echo of Moscow"*, 12/5)

"SIBERIA"

■ The Kuzbass coal mines have refused to supply coking coal to the Ukraine. Two reasons are cited for this decision. First, the Ukraine owes the coal miners some 11,000 tons of sugar. Second, while buying coal cheap,

(Continued on Page 5)

News in Brief. . . News in Brief. . . News in Brief

■ A series of public opinion polls, conducted recently, show that only such political figures as Yeltsin, Burbulis and Khasbulatov get positive assessment from the Soviet people. The rating of Gorbachev, Rutskoy and Sobchak is mostly negative. (*TV Inform*, 12/19)

■ The USSR State Statistical Committee announced that there are currently 2 million unemployed in the Soviet Union. About 80% of them live in Russia. Four hundred and nine thousand out of a million jobless people manage to find jobs through the unemployment centers. Six thousand people receive unemployment benefits.

which amount to 75% of their salaries at their last place of work. (*Trud*, 11/14)

■ The number of crimes committed against foreign citizens in our country has gone up in comparison with last year by 21% (not more than a third of them were solved) according to the information given at the USSR Interior Ministry briefing. Guests of our country are usually robbed of money, clothes, VCR's and cameras. About half of the crimes are committed in hotels, hostels, camping sites and so on. (*Komsomolskaya Pravda*, 11/13)

■ The Deputy Minister of Railroads

declared that as of January 1 all Soviet Citizens travelling abroad by rail will have to buy tickets for hard currency. (*Kuranty*, 11/19)

■ Losses caused by the conversion of the military industry have totalled 3.3 billion rubles for the converted enterprises. The losses were supposed to be replenished from the so-called Stabilization Fund. However, the Fund has ceased to exist. (*St. Petersburg TV Program*, "600 Seconds," 11/20)

■ According to statistics every third patient in the Soviet Union is not operated

News from The Republics

Ukrainian representatives offer sugar at commercial prices. The miners' proposal to conduct trade at world prices has been left unheeded. (*Radio "Echo of Moscow," 11/12*)

■ Authorities of the Chita region in Siberia are going to sabotage all the decrees of the Russian President. Eighteen leaders at various levels met in Chita and formed a committee which proclaimed the protection of the interests of the Siberian population to be their top priority. They will insist on the formation of the Far Eastern republic, which would be independent of the Russian "center" in its social policy. (*Izvestiya, 11/21*)

■ Yakutiya does not plan to secede from the RSFSR yet. Its Presidential election will take place on December 20th. There are four candidates for this post, among them three Yakuts and one Evenk. The Russian people, who make up more than half of the republican population, have not nominated their own candidate so far. (*Kuranty, 11/21*)

■ On November 19th, the parliament of the Chechen Republic adopted a special statement containing its assessment of Yeltsin's decision to impose a state of emergency in the republic. The statement says that the Russian leadership seeks to destabilize the situation not only in Chechnia, but in the whole of the

Caucasus. (*Radio "Echo of Moscow," 11/19*)

■ Chechen President Jokhar Dudaev today assumed full control of the republic following the former Prime Minister's resignation.

Feature Articles

(Continued From Page 1)

and the tasks of overcoming the present crisis, the preservation of its statehood and the continuation of democratic reforms." The president does not exclude the possibility of a national referendum on this question.

On December 10, the Soviet president's press secretary, Andrei Grachev, rejected as unfounded rumors of Mikhail Gorbachev's possible resignation.

With regard to the new political role of Mikhail Gorbachev, Lithuanian leader Vitautas Landsbergis does not rule out the possibility of attempts to regain his former authority, which may take the form of a coup.

On the same day, Ukrainian President Kravchuk pointed out that the

Commonwealth is in full accord with international law and the Ukraine's declaration of independence. Asked who could join the new commonwealth of nations, Kravchuk first named Kazakhstan and then the Baltic states. He did not exclude Bulgaria and any other European countries, saying that "whoever decides to join us will not regret it."

Armenia was the first to express support for the new commonwealth. President Ter Petrosian has stated that Armenia is ready to seriously consider joining.

Russia's senior Vice Premier, Gennady Burbulis, stated that the signing of the accord between Russia, the Ukraine and Byelarus does not mean the

(Continued on Page 6)

News in Brief . . . News in Brief . . . News in Brief

on although he needs an operation. This is due to the lack of drugs, equipment and highly skilled doctors. (*Vesti, 11/27*)

■ The humanitarian aid sent to the Soviet Union is not successfully distributed among the poor. Items are often given to two people to be shared. Very often the two people are absolute strangers. (*St. Petersburg TV Program "600 Seconds," 11/27*)

■ The magazine "Stolitsa" published information from an ex-employee of the KGB saying that the All-Russian Stock Exchange Center (ARSEC) and its affilia-

tions are headed by ex-KGB officers. According to this information, Vice President of ARSEC, Boldyrev, and Head of the Financial Department, Chukhlantsev, were senior officers of the KGB. The ex-KGB man claims that the Stock Exchange Centre was created to launder the money which belongs to the military industrial complex, the KGB and most probably to the CPSU. (*Vesti, 11/14*)

■ A new privatization concept has been developed in Moscow by a group led by Larisa Piyasheva, Deputy Director General of the Moscow mayor's office. Under it, trade, catering and service businesses are

to be turned over to private owners without delay. The workers of these enterprises are to collectively send an application to the privatization center and pay a percentage of the asking price. If they fail to meet the deadline, their enterprises will be auctioned to other buyers, including foreigners. (*TV News Service, 11/18*)

■ Although the USSR State Bank continually prints money to cover the expenses of the Finance Ministry to cover the budget deficit, there is money in the country: enterprises and organizations have as much as 172 billion rubles in their accounts. Individuals have accumulated nearly 564

Feature Articles

(Continued from Page 5)

immediate death of the USSR. He added that the USSR will cease to exist in the course of the establishment of new statehood. According to Durbulis and other Russian officials, the document must in no way be interpreted as a Slavonic accord. It is open for all sovereign states. Foreign Minister Andrei Kozyrev, and State Counsellor Sergei Shakhrai rejected the idea that the agreement removes Gorbachev from politics. The Foreign Minister describes the accord as the last chance to avoid the repeat of the Yugoslav scenario on the territory of this country.

According to Nursultan Nazarbayev, Kazakhstan's President, a union of Central Asian republics which he planned to form to counterbalance the newly born Slavic commonwealth of three independent states will not be created.

After parliaments of all the three member countries ratified the Treaty on Commonwealth, they recalled their representatives from the USSR Supreme Soviet.

Nevertheless, a session of the USSR Parliament took place on December 12. Probably it was the USSR People's Deputies who were the most indignant over the creation of the new Commonwealth. The chairman of the

federal parliament, Konstantin Lubchenko, contended that the document is contrary to the laws of the USSR and anti-government. Among the dangerous consequences of the Minsk treaty he named the loss of control over the nuclear potential of the country, the danger of an even worse economic and political crisis, the "pushing" of the "Moslem" republics into the embrace of the Islamic world, which is itself on the brink of creating its own nuclear weapons. Deputies demanded to convene an extraordinary session of the USSR People's Deputies "in order to restore the Constitutional order on the territory of the USSR." This decision was supported by President Gorbachev.

Gorbachev did not speak at the session of the USSR Parliament as had been expected. There was unofficial information that he decided not to influence the opinions of the deputies in any way and to give them a chance to determine their own attitude to the treaty. But later the USSR President made a statement to TASS: "Such decisions in the present difficult economic and political situation in the country do not work for the stabilization of society. At present, when the fate of the country is at stake, everything should be done to make the decisions on this matter well-bal-

anced, mature and unmistakable. And this can be done only on the basis of a Constitutional and normal democratic process. There should be no rash decisions. Because they can be the cause of fatal consequences for our people. I call upon the Parliaments of Byelorussia and the Russia once again to reconsider their decision to recall their deputies from the session of the USSR Parliament." He believes that it is necessary to declare the transfer of power to a new political structure, to the Commonwealth of Independent States, in a civilized way at the last session of the USSR Parliament.

A statement by the political board of the Civil Reconciliation described the creation of the Commonwealth as "an act of arbitrary rule which will result in disagreements." The Civil Reconciliation group incorporates many parties and movements, including the Liberal Democratic Party, the Vseslavyanski Sobor (*All-Slavic Assembly*), the Marxist Platform of the CPSU and the Monarchy Party. According to G. Gusev, the secretary of the political board of this amalgamation, the group calculates that its statement will be supported by the broad masses.

On December 12, a meeting of the Presidents of the "Moslem" republics took place in Ashkhabad. The President

(Continued on Page 7)

News in Brief. . . News in Brief. . . News in Brief

billion rubles in their savings bank accounts. The economy is in a free fall, and one of the reasons is the policy of the State Bank to charge an exceedingly high interest rate making it unprofitable for the enterprises to ask for loans. Since January 1991 the demand for bank credits has dropped by 25 billion rubles. Enterprises now try to stick exclusively to barter deals to avoid the high interest rates (*Narodny Deputat*, No. 14)

■ Free economic zones are currently being set up in 13 regions of Russia. Some are: the Moscow, St. Petersburg, Novgorod, Kaliningrad, Zelenograd, Buryat, Chita, Taimyr, Tomsk and Nakhodka zones and

that of the Jewish autonomous region. According to the Russian State Committee on Statistics, the total area of the 13 Russian free zones is 1.3 million sq. km. Their total population is about 18 million people, or 12% of the population of Russia. (*Ekonomika i Zhizn*, No. 48)

■ A Siberian chemical plant has earned its first million US dollars by selling 10 kilograms of processed uranium to Canada. Impressed by the high quality of the product, the Canadians have expressed an interest in continued cooperation and signed a new \$1,000,000 contract. A similar project, this time for \$6,000,000, is be-

ing considered by Americans. (*Trud*, 12/13)

■ In early December, the Vneshekonombank resumed operations selling hard currency to Soviet citizens. The bank will buy US dollars for 90 rubles and sell them at a rate which is 10% higher. At the same time, the Moscow Business Bank started buying US dollars for 117 rubles and selling them for 130 rubles, thus undermining the activity of the Vneshekonombank. (*reported by Natasha Lozitskaya, WPS*)

■ Apple Computer has signed an agreement with the Soviet-American joint venture, ParaGraph, to purchase technol-

Feature Articles

(Continued From Page 6)

of Uzbekistan, Karimov, expressed his views on the problem: "On all the questions which we had for the leaders of the three Slavic republics we have received satisfactory answers. We still have to determine our attitude to the Commonwealth but I can tell you that we treat it with understanding and do not exclude the possibility that our republic may join it in the future."

The recent congress of the Democratic Reform Movement supported the idea of a commonwealth of independent states, expressing the hope that the new association will follow the road of democracy and respect for human rights. The congress represented over 30 political parties and 70 public movements, all former union republics and 15 autonomous republics. It elected seven co-chairmen of the Democratic Reform Movement: Alexander Yakovlev, Eduard Shevardnadze, Stanislav Shatalin, Arkady Volsky, Gavril Popov, Anatoly Sobchak and Viacheslav Shestakovsky.

On December 17, Presidents Gorbachev and Yeltsin met in the Kremlin to discuss the results of their talks with the US Secretary of State Baker and questions related to the commonwealth. They agreed that before the end of the year all structures of the

former Soviet Union should be either closed down or transferred to Russia's jurisdiction. (Compiled from reports by Soviet media)

CENTRAL ASIA, KAZAKHSTAN REACT TO YELTSIN'S COMMONWEALTH

On the night of December 13th, a joint statement of the leaders of Central Asia and Kazakhstan, N. Nazarbayev, I. Karimov, S. Niyazov, A. Akayev and R. Nabiyeu, was signed in Ashkhabad.

The document runs: "We perceive the Commonwealth of Independent States with understanding. There is no other way out, because democratization is in a deadlock, and the shortsighted policy pursued by the Center has resulted in the breakup of everything which could be broken up..."

A. Akayev made this statement later: "Gorbachev's mistake was that he has always wanted to see a Union state, but not a union of states."

The republics of Central Asia and Kazakhstan are ready to join the Commonwealth. However, only under the following condition: they must be co-initiators enjoying equal rights with the initial contracting parties. While the

Brest agreement must be revised taking into consideration another five republics with their social and economic peculiarities.

It seems that, choosing between Yeltsin and Gorbachev, the central asian presidents have preferred Yeltsin. They have preliminarily coordinated all the points of their statement with the Russian President over the phone, but none of the five has phoned Gorbachev. Moreover, Nazarbayev, while speaking about the lack of confrontation among his colleagues, said that it's time Gorbachev stopped shouting about the coming war and blood. In Nazarbayev's opinion, the new Commonwealth will not lead to it in any case. (Komsomolskaya Pravda, 12/14)

News in Brief. . . News in Brief. . . News in Brief

ogy used for scanning handwritten text. According to William Pirlman, leader of ParaGraph, "our Soviet partners managed to accomplish what Americans have been trying to do for 20 years." (*Business and Banks*, No. 44)

■ According to Norwegian businessman, Oivin Otesstad, recently appointed as an advisor to the Russian government, Russia has signed two contracts with foreign companies to research Russian consumer and banking services, including automating 40,000 Russian savings banks. It is planned to introduce VISA cards as well. It is still unclear who will finance both

projects. (*ibid*)

■ For the first time in Russian history, the Moscow commercial Inkombank is issuing hard currency deposit certificates for legal entities and individuals, including foreigners. They will be sold as of January 1, 1992. Certificates' nominal value is 1, 10 and 50 thousand dollars, as well as 1, 10 and 50 thousand German marks. The total sum of certificates will be 10 million dollars and 10 million marks. According to the bank employees, large foreign trade amalgamations, joint ventures, and a number of individuals have already placed their orders for the purchase of certificates.

Experts stress that because hard currency payments through both state and commercial banks are usually being delayed, certificates may become a universal means of payment between enterprises. Besides, if the RSFSR Supreme Soviet adopts the Decree on Liberalization of Foreign Economic Activity on the Territory of the RSFSR proposed by Yeltsin and prohibiting hard currency payments on the territory of Russia, these certificates will present a chance to ignore this prohibition. (*Kommersant* No. 45)

Feature Articles

BORIS YELTSIN: "IT IS DIFFICULT, BUT WE SHALL SURVIVE"

His comments on the Formation of the Commonwealth.

"I am convinced that the most important condition for providing stability is maintaining links between the republics. I think that during the recent months (and especially days) the Union was at the edge of an abyss which we managed to avert having concluded the Commonwealth Agreement..."

"I have already said several times that the Ukraine's nonparticipation in discussing the new Union Treaty put Russia in a position where it could not continue discussions because we did not imagine a Union without the Ukraine. This is for several reasons: First, it has a population of over 52 million people; second, 11 million of them are Russians; third, we are linked by a thousand-year-old joint history and thousands of modern economic, political and social links. The all-national referendum in the Ukraine has demonstrated that the Ukrainian people do not want to be part of any union at all. While the Novo-Ogaryovo treaty implied a state (though a confederative one) consisting of sovereign republics, it became clear that if Russia signed the treaty in Novo-Ogaryovo, its road with that of the Ukraine would diverge. We could not afford it, and that is why we started to search for a way out... A new approach to joining forces..."

"In addition, the republics saw that while verbally the Center favored the independence of the republics, in fact it continually sought to preserve the status-quo... Then everyone understood that the so-called 'radical' Novo-Ogaryovo reforms were nothing more than just another attempt by the Center to continue its same influence, but under a different shape. When this became clear, the breakup and separation of the republics began in earnest."

"Our way to fight back was to start a contra-movement, but with such separatist forces driving us apart, how?

Our one way out was to become united, not within the framework of one state, but within the framework of a commonwealth of states, similar to what the European states are doing now. That was how the idea of a Commonwealth of Independent States was born. I would like to emphasize that it seems to me that we have found an optimal pattern. It allows us to:

- preserve existing borders without remapping and dividing the republics;

- preserve the common economic system and the unified ruble system;

- pursue a coordinated pricing policy and continue further with reform strategies;

- prevent disintegration of the Army into separate republican segments, thus preserving a unified command of Air Defense Troops, Air Forces, and strategic, tactical and nuclear weapons..."

"Regarding the fact that we did not initially invite President Nazarbayev to Minsk, we at first had to find out the Ukraine's position. When we managed to agree with the Ukraine and closely approached signing the agreement, I called Nazarbayev and told him about everything. He was ready to fly to Byelorussia immediately, but it turned out that a day later he was to be inaugurated as president and immediately after that he had a meeting with Gorbachev on the schedule. He could cancel neither of these occasions. However, when President Nazarbayev got acquainted with the final document on Commonwealth, he said that in all practicality he agreed with everything..."

"I can positively tell you that we shall speak about Kazakhstan's joining the Commonwealth. Maybe, some amendments will be made. In addition, Armenia and Kirgizia have already announced their readiness to join the Commonwealth."

Member-countries have also unanimously confirmed the common

opinion that a unified command over the common military strategic system is a must. This requirement concerns nuclear weapons as well."

"I have met with Gorbachev several times since I returned from Minsk. The conversation was polite and gentle, although its very structure reminded me of a talk between a plaintiff and a defendant (my part being that of a defendant, of course). Later, however, he changed his tone." (*Trud*, 12/14)

NEW BANK REGISTERED IN RUSSIA

In late November, a first officially registered bank, named "Help," has been formed with the help of private investments. Thus, the Russian Central bank has officially recognized the possibility of appearance of private banks. Rolan Bykov, a famous Soviet actor and businessman, has been nominated its chair. Besides him, 18 other Soviet millionaires made their investments of 100,000 rubles each. The bank primarily intends to provide credits for small and medium-sized businesses. In the course of three or four months the bank plans to set up a chain of hard currency exchange offices. It will also provide individuals with safes for storing valuables, whose leasing cost will be approximately 10,000 rubles a year.

The bank is open for new investors, provided they are millionaires who have proven their competency in commercial and legal entities, both Soviet and foreign. By now, an Israeli, a Japanese and a German bank have applied for membership. The bank's phone numbers are (095) 253-5055 and (095) 253-8602. (*Kommersant*, No.45)

SOVIET TRADE 101

BY CAROL VIPPERMAN

Green salad. Oh how I longed for green salad during my recent trips to the Soviet Union.

Westerners face many hardships in pursuing opportunities in the Soviet Union; the lack of Western foods is only

one of them. There's the grueling travel, the differences in living standards (hotel, food, service), communication problems, and the totally foreign business cultures and work ethics. Each of these alone is reason enough to think twice about doing

business in the USSR.

There are ways to escape the personal hardships — you can stay in \$400-a-night Westernized hotels like the Savoy and experience what *U.S. News & World Report* calls "Moscow on \$1,370 a Day." Better for doing business is to rough it a bit by living with families or staying at an assortment of hotels and dormitories to learn more about the real life of the Soviets and to be accessible to Soviet entrepreneurs.

As president of the Foundation for Soviet American Economic Cooperation since 1989, I have traveled extensively in the Soviet Union to explore potential opportunities and contacts for Northwest businesses. I have had many opportunities to learn about Soviet life and to make business contacts.

It hasn't always been easy. Misunderstandings can crop up in the most innocent situations. For example, I quickly found that for many Soviet business leaders, the concept of a "non-profit" organization is foreign.

But in the USSR, even a non-profit representative like me gets bombarded by budding Soviet entrepreneurs with joint venture opportunities at all times of day and night. It has been difficult to separate the dreams from real opportunities.

And entrepreneurial spirit remains strong in the USSR today, even under the strain of recent political and economic problems. On a recent visit to the USSR, I lead a group from the Soviet Far East to Moscow to explore business opportunities and conduct workshops on Western business techniques. The Soviets seemed even more interested in Western business techniques now than during earlier visits.

Indeed, there are many challenges for Northwesterners establishing businesses in the USSR however. Here are some of the most common obstacles:

1. Knowing who to do business with is one of the greatest challenges facing a Westerner. Dun and Bradstreet and bank reports are not available in the USSR. The best alternative may be to meet with many of the entrepreneurs who present themselves with proposals.

It is getting a little easier as more



\$85.00
U.S.
per room/
per night

If you live in Washington or Oregon, you can experience the Chateau Whistler Resort for a very small price. Just \$85 U.S. per room per night. You'll be in the middle of some of the best vacation territory anywhere. Golfing, Cycling, Mountain biking, Glacier skiing, Tennis, Canoeing, Windsurfing, Trail-walking. Call us direct at 1-938-8000 or toll-free 1-800-828-7447. Our specialty is you!

We treat people who live in the Pacific Northwest
extra special.

Canadian Pacific  Hotels & Resorts

Chateau Whistler Resort

Just a few of the activities you can enjoy in and around Chateau Whistler Resort:

- \$85 U.S. per room / per night
- Adventure Desk
- In lobby
- Indoor/outdoor pool
- State-of-the-art health club
- Massage therapy
- Tennis centre with resident pro
- Tennis Tigers children's program
- Bicycle trails
- Mountain bike rentals (in-house)
- Bicycle storage also available
- Two restaurants including kids' menus
- Fabulous shopping

Offer available March 27 - October 31, 1991. Taxes extra. Limited room availability based on moderate accommodations.



INTERNATIONAL TRADE

Soviet entrepreneurs recognize the importance of translating their proposals into English. Also, new associations, foreign trading organizations, and Western consulting firms are emerging as trade resources.

2. Knowing who has the authority to make decisions is also a constant dilemma facing businesses, particularly those who are interested in exporting natural resources. Often the republic says they have the power to make the decision, but ultimately the central government needs to approve the contract. In addition, the more recent political difficulties and changes in laws and regulations continue to make co-production or joint ventures difficult.

3. The red tape frustrations are endless. The changing and sometimes conflicting regulations imposed by either the central republic, city, or local regional governments are often overwhelming. Converting rubles into other currencies or exportable items continues to be difficult. The need to train, reinforce and find ways to reward the work force so that they will deliver the needed level of production can tax the most patient person.

4. Financing is and will continue to be problematic for Westerners. Currently, there are not many financing resources available through U.S. banks or the government, which gives an unfair advantage, some entrepreneurs state, to Europeans and Asians who receive government assistance for their exports to the Soviet Union.

Some recent developments in the Soviet Union are encouraging, however, especially one decision which potentially allows foreign companies full ownership of their ventures, thus protecting their investments. In addition, President Bush's six-month waiver of the Jackson-Vanick act — which restricts U.S.-Soviet trade until the USSR establishes an emigre policy — will hopefully pave the way for MFN status for the Soviet Union.

Why pursue this market? The Foundation asked this question in a 1990 survey of Northwest business persons working

with the USSR. One respondent summed it up by pointing to the "great potential of the vast, untapped Soviet consumer market and the incredible mineral resources of the Soviet Union, which have either been mismanaged or completely unmanaged."

The USSR is not for the faint hearted. Even though some positive moves are being taken to facilitate trade, only those U.S. entrepreneurs who are willing to be patient, long-term oriented, and creative about getting their money out will be

rewarded. However, those companies and individuals who make and nurture business relationships now will be best poised to reap the rewards financially and personally. ■

Carol Vipperman is president of the Foundation for Soviet/American Economic Cooperation, a non-profit, membership organization that fosters business and trade between the Soviet Union and the Northwest.



One picture is worth \$265,500.

That's what college plus a medical degree could cost by the year 2000.

Good reason to start talking now to a CLU (Chartered Life Underwriter) or a ChFC (Chartered Financial Consultant).

The initials "CLU" or "ChFC" beside your financial

advisor's name mean you've found a financial professional to help you achieve goals and avoid pitfalls.

And in a few years, with any luck, you'll have a professional or two of your own in the family. Your son, the doctor. And perhaps your daughter, the lawyer.



Put a CLU or a ChFC
into your
planning picture.



American
Society
of CLU & ChFC

BREAKING TRAIL

Foundation works toward matches for Soviet trade

Kennewick potato farmer John Peterson had been trying for four years to find out if the Soviet Union might be interested in setting up a farm there, American-style. "My letters and phone calls to American and Soviet officials went unanswered or only elicited the most superficial responses," Peterson explains. Then he found out about the Foundation for Soviet/American Economic Cooperation. Eight months later he's close to signing a lease agreement for 400 acres in Tashkent. What's more, negotiations with McDonald's to supply the Moscow fast-food purveyor with potatoes are nearing completion.

In arranging such cooperative ventures, contacts can mean the difference between success and failure. More and more the person to know when considering U.S.-Soviet projects is Carol Vipperman, the energy source behind the recently formed Foundation for Soviet/American Economic Cooperation.

VIPPERMAN'S non-profit organization and its 18-member policy-setting board of trustees provide information to business and government agencies in both America and the Soviet Union. The foundation makes introductions and helps smooth the way to a productive relationship. It's a membership-based organization with a roster of more than 50 Northwest businesses. The majority of the businesses are small enterprises.

Linking American surplus to Soviet need is more than a simple exercise in supply-side economics. Obstacles are numerous, not the least of which are obsolete trade regulations. But despite obvious

political, cultural and economic differences, there are important similarities between the Pacific Northwest and the Soviet Far East, Vipperman explains. For example, the Soviet Far East is geographically closer to the Pacific Northwest than to anywhere else in the U.S. And both the Pacific Northwest and the Soviet Far East are rich in natural resources. But America also has a valuable commodity the Soviets lack: technology.

THE OBSTACLES to making matches among common interests are finally beginning to look less forbidding, Vipperman says. "The issue of doing business with the Soviets is really a matter of trade regulations. We now have the opportunity to influence trade policy, which is crucial to exploring Soviet markets."

Vipperman will be in the thick of it. She's well-known in regional and state governmental circles for her energy and leadership. In addition to managing her own marketing business for the past 13 years, she is serving on the Washington State Efficiency and Accountability Commission and the state tourism commission, and has chaired the Governor's Small Business Improvement Council.

"Carol's very committed and very honest," says Steve Odom, program manager for the Washington State Department of Trade and Economic Development. "Her organizational ability, her standing in the business community and the focus she brings to the foundation have been valuable assets to those seeking trade with the Soviets."

The impetus for forming the foundation was a citizen-diplomatic mission to Mos-

cow and Leningrad in May 1989. Viperman was one of the only visitors knowledgeable about pre- and post-revolution Soviet culture and able to communicate in Russian. The trip was moving and exhausting. "At one point" she says, "we were listening to children sing an American song and my host

raised nearly \$40,000 from corporate and individual sponsors. The foundation's goal for funding is \$150,000.

Viperman's success with the foundation can be attributed to commitment, hard-headed business acumen and an eye for more than bottom-

Viperman explains the complexities of cooperation.



leaned over and said, 'This is what keeps me going, knowing there are children here and in the U.S. who will have a different kind of world.' I know that's emotional, but it really affected me."

Back in Seattle, Viperman

line results. "I feel strongly that, aside from making sound business sense, this has real meaning," she says. "We're not only learning a lot about each other, we're helping to bring two worlds closer together." —Loryn Paxton

JAPAN'S LAZY 8

Consensus management finding a home on the range

Montana's Lazy 8 ranch may have its barbed wire fences, its bunkhouses and its horse troughs, but it's not your typical spread. There's a Japanese garden, raked daily, just outside the ranch house and, inside, rows of slippers and bottles of sake—and cold Coors—await visitors. Consensus management has replaced the traditional chain of command, in which orders traveled straight from ranch house to bunkhouse. Here, cowboys meet with their bosses in a barn each week to discuss goals and fundamental principles.

This novel arrangement has left some farmhands feeling a little fenced in. About half of them have departed for greener pastures since Zenchiku Ltd., one of Japan's largest beef distributors, purchased the Lazy 8, a 77,000-acre spread near Dillon, in southwestern Montana, two years ago.

On the other hand, the ranch has become a popular destination among Japanese. One or two Japanese management trainees are always on hand, working side by side with the farmhands and ranch executives. "You can't learn much from looking out a window," says president John Morse, who also shows trainees the business side. He's entertained more than 250 Japanese businesspeople here. They drop by on their way to Las Vegas or other travel

In a world filled with cookie cutter hotels, this breaks the mold.



For about the same price as a cramped hotel room, you can live it up in one of our suites.

Located directly across the street from the Convention Center in downtown Seattle, every suite features a fully equipped kitchen. Many include a fireplace with a comfortable recliner just a few feet away. And when it's time to revitalize, there's a weight room and jacuzzi at your disposal.

Whether you're staying for a night or for a month, check into a place that gives you more than just a room with four walls.

For information or reservations, please call

us toll-free at 1-800-426-0676. As always, we look forward to your stay.

WestCoast Plaza Park Suites

Downtown Seattle's only suite hotel.

1011 Pike Street, Seattle, WA (206) 682-8282

Earn 500 miles per stay towards Alaska Airlines Mileage Plan.



"The U.S., in particular, has an important role to play in encouraging business growth and change within the USSR," says Carol Vipperman. "There is a timeliness and urgency to build economic and business bridges now."

THERE'S MORE TO GOODWILL GAMES THAN GAMES

This month *Washington CEO* celebrates the 1990 Goodwill Games with a special report on the people behind the Games and the significant events taking place in conjunction with this unique athletic and cultural extravaganza.

As Bob Walsh, president of the Seattle Organizing Committee, says in our CEO Closeup story beginning on page 16, "It's the largest international event that will take place in North America in the next decade."

While the Games promise to pump hundreds of millions of dollars into Washington's economy and give the state an untold level of worldwide media exposure, there are other more intrinsic forces at play here that deserve equal attention. Indeed, the Games will unite athletes, artists and influential citizens from 50 countries — including the Soviet Union — at a time when the global cry for freedom has practically thawed the Cold War and shredded the Iron Curtain.

Perhaps the best thing to come out of the Games will be the comradery and good tidings that occur during the two-week event as Soviet visitors, and those from other countries, share our homes, eat our food, take in our sites and enjoy our hospitality. There's no doubt the Games can, and will, have a significant impact on improving relations between the United States and the Soviet Union. Washington state is positioned to play a major role in this process.

Already, Mikhail Gorbachev's glasnost or openness policy has allowed cultural exchanges between the two countries that were unheard of as recently as 1986 when Ted Turner's original Goodwill Games were held in Moscow.

Now business groups all over the country, including many in Washington state, are setting their sights on the Soviet Union as that nation slowly shifts from a production economy to a market economy.

"The U.S., in particular, has an important role to play in encouraging business growth and change within the U.S.S.R.," says Carol Vipperman, executive director of the Foundation for Soviet American Economic Cooperation based in Seattle. "There is a timeliness and urgency to build economic and business bridges now."

The nonprofit corporation, originally known as the Foundation For U.S./U.S.S.R. Cooperation ("We changed the name 'cause the latter was a mouthful," says Vipperman) started last June following a small-business education mission to the Soviet Union led by Vipperman and a group of other consultants. "We put on seminars and explored other ways to help them," says Vipperman. "We saw this as a real important window of opportunity, but felt we needed to do something long term." Thus the Foundation was born.

The Foundation, says Vipperman, exists to foster business activities between firms in the United States as well as Soviet Cooperatives and State Enterprises. It provides the following:

- Advocacy for increasing the awareness of economic possibilities and the removal of trade impediments and legislative restrictions between the U.S. and U.S.S.R.;
- Policy development in formulating new directions and providing new trade opportunities; and,

- Economic development by increasing specific business and trade ventures.

A particular focus of the Foundation, Vipperman says, is increasing economic development in the Pacific Rim area by uniting the Soviet Far East with the Western U.S.

"It clearly needs to be an organization that's advocating trade with the Soviets and is used as resource," says Vipperman, who is one of the Foundation's 15 volunteer board members. "It's one place where people can go to get started." The Foundation, which has received financial support from U.S. West Communications Inc. and Alaska Airlines Group, is already getting phone inquiries from California and other states. One caller wanted to raise Arabian horses in the Soviet Union, but she didn't know where to turn, recalls Vipperman. "We connected her with a man who's putting together a joint venture to build a racetrack in Leningrad. She was ecstatic."

Among its other services, the Foundation provides a common thread for individuals and groups to participate in economic development opportunities. In each of the organization's three specialty areas — advocacy, policy development and economic development — it offers the following services:

- Access to a data bank of Soviet/American companies for possible business partnering;
- A referral system of names of traders, buyers, government agencies and others who can assist businesses;
- Working cooperatively with individual businesses and government agencies to foster new policy directions;
- Research and analysis of current and proposed trade policies and providing information on Soviet policies;
- Seminars, training programs, educational courses and business development seminars in both the U.S. and U.S.S.R. in order to spread knowledge of natural business practices;
- Promote and inform the business communities in both countries of opportunities through co-sponsored public seminars, forums, lectures and other relevant informational activities;
- Provide publications on the "how-to's" of doing business in each country as well as broader policy questions;

"We want to make a contribution," says Vipperman. They already have. For more information on the Foundation call (206) 443-1935.

Kevin Dwyer

Managing Editor



ФСН-А.ІЯСКН



Foundation for Social Innovations-Alaska

*"...and now Alaska and the Soviet Far East
have additional opportunities to develop ties."*

*Gennady Gerasimov
chief spokesperson
Minister of Foreign Affairs, USSR*

Foundation for Social Innovations Alaska
JoAnn Zentner, Executive Director
119 Seward Street, Suite 3
Juneau, Alaska 99801
Tel: 907-463-5586
FAX: 907-463-5334
Electronic mail: igc:jzentner

Foundation for Social Innovations Alaska
Vladivostok Office
Mr. Sergey Frolov, FSIA Soviet Far East Rep.
Mr. Sergey Kirillov, FSIA Vladivostok Rep.
Leninskaya Street, 47, 5th Floor
Vladivostok, USSR, 690091
Tel: 25-39-23
Telex 871213229

FSI-ALASKA

ФСН-АЛЯСКИ

A non-profit organization dedicated to providing assistance to pioneering ventures of cultural exchange, commerce and citizen diplomacy between the U.S. and the U.S.S.R., with an emphasis on exchanges between Alaska and the Soviet Far East.

The Foundation for Social Innovations-Alaska (FSI-Alaska) is an independent U.S. affiliate of the Foundation for Social Innovations (FSI-U.S.S.R.), a non-profit foundation based in Moscow.

FSI-U.S.S.R. was founded by Gennady Alferenko, a Soviet citizen, to facilitate grass-roots social initiatives in the U.S.S.R., including international cooperation. In 1988, with the backing of 24 Soviet news agencies, FSI-U.S.S.R. became the first private non-profit foundation ever established in the Soviet Union. Soviet citizens have since proposed thousands of projects to the foundation and have contributed millions of rubles to fund the best ideas.

During a trip to Alaska in February of 1989, Mr. Alferenko determined that the dynamic conditions existing between Alaska and the Soviet Far East called for the creation of an affiliate organization, and FSI-Alaska (originally called the Alaska-Siberia Project) was founded in Juneau, Alaska's capital.

Pioneers of U.S./U.S.S.R. exchange face major barriers

Citizen diplomacy efforts across the Alaska/Soviet Far East frontier in the 1980's presaged the thawing of the Cold War. When the borders that had been sealed for 40 years began to open, excitement was high on both sides of the frontier. This was especially so among Eskimos with family ties on both sides of the Bering Strait. Numerous plans were made for visits and cooperative endeavors.

Despite the political thaw, however, many formidable obstacles remained to frustrate or block such exchanges.

- The Soviet Far East is still officially closed to foreigners, and entry is possible only with special invitations ap-

"Your task is a challenging one: navigating the rough seas of government bureaucracies is every bit as difficult as the barriers faced by the explorers and adventurers who preceded you. I am confident that together, we will meet that challenge."

*Alaska Governor Steve Cowper
in a letter to Gennady Alferenko,
founder of FSI-U.S.S.R.,
March 1989*



Governor Steve Cowper of Alaska signs a legislative proclamation endorsing an FSI-Alaska project, April 1989.

"We appreciate the importance of building bridges of understanding between our two countries at all levels and in every sector of our respective societies. In that respect we view the foundation as one of the major engineers in this endeavor."

*Juneau, Alaska Mayor
Bruce Botelho*

proved by Moscow and with permissions from regional Soviet authorities.

- The infrastructure of the Soviet Far East is designed to serve socialized enterprises and is not normally available to visitors.
- The inconvertibility of the Soviet ruble hinders trade and travel; the absence of scheduled air traffic between western North America and the Soviet Far East also limits contacts.
- Although Alaska and the Soviet Union are separated by a mere two miles at their closest point, international mail must travel around the world.

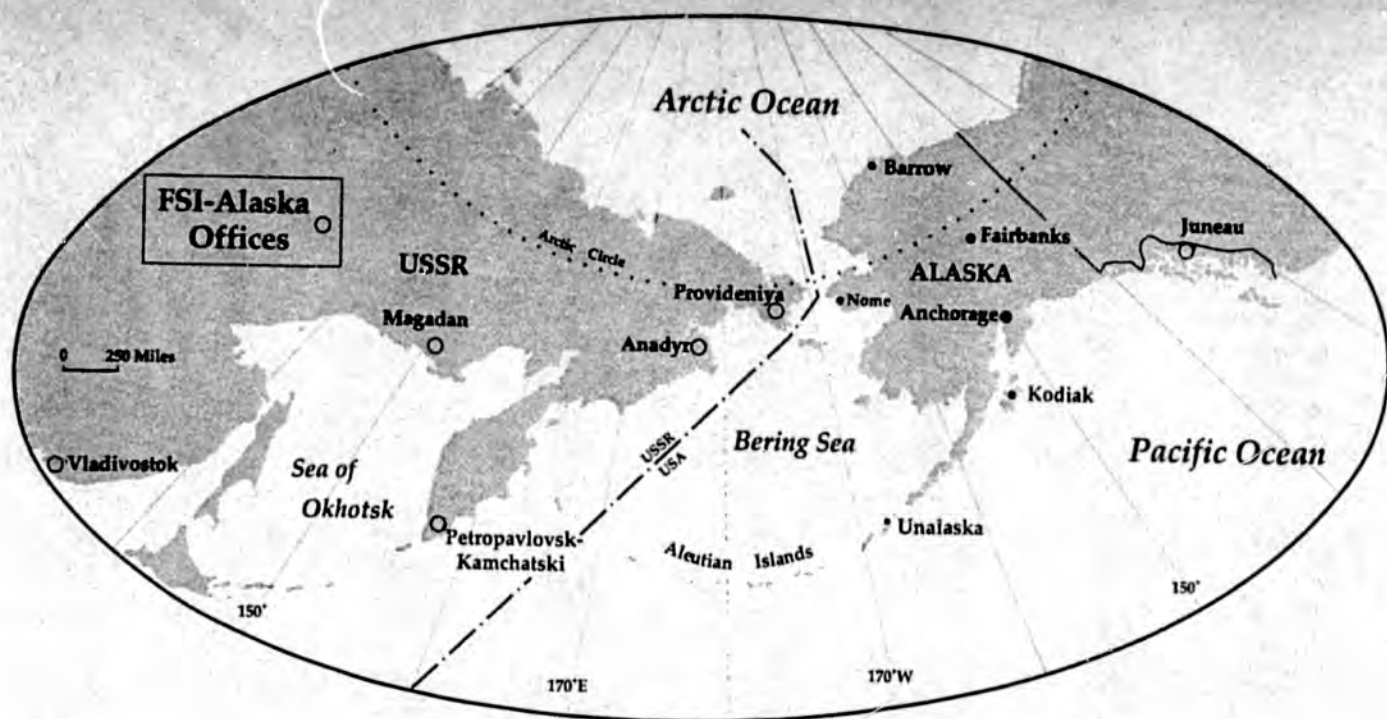
All these problems are compounded by differences in language, culture and governmental systems. As a politically knowledgeable and efficient intermediary, FSI-Alaska has played a critical role in overcoming the obstacles blocking exchanges between the northern frontiers of these two nations.

With the help of FSI-USSR, FSI-Alaska has worked successfully to bridge many of these barriers, obtaining government permissions, establishing electronic communication links, arranging transportation and complex logistics, fostering negotiations and attending to all of the organizational details necessary to transform the dreams, ideas and plans of citizen exchanges into reality.

As FSI-Alaska has grown, so has the demand for its services.



The Communist Party Central Committee of the Primorskiy Region met with members of an FSI-Alaska delegation to discuss the opening of a FSI-Alaska office in Vladivostok and the sister city relationship between Juneau and Vladivostok.



FSI network links northern frontiers

During its first year and a half of operation, FSI-Alaska built an infrastructure including FSI-Alaska offices in the Soviet Far East whose operations are directed by staff in the Juneau headquarters. The central office for the Far East is in Vladivostok; other offices are located in Anadyr, Magadan, Petropavlovsk-Kamchatski, and Provideniya. In addition to these offices in the Soviet Far East, FSI-Alaska is also linked with its sister organization, FSI-USA, headquartered in San Francisco. The breadth of this network enhances the potential for Pacific Rim co-operation.

♦ **Electronic Mail** FSI-Alaska exchanges messages via computers, fax machines and satellite-linked telephone lines with FSI-U.S.S.R. in Moscow and with its offices in the Far East, capabilities unusual in the Soviet Union. In addition we are linked electronically to four Foundation for Social Innovation (FSI) offices in major cities throughout the Soviet Union, and to the FSI-USA office in San Francisco.

♦ **Air Travel** The establishment of regularly scheduled air service between Alaska and the Soviet Far East is the most vital piece of infrastructure needed to give substance to Alaska-Soviet relations.

In February 1989, a pioneering Soviet Aeroflot jet flight co-sponsored by FSI-USSR brought a group of 92 Soviet citizens to Anchorage. This was the first civilian flight to fly the air corridor from Moscow east to the U.S.. As a result of this and subsequent flights, permissions allowing Aeroflot to land in Alaska are now commonplace. Establishing regular air service continues to be a major focus of FSI-Alaska. Toward this end, the foundation has worked with the USSR Ministry of Civil Aviation and its American counterparts, with other relevant government agencies, and with the private sector. An air taxi service is now making charter flights from Nome to Provideniya, and scheduled jet service between Anchorage and the Soviet Far East cities of Khabarovsk and Magadan will begin in April 1991.

Of necessity, FSI-Alaska's early efforts were devoted to establishing communication and transportation systems to link Alaska with its Soviet neighbors more efficiently. Without electronic mail and the opening of air routes for charter flights, implementation of many projects would have been unthinkable. Leaders in science, art, culture and education as well as business entrepreneurs can now use this network, promoting a new and dynamic flow of ideas.

Arts & Cultural Exchanges

"It was only with the help of the Foundation for Social Innovations office that permissions were finally acquired for our 3-9 August, 1988 visit to the village of Novoye Chaplino aboard the schooner 'Cyrano.' This allowed us to bring eleven Eskimos from Gambell, St. Lawrence Island, to recontact and actually stay in the homes of their relatives for the first time in forty years."

*Dr. David Lewis and
Dr. Mimi George
University of Alaska
anthropologists*

All relationships are built on cultural understanding; therefore, FSI-Alaska emphasizes cultural exchanges which bridge our differences by communicating what Soviets and Alaskans have in common.

The indigenous people of Alaska and the Soviet Far East have family ties which span the Bering Strait. The Russian culture established in Alaska 100 years before it became a territory of the United States still thrives in several Alaskan communities. Other communities were established in Alaska more recently by Russian "Old Believers."

In addition to these historical ties, the people of this region have geographic bonds, with similar climatic and social struggles, natural resources, and the common experience of life in a northern frontier, distant from the centers of power.

Similarities in art and culture have been the basis for many of the unique exchange projects facilitated by FSI-Alaska, including:

♦ **The Pilliken Expedition** reuniting Siberian Yupik Eskimos with their relatives in Alaska by crossing the Bering Strait in traditional skin-covered boats, the first such crossing in 48 years.

♦ **Through Eskimo Country**, an epic four-year traverse of the Northwest Passage in Eskimo skin-covered boats. Departing from the Soviet Union, the voyage crossed the Bering Strait in 1990 and will continue along the arctic coast of Alaska and Canada to Greenland. The crew consists of Eskimos from these four arctic countries, and several non-native Russians and Americans.

Pilliken Expedition crosses the Bering Sea



♦ **Russian Orthodox Church** Members of the Moscow Patriarchate exchanged visits with members of the Anchorage, Kenai, Kodiak and Unalaska Orthodox churches in June of 1989. Relations continue with a constant flow of visitors to and from the Soviet Union.

♦ **Vasily Peskov**, a Soviet television celebrity and author, traveled through Alaska to conduct research for a book and film showcasing the historical ties and newly reestablished relationship between Alaska and the Kamchatka Peninsula.

♦ **Veche**, a Vladivostok folk ensemble, plans to tour communities throughout Alaska in April 1991. An Alaskan group will reciprocate with a tour of the Soviet Far East the following summer.

♦ **Art Bridge** is an exchange of artworks organized by citizens of Juneau and Vladivostok to celebrate Soviet-Alaska ties. The art currently hangs in Vladivostok. A reciprocal show will travel to Juneau in the Spring of 1991.

- ◆ **Museum Directors** benefited from an exchange between museums in the Soviet Far East, Alaska and Canada.
- ◆ **Chess Games** were facilitated via electronic mail between subscribers of the *Anchorage Daily News* and *Anchorage Times*, and *Komsomolskaya Pravda*, a Soviet national paper with 21 million readers.
- ◆ **Project Baidarka**, with FSI-Alaska as its chief coordinator, involved the construction of a traditional Aleut skin-covered boat in Unalaska, Alaska.

Образовательные Проекты

Education Projects

While the United States is very active in the global economy, many American citizens remain intellectually isolated due to their lack of knowledge regarding political and cultural geography. The public education system provides American students with little information about Eastern Bloc nations. Similarly, Soviet schools have taught an ideologically determined version of the history and society of a Cold War enemy. Both the U.S. and the U.S.S.R. require reform of their international education curricula.

◆ **Educators' Conference** To facilitate connections between the University of Alaska Statewide System and the Soviet State Education Committee, FSI-Alaska arranged for two representatives from the Soviet Committee to travel to Alaska to meet with their Alaskan counterparts.

◆ **Project World 2000** In October 1989, a group of Juneau educators traveled to Moscow to share co-operative learning techniques and to develop a joint environmental education program focusing on global health issues. A high school class in Juneau was linked by electronic mail with a class in Moscow so Soviet and Alaskan students could share their school work for this curriculum. The course is now in its second year, and the curriculum has expanded to include other topics.

◆ **Student Exchange** FSI-Alaska initiated student exchanges between the University of Moscow and the University of Alaska Southeast (U.A.S.) in Juneau. A Moscow student hosted by the university and the Juneau Rotary Club is currently attending U.A.S. In September 1991 a U.A.S. student will travel to Moscow to attend school at the University of Moscow.

◆ **Vladivostok Connections** In February and May of 1990, FSI-Alaska sponsored delegations including Alaskan education, civic, business and cultural leaders to establish relations with groups in the Soviet Far East capital city of Vladivostok. The University of Vladivostok was a special focus; plans for teacher and course exchanges were developed for implementation during the coming academic year. The opening of FSI-Alaska's Soviet Far East headquarters office in Vladivostok was one of the highlights of these visits.

"...Soviet delegations have visited Alaska and other Alaskan groups have had rewarding experiences in the Soviet Union. Again, these have been valuable to the University of Alaska. The Foundation has often served as a catalyst."

*George C. Christensen
Vice President for Academic
Affairs, University of Alaska*



Students in Moscow School 1201.

Социальное и Экономическое Развитие

Social and Economic Development: Building on Cultural Exchanges

FSI-Alaska is presently entering a transition period between the enthusiastic friendship exchanges of 1988-1990 and the beginning of complex cooperative undertakings and commercial ventures.

Although major shifts in Soviet and American relations have broken down many of the ideological barriers separating our two countries for so long, the development of commerce does not automatically follow. Many impediments — cultural, monetary, technological, logistical and governmental — remain, and Soviet economic restructuring lends both opportunity and uncertainty to our relationships at this time. The Board of Directors has adopted this transition as its special focus for the next three years.

The strategy is to build a foundation for successful ventures by encouraging the growth of social and economic infrastructure connecting Alaska and the Soviet Far East, and by expanding the knowledge needed to make cooperative ventures work. Moreover, as Soviet economic restructuring begins in earnest, opportunities will be identified for aiding development of the private sector in the Far East.

The strategy envisions symposia and technical exchanges designed to attain concrete objectives. At the same time, sister cities connections, television program exchanges, and student exchanges will enhance mutual understanding and generate business opportunities. The benefits of sharing information and technology are evident on both sides of the Pacific.

"We feel it is essential that the true 'citizen diplomacy' efforts have such an office available to assist them, for they lack the powerful leverage of the political-economic establishment."

*David Lewis, Ph.D. and
Marianne George, Ph.D.
University of Alaska
anthropologists*

Sister City Delegations

Among the most enthusiastic delegations travelling to the Soviet Union under the sponsorship of FSI-Alaska are citizen groups travelling to establish sister city relationships. Under the umbrella of these people-to-people exchanges, business ventures are initiated and areas of mutual interest in health, education, communication and transportation are identified. As the Soviet government becomes more decentralized, local governments must take on new roles and may benefit from a first-hand knowledge of municipal government in Alaska.

◆ **Petropavlovsk-Kamchatki and Unalaska, Alaska** have established a sister city relationship as the result of negotiations facilitated by FSI-Alaska.

◆ **Vladivostok and Juneau** are discussing a sister city relationship. Nego-



Students of the Soviet port city of Vladivostok, which was closed to foreign visitors for over 60 years, greet a student from Juneau, Alaska traveling with a FSI Alaska delegation in May 1990.

tiations were begun when the mayor of Juneau and representatives of FSI-Alaska visited Vladivostok in May of 1990. Discussions will continue in December 1990, when 120 people will fly from Juneau to Vladivostok for an eight-day visit. Soviet permission and organization of this visit was coordinated by FSI-Alaska. Plans are being made for a reciprocal visit by 120 people from Vladivostok to Juneau in spring 1991.

♦ **Vitus Bering "250"** Many projects are being planned to celebrate the 250th anniversary of the discovery of Alaska by a Russian expedition led by Vitus Bering. FSI-Alaska has been asked to serve as logistical coordinator for this joint celebration involving the State of Alaska and the four regions of the Soviet Far East (Chukotski, Magadan-ski, Kamchatski and Primorski) during the summer of 1991.

Commercial Ventures

Building on its cultural and sister-city exchanges, FSI-Alaska has already sponsored or assisted several commercial ventures, including:

♦ **Tourism** An 11-day exploratory trip by kayak and other craft along Siberia's Chukotka Peninsula undertaken by the Far Eastern Expedition Center of Vladivostok and Alaska Discovery, a Juneau-based wilderness guiding company, was a successful first step toward marketing this kind of adventure trip.

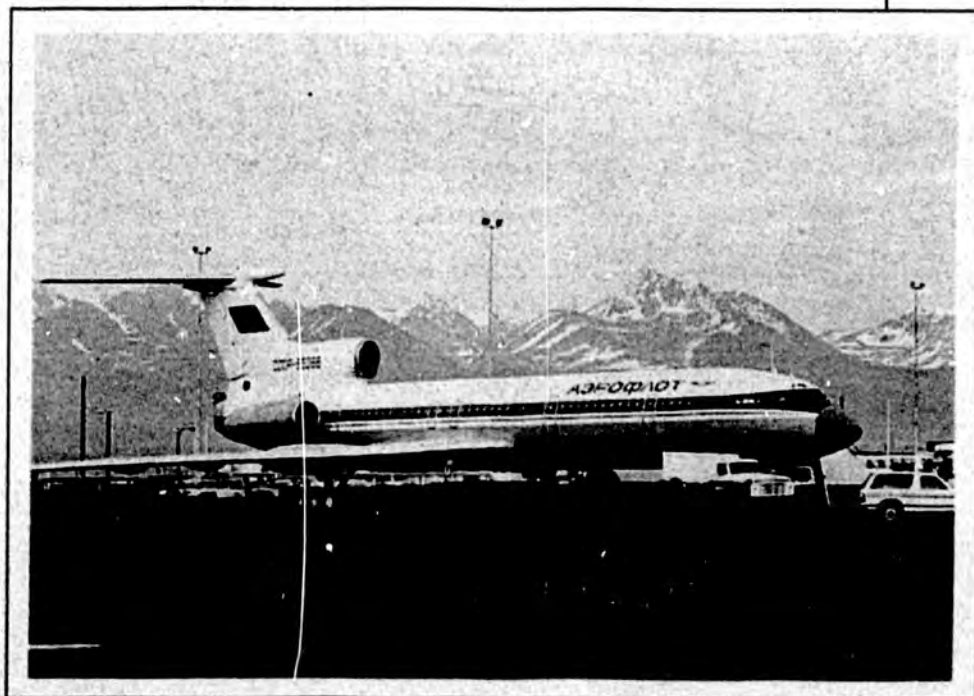
♦ **National Geographic Arrangements** by FSI-Alaska made it possible for National Geographic magazine staff to travel throughout the Chukotka Peninsula conducting research for a story on the Bering Sea. While in Chukotka, National Geographic staff accompanied FSI-Alaska's Through Eskimo Country expedition on the first leg of their journey through the circumpolar region.

♦ **Television** FSI-Alaska is working on an exchange of television programs between Alaska and the Soviet Union, so that viewers from both societies can learn more about each others lives.

A number of other ventures with commercial potential are presently being reviewed by FSI-Alaska.

"One of the most exciting possibilities of the next decade is the blossoming relationship between Alaska and the Soviet Far East. FSI-Alaska is doing pioneering work to cultivate these possibilities with its inspiring energy, bold ideas and innovative activities."

*Juneau, Alaska Mayor
Bruce Botelho*



Aeroflot jet chartered by FSI-Alaska, on the ground in Anchorage.

Project Funding

"In many cases there is no replacement or alternative to what the FSI-Alaska office is doing for these initiatives....The office has shown itself to be on the cutting edge of new projects and proposals which do not always qualify for—nor can they wait for—traditional funding and support."

David Lewis, Ph.D.
and Marianne George, Ph.D.
University of Alaska
anthropologists

The University of Alaska Southeast generously provided in-kind support for all FSI-Alaska office expenses during the first year and a half. During that period, FSI-Alaska secured federal tax exempt status and received contributions from business and government sources, including a share of grants received by FSI-USA in San Francisco.

Given the organization's expanding role, the board of directors has initiated a campaign to diversify FSI-Alaska's funding sources. In addition to charging fees for the services provided to businesses, FSI-Alaska is actively soliciting corporate sponsorships, foundation grants and in-kind contributions. In conjunction with its funding campaign, FSI-Alaska has launched a media campaign in Alaska to promote the organization and to help raise funds in the state.

FSI-Alaska is seeking general financial support to fund operations in Juneau and to maintain the FSI-Alaska network of offices in the Soviet Far East. Individuals and organizations are also invited to contribute to selected projects, planned or in progress. In addition to acknowledgement for their sponsorship, contributors may be involved in project planning and status.

Contributions will be used in accordance with the goals expressed in this prospectus. In addition to office staff expansion, the board of directors has elected to facilitate the following projects during the next quarter:

- Facilitating television program exchanges between Alaska and the Soviet Union;
- Providing logistical coordination for the Vitus Bering 250 celebration;
- Continuing sponsorship of the Through Eskimo Country project as it enters its second year enroute to Greenland;

Detailed descriptions of these projects are available from the FSI-Alaska office.

Supporters of FSI-Alaska

Organizations

Aeroflot, Moscow
Alaska Airlines
Alaska Department of Education
Alaska Department of Natural
Resources
Alaska Discovery, Inc.
Alaska Office of the Governor
Alaska State Museum
Alternativa
Baranof Hotel
Bering Air
Camai
Dyn Air
Executive Committee, City of
Petrovsk-Kamchatki
Executive Committee,
Primorski Region
Executive Committee,
City of Vladivostok
City of Fairbanks

City of Gambell
City of McGrath
Far East Expedition Center
Foundation for Social Innovation-
USA & USSR
Foundation for the Survival and
Development of Humanity
Greyhound Bus Lines
Inland Boatman's Union
International Airport Systems
City of Juneau
Juneau School District
Komsomolskaya Pravda
KTOO, Juneau Public
Broadcasting Station
Little Feet, Inc.
National Endowment for the Arts
City of Nome

Government of the Northwest
Territories, Canada
Oonashka Corporation
Peninsula Air
Rockefeller Foundation
Russian Orthodox Church
Scandinavian Airlines
School 14, Vladivostok
School 1201, Moscow
Sealaska Heritage Foundation
Team Marine
Tesoro Petroleum Company
City of Unalaska
University of Alaska Southeast
U.S.S.R. Ministry of Civil
Aviation
U.S.S.R. Ministry of Foreign
Affairs
Vitus Bering "250" Celebration
Committee

Individuals

Patrick Anderson
Rose Arvidson
Dixie Belcher
Gretchen Birch
Don Black
Sergey Bogoyavlensky
Sergey Braga
Judy Brakel
Ken Burch
Louise Champagne
George Christiansen
Susan Clark
Stoney Compton
Sharon Cook
Larry Cotter
Laurie Ferguson Craig
Karen Cummins
Henry Dakin
Andrei Diatlov
Stan Fischer
Jack Frost

Mark Garber
Mimi George
Nelli Gregorian
Dawn Groves
Pat & Tuckey Hayes
Cindy Holland
Dan Hopson
Daniel Johnson
Karil Kassatkin
Sergey Kirillov
Nancy Korn
Steve Krall
Madeleine Lefebvre-Fisk
Ken Leghorn
David Lewis
Andra Martin
Tom Matheson
Mike McKennett
Jo Michalski
Giorgi Nachaev
Jim Noyes
Shirley Nygard

Jason Ohler
Marina Paskina
Jim Rowe
Sandy Rutherford
Evgeniy Ryabov
Kathleen Samalon
Velodia Sertoon
Joyce Shales
Lena Sherbakova
Sherri Sirkin
Walter Slipchenko
Don Southerland
Jim Stimpfle
Barbara Swedell
Andrei Symikov
Teri Tibbett
Rosemary Van Der Laan
Todd Weir
Kent Woodman
Dan Zantek
Alexei Zhukov

FSI-Alaska Board of Directors



JoAnn Zentner

has served as Executive Director of FSI-Alaska since its inception in February, 1989. Ms. Zentner holds a degree in sociology and is the former director of the Institute for a Violence Free Society, which, among other activities, worked to develop relations between Alaska and the Soviet Union. She was invited by Mr. Alferenko to establish the Alaska regional office of F.S.I. She has resided in Alaska for fifteen years and travels frequently between Alaska and the Soviet Union. Ms. Zentner lives in Juneau, Alaska with her two children, Eric and Katie.

Bruce Botelho

is an assistant attorney general for the State of Alaska and mayor of the City of Juneau. He is a former deputy commissioner of the Alaska Department of Revenue, supervising oil and gas taxes and the permanent fund dividend program, and is past chairman of the Alaska Resources Commission. He is president of the Juneau International Folkdancers and has served on a number of other Juneau area civic organizations. He has traveled to the Soviet Union to promote a "Sister City" relationship between Juneau and Vladivostok.



Mike Davis

has been a member of the Alaska House of Representatives since 1983, serving the Fairbanks area. His areas of expertise include natural resources, environmental law, international trade and legislative ethics. Davis has worked as a commercial fisherman, college instructor in math and government, school teacher in bush villages, counselor/advisor for the University of Alaska, Vista volunteer and legislative aide. He has been instrumental in promoting FSI-Alaska among the state's political leaders.



Sergey A. Frolov

a native of Petropavlovsk-Kamchatskiy, USSR, is president of the Far Eastern Expedition Center in Vladivostok; consultant to the History Department, University of Leningrad and the Magadan Museum, Magadan, USSR; and a member of the Board of Directors of the USSR Expedition Society. He has served as a ranger on a nature reserve, a marine engineer with the Far East Scientific Research Institute, Vladivostok, and an instructor of traditional boat-building and sailing in both the USA and USSR. His extensive experience in marine expeditions has culminated in a leadership role in "Through Eskimo Inuit Country", a four-year ethnographic expedition through the Northwest Passage.



Paul Fuhs

is mayor of the City of Unalakleet/Dutch Harbor. In addition to serving as Business Relations Director for the FSI-Alaska, he is a commercial diver and underwater explosives expert. Mr. Fuhs is co-chairman of Ports Alaska and has been a leader in promoting large-scale Soviet/Alaskan transportation and communications business ventures. In his current position as Executive Director of the Bering Sea Marine Institute, Mr. Fuhs has been promoting cooperative Soviet/Alaska fisheries research and environmental protection programs in the Bering Sea.





Ernst Holland

has lived in Alaska for 11 years, residing in Anchorage with his wife, Cindy, and his four children. He is in the retail shoe business and carries on hunting and fishing ventures. He participated in the first Aeroflot charter flight sponsored by FSI-Alaska and the Ministry of Civil Aviation and has been an active board member since the inception of the organization. Mr. Holland has made numerous trips to the Soviet Union in the last few years and has great interest in helping to facilitate exchanges of all kinds between the Soviet Union and the USA.

Marshall L. Lind

has served as Chancellor of the University of Alaska Southeast since April 2, 1987. Prior to that he served as Commissioner of Education, Alaska Department of Education for over 14 years. In his role as UAS Chancellor, Lind took an active role in the creation of The Foundation for Social Innovation/Alaska Siberia Project by providing the office space in which to get started. He has served on its board of directors since its inception and has taken an active interest in Soviet issues through the University's presentation of an Honorary Doctor of Humanities to President Mikhail Gorbachev, and in promoting program development and exchanges between UAS and Soviet universities.



Steve Nelson

has 15 years of television and radio experience in Alaska including Radio Production Director, Videographer, Engineer, Editor, Producer and Chairman of the Board of Directors of KTOO/Juneau and Chief Videographer for C-SPAN in Washington, D.C. He currently works for the Governor of Alaska producing video news releases and special programs. He has visited the Soviet Union twice, once as Producer for an independent news crew which provided CNN and CBS with video segments on Soviet activities, and again as part of an Alaskan delegation to coordinate program exchanges between Soviet and Alaska television stations.

Greg Pease

serves as chairman of the board of FSI-Alaska and is also Executive Director of Gastineau Human Services Corporation, a private non-profit organization providing aid to socially disadvantaged people. He has promoted the international radio "Global Town Meetings", co-produced the television spacebridge "Alaska Celebrates the International Year of Peace", sung in the "Alaska Performing Artists for Peace" tour, served as Pacific Rim chairman of the "International Association of Residential and Community Alternatives", co-founded the "University of Alaska Institute for Circumpolar Health," attended the joint "USSR/USA Film Summit" and served as a board member of the "CAMAI Foundation."



PHOTO: MARY FANDLETT

James Schoppert

is a native Tlingit sculptor living in the Seattle area whose art is widely exhibited throughout the Northwest and Alaska. He says of his work, "I am especially influenced by the art conventions of the Tlingit and the freedom and whimsy seen in the traditional art of Alaska's coastal Eskimos. This ancestral influence is then interfaced or mingled with approaches to art developed in Western art.... When I look at the historical works of the Eskimo peoples I'm inspired to take the pictographic and surrealistic imagery into a more modern context." He holds a Master of Fine Arts degree from the University of Washington.

W1100S
#38

Canada United States Air Transport Agreement

B a c k g r o u n d I n f o r m a t i o n

October 1990

CANADA-U.S. AIR TRANSPORT AGREEMENT

Bilateral Air Agreement

A bilateral air agreement sets out how scheduled air services may be operated between two countries. It specifies:

- . the cities that may be served and under what conditions,
- . the frequency of flights,
- . the routes (including how they may be combined with services to other countries),
- . tariffs or pricing,
- . provisions for safety and security,
- . provisions for ground handling, and
- . other details.

Bilateral air agreements are negotiated by delegations of officials from both countries.

Canada's aim in such negotiations is to conclude agreements that are in the best interests of the travelling and shipping public, communities, the tourism industry and Canadian airlines.

Canada-U.S. Agreement

The Canada-U.S. air agreement covers the single largest air bilateral relationship in the world. The U.S. is Canada's single largest international market for air services.

Canada's bilateral air agreement with the United States is the most complex of its 46 agreements with foreign countries. It consists of a number of separate documents dealing with:

- . scheduled services (the main Air Transport Agreement),
- . charters (the Nonscheduled Services Agreement),
- . customs and immigration services in the other country (the Preclearance Agreement),
- . cargo services (the All-Cargo Notes),
- . commuter services (the Regional, Local and Commuter Services Notes) and
- . aviation security.

History

The most important of these documents were revised in 1974 and no major changes have been made since that time. The consequence has been that for the past 16 years, Canadian and U.S. scheduled air service patterns have been limited to what is permitted in the route schedules agreed to in 1974. Important market pairs such as Montreal-Atlanta, Toronto-Washington or Vancouver-Denver do not have direct service.

During this same period, the North American air industry has changed significantly. The U.S. (in 1978) and Canada (in 1988) deregulated their domestic air services, with the result that today's services are determined by the commercial decisions of airlines and not government regulators.

In order to achieve the highest degree of efficiency and best use of their aircraft, airline companies have chosen to concentrate their city-to-city connections at certain major airports, which are referred to as "hubs". The cities which feed hubs with passenger traffic are known as "spokes".

The emergence of hub and spoke networks, especially in the U.S., has created new traffic patterns and new opportunities for carriers that were not envisaged at the time the main agreement was negotiated.

With growing trade relations between Canada and the U.S., the communities want transborder air services opened up to allow air carriers to respond to this new economic environment.

Today more than 13 million passengers move annually between the two countries, generating some \$2.3 billion in revenues.

Scheduled and Charter Air Services

Scheduled air services between Canada and the U.S., including local and regional services, are provided on 83 city pairs. Canadian carriers are the sole operators in 26 of these markets while U.S. carriers have exclusivity in 39 markets. Carriers from both sides share 18 city pairs.

Canadian carriers are particularly strong in the smaller charter market with over 95 per cent of the traffic, while U.S. carriers dominate scheduled air services, taking almost two-thirds of the traffic.

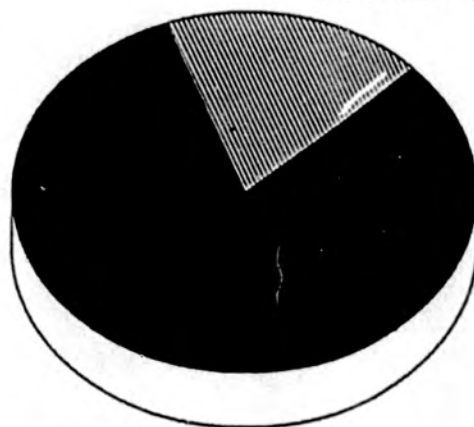
The charter market is concentrated in three areas - Florida, Nevada and Hawaii, with Florida representing more than 50 per cent of the market.

CANADA - U.S. AIR AGREEMENT - TOTAL TRAFFIC - (1989)

	Number of Passengers Carried <u>(millions)</u>	<u>%</u>
Scheduled Services	10.7	82%
Charter Services	<u>2.4</u>	<u>18%</u>
Total	13.1	100%

PASSENGERS

CHARTER SERVICES 18%

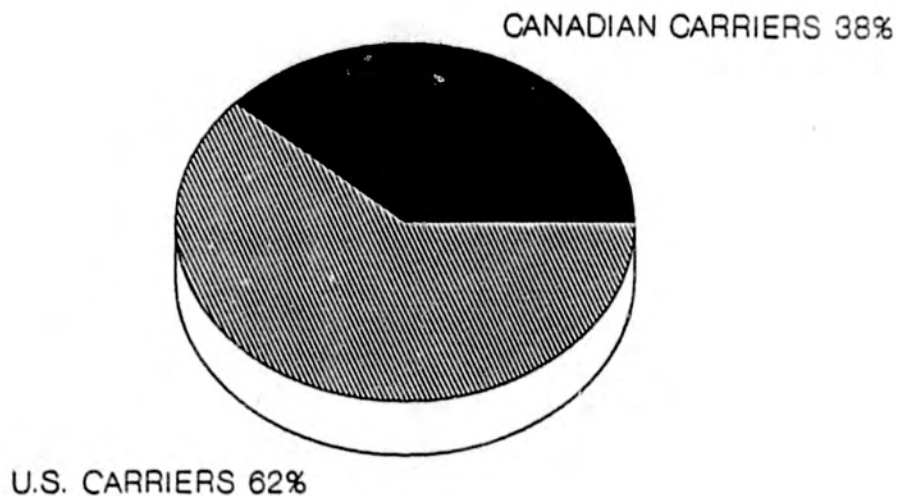


SCHEDULED SERVICES 82%

CANADA – U.S. AIR AGREEMENT – SCHEDULED SERVICES – (1989)

	Number of Passengers Carried <u>(millions)</u>	<u>%</u>
Canadian Carriers	4.1	38%
U.S. Carriers	6.6	62%
Total	<u>10.7</u>	<u>100%</u>

PASSENGERS

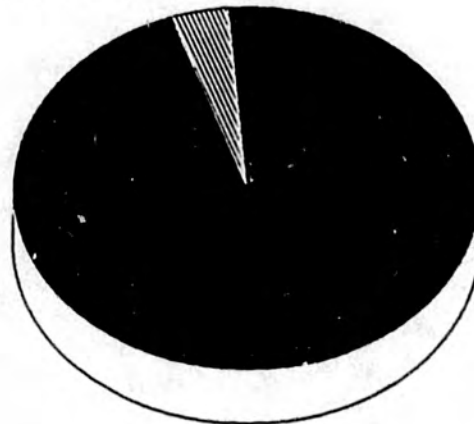


CANADA - U.S. AIR AGREEMENT - CHARTER SERVICES - (1989)

	Number of Passengers Carried (millions)	<u>%</u>
Canadian Carriers	2.3	96%
U.S. Carriers	0.1	4%
Total	<u>2.4</u>	<u>100%</u>

PASSENGERS

U.S. CARRIERS 4%



CANADIAN CARRIERS 96%

SCOMM

83:5

FISCAL NOTE

STATE OF ALASKA
1991 LEGISLATIVE SESSION

BILL NO. CSHB12

Revision Date: March 12, 1991
Title: An act relating to the water's edge method of taxation
Sponsor: Representative Moyer
Requestor: _____

Department Affected: Department of Revenue
BRU: Revenue Operations
Component: Income and Excise Audit

COMPONENT SERIAL NO. 1 1 3

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 92	FY 93	FY 94	FY 95	FY 96	FY 97
PERSONAL SERVICES	0.0	0.0	63.8	63.8	63.8	63.8
TRAVEL	0.0	30.0	34.8	39.3	39.3	39.3
CONTRACTUAL	13.0	15.0	17.0	17.0	17.0	17.0
SUPPLIES	0.0	2.5	2.5	8.0	8.0	8.0
EQUIPMENT	0.0	0.0	14.5	2.5	0.0	0.0
LANDS & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	13.0	47.5	132.6	130.6	128.1	128.1
CAPITAL	0.0	0.0	0.0	0.0	0.0	0.0
REVENUE	(500.0 - 1500.0)	(1000 - 3000)	(1000 - 3000)	(1000 - 3000)	(1000 - 3000)	(1000 - 3000)

FUNDING: (Thousands of Dollars)

GENERAL FUND	13.0	47.5	132.6	130.6	128.1	128.1
FEDERAL FUNDS						
OTHER						
TOTAL	13.0	47.5	132.6	130.6	128.1	128.1

POSITIONS:

FULL-TIME	0.0	0.0	1.0	1.0	1.0	1.0
PART-TIME						
TEMPORARY						

Estimate of current year impact: _____

ANALYSIS: Attach a separate page for analysis.

ATTACHED

Prepared By: William F. Schuchman
Division: Income and Excise Audit Division

Phone: (907) 465-2320
Date: March 12, 1991

Approved by Commissioner: Lee E. Fisher
Agency: Department of Revenue

Date: 3-12-91

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

Fiscal Note Analysis, CSHB12
Income and Excise Audit Division
Prepared by Bill Floerchinger
March 12, 1991

The proposed legislation mandates the use of a water's edge method of accounting under the income tax law for non-oil and gas taxpayers. The legislation would be effective for tax years beginning in calendar 1992. Returns would be due in calendar 1993 and audits would begin in FY94. The data below shows the timing for the various cost components required to administer the proposed legislation.

<u>Personal Services</u>	<u>FY92</u>	<u>FY93</u>	<u>FY94</u>	<u>FY95</u>
1 Revenue Auditor IV, Anchorage	\$0.0	\$0.0	\$63.8	\$63.8
Total Personal Services Costs	\$0.0	\$0.0	\$63.8	\$63.8
<u>Travel</u>				
Training, 5 @ \$10.0	\$0.0	\$30.0	\$10.0	\$10.0
Management Review, 4 @ \$.5	\$0.0	\$0.0	\$2.0	\$2.0
12 Audits completed @ \$1.9	\$0.0	\$0.0	\$22.8	\$22.8
9 Appeals completed in Anchorage @ \$.5	\$0.0	\$0.0	\$0.0	\$4.5
Total Travel	\$0.0	\$30.0	\$34.8	\$39.3
<u>Contractual</u>				
Printing and Advertising Costs	\$13.0	\$13.0	\$13.0	\$13.0
Telecommunications, Centrex	\$0.0	\$2.0	\$4.0	\$4.0
Total Contractual	\$13.0	\$15.0	\$17.0	\$17.0
<u>Supplies</u>				
Office supplies, Computer supplies, Audit Manuals and References	\$0.0	\$2.5	\$2.5	\$8.0
Total Supplies	\$0.0	\$2.5	\$2.5	\$8.0
<u>Equipment</u>				
2 Wang PC Computers, Cable Hookup	\$0.0	\$0.0	\$7.5	\$2.5
2 Laptop Computers	\$0.0	\$0.0	\$7.0	\$0.0
Total Equipment	\$0.0	\$0.0	\$14.5	\$2.5
TOTAL COSTS	<u>\$13.0</u>	<u>\$47.5</u>	<u>132.6</u>	<u>\$130.6</u>

FISCAL NOTE

STATE OF ALASKA
1991 LEGISLATIVE SESSION

BILL NO. HB12

Revision Date: _____
Title: An act relating to the water's
edge method of taxation
Sponsor: Representative Moyer
Requestor: Representative Moyer

Department Affected: Department of Revenue
BRU: Revenue Operations
Component: Income and Excise Audit
COMPONENT SERIAL NO. | 1 | 1 | 3 |

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 92	FY 93	FY 94	FY 95	FY 96	FY 97
PERSONAL SERVICES	0.0	56.1	183.7	247.7	247.7	247.7
TRAVEL	0.0	40.0	44.8	39.3	39.3	39.3
CONTRACTUAL	13.0	15.0	17.0	17.0	17.0	17.0
SUPPLIES	0.0	2.5	7.5	10.0	10.0	10.0
EQUIPMENT	0.0	0.0	22.0	5.0	0.0	0.0
LANDS & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	13.0	113.6	275.0	319.0	314.0	314.0
CAPITAL	0.0	0.0	0.0	0.0	0.0	0.0
REVENUE	(500.0 - 1500.0)	(1000 - 3000)	(1000 - 3000)	(1000 - 3000)	(1000 - 3000)	(1000 - 3000)

FUNDING: (Thousands of Dollars)

GENERAL FUND	13.0	113.6	275.0	319.0	314.0	314.0
FEDERAL FUNDS						
OTHER						
TOTAL	13.0	113.6	275.0	319.0	314.0	314.0

POSITIONS:

FULL-TIME	0.0	1.0	3.0	4.0	4.0	4.0
PART-TIME						
TEMPORARY						

Estimate of current year impact: _____

ANALYSIS: Attach a separate page for analysis.

ATTACHED

Prepared By: Carl Meyer, Acting Director Phone: (907) 465-2320
Division: Income and Excise Audit Division Date: February 5, 1991

Approved by Commissioner: Lee Fisher
Agency: Department of Revenue Date: 2-7-91

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

Fiscal Note Analysis, HB12
Income and Excise Audit Division
Prepared by Carl A. Meyer
February 5, 1991

The proposed legislation mandates the use of a water's edge method of accounting under the income tax law for non-oil and gas taxpayers. The legislation would be effective for tax years beginning in calendar 1992. Returns would be due in calendar 1993 and audits would begin in FY94. The data below shows the timing for the various cost components required to administer the proposed legislation.

<u>Personal Services</u>	<u>FY92</u>	<u>FY93</u>	<u>FY94</u>	<u>FY95</u>
1 Revenue Auditor IV, Seattle	\$0.0	\$56.1	\$56.1	\$56.1
2 Revenue Auditor IV, Anchorage	\$0.0	\$0.0	\$127.6	\$127.6
1 Appeals Officer, Juneau	\$0.0	\$0.0	\$0.0	\$64.0
Total Personal Services Costs	\$0.0	\$56.1	\$183.7	\$247.7
<u>Travel</u>				
Training, 7 @ \$10.0	\$0.0	\$40.0	\$20.0	\$10.0
Management Review, 4 @ \$.5	\$0.0	\$0.0	\$2.0	\$2.0
12 Audits completed by 3 auditors @ \$1.9	\$0.0	\$0.0	\$22.8	\$22.8
9 Appeals completed in Anchorage @ \$.5	\$0.0	\$0.0	\$0.0	\$4.5
Total Travel	\$0.0	\$40.0	\$44.8	\$39.3
<u>Contractual</u>				
Printing and Advertising Costs	\$13.0	\$13.0	\$13.0	\$13.0
Telecommunications, Centrex	\$0.0	\$2.0	\$4.0	\$4.0
Total Contractual	\$13.0	\$15.0	\$17.0	\$17.0
<u>Supplies</u>				
Office supplies, Computer supplies, Audit Manuals and References	\$0.0	\$2.5	\$7.5	\$10.0
Total Supplies	\$0.0	\$2.5	\$7.5	\$10.0
<u>Equipment</u>				
4 Wang PC Computers, Cable Hookup	\$0.0	\$0.0	\$15.0	\$5.0
2 Laptop Computers	\$0.0	\$0.0	\$7.0	\$0.0
Total Equipment	\$0.0	\$0.0	\$22.0	\$5.0
TOTAL COSTS	<u>\$13.0</u>	<u>\$113.6</u>	<u>275.0</u>	<u>\$319.0</u>

The Department is not able to determine the revenue impact of this legislation. However, it should fall within the range of the \$1-\$3 million per year reduction estimated during the 1990 legislative session in CSSB119. The Department is working to develop better numbers and will revise this fiscal note when those numbers become available.

An agency position paper is attached.

HOUSE SPECIAL COMMITTEE ON INTERNATIONAL TRADE AND TOURISM

ALASKA STATE LEGISLATURE

P.O. BOX V, JUNEAU 99811

(907) 465-2973



MEMORANDUM

To: Representative Mike Navarre
Co-Chairman, House Finance Committee

March 13, 1991

From: Representative Tom Moyer *TEM*

Re: CSHB12, Corporate Income Tax Reporting Methods

I would like to request the Finance Committee hold a hearing at your earliest convenience on CSHB12. As you know, I am the bill's sponsor and both the International Trade and Tourism and Labor and Commerce Committees have considered the bill and favorably passed it out.

The bill is designed to attract foreign investment to Alaska by replacing Alaska's unitary tax, widely considered a barrier to foreign investment, with a so-called "water's edge" tax system. Under the bill, only the domestic activities of a foreign or international corporation would be subject to Alaska taxes and oil and gas companies would be exempt.

The bill has received broad support in the two earlier committees of referral. It is backed by a number of Alaska business groups including the State Chamber of Commerce, Alaska Miners' Association, Anchorage Economic Development Corp., a host of private companies doing business in the state as well as the Hickel administration. As you'll recall, a similar version of this bill passed the state Senate last year.

A complete bill file is being transferred to your committee and I am happy to provide any additional information should you need it. I'm also pleased to make myself available to testify about the bill at your convenience.

CC: Representative Eileen MacLean

DIVISION OF LEGAL SERVICES

LEGISLATIVE AFFAIRS AGENCY STATE OF ALASKA

P.O. Box Y, Juneau, Alaska 99811
(907) 465-3867 or 465-2450
FAX (907) 465-2029

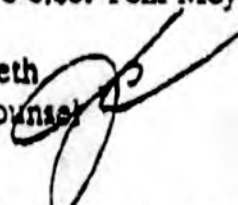
Deliveries to: 240 Main Street
Court Plaza, Room 300
Mail Stop 3161

MEMORANDUM

December 17, 1990

SUBJECT: Water's edge tax (Work order 7-0237A)

TO: Representative-elect Tom Moyer

FROM: Jack Chenoweth
Legislative Counsel 

This draft legislation, based on last session's CSSB 119 reported by the Senate Finance Committee, amends the method of income tax computation for certain corporations in order to set aside a perceived barrier to investment. Simply stated, the measure would direct corporations subject to Alaska's Net Income Tax that are members of affiliated groups owned by foreign corporate parents to file returns based on the so-called "water's edge" method of taxation. That taxing method takes into consideration only the domestic (i.e., United States) activities of the foreign corporation and does not consider income derived from the companies' non-American operations.

In the draft previously provided --

Bill section 2 is the measure's principal operative provision. It adds a new section, proposed AS 43.20.073.

Subsection (a) of proposed AS 43.20.073 sets out the general requirement that a corporation that is a member of an "affiliated group"--a group of two or more corporations in which at least 50 percent of the voting stock of each member of the group is held by one or more common owners or by one or more of the members of the group--must file its state tax returns using the "water's edge combined reporting method." The water's edge combined tax return is to be used by (1) corporations that do substantial business within the United States, irrespective of where incorporated; (2) domestic and foreign sales corporations; and (3) so-called "tax haven" corporations (that have been formed for the purpose of avoiding taxes in the United States). Under this subsection, a corporation is considered to be part of the taxpayer's water's edge tax family, and its income taxable in Alaska, if 20 percent or more of its average property, payroll, and sales factors are within the United States. Under this subsection, a corporation is considered to be part of the taxpayer's water's

Representative-elect Tom Moyer

December 17, 1990

Page 3

taxpayers operating as oil and gas transporters by regulated pipeline. Those taxpayers to determine their tax liability using the worldwide combined report.

Proposed AS 43.20.073(g) sets out pertinent definitions of terms used in the section.

As drafted, the measure would take effect immediately [bill section 4], but apply to tax years beginning January 1, 1992 [bill section 3].

JBC:LMB

90-035.LMB



Anchorage Star of the North
Chamber of Commerce

January 23, 1990

The Honorable Fran Ulmer
House Finance Committee
P.O. Box V
Juneau, AK. 99811

Reference: House Bill 281

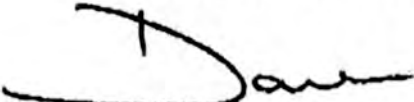
Dear Fran:

We understand that the unitary tax issue will likely be raised again in the 1990 session of the Legislature.

Last year the Anchorage Chamber of Commerce presented testimony on Senate Bill 119 concerning corporate income tax reporting methods. Our testimony recommended repealing unitary worldwide tax for both foreign and domestic multinational corporations in a way which encourages domestic and foreign corporations to locate in Alaska and help diversify our economic base, while not adversely affecting the tax burden of Alaska's oil industry.

The Anchorage Chamber recommends that multinational corporate tax policy be modified in accordance with the philosophy expressed above, and that domestic and foreign companies be treated equally.

Sincerely,
ANCHORAGE CHAMBER OF COMMERCE


Dave Harbour
Chairman

437 E Street, Suite 300, Anchorage, Alaska 99501-2365 (907) 272-2401 FAX (907) 272-4117
Founded 1915

February 6, 1991

H B 12
POSITION PAPER
DEPARTMENT OF REVENUE

House Bill No. 12 would mandate the use of a water's edge method of accounting under the income tax laws for non-oil and gas taxpayers. The bill would be effective for tax years beginning in 1992.

All domestic and foreign corporations at least 50% owned, directly or indirectly, by a common parent may be engaged together in the conduct of a unitary business. Under current law, all such unitary corporations would be included in a worldwide unitary combination. Each corporation with a taxable nexus in Alaska would then be required to file an Alaska income tax return.

HB 12 would limit the corporations that could be included in the unitary combination. Generally, only those domestic and foreign corporations whose United States property, payroll, and sales average 20% or more of the total of such factors both in the U.S. and foreign jurisdictions could be included in the combination. It is not entirely clear whether each of the three factors must average 20% or more or whether it is simply the average of the three. From an administrative standpoint, either will require an additional audit inquiry, especially as to those corporations that are close to the 20% threshold.

HB 12 would also exclude from income 80% of all dividend income from foreign corporations, all dividend gross-up, and 80% of all royalties from foreign corporations. Expenses associated with the 80% excluded from income may not be disallowed as the 20% subject to tax is deemed to be compensation for the expenses related to the 80%. The stated purpose of the bill in Section 1 is to "promote investment and trade opportunities in the state" and, presumably, the intent is to attract those taxpayers who oppose the worldwide combined reporting method.

However, the exclusion of dividends and royalty has absolutely nothing to do with use of either worldwide or domestic water's edge combination. Exclusion of income is a separate issue and the exclusion could just as well have been for any other item of income. Further, since this income is not excluded from the tax base of oil and gas taxpayers under AS 43.20.072, serious constitutional questions might arise under AS 43.20.072. We would not want to jeopardize the tax revenues under AS 43.20 by allowing a deduction to non-oil and gas companies that is not allowed to the oil and gas companies. The Department of Law should review this provision.

A state tax exemption for foreign dividends and royalty could well favor foreign over United States investment. That is because, unlike foreign income, domestic income is subject to both federal and state tax before being paid out as a dividend. The provision could thus have an effect opposite from that intended.

The dividend and royalty exclusion might well also result in an increased effective tax burden on purely domestic and small businesses. That is because these taxpayers are taxed on 100% of their federal tax base while the larger taxpayers with multinational operations will be taxed on less than 100% of their federal tax base. Smaller established Alaska businesses would not receive this tax break.

Multinational corporations have the opportunity to arbitrarily shift income between jurisdictions under all accounting methods other than the worldwide combined reporting method. Under the Internal Revenue Code, Sec. 482 is designed to prevent that shifting of income. A copy of Sec. 482 is attached as Exhibit A. This section is designed to determine if related parties have charged an arm's length price. An October 18, 1988 Treasury discussion draft on "A Study of Intercompany Pricing" concludes that 482 pricing audits require large commitments of audit resources. The California experience certainly affirms that observation. See Exhibit B. A move to water's edge will mean application of 482 in Alaska audits. Therefore, a change to water's edge will require substantial additional staff to administer.

According to a report to the Commissioner of Internal Revenue and the Assistant Attorney General by the Special Counsel for International Taxation on January 12, 1981, the provisions of the tax law applicable to international transactions, and specifically Sec. 482, are among the most complex in the Internal Revenue Code and are among the most difficult to administer. See Exhibit C. In 1990, the House Ways and Means Oversight Subcommittee held hearings on Sec. 482 and the problem of federal tax avoidance due to transfer pricing. Testimony indicated potential underpayment of federal taxes as high as \$50 billion. A former IRS auditor testified that obtaining appropriate information was extremely difficult, of little assistance in determining an arm's length price, and that the so-called arm's length standard exists only in a world of "smoke and mirrors" where no one knows what it means and it doesn't work where the market place is controlled. See Exhibit D. That testimony is consistent with the views of a former attorney in the Office of International Tax Counsel of the Treasury Department printed in the February 17, 1986 issue of Tax Notes. See Exhibit E. Further, House Majority Leader Richard Gephardt testified in the hearings that competitiveness suffers when foreign controlled corporations do not pay their fair share of taxes.

A June 8, 1989 Research Report to the Alaska State Legislature (a copy of the report to Research Request 89.165 is attached as Exhibit F) contains the following quote from Montana's director of Revenue:

it struck me that the changes in the tax laws that we've seen now in the last two or three years in a number of

states, moving away from worldwide to water's edge, have served to substantially increase the cost of compliance for both taxpayers and tax agencies. We have reduced the tax base in a number of states, we have moved the states away from uniformity, have shifted the tax burden, and we have looked for an economic boom that has not happened. Therefore, I have to wonder if somewhere down the road, we are going to have to re-invent worldwide unitary.

That statement suggests that despite claims to the contrary, foreign investment is not withheld from a state simply because of tax policy. See Exhibit G. Markets, not tax policy, apparently influence investment. The state has yet to receive any stated commitment to increased jobs and investment in return for a change in the tax policy.

The substantial weight of authority is that taxes do not play a major role in business locational decisions and also are not a major influence on state economic growth. See Exhibits H and I. A nationally recognized expert on job growth, David Burch, a professor at the Massachusetts Institute of Technology, has stated that

"taxes are to economic development what race is to schools. It is irrelevant. The important thing is the quality of the schools. And the quality of economic development is not related to tax policy." See Exhibit J.

Under the circumstances, it would be difficult to justify supporting this legislation. Action on this legislation should be deferred until further study is performed to determine the validity of the assumption that water's edge will promote investment and trade in Alaska. That is a question the administration is interested in pursuing. However, at present we are skeptical and certainly not convinced there is anything to be gained by changing from worldwide to the water's edge.

Further, the expressed policy of the administration is to reduce the size of government. This legislation would be counter to that policy because of the additional cost to the state to administer the income tax provisions under water's edge as compared to worldwide combination. We must be convinced before we can support this legislation that other factors, such as increased investment and employment opportunities as a direct result of the legislation, will offset the revenue losses and the increase to the cost of state government.



ALASKA STATE LEGISLATURE
HOUSE OF REPRESENTATIVES
RESEARCH AGENCY

P.O. Box Y, State Capitol
Juneau, Alaska 99811-3100
Mail Stop 3100
(907) 465-3991

June 8, 1989

MEMORANDUM

TO:

ATTN:

FROM: Ginny Fay
Legislative Analyst

RE: Alaska's Unitary Corporate Taxation: Alternatives and Impacts on Revenues
Research Request 89.165

You requested information on 1) unitary corporate tax laws in Alaska and other states, 2) alternatives to the method of tax collection currently used in Alaska, and 3) the source of Alaska's revenues and impacts on these revenues of changing Alaska's tax law. Specifically, you asked this agency to update House Research Agency Memoranda 85.012, 85.014, and 85.047. To answer your questions, the first part of this memorandum provides an overview of state corporate taxation. This is followed by information on alternative tax methods. The final section identifies sources of Alaska revenues and the potential impact on revenues of changes to Alaska's corporate tax method.

Background

The form of corporate taxation commonly known as unitary tax is based on the concept that the most equitable and efficient method of determining corporate income subject to state taxation is formula apportionment. Under unitary taxation, the total income of a corporation or of an affiliated group of corporations engaged in a unitary (related) business activity is apportioned among states, usually based on the portion of corporate payroll, property, and sales attributable to each state. This apportioned income is the taxable income subject to the respective state's tax rates. Approximately 45 states (including the District of Columbia) currently use some form of the unitary tax to apportion corporate income for state income tax purposes. Alaska currently taxes corporate income by using a form of the unitary tax called worldwide combined reporting.

June 8, 1989

Page 3

double taxation because this income is taxed by foreign governments. Foreign multinational corporations have been especially vocal in their criticism of worldwide combined reporting.

Alternatives to Worldwide Combined Reporting

In 1984, eleven states used worldwide combined reporting. As a result of federal government opposition and the threats of economic reprisal by foreign corporations, ten states have changed taxing methods. The degree to which states have backed-off taxing foreign income varies considerably as a result of inconsistency in states' definitions of "waters edge." Alternatives to worldwide combined reporting include:

- worldwide combined reporting for domestic corporations with an alternative tax levied on foreign multinational corporations;
- a waters edge method that includes foreign source dividends in taxable income and includes 80/20 corporations within the definition of waters edge;⁴
- a waters edge method that excludes foreign source dividends from income and excludes 80/20 corporations from the definition of waters edge; and
- separate accounting.

Worldwide Combined Reporting that Excludes Foreign Multinationals. This alternative allows United States subsidiaries of foreign corporations to pay an alternative tax rather than a tax based on income apportioned using worldwide combined reporting. Although many types of alternate taxes could be devised, state representatives on the 1984 unitary tax task force recommended that the tax be based on in-state property, payroll, and sales and that the tax rate be based on the tax paid by firms in the same industry conducting unitary business in the state.

Proponents of this option claim that it would reduce the threat of foreign retaliation against U.S. corporations. In addition, this option is claimed to be a fair way to exclude foreign multinational corporations from worldwide combined reporting while protecting the competitive advantage of U.S. multinational corporations and domestic business. This option would also protect state revenues and be relatively easy to implement. Opponents, however, do not view this alternative as an adequate alternative to worldwide combined reporting because corporate income tax rates based on industry

⁴These corporations are U.S. based corporations that have 80 percent or more of their business activity occurring outside of the United States.

Separate Accounting. This alternative to worldwide combined reporting would completely eliminate the use of the unitary tax. States would tax corporate taxpayers only on the income earned in the state and each corporation would be treated as a separate entity for tax purposes (as opposed to a unitary group). This method is also called "arm's length accounting" because all transactions between related corporations are assumed to occur as if no special relationships exist (such as a subsidiary corporation supplying a parent corporation) so that prices are fair market values.

In general, business leaders would like to have all states determine taxable income by using separate accounting because it uses information directly related to traditional accounting income. Opponents, which include many states, claim separate accounting makes states vulnerable to manipulation of income to reduce tax liabilities by corporations that do business in more than one state. However, under the separate accounting method Alaska imposed on the petroleum industry under AS 43.21, revenues from the corporate income tax were considerably higher than under either the standard apportionment formula applied before 1977 or the modified formula used after 1981.⁵

Attachment A provides information on how states using the waters edge unitary approach to corporate taxation treat foreign-source dividends (i.e., the first three alternatives discussed above). In summary, California's approach best represents the first option of providing an alternative tax to foreign multinational corporations. Another ten states would fit under the second option which taxes foreign-source dividends. Nine states partially exempt foreign dividends; 14 fully exempt foreign dividends; and 11 fully exempt dividends if a corporation meets specified conditions, i.e., 34 states' corporate taxation method is similar to the third option.

Alaska Revenue Sources and Relationship to Unitary Taxation

The revenues that the State of Alaska collects fall into one of three categories:

- **unrestricted revenues** go to the general fund to be appropriated for any purpose,
- **restricted revenues** are received for specific purposes, and
- **special fund revenues** are received by statutorily established funds such as the International Airport Fund.

⁵For information on the formulas used for corporate taxation in Alaska, see House Research Memoranda 85.012 and 89.303.

Table 2 provides a breakdown of unrestricted revenue by source. As mentioned previously, unrestricted revenues are the only source that allow legislative discretion in appropriation.

TABLE 2
SOURCES OF UNRESTRICTED REVENUES, FY 88
(Millions of Dollars)

REVENUE SOURCE	REVENUE	PERCENT OF TOTAL
Corporate Income Tax	\$181.4	7.9
Gross Receipts Tax	58.5	2.5
Severance Tax	818.7	35.5
Property Tax	96.2	4.2
Sale/Use Tax	51.8	2.2
Licenses and Permits	28.3	1.2
Intergovernmental Receipts	8.9	0.4
State Resource Revenues ^a	843.9	36.6
Facilities Related	32.3	1.4
Service Related	7.5	0.3
Other	16.4	0.7
Special Settlements ^b	161.9	7.0
TOTAL	\$2,305.8	100.0

^aIncludes \$694.8 million in royalty income, \$132.6 in investment earnings, and \$6.0 million in rents. Petroleum resource revenues are shown in more detail in Table 3.

^bOuter Continental Shelf "8(g)" or Dinkum Sands settlement partial payment.

Sources: Alaska Department of Revenue, "Revenue Sources," Fall 1988.

Table 2 indicates that the largest contributions to state unrestricted income are derived from petroleum producers. In fact, the various petroleum revenues account for 85 percent of all state unrestricted revenues--this proportion has not changed since our earlier memorandum on FY 83 revenues.

June 8, 1989

Page 9

Salmon enhancement taxes (AS 43.75) are levied on limited entry fishing permit holders within qualified regional aquaculture associations. Rates are two or three percent of the value of the salmon caught, depending on the vote of the aquaculture association. In FY 88, total Salmon Enhancement Tax receipts were \$5.8 million. In effect, this is a pass-through program, since the legislature appropriates these tax revenues to the regional associations from whose members they were collected.

A **seafood marketing tax** (AS 16.51) is levied on seafood processors at a rate of 0.3 percent of the ex-vessel value of seafood products purchased (over \$50,000) in Alaska. Revenue in FY 88 was \$2.7 million. Similar to the Salmon Enhancement Tax, these revenues are passed through to fund the Alaska Seafood Marketing Institute (ASMI).

Insurance premium taxes (AS 21.09, AS 21.33, AS 21.34, and AS 23.33) are levied on gross premiums (less certain deductibles) at various rates ranging from 0.075 to 3 percent depending on the type of insurance. In FY 88, revenue from these taxes totaled \$25.6 million.

Severance Taxes. Oil production taxes are levied upon oil producers for all oil produced from each lease or property in the state, less any part of production exempt from taxation (AS 43.55). The tax is 15 percent of gross value (except 12.25 percent for the five-year period following commencement of new oil production after June 30, 1981) adjusted by the Economic Limit Factor (ELF) for mature oil fields. The ELF, however, was repealed effective January 1, 1989.⁶ Gross value is calculated as the sales price minus transportation costs at the point of production. Gas production taxes (AS 43.55) are levied at the greater of a rate of \$0.64 per thousand cubic feet of taxable gas or ten percent of the gross value of taxable production calculated at the point of production, multiplied by the ELF. During FY 88, \$816.4 million was collected in oil and gas production tax revenues.

The **oil and gas regulation and conservation tax** (AS 43.57) is levied upon oil and gas producers at the rate of four mills per barrel (oil) and four mills per 50,000 cubic feet (gas) of oil and gas removed or sold from each lease or property in the state,

less any tax exemptions. Gross value is calculated as for the production taxes. This tax contributed \$2.3 million to state revenues in FY 88.

Property Taxes. The oil and gas property tax (AS 43.56) is levied at 20 mills on the full and true value of taxable property used in oil and gas production and exploration. If a municipality levies a property tax against the same

⁶The actual effective date on HB 118, Chapter 25 SLA 89, is August 6, 1989, with a retroactive effective date of January 1, 1989. The ELF, however, was in place during FY 88.

June 8, 1989

Page 11

State Resource Revenues. State royalty payments (AS 38.05) include royalties from minerals and oil and gas. Depending on the type of resource, royalty payments can be taken in kind. Revenues from royalties are apportioned between the permanent fund and the general fund. General fund royalty revenues totaled \$694.8 million in FY 88.

Other revenue sources within this category are state property sales (\$3.8 million), resource bonus sales (\$5.6 million), state rental revenues (\$6.0 million), and the sale of resources not classified as minerals such as gravel and timber (\$1.1 million).

Facilities-related charges include receipts from airports, the ferry system, food services, and other state facilities. These charges totaled \$32.3 million in FY 88.

Service-related charges include receipts from statutory inspection fees, the court system, and other state service charges. These fees totaled \$7.5 million in FY 88. Another \$16.4 million was collected in miscellaneous revenues.

During FY 88, a special settlement of \$161.9 million was paid to the general fund. The money was 49.5 percent of the \$322.9 million Outer Continental Shelf (OCS) "8(g)" or Dinkum Sands revenue sharing settlement. Fifty percent of the settlement was paid to the Permanent Fund and 0.5 percent to the Public School Fund. The FY 88 figure also reflects \$2.1 million in TransAlaska Pipeline Settlement (TAPS) receipts owed to the general fund.

Revenue Implications of Changing Alaska's Corporate Income Tax

While a recent U.S. Supreme Court case, *Shell Oil Company v. Iowa Department of Revenue*, upheld states' use of unitary tax apportionment to calculate taxes owed by multistate and multinational corporations, the determination of a consistent form of the unitary tax still remains to be decided.⁷ There are two significant cases whose outcomes are likely to affect Alaska's use of worldwide combined reporting.

In the first case, the U.S. Supreme Court has agreed to decide *Franchise Tax Board of the State of California v. Alcan Aluminum* (No. 88-1400). The hearing for Alcan, a Canadian company, is to determine whether the firm has standing to sue in federal courts over disputed taxes. If the plaintiff prevails, the case will likely go back to lower courts. In this case, Alcan is challenging California's relatively recent changes in corporate taxation. Under pressure from foreign firms, California legislators moved to repeal their worldwide

⁷"Supreme Court Approves State's Unitary Tax," *Oil & Gas Journal*, November 14, 1988, p. 30, and "Iowa Wins Tax Fight with Shell," *Governing*, January 1989, p. 15.

a number of states, we have moved the states away from uniformity, have shifted the tax burden, and we have looked for an economic boom that has not happened. Therefore, I have to wonder if somewhere down the road, we are going to have to re-invent worldwide unitary.

This conclusion is confirmed by surveys that indicate that state tax treatment is, at best, ranked fourth among corporate factors regarding the location of manufacturing plants in the U.S.¹⁰ A foreign corporation that wishes to invest in a state by constructing a manufacturing plant will try to find a location that offers cheap land and utilities, a skilled labor force, low living costs, and cheap access to suppliers and markets. As long as the particular location can offer these basic benefits, one location is not very different from another. It is this inter-changeability that makes states fearful of foreign threats of economic reprisal.

Foreign corporations that wish to invest in resource extraction have a more limited choice; they must go to the resource location. Because it is so expensive to do business in Alaska, foreign investments are usually relatively large in scale and have high potential profitability to offset the high cost and risks. In this investment climate, the type of taxes levied by a state are probably a secondary consideration.

A related question is the impact of worldwide combined reporting in deterring the development of Alaska as a manufacturing state. It seems unlikely that Alaska will be able to compete in the near future with other states for manufacturing that does not depend on natural resources. Alaska would have trouble competing with other locations based on the criteria mentioned above.

Federal Action to Ban the Use of Worldwide Combined Reporting. It is quite clear that the federal government opposes the use of worldwide combined reporting. At this point, however, there is little action to ban worldwide combined reporting because all states except Alaska have moved to waters edge taxation.

U.S. Supreme Court Action. As mentioned previously, the next chapter on the application of unitary taxation is likely to be written by the U.S. Supreme Court. Based on the outcome of current lawsuits, Alaska may have little choice but to change its corporate tax law.

¹⁰Larry C. Ledebur and William W. Hamilton, "The Failure of Tax Concessions as Economic Development Incentives," in *Reforming State Tax Systems*, ed., Steven D. Gold, National Conference of State Legislatures, December 1986. Attachment B is a copy of this article.

June 8, 1989
Page 15

providing equal competitive footing to U.S. multinational corporations--a \$3 to \$4 million cost is relatively low. It should be noted, however, that many states expect increases in personal income tax revenues--resulting from employment growth--and increase in sales tax revenues--from increased economic activity--to offset corporate tax losses. Alaska currently lacks both of these vehicles for offsetting losses.

With no state personal income tax or sales tax, Alaska currently has a very narrow tax base--taxes on the petroleum industry account for 85 percent of unrestricted revenues. The 13 cents per pack cigarette tax increase passed in House Bill 80 during the 1989 legislative session is expected to increase state revenues by approximately \$4 million annually--enough to offset the expected decrease in nonpetroleum corporate income taxes. Similarly, repeal of the ELF is expected to result in an annual increase in state revenues of over \$150 million. Reinstating the personal income tax at about 1.9 percent would raise about \$217 million annually in revenue and a one percent state sales tax would raise \$49 million annually. Therefore, because of the options available to offset any tax losses, modification of the state corporate income tax is more a public policy question than a revenue question.

* * *

I hope this answers your questions. If you would like additional information, please do not hesitate to call.

Attachments

ATTACHMENT A
State Treatment of Foreign-Source Dividends

STATE TREATMENT OF FOREIGN-SOURCE DIVIDENDS
Jean A. Walker, Committee on State Taxation

	Exempt	Exemption Conditional	Partial	Treatment of Balance		Statute(s)
				Allocate	Apportion	
ALABAMA				X		§440-18-36, 40-18-36(14), Reg. 810-3-31.02
ARIZONA	X					§43-1122(d), L. 1986, c. 109, eff. for taxable years beginning from/after 12-31-83
ARKANSAS		If 95% ownership of payor.			X	§84-2008(2)(j)
CALIFORNIA 1)		If more than 50% ownership of payor, 75% exclusion of base period dividends (greatest amount of dividends received in any one of 1984, 1985 or 1986 income years); exclusion of foreign dividends in excess of base period amount dependent upon increase or decrease in foreign payroll factor.			X	§524271, 24402
2)					X	§24411, L. 1986, c. 680, eff. for tax years beginning on/after 1-1-88
COLORADO			Amount of exclusion of all foreign-source income dependent upon election of federal foreign tax deduction or credit.	X		§29-22-304, §29-22-305(10); L. 1985, H. 3010, eff. for tax years beginning on/after 1-1-86
CONNECTICUT	X					§12-217(d)(D)
DELAWARE	X					§1903(a)(2)
FLORIDA	X					§220.13(1)(b)2.a, ch. 64-549, Laws of Florida, eff. for tax years beginning on/after 9-1-84
GEORGIA	X					§40-7-21(b)(9)
HAWAII				X		§236.7(c)
IDaho 1)			85% exclusion.	X		§43-3022
2)				X		§43-3027, L. 1986, c. 342 (HB 669), eff. for tax years beginning 1-1-88
ILLINOIS		If 80% ownership of payor.	Otherwise, 85% exclusion.	X		§2-208(b)(2)(D), L. 1982, P.A. 82-1029, eff. for taxable years ending on/after 12-31-82
INDIANA 1)		If 80% ownership of payor.	Otherwise, 85% exclusion if ownership of payor is less than 80% but at least 50%, or 50% exclusion if less than 50% ownership of payor.	X		§43-3027, L. 1987, P.L. 383, eff. for taxable years beginning after 12-31-87
2)				X		
IOWA				X		§422-35
KANSAS 1)			80% exclusion.	X		§79-32, 138
2)				X		§79-32, 138(c)(vi), L. 1987, c. 306, eff. for taxable years beginning after 12-31-87
KENTUCKY	X					§141.010(12)(b)
LOUISIANA				X		§542.A, 63, 242(1)(d), 243.A(4)

	Exemption			Treatment of Balance		Statute(s)
	Exempt	Conditional	Partial	Allocate	Apportion	
RHODE ISLAND SOUTH CAROLINA1)		If 80% ownership of payor.		X	X	§§44-11-11, 44-11-12 §12-7-700(15) repealed L. 1985, S351, eff. for tax years beginning after 12-31-84; §12-7-1120(2)
2)				X		§§12-7-415, 12-7-430 added L. 1985, S351, eff. for tax years beginning after 12-31-84; §12-7-1120(2)
TENNESSEE UTAH		If 80% ownership of payor.	50% exclusion.		X	§§7-2704(b)(2)(A) §§9-12-8(2)(d), L. 1984, c. 80 (§§ 30), eff. for tax years beginning on or after 7-1-85
VERMONT VIRGINIA WEST VIRGINIA 1) X		If 50% ownership of payor.		X		§§11(10) §§10-211, 102(1), §§151-157 §11-24-6(c)(3), L. 1985, S351, 1987 added to §11-24-6(c)(3) beginning before 7-1-87
2) 3) X						§§11-24-6, 11-24-7(d)(3) §11-24-6(c)(10), L. 1986, HB 4475, eff. for taxable years ending after 7-1-88
WISCONSIN DISTRICT OF COLUMBIA		If 80% ownership of payor.		X	X	§71-04(4) §47-1810.1
<u>Worldwide Combination States*</u>						
ALASKA						§41-20-030

*Dividends between combined corporations are eliminated from income, thus the indicated treatment of dividends is only to dividends received by members of the combined group from corporations not included in the combination.

RECEIVED
ALASKA DEPARTMENT OF REVENUE

MEMORANDUM

JAN 28 1991

STATE OF ALASKA

DEPARTMENT OF REVENUE

COMMISSIONER'S OFFICE

TO: Lee Fisher
Commissioner
Department of Revenue

DATE: January 28, 1991

FILE NO:

TELEPHONE NO: 465-2343

SUBJECT: Constitutionality
of Worldwide Combined
Reporting-The Barclays
Case-Some Thoughts.

FROM: Carl Meyer *Carl*
Acting Director
Income and Excise Audit Division

This memorandum is in response to your request of January 23 for an overview addressing, among other things, the constitutionality of the worldwide combined reporting method as recently viewed by two lower courts in California and the impact on the state in the event the method would ultimately be declared unconstitutional by the United States Supreme Court. Before addressing these matters, however, a brief description of the so-called "unitary tax" concept is appropriate.

The term "unitary tax" is actually a misnomer. A tax is not imposed upon the unitary business nor upon all the corporations included within the unitary business. The tax can only be imposed on those corporations having a taxable presence in the state and the tax must be designed to reach only those profits earned within the state. Earth Resources v. Alaska, Dept. of Revenue, 665 P.2d 960 (Alaska 1983).

The unitary concept actually focuses on the nature of the business activities of one or more corporations. A factual inquiry is necessary to determine the parameters of a unitary business. Once the facts have been established, the sufficiency of those facts to establish a unitary business is a question of law. A business is considered unitary if it is characterized as having the attributes of functional integration, centralization of management, and economies of scale. Essentially, this means there must exist a flow of value within the business. Container Corp. of America v. Franchise Tax Board, 463 U.S. 159 (1983).

Once the unitary business has been identified, various accounting methods may then be applied to determine the income earned or attributed to those corporations with a presence in the state. The accounting methods applicable to unitary businesses include worldwide combination and water's edge combination. There can be unique variations to each of the methods. It has been held that the linchpin of apportionability in the field of state income taxation is the unitary business principle.

Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980). The courts and legal scholars have generally favored apportionment. However, while separate accounting is not constitutionally required, it is a permissible state method. Atlantic Richfield Company v. State Department of Revenue, 705 P.2d 418 (Alaska 1985).

Separate accounting disregards the unitary business in its entirety. The difference between an arms length/separate accounting method and the unitary method is that the latter focuses upon the extent of business activity in a state while the former ignores business activity and focuses upon the precise geographic source for the generation of the income. Because of the transactional nature of the focus under separate accounting, it is subject to much manipulation by taxpayers. Administratively, separate accounting is much more difficult and time consuming to audit and administer.

Alaska still requires worldwide combination. Worldwide combination is also required in California although a taxpayer can elect water's edge. A taxpayer in California must pay an election fee to escape worldwide combination. Since 1983, Arizona, Colorado, Oregon, North Dakota, Utah, Montana, Florida, Indiana, New Hampshire, and Idaho have also moved from worldwide to water's edge. Like California, however, North Dakota, Montana, Utah, and Idaho also place restraints or conditions on the water's edge election.

The United States Constitution imposes various requirements or preconditions on the authority of a state to impose a tax on a multistate or multinational business enterprise. See Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977). The first of these requirements is a nexus standard; that is, there must exist a minimal connection between the activities outside the state with those inside the state. Nexus is generally supplied when a taxpayer avails itself of the substantial privilege of carrying on business within a state. Wisconsin v. J.C. Penney, 311 U.S. 435, 444 (1940).

The second requirement is that there be a rational relationship between the income attributed to the state and the intrastate values of the enterprise. Basically, all that is required is that the measure of the tax be reasonably related to the extent of a taxpayers contact with the state. See Commonwealth Edison v. Montana, 453 U.S. 609 (1981).

The third requirement is that the tax be fairly apportioned. The fact that the apportionment formula looks to affairs outside the state in valuing the instate activity does not destroy the validity of the tax. The tax is fairly apportioned if the formula is designed to reach only those profits measured by approximating the income that is reasonably related to the instate activities. Wallace v. Hines, 253 U.S. 66 (1920); Sjong v. State Department of Revenue, 622 P.2d 967 (Alaska 1981).

The last requirement is designed to prohibit states from

discriminating against interstate commerce through the establishment of economic barriers against competition with the products of another state or the labor of its citizens. See Hughes v. Alexandria Scrap Corp., 426 U.S. 794 (1976). The Alaska Supreme Court has determined that the standard three factor apportionment formula does not violate these constitutional provisions. See Earth Resources Company of Alaska v. State, Department of Revenue, *supra*.

Additionally, in the context of foreign commerce, two additional constitutional tests have evolved. First, the tax must not create a substantial risk of international multiple taxation. Second, the tax must not impair federal uniformity in an area where federal uniformity is essential by preventing the United States from "speaking with one voice" in regulating foreign trade. Japan Line, Ltd. v. County of Los Angeles, 441 U.S. 434 (1979). Courts in California have held that it is these constitutional tests that preclude the use of worldwide combined reporting. See Barclays Bank International Limited v. Franchise Tax Board, Court of Appeal, Third Appellate District (Sacramento), November 30, 1990; Colgate-Palmolive Co. v. Franchise Tax Board, Superior Court (Sacramento), December 12, 1988).

The Barclays case involves a foreign parent corporation with a foreign subsidiary doing business in California directly and through a California subsidiary corporation. California required the foreign parent and all the foreign subsidiaries to be included in a worldwide combined report. The California Court, in rejecting the application of worldwide reporting as applied to foreign parents, held:

On this record we feel confident in saying that the executive branch has spoken clearly. Through that branch, the policy of the United States since the (worldwide combined reporting) problem in the present context arose in the 1970's has been established; (Worldwide combined reporting) is not to be applied to foreign based corporate groups--those groups are to be taxed by the states only on income derived from the United States.

In Colgate-Palmolive, the taxpayer is a United States corporation engaged in business in California. In addition, the taxpayer owns a controlling interest in 75 foreign subsidiaries. California required that the foreign subsidiaries, none of which were engaged in business in California, were to be included in the worldwide combined report of the taxpayer for California tax purposes. The trial court held that worldwide combined reporting as applied to domestic multinationals was unconstitutional:

I find that the executive branch of the federal government has clearly expressed a federal policy supporting the principle of water's edge taxation of multinational corporations and disapproving the world-wide unitary method. Thus, inescapably, defendant's unitary method of taxation of multinational corporations

impermissibly interferes with the federal government's power to conduct foreign commerce and is thus unconstitutional.

Therefore, for California purposes Barclays represents a victory for taxpayers with foreign parents while Colgate-Palmolive represents a victory for taxpayers with domestic parents. If the underlying rationale of the cases is correct and sustained by the United States Supreme Court on the constitutional grounds, the combination of the two cases would certainly result in the instant death of the worldwide combined reporting method. However, there is no compelling reason to believe the Court would reverse its prior decisions so readily. The combination of the two California cases results in holding form over substance and places domestic corporations at a severe competitive disadvantage. Robert Horton, the Chairman of British Petroleum, stated that:

. . . we are officially a foreign company. But actually, we are no more foreign than IBM, when you think about it. . . We have more American employees than we have any other nationality. Most of us have spent a lot of our career working overseas. We produce more crude oil than any other American company. And the fact that we are registered in London is a historical accident.

CNN Moneyline, May 14, 1990.

Thus, there are compelling reasons and arguments to counter the California cases. The war is certainly not over. Furthermore, the California decisions may likely reflect unstated but understood state policy concerns that would not exist in states such as Alaska.

The opinions expressed by taxpayers and others lead me to believe the California Supreme Court will not grant review of the Barclays decision. Perhaps that is based on the backlog in docketed cases before that Court or because of the view the United States Supreme Court will decide the case eventually in any event. Therefore, the case might well move next on certiorari to the United States Supreme Court. In that event, and assuming the Court grants the cert, a decision could be handed down in 1992.

It is important to note, as mentioned above, that the United States Supreme Court in Container Corp. of America v. Franchise Tax Bd., 463 U.S. 159 (1983), held that there was no constitutional bar to application of world-wide combination to a multinational group of corporations engaged in a unitary business in the state, at least where the parent of the group was a domestic corporation. The Court found no foreign commerce problem on the basis that the "tax here falls, not on the foreign owners of an instrumentality of foreign commerce, but on a corporation domiciled and headquartered in the United States." The implication of Container, at least as argued by some, is that worldwide combination involving foreign parents is precluded under the Commerce Clause. Barclays reflects that implication. However, it would be premature to assume the United States Supreme Court will embrace the

Barclays decision.

Colgate-Palmolive goes further that Barclays and is opposite to the Container decision. Yet, it distinguishes Container based on the fact that the position of the federal government had not been made clear in that case. The federal government did not file an amicus curiae brief in the Container case. Colgate-Palmolive found that "the position of the executive branch of the federal government is now crystal clear" and "the President of the United States instructed the Secretary of the Treasury to pursue through legislation and the Attorney General to pursue through litigation, the federal policy that multinational corporations be taxed by states only on income derived from the United States and not on income derived from foreign subsidiaries, i.e. the unitary method." The Court found no distinction between foreign and domestic parents by the federal executive.

Alaska has aggressively applied the worldwide combined reporting method for the last 15 years. It goes without saying that California decisions have no precedential weight in Alaska. However, for the sake of argument and assuming the method is determined to be unconstitutional, the impact would essentially be in two areas. First, potential contingent liabilities for refunds. Second, a mandated change to the statutory tax reporting method.

The determination of whether a constitutional decision of the United States Supreme Court is retroactive is a matter of federal law. See Great Northern R. Co. v. Sunburst Oil & Refining Co., 287 U.S. 358 (1932); Chapman v. California, 386 U.S. 18 (1967). Of course, state courts must make the initial inquiry of determining appropriate relief. See American Trucking Associations, Inc. v. Scheiner, 483 U.S. 266 (1987).

In Chevron Oil Co. v. Huson, 404 U.S. 97 (1971), the United States Supreme Court established a three prong test in determining whether a decision of the Court is retroactive. The first prong concerns whether the decision establishes a new principal of law, either by overruling clear past precedent on which litigants have relied, or by deciding an issue of first impression whose resolution was not clearly foreshadowed. The second prong focuses upon whether the Commerce Clause dictates retroactive application of the decision to deter future violations by states. The third prong analyzes whether retroactive application would produce substantial inequitable results.

It is certainly arguable that a decision finding worldwide combination to be unconstitutional would meet the Chevron test for nonretroactivity. The last word from the United States Supreme Court, at least with respect to domestic parents, is that worldwide combination is constitutional. See Container, *supra*. Further, since the Commerce Clause does not prohibit legitimate state taxation of interstate or foreign commerce, and worldwide combination is consistent with legitimate

state taxation as evidenced by the Court's prior decisions, the Commerce Clause would not appear to dictate retroactive application abstractly to deter potential future free trade violations. Lastly, it would seem to be unjust and inequitable to penalize the state for relying on past precedents.

Nevertheless, where a state can foresee the invalidation of its law, there is little merit to reliance on past precedents. See McKesson Corporation v. Florida, ___ U.S. ___ (1990). The reservation of the foreign parent situation in Container, coupled with the federal executive's communication to the states of the federal policy concerns with worldwide combination, could arguably be viewed as giving the states an indication that the system would be invalidated. There are other recent cases involving unrelated issues that have addressed the retroactivity problem. See American Trucking Associations, Inc. v. Smith, ___ U.S. ___ (1990); Ashland Oil, Inc. v. West Virginia, ___ U.S. ___ (1990); National Mines Corporation v. West Virginia, ___ U.S. ___ (1990); Ragsdale v. Oregon Department of Revenue, ___ P.2d ___ (Oregon 1990).

Regardless of the federally mandated result on the retroactivity issue, state law likely would allow refunds to many taxpayers in any event. AS 43.05.275 allows refund claims to be filed within three years from the date the tax return is filed or two years from the date the tax is paid, whichever is later. Since virtually all taxpayers that are in appeal statuses have not yet paid the additional assessments, the taxpayers at a minimum could seek an offset against the additional assessment. Most taxpayers, however, have already raised the constitutional issue in the protest and made it a direct issue to be resolved in the administrative appeal process. Thus, there would be no requirement for these taxpayers to file a refund claim.

The statute of limitations for closed audit cases should preclude refunds to those taxpayers. Similarly, refunds would not be appropriate to taxpayers that have entered into settlement agreements. This is a two way street since worldwide combination may have been favorable to individual taxpayers.

The second impact is that a decision invalidating worldwide combination would require the application of some other method. While it is clear that there is currently no statutory "backstop" provision to fill the void, and considering that the Alaska statutes specifically require "worldwide" factors, it might be reasonable to assume that a contraction of the worldwide method to the United States water's edge would be acceptable to the courts. That cannot be a certainty, however, and the worst case scenario is that there would be no tax method in place to apply to the oil and gas companies.

Perhaps another scenario is that the Department would be free to use any appropriate method. For instance, separate accounting was stated by

the legislature to be the preferred method in 1981 for oil and gas companies but was abandoned due to the fear of the constitutional challenge to that method and the devastating impact on the budget refunds would have. However, separate accounting requires a much different approach than the worldwide method found in AS 43.20. During the separate accounting years, those unique provisions were contained in AS 43.21. Because of the great differences between combination and separate accounting, it is more reasonable to believe that some form of combination would be preferred by the courts over separate accounting.

There are no definitive numbers available to quantify the revenue impact between worldwide and water's edge combinations. However, it was estimated last session that revenues would be reduced by approximately \$3 million dollars each year by moving all non-oil and gas corporations to the water's edge. We believe the revenue impact each year for oil and gas corporations would run well into the hundreds of millions of dollars. Conversely, we believe separate accounting would result in increased revenues in the near term and decreased revenues in later years.

The 1981 legislature enacted modified apportionment on a worldwide basis based on the fact it, combined with an increase in the severance tax rate, would generate total revenue equal to those then generated under separate accounting. That did not materialize for various reasons and revenues were substantially less than anticipated. The legislature also envisioned the modified apportionment system would be constitutional. If in the worst case scenario neither of these legislative assumptions are correct, the oil and gas taxpayers have no legitimate complaint to an effort by the state to rectify the problem. Historical data establishes that they have reaped significant benefits.

Therefore, and for all the reasons expressed in the foregoing paragraphs, strategies such as backstop legislation could be considered at this time. However, caution must be exercised before any changes to the current statutory scheme are recommended. The California cases are certainly there, but their underlying validity has yet to be tested by either the Alaska Supreme Court or the United States Supreme Court. It would be a serious mistake to automatically accept the basis of the California decisions as constituting a correct interpretation of the federal constitutional provisions.

Correspondingly, and with respect to the question whether fiscal incentives or taxes play a major part in attracting increased state investment, your intention to schedule a meeting on the unitary tax issues with the Department of Trade and Economic Development and their Division of International Trade is a very good approach. Perhaps the Department of Law might also be included for their view of the legal climate.

I am not aware of any empirical evidence that establishes tax methods have any significant impact on business location decisions. In

Commissioner Lee Fisher
January 25, 1991
Page 8

fact, the studies generally conclude that taxes and tax policy, with one possible exception, are not a major influence on state economic growth. The one exception might be that a fiscal climate of stability, predictability, and uniformity is more likely to attract business—regardless of the taxes and tax methods in place in a state. For that reason, the burden of proof for using tax policy to stimulate growth generally rests with those who advocate a change. Otherwise a change, even should it reduce state revenue in favor of the taxpaying population, could have precisely the opposite result than was contemplated.

I am available at your convenience should you desire to discuss further any of the matters addressed in this memorandum.

cc: William E. Floerchinger

A PERSPECTIVE
OF
UNITARY TAX REFORM

BY: THE IBM CORPORATION

The unitary principle of taxing multinational corporations has been the most controversial state tax issue of the eighties. This Study examines many of the policy issues which have been part of the unitary tax debate.

There is little consistency between the states in how the unitary principle is applied. Some states, such as New York, use the unitary principle to combine the income and factors of only companies which have "nexus" (are doing business) in the state. Others apply the unitary principle to include in the combination not only companies doing business in the state, but unitary companies which are not doing business in the state. This group either limits the unitary combined group to domestic corporations, or, in the case of Alaska, extends the unitary combination to the worldwide operations of the Corporation.

Worldwide unitary requires a corporation to report its total worldwide income. The worldwide income is apportioned to the state by means of an apportionment formula that uses property, sales, and payroll in the state to property, sales, and payroll worldwide.

The count of states that have historically required worldwide unitary varies, but most commentators have included a dozen states on the list.^{/1} Since the U.S. Supreme Court's decision in *Container Corp. of America vs. Franchise Tax Board*,^{/2} all of these states except Alaska, California, Idaho Montana and North Dakota have totally repealed worldwide unitary. California, Idaho, Montana and North Dakota have enacted legislation partially repealing worldwide unitary by permitting taxpayers to elect "water's edge" (limitation of the unitary combination to domestic corporations). The only state which continues to require worldwide unitary is Alaska.

1. Bureau of National Affairs Daily Tax Report, September 19, 1983, p. G-7 listed 12 states then using worldwide unitary, according to the Multi-state Tax Commission: Alaska, California, Colorado, Florida, Idaho, Indiana, Massachusetts, Montana, New Hampshire, North Dakota, Oregon and Utah.
2. *Container Corp. of America v. Franchise Tax Board*, 103 S. Ct. 2933 (1983). In this decision, the U.S. Supreme Court upheld California's right to impose worldwide unitary on U.S. multinational corporations as discussed later in this paper; however, the continued validity of this decision is open to some serious speculation.

general rule, wages and prices are substantially lower in foreign countries. Due to these lower costs, foreign operations may also be more profitable. When foreign results and foreign factors are included under the unitary method, the inevitable result is distortion. This distortion is compounded by exchange rate fluctuations and different foreign accounting practices. The following example illustrates typical distortion produced by unitary:

TABLE 1.

	SALES -----	PROPERTY -----	PAYROLL -----	INCOME -----	APPORTIONED INCOME -----
DOMESTIC:					
In-State	<u>100</u>	<u>200</u>	<u>120</u>		
Everywhere	1,000	4,000	2,000		
Factor	.10	.05	.06		
Income				40	
Average Factor			.07		
	(equals .07 times income of 110)				2.80
WORLDWIDE:					
In-State	<u>100</u>	<u>200</u>	<u>120</u>		
Everywhere	2,000	6,667	3,000		
Factor	.05	.03	.04		
Income				100	
Average Factor			.04		
	(equals .04 times income of 100)				4.00
DISTORTION					43% ⁴

4. The distortion percentage (43%) is calculated by comparing the difference between the domestic apportioned income and the worldwide apportioned income.

state income taxes include real estate, personal property, payroll, sales, etc. So when business decides not to invest further in a state, the lost revenue to that state is many times the potential income tax.

Just in the last few weeks, California's legislature began considering and almost passed a so-called alternative to worldwide combination. That legislative proposal is deceiving in that it appears to move away from Worldwide Unitary. The deception lies in the fact that the legislation also calls for the taxation of earnings distributed as dividends by foreign subsidiaries after they have already borne full taxation abroad. As I mentioned before, this alternative would increase IBM's tax by 50%. But the legislation's purpose is to provide discriminatory benefits to foreign-owned companies. Foreign multinationals will elect the California alternative to escape worldwide taxation because the dividend approach in the legislation does not negatively affect foreign-owned companies and will reduce their cost of doing business in California. Our foreign competitors will now be able to use California to ship to other states at a competitive advantage over U.S.-owned companies.

Certainly, the approach of the California proposed legislation fails any reasonable man's standard of implementing a fair solution to the problem of taxing foreign income with which the Working Group grappled. For U.S. multinationals like IBM, the California so-called alternative is worthless and would only increase our tax burden. The proposed California legislation would lead to unfair advantage to our foreign-based competitors because combining foreign earnings distributed as dividends in the states' tax base is even more onerous than worldwide combination for U.S. multinationals but results in a decrease in the California tax of foreign multinationals."

Another IBM executive, Ray S. Abuzayyad⁷, commented on the same California proposed legislation that:

"(it) subsidizes failure and penalizes success. Less efficient U.S.-based companies that are losing money abroad can write off those losses in California. In effect, California taxpayers would be forced to subsidize those overseas losses.

Ironically, the proposed bill would penalize success by raising the taxes of those companies that make a positive balance-of-payments contribution to the United States via

7. Ray S. AbuZayyad, President, IBM General Products Division, "Unitary Tax Bill Punishes Success, Subsidizes Failure", San Jose Mercury, August 13, 1985.

Illinois railroad companies. The decision applied the "unit rule" to property physically connected over state lines, allowing the total value of the unit to be allocated to each state by formula. Other decisions expanded the unitary concept and extended it to corporate taxation.^{/10.}

10. Ohio State Auditor, 166 U.S. 185 (1897) applied the Railroad decision to property that was not physically linked.

Underwood Typewriter Co. v. Chamberlain, 245 U.S. 113 (1920) was the first corporate unitary income decision.

Bass, Etc., Ltd. v. State Tax Commission, 266 U.S. 271 (1924) upheld application of the unitary concept to a British corporation doing business in New York.

Hans Rees' Sons, Inc. v. North Carolina, 283 U.S. 123 (1931) restrained the power of the state to apply arbitrary or unreasonable unitary allocations.

Butler Bros. v. McColgan, 315 U.S. 501 (1942) approved California's application of unitary to a corporation operating through divisions in several states.

Edison California Stores, Inc. v. Mc Colgan 183 P.2d 16 (Sup. Ct. Cal. 1947), extended application of the Butler decision to affiliated controlled corporations.

taxpayers threatened with audit by the MTC.^{/13.}

Immediately following the U.S. Steel decision, the MTC undertook extensive multi-state audits of large groups of taxpayers. Many of these audits remain unsettled to this day. Although the MTC contends today that it does not officially endorse worldwide unitary,^{/14.} these earlier assessments in fact were proposed on a worldwide unitary basis. In contrast to the MTC's current position, the Commission adopted the following resolution in May, 1977, which strongly suggested an official MTC position in favor of worldwide unitary: ^{/15.}

"Be it RESOLVED that:

(1) It is the official policy of the Multistate Tax Commission that the unitary business concept is appropriate for attributing income with respect to all businesses affected by the Uniform Division of Income for Tax Purposes Act; and that

(2) It is appropriate on a worldwide as well as a domestic basis regardless of whether the parent or some or all of the

-
13. U.S. Steel, Standard Brands Inc., General Mills, Inc. and the Procter & Gamble Distributing Co. filed the action. Bethlehem Steel Corp., Bristol Myers Co., Eltra Corp., Goodyear Tire & Rubber Co., Green Giant Co., International Business Machines Corp., International Harvester Co., International Paper Co., International Telephone & Telegraph Corp., McGraw Hill, Inc., NL Industries, Inc., Union Carbide Corp., and Xerox Corp. intervened as plaintiffs. IBM and Xerox withdrew as intervenor plaintiffs before decision.
14. Gene Corrigan, first Executive Director of the MTC, and later General and Executive Counsel until leaving the MTC in January, 1989, stated in "A Final Review", published in MTC Review, March 1989, that "(F)rom the beginning, I advocated combined reporting along lines previously established by California and Oregon. EVEN THOUGH THE MTC NEVER TOOK AN OFFICIAL POSITION ON THE SUBJECT, most of its member States supported that approach." (emphasis added).
15. Jerome R. Hellerstein, State Taxation, Warren, Gorham & Lamont, (1983), Chapter 8.10[7], footnote 252.

The states obviously were concerned by what they considered federal intrusion into state's prerogatives^{/18}.

The estimated revenue affect for the three states was \$40 million. The quid pro quo from U.K. was \$375 million under the U.K. ACT.^{/19} A spokesman for the British Embassy told Tax Notes^{/20} that he could not pinpoint the course of action that Britain would take toward the Senate reservation. That course ultimately proved to be the U.K. retaliation threats which propelled unitary reform and which are now central to the issues on appeal in the Colgate case.

During the Senate debate on the U.K. Treaty, Governor Jerry Brown of California "threw the state lobbyists into high dungeon" by writing the Senate Foreign Relations Committee to support the worldwide unitary prohibition. The California Franchise Tax Board continued to oppose Article 9(4) of the treaty, but both California senators supported it including the worldwide unitary prohibition. Oregon and Alaska senators opposed Article 9(4).^{/21}

-
18. Ironically, however, a recent decision from a California superior court ruled that application of worldwide unitary principles to domestic multinational corporations violates the U.S. Constitution because worldwide unitary involves impermissible intrusion by states into U.S. foreign policy. Colgate-Palmolive Co. v. Franchise Tax Bd., California Superior Court No. 319715 (1988). This decision is currently being appealed to the California Courts of Appeals.
 19. ACT (Advance Corporation Tax) was designed to eliminate double taxation of American investors in the U.K.
 20. "Senate Reserves Article 9(4), "Tax Notes", July 3, 1978
 21. U.K. Treaty: Whose Horses Got Traded?, Tax Notes, November 7, 1977, p.9.

question of how far the limits of distortion could be pushed before the tax was overturned.^{/23.}

In the famous footnote 32 of the decision, the court implies that a different result might be reached in the case of a foreign parent^{/24.} and Justice Powell in his dissent speculates that such a tax would be unconstitutional, ultimately invalidating the unitary method for both foreign and domestic multinationals.^{/25.}

-
23. The court found that distortion in Container is 14 percent, "a far cry from the more than 250 percent difference which led us to strike down the State tax in Hans Rees' Sons, Inc., and a figure certainly within the substantial margin of error inherent in any method of attributing income among the components of a unitary business."
24. In distinguishing Container from Japan Lines on the issue of impairment of the Federal government's ability to "speak with one voice" on international trade matters, the court stated in footnote 32 that "we recognize that the fact that the legal incidence of a tax falls on a corporation whose formal corporate domicile is domestic might be less significant in the case of a domestic corporation that was owned by foreign interest. We need not decide here whether such a case would require us to alter our analysis."
25. "The Court's argument is even more difficult to accept when one considers the dilemma it creates for cases involving foreign corporations. If California attempts to tax the American subsidiary of an overseas company on the basis of the parent's worldwide income, with the result that double taxation occurs, I see no acceptable solution to the problem created. Most of the Court's analysis is inapplicable to such a case. There can be little doubt that the parent's government would be offended by the State's action and that international disputes, or even retaliation against American corporations, might be expected. It thus seems inevitable that the tax would have to be found unconstitutional--at least to the extent it is applied to foreign companies. But in my view, invalidating the tax only to this limited extent also would be unacceptable. It would leave California free to discriminate against a Delaware corporation in favor of an overseas corporation. I would not permit such discrimination without explicit congressional authorization."

This decision came after a long series of unsuccessful challenges by foreign parent companies,^{/31.} prompted by the open question in Container of the constitutionality of applying unitary taxation to foreign-based multinationals.

In upholding Alcan's and Imperial's standing to challenge California's unitary tax, the Seventh Circuit stated that:

"(t)hese companies will show a higher taxable income in California under the unitary tax scheme than they would if they engaged in precisely the same foreign commerce through arm's length contracts with unaffiliated companies. From the perspective of the foreign parent, therefore, the unitary tax diminishes the attractiveness of owning American subsidiaries in comparison with entering into contracts with independent companies as a means of engaging in foreign commerce.

Viewed in these terms, Alcan's and Imperial's injuries are direct and independent of the injury to their subsidiaries and standing should follow. To the extent that California's franchise tax burdens foreign companies' decisions to conduct business through subsidiaries operating in California, it threatens to offend this country's trading partners, many of whom must deal with conflicting internal views on the proper role of American investment in their economies, and to elicit retaliatory measures.

It is important that these injuries, which the FTB would have us label indirect under an expansive view of the shareholder standing bar, have fueled a simmering trade controversy which has raised concerns about foreign retaliation and the country's ability to speak with one voice on matters of foreign commerce -- concerns that are central to the purposes of the foreign commerce clause."

On April 17, 1989, the U.S. Supreme Court agreed to review the

31. In *Shell Petroleum v. Graves*, 709 F2d 593 (CA 9 1983), the court held no injury independent of the domestic subsidiaries; in *Alcan Aluminum Ltd. v. Department of Revenue*, 724 F2d 1294 (CA 7 1984), the court dismissed Oregon's unitary application as "unripe"; in *EMI Ltd.*, 738 F2d (9th Cir.) cert. denied, 469 U.S. 1041 (1984) and in *Alcan Aluminum Ltd. v. Franchise Tax Board*, 742 F2d 1430 (2d Cir. 1983), cert. denied, 464 U.S. 1041 (1984), the court held injuries to be indirect, suffered in status as majority shareholders.

At its first meeting on November 2, 1983, the Working Group appointed a Task Force to study the issues and develop options. Between November and April, 1984, the Task Force met in Washington 20 different times for a total of about 150 working hours (not counting countless hours of private deliberation by state and business groups). The Working Group was unable to agree on the six options presented to it by the Task Force. Although there were some common areas of agreement, both sides held fast to their positions on taxation of foreign dividends and 80/20 companies. Nevertheless, the process did clarify the issues and narrow the differences, and probably facilitated the legislative process considerably in states undertaking unitary reform subsequent to the Working Group effort.

At the final meeting of the Working Group on May 1, 1984, agreement was reached that State tax policy in this area should be based on three principles:

- (1) Water's edge unitary combination for both U.S. and foreign based companies.
- (2) Increased Federal administrative assistance and cooperation with the States to ensure full taxpayer disclosure and accountability.
- (3) Competitive balance for U.S. and foreign multinationals and purely domestic businesses.

Both sides agreed that the three principles are "an indivisible package".

On July 31, 1984, Secretary Regan submitted the "Chairman's Report on the Worldwide Unitary Taxation Working Group: Activities, Issues and Recommendations". The letter transmitting

States' and MTC's attitude throughout the Working Group sessions that multinational corporations engaged in widespread tax cheating. Finally, he outlines six reasons which, he asserts, justify different treatment for foreign multinationals than for domestic multinationals.

In his response, Mr. Mattson, who was a member of the Task Force of the Working Group and actually participated in it's deliberations, disputes Mr. Dexter's contention that the scope was limited to considering the affect of worldwide unitary taxation on foreign multinationals. He rebuts each of the "six reasons", and generally portrays the efforts of the Working Group in a more favorable light.^{/36.}

Mr. Mattson concludes with the following prediction:

"The principle of equal treatment for domestic and foreign MNC's (multinational corporations) makes sense from both an economic and a constitutional standpoint. Nondiscrimination is required by the Working Group Principle Three. Indeed, THE PRINCIPLE OF NONDISCRIMINATION IS THE ACHILLES' HEEL OF THE ADVOCATES OF THE WORLDWIDE COMBINED UNITARY TAX. The litigation regarding the constitutionality of the worldwide combined scheme as applied to foreign MNC's is proceeding in both the state and federal courts and will soon reach a trial on the merits. If, as seems inevitable, the tax is ultimately found unconstitutional, the tax as applied to domestic MNC's will have to be relitigated on the issue of discrimination. Under those circumstances, the victory of California in Container Corporation may ultimately turn out to have been both narrow and interim."

-
36. "The considerable debate in a highly structured forum served to clarify many misunderstandings and bring the adversaries together on a long list of points of contention. Indeed, Mr. Dexter's continued hyperbole on the fringes of the argument serve only to undo the considerable goodwill generated by the task force effort."

During 1986, after the introduction of S. 1974, California, Idaho, New Hampshire and Utah enacted unitary legislation, bringing the number of states that had repealed or modified their unitary laws to nine. Subsequently, in 1987, Montana and North Dakota passed water's edge legislation, leaving Alaska the only remaining worldwide unitary state.

Because of the progress that had been made during 1986, the Administration as well as the sponsor withdrew support for S. 1974. Both, however, made statements citing major remaining questions involving inadequate relief provided for foreign dividends^{/39.} and taxation of 80/20's in certain states. These problems remain, despite modifications to California's unitary reform in 1987 and 1988. Consequently, Federal legislation was re-introduced in 1987^{/40.} and 1989.^{/41.}

-
38. Statements of J. Roger Mentz, Assistant Secretary, Treasury, and Sen. Pete Wilson, Hearings, September 29, 1986.
39. California's 75 percent exclusion and linkage to foreign payroll factors; New Hampshire's "bifurcated formula"; and Utah's 50 percent exclusion with factor relief on taxable 50 percent. Additionally, Alaska's continued mandatory imposition of worldwide unitary.
40. H.R. 2940, Rep. Frenzel (R-Minn.) / S. 1843, Sens. Roth (R-Del.) and Fowler (D-Ga.), carried over to 1988.
41. H.R. 1390, Rep. Frenzel and 13 other representatives, 9 of whom are members of Ways and Means / S. 1139, Sens. Roth, Fowler, Glenn, Simon, Symms, Lugar and Nunn.

business will shun such states. They will not invest that extra dollar over and above what is necessary to maintain its presence in the state, but will look elsewhere when making discretionary investments.

This does not necessarily mean that business will seek out the low tax state. In fact, low taxes may result in a lack of the very resources which may be far more important. Corporations are willing to pay a high tax bill to support conditions which it feels are necessary for the conduct of its business. But few CEO's would invest that extra dollar in a unitary state.

After Container, this realization suddenly became obvious to state legislatures and others in state government responsible for economic development. The depth of business' attitude to unitary encouraged a growing recognition that states could not continue to impose such a universally disliked tax. This contributed to the unitary retreat perhaps more than any other factor.

(2) STATE COMPETITION AND ECONOMIC DEVELOPMENT

The mirror image of a negative business climate created by the imposition of bad taxes is development of a positive economic development policy and active competition with other states for business investments.

Over the years, many studies have been made on the impact of taxes on economic development. Earlier ones generally discounted

Then, in 1987, Johnson said, the Iowa governor came to Nebraska asking companies to move to his state. ConAgra, the state's largest employer, had done a state-by-state study of the tax climate and was planning to move to Tennessee. In response, Nebraska passed legislation giving tax breaks to business. As a result, according to Sen. Johnson, ConAgra stayed, and Nebraska gained 15,000 new jobs in the first year after the legislation was enacted.

Business in general reacts more favorably to the overall tax policy of a state than it does to "special deals" given on a company-by-company basis. As Bill Brown, President of COST has stated "in the long run indiscriminate use of special incentives or deals are likely to be counterproductive. For one thing the company that is attracted by such an approach is likely to move on to 'greener pastures' or attempt to 'extort' further concessions."/⁴⁶ Mr. Brown goes on to state that

"(i)n order for a tax incentive to contribute to a Good Business Climate, and not detract, it should be generally available to all taxpayers with like circumstances. It definitely should not discriminate against existing businesses - yet most special incentives or deals do exactly that! It needs to be recognized that generally the best prospect for increasing jobs is expansion of existing businesses rather than chasing around the country attempting to lure some prospect that everybody else is working on too."

The folly of using special tax deals to encourage development

46. National Tax Association - Tax Institute of America
Annual Conference, Des Moines, Iowa, September 26, 1988.

See also, "Holdup in the Windy City -- Chicago is the latest loser in the tax-incentive wars", U.S. News & World Report, July 17, 1989.

Alaska Unitary Statement

My name is Susan Burke and I am here today representing the IBM Company and their interest in corporate tax reform.

IBM has a long business history in Alaska. They currently employ 170 people in our State. Their annual payroll exceeds \$10 million. The company is an active corporate citizen contributing more than \$125,000 to charities and community projects in the last year.

IBM is most interested in the Governor's proposal to reform our State's worldwide unitary method of taxation. However, they are disappointed and concerned that the proposed legislation is limited to only foreign corporations. The proposed legislation benefits only corporations who are non U.S. companies and thus would discriminate against U.S. domestic corporations and put them at even more of a tax disadvantage than today. IBM agrees with the fundamental need to repeal Alaska's world wide unitary taxation; however, the legislation must be expanded to include domestic corporations or it will only exacerbate tax inequities for U.S. companies.

While one issue is competitive fairness between foreign and domestic companies, an equally important issue is good tax policy. Repeal of worldwide unitary taxation has been a priority of IBM and the business community for years.

Alaska is the only state currently requiring worldwide unitary taxation. In the past four years, 11 states have revised their tax laws to no longer require this form of state taxation. In addition, no country in the world uses this method of taxation. In fact, many countries have petitioned the U.S. government protesting the fact that states use worldwide combination.

Why does IBM oppose worldwide unitary taxation? IBM operates in more than 130 countries around the world. When an IBM overseas affiliate earns income, it pays taxes to the country in which the income was earned. In most cases, the foreign tax is at a higher rate than in the United States. A fundamental tenet of international tax law and practice is that foreign source income is not taxed by the home country until it is repatriated and then only to the extent that it is not offset by foreign tax credits. Clearly, the intent of this policy is to avoid double taxation of foreign source income.

A state, like Alaska, that uses worldwide unitary taxation, taxes foreign source income when it is earned even if it is never brought back to the U.S. Furthermore, using foreign income in calculating state tax liability may result in over apportionment of income to a state, taxation of income already taxed by a foreign government (and not taxed by the U.S. government), and potentially disruptive effects on international trade. Thus, use of the worldwide unitary method of taxation can distort a

company's taxation relationship to a state and mean double taxation of income earned in another governmental jurisdiction.

Corporate taxes are a basic and significant cost of doing business and no company can withstand a tax disadvantage without suffering an important economic impact. Therefore, IBM strongly recommends repeal of Alaska's worldwide unitary tax system for all corporations.

Reform of the worldwide unitary system will make Alaska a more attractive place to invest if it is applied equally to domestic U.S. corporations and foreign corporations. If worldwide unitary reform applies only to foreign corporations, they would no longer be taxed on their foreign income, while U.S. corporations will continue to be taxed of foreign income. This is not only a disincentive to investment in Alaska by U.S. corporations, but penalizes them compared to their foreign competitors.

IBM would be pleased to work with the Legislature in an effort to draft legislation that provides meaningful and comprehensive reform of the worldwide unitary tax system.

WILLOS
9:38

FISCAL NOTE

STATE OF ALASKA
1991 LEGISLATIVE SESSION

BILL NO. CSHB46(ITT)

Revision Date:

Title:

Creating AK Aerospace
Development Corporation

Department Affected: University of Alaska

BRU: ALL

Component:

Sponsor:

Moyer

Requestor:

ITT

Component Serial No. ALL

Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY92	FY93	FY94	FY95	FY96	FY97
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL						
---------	--	--	--	--	--	--

REVENUE	0.0	*	*	*	*	*
---------	-----	---	---	---	---	---

FUNDING: (Thousands of Dollars)						
GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS:						
FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year impact: _____

ANALYSIS: (Attach a separate page if necessary.)

SEE ATTACHED

Prepared by:

Brian Rogers

Division:

Vice President for Finance

Phone: 474-7448

Date: 3/7/91

Approved by:

Brian Rogers, Vice President for Finance

Agency:

University of Alaska

Date: 3/7/91

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

Rev 10/90

Page 1 of 2