

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 8672
103 SCOMM 9: HOUSE SPEC. COMM. ON PERMANENT FUND 1977-78

enough, the Bank may be able to order increased subscriptions without calling in any capital.

The European Investment Bank acquires virtually all its loan funds on the European bond market. Although the Bank resorts mainly to the European market, it has been able to sell its debt internationally, particularly in the United States and Japan.

The issues range from a low of 6.3 million UA to a high of 239.1 million, averaging from 20 to 40 million. About 40 percent of these issues are placed privately. Since 1974, the Bank has raised more than 800 million UA per year through the sale of bonds. Virtually all the public issues are underwritten by syndicates composed of European commercial and savings banks.

The interest rates the EIB must pay are in line with its strong backing. Rates rose from about 7.0 percent in 1972 to nearly 10.0 percent in 1974, and has since declined. In fact, the Bank has just adjusted its uniform lending rates downward to reflect this movement.

The most noteworthy aspect of the EIB bonds is that they are all long-term. There are a few occasions where the Bank borrowed for less than seven years. Most issues are for at least 10 years, with some going for as long as 15 to 20. The lengths of these liabilities match that of the productive capacity of the assets EIB finances--capital intensive plant and infrastructure.

Table 2
FUNDS RAISED UP TO AND INCLUDING 1976

Year	Issues				Participations by third parties in EIB loans (mil. UA)	Funds raised (mil. UA)
	Number	Amounts (mil. UA)				
		Private issues	Public issues	Total		
1961	3	7.6	13.8	21.4	-	21.4
1962	2	-	32.3	32.3	-	32.3
1963	3	8.0	27.2	35.2	-	35.2
1964	5	13.5	53.3	66.8	-	66.8
1965	4	-	65.0	65.0	-	65.0
1966	6	24.0	114.5	138.5	-	138.5
1967	8	40.0	154.5	194.5	-	194.5
1968	13	112.5	100.0	212.5	-	212.5
1969	9	63.7	82.3	146.0	-	146.0
1970	7	66.6	102.3	168.9	-	168.9
1971	20	208.0	204.9	412.9	-	412.9
1972	19	133.4	328.6	462.0	17.5	479.5
1973	22	207.0	101.0	608.0	4.3	612.3
1974	16	704.2	121.3	825.5	-	825.5
1975	26	318.6	495.1	813.7	17.0	830.7
1976	17	221.0	510.9	731.9	17.0	748.9
1961-1976	180	2128.1	2807.0	4935.1	55.8	4990.9

The EIB has enviable access to the European bond market and is beginning to offer its issues in the American and Japanese markets. The burgeoning growth of its demand for funds, shown in Table 2, has not compromised this access. The benefits of timely access to funds, long repayment terms and favorable interest rates derived from EIB's strong backing are transferred to its borrowers.

III. USES OF FUNDS/LENDING OPERATIONS

By Sector

Over EIB's operating history, its loans, in terms of money volume, have been concentrated in infrastructure projects, predominately in energy, transportation and telecommunications. EIB has made about four times as many loans to industrial sectors as to infrastructure projects. However, total money volume of these loans was only about half of that devoted to infrastructure. Manufacturing projects have received the preponderant number of industrial loans. Table 3 summarizes this allocation pattern and Tables 4 and 5 give more complete breakdowns of historical and current activity.

By Objective

In reporting its loan activities by statutory objectives, EIB

Table 3
EIB FINANCING, 1976 AND TOTALS 1958-1976

Sector	1976			1958-1976		
	#	Amt. (mil. UA)	% of Total	#	Amt. (mil. UA)	% of Total
<u>Infrastructure</u>						
Agriculture	1	30.1	2.8	8	123.9	2.0
Water Supply	6	74.3	6.8	19	220.9	3.7
Transport	6	107.2	9.9	60	1001.2	16.7
Telecommunication	8	200.1	18.4	38	853.7	14.2
Other	-	-	-	2	16.3	0.3
Energy	18	376.5	34.7	109	1764.2	29.4
Total	39	788.2	72.6	236	3980.2	66.3
<u>Agriculture, Industry and Services</u>						
Agriculture	-	-	-	5	7.5	0.1
Industry	120	297.8	27.4	874	2004.0	33.4
Services	-	-	-	7	13.7	0.2
Total	120	297.8	27.4	886	2025.2	33.7
<u>Grand Total</u>	159	1,086	100	1122	6005.4	100.0

All figures in millions UA.

Table 4
SECTORAL BREAKDOWN OF FINANCING PROVIDED WITHIN THE COMMUNITY, 1958-1976

Sector	Number		Amount (million u.s.)		% of total
	Total	of which global loan allocations	Total	of which global loan allocations	
Infrastructure	236		3 980.2		66.3
Agricultural development	8		123.9		2.0
Water supply and distribution	19		220.9		3.7
Transport	60		1 001.2		16.7
Railways	14		221.8		3.7
Roads, bridges and tunnels	34		587.9		9.8
Shipping and inland waterways	8		144.9		2.4
Airlines	3		41.7		0.7
Other	1		4.9		0.1
Telecommunications	38		853.7		14.2
Other	2		16.3		0.1
Energy	109		1 764.2		29.4
(Production)	(77)		(i 243.7)		20.7
Nuclear	29		620.2		10.3
Thermal power stations	13		133.2		2.3
Hydroelectric and pumped storage plant					
Development of oil and natural gas deposits	17		245.5		4.1
Solid fuel extraction	10		223.1		3.7
(Transport)	2		16.7		0.3
Transmission lines	(32)		(520.5)		(8.7)
Gaslines and oil pipelines	6		65.8		1.1
	26		454.6		7.6
Agriculture, industry and services	886	553	2 025.2	262.4	33.7
Agriculture, forestry, fishing	5	4	7.5	2.0	0.1
Industry (2)	874	549	2 004.0	255.9	33.4
Mining and quarrying*	18	15	12.8	6.4	0.2
Metal production and semi-processing*	77	31	608.1	22.5	9.3
Construction materials*	63	39	107.2	20.1	1.8
Woodworking	39	37	19.2	13.2	0.3
Glass and ceramics	25	13	33.2	6.9	0.6
Chemicals*	97	25	457.2	12.1	7.6
Metalworking and mechanical engineering	153	119	166.9	52.9	2.8
Motor vehicles, transport equipment	32	19	139.5	8.3	2.3
Electrical engineering, electronics	47	32	74.1	18.4	1.2
Foodstuffs	132	95	159.4	46.3	2.7
Textiles and leather	65	53	37.2	23.2	0.6
Paper and pulp*	28	23	29.6	10.3	0.5
Rubber and plastics processing	41	30	58.7	12.7	1.0
Other	14	11	6.9	3.9	0.1
Building -- civil engineering	4	4	1.7	1.7	—
Global loans	39	—	141.6(3)	—	2.4
Services	7	3	13.7	1.4	0.2
Tourism	5	3	9.3	—	0.1
Research and Development	2	—	4.4	—	0.1
Grand Total	1 122	553	6 005.4	262.4	100.0

(1) See note 4 to Table 2, page 23.

(2) Of which basic industries (marked with an asterisk): 1 165.2 million u.s.

(3) This amount represents the unallocated portion of the global loans.

Table 5
SECTORAL BREAKDOWN OF FINANCING PROVIDED WITHIN THE COMMUNITY, 1976

Sector	Number		Amount (in million u.s.a.)	
	Total	of which global loan allocations	Total	of which global loan allocations
Infrastructure	39		788.2	72.6
Agricultural development	1		30.1	2.8
Water supply and distribution	6		74.3	6.8
Transport	6		107.2	9.9
Railways	1		19.7	
Shipping and inland waterways	5		87.5	
Telecommunications	8		200.1	18.4
Energy	18		376.5	34.1
(Production)	(11)		(247.6)	
Nuclear	3		111.3	
Thermal power stations	2		30.4	
Hydroelectric and pumped storage plant	2		42.1	
Development of oil and natural gas deposits	3		60.5	
Solid fuel extraction	1		3.3	
(Transport)	(7)		(128.9)	
Gaslines and oil pipelines	7		128.9	
Agriculture, industry and services	120	86	297.8	47.5
Industry (1)	120	86	297.8	47.5
Mining and quarrying*	3	3	2.2	2.2
Metal production and semi-processing*	21	11	159.3	8.3
Construction materials*	8	7	7.2	3.6
Woodworking	4	3	3.8	1.4
Glass and ceramics	2	1	4.7	0.6
Chemicals*	15	8	83.7	4.2
Metalworking and mechanical engineering	14	13	8.7	6.1
Motor vehicles, transport equipment	4	3	17.1	2.0
Electrical engineering, electronics	9	8	6.3	4.6
Foodstuffs	16	15	7.7	6.0
Textiles and leather	5	5	4.4	4.4
Paper and pulp*	3	3	1.3	1.3
Rubber and plastics processing	7	4	11.9	2.1
Other	1	1	0.1	0.1
Building - civil engineering	1	1	0.6	0.6
Global loans	7	—	13.7 (2)	—
Grand Total	159	86	1 086	47.5

(1) Of which 11 industries (marked with an asterisk): 218.7 million u.s.a.

(2) Difference between the sum of the 7 global loans granted in 1976 (€1.2 million u.s.a.) and the sum of the allocations to the same 7 global loans (€7.9 million u.s.a.) in 1976.

consolidates its three mandates (see page 1) into two classifications: projects for "regional development" and projects of common interest to several member countries. Some projects cannot be unambiguously classified and are counted in both categories. About 18 percent of all projects undertaken by EIB since it began operations have been so counted. Keeping that in mind, some 76 percent of EIB's 6 billion UA in loans have been justified on the basis of furthering the development of less developed regions. Projects of interest to several countries have been mostly in the fields of energy and transportation. Table 6 shows a more complete breakdown of loans by objective.

Global Loans

The management of EIB recognizes that small enterprises are the dominant type of industrial organization in labor-intensive sectors. These firms seldom have capital needs which match EIB's 1 million UA direct lending minimum. However, they are an important source of employment and, in certain sectors and areas, an efficient form of organization.

In order to meet these firms' needs, EIB lends to intermediate institutions, usually regional development authorities who in turn lend to small firms. The authorities are allocated a given amount and are given a finite period in which to use the funds.

Table 6

FINANCING PROVIDED WITHIN THE COMMUNITY IN 1976 AND FROM 1958 TO 1976
Breakdown by Economic Policy Objective

Objective	1976		1958-76 (2)	
	million E.C.U.	%	million E.C.U.	%
Regional development (1)	820.0	100.0	4 558.6	100.0
Belgium	17.9	2.2	75.1	1.6
Denmark	9.1	1.1	35.7	0.8
Germany	9.2	1.1	366.4	8.0
France	50.1	6.1	846.0	18.6
Ireland	57.4	7.0	164.1	3.6
Italy	347.1	42.3	2 200.6	48.3
Luxembourg	—	—	4.0	0.1
Netherlands	30.4	3.7	70.5	1.5
United Kingdom	228.8	28.2	786.2	17.5
Common interest to several Member Countries (2)	438.6	100.0	2 470.1	100.0
Energy	376.5	85.9	1 490.3	60.3
Thermal power stations	30.4	8.0	30.4	1.2
Hydroelectric and pumped storage power stations	42.1	11.2	141.4	5.7
Nuclear	111.5	29.4	598.6	24.2
Development of oil and natural gas deposits	50.5	13.4	258.6	10.5
Solid fuel extraction	3.3	0.9	27.9	1.1
Gaslines and oil pipelines	128.9	34.2	133.4	5.4
Transport	16.4	4.4	589.6	23.9
Railways	—	—	103.9	4.2
Roads and bridges	—	—	423.9	17.2
Shipping	16.4	4.4	40.4	1.6
Airlines	—	—	3.5	0.1
Other	—	—	4.0	0.2
Telecommunications	—	—	30.5	1.2
Other infrastructure	—	—	16.3	0.7
Protection of the environment	—	—	18.0	0.7
Industrial cooperation	25.9	6.9	213.6	8.7
Research	—	—	2.7	0.1
New technology	19.7	5.4	19.7	0.8
Modernisation and conversion of undertakings (3)	—	—	69.4	2.8
<i>DEDUCT to allow for duplication in the case of financing justified on the basis of both objectives</i>			<i>172.6</i>	
Total	1 086.0		6 005.4	

(1) Article 130 (a) and (b) of the Treaty of Rome.

(2) Article 130 (c) of the Treaty of Rome.

(3) Article 130 (b) of the Treaty of Rome; these projects, classified as 'Common interest to several Member Countries' in the 1976 Annual Report, have now been included under 'Common interest to several Member Countries' by way of simplification and in view of the modest amount involved. In the 1976 Annual Report, the total amount of financing provided for these projects was 133.9 million E.C.U., of which 39.5 million, relating to projects included among 'substantial projects of common interest to several Member Countries', has now been deducted to avoid duplication: 133.9 - 39.5 = 94.4 million E.C.U.

Projects so financed must meet EIB criteria and be located in a specified area, usually one of the less-industrialized regions. If suitable projects cannot be found within the specified time, the loan money is restored to EIB.

In the nine years of this program's operations, 404 million UA have been allocated to various regional authorities, of which 262.4 million has actually been disbursed. EIB has withdrawn from participating national and regional financial intermediaries 11 of the 38 global loans it has made in the last eight years. Apparently these institutions were unable to find suitable investments, and EIB was intent on enforcing its lending criteria. The average size of the loan has been 474,000 UA, and most have been concentrated in depressed areas of Italy, France and Germany. Although the global loan program represents a sound concept, allowing small firms access to an expanded capital market, it comprises a very small part of EIB's total lending activity--about six percent in 1976.

The overriding impression left by this review of EIB's operations is that the Bank takes a regional approach to its lending--acknowledging the interaction of public investment and private productivity. It then cooperates with national and regional level public and private financial institutions to provide capital to directly productive enterprises.

This pattern has been particularly evident in EIB's operations in the Mezzogiorno (southern Italy), one of the most depressed regions in Europe. Over the years 1961-1972, the Bank provided 7.5 percent of all investment capital coming into the region, concentrating its investments in roads, telecommunications, energy distribution systems and capital intensive industry. I cooperated with the World Bank and Italian public and private financial institutions in encouraging coordination and planning, providing capital to finance these plans where Italian sources were insufficient.

IV. MANAGEMENT

There are three basic levels of administration at EIB. The Board of Governors is responsible for strategic decisions; ensuring that statutory directives are carried out, designating levels of subscribed capital, authorizing changes in policies conditioned on movements in exchange rates, etc. Each member state appoints one Governor. A majority of the Board, representing at least 40 percent of subscribed capital, is necessary to carry motions.

The Board of Directors is responsible for all lending and borrowing decisions. They are appointed by the Board of Governors and have renewable terms. The number of directors from each

member state is set by statute, and the larger states, France, Germany, the United Kingdom and Italy are most heavily represented.

The Management Council, headed by a President, is responsible for seeing that the professional staff carries out the Director's decisions. The EIB retains agents and industry specialists in all member states to evaluate and monitor loans. Loan agreements are executed under the national laws of the state in which the project is located.

V. ACCOUNTABILITY

There is a minimal formal structure of reporting and sanctions by which the Board of Directors, EIB's operating decision-makers, are held responsible for their work. The Board of Governors, acting on behalf of the executive of their respective states, must approve the Directors' Annual Report. If performance is not satisfactory, Directors may be dismissed. States may further effectively censure Bank decisions by refusing to subscribe more capital. But all these measures would operate only in extreme cases of mismanagement or violation of statutory directives. In the important daily work of lending and borrowing, the Directors seem to have a free hand.

VI. EVALUATION

EIB is an operating arm of the European Commission, the central planning and policy-making body of the European Community. We have seen that EIB's major operations have been concentrated in aiding efforts to develop regions characterized by lack of industrialization (the Italian Mezzogiorno) or inefficient industries declining under the force of increased competition stemming from the lowering of trade barriers (Belgian coal regions).

The European Commission has not yet developed a Community-wide policy for coordinating the planning and finance of economic development in subnational regions. In such efforts, national authorities must take the initiative and be responsible for overseeing or executing the planning, financing and administering activities involved. Where the financing of costly industrial plant or infrastructure is involved these authorities may not be able to raise sufficient capital in a timely manner. The private or quasi-public financial systems of the several members states are set up primarily to service national needs. As yet there exists no institutional mechanism to coordinate these systems to provide the massive amounts of capital necessary to finance large-scale development projects.

EIB is designed to do just this. With its solid equity backing, it can raise large amounts of capital quickly in the inter-

national bond market on the terms necessary to finance long-lived assets such as capital intensive physical plant and infrastructure. Because EIB borrows and lends in stable currencies, some promoters in countries with weaker currencies have been unwilling to take EIB loans. They would suffer a loss if their national currency, in which they would receive the revenues generated by the asset financed, were devalued in relation to the currency in which they would have to pay off the loan. This risk is offset in many cases by the favorable interest and repayment period terms on which EIB can offer its funds. For example, Italian firms and authorities have been EIB's largest borrowers.

Real economic factors affecting a borrower's potential performance are not susceptible to EIB influence. Long and concerted effort is needed, for instance, to improve infrastructure, labor productivity and the stability of the regional population in the Mezzogiorno before it becomes a suitable location for the capital intensive facilities the EIB prefers to finance.

The Bank appears to take these considerations into account in pursuing its policies. First, it lends to infrastructure projects, where the ability to mobilize large amounts of capital is critical. Second, it will not lend more than 40 percent of the value of an asset. In a fact, its participation has been substantially less in most cases. EIB seeks to provide the incremental

amount of financing needed to implement a project which already enjoys sound national managerial and financial backing. Financial responsibility is thus not transferred from local government and business organizations whose political and economic fortunes are closely tied to the success of the projects. Unfortunately, EIB's performance, in terms of allocating capital to efficient uses, cannot be inferred from its financial success. Most of its loans are secured by guarantees from national governments. The performance of its borrowers is not reported in central documents. Due to the guarantees, poor performance does not show up as a default rate. The pattern of financial responsibility and ultimate accountability therefore corresponds to the European Commission's as yet decentralized regional development policy.

VII. RELEVANCE TO THE ALASKA PERMANENT FUND

Purposes: The primary way in which the European Investment Bank is relevant and important to the Alaska Permanent Fund is in the strong regional orientation of the European Investment Bank, where 63 percent of its portfolio has been invested in the development of lesser developed regions of Europe. It is important to note that although the vast percentage of its resources has been employed in regional development, only six percent of those resources have been employed through the "global loan program." The importance of that point to the Alaska Permanent Fund is that the global loan program would be most analogous to a regionalized effort in which the regional projects of the Alaska Permanent Fund were implemented through the regional and local community development corporations. This matter bears further consideration.

It is also worth noting that the European Investment Bank rarely takes more than 40 percent positions in its loans, to ensure that the risk and responsibility are borne by both local financial institutions and the private marketplace. Analogously, in Alaska, this is the intent of the present language of the Alaska Permanent Fund and in the case of regional development suggests the wise course of joint venturing with the

regional corporations and with the private marketplace in all regional loans.

Sources and Uses of Funds: There are three principal matters concerning the European Investment Bank's capitalization which are worth noting for the design of the Alaska Permanent Fund:

First, all of the earnings of the European Investment Bank have been retained for reinvestment in strengthening the capital structure of the European Investment Bank. This is a different use of retained earnings than those of either the Alaska, Inc. proposal or a proposal to use the earnings for General Fund purposes at some future date.

Second, with a strong equity base the European Investment Bank has been very successful in borrowing the substantial amount of its capital needs in European and worldwide private capital markets. This is a very important model for the Alaska Permanent Fund. In designing the Alaska Permanent Fund the \$2 to \$4 billion of oil revenues should be viewed as a paid-in equity capital base for the Alaska Permanent Fund against which it can then borrow for its lending purposes on world markets.

Third, the European Investment Bank has a nice balance of its sources and uses of funds. The majority

of the European Investment Bank's borrowings in world capital markets are for seven to ten years, to support expansion capital lending running seven to ten years. The longer infrastructure loans of 15 to 20 years are then in turn supported by borrowings in the international capital market of from 15 to 20 years.

Fourth, all of the infrastructure investing is backed by a government guarantee. In my judgment, it would be much more efficient for Alaska to do the majority of its infrastructure financing through the Permanent Fund, but backed by general revenues.

Management and Accountability: The management and accountability issues of the European Investment Bank are less relevant to the Alaska Permanent Fund.

E. AN ALASKA CENTRAL BANK OWNED BY LOCAL COOPERATIVE
DEVELOPMENT BANKS

1. BRITISH COLUMBIA CENTRAL CREDIT UNION
Discussion Draft

September 14, 1977
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I. PURPOSES

The British Columbia Central Credit Union is a private, federally-chartered financial institution owned by the credit unions of British Columbia. Established in 1944, its major function is that of a reserve bank for British Columbia's 178 credit unions. In 1970, it merged with the B.C. Credit Union League, a promotional and educational institution and has since provided a wide range of financial and administrative services to its members. Credit unions require most of these services in order to compete with other types of financial institutions for the deposits and loan business of British Columbia savers. In general, credit unions are too small to undertake the capital expenditure and staff requirements necessary to provide these customer services efficiently.

Credit Unions in British Columbia - Credit unions are deposit institutions offering a full range of customer services. Their investments tend to be concentrated in home mortgages, consumer credit and property development. They are distinguished from banks in that they are cooperatively owned by their depositors, each of whom is entitled to one vote in electing the board of directors and who may participate in membership-management meetings.

All members are required to have a "common bond," a legally construed economic association. These bonds may be of three types: community (those who live or work in a given political jurisdiction serviced by the credit union), associational (e.g., ethnic or church groups) or occupational. About one half of the credit unions in B.C. have community common bonds.

In 1975, there were 178 credit unions with 261 branch offices in B.C. These serviced some 600,000 members, about 23% of the population and composed some 23% of all deposit institution offices in the province. About one half of these offices are located in the greater Vancouver area.

The industry has grown remarkably and become more concentrated in recent years. Since 1971, membership has been growing at a compound annual rate of 11%, assets at 35%. In 1971, there were 217 credit unions holding slightly less than \$500 million in assets. In 1975, the 178 credit unions held over \$1.5 billion in assets, with half of these held by the 15 larger units. (The remaining units are extremely small, median asset size being less than \$70 million.) Credit union assets account for 10% of those held by all financial institutions in the province (20% if corporate business is excluded). Individual units are usually located within communities serviced by commercial banks and are in competition with them for deposits.

Distribution of assets - There has been a sharp rise in the demand for housing in B.C. due to the migration of large numbers of young families. Consequently, the credit unions' assets have become concentrated in home mortgages. In 1971, they composed 62% of the \$400 million in loans outstanding. In 1975, they composed 76% of the \$1,280 million in loans outstanding. Other credit union assets include municipal, provincial and federal government securities and consumer loans.

Liabilities - The main source of funds to credit unions is the deposits of members. Credit unions offer term and demand accounts as well as retirement and home owner savings plans. The latter two types of deposits have grown at a remarkable compound annual rate of over 100% in the past four years. Of the \$1,409 million on deposit in 1975, 36% were in demand and 64% were in term accounts.

Liquidity - Credit unions are required by law to maintain liquidity reserves with a bank, a central credit union or in qualifying federal government securities equal to 10% of deposits shares and borrowings. Virtually all British Columbian credit unions maintain their reserves and surplus in B.C. Central. In recent years, aggregate Loan/Deposit ratios for the industry have exceeded 90%. The credit unions as a whole, then, have

demanded funds from other sectors of the capital market. This borrowing and the cash management involved have been handled by B.C. Central. B.C. Central's functions within the credit union system and its mediating role between the system and the outside capital market is the subject of the following sections.

B.C. Central Operations

Financial - B.C. Central's main financial function is to provide individual credit unions with funds sufficient to meet local loan demand when local deposits prove inadequate. These funds are provided in the following forms:

- non-restricted reserve credit lines equal to 10% of the credit union shares and deposits for use only in meeting any net reduction in shares and deposits due to increased loan demand;
- restricted and non-restricted credit lines to credit unions equal to four to six times a credit union's monthly cash flow for operational purposes. Approved lines of credit under these first two provisions equaled \$262 million in 1975;
- term loans to credit unions to finance office buildings and credit union mortgage loans;

- emergency loans through the Canada Deposit Insurance Corporation.

Actual borrowings by credit unions from B.C. Central have grown rapidly in recent years from \$26.1 million in 1971 to \$91.8 million in 1975, reaching a high of \$108 million in the tight money market of 1974. Credit union credit line and loan requirements are worked out annually in consultation with B.C. Central's financial staff on the basis of financial statements, loan records and cash flow projections.

Credit union deposits are not covered by the Canadian Deposit Insurance Corporation. Insurance of deposits is handled by another central institution, the Credit Union Share and Deposit Guarantee Fund. The Fund is administered by a five member Board of Directors, three of whom serve on the B.C. Central Board. The Fund, which stood at \$13 million in 1975, is capitalized by annual assessment of member credit unions. The Board of the Fund may intercede directly in the operations of individual credit unions experiencing financial difficulties and may grant financial assistance where deemed necessary.

B.C. Central provides other important financial services to its members. These include centralized check clearing, bad debt collection, investment management for retirement and home ownership saving plans and secondary marketing of credit union

mortgages. The last service is another form of increasing member liquidity.

Non-financial services - B.C. Central's most important non-financial service is the provision of on-line teller terminal data processing to handle deposit and loan transactions in local offices. In 1975, this system covered one-half of all credit union offices. The savings in time and cost effected by this system increase credit union ability to compete with other deposit institutions. Other nonfinancial services provided for the most part on a fee basis are economic forecasting, personnel recruitment, printing and supply purchase, collection assistance, data processing and systems development, market research, facilities design and planning, education, advertising and public relations, legal counsel, housing development and travel services. B.C. Central also provides financial services to British Columbia's 108 cooperatives.

II. SOURCES OF FUNDS/CAPITALIZATION

Equity - B.C. Central's major source of equity is the sale of shares to member credit unions. In 1975, members held 6.26 million shares with a par value of \$31.3 million, all of which was paid in to B.C. Central. B.C. Central is required by law to maintain a 10/1 debt/equity ratio. Their debt consists

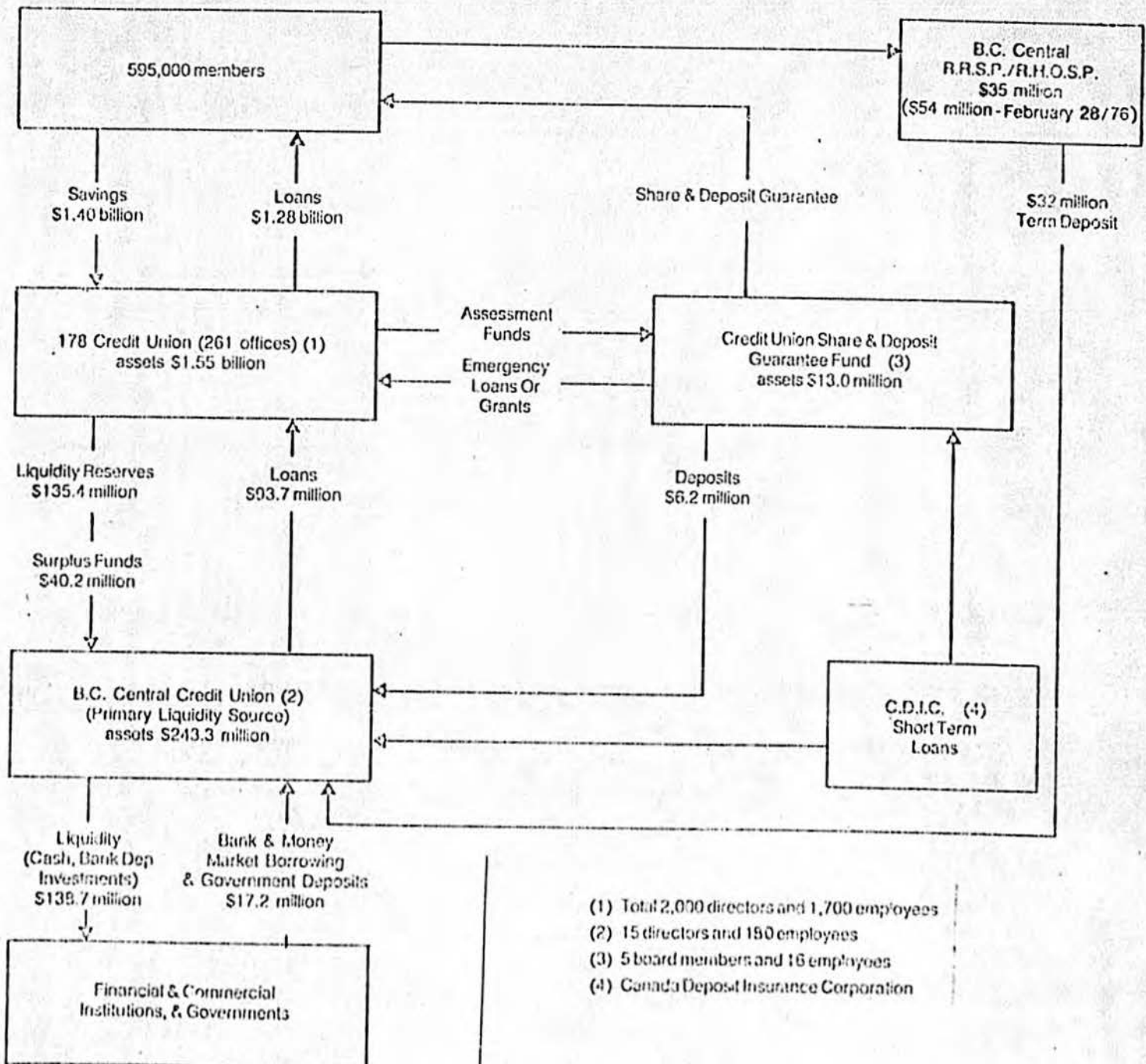
of deposits and borrowings; equity of membership shares, retained earnings and provisions for dividends. Despite rapid recent growth of deposits in the credit union system and consequently in B.C. Central's deposits, its debt/equity ratio was a fairly conservative 5.7 in 1975.

Deposits - B.C. Central's deposits are comprised of the liquidity reserves and surplus funds of its members. As credit union deposits have grown, so has B.C. Central's; from \$49.7 million in 1971 to \$195.8 million in 1975. These developments are illustrated in Table I. B.C. Central also receives one-half the total in the Credit Union Share and Guarantee fund as deposits. In 1975, this amounted to \$6.2 million. Central pays interest on all deposits, which composes its largest capital expense. See Table 3.

Borrowings - Because credit unions' lending activity has outstripped their deposit base in recent years, they have been demanders of funds from sources outside their system. These demands are mediated by B.C. Central. To finance loans to credit unions, B.C. Central borrows from Canadian, US and foreign banks and has established non-restrictable credit lines with three of the largest Canadian commercial banks. Borrowings vary greatly from year to year depending on the level of deposits

FIGURE I
Credit Union Financial System in British Columbia

December 31, 1975



- (1) Total 2,000 directors and 1,700 employees
- (2) 15 directors and 150 employees
- (3) 5 board members and 16 employees
- (4) Canada Deposit Insurance Corporation

TABLE I

Summary Statistics for B.C. Central Since 1971

(000's except where indicated)

	1975	1974	1973	1972	1971
ASSETS					
Liquid Assets	\$127,885	\$ 61,824	\$ 64,408	\$ 50,541	\$35,626
Loans to members	91,823	108,973	56,705	45,371	26,177
Total assets	243,290	193,225	141,721	109,027	67,807
LIABILITIES					
Notes payable	4,500	12,490	13,150	23,519	5,643
Members' Deposits	195,817	145,048	101,685	66,389	49,679
Members' Shares	31,300	24,815	18,317	12,746	9,153
INCOME AND EXPENDITURES					
Income	27,175	19,938	12,768	7,296	4,916
Expenses (financial)	18,941	13,906	8,032	3,962	2,706
Net Income	2,299	1,621	1,103	1,343	1,008
Dividends per share	35¢	35¢	35¢	30¢	30¢
Percent Growth in Assets	25.9%	36.3%	30.0%	60.8%	29.7%

and loan demand at the local level. See Table I, "Notes Payable," for the level of debt outstanding in recent years.

Income - B.C. Central derives between 80 and 85% of its income from interest payments on loans and returns on investments in securities. The split between loan interest and investment income varies from year to year, depending on loan demand from members. Other sources of income are service charges, fees for services to members and membership dues. Gross income has grown from \$4.9 million in 1971 to \$27.2 million in 1975.

III. USES OF FUNDS/INVESTMENTS

Reserve Requirements - B.C. Central is required to maintain liquidity reserves in cash or short term assets equal to 20% of its deposits and commercial paper liabilities. In 1975, it held \$48.3 million in such assets; 23.5% of its deposits and market liabilities. See Table II.

Loans and Investments - B.C. Central's longer term uses of funds are concentrated in loans to members and investments in securities. The flow of loans to members varies from year to year, depending on demand. Interest rates are adjusted to B.C. Central's borrowing terms, and a spread of 1/2% is permitted by law.

B.C. Central invests primarily in high yield, short term notes of Canadian corporations. Other securities held include Canadian Governments, Canadian corporate bonds, bonds of co-operatives and shares in other credit unions and cooperatives.

Operating Expenses - All expenses involved in providing B.C. Central's many services--salaries, materials and rents--are paid out of B.C. Central's operating income. After-tax earnings, having subtracted financial and administrative expenses, came to \$2.29 million in 1975. Of this, \$1.87 million was distributed as dividends to members. (The current dividend on membership shares is 7%.) Retained earnings at the end of 1975 totaled slightly over \$3 million. See Table III for a complete breakdown of income and expenses. See Figure I for a schematic representation of the relationships described above.

IV. MANAGEMENT

The strategic management policies of B.C. Central are set by a 14-member Board of Directors elected by the member credit unions. Day-to-day management of the institution is handled by a managerial staff of 80 (total staff - 180) in three divisions: Administration and Finance, Services and Development.

Each division is headed by a manager and is further subdivided along functional lines.

V. ACCOUNTABILITY

B.C. Central is a privately owned institution and is subject to no special forms of government oversight or control. Its operations are inspected annually by the federal Superintendent of Insurance office. On the provincial level, Central's operations are monitored by the Department of Consumer Affairs to ensure that consumer and mortgage credit practices accord with department guidelines and provincial usury laws.

VI. EVALUATION

B.C. Central has performed its function of helping a system of small depository units operate effectively and grow in highly competitive and quickly changing local markets. The most remarkable feature of B.C. Central is that it invests primarily within the system from which it draws its funds. Of its \$173 million in loans and investments outstanding in 1975, 50% were directly in cooperatives and credit unions. Another 36% were held in very short term corporate notes for cash management purposes and could presumably be converted to cash should there be a sudden increase in membership loan demands. Thus,

virtually all credit union deposits remain within the system.

B.C. Central's importance as a promotional institution should also be noted. Competition for deposits demands timely and cost-efficient customer service as well as professional promotional activity and well-trained personnel. These are functions which all but the largest credit unions could not afford to undertake on their own.

VII. RELEVANCE TO THE ALASKA PERMANENT FUND

Purposes: B.C. Central, as noted in the July 11, 1977 report, is the best model of a cooperatively owned state central bank capable of providing deposit and lending services to those rural areas too small for full commercial banking services. It has the twin advantages of insuring local, cooperative ownerships sensitive to local needs on the one hand. On the other hand, it provides aggressive centralized capital and management services to ensure that each village receives the most sophisticated economic development assistance possible.

It is also important to note that British Columbia's economy, geography and demography is not unlike Alaska's.

Sources of Funds: B.C. Central's equity comes from the local member cooperative banks or credit unions. It is owned

and governed by local users. As noted in the July 11, 1977 report, the Permanent Fund could initially capitalize the state central bank, and then arrange to transfer ownership to the local cooperative banks. This could be along lines used to devolve ownership of the Farm Credit System from the Federal Government to local users. For a description of that procedure, see II.

Rationalization Models and Options in this Report

B.C. Central's debt is raised in international capital markets, based on its strong equity base and sound management. The Alaska Permanent Fund and its affiliated Alaska State Central Bank could do the same.

Uses of Funds: B.C. Central is a model of a strong central organization capable of raising international capital to support effective local economic development under effective local control.

Management: B.C. Central is governed by its local user institutions and attracts extremely able and aggressive central management.

Accountability: B.C. Central is fully accountable to its local member cooperative banks. The Alaska Permanent Fund could ensure that it is equally accountable to public purposes.

TABLE II
Consolidated Balance Sheet
1975

ASSETS

Cash and Demand Deposits	\$35,296,728
Short Term Deposits, due 1976-1979 (callable notice 1 - 15 days)	13,000,000
Investments	81,680,246
Loans	91,823,385
Mortgages Receivable	15,165,509
Accounts Receivable and Accrued Interest	4,099,861
Land, Buildings and Equipment	2,224,522
	<hr/>
	<u>\$243,290,251</u>

LIABILITIES

Notes Payable and Deposit Balances	\$200,317,269
Accounts Payable, Accruals, and Outstanding Acceptances	6,495,372
Deferred Income Taxes	215,400
Provision for Dividends	1,875,595
Retained Earnings	3,086,610
Members' Shares	31,300,005
	<hr/>
	<u>\$243,290,251</u>

TABLE III
Income and Expense Statement - 1975

INCOME	
Loan interest	\$ 7,745,411
Investment income	15,096,769
Service charges and sundry	1,340,040
Fees for services to members	2,643,521
Members dues	349,007
	<u>27,174,748</u>
DIRECT EXPENSES	
Interest on deposits	14,393,292
Interest on borrowings	4,123,399
Service charges and sundry	423,963
	<u>18,940,654</u>
INCOME LESS DIRECT EXPENSES	<u>8,234,094</u>
ADMINISTRATIVE AND GENERAL EXPENSES	<u>5,803,650</u>
EARNINGS BEFORE TAXES	2,430,444
Income taxes - deferred	131,609
NET EARNINGS FOR THE YEAR	<u>2,298,835</u>
Retained earnings - beginning of year	<u>2,659,631</u>
	4,958,466
Dividends	<u>1,871,856</u>
RETAINED EARNINGS - END OF YEAR	<u>\$ 3,086,610</u>

I. PURPOSES

The Deutsche Genossenschaftsbank (German Cooperative's Bank or DG Bank) is the central reserve bank of the vast West German cooperative system. Founded as the Deutsche Genossenschaftskasse, a cooperatively-owned financial institution, shortly after World War II, it was reorganized as a corporation and renamed the Deutsche Genossenschaftsbank in 1972.

DG Bank is the apex institution of a three-tiered system which holds 13% of all deposits in German financial institutions. The base of the system is composed of some 6,400 small banks and building societies which service the members of agricultural, industrial and trade cooperatives, as well as unaffiliated depositors. Ten regional cooperative banks provide liquidity management, auditing, check clearing and investment services to the base. DG Bank provides similar services to the regional banks. This system and DG Bank's place in it are described below.

Cooperatives in Germany

Structure of the Movement - After World War II, the German cooperative movement was organized into four sectors, each with its own credit system and network of regional and national unions.

The four sectors are agriculture, industry, consumers coops and non-profit housing finance societies.

By far the largest of these sectors is agriculture. In 1971, more than 1.8 million farmers were members of one or more of the 12,590 local societies. 1,650 marketing and supply cooperatives, 4,300 trade cooperatives and 12 centralized cooperatives with 1,500 branches or depots were engaged in the buying and selling of goods and achieved a total turnover of \$6.4 billion.* In addition, there were in 1971, 4,780 specialized cooperatives with 29 affiliated regional federations. The agricultural credit coops take deposits from and finance the fixed and working capital requirements of their members.

The industrial and trade cooperatives perform similar functions, and are active primarily as central material purchasers for their members. They were serviced by 624 coop banks in 1971.

Consumer and non-profit housing coops (central purchasing agents for the residential construction industry) comprise a relatively small part of the system.

The breakdown of local financial institutions servicing these sectors in 1971 was as follows:

*All monetary figures in the text are given in dollars, converted from DM at the exchange rate prevailing at the time the figure was reported. This is done for ease of comprehension. Figures in Tables I and II are presented in DM, where a sense of proportion is more important than absolute totals.

Agriculture	5,680
Industry	668
Housing and Consumer	45
	<hr/>
Total	6,393

The system also includes 10 mortgage banks unaffiliated with cooperative societies.

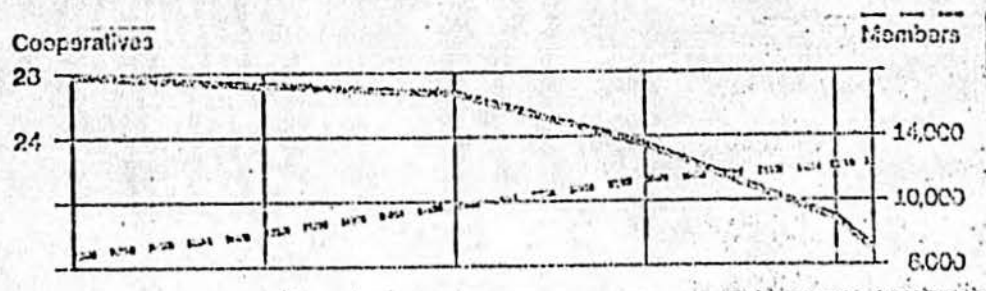
Recent trends in total units and membership are illustrated in Figure I. Overall, the graphs show increasing membership and concentration, especially in the two most important sectors, agriculture and credit. Concentration has mostly been achieved through the merger of two units.

Despite these mergers at the local level, the cooperative system maintains the most extensive branching system of any sector of the German financial market, and its units are incredibly small. In 1971, there were 18,665 coop bank branches, compared to 14,506 for savings and 5,428 for commercial banks. In terms of aggregate balance sheet totals, the cooperatives are behind both the other sectors. The average balance sheet total for the banks serving industrial coops was \$23.3 million; for those servicing agricultural customers, only \$3.7 million.

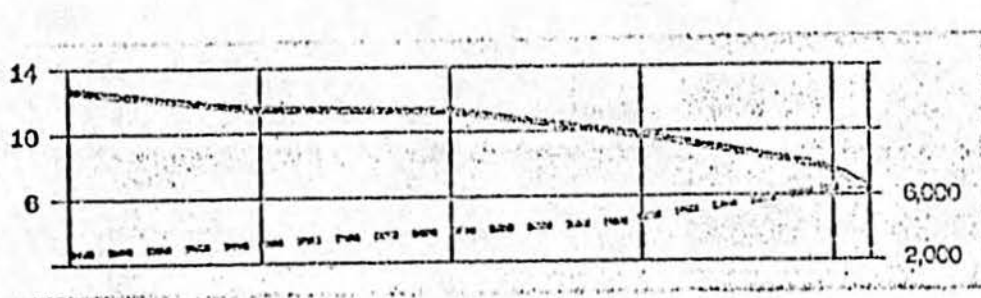
These changes at the primary level have affected the structure and operations of the regional cooperative banks. Each merger of two local units tends to reduce deposits with the regional banks, because the compensatory movements of

FIGURE I

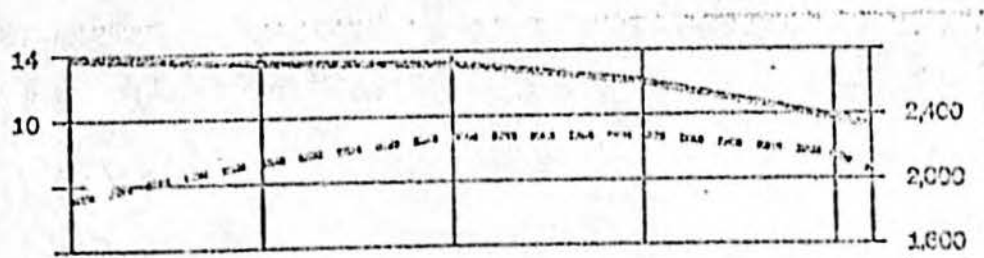
Cooperatives and Their Membership in the
Federal Republic of Germany



Primary Cooperatives - Total

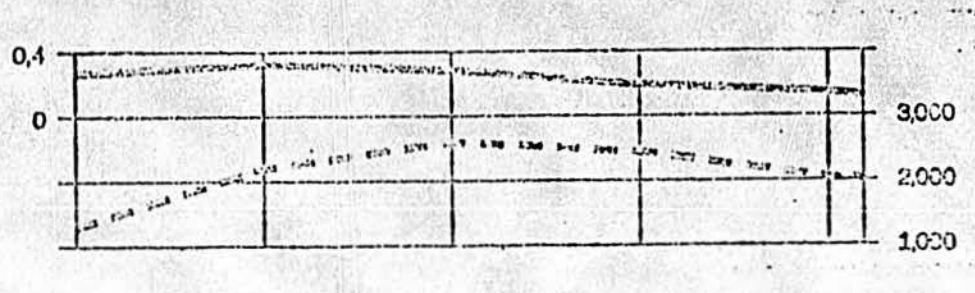


Cooperative Banks

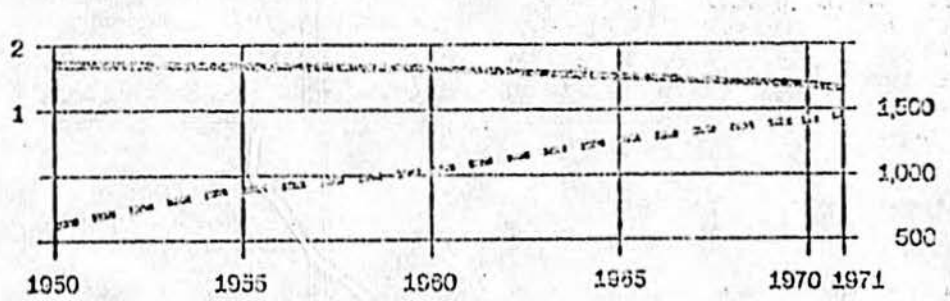


Trade and Service Cooperatives

FIGURE I (continued)



Consumer Cooperatives

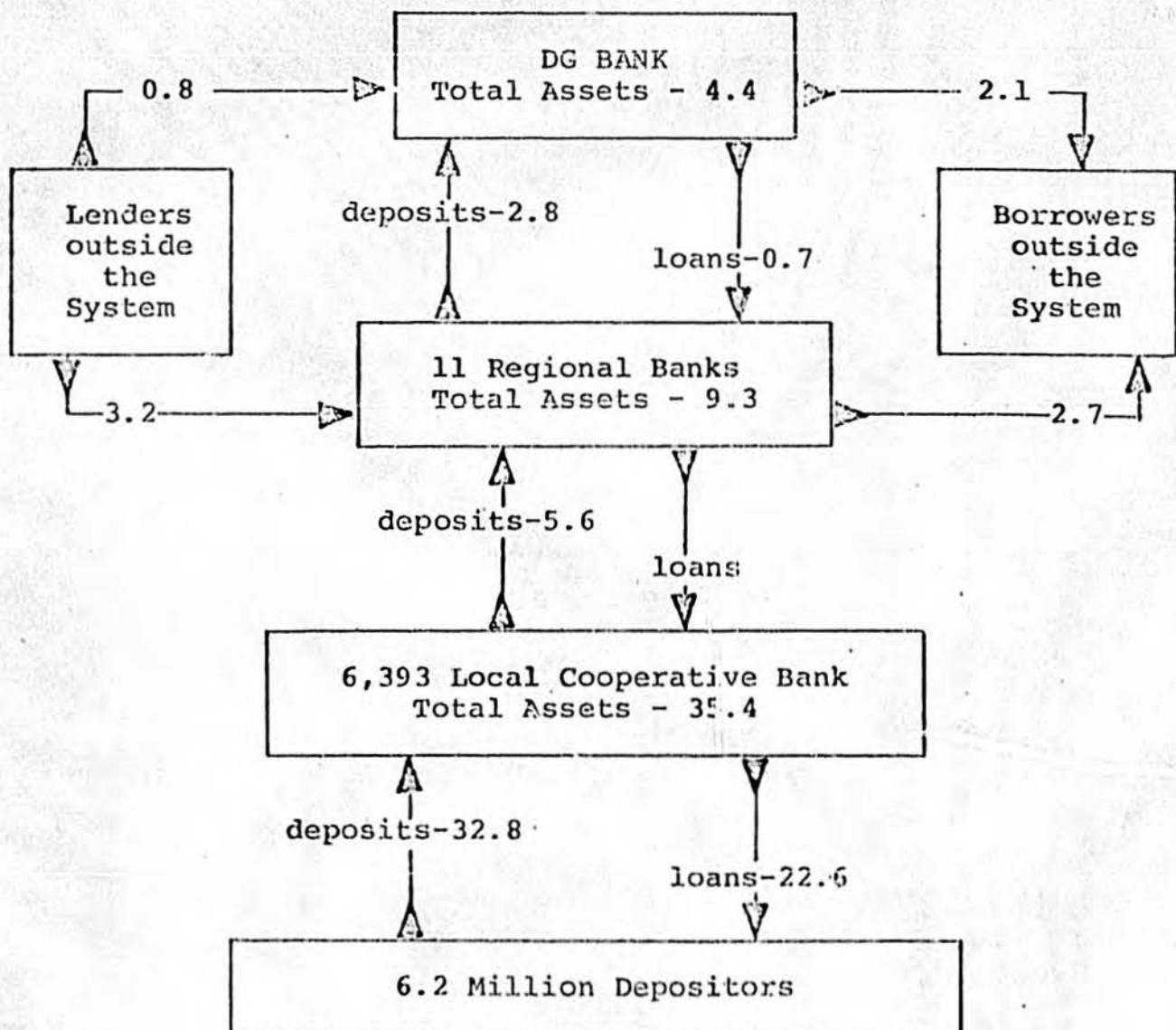


Cooperative Building Societies

FIGURE II

The German Cooperative Financial System (1971)

Figures in billions of dollars (US) at the then-prevailing exchange rate



liquid funds increasingly take place within the new unit, instead of passing through the central institution. The percentage of customers' deposits held by the local cooperative banks at their affiliated regional bank has therefore been declining. Also, larger local cooperative banks usually make heavier demands on their regional banks, on which they depend for long-term funds to finance expansion in the volume of lending.

This situation has led to the need for larger units at the regional level, capable of maintaining larger balances of loanable funds and providing services such as check clearing where economies of scale can be realized. Since 1968, the parallel regional systems of the various primary cooperative sectors have been in the process of consolidation, and the number of regional cooperative banks has fallen from 18 to 10. Of these, seven have reorganized as corporations able to sell shares to the general public. These regional banks, in turn, rely on DG Bank for depository, liquidity management and other essential services. The financial interrelationships of this system, from local depositors to DG Bank are shown schematically in Figure II.

Sources of Funds - The source of funds to the local system is the deposits of members. The local coops offer a full range of deposit accounts and instruments: checking and savings

accounts, negotiable and non-negotiable savings certificates. These last instruments are issued for terms of 7 years and their proceeds are earmarked for term lending to medium-sized firms.

Uses of Funds - Besides consumer, home mortgage and business loans to members, coop banks undertake a number of lending and investment activities. These include construction financing, term loans to other credit cooperatives and industrial customers and leasing.

DG Bank Operations - DG Bank provides financial and non-financial services to the regionals in order to help them facilitate these local activities. Such tasks performed jointly by DG Bank and the regionals include check clearing, centralized electronic transaction procession, property broking, secondary mortgage marketing, advertising, personal training, and the placement of reserve and surplus funds in investments outside the cooperative system. This last function is reserved primarily to DG Bank. They underwrite and market domestic and foreign corporate equities and securities of various governments and public authorities.

II. SOURCES OF FUNDS/CAPITALIZATION

Equity - DG Bank is capitalized by the purchase of shares. Of the \$134.5 million in paid-in equity in 1975, some 75% was

held by the regional banks. The rest was held by corporate and institutional investors outside the cooperative system. The current dividend on shares is 8%.

Deposits - DG Bank's main source of deposits is the regional banks' reserve and surplus. Of the \$7.92 billion on deposit in 1975, \$5.36 billion was attributable to the regionals. Other banks and corporations provided the balance of the deposits. DG Bank pays interest on these deposits at prevailing rates, and these interest payments compose their largest financial expense. The volume of deposits in the entire system has risen rapidly in recent years.

Borrowings - When necessary to increase its base of loanable funds, DG Bank will raise money on the European bond market through issue of its own bonds. In 1975, it had \$832 million outstanding--down from recent years due to the simultaneous increase of deposits and decrease of loan demand within the coop system.

Income - Net interest payments on loans compose by far the largest portion of DG Bank's income, some 86% of the \$606.5 million in 1975 gross earnings. Other sources of income include that from investments and securities, commissions and fees and miscellaneous sources amounting to \$11.8 million.

III. USES OF FUNDS/INVESTMENTS

Because loan demand in the sectors from which the cooperative system draws its deposits--agriculture, small business and middle-income individuals--has fallen in recent years, DG Bank has had to find uses for its investible funds outside the cooperative system. Some 57% of its \$7.5 billion in loans outstanding in 1975 were to banks outside the cooperative system. Another 26% were to non-bank, corporate customers, leaving 17% to be channeled back to the regional banks. Over 70% of these loans were for terms of less than four years.

Unlike American banks, German banks are not restricted from engaging in equity and underwriting transactions involving corporate securities, and they may own subsidiaries directly instead of through a holding company. All these activities figure prominently on DG Bank's balance sheet. Of the \$1.24 billion in investments held by the bank, 46% are in corporate bonds, many of which DG Bank underwrote. Three percent was held in other securities, mostly corporate equities, 12% in shares of subsidiaries and 39% in Treasury notes.

DG Bank's underwriting business is substantial. In 1975, it underwrote 17 large issues, mostly for German public authorities and political units. The Bank also participated

in 47 other issues as guarantors for various private and public entities.

DG Bank held equity interest in over 50 other financial institutions, including the seven regional banks reorganized as corporations. Among the Bank's wholly-owned subsidiaries is the Deutsche Genossenschafts-Hypothekenbank, one of Germany's largest mortgage banks, several closed-ended mutual funds and several foreign subsidiaries engaged in placing DG funds in investments abroad. DG Bank also owns 19 and 50%, respectively, of the shares of the two leasing firms whose services they broker to the regional banks.

Thus, using the very sparse information provided in DG Bank's annual reports and including accounts which may register holdings outside as well as within the cooperative system, it appears that only 18.6% of DG Bank's investments are in the cooperative system.

IV. MANAGEMENT

The top level of management is the Managing Board, composed of five members elected by representatives of the regional banks and cooperative unions. DG Bank does not report the breakdown of managerial responsibility between its various divisions. Nor do they present any overriding management policies besides

a commitment to helping local credit cooperatives achieve a greater market share.

V. ACCOUNTABILITY

DG Bank is a privately-owned corporation and thus enjoys almost total freedom in its investment and liability-generating policies. It is restricted only insofar as it must obey laws designed to protect depositors.

VI. EVALUATION

DG Bank's major purpose is to help the thousands of tiny financial units which compose the cooperative credit system remain competitive with other sectors of the German financial system characterized by larger units. Banks in these other sectors tend to deal in larger blocks of money and thus have lower unit transactions costs. DG Bank and its regional affiliates seem to do this job well. From 1973 to 1975, the share of deposits in all German banks held by cooperatives increased from 11 to slightly more than 13%.

Perhaps the most striking aspect of DG Bank's operations is the extent to which it invests outside the cooperative system, especially when compared to the British Columbia Central Credit Union. Such a comparison is misleading, however, in that the

real economic conditions in the two institutions' deposit markets may be entirely different. Young families are heavily represented among the British Columbian cooperatives' members. Their demand for large mortgage loans is high, and they tend to keep little in savings. Thus, their central bank must channel funds from outside the system to its member units if they are to continue to compete for loan business.

DG Bank is the lead institution of a complex system financing many types of economic activity. Its managers claim and behave as if loan demand is declining in these sectors. An analysis of these sectors and a critique of DG Bank's lending policy is impossible given the paucity of information on these activities available in secondary sources and the Bank's own tight-lipped reporting policies. Management may be doing its members a service by investing outside the system if that is where their funds can earn the greatest return.

However, one of the Bank's financial policies does seem to be a disservice to the member cooperatives. This is the selling of shares by both the regional banks and DG Bank to investors outside the cooperative system when liquidity appears to exist among the individual cooperatives to buy these shares. Thus, earnings on the deposits contributed by the units at the base of the system (and ultimately their members) are siphoned off

to outside investors through the payment of dividends. According to our own calculations based on information given in DG Bank's annual reports, these payments outside the system amounted to 18.9% of the Bank's net earnings in 1975.

VII. RELEVANCE TO THE ALASKA PERMANENT FUND

Purposes: DG Bank provides an important counterpoint to BC Central. It shows what happens to a similarly constituted cooperative development bank when it matures in a mature industrial economy.

Sources and Uses of Funds: DG Bank is no longer wholly owned by its users. It now is a net exporter of funds--not only out of local cooperatives, but out of Germany.

Management and Accountability: DG Bank is increasingly less accountable to its local cooperatives. It manages its funds similar to a large multi-national bank.

TABLE I
Balance Sheet - 1975

	DM Million
ASSETS	
Cash and Bills Receivable	627.4
Due from Regional Cooperative Banks	3,198.3
Due from Other Banks	
Less Than Four Banks	9,852.9
Four Years and Over	909.5
Treasury Bonds	1,313.1
Bonds and Notes	1,625.5
Other Securities	117.8
Loans and Advances to Non-Bank Customers	
Less Than Four Years	3,324.9
Four Years and Over	1,459.6
Due from Public Authorities - Equalization Claims	86.9
Own Bonds Held for Trading Account	38.0
Fiduciary Transactions	165.2
Investments in Subsidiaries and Affiliates	413.0
Premises and Equipment	45.1
Other Assets	107.6
Total Assets	<u><u>23,284.8</u></u>
LIABILITIES	
Deposits of Regional Cooperative Banks	13,381.9
Deposits of Other Banks	
Less Than Four Years	3,528.4
Four Years and Over	1,683.9
Deposits of Non-Bank Customers	1,192.5
Bonds and Notes Issued	2,302.1
Fiduciary Transactions	165.2
Other Liabilities	283.5
Capital Stock	366.6
Reserves	355.0
Profit After Transfer to Reserves	25.7
Total Liabilities	<u><u>23,284.8</u></u>
Endorsement Liabilities	417.8
Guarantees	1,694.7

TABLE II
Income and Expenses - 1975

INCOME	DM '000
Interest Earned	1,305,936.6
Income from Securities and Investments	159,911.1
Commissions and Fees	18,741.5
Other Income Including Adjustment of Special Reserves	29,471.3
Total Income	<u>1,514,060.5</u>
EXPENSES	
Interest Expense	1,272,019.7
Commissions	1,813.7
Depreciation, Provisions, Transfer to Special Reserves	32,048.8
Staff Expenses	34,542.4
Other Operating Expenses	23,918.2
Taxes	19,192.4
Other Expenses	4,852.5
Total Expenses	<u>1,388,387.7</u>
NET INCOME	125,672.8
Transfer to Reserves	100,000.0
PROFIT AFTER TRANSFER TO RESERVES	<u>25,672.8</u>

II. REGIONAL MODELS AND OPTIONS

REGIONAL MODELS
Discussion Draft

September 14, 1977
Page 149

International and Domestic Patterns

International development banking provides a pattern for regionalizing the Alaska Permanent Fund which is strikingly paralleled in a number of publicly-sponsored American development finance systems. In each instance a three-tiered arrangement has evolved with these common elements:

First, a government-sponsored development bank or fund which oversees the whole system.

In the middle, regional development banks or corporations which are more sensitive to local differences and act as a bridge between local needs and national or state resources.

At the bottom, local development corporations or banks with a great deal of autonomy and flexibility to respond to local needs and differences.

This essential three-tiered pattern is found in the international development banking system headed by the World Bank, in sophisticated national development banking systems in Third World countries such as those of Brazil, Mexico and India, and in regional development banking systems of developed countries of Europe such as France or Italy. The same pattern is followed in publicly-sponsored American credit systems such as the Farm Credit system and the Federal Home Loan bank system.

It is no coincidence that this pattern repeats itself in such a range of settings. The advantages of this pattern are elementary, sensible, and obvious.

In each instance, the system is publicly-sponsored and accountable but independently operated by an experienced, career-minded professional staff. Both capital and management are organized on a long-term basis and initial public investment is used to generate larger amounts of private capital from the private capital market.

Just as international and domestic experience provides us with important parallels, each gives us a better understanding of different aspects of the overall structure and organization which could help define the Alaska Permanent Fund as a development bank capable of supporting the quite different regional economic needs of different areas of Alaska.

For instance, international development banking systems are superior to American development finance systems in the provision of infrastructure financing and venture capital. By definition two major American credit systems, the Farm Credit system and the Federal Home Loan bank system, do not provide either long-term infrastructure finance or essential venture capital to new enterprise. Venture capital is essential to the development of rural regions of Alaska and lower-income

communities in those regions, as it is in Africa, Asia or Latin America.

Just as the international development banking systems help us understand the basic capital formation instruments for development banking systems, particular American experience in structuring financial institutions gives us a set of basic guidelines for constructing the regional units of the Alaska Permanent Fund. After looking at the evolution of international experience, it is worth taking a close look at the specific legal, financial and organizational mechanisms used by successful American development finance systems.

International Models

One of the most appropriate transferable lessons from international development banking experience is that a network is necessary in order to support regional economic development--not a single, monolithic institution. This is especially true where regional and ethnic distances are great, where infrastructure is inadequate, and where sensitivity to local needs must be particularly acute.

The evolution of the international development banking system into a geographically decentralized and functionally differentiated worldwide system was neither wholly planned nor

conscious. It simply evolved to fit the rising needs of various developing countries and regions of the globe.

For instance, early on, the World Bank began to recognize the value of working through local intermediary development banks, since they were much more sensitive to local practices and, in many cases, more likely to make sound financial judgments about loans and investments. The World Bank group began to work with existing national development banks and to sponsor the creation of a worldwide network of national private development finance corporations in a host of Third World countries.

Second, in large and complex countries with large geographic areas and significant regional differences, we can observe a tendency to complement this international decentralization with an intranational regional decentralization to subnational institutions. In one study of 209 development banks, nearly 40 percent were located in 10 countries--Argentina, Brazil, Colombia, India, Malaysia, Nigeria, Pakistan, the Philippines, Spain, and Venezuela--each of which has developed extensive, decentralized and regionalized development banking systems.

Third, this pattern repeats itself once again in the sophisticated and elaborate regional development banking systems which have been organized in France, Italy, and the United Kingdom.

At the base of each system is the fundamental unit--the local development bank or corporation which serves to broker the risk between the local entrepreneur and the outside sources of capital. Between the local development corporation and the apex of the system there is often a regional development bank or corporation which mobilizes its own capital for local use and may be required to broker-finance between the local and the top institutions. At the higher levels in any event there is also a careful elaboration of different infrastructure and equity "windows" to provide more discrete forms of capital for specialized purposes. Figure 1 provides a highly abstract and stylized version of the institutional relationships among the World Bank, multinational regional development banks, and local national institutions on the one hand, and national development banking institutions, regional and local development corporations on the other hand.

An American Parallel: The Farm Credit System

The Farm Credit system has evolved as a highly sophisticated, publicly-sponsored but user-owned development finance system like the international development banking network. It has unfolded gradually since its establishment in 1916, assuming new functions and becoming more decentralized in response to

the credit needs of farmers. Today the federal Farm Credit Board and the Farm Credit administration operate at the financial level, while twelve district Farm Credit Boards at the regional level serve hundreds of constituent associations and cooperatives at the local level. The functional diversity of this system is reflected in twelve federal Land Banks serving 594 constituent Federal Land Bank Associations, twelve Federal Intermediate Credit Banks working with 442 local production credit associations, and twelve banks for cooperatives serving constituent farmers in cooperatives. This arrangement provides three different functional "windows" of credit to member farmers and ranchers in each of the twelve regional Farm Credit Boards.

The Farm Credit grid system, then, parallels the international development banking patterns both in its geographic decentralization of decision making and its separation of different functions. The pattern of geographic decentralization is repeated again in other American financial networks such as the Federal Home Loan bank system and, of course, the Federal Reserve system. These important domestic parallels not only confirm international experience; they also provide us with proven, workable, legal, financial and organizational precedents for a regionalized Alaska Permanent Fund.

The Farm Credit system has, for example, developed two structural attributes worth noting and using in constructing a regionalized Alaska Permanent Fund. In a characteristically American fashion, on December 31, 1968, the Farm Credit system became 100 percent user-owned with retirement of the original federal government capital investment in the system. Part of each farmer's loan purchases stock ownership in the capital structure of the banks and associations. Member farmers elect the Board of Directors of the Federal Land Bank Association, production credit associations, and cooperatives; the Boards of the associations and cooperatives in turn elect the District Farm Credit Board and make nominations to the President for the federal Farm Credit Board (see attached Figure 2).

The local users govern the system by electing or nominating each governing board in the system. The local users eventually repurchase the ownership of the system from the federal government with a small percentage of the proceeds received from the system. This user governance and eventual user ownership is a critical precedent for establishing local cooperative banking institutions in communities in the state too small to properly support a full-service bank.

Second, the private capital market finances the \$8 billion debt of the Farm Credit system through the sale in the bond

market of consolidated federal Farm Loan bonds. "Consolidated" is primarily what they are: thousands of individual farm mortgages, crop loans and farm equipment loans which have been put together by the Farm Credit system for resale in the private capital market. The private capital market supplies the bulk of the funds used, not the Treasury. On the other hand, the Treasury's standby credit is assurance to the market that the government stands behind the obligation, even though there is no direct government guarantee. I similarly feel that with the huge paid-in capital base of the Alaska Permanent Fund it will similarly be possible to sell many such packaged private obligations in consolidated bonds in the marketplace with the standby backing of the Alaska Permanent Fund itself.

Unlike virtually all international development banking systems, the Farm Credit system has not developed an affiliated venture capital corporation. As a result, the Farm Credit system is precisely that--a 100 percent debt financing system which is no longer able to respond adequately to the needs of those low-income farmers and lesser-developed regions of the country which it was originally set up in the 1920's to serve. Nor has it been able to be effective in its original purpose of seeking to end farm tenancy by making landowners out of share-croppers. Credit does not make owners, only debtors. The

banks for cooperatives, for example, usually limit facility loans to not more than 60 to 40 percent of the value of the security offered by the cooperative, and expect the balance to be financed by the association's permanent or long-term capital. This is fine for a wealthy cooperative that has built up sizable membership equity, but it is not very helpful to low-income cooperatives whose members by definition have no equity and, therefore, whose cooperative is ineligible for a loan from the bank for cooperatives.

It is for this reason that I have argued strongly in my memorandum to the committee of July 11, 1977 that the community development provisions of the Alaska Permanent Fund legislation should provide for equity investment as well as debt and guarantees, just as with productive private enterprise.

Other Domestic Models

The pattern for establishing and operating the Farm Credit system is paralleled in other major American financing systems such as the Federal Home Loan bank system. In each instance there is one initial large public capital stock purchase by the Treasury, which starts the system. After that the system pays its own way except for relatively small periodic appropriations to cover non-recoverable infrastructure and social overhead

capital costs. Eventually the Treasury stock is repaid and completely replaced by user-owned stock. For example, the initial \$75 million of Treasury stock that started the Federal Home Loan bank system in 1933 was fully retired by 1950, just as was the Farm Credit system.

With strong debt to equity ratios most of these same systems have been able to raise the substantial body of their capital on the private market through secondary marketing operations with strong paid-in equity capital backup.

FIGURE 1.

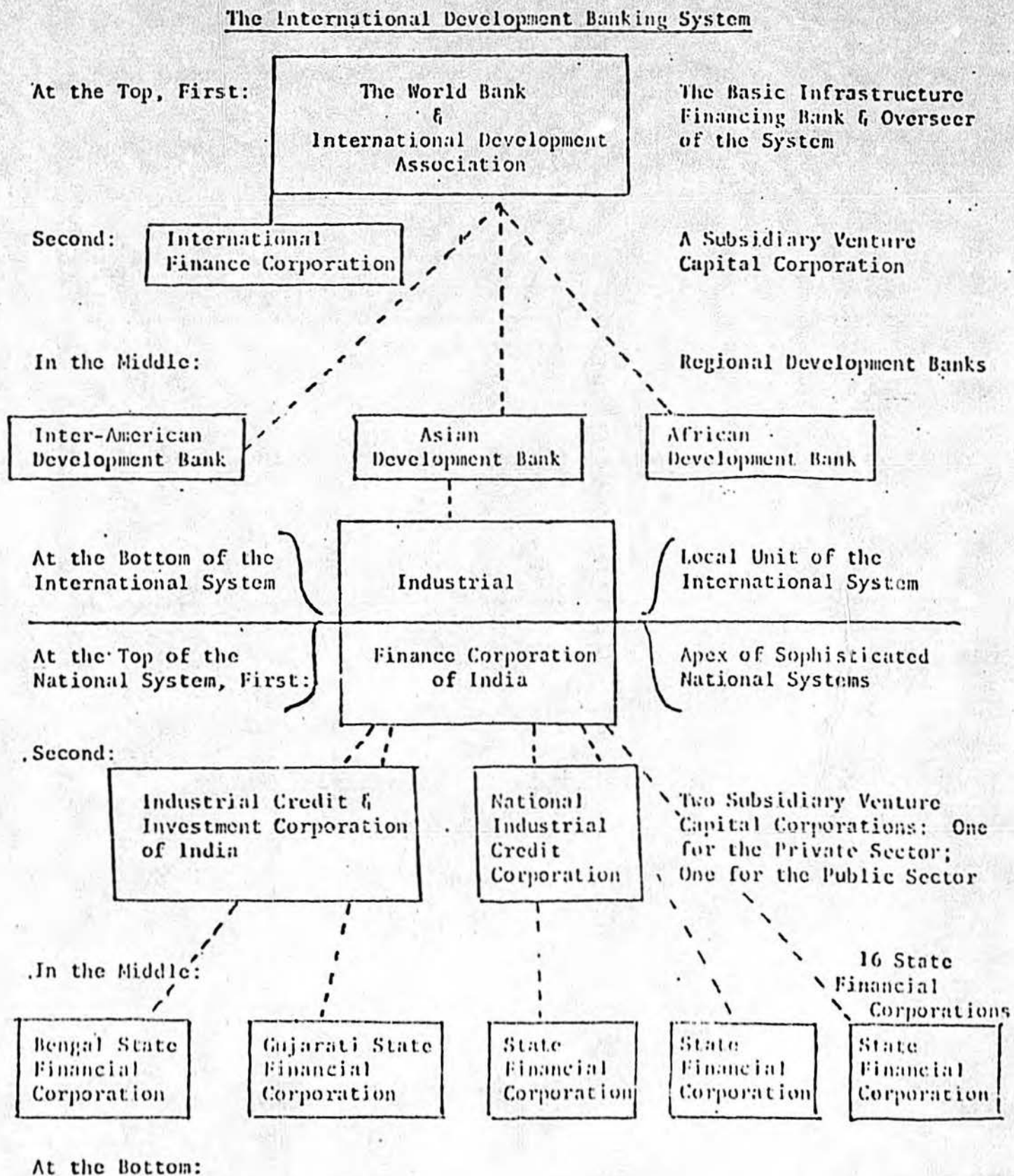
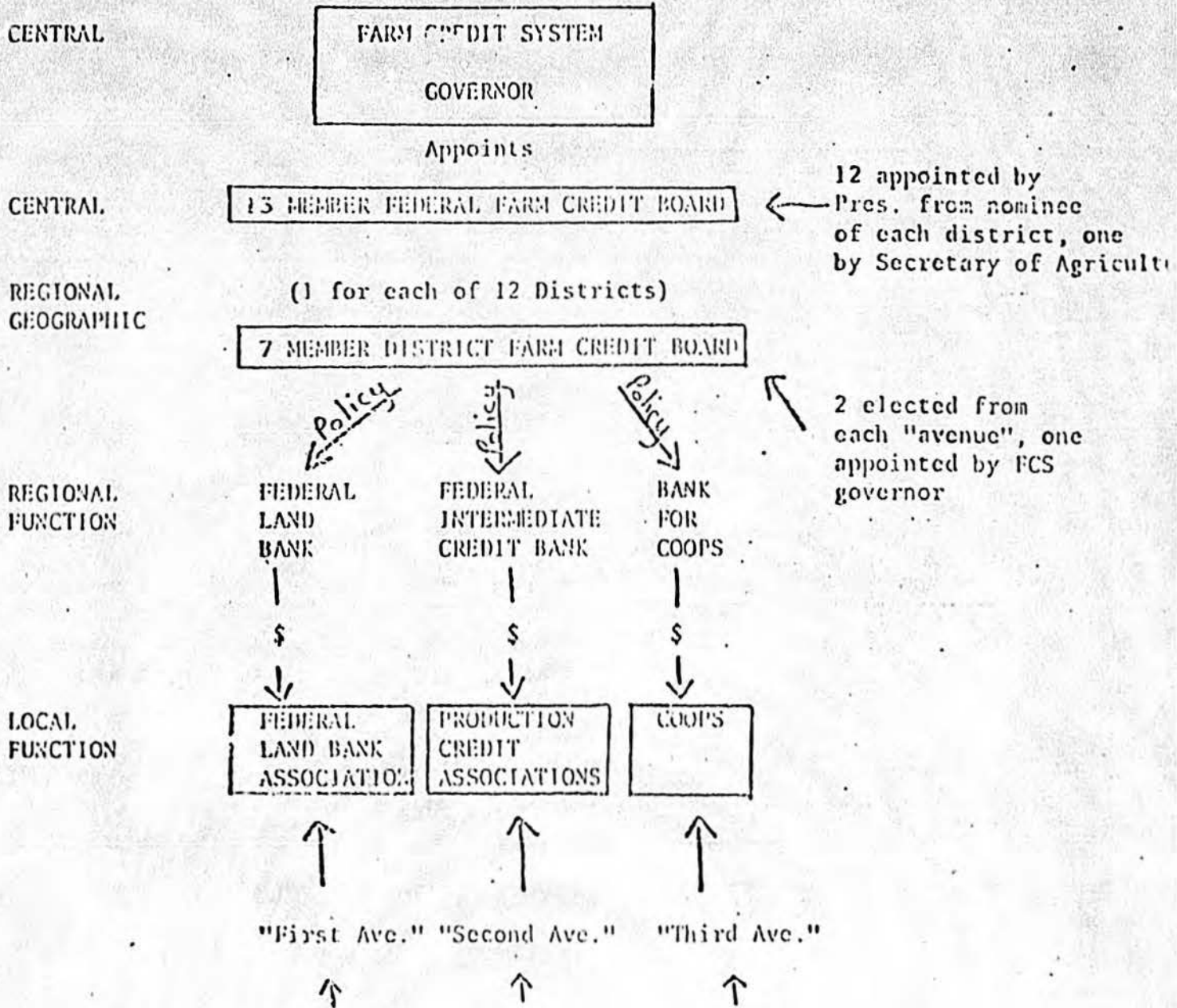


FIGURE 2

THE FEDERAL CREDIT SYSTEM



The Boards of Directors of the Federal Land Bank Associations, Production Credit Associations, and Cooperations are elected by member farmers.

In Summary: A Range of Options for Regionalization Available
to the Alaska Permanent Fund

The experience of domestic and international development banks points out that the Alaska Permanent Fund has a number of specific options that might be used for purposes of regionalization. Specifically, the Alaska Permanent Fund might make local regionalized investments through: independent regional or local development banks or corporations; affiliates; subsidiaries; user-owned local institutions; branches; or some flexible combination of the above developed on an ad hoc basis. Each of these will be briefly referred to below.

Independent regional or local development banks or corporations: The World Bank and the European Investment Bank are both examples of institutions which primarily operate by making loans to and through independent regional and local intermediaries. Analogously, the Alaska Permanent Fund might make all regional investments to or through Alaskan regional and local community development corporations.

Affiliates: The French Crédit National finances its regional development through affiliated Regional Development Corporations. It has a substantial although not controlling stock interest in each of these SDRs. The predominant equity interest is held by local financial and development institutions with a greater sensitivity to local needs and conditions.

Subsidiaries: To the best of our knowledge, no development banks within the United States or overseas operate through their regional development programs through wholly-owned subsidiaries. On the other hand, many development banks, including the World Bank and the D.G. Bank, do use wholly-owned subsidiaries in order to undertake specialized functional financing activities such as equity investment.

User-owned local development banks or corporations: As we have extensively documented, the Farm Credit System, the Federal Home Loan Bank System, the British Columbia Central Credit Union, and the D.G. Bank are all institutions which are user-owned at both the regional and central level by local, cooperatively-owned development banks.

Branches: The Federal Reserve System and the British Finance for Industry are two central financial institutions which operate their regional activities through branches.

A flexible, ad hoc approach: The National Enterprise Board and the Canada Development Corporation are two large national development banks which have taken a needs-oriented ad hoc approach to regionalization. The National Enterprise Board, for instance, has recently established branches in Liverpool and Newcastle in order to get a better sense for how they could intervene in regional economic development. The Canada Development

Corporation has a sole branch in Vancouver in order to be more responsive to the regional economic development needs of western Canada and is undertaking its venture capital program through investments in affiliated privately-owned venture capital companies.

Our purpose in this regionalization paper, as in each of the sections of this second report, is to suggest a number of options which can then begin to be tailored to fit the specific purposes, needs and political economy of Alaska in designing the Alaska Permanent Fund. Based on the response of the legislature, this paper may also raise a number of follow-up questions which deserve further attention.

III. THE PROBLEM OF ACCOUNTABILITY

AN INTRODUCTION TO THE ISSUE

The question of assuring the accountability of the Permanent Fund management to the electorate, legislature and executive to carry out its public purposes is probably the single most important issue before the Special Permanent Fund Committee. In this final section of the report, we begin to suggest some measures by which the management of public enterprises such as the Alaska Permanent Fund may be held accountable for their performance. Because this is such a central issue, our aim in this section is simply to introduce the problem and begin to suggest some of the options available to ensure public accountability. We will detail some of the tradeoffs involved and cite specific cases from domestic and international experience.

It is important to point out at the beginning that the record is generally not a good one. In more cases than not, public accountability has been sacrificed for market efficiency. The task of overseeing the Permanent Fund to ensure that its public purposes are carried out will not be an easy one. Our sense is that this introductory discussion will raise many more questions that the Committee will want to consider between now and December 31, 1977. By "accountability" we mean the effectiveness

of the mechanisms by which the government seeks to assure that the managers of a public enterprise invest public resources in order to maximize the benefits to the ultimate providers of the funds. In the case of the Permanent Fund, those providers are the people of Alaska.

In some respects, the position of Alaskans in this enterprise is analogous to that of an investor in a private firm. The active investor gathers as much information as possible about the firm in which he invests. Using this information, he forms an independent judgment on appropriate management policies. He then seeks to have these judgments acknowledged and effected by participating in shareholders' meetings and by voting his shares. If, after these measures are exhausted, he is dissatisfied with managerial performance, he will seek to impose sanctions on the firm's operations by voting out management or, more likely, by withdrawing his money from the firm. In all these activities he is motivated by the principle of maximizing his benefit from the investment--his short-run money profit.

The benefit Alaskans expect from the Permanent Fund, however, is a good deal more complicated and long-lived than that sought by the private capitalist. Certainly, short-run financial results must be considered, but the idea behind the Alaska Permanent Fund is to convert non-renewable mineral resources into renewable

capital resources which benefit the Alaskan economy and Alaskans. These investments could generate many types of public costs and benefits. A small sample of costs Alaskans would seek to avoid includes degradation of the environment and social dislocation caused by the boom-bust nature of certain enterprises. Benefits might include wider participation of Alaskans in the management and wealth generated by business enterprises and the improvement of human services.

Experience has demonstrated that publicly-capitalized investment banks tend to operate solely under commercial profit-maximization criteria unless they are compelled to do otherwise through various forms of government direction and control. Our basic problems, then, are: 1) How is the substance of these directions to be determined? and 2) How are they to be enforced?

It is likely that no stable consensus can be reached on the proper mix of objectives for the Permanent Fund. Rather the Fund has many constituencies, each with different and often conflicting economic interests and with differential access to the political and economic means by which to have these interests effected.

To design the institutions surrounding the Permanent Fund as if the consensus mentioned above existed, as if it were the Fund's only task to interpret these objectives in its investment policy, may be virtually impossible, based on the experience of others.

Rather, the design of the Permanent Fund must provide a forum in which conflicts of interest can be aired and resolved on a continuing basis.

These conflicts are likely to arise at two points in the continuing operation of the Permanent Fund: first in the formulation of investment criteria and then in the application of those criteria. Those affected by these processes must have a chance to influence each of these sets of decisions. They must then have the means by which to review how these decisions are implemented.

In our investigations of the institutions profiled in Section I and other public enterprises we shall note, we have identified four stages in the accountability process. Two may be classified as forums in which the decisions mentioned above are made, two as means by which these decisions are implemented. In practice, these processes are carried on simultaneously.

Specifically, these stages are:

1) Setting of Goals and Priorities: The essential questions here are: Who sets the goals and how are they phrased in legislation, statutory directives, or guidelines?

2) Formulation of Measurement and Reporting Procedures: Goals are given operational substance by the establishment of measures to evaluate management performance. The issues here are: the relevance and quality of the measurements, the form in which

this information is presented, and who gets the information?

3) Governance: Public Inputs into Operating Decisions:

In most public enterprises, the elected government usually has a variety of formal and informal means of influencing day-to-day operating decisions. The enterprise's various constituencies also have such means. The important issues here are: Whose interests are made known to the Board? How and at what point in the decision-making process are they made known? What influence do they actually exert on the institution's operating decisions?

4) Operating Sanctions: What can an elected government do if it is dissatisfied with the results the management of a publicly-capitalized enterprise achieves? The most frequently available formal sanctions are the replacement of management and the withholding of funds from the agency. There are informal sanctions as well, such as publicity of mismanagement.

In the case of dismissal of management, the issues are: How and for what reasons can management be removed?

In the case of control of funds, some of the issues are: The source of funds and the conditions on which they are provided, who controls the funds once they are pooled for agency use, and the conditions under which the sanction of withholding funds can be exercised?

At each of the four stages, democratic elements of the

process must be traded off against the operating requirements of an efficient investment bank, i.e., the ability to make independent investment decisions and effect those decisions in a timely and flexible manner.

At each stage, outside control can range from zero to a level at which the operations of the agency are totally disrupted. Each level of control is characterized by a set of costs and benefits. In reviewing the four stages outlined above, we will present examples of mechanisms which have been used. They will be ranked from lowest to highest by the degree to which they effect management's deviation from standard commercial investment criteria. Finally, we will begin to suggest the nature and incidence of the costs and benefits of each strategy examined.

A. Setting of Goals and Priorities

Historically, the determination of goals and their definition in legislation has been the least important element in the accountability structure of public enterprise. In terms of enabling legislation itself, provisions for capitalization, organizational powers and management selection have had a much greater impact on the performance of these enterprises. The outcome of informal political and economic power struggles among the enterprises' various constituencies and principals has been more important to the active operation of development banks.

The goals of public banks are found in the opening sections of their enabling legislation. Seldom, however, do they represent the results of legislative deliberation. Bills are generally drafted by individuals who have some interest in the successful and continuing operation of the entity they are creating, and legislative attention is usually directed toward the operational aspects of the draft. In a few cases, the goals and objectives of development banks have been publicly debated, but, as in the case of the Canada Development Corporation, this does not assure that the public interest will be served.

The legislated purposes of most public enterprises tend to be more exhortatory than directive, legalisms intended to justify the use of public funds. In the case of authorities producing a good or service, the purpose is to do so efficiently; in the case of a public investment bank, it is to encourage the development of productive enterprise in the jurisdiction.

There are good reasons for leaving the statement of purpose vague, which have to do mainly with the legislative process: It is easier to build legislative consensus, easier to change operational direction to fit changing economic conditions, and harder to make small changes in language as the bill proceeds to enactment which substantially changes the intent.

Still, attempts have been made to formulate goals so that

they are useful as guideposts to management and criteria for managerial performance. Usually this entails relating goals to specific measurable achievements and administrative procedures in the legislation.

In most cases, the legislated goals of public enterprises or banks have had little bearing on their actual operations. This condition breaks down into two sets of conceptually separable experiences: In the first, management has found it convenient as well as legally and politically possible to evade its statement of purpose, undertaking operations for which the institution was not designed or refusing to undertake mandated functions. In the second, the statement of purpose has been so vague or founded on faulty analysis that the management has effectively been given a free hand.

Examples of the first type of experience occur most frequently in public authorities providing a good or service. Instances of selective adherence to statement of purpose arise in the history of the Port of New York Authority (PNYA). Established in 1921, the PNYA was charged with "developing terminal, transportation and other facilities of commerce." After a decade of unsuccessfully and unprofitably attempting to rationalize rail-sea connections, the Authority was allowed to acquire three motor vehicle bridges and the Holland Tunnel from other authorities.

These facilities were highly successful financially, and the Authority justified their continuing ownership of the bridges by claiming the revenues they generated were necessary to meet Authority bond contracts.

The PNYA used this same tactic in reverse in the Fifties and Sixties to resist public pressure to assume the ownership and management of the region's undercapitalized and unprofitable commuter rail system. Maintaining that the projected deficits of such operations would prevent them from executing bond contracts in good faith, the Authority's management withstood this pressure to undertake its mandated purpose for over a decade. A compromise was reached in the late Sixties when the Authority took over the most heavily-used portion of the commuter network in return for the approval of the Governor of New Jersey to use PNYA funds to build the World Trade Center. Many analysts view the Center as a speculative real estate transaction only peripherally related to the Authority's purposes. The commitment of substantial funds to the Center has in turn precluded the Authority's taking a significant role in the rail lines.

A similar instance can be found in the now-infamous case of Robert Moses' Triborough Bridge Authority. Its legislated purposes were solely to construct and operate the Triborough Bridge until it was paid off. However, through the imaginative use of

bonding power, bond contract drafting and the subtle use of clauses in the powers sections, the Authority's life and latitude in operations were enormously extended.

The statement of purpose for most public development banks fall into the second category outlined above: they are too inclusive to effectively direct managerial policy. The Canada Development Corporation is a prime case in point. In the CDC profile we noted how management's interpretation of the Corporation's goals threatened the achievement of the public purposes of the institution. This interpretation was permitted, however, by the CDC Act's statement of corporation objectives. These read:

"The objects of the company are;

- a) to assist in the creation or development of businesses, resources, properties and industries of Canada;
- b) to expand, widen and develop opportunities for Canadians to participate in the economic development of Canada through the application of their skills and capital;
- c) to invest in the shares or securities of any corporation owning property or carrying on business related to the economic interests of Canada; and
- d) to invest in ventures or enterprises including the acquisition of property likely to benefit Canada;

and shall be carried out in anticipation of profit and in the best interests of the shareholders as a whole."

These objects permit virtually any investment activity so long as it is profitable. They offer no priorities. More

importantly, only in the case of expanding investment opportunities do they provide an occasion for the application of quantitative measurements to some recognized standard of achievement. CDC's financial participation has led to the creation of only one new enterprise so far and has done little to open up investment opportunities for the greater number of Canadians. Yet this result is perfectly compatible with the Corporation's goals.

The British National Enterprise Board's statutory purposes, while broadly stated, are more amenable to measurement than CDC's and could thus become the basis of an accountability process. The purposes of the Board, as listed in the Industry Act of 1975, are:

- "a) to develop or assist the economy of the UK (or any part of the UK),
- b) to promote industrial efficiency and international competitiveness; and
- c) to provide, maintain or safeguard productive employment."

The first purpose is so broad as to accommodate any action the Board wishes to take within its extensive powers. The second two, however, are expressions of economic phenomena for which accepted empirical measurements exist. Industrial efficiency can be measured by cross-national comparisons of costs within sectors and the changes in profitability of individual firms; international

competitiveness by changes in the volume of export sales. The provision or maintenance of employment is similarly measurable, with differing degrees of sophistication.

The Community Development Finance Corporation Act goes one step beyond providing measurable goals by relating the goals to a specific set of problems described in the Act. Thus, the bill performs a clarifying function usually reserved to committee reports, and reduces the possibility of misinterpreting the goals in their implementation. The essential elements of the findings preceding the statement of purpose are:

- 1) that a substantial and persistently low level of employment and economic activity exists within certain areas of the state;
- 2) that it is beyond the ability of the government to correct these conditions solely through the exercise of regulatory power;
- 3) that it is beyond the ability of the private sector to counter these tendencies without capital assistance;
- 4) that Community Development Corporations have made substantial improvements in these areas, but cannot continue to do so without public provision of investment funds.

These findings all point directly to the purpose of the institution, which is to "increase the number of development projects in decadent substandard and blighted areas" through the agency of CDCs. The findings also militate against any alternative reading of the Act which might permit evasion of the administrative procedures outlined in the Act.

Such a specific set of findings, tied to specific objectives,

administrative procedures and reporting requirements, is one way of making the legislation statement of goals more meaningful.

F. Formulation of Measurement and Reporting Procedures

Public accounting is an essential element of governmental control over the activities of a public enterprise. This exposure forces management to keep operations in line with what is expected of them, and this pressure can work in anticipation of government censure as well as retrospectively.

Overseers of the Alaska Permanent Fund are interested in the social as well as financial achievements of the institution. On the financial side, public enterprise must be held to the highest standards of financial disclosure now universally applied to private enterprise. On the other hand, universally recognized measurement and reporting procedures have not yet been developed for social impacts. Many of the items presented for consideration by Singer and Mollenkopf in "After the Oil is Gone" are not amenable to quantification or comparison with unlike outcomes. This problem is treated in that useful paper, and we will not discuss it further here. Rather, we will note some practices used by some development banks to measure non-financial results, and comment on their appropriateness to the Permanent Fund.

Finally, accounts are inherently incomplete in that they

show only what has already happened--and not always very accurately. If an institution is expending public money, it should be concerned with the social choices it faces and present these choices to its overseers. We will look at some of the attempts public investment banks have used to address this problem through cost-benefit analysis and various other types of projection techniques and discuss their applicability to contemplated Permanent Fund operations.

Financial Reporting

Given the geographic and cultural distance from the institutions we have noted, it is difficult to evaluate the accuracy or fairness with which they represent their performance in annual reports. It must be noted, however, that management of public as well as private firms is motivated to present its accomplishments in the most favorable light.

What, then, is presented besides the usual balance sheet, income and expense statement, and report of changes in capital? One of the most important and useful parts of the annual report, usually required by national corporation laws, is separate reports on the activities of subsidiaries, major loan recipients or subdivisions. Consolidated financial records may conceal cross-subsidations, multiple accounting of depreciation of a given

asset and, most importantly, the true cause of poor performance, whatever it may be. This has been the case with the Small Business Administration's loan guarantee program. For years, the high loss rate of this program had been attributed by the SBA to instability in the small business sector. Investigation of the program by the General Accounting Office, however, revealed that poor administration and intentional disregard of program guidelines were responsible for a large percentage of loan losses.

For the most part, the degree of detail in the reports varies by who gets them. Usually the funding source has privileged access. For example, the report of agency financial operations in Connecticut Development Authority bond prospectuses are much more thorough and scrupulous than the report which goes to the Commissioner of Commerce. Similarly, the British Cabinet Secretary overseeing the operations of the National Enterprise Board may requisition all operating records. Generally, the legislature and the public must accept annual reports prepared by the enterprise and occasional ad hoc investigative reports as their sole sources of information on the financial activities of the enterprise. In the institutions we have noted, these vary greatly in the detail and usefulness of disclosure--from vague accounts for CDC, to quite detailed accounts for NEB.

Social Reporting

Few of the investment banks reviewed make any use of social performance accounting. CDC, NEB, and EIB make no specific provisions for reporting even easily measurable social indices such as total employment of the firms in which they invest. NEB lists environmental impact and encouragement of worker participation in management as criteria for investment, but they provide no benchmarks, measurements or reporting schedule by which to evaluate projects, prospectively or retrospectively, along these dimensions. The Connecticut Development Authority reports total employment of the firms it finances, but this is an utterly inadequate measure of its performance in creating or maintaining jobs. As with all expenditures of publicly-raised funds, it is the marginal addition to some stock (such as employment) rather than the gross size of that stock which is the barometer of performance. Proposed CDFC economic impact indices, described in that institution's profile, are somewhat more sophisticated but still do not address the "with/without" problem in evaluating the benefits of social programs. In other words, would any of the benefits have been realized anyway even if CDFC had not made the investment?

Projections

Projections are necessary to evaluate investment projects,

especially when there are several competing for the same pool of funds. CDFC is contemplating a simple projection procedure: applying its social accounting procedures to the business plan projections of investment applicants. Thus CDFC will have a two-track set of projections--for both financial and social returns, both of which will be subject to post audit.

Cost-Benefit Analysis

More elaborate methods of project evaluation have been developed by the World Bank and its national affiliates. These address the divergence of market and social valuations of the costs and benefits which can be anticipated from various large-scale capital investment projects. These divergences are usually caused by such factors as monopoly domination of markets, state regulations and externalities. The method is essentially one of cost-benefit analysis in which all quantities are reduced to monetary terms, as described in John Mollenkopf's paper.

These types of analysis are expensive due to their enormous requirements for data and skilled analysis. Therefore, they are usually applied only to large projects such as capital-intensive industrial plants or infrastructure which require massive fixed investments. There are some institutional benefits to offset these expenses. Such studies are usually carried out by consultants

in cooperation with local officials and managers. Thus, some permanent, resident expertise in this kind of analysis can be developed. Also, data developed for one study may be used to analyze subsequent projects.

In summary, again, the record to date of detailed financial reporting by development banks is mixed, at best, and social indices are virtually nonexistent.

C. Governance: Public Inputs into Operating Decisions

The most important factors affecting the results achieved by public enterprises have been the structure and dynamics of the day-to-day decision-making. For each institution reviewed, there has been a complex web of attachments, interests and attitudes which are brought to bear on each type of operating decision. For each institution these circumstances are different.

We can begin to analyze this experience by identifying the groups of players involved in the operation of all public enterprises and the nature of the relationships between the groups. We will then explore examples of these relationships, focusing on elements of democratic or at least pluralistic control.

The four basic groups with whom we are concerned are:

- 1) Elected officials and their appointed ministers or secretaries: This group is usually (but not always) statutorily

responsible for the oversight of the public enterprise. Their degree of involvement in day-to-day activities of the enterprise is slight--generally by design. After all, the enterprise's very existence is premised on its carrying out social purposes without the full expenditure of effort by the government itself. Elected and appointed officials are lumped together here because their tenures tend to be coterminous.

2) The Board of Directors is usually the ultimate authority for all decisions concerning the sources and uses of funds and setting the overall strategy for the enterprise. They generally serve finite, overlapping terms which may or may not be renewable.

3) The Professional Staff carries out the policies of the Board, policies which they generally propose to the Board. Their initiative in promotion and competence in administration has the single greatest impact on the overall performance of the enterprise. Generally, they prepare the analyses on which the Board makes its decisions. Their attachments to the enterprise tend to be of longer standing than any of the other groups, a situation which enhances their power considerably. Also, they are closest to the enterprise's constituencies at all levels of decision.

4) Constituents: By constituents we mean those groups in the general public which have organized, regular dealings with the enterprise. These groups include firms which do business