

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 86/2

235 SCOMM 9: HOUSE SPEC. COMM. ON PERMANENT FUND 1977-78

STATE OF ALASKA
PUBLIC EMPLOYEES' RETIREMENT FUND
COMPOSITION OF INVESTMENT HOLDINGS
JULY 31, 1977

	CURRENT MONTH			PRIOR MONTH
	% of Total Cost Value	Cost	Yield	Cost
<u>MARKETABLE SECURITIES ACCOUNT</u>				
<u>Cash Deposits</u>				
Savings	2.4	\$ 2,170,328.96	5.00	\$ 3,331,939.87
<u>Short Term Issues</u>				
Bankers Acceptances		\$ -0-		\$ 1,488,428.34
<u>Intermediate/Long Term Issues</u>				
U. S. Treasury Notes & Bonds:				
2 - 5 Years	4.5	\$ 4,012,349.00	7.35	\$ 2,005,000.00
5 - 10 Years		-0-		1,996,724.00
Over 10 Years	4.5	4,078,012.50	7.81	997,500.00
Sub-Total	9.0	\$ 8,090,361.50		\$ 4,999,224.00
Federal Agency Securities:				
5 - 10 Years	9.8	\$ 8,829,921.88	8.67	\$ 8,829,921.88
Over 10 Years	4.9	4,384,218.75	8.36	-0-
Sub-Total	14.7	\$ 13,214,140.63		\$ 8,829,921.88
Government National Mortgage Assn.	52.9	\$ 47,465,782.31	8.10	\$ 46,049,985.91
Corporate Notes & Bonds:				
5 - 10 Years	1.4	\$ 1,243,750.00	9.55	\$ 1,243,750.00
Over 10 Years	17.7	15,927,530.00	8.48	21,205,292.50
Sub-Total	19.1	\$ 17,171,280.00		\$ 22,449,042.50
Private Placements	1.9	\$ 1,700,000.00	9.125	\$ 1,700,000.00
Total Issues	97.6	\$ 87,641,564.44		\$ 84,028,174.29
TOTAL	100.0	\$ 89,811,893.40		\$ 88,848,542.50
<u>COMMON STOCK ACCOUNT</u>				
<u>Cash Deposits</u>				
Demand		\$ 77.78	N/A	\$ 44,557.80
Savings		1,567.31	5.00	137,629.09
Sub-Total		\$ 1,645.09		\$ 182,186.89
<u>Repurchase Agreements</u>	1.6	\$ 445,000.00	4.50	-0-
<u>Short Term Issues</u>				
Commercial Paper	13.1	3,674,354.45	4.94	5,169,028.16
<u>Intermediate/Long Term Issues</u>				
U. S. Treasury Notes & Bonds	21.5	\$ 6,039,905.00	6.97	\$ 3,976,623.75
Corporate Notes & Bonds	1.8	496,562.50	7.30	-0-
Sub-Total	23.3	\$ 6,536,467.50		\$ 3,976,623.75
<u>Common Stock</u>	62.0	\$ 17,441,504.75	3.40	\$ 16,750,590.41
TOTAL	100.0	\$ 28,098,971.79		\$ 26,078,429.21

STATE OF ALASKA

PUBLIC EMPLOYEES' RETIREMENT FUND

COMPOSITION OF INVESTMENT HOLDINGS
JULY 31, 1977

	CURRENT MONTH			PRIOR MONTH
	% of Total Cost Value	Cost	Yield	Cost
<u>LOAN AND MORTGAGE PROGRAMS</u>				
FHA Mortgages	14.1	\$ 10,826,572.69	7.32	\$ 10,984,573.57
Small Business Loans	7.6	5,825,754.33	8.83	5,893,997.20
Conventional/Residential Mortgages	78.3	60,269,370.66	9.85	57,851,110.95
TOTAL	<u>100.0</u>	<u>\$ 76,921,697.68</u>		<u>\$ 74,729,681.72</u>
<u>ALASKAN DEPOSITS</u>				
Arctic First Federal Savings & Loan Association	84.6	\$ 550,000.00	7.50	\$ 550,000.00
First Federal Savings & Loan Assn.	15.4	100,000.00	7.50	214,000.00
TOTAL	<u>100.0</u>	<u>\$ 650,000.00</u>		<u>\$ 764,000.00</u>
<u>SUMMARY OF COMPOSITION</u>				
Marketable Securities Account	45.9	\$ 89,811,893.40		\$ 88,848,542.50
Common Stock Account	14.4	28,098,971.79		26,078,429.21
Loan and Mortgage Programs	39.4	76,921,697.68		74,729,681.72
Alaskan Deposits	.3	650,000.00		764,000.00
TOTAL INVESTMENT HOLDINGS	<u>100.0</u>	<u>\$195,482,562.87</u>		<u>\$190,420,653.43</u>

STATE OF ALASKA
PUBLIC EMPLOYEES' RETIREMENT FUND
CHANGE IN PORTFOLIO COMPOSITION
July 31, 1977

	<u>Current Month</u>	<u>Prior Month</u>
<u>MARKETABLE SECURITIES ACCOUNT</u>		
<u>During the Month Funds were Provided by:</u>		
Portfolio Operations		
Interest Income	\$ 517,260.73	\$ 475,133.24
Net Gain on Sale of Securities	146,090.17	122,872.87
Total Provided by Operations	<u>\$ 663,350.90</u>	<u>\$ 598,006.11</u>
Sale of Marketable Securities	\$12,829,740.84	\$17,446,006.68
Maturity of Marketable Securities	349,197.92	165,776.86
Net Contribution from General Fund	<u>2,300,000.00</u>	<u>-0-</u>
TOTAL Funds Provided During the Month	<u>\$16,142,289.66</u>	<u>\$18,209,789.65</u>
<u>During the Month Funds were Used for:</u>		
Purchase of Marketable Securities	\$15,303,900.57	\$22,178,176.05
Net Contribution to Loan and Mortgage Programs	-0-	4,000,000.00
Common Stock Account	<u>2,000,000.00</u>	<u>-0-</u>
TOTAL Funds Used During the Month	<u>\$17,303,900.57</u>	<u>\$26,178,176.05</u>
NET CHANGE IN FUNDS	<u>\$ (1,161,610.91)</u>	<u>\$ (7,968,386.40)</u>
<u>COMMON STOCK ACCOUNT</u>		
<u>During the Month Funds were Provided by:</u>		
Portfolio Operations:		
Interest and Dividend Income	\$ 3,859.07	\$ 123,000.68
Net Gain (Loss) on Sale of Securities	16,683.51	(116,851.35)
Total Provided by Operations	<u>\$ 20,542.58</u>	<u>\$ 6,149.33</u>
Sale of Marketable Securities	\$ 217,211.44	\$ 796,062.31
Maturity of Marketable Securities	6,028,150.24	6,224,567.91
Net Contribution from Marketable Securities Account	<u>2,000,000.00</u>	<u>-0-</u>
TOTAL Funds Provided During the Month	<u>\$ 8,265,904.26</u>	<u>\$ 7,626,779.55</u>
<u>During the Month Funds were Used for:</u>		
Purchase of Marketable Securities	<u>\$ 8,001,446.06</u>	<u>\$ 8,535,905.86</u>
NET CHANGE IN FUNDS	<u>\$ 264,458.20</u>	<u>\$ (909,126.41)</u>

Schedule continued on following page

STATE OF ALASKA

PUBLIC EMPLOYEES' RETIREMENT FUND

CHANGE IN PORTFOLIO COMPOSITION - Continued
July 31, 1977

	<u>Current Month</u>	<u>Prior Month</u>
<u>LOAN AND MORTGAGE PROGRAMS</u>		
<u>During the Month Funds were Provided by:</u>		
Interest Income	\$ 396,120.11	660,998.36
Principal Repayments	733,093.16	798,609.35
Net Contribution from:		
General Fund	1,667,097.32	3,398,002.26
Alaska Deposits	128,798.53	-0-
Marketable Securities Account	-0-	4,000,000.00
Total Provided by Contributions	<u>\$ 1,795,895.85</u>	<u>\$7,398,002.26</u>
TOTAL Funds Provided During the Month	<u>\$ 2,925,109.12</u>	<u>\$8,857,609.97</u>
<u>During the Month Funds were Used for:</u>		
Purchase of Loans and Mortgages	<u>\$ 2,925,109.12</u>	<u>\$8,857,609.97</u>
NET CHANGE IN FUNDS	<u>\$ -0-</u>	<u>\$ -0-</u>
<u>ALASKAN DEPOSITS</u>		
<u>During the Month Funds were Provided by:</u>		
Interest Income	\$ 14,798.53	\$ -0-
Redemption of Certificates	<u>114,000.00</u>	<u>-0-</u>
TOTAL Funds Provided During the Month	<u>\$ 128,798.53</u>	<u>\$ -0-</u>
<u>During the Month Funds were Used for:</u>		
Net Contribution to Loan and Mortgage Programs	<u>\$ 128,798.53</u>	<u>\$ -0-</u>
NET CHANGE IN FUNDS	<u>\$ -0-</u>	<u>\$ -0-</u>
<u>SUMMARY OF CHANGES</u>		
Marketable Securities Account	<u>\$(1,161,610.91)</u>	<u>\$(7,968,386.40)</u>
Common Stock Account	<u>264,458.20</u>	<u>(909,126.41)</u>
NET CHANGE IN FUNDS	<u>\$ (897,152.71)</u>	<u>\$(8,877,512.81)</u>

STATE OF ALASKA THE LEGISLATURE

POUCH Y - STATE CAPITOL
JUNEAU, ALASKA 99811
907-465-3800

LEGISLATIVE AFFAIRS AGENCY

September 17, 1977

MEMORANDUM

SUBJECT: Interim Fisheries Investigations

TO: , The Honorable Alvin Osterback, Chairman
Interim Resources Subcommittee

FROM: John Williams, Research Analyst
(with Gregg Erickson, Director of Research)

You have requested that the Research Division supply information relative to some specific aspects of the Interim Natural Resources Committee's investigations into the development of the Alaska bottomfish industry.

Our report is organized in seven parts: (1) a summary of information we have received from interviews with the seafood processing industry about their development activities; (2) bottomfish supply considerations; (3) bottomfish marketing considerations; (4) foreign industry responses; (5) the state role as perceived by the processing sector; (6) floating vs. shore-based processing, and (7) incentive programs in other jurisdictions. In addition to this specifically requested information, we are currently preparing some information sheets which will discuss other material which we have obtained.

I Current Development Activities

To our knowledge at least nine companies have expressed enough interest in the bottomfish industry to at least initiate some small scale purchases of groundfish species or are in the development planning stage. Seven of these are shore-based; two involve floating processors (one is a combined catcher/processor). Some of these companies are hoping to institute initial processing of at least cod species on board fishing boats. Others in the industry suggest that any on board processing is unreasonable for reasons of space, weather, fishermen distaste for such an operation, and economics. At least two processors are experimenting with pot fishing (as opposed to dragging).

We learned of four companies (three in Kodiak, one in Dutch Harbor) which are now buying small quantities of bottomfish for experimental processing and marketing, including occasional purchases of pot caught cod species with deliveries made in live tanks. Two of these companies are also purchasing or have purchased gutting machinery which they

intend to place on board fishing boats. Two extra men (total of 6) would then be carried on board to do the initial processing of cod species. Pot fishing and on-board gutting are techniques being looked at in order to guarantee product quality, a factor to which price is highly sensitive.

These four companies are presently offering prices for small quantities of unprocessed fish (some less than 10,000 pounds) which are significantly above those that would be expected to prevail assuming some minimum level of enterprise profitability and current prices in final product markets. In our view this reflects an effort by the processors to encourage some prospecting by the fishing captains who may be interested. For example, the Dutch Harbor operation has guaranteed a specific fisherman a minimum income to encourage him to pot fish for cod and sablefish. Thus far, he has had a difficult time in locating the target species in any concentration. In fact, all the companies we spoke with stated that they were receiving disappointing quantities of product.

New England Fish Company (NEFCO) and Icicle Seafoods, Inc. (dba PFI, Petersburg) have both signed contracts with the Alaska Department of Commerce and Economic Development for groundfish processing activities. The contracts guarantee against loss for up to 3¢/pound, with a \$145,000 ceiling on the total potential payment. In return, the companies are to supply the state with access to the information generated by the pilot projects. NEFCO has yet to initiate processing activities; PFI did some exploratory work this spring. NEFCO hopes to begin full scale processing activities in Kodiak in October or November of this year. PFI will again begin groundfish processing in Petersburg in October.

NEFCO has announced nationally their intent to enter groundfish processing in a big way. NEFCO has had some financially difficult years recently, and it is undoubtedly their hope to recover some financial footing in groundfish - a decision which could be interpreted as an extraordinary effort to regain a profit margin.

NEFCO's development plans call for targeting on pollock, cod, and sole. They need three vessels, each committed to making 200,000 pound deliveries, to make possible a minimum of 220 processing days per year. They have invested \$580,000 in machinery, with total investment in their Kodiak bottomfish operation expected to be about \$1 million. Pollock will be processed into 18.5 pound finished blocks. Cod is to be filleted, individually quick frozen, and marketed domestically. Minced flesh from both species would be reprocessed in Seattle into fish cake products. Flatfish (sole) would be bulk frozen and processed in Seattle.

Another company with which we talked is in the process of completing its development plans for a \$6 million operation in the westward region, to be targeted on cod species and pollock. They initially hope to process 150,000 pounds of product per day, and anticipate a labor need for 35 people. The company hopes to be in operation in 1978.

We additionally learned of a Seattle consortium of fishermen, lead by Mr. Maggie Ness, which has obtained financing and has begun the reconstruction of a vessel to serve as a catcher/processor for several species, including bottomfish. Their investment is \$2.5 million, which includes \$600,000 in machinery (including bottomfish processing machinery). They hope to process (for all target species) ten months each year.

Although we have not talked with them directly, it is also known that All Alaska Seafoods, Inc., a corporation started in 1975 by a group of Kodiak fishermen, intended to enter the bottomfishery when they equipped the floating processor All Alaska. This vessel has been processing crab and herring during the past year, and it is not known what the firm's future plans call for.

In general, our conversations with processors and potential processors have revealed widely ranging intentions with respect to the degree of processing which will occur at Alaskan locations. One company has a market for a large quantity of headed and gutted pollock which would be further processed by the buyer. Several of the firms which are "testing the winds" are freezing either whole or gutted cod and sending the product to Seattle plants for further processing. Still others intend to do the bulk of processing in Alaska with by-product reprocessing and breaching and battering operations to occur in Seattle. One company is specifically looking to internationally market their pack via Anchorage International Airport. It is also known that Flying Tiger Airlines, which presently flies fish from Alaska to the Orient during the summer months, has been actively investigating the potential marketing of bottomfish from Alaska in the Orient.

Most industry and banking sources seem to agree that the ability to substitute capital for "high cost" domestic labor (along with an assured raw product supply - discussed below) will be the key to deciding the competitiveness of domestically processed bottomfish products in the international and national market.¹

The ability to finance, acquire and install modern, automated or semi-automated processing machinery, the majority of which is manufactured in Europe, will clearly be critical to full scale, profitable operations, in an industry where the major foreign competitors pay wage rates in the neighborhood of 30¢ per hour.

In fact, the fisheries loan officer of the bank which is by far the most active in the fisheries loan area told us that his decision to finance the Maggie Ness operation hinged upon his being convinced that the processing machinery technology was well enough advanced to supplant a major portion of the labor requirement.

¹ We are seeking more information about the labor component of existing bottomfish processing operations on the West Coast.

II Bottomfish Supply

Supply of product to the processing sector is viewed as the major bottleneck at this time by the processing industry. This is not to say that other important unknowns exist with respect to pricing and marketing, but simply reflects the response thus far by the fishing vessel owners to opportunities to begin either prospecting or full scale bottomfish activity. NEFCO has stated they will be ready to begin full scale operations before the end of this calendar year - yet they had not, at the time of our interview, been successful at contracting for even one of the 3 vessels their development plan calls for. Even the higher-than-market price offered by processors has, at least in the case of one Kodiak firm, not brought forth any supplies, this despite their willingness to accept relatively small quantities.

An added indicator of the currently low level of fishermen interest is the inability of Mr. Robert Devanney (who has a contract with a Korean company) to entice American fishermen to supply product to foreign processing ships; and the refusal of the North Pacific Fishing Vessel Owners Association, a Seattle based group of mostly Alaskan crab fishing vessels, to be in favor of joint venture operations with any of the numerous foreign interests which have approached them to supply groundfish species to offshore processing operations.

The Alaska shellfish fleet is looked to most often as the source of vessels to enter the new fishery because of vessel size, horsepower, and seaworthiness which this fleet represents and which will also be required for vessels entering a groundfish fishery. The reasons for this fleet's apparent lack of immediate interest are straightforward: the average boat in the Alaska shellfish fleet is realizing a very good return on investment in the shellfish fisheries. From 1970 to 1975, the harvested quantity of king crab increased 87%, while the ex-vessel value for the same time frame increased 190%. Using the same 1970-75 time frame, the harvested tanner crab increased by 223%, while the value increased by 400%. For shrimp, the harvested quantity increased by 33%, while the value of the catch increased by 163%.² These figures would necessarily have to be discounted for inflation, but stand to represent the trend that is occurring in the Alaska shellfish industry.

In addition to the trends as demonstrated by past landings and values, recent events would seem to guarantee that the resource base will continue to expand for the near future, and the value of the product shows no signs of declining. It can be expected that the foreign harvest of shellfish resources in the Bering Sea will be halted, making that total resource available to domestic harvest.

Another consideration is the amount of investment that has occurred in shellfish fishing vessels. With new vessel costs well above \$1 million, the fixed costs for operation and debt servicing mandate a minimum of hundreds of thousands of dollars of cash flow for each of the \$1 million

² Alaska Department of Fish and Game, Statistical Leaflet No. 28, "Alaska 1975 Catch and Production".

plus vessels. Many of the newer vessels participating in the crab fisheries did include some plan modifications to make the boats convertible to dragger operations. Stern ramps and excess horsepower are present on many of the vessels. Hence, some investment has occurred in anticipation of expanding into groundfish. However, the gear costs alone to equip a suitable hull for dragging are 50-100% higher than equipping the same hull for crab fishing. Considering the risk involved in interrupting cash flows on top of the lucrative status of the shellfish fisheries, we will not likely see many of the new vessels in the shellfish fleet abandon a relatively low risk, high return on investment fishery to enter a completely new, highly risky fishery.

The final aspect which leads many industry observers to discount the possibility of drawing upon the fleet is the time available for shellfish vessels to fill in between seasons by groundfishing. If such fill in activity could be initiated, the fishermen would have a better opportunity to weigh the economic opportunities and risks of their existing operations against the new fishery.

Realistically, considering the gear up time required to prepare for a season and the down time that is necessary to allow for annual maintenance to the vessel and gear, most of the vessels are fully committed in their present activities. Many boats were going to Seattle only once each two years for the annual maintenance, but this practice has significantly diminished as of late, as a result of an improved perception of the costs incurred by a fishing captain in lost fishing opportunities in the event of a break down. Hence, at least one month will be spent in Seattle each year by most shellfish vessels.

The question then becomes what kinds of vessels and fishermen will enter the bottomfish industry and under what conditions. Some industry personnel have suggested that because of the sea conditions and the distance from shore that the vessels must operate during the winter months, vessels of the 110-130 foot class will be required for a year-round bottomfish industry. This would imply deliveries in the range of 250,000 pounds and vessel costs of \$2 million.

Others in the industry have suggested that the overhead costs of the large vessels and the keeping qualities of the target species will mandate much smaller, cheaper vessels making smaller deliveries more frequently. A Gulf of Mexico constructed 80 foot class of vessel (considered the "Model T" of the fishing industry) would cost in the neighborhood of \$350-400,000. Thus the overhead costs would be greatly decreased, as would the hold capacity.

In our opinion, the most likely scenario (absent of vertical integration by the processing companies or guarantees to fishermen - which will be discussed later) is one of older, smaller vessels conducting necessary modifications to enter the groundfishery. The value of this class of vessels has been significantly amortized in past use, thus diminishing the cash flow requirements. This class of vessel also would typically have a technology disadvantage in existing fisheries which have realized

a large amount of new capital investment. Thus, older vessels which have low overheads and an economic disadvantage in existing fisheries would realize the least risk and have the lowest opportunity cost of venturing into a new fishery. This scenario would allow a number of fishermen to participate in the new fishery for a while, test the economics of that fishery, and test the techniques and operation setup to determine what the ideal configuration would be in a new vessel constructed explicitly for that fishery. This potentially means vessels new to the Alaska fishery entering from fisheries Outside.

Regardless of how the fleet structure develops, two alternatives appear to be available to processors who, such as NEFCO, have made business commitments to invest in bottomfish development. The first is vertical integration, which would involve a processor purchasing vessels to serve as suppliers. The processor would then hire a crew on a salary or a pay system which ties crew income to catch. Vertical integration does exist to a very small degree at present in Alaska, although it is considered to be less preferable than the current Alaska pattern of vessels being owned by their captains.

The second option available to processors is to hire a vessel and captain to supply groundfish. The vessel, captain, and crew would be guaranteed a minimum wage, most likely based upon their earning power in alternate fisheries. As an incentive, the processor could offer a bonus for supply in excess of mutually agreed upon minimum supply or in response to a favorable change in the value of the product at the wholesale level. Bonuses could also be structured to respond to the quality of the supplied product, as determined by the value of the processed final product.

III Bottomfish Markets

Although there appears to be an immediate problem with respect to supply, the longer range concerns about the development of the Alaska bottomfish industry center on market uncertainties. The U.S. and Canadian East Coast supports a large bottomfish industry, but produces almost exclusively for "fresh" markets.³ Since Alaska products will typically be marketed in frozen packs, the applicability of the East Coast experience to Alaska is very limited.

Since World War II, the U.S. has become a major importer of fishery products, with 1976 net imports exceeding \$1.5 billion. U.S. imports of frozen fish blocks (mostly bottomfish) last year totaled 379 million pounds, while U.S. production of these products was approximately 2 million pounds. The average wholesale value of the U.S. production

³ The smaller West Coast bottomfishery also produces mainly for "fresh" markets, mostly in California. Although some industry sources indicate that the West Coast fresh market would be key to the development of the Alaska industry, it will not be the major buyer of Alaskan products.

was 69.6¢ per pound.⁴ Of the major species available in Alaska for block production, the U.S. imported 180 million pounds of cod blocks and 96 million pounds of pollock blocks, at values ranging from 31¢ to 47¢ per pound for pollock and 65¢ to 81¢ per pound for cod.⁵

It is more difficult to determine the values of frozen groundfish fillets and steaks, (both domestic production and imports) since the National Marine Fishery Service (NMFS) market reports do not separate fresh from frozen. Thus, trying to analyze what part of that market form is frozen and thus more likely to be open to entry for Alaskan products is speculative at best. One might assume that U.S. imports of fresh or frozen fillets and steaks of groundfish would typically be in the frozen form. This does not hold true, however, since Canada supplies substantial quantities of groundfish products to the East Coast "fresh" market. The U.S. imported \$725.2 million worth of fish products from Canada in 1976 - much of it from the Canadian East Coast groundfishery.⁴

There has been little scientific investigation into the size and structure of the West Coast "fresh" market. Researchers on the West Coast tend to discount its importance, although a few sources do suggest that it is vitally important. The other major consideration, of course, is the cost of air freighting fresh products from Alaska. Historically, transportation costs have been declining as a percentage of final product value. The East Coast groundfishery is supplying markets all along the East Coast, Gulf Coast, and as far inland as Denver. The largest category of air freight shipped from Boston is fresh fish.

We have very little information about perspective markets which have been identified by the seafood industry. We do know of one company which has an order for 20 million pounds of pollock. Other companies have told us that the market size for domestic consumption of pollock blocks is 40-45 thousand metric tons, and that the world market for frozen cod would appear to be in the 250,000 metric ton range.

In order to assist the industry in the relatively high risk task of market development a few industry observers have suggested to us that direct state involvement might be appropriate. At present, the only marketing activity involving the state is the King Crab Marketing and Quality Control Board, established under AS 18.90. The Board, which consists predominately of members of the Alaska king crab processing sector, presently assesses producers of king crab 0.4 percent of the value, resulting in a projected budget of \$336,000 for FY 78. The largest part of the proceeds are utilized to promote king crab consumption in the Lower 48.

⁴ National Marine Fisheries Service, Current Fishery Statistics No. 7200, April 1977, "Fisheries of the United States, 1976".

⁵ N.M.F.S. Northwest Market News Service, undated, "U.S. Landings & Values of Selected Species".

The Committee may wish to consider an equivalent marketing service for bottomfish or for all Alaska seafood, and investigate industry attitudes toward such a development.

One company that we spoke with was orienting much of its present international marketing to label identification. They believe that Alaskan products should be identified as to source in international markets and are guaranteeing the identification of their products in Japan by requiring those Japanese companies who purchase their pack for the Japanese market to label the product under the U.S. company brand. As far as we know the firm is the only one pursuing this particular marketing tactic. The importance of label identification to individual processors will vary depending upon their developed markets. Certainly those companies which have developed a label identification at the retail level would benefit from such label penetration. It is also likely that the Alaska bottomfish industry would benefit as a whole if the production could be identified throughout the world as to source.

Much more information needs to be developed before we can understand the marketplace implications of the development of the Alaska groundfishery. There is very little known about the consumer of bottomfish products, the relationship of these products to replacement products such as chicken and red meat, and the price elasticity of groundfish. In one of the information sheets which will follow at a later date, we identify the research activities which are being conducted at this time by various university and government agencies.

IV Foreign Industry Actions

Our sources had mixed responses when asked about their opinion of the status of foreign fishing interests, especially Japan and Korea. There seem to be two themes which can be developed - one demonstrating that these interests may attempt to prevent the expansion of the U.S. industry into bottomfish by blocking penetration of world markets; the other indicating that foreign companies will be actively seeking trading arrangements with domestic operations.

Among our sources, the bankers seemed to be most concerned about the potential impact that foreign interests may have in blocking the U.S. domestic industry's penetration of those species markets historically controlled by foreign interests. This concern seems to hinge on the control of the international markets. One could assume that these two countries could, for a period of time, sell at less than cost internationally in order to gain continued hegemony in their historical market.

Concern has been generated within the U.S. fishing community by reports of greatly expanded Japanese government fishery agency budgets for the current fiscal year. As reported by the NMFS Language Services Branch,⁶

⁶ NMFS Language Services Branch, February 11, 1977, "Bi-Weekly Report".

approximately 8.5% of the \$589.7 million budget (\$50 million) is earmarked under a broad category of "Promotion of the 200 Mile Zone Countermeasures". This year's budget also triples the appropriation to the Japanese Foreign Ministry.

The major portion of the industry that we talked with seem to feel that those Asian countries which had historically fished off Alaska will be excellent markets for domestically produced products. Japan, for example, has not only lost some fishing rights off Alaska but also received a 62% reduction in their pollock quota off the Pacific Coast of the U.S.S.R. (400,000 MT). Of the major fish exporting countries, Korea and Japan will be among those that are most adversely affected by the expansion of exclusive fishing zones to 200 miles.⁷ Industry in both countries had depended very heavily upon the catch of their distant water fleets. Their apparent initial response to the new events is to attempt to supply their domestic markets first. We have not yet verified a statement which was made to us that the Korean government had prohibited further export of pollock from that country until the government is satisfied that their domestic demand can be met. The Japanese response thus far appears to be one of hoarding. Their warehoused surpluses are reported to be extremely high at this time, which is consistent with their very aggressive buying in the international market during this year.

On the other side of the coin, Iceland, Norway, and Canada will all gain significant advantage from the expansion of fishing zones. These three countries are also major sources of groundfish blocks imported by the U.S. There have been a number of instances when, especially Icelandic companies, have practiced what is known as "dumping"--an action resulting in the flooding of a market with product in such quantity and at such a price to severely impact the sale of similar domestic products. The practice has apparently been substantiated by Federal Trade Commission investigations, but no tariff or other policy response has resulted. Considering the added economic advantage realized by most North Atlantic fish exporting countries, and the importance of available markets to the development of Alaska's groundfishery, any future repetition of such practices must be considered as severely detrimental to Alaska's infant bottomfishery.

V The State Role

The last category of questions we presented to the banking industry and processing executives dealt with their perception of the State role in the development of the bottomfishery. The industry, as a rule, did not perceive any real capital shortages, except in the instance where there would be a need to construct new floating processors (as opposed to reworking an existing hull). The costs for such a venture were projected at initially \$6 million. The largest and most active banks in fishing loans seem to feel that none of the companies which had ex-

⁷ The major exporters of frozen blocks to the U.S., in rank order, are Iceland, Korea, Canada, Denmark, Norway and Japan. See reference 4.

pressed interest in entering the new fishery were sufficiently financed to assume the risk of making the investment necessary in a full scale, new operation.

Pan Alaska, a subsidiary of Castle and Cooke and a major force in the Alaska industry, indicated an interest in pursuing the possibility of joint venturing with other processors and the state and federal government in the construction and operation of a bottomfish processing facility. When the prospect of such a venture was presented to other processors, the responses ranged from lukewarm to absolutely no interest. One company felt that "socialism" had no place in the Alaska fishing industry. Others expressed concern that the state would be regulating an industry that it also had a vested interest in. We anticipate hearing more from those companies which expressed some interest.

With respect to State loan policy, the processors again did not give a single category recommendation. One company expressed great interest in having the State design a subsidized loan program specifically to service fishing boat owners in reworking their vessels for the groundfishery. Another did not want the State involved in any way in boat loans. A consideration here may be the maintenance of raw product supply by financing fishing vessel construction (and fishermen) on a demand note or similar basis.

It was suggested by Dr. Fred Smith of Oregon State University that as between loans or tax incentives, loans had two inherent advantages: (1) they supplied money at the front end of the operation, thus assisting cash flow considerations, and (2) the State could gather more information about the structure of the industry and financial transactions if they offered loans as opposed to tax incentives.

When queried about State fisheries tax policy, one company specifically suggested incentives based on an infant industry status for bottomfish development. Most of the other firms suggested that it was a decision that the State had to make based upon all criteria and not just industry attitude. They did advocate, of course, a structure that would not discourage entry into the new fishery.

The only other suggestion we received about the State role concerned State financing of various demonstration-type projects. Suggestions included the financing of trips abroad for Alaska fishermen to view groundfish operations in the major world groundfisheries, or financing the expense of bringing industrial expertise from other parts of the world to consult to members of the Alaska industry.

VI Floating Vs. Shore-Based Processing

The historic industrial organization used by the foreign industry in harvesting Alaska groundfish has involved fleets of catcher boats supplying floating mothership processors. Gear technology has been developed to the point where the crew of a catcher boat can detach the cod

end of a trawl without bringing it on board, tie it off and either buoy mark it or tow it to the mothership. A new cod end is then attached onto the trawl and the next drag begins. The whole procedure maximizes the available fishing time for the catcher boat.

Within the established Alaska industry, this organization is not common (the roe herring fishery works in a similar fashion). Even for "floating" processors, the catcher vessels typically carry their catch to a shore side location, where the processor is secured. Floating processors locate at shore-side moorages so that, under Alaska law, they are considered as shore plants (and are thus subject to a one percent rather than a four percent raw fish tax). For the shellfish fleet, this requires one or two days running time both to and from the fishing grounds, one to two days to unload the catch, and, in the case of bottomfish, will require additional lost fishing time to bring the catch on board for sorting and icing (icing could be supplanted with refrigerated sea water systems at an expense of approximately \$60,000).

Mr. Sig Jaeger, Manager of the North Pacific Fishing Vessel Owners Association, has prepared an analysis conducted by several members of his association with the assistance of outside experts.⁸ He has projected the earning capacity of a given vessel which in "case one" is delivering bottomfish to a shore-based plant, and in "case two" to a high seas floating processor. His calculation found that a vessel making deliveries to an on-shore or shore-side plant could fish 108 days per year - compared to 180 days for the same vessel making deliveries to a high seas processor. The gross annual earnings were projected to be \$288,097 for "case one", and \$480,161 for "case two". The individual crew share (7% of gross) was \$12,084, and \$27,636, respectively; the net boat share \$70,119 and \$222,511; the balance for profit, depreciation, taxes, etc., was -\$7,380 and \$148,011.

Even with the advantage of high seas versus shore-side delivery, it is nevertheless more profitable for a vessel of the type used in the above comparison to deliver shellfish to shore than bottomfish on the high seas. Mr. Jaeger states: "The example vessels used in the comparison have an earning potential from crab fishing of nearly double the pollock earnings potential of delivering to the floating [high seas] processor, and in a 7 to 8 month period rather than 10 months trawling for pollock. Moreover, that crab earning potential is 'now', without another \$250,000 invested in trawl gear and winches."

In a separate report Mr. Jaeger suggests that if a fishing vessel could save 15 minutes on each tow by not bringing the load on board but rather deliver it directly to a high seas processor, the potential increased gross earnings from additional fishing time could amount to \$80,000 annually.⁹

⁸ Jaeger, Sig, August 5-6, 1977, "Presentation to the North Pacific Fisheries Management Council on the Subject of Foreign Joint Ventures".

⁹ Fifteen minutes saved per tow (6 tows per day) for 180 fishing days equals 270 towing hours. This represents an additional catch potential of 660 metric tons at a catch rate of 22 metric tons per day (9 towing hours per day).

Though the use of high seas processors would obviously be advantageous to the fishing fleet operators, they present some inherent problems for the processor. These would include: (1) the crew accommodations, which would be far more expensive under American labor regulations than experienced by foreign operations, (2) operating conditions, which would be necessarily much less pleasant because of weather, seas, and confinement, (3) Food and Drug Administration regulations, which require more sanitary operations than generally experienced on foreign vessels, which means more expense in line operations, water quality, sewage treatment, etc., and (4) general supply problems of provisions, packaging, and parts and equipment in case of breakdowns. Additionally, the capital investment in all presently established fisheries is mostly in shore-based operations. For those floating processors which are in service today, few have been designed with bottomfish in mind, and the space restrictions and overhaul costs would generally discourage reworking the vessels. Conversely, many shore-side plants have enough existing space to accommodate bottomfish processing lines. Several new plants, especially a number in Kodiak and westward, were built with floor space available for future bottomfish operations.

There is reason to speculate that as the American bottomfish industry develops, it will do so within a scenario which could be considered a hybrid of the typical domestic shore-side operations and foreign high seas fleet operations. Considering (1) the diseconomies presented by Sig Jaeger's paper, (2) the adamant feeling of many members of the industry that initial processing on board of fishing vessels is unrealistic for Alaskan fishing vessel operations, and (3) the capital investment required to supply a number of new floating processors, we believe an alternative development path is likely.

Bottomfish operations could conceivably develop in a manner very similar to those of the Alaska salmon fishery in which shore-based processors supply a tender or tenders which directly receive detachable cod ends from catcher vessels, sort and initially process the catch (icing and evisceration to maintain quality),¹⁰ and deliver the supply to a shore-side plant for further processing. We have been informed by one processor that they have already ordered the construction of a vessel which could serve such a purpose.

This scenario is also consistent with our expectation of smaller, lower overhead vessels increasingly acting as catcher vessels. The hold capacity of a smaller vessel would not be considered a limiting factor if the fishing vessels are not required to handle the catch on board.

As an added note, we were reminded during our interviews that the future value of high seas motherships now owned by countries who have developed distant water fleets is uncertain. It was suggested to us that these floating processors could be sold to American companies and

¹⁰ High seas evisceration will mitigate the onshore waste treatment requirements presently being instituted by the Environmental Protection Agency.

utilized as domestic floating processors, so long as they were not classified as vessels (it was suggested to us that removal of the screw would likely alleviate any statutory problems about their utilization).

As noted above present State fisheries taxation policy discriminates between high seas and shore-side processors. The historical aspects of this policy relate to the initial development of floating processors. They were considered to be "Outside" interests who offered fewer benefits to the State and its citizens. The State thus implemented a 4% raw fish tax for floating processors, as opposed to a 1% raw fish tax for land-based cold storage operations.

A shore-based plant is described as one which does not change location for one calendar year. As a consequence, most processors which might be considered "floaters", are, under the law, shore-based operations.¹¹ Recently constructed "floating" processors have been brought to Alaska and typically stationed in one location for an extended period of time. All Alaska Seafoods, Inc. a wholly owned Alaska corporation, operates a mobile floating processor. The catcher/processor operation headed by Maggie Ness is a wholly outside owned interest. Other "floaters" are typically processing plants owned by larger companies who have plants in several locations in Alaska.

Most floating processors (both high seas and shore-side) would appear to employ predominately Outside labor, both with respect to processing line crews and vessel crews. Since the vessels are typically equipped in a Northwest location (Seattle) and return to the Northwest for periodic overhaul, and the usual location of these vessels is in sparsely populated areas of the State, the labor source drawn upon for manning the vessels is usually the Seattle area. We do not know the actual employment data for onshore vs. floating processors. We will attempt to answer that question with an investigation of Department of Revenue and/or Department of Labor data.

A floating processor operating on the high seas presents two additional problems to the State. The first relates to the State's taxation jurisdiction; the second to the management of the resource.

The State Supreme Court has found that the state's interest in the management of fish stocks over their entire range (inside and outside of the three mile limit) is sufficiently strong to warrant the application of fisheries management regulations over the entire area covered by a stock of fish in the absence of other jurisdiction. With the enactment of the Fisheries Conservation and Management Act, there is now "other jurisdiction" present to regulate those stocks which are predominately outside of three miles.

¹¹ AS 43.75.060(3).

However, the taxation jurisdiction of the State is not similarly expanded to areas more distant than three miles. The general application of tax law, as implied from Alaska v. Arctic Maid et al,¹² is that fish caught within three miles of mean high water are always taxable under State law, whether delivered to shore-side processings plants or floating processors anchored outside of three miles. Any fish delivered to a plant within three miles of shore, whether caught inside or outside of three miles is subject to the raw fish tax.

The question of the application of Alaska's income tax to operation within and outside of three miles is being litigated at this time under Sjong v. State of Alaska. The case is presently before the Superior Court and is expected (because it is a test case) to go to the State Supreme Court. The administrative ruling which has been delivered on the case (by the Department of Revenue) has suggested that a fisherman is liable for income tax on all income earned from catching fish within three miles. For catches outside of three miles, a fisherman is liable for the percentage of time spent in port in Alaska divided by the time spent in all ports while engaged in business relative to the particular catch in question. Thus, the administrative ruling suggests an apportionment of taxable income on a basis similar to that used to assess taxes from interstate transportation business. We will be happy to report to you the results of the Superior Court ruling. The trial is set for approximately two weeks from the date of this memorandum.

The utilization of floating processors would also exacerbate the biological management of fisheries stocks. Enforcement of fishing regulations and monitoring of catch levels for those fishermen who make deliveries to processors operating on the high seas will be much more difficult than the performance of those same functions at fishing ports. It would appear to be reasonable to expect a processor operating in such a fashion to mandatorily accept the additional cost of maintaining a regulatory agent on-board his processor, since that is the only obvious means to secure adequate management control.

VII Incentive Programs

Our investigation into incentive programs has only been of a preliminary nature. The Department of Resource Economics at the University of Rhode Island (URI) has probably looked at this issue on an international basis more so than any other agency. We talked with Dr. Andreus Holmsen at URI for the better part of one day. He suggested that an international review of fisheries incentive offerings in other countries is not readily available and would be very difficult to obtain because of the difficult task of construing what are incentives within the fisheries policies of the various fishing nations.

¹² Alaska v. Arctic Maid, 366 U.S. 199 (199-206) United States Court of Appeals for the Ninth Circuit.

URI has specifically investigated the structure of subsidy programs in some nations, most recently Canada. We are attaching as an appendix the paper prepared by Dr. Virgil Norton on this subject. In addition, Dr. Holmsen has published an article relating to the economic activities of trawlers in the North Atlantic, which includes specific references to subsidies and transfer payments made by the respective governments.

We did inquire as to the subsidies which are offered by east and west coast states to the resident fishing industry. Although we talked with people who were familiar with Washington, Oregon, California, Massachusetts, and Virginia, the only state which makes special consideration for their resident fishing industry appears to be Rhode Island. Rhode Island exempts fishing activity from property and sales tax liability. Additionally, that state owns and maintains most wharfs on a subsidized basis. We found no evidence of subsidized loan programs, tax incentives, or any other means which is an established subsidy in any of the other states.

Attachments

JW:dh

Alaska State Legislature

SPECIAL COMMITTEE ON
THE ALASKA PERMANENT FUND
(907) 276-3433

528 W. 5TH, SUITE 270
ANCHORAGE, AK. 99501
(POUCH V, JUNEAU, AK. 99811)
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MEMBERS

REP. CLARK GRUENING, CHMN.
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REP. RUSS MEEKINS
REP. BILL MILES
REP. LEO SCHAEFFER
REP. RICK URION

House of Representatives

September 19, 1977

Jim Edenso
Deputy Commissioner
Department of Revenue
Pouch S
Juneau, AK 99811

Dear Jim:

Here's a copy of Belden Daniel's report to the Committee, delivered in Kotzebue Saturday. If you want more copies, we are sending the original to the printer and hope to have some by next week. We also will have transcripts of the meeting held last week as soon as they can be prepared, before Christmas, I hope.

Sincerely,

A handwritten signature in cursive script that reads "Mike".

Mike Doogan
Administrative Assistant

MD:LAD

Enclosure

STATE OF ALASKA

DEPARTMENT OF REVENUE

#135
JAY S. HAMMOND, Governor

POUCH SB-JUNEAU 99801

February 16, 1977

The Honorable Hugh Malone
Alaska State Representative
State Capitol
Juneau, Alaska 99811

*Sent note of thanks
to Jim Edwards*

Dear Representative Malone:

The proposed legislation prepared by the State Investment Advisory Committee for consideration by the Governor on the Alaska Permanent Fund has not been submitted to the legislators at this date. The Commissioner of Revenue and the Governor have held a series of meetings with members of the Cabinet and members of the Alaska Legislature concerning the bill as prepared by the Investment Advisory Committee. The outcome of these meetings has resulted in some amendments to the bill as initially prepared.

The bill has not been changed substantially in any respect from the initial preparation by the State Investment Advisory Committee. For your information I am enclosing a copy of the current bill as revised by the Commissioner and the Governor's office. The following changes should be noted:

1. Sec. 37.13.020. Composition of the Permanent Fund. The Permanent Fund contribution factor has been increased to 50 per cent of all mineral lease rentals, royalties, royalty sale proceeds, and federal mineral revenue sharing payments and 100 per cent of all bonuses received by the State. The Commissioner, after reviewing the tax revenues and royalty revenues to be received by the State, was able to demonstrate that a 50 per cent contribution factor and a 100 per cent contribution factor from bonuses would not impair the State's general fund nor put a constraint on the ability of the State to pay operating expenditures.

2. Sec. 37.13.030(a). The Permanent Fund Policy Board is appointed by the Governor and "confirmed by the Legislature in joint session assembled." The Governor has agreed to this amendment to the bill and does support it.

3. Sec. 37.13.030(d). "Members of the Permanent Fund Policy Board shall receive \$250 per meeting day and are entitled to per diem and travel allowances as provided by law for members of State boards and commissions." It was felt that the Policy Board members should receive some compensation for the time and effort that would be required of the membership.

4. Sec. 37.13.050. Permanent Fund Investment Committee. In paragraph (a) membership requirements have been changed to read: "All members must have been residents of Alaska for at least three years, may not be State employees, and shall be persons of recognized competence and wide experience in investments, finance, and other business management related fields." The legislators felt that this would more clearly spell out the definition of residents.

February 16, 1977

5. ^xSec. 37.13.100. Operational Principles. Paragraph (8) has been changed substantially and now reads: "The Permanent Fund shall analyze the economic and other effects of an investment decision, including the effects on employment, income distribution, environment, health, social and other factors. The Permanent Fund shall be sensitive to the views of affected local communities and shall include an analysis of those views in proposals for large investments." There was considerable discussion between the members of the Governor's office and the Department of Revenue and legislators concerning this paragraph. It was felt that the paragraph was too generally written and that the proposed amendment was more desirable.

6. Sec. 37.13.120. Reports and Publications. The following sentence was added to the last section of the first paragraph: "The Policy Board of the Permanent Fund is prohibited from any campaign or general advertising expenditures to either promote or defend its policies and operations." This amendment was suggested by legislators concerned that the Permanent Fund may use its resources in inhibiting passage of legislation affecting the Permanent Fund.

7. Sec. 37.13.160. Political Activity. This is a new paragraph you should note. The members of the Policy Board, members of the Investment Committee, and officers and staff of the Permanent Fund shall not engage in partisan political activities which involve the Permanent Fund, and resources of the Permanent Fund shall not be used to finance any partisan political activities." It was felt that this amendment was necessary in order to disallow the Permanent Fund from engaging in any political activities.

8. Sec. 37.13.170. Public Access Information. This section was rewritten in order to more clearly and positively state the fact that the information in the Permanent Fund is public information.

There may be other amendments which I have missed in my initial review of the bill as it now stands. Any comments you may have concerning the amendments on the proposed bill should be brought to my attention.

Sincerely,



Jim Edenso
Deputy Commissioner

JE:ge
Enclosure

MEMORANDUM

State of Alaska

TO: State Investment Advisory Committee

DATE : December 27, 1976

FROM: Sterling Gallagher

SUBJECT: Attached Article

Enclosed is an article on sources and uses of capital in the overall national economy. As far as I know, there has never been any work done on the total size and proportion of the capital market in Alaska.

SG/lc
enc.

Greater Than Expected Expansion in '77; Credit Demand Up 12%

By HENRY KAUFMAN,
JAMES J. McKEON and
JEFFREY L. COHN

The volume of credit demands satisfied in 1977 will reach an annual record of \$243 billion, almost 12% more than the year now ending.

The U.S. Economy will rise somewhat faster in 1977 than is now commonly expected. We anticipate year-to-year growth of 5%-5½% in real terms and as much as 10%-11% in nominal terms. We base this upon the likelihood of moderate fiscal stimulus, recent gains in financial soundness on the part of key sectors of the economy and relatively conducive market conditions at the start of the new year.

The kind of business expansion we foresee is unlikely to produce severe financial strains or conflict with the objectives of the central cyclical manifestations in terms of costs of funds such as we have not yet seen in the current recovery.

Business Firms will remain reasonably prudent, but will nevertheless have to finance an increasing volume of operating expenditures and investments.

Internally generated corporate funds will rise from \$129 billion in 1976 to \$140 billion, based upon a growth of before tax profits of 16% (as compared to 32% in 1976). Nevertheless, since

Next year's business expansion is likely to produce cyclical manifestations in terms of costs of funds such as we have not yet seen in the current recovery.

business physical investment expenditures will reach \$122.5 billion in the

million units in 1976 to 1.78 million, and completions should rise almost as much.

Net new mortgage formation will increase from \$76.3 billion to \$86.5 billion and most of the increase will be privately financed. The rise will be heavily concentrated in home mortgages. Households will continue to pour a large proportion of their savings into financial intermediaries, but the volume of direct credit market investment, now at a very low level, will gradually rise as the year progresses.

The U.S. Government will pursue fiscal stimulus in 1977. We expect a tax rebate of about \$8 billion and an acceleration in expenditures. We calculate that this will produce a calendar year budget deficit of about \$57 billion and demands upon private investors including foreigners of

tions will remain very large in 1977, but mortgage commitments and take-downs are gradually rising to meet them. While mutual savings banks and savings and loan associations will add to their holdings of U.S. Governments, Federal agencies and corporate bonds for the year as a whole, sometime, later in the year probably, liquidity building will end.

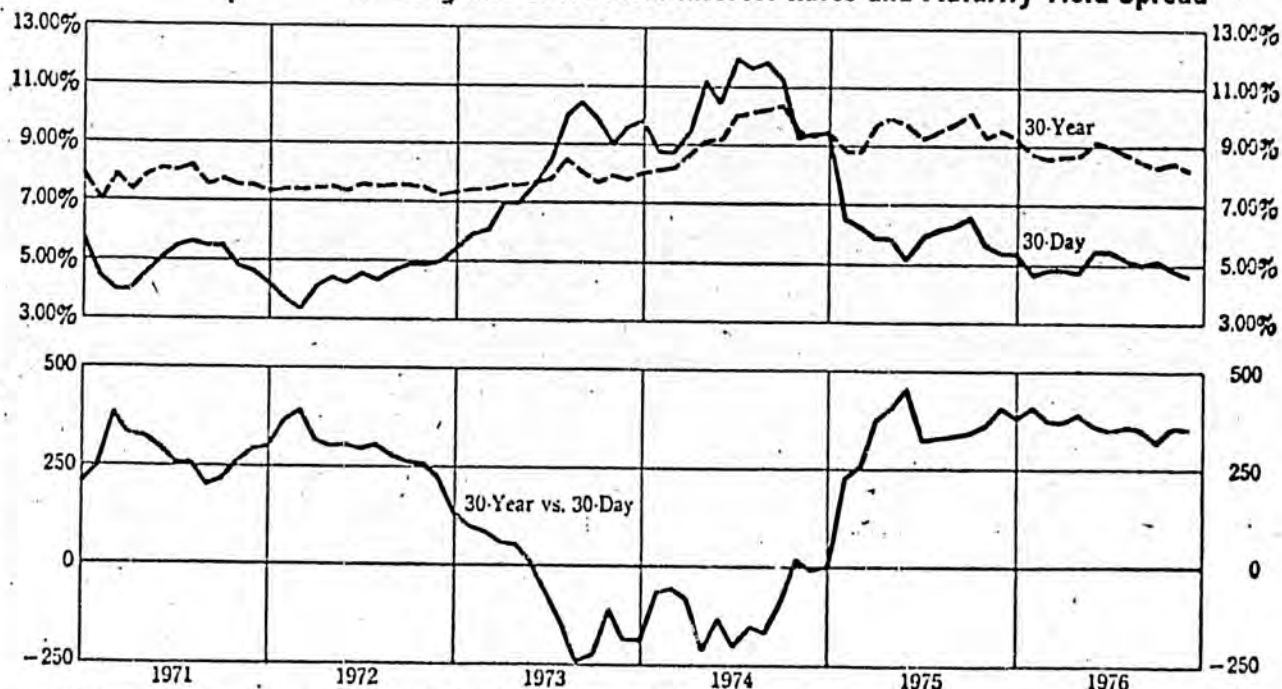
Contractual Institutions, such as life insurance companies and retirement funds, public and private, will be favored by rising premiums and contributions, producing record net inflows of investment funds again this coming year.

While they will acquire fairly large amounts of fixed income securities such as corporate and foreign bonds, they will be more receptive to equities than in either of the two most recent years, especially since opportunities

This is dramatically evident in the chart at the bottom of this page. After backing up in the second quarter, they resumed their decline and have fallen substantially since, reaching in most cases new cyclical lows just recently.

The developments outlined in the preceding pages lead us to the belief that the decline in rates will end very early in the coming year, at the latest. They suggest that, in 1977, rates will

Trends in Representative Long and Short-Term Interest Rates and Maturity Yield Spread*



*Longs are represented by 30-year new deferred call Aa utility bonds (yield to maturity), shorts by 30-day commercial paper rates (discount basis) and the maturity yield spread by the former over the latter.

Net Changes in the Volume of Selected Privately Held Money Market Instruments Outstanding

(\$ Billions)

	1974	1975	1976	1977
Treasury Bills	11.0	27.1	24.4	10.0

in the current recovery.

business physical investment expenditures will reach \$172.5 billion in the year ahead and liquidity building will remain fairly large, total external financing requirements for non-financial business corporations will rise to \$50 billion.

The huge refunding programs of the past two and one-half years appear to be drawing to a close. We expect a moderate cyclical increase in business loans and commercial paper financing (\$21 billion as compared with only \$1.5 billion in 1976 and an actual run-off of \$15.8 billion in 1975).

The net volume of corporate bond issuance will fall about 13% to \$24.1 billion in the coming year. Gross new straight public offerings of domestic corporate bonds will fall from around \$24 billion this year to \$21 billion in 1977. This will be partly offset by an increasing volume of foreign bond financing, especially new "Yankee bonds."

Households will both spend and borrow at higher levels than over the past several years. Consumer installment debt will rise \$21 billion, a new annual record. Housing activity will increase by virtually all significant measures. Starts will rise from 1.5

Dr. Kaufman is general partner and member of the executive committee of Salomon Brothers. Messrs. McKeon and Cohn are senior capital market analysts and research assistant, respectively. These are the summary and conclusions from their study, just published, "Prospects For The Credit Markets in 1977." In it, they say the demand for credit market funds in the U.S. will reach a new high of \$213 billion in 1977 as the economy expands faster than is now commonly expected. It is unlikely that real growth of 5% to 5½% will produce financial problems, although interest rates will probably bottom out in the first few months of 1977.

a tax rebate of about \$8 billion and an acceleration in expenditures. We calculate that this will produce a calendar year budget deficit of about \$57 billion and demands upon private investors including foreigners of about \$50 billion (compared with \$62 billion in 1976).

A much higher proportion of the marketable debt issuance in 1977 will take the form of new bills than has been the case this year.

Federal Credit Agency Issuance will rise from this year's \$13 billion to \$18.5 billion in 1977. The rise will reflect Federal Home Loan Banks' advances to savings and loan associations and the GNMA guaranteed mortgage "pass-thru" program.

State and Local Governments will issue more bonds and retire less notes than in 1976. Improving market reception, the growth of new open-end municipal bond funds and pre-refundings combine to suggest bond issuance will rise from \$13.7 billion to \$17 billion.

Savings Inflows at Thrift Institu-

While they will acquire fairly large amounts of fixed income securities such as corporate and foreign bonds, they will be more receptive to equities than in either of the two most recent years, especially since opportunities to invest in commercial mortgages will remain limited.

Commercial Bank Credit Expansion will reach \$58 billion next year, mostly loans because of increased business demand. We also expect a moderate net issuance of negotiable certificates of deposit for the first time since 1974.

These points are summarized in the accompanying table. The residual, which largely reflects households' direct market purchases, will decline by a small margin. (The residual is now "cleaner" than in years past, since we have now broken out bank managed personal and common trust funds as well as foundations and endowments.)

Interest rates, both long and short, have declined with but a few significant interruptions since mid-1974.

Money Market Instruments Outstanding

	1974	1975	1976	1977p
Treasury Bills	11.9	37.1	2.4	18.8
Agency Disc. Notes ..	1.6	1.1	-0.1	1.1
Commercial Paper ...	7.0	-1.5	2.6	4.3
Bankers' Acceptances ..	9.6	0.2	3.0	2.7
Certificates of Deposit ..	28.5	-10.1	-20.8	6.0
Total	58.6	26.8	-12.9	32.9

tend to betray cyclical influences for the first time since the current economic recovery began.

Markets for goods and services will begin to reflect rising expenditures for housing and business fixed investment, and markets will see growing demand for mortgages, consumer loans and commercial loans at banks. Governmental financing will remain substantial and in some cases rise somewhat. Liquidity building at financial institutions will be pared down at first and then end.

Such considerations, however, will put greater pressure upon short-term rates than upon long. It is our expectation that money market rates will rise gradually but not continuously throughout 1977. Sometime in the year, they should reach their 1976 highs. Possibly the most telling evidence for the reversal in the trend in short-term interest rates in prospect is in the accompanying table, which projects a fairly substantial \$33 billion increase in privately held money market instruments. This is in sharp contrast to the nearly \$13 billion net runoff that has occurred in the year just ending.

The table also suggests why yield spreads of privately-issued money market instruments over Treasury bills have narrowed to extremely small margins in 1976. When the outlets for (short-term) investments decline, pressure on spreads is exerted by (short-term) investors trying to maintain earnings as high as possible.

In the coming year, despite the reversal in the supply of short-term investment instruments, we anticipate

Summary of Supply and Demand in U.S. Credit Markets

(Annual Net Increases in Amounts Outstanding \$ Billions)

Realized Net Demands	1971	1972	1973	1974	1975	1976e	1977p
Privately Held Mortgages	44.3	68.8	68.7	42.8	38.5	61.3	69.5
Corporate and Foreign Bonds	25.6	19.9	14.5	29.7	39.0	36.9	34.5
Business Loans & Open Market Paper ..	7.6	26.4	46.7	50.9	-15.8	4.5	21.0
Consumer & Other Loans	17.0	26.6	27.1	12.2	9.7	26.0	33.0
Privately Held Treasury & Agency Debt ..	21.7	24.2	19.2	28.1	83.5	74.9	68.0
State & Local Debt	21.7	12.8	14.1	14.5	15.7	13.7	17.0
Total Demand for Credit	137.9	178.7	190.3	178.2	170.6	217.3	243.0
Invested Net Supply:							
Thrift Institutions	41.2	48.8	36.3	28.1	57.5	69.8	72.9
Insurance & Pension Funds	12.8	15.0	18.9	27.7	35.5	38.3	39.7
Investment Companies	0.5	1.6	1.6	1.9	3.4	3.5	4.6
Other Investing Institutions	12.1	14.2	19.1	5.5	0.6	8.7	14.1
Commercial Banks	50.9	73.3	77.6	59.8	31.0	44.5	58.0
Various Other (Primarily Money Market)							
Investors*	25.3	15.5	8.8	20.1	17.6	28.0	31.5
Residual: Households Direct	-4.9	10.3	28.0	34.1	25.0	24.5	22.2
Total Supply for Credit	137.9	178.7	190.3	178.2	170.6	217.3	243.0

* Consists of business corporations, state and local governments and foreign investors.
e estimated.
p projected.

Continued on page 39

Bigger '77 Boom Seen; Credit Demand Up 12%

Continued from page 17

these spreads to remain relatively narrow, inasmuch as the volume of Treasury bills will expand significantly more than that of other money market instruments.

The spread of CDs over bills could prove, from time to time, more volatile than the rest of these spreads, however. Issuance of CDs, and thus their rate competitiveness, will vary with commercial banker's expectations of loan demand.

Expectations will also affect the relative steepness of money market yield curves. Now relatively flat, maturity yield curves will become steeper on balance in the coming year when rate levels start to rise, producing expectations of further rises.

We also believe that the spread of the prime loan rate over open market borrowing rates, now wide, will gradually decline as competition for loans increases, modifying the current emphasis upon maintaining profit margins.

The upward pressure we foresee acting up interest rates in 1977 are not likely to become so manifest in long-term rates as in short, nor are they likely to take effect upon the former quite so soon as upon the latter. There are a number of factors suggesting that bond rates will remain more resistant to these pressures for a while yet.

Institutions are now quite liquid with no signs of any flagging in the rate new investable funds are pouring in. Furthermore, at least in the taxable bond market, investment opportunities, especially higher quality offerings, are likely to be somewhat less ample in 1977. Finally, inflation rates have been falling recently.

On the whole, however, the lows in, say, high grade corporate bond yields are likely to be experienced within the first few months of the year. Periods of divergent trends between long and

already narrowed appreciably from their very high levels of 1974-5.

When yield levels rise towards the second half of the year, however, the increasing volume of medium quality issues might widen spreads between, say, A and Baa rated issues.

As a consequence of the recent sharp rally in corporates, mortgages now yield more relative to the former than is typical. These spreads could narrow for a while early in the year, especially for mortgages on multi-family and commercial properties.

The spreads of conventional home mortgages over high grade corpo-

Annual Net Purchases of Corporate (and Foreign) Securities for Selected Types of Financial Institutions

(\$ Billions)

	1974	1975	1976e	1977p
Life Insurance Companies:				
Bonds	4.0	9.1	13.9	14.1
Stocks	2.1	2.1	2.8	3.2
Private Non-Insured Pension Funds:				
Bonds	4.7	2.8	1.9	2.6
Stocks	2.3	5.7	7.6	8.7
State and Local Retirement Funds:				
Bonds	7.8	3.8	4.2	5.4
Stocks	3.5	2.5	3.0	3.1
Personal & Common Bank Trust Funds:				
Bonds	1.0	1.0	1.3	1.1
Stocks	3.1	5.5	7.3	8.0
Foundations and Endowments:				
Bonds	0.7	0.8	0.7	0.7
Stocks	0.8	-0.9	2.0	2.4

rates, on the other hand, may not decline so much as those for income properties, and, as commitments are rising, these spreads should level out sooner.

Annual Percentage Growth in Financial Assets of Selected Financial Institutions

(Annual Percentage Increases in Amounts Outstanding)

	1971	1972	1973	1974	1975	1976e	1977p
Commercial Banks*	12.3	14.4	14.2	9.1	4.5	5.8	7.6
Mutual Savings Banks	13.4	12.2	6.0	3.5	10.5	10.7	9.3
Savings & Loan Associations	17.1	18.1	11.9	8.7	14.5	15.2	13.6
Life Insurance Companies	6.5	6.8	7.2	6.7	8.3	8.2	7.9
Private Non-Insured Pension Funds	7.4	6.4	6.8	8.6	9.6	10.0	8.4
State & Local Retirement Funds	11.4	13.8	12.5	13.0	11.5	11.0	9.6

* Assets include reserves.

invest substantially in U. S. Governments.

In the coming year, as in 1976, banks will be able to finance a large part of such purchases through negotiating repurchase agreements with large business corporations awash with liquidity.

The improving operating positions of state and local treasuries and circumstances favorable to arbitraging the proceeds of advance refunding issues makes another large input of these funds reasonably certain.

Foreign purchases will also remain large, probably larger than the expected \$10 billion total for 1976. Another substantial trade deficit and increasingly reduced alternative outlets for OPEC surpluses are the major reasons these purchases will remain heavy.

The balance of Treasury needs will have to be met by direct market purchases by individuals. We believe that these acquisitions will be smaller in 1977 especially after netting out U. S. Savings Bond purchases. The Treasury, consequently, may not have to schedule as many of the subscription offerings which proved so popular this past year.

Quite apart from the Treasury, the Federal Government will project a somewhat larger presence in the credit markets in 1977, as a result of Federal agency and agency guaranteed financing. In addition to the continued growth of the GNMA guaranteed "pass-thru" program, more traditional agency borrowers will be returning to the market in the year ahead.

Private mortgage lenders continue to take advantage of the GNMA program by pooling holdings of seasoned mortgages. These issues dominated

The increase of funds available for investment in this market, at first in response to favorable spreads and now as a consequence of the perceived improvement in credit quality, is another beneficial development.

The casualty insurance industry with improved earnings is sharply increasing its activity in this market once more. A profusion of new municipal bond funds are being organized. Thrift institutions have also expanded their net purchases with marginally higher effective tax rates.

The commercial banks, which in past periods of monetary ease and slack loan demand were major investors in tax-exempts, have been only moderate buyers of these obligations during the past two years. They purchased net an estimated 29% of the new municipal offerings in 1976 and 15% in 1975 compared with more than 50% in 1971 and 1972.

Demand factors also suggest an increase in tax-exempt bond offerings. Many governmental units will fund, rather than roll over, maturing notes, and the volume of pre-refundings of high coupon bond debt should increase over 1976 levels. The decline in recent months of municipal bond yields should also encourage a larger volume of pollution control issuance in 1977.

Three major points emerge from our projections of institutional activity in the coming year. First the rising demand for residential mortgage credit will increasingly absorb new deposits flowing into thrift institutions; the huge buildup of liquidity that occurred at thrifts over the past few years, consequently, is likely to come to an end sometime later in the year.

terings, are likely to be somewhat less ample in 1977. Finally, inflation rates have been falling recently.

On the whole, however, the lows in, say, high grade corporate bond yields are likely to be experienced within the first few months of the year. Periods of divergent trends between longs and shorts are hardly abundant and never last for more than a few consecutive months.

Whether long-term interest rates decline a bit initially or not, we expect them to fluctuate within a trading range, without establishing a trend for most of the first half or so of calendar 1977. There after, the advance in short rates and rising business expectations should carry long-term rates moderately higher.

They would end 1977 at higher levels than those at which they started, certainly, but we consider it unlikely that they will, in 1977, reach their

Net Purchases of Municipal Obligations by Commercial Banks

	Bank Purchases (\$ Billions)	Total Issuance	Banks as % of Total
1971.....	12.8	21.7	59
1972.....	7.1	12.8	55
1973.....	3.9	14.1	28
1974.....	5.7	14.5	39
1975.....	2.4	15.7	15
1976e.....	4.0	13.7	29
1977p.....	3.0	17.0	18

highs for the year now ending (late May, for the most part).

It is important to recognize, however, the extent to which expectations play into the behavior of long-term rates as opposed to shorts. However accurate they may chance to be, credit flow projections as such, therefore, are at best fallible guides to long-term rate movements.

The smaller volume of bond offerings in the coming year, especially high quality issues, and large inflows of investable funds at investing institutions should exert continuing pressure upon quality spreads for much of the year. These spreads have

rates, on the other hand, may not decline so much as those for income properties, and, as commitments are rising, these spreads should level out sooner.

Assuming that the Federal tax rebate will take effect in the second quarter of next year and the growth in expenditures will be more or less evenly distributed through the year, more than 55% of the net issuance of Treasury marketable debt will fall into the first half. Typically, the preponderance of Treasury financing, tends to fall into the second half.

A material change in the composition of new Treasury issues will take place in 1977, with important implications for the market. Offerings of coupon issues will remain large by comparison with any period save the past few years. The routinization of such financing was an important element in debt management policy, and is likely to remain so even with a new team at the Treasury.

Nevertheless, greater emphasis is likely to be placed on the issuance of bills. The volume of Treasury marketable debt outstanding has risen \$60.4 billion in calendar 1976; bills have accounted for only \$6.7 billion, or 11.1%, of this increase. With the change in Administration, the net issuance of bills may well account for 30% to 40% of total net issuance of marketables.

A number of supply factors, however, suggest that the Treasury's task in the coming year will not prove overly burdensome. Thrift institutions and a number of other primarily long-term investing institutions will continue to provide a significant volume of funds to this market — although not quite so much as in the year just ending.

The Treasury market will also benefit from continued heavy investment by commercial banks, state and local governments and foreign central banks. Even with more typical loan demand developing, banks will still

guaranteed "pass-through" program, more traditional agency borrowers will be returning to the market in the year ahead.

Private mortgage lenders continue to take advantage of the GNMA program by pooling holdings of seasoned mortgages. These issues dominated the agency borrowing programs in the year now coming to a close.

While we expect the dollar volume of such issues to continue growing next year, most of the year-to-year increase in total agency financing will be due to the reversal of the role of the Federal Home Loan Banks.

Over the past two years, the FHLB system acted as a conduit from savings rich savings and loan associations back to the market. In 1977, by way of contrast, they will be absorbing market funds once more.

As to state and local government offerings, improved market conditions favor a moderate, continuing surge in tax-exempt bond financing in the coming year.

The trauma under which New York City has staggered since mid-1975 continues, but the effects upon the issuance of other state and local issuers are increasingly marginal. One sign of the improved reception for tax-exempt securities is the return of spreads versus taxable obligations of comparable maturity and quality to more normal dimensions.

rising demand for residential mortgage credit will increasingly absorb new deposits flowing into thrift institutions: the huge buildup of liquidity that occurred at thrifts over the past few years, consequently, is likely to come to an end sometime later in the year.

Second, such institutions as life insurance companies, private pension funds, public retirement funds and bank trust managed personal assets are likely to continue channeling very large amounts of money into corporate securities, especially stocks, in the absence of heavy commercial mortgage financing.

Third, commercial banks will experience, for the first time in the current recovery, business loan demands of normal cyclical dimension, and, in turn, are likely to issue a moderate volume of negotiable CDs.

Non-bank institutions other than the thrifts, will continue to show rising net inflows of new funds in 1977, as a consequence of large intakes of premiums and contributions and improved investment earnings. We expect life insurance companies' assets to rise by a record \$25 billion in 1977, a shade over what we have estimated for 1976.

Improved earnings and mandatory higher contributions will increase the net new investable funds of both private non-insured and public retire-

Continued on next page

Supply and Demand of Corporate Bonds Summary of Supply and Demand in U.S. Credit Markets

	1971	1972	1973	1974	1975	1976e
Bills	9.6	6.4	3.9	12.0	37.7	6.7
Coupons	4.7	1.1	-3.2	0.7	42.6	53.7
Total Marketable	14.3	7.5	0.7	12.7	80.3	60.4
Savings Bonds	2.4	3.3	2.8	3.0	4.1	4.4
Foreign Issues	11.1	3.9	5.4	-3.2	-1.2	1.1
State and Local Series	0.1	0.1	0.2	0.2	0.6	2.4
All Other	7.1	5.9	11.5	10.9	-0.5	11.6
Total Non-Marketable	20.7	13.2	19.9	10.9	3.0	19.5
Grand Total	35.0	20.7	20.6	23.6	83.3	79.9

†Includes Federal Reserve holdings.

Credit Demand

Continued from preceding page

ment plans to \$16 billion and \$12.5 billion, respectively. We would also anticipate higher inflows into bank managed personal trusts and common trusts as well as foundations and endowments.

All of these institutions continue to have somewhat restricted investment alternatives (commercial mortgage demands are expected to remain moderate). They will be investing heavily, consequently, in corporate securities, both bonds and stocks. However, we believe that investing institutions will continue their gradual return to equities as opposed to bonds.

The sharpest turn-arounds, since 1974, in portfolio preferences be-

tween stocks and bonds have occurred in (largely bank managed) private non-insured pension funds and also bank managed personal and common trust funds. In 1977, we expect that equity purchases will constitute 54% and 59%, respectively, of the net new investable funds of these two types of institutions.

Investment companies will experience rather diverse responses from investors in 1977. These institutions rise, and then fall out of favor, as investment opportunities shift. Closed-end corporate bond funds were popular in the early 1970's but have not been visible in the markets since.

Open-end stock funds have, in recent years, and will continue in 1977, to suffer net redemptions which will be matched by net sales of stock holdings back into the market. In 1977,

the investment companies that are likely to attract new money are money market mutual funds and the new open-end municipal bond funds.

The former should experience slightly increased net inflows with rising short-term interest rates. With increases in the number of the latter now being organized, we expect that the assets of all municipal bond funds, closed-end and open-end alike, will rise roughly 50% in the coming year.

Commercial bank credit will expand sufficiently in 1977 to accommodate a cyclical rise in loans and some net additions to security portfolios. The volume of net new loans put on the books, however, will account for a much greater proportion of total credit expansion, \$42.5 billion out of \$58.0 billion (or 73%) than was the case in either 1975 or 1976.

It is worth noting that the anticipated increase in lending next year will not compare with that which occurred in the same part of the previous expansion.

The main reason for the increased lending is that business loans will increase, rather than decline, for the first time in the past two years. The reversal in the trend of these loans reflects the end of massive bond funding and greater working capital needs, on the part of business, as well as the increasing willingness, on the part of banks, to lend at narrower profit margins.

As these demands make themselves felt, the substantial liquidations of CDs of the past two years will also come to an end and be replaced by a moderate volume of net issuance. ■

Under the provisions of the Acts of Congress now in force, the bonds offered hereby and the interest thereon are, in the opinion of Bond Counsel, exempt from Federal, State, Commonwealth of Puerto Rico and local taxation.

NEW ISSUE

RATINGS:
Moody's: A
Standard & Poor's: A

\$35,000,000

Puerto Rico Aqueduct and Sewer Authority

Revenue Bonds, Series 1976

Dated December 1, 1976

Due July 1, as shown below

Principal and semi-annual interest (January 1 and July 1, first payment July 1, 1977 representing seven months' interest) payable at the Corporate Trust Office of The Chase Manhattan Bank (National Association), in New York, New York, or at The Chase Manhattan Bank (National Association), in San Juan, Puerto Rico, at the option of the holder. Coupon bonds in the denomination of \$5,000, registrable as to principal alone or as to both principal and interest. Bonds registered as to both principal and interest are convertible into coupon bonds at The Chase Manhattan Bank (National Association), New York, New York, Trustee. The Series 1976 Bonds are subject to redemption on and after July 1, 1986 as more fully described in the Official Statement.

The Series 1976 Bonds are being issued pursuant to a Trust Agreement dated July 1, 1949, as amended, and a Supplemental Agreement dated October 1, 1973, between the Authority and The Chase Manhattan Bank (National Association), Trustee, and, together with \$125,127,000 Revenue Bonds outstanding as of October 31, 1976 and such additional Revenue Bonds as may be issued, are payable solely from the Net Revenues of the water and sewer systems of the Authority. Neither the credit of the Commonwealth of Puerto Rico nor that of any of its political subdivisions is pledged for the payment of the Revenue Bonds of the Authority.

STATE OF ALASKA

DEPARTMENT OF REVENUE

Dept Revenue

JAY S. HAMMOND, Governor

POUCH SB-JUNEAU 99801

June 14, 1977

The Honorable Clark Gruening
Chairman, House Permanent Fund Committee
940 Tyonek
Anchorage, Alaska 99501

Dear Clark:

Thank you for your letter of June 10 concerning the proposed sectoral analysis of Alaska's economy. I was disappointed to read that rather than proceed with the sectoral analysis even on a limited basis you choose to recommend an entirely different route which would encompass a study for evaluation of the effect on Alaska's economy of the proposed State Investment Advisory Committee approach, the proposed approach of non-recourse loans to individuals, and an approach which would consider investing all of the Alaska Permanent Fund monies out of state.

It was my understanding subsequent to our meeting in Anchorage on June 10 the Department of Revenue and the State Investment Advisory Committee would undertake a limited sectoral analysis of Alaska's economy which would include an evaluation of at least all of the identified non-renewable resource sectors of the economy and would also evaluate the two proposals which encompass the non-recourse loan approach and the proposal to invest all of the Alaska Permanent Fund monies out of state. I believe that the use of the funds in question for evaluation purposes would be better spent to undertake the proposal as I have just suggested. Restating, it is my recommendation that the State Investment Advisory Committee and the Department of Revenue immediately undertake a limited sectoral analysis of Alaska's economy to include the non-renewable sectors of the economy and an evaluation of the proposals for the non-recourse loan approach, and the investment of all the Permanent Fund monies out of state.

I would like to discuss this with you further at your earliest convenience. My schedule calls for me to be out of Juneau on June 20, 21 and return on June 22. It will be possible for me to come to Anchorage on June 22 to meet with you on June 23 on this matter. Please let me know if this is at all possible.

Sincerely,



Jim Edenso
Deputy Commissioner

JE:ge

cc: Senator George Hohman
Commissioner Sterling Gallagher

STATE OF ALASKA

DEPARTMENT OF REVENUE

PF correspondence

JAY S. HAMMOND, Governor

POUCH SB-JUNEAU 99801

February 16, 1977

The Honorable Clark Gruening
Alaska State Representative
State Capitol
Juneau, Alaska 99811

Dear Representative Gruening:

The proposed legislation prepared by the State Investment Advisory Committee for consideration by the Governor on the Alaska Permanent Fund has not been submitted to the legislators at this date. The Commissioner of Revenue and the Governor have held a series of meetings with members of the Cabinet and members of the Alaska Legislature concerning the bill as prepared by the Investment Advisory Committee. The outcome of these meetings has resulted in some amendments to the bill as initially prepared.

The bill has not been changed substantially in any respect from the initial preparation by the State Investment Advisory Committee. For your information I am enclosing a copy of the current bill as revised by the Commissioner and the Governor's office. The following changes should be noted:

1. Sec. 37.13.020. Composition of the Permanent Fund. The Permanent Fund contribution factor has been increased to 50 per cent of all mineral lease rentals, royalties, royalty sale proceeds, and federal mineral revenue sharing payments and 100 per cent of all bonuses received by the State. The Commissioner, after reviewing the tax revenues and royalty revenues to be received by the State, was able to demonstrate that a 50 per cent contribution factor and a 100 per cent contribution factor from bonuses would not impair the State's general fund nor put a constraint on the ability of the State to pay operating expenditures.

2. Sec. 37.13.030(a). The Permanent Fund Policy Board is appointed by the Governor and "confirmed by the Legislature in joint session assembled." The Governor has agreed to this amendment to the bill and does support it.

3. Sec. 37.13.030(d). "Members of the Permanent Fund Policy Board shall receive \$250 per meeting day and are entitled to per diem and travel allowances as provided by law for members of State boards and commissions." It was felt that the Policy Board members should receive some compensation for the time and effort that would be required of the membership.

4. Sec. 37.13.050. Permanent Fund Investment Committee. In paragraph (a) membership requirements have been changed to read: "All members must have been residents of Alaska for at least three years, may not be State employees, and shall be persons of recognized competence and wide experience in investments, finance, and other business management related fields." The legislators felt that this would more clearly spell out the definition of residents.

February 16, 1977

5. Sec. 37.13.100. Operational Principles. Paragraph (8) has been changed substantially and now reads: "The Permanent Fund shall analyze the economic and other effects of an investment decision, including the effects on employment, income distribution, environment, health, social and other factors. The Permanent Fund shall be sensitive to the views of affected local communities and shall include an analysis of those views in proposals for large investments." There was considerable discussion between the members of the Governor's office and the Department of Revenue and legislators concerning this paragraph. It was felt that the paragraph was too generally written and that the proposed amendment was more desirable.

6. Sec. 37.13.120. Reports and Publications. The following sentence was added to the last section of the first paragraph: "The Policy Board of the Permanent Fund is prohibited from any campaign or general advertising expenditures to either promote or defend its policies and operations." This amendment was suggested by legislators concerned that the Permanent Fund may use its resources in inhibiting passage of legislation affecting the Permanent Fund.

7. Sec. 37.13.160. Political Activity. This is a new paragraph you should note. The members of the Policy Board, members of the Investment Committee, and officers and staff of the Permanent Fund shall not engage in partisan political activities which involve the Permanent Fund, and resources of the Permanent Fund shall not be used to finance any partisan political activities." It was felt that this amendment was necessary in order to disallow the Permanent Fund from engaging in any political activities.

8. Sec. 37.13.170. Public Access Information. This section was rewritten in order to more clearly and positively state the fact that the information in the Permanent Fund is public information.

There may be other amendments which I have missed in my initial review of the bill as it now stands. Any comments you may have concerning the amendments on the proposed bill should be brought to my attention.

Sincerely,



Jim Edenso
Deputy Commissioner

JE:ge
Enclosure

MEMORANDUM

TO: ☐

Jim Edenso
Deputy Commissioner
Department of Revenue

DATE : June 14, 1977

FROM:

Bill
William L. Means
State Investment Officer
Department of Revenue

SUBJECT: Alaska Permanent Fund

Today the Treasury Division purchased the following securities for the account of the Alaska Permanent Fund for settlement June 15, 1977:

				Price	Yield
\$3,000,000	7%	UST Notes	11/15/83	101-4/32	6.78%

WLM:ba

SCOMM

#9:136

Alex Miller
Vice President
Government and Labor Relations

P.O. Box 60029
Fairbanks, Alaska 99701
(907) 452-7171
Telex: 090-35454

File Royalty oil

I am Robert W. Johnson. I appear before you today, as the representative of TEAMSTERS LOCAL 959, bargaining representative for more than 23,000 Alaskan workers.

Our Local Union has worked for Alaska's resource development for many years, now. We have begged, pleaded, urged and even - on occasion - propagandized for this resource development, including the development of a petrochemical industry. Our record, carved over the years, clearly demonstrates our pro-development stand.

Accordingly, it grieves us very much to come here, today and urge that this particular development be held off, until such time as the State has fulfilled its part in the development.

Mr Chairman, Members of the Committee, I would direct your attention to an item clipped from the Anchorage Times of Wednesday, November 30th, last. This article, entitled "LeResche Wants Possible Problems Analyzed," refers to a letter sent from the Commissioner of Natural Resources to the Commissioner of Environmental Conservation. It requests the Environmental Commissioner to expedite certain, limited studies regarding the suitability of the Kenai area for this petrochemical development.

Ladies and gentlemen, this is too little, too late. In the bluntest terms, no matter where this petrochemical development is placed, there is going to be a lawsuit, or lawsuits, regarding the environmental factors involved. To approach any development without being prepared for such legal action is sheer insanity and the State is obviously unprepared.

So far as we have been able to learn, the State is likewise

unprepared for the many items it must furnish to any developer. The placement of this petrochemical industry involves - ultimately - the creation of a new city of 12,000 - 15,000 persons. This means schools, sewers, water, health facilities, streets and all the other elements which go into the making of such a community. Since nearly every area under consideration lies within either a second-class borough, or an area without government, at all, the burden for working out such details, lies with the State.

It may be claimed that there is five years, before all this will be required and that is more than adequate to work out all the details. Our answer to that is, "Hogwash!" If there is any basic truth about the development of our State, it is this: WE ABSOLUTELY MUST DO IT RIGHT THE FIRST TIME.....FOR WE ARE NEVER GOING TO BE GIVEN THE SECOND CHANCE WHICH THE OTHER STATES ARE NOW RECEIVING.

THE FIRST MISTAKE ALASKA MAKES IN ITS DEVELOPMENT WILL BE THE TOMBSTONE ON THE GRAVE OF ALL DEVELOPMENT.

There are additional reasons for asking that you study and research this petrochemical development, before granting a contract for hasty development.

First, full petrochemical development will come only by the combining of oil with natural gas. It is imperative that the developer be assured adequate supplies of the gas for the full life of the contract.

Second, oil and gas, as energy, are one of the three basic requirements for the development of all other mineral resources in our State. Given an available market, transportation for the ore,

or concentrates and energy for the mining and the transportation: and we have a chance to build other industries. However, this requires advance planning, preparation and above all, an over-all view which is totally lacking, today.

A crash program for petrochemical development could very well crash and burn all prospects for the development of other minerals. This would be an irreparable loss, so far as the future of our State is concerned.

Third, we have local considerations which must be weighed in planning this petrochemical development. Fairbanks desperately needs natural gas fuel for the correction of winter air pollution. Unless this air pollution is cleared, there is ample reason to believe any future growth of that city will be absolutely stalemated.

Many of the villages, particularly in the Northwest, are paying horrendous prices - as high as \$ 1.63 per gallon - for oil fuel. On their extremely limited funds, this creates a hardship. Every effort must be "built in" to this development to gain them some relief - hopefully in the form of propane, or liquified natural gas.

Finally, Alaska needs to program the base requirements for its full development, before rushing into a contract involving one of the three, base-requirements for any development beyond this particular industry.

We would urge this Committee to back away from any contract for twenty to twenty five years; to research and study all aspects of this petro-chemical industry, with especial emphasis on all matters

related to the environment; to coordinate all studies with the subsequent development of both renewable and non-renewable resources; and then, when the knowledge to proceed is available, get the show on the road.

This may well result in a one, or two year delay. So be it. The only thing we have to lose is our ignorance and we fail to see that as a fatal loss.

One last thing, about this matter of rushing to catch up on development. There is an old problem in logic which illustrates the futility of such an effort.

According to this problem, you are driving from Point "A" to Point "C", a distance of two miles. Point "B" sits right in the middle, one mile from both "A" and "C". If you go 30 miles an hour from Point "A" to Point "B", how fast must you drive from Point "B" to "C" to average 60 miles an hour?

The answer is.....it can't be done. You've already used two minutes to go the first mile.

Since we can't "catch up" on development, let's take the time to make certain we do it right. The State we save may be our own.

LeResche Wants Possible Problems Analyzed

Natural Resources Commissioner Robert LeResche has urged the Department of Environmental Conservation to analyze potential air and water quality problems which might result from adding a royalty oil processing plant at North Kenai.

All state departments have been asked to submit comments by tomorrow on the anticipated impact of such a plant.

In a letter to Environmental Conservation Commissioner Ernst Mueller, LeResche said: "Your department has been very helpful in flagging potential air quality problems in Valdez should royalty oil processing be added to the existing terminal activities. Now that industry attention is focusing on North Kenai, I hope your department can likewise take a rough cut at potential air and water problems at that location."

LeResche said he hoped Mueller's department would "not only consider the incremental emissions of a refinery of the existing airshed quality in the North Kenai area, but that you will also evaluate the cumulative effects of this proposed project with that of the pending Pacific

Alaska LNG project."

The letter continues, "Apparently the (federal) Environmental Protection Agency has some concerns about the development of the Kenai area as an industrial center and is undertaking a one-year study to determine the environmental capacities.

"While we certainly cannot hope to duplicate the EPA study, particularly in light of our limited time and resources, and while detailed analyses is a function of the permit processes which will follow a royalty (oil) sale, I do hope the advice of

your department on this will broadly reflect such long-range considerations."

Four bidders have submitted final proposals for purchase of the state's one-eighth royalty share of Prudhoe Bay oil. The state's requirement for bids specified that potential purchasers must agree to process the oil in Alaska. The four who have submitted bids have offered to construct refineries and petrochemical plants ranging in size from 150,000 to 250,000 barrels a day and ranging in investment from \$400 million to \$2.5 billion.

LeResche has said he hopes to

submit a final contract or contracts for sale of the royalty oil to the Roy-

alty Oil and Gas Development Advisory Board by early January. If the

board approves, the contracts would go to the legislature prior to Feb. 1.

#q:137

SCOMM

IMPORTANT MESSAGE

FOR Brian Rogers

DATE _____

TIME _____

A.M.
P.M.

PHONE NO. _____

TELEPHONED	☐	PLEASE CALL	☐
CALLED TO SEE YOU	☐	WILL CALL AGAIN	☐
WANTS TO SEE YOU	☐	RUSH	☐

MESSAGE _____

Here's Jim Rhodes ms.
he asked me to forward
to you - Please advise me
of your next meeting.

SIGNED _____

LAA 30

A Short History of the Alaska Permanent Fund

This recent amendment of the state constitution had its origins in a proposal made in 1970, several months after the famous \$900 million sale of North Slope leases. Governor Keith Miller urged that the money be set aside in U.S. Treasury bills and other high grade securities to provide a perpetual stream of earnings to help bear the costs of state government. Although the Legislature accepted the separate investment of the funds (by the Bank of America, the world's largest), some \$36.4 million was taken for "one time" capital improvements, chiefly roads, ferries, docks, and airports. The Governor suffered this reverse in part because he was a sudden, relatively unknown successor to Walter Hickel (who became Secretary of the Interior) and was believed to have limited prospects for winning a term in his own right. But far more important was the widely felt need to "catch up" with the other states after the meager revenues during Federal rule and the first decade of Statehood.

By 1974, regular and new programs of the state government were cutting deeply into ~~surrounding~~ the principle and earnings of the "North Slope Account".

As the result of growing concern over the lack of lasting benefits from oil revenues and, in particular, because of the severe decline of the fisheries, the Legislature created the Renewable Resources Revolving Loan Fund. Beginning in 1978, ^{5%}~~2%~~ of royalty and related non-tax revenues from minerals were to be used for loans, ~~and~~ grants, and operating expenses

to ~~some~~ industries that ^{could} be sustained indefinitely. Judging from the record, some legislators expected this fund to be administered through a number of state agencies (and to include park acquisitions and the like) while others saw it as being under one new entity.

Any money not committed in the year received was to be placed in a "permanent fund" from which only earnings could be spent. When this fund reached \$200 million, it and the parent fund would receive no further revenue. Observers have noted that this shutdown feature of the legislation may bring irresistible pressures to obligate all revenues every year. The inner permanent fund may never exist.

A further legislative initiative was taken in 1975 with the creation by statute ^{of} a "Permanent Fund" derived from 50% of royalties and other non-tax revenues from minerals. The Legislature would decide what programs were eligible under the fund, the record indicating that some grants, such as those for roads, ports, and other "infrastructure", could be deemed "investments". The lack of a strict requirement that investments produce direct income was offset somewhat by a provision that loan losses be made up fully before more loans could be made. In a similar vein, all earnings were to be retained by the fund. Governor Jay Hammond vetoed the measure on the grounds that it was a dedication of revenues prohibited by Alaska's constitution.

At the opening of the 1976 session, estimates revealed that the

\$900 million and some \$300 million in earnings would be exhausted by mid-year. (Admittedly, some ~~\$~~ **88** million was at rest in veterans' loans, but these could only be turned into cash by discounting them at considerable loss.) State budget growth had been rising at the compound rate of 26% annually or, when adjusted for new population and higher prices, spending was ~~times~~ **twice** the level in 1969. Moreover, there were rising doubts about the effectiveness, if not wisdom, of many programs. Yet even before these facts were generally known, the Administration and legislators close to the issue had agreed to offer the voters a constitutional amendment.

The desire to slow the expansion of state government and to save a part of future revenues for the end of the oil era, the housing problems, crime, and other side-effects of the pipeline boom, and the national questioning of the size and conduct of government were the greatest forces leading to the Alaska Permanent Fund. Another significant factor was the hope of altering the structure of the economy, as distinct from simply enlarging it. This meant reducing unemployment and seasonality, improving incomes, and even changing the timing and placing of investments. How far this can or should be done was a matter of minimal discussion.

Specifically, the amendment ~~reflects~~ **ACHIEVES** the desire to slow government and save oil revenues by adopting or avoiding various aspects of earlier proposals. This was not always conscious, of course. "At least 25%" of non-tax mineral revenues are to be put aside, thus

rejecting the fixed ceilings used before. Actually, the House version of the amendment called for tax as well as non-tax mineral revenues to be set aside. The Senate argued, however, that only revenue arising from the state's role as resource owner belonged in the fund. Revenues from the power to tax were for current expenses. The House accepted the change, though upon the different premise that mention of tax revenues was unnecessary because the Legislature always has the power to appropriate for any valid public purpose. Regardless of how this point is resolved, the Senate approach reflects the skepticism in that body about "tying up revenues" and diverting them from "unmet needs" for public services.

By stating that investments were to be "income producing", the framers removed the narrow focus on renewable resources. This allowed pure savings, business development, or loans to communities and non-profit groups. Or any combination of them. It also insured that projects would be subject to some of the tests of private finance. Clearly, the absence of grants, let alone money for operating expenses, tends to reduce added state employment. Still, certain investments may ~~have~~ impact on state programs or require special programs.

~~For the purpose of this study, the following is a summary of the state.~~

Further, rejection of a two-part fund, as in the Renewable Resources Revolving Loan Fund, favors better loan review.

Placing the Permanent Fund in the constitution was a sharp departure, heightening its chances for political survival and prolonging the period its assets ^{could not} ~~cannot~~ be put into regular government. Perhaps the most important break with the past may ^{HAVE BEEN} ~~be~~ the language dispersing the earnings of the fund to the general fund "unless

otherwise provided by law". This opens^{up} numerous possibilities, including the pledging of earnings as security for state and local debt (or debt of the fund itself), increased municipal revenue sharing, and cash payments to specified Alaskan residents (the seed of the Alaska, Inc. proposals).

Our political and economic history have produced a Permanent Fund that combines restraints and flexibility in a unique way. There is no evidence that investment funds elsewhere, including the Alberta Heritage Trust Fund of oil revenues, were an inspiration for our fund, and later study has found no close parallels anywhere in the world. The goals and management of the fund are open today, but the idea that has evolved so far has been described as a second, perhaps last, chance, to use public money to meet the challenges facing Alaska.

SCOMM

#9:138

#138

August 31, 1977

Donnan
Ferguson
Sackett

Dear :

Enclosed is a copy of the House Committee's meeting schedule. It is sent to you in the hopes that you will be able to attend the meetings and participate in our work.

We are particularly hopeful that you will be able to attend the symposium scheduled for September 10 in Anchorage. Participants will include Dr. Donald Gordon of Simon Fraser University, Dr. Barbara Bergman of the University of Maryland, Dr. George Rogers, John Havelock, Dr. John Lindauer and Jamie Love. The symposium begins at 9:00 a.m. in the Alaska Room of the Anchorage Westward Hilton Hotel.

If you are interested in participating in the symposium, the Committee will be happy to pay your travel costs. If you wish to take us up on this offer, we would appreciate your calling the number listed above to confirm.

Also enclosed are some legal opinions we have received on various matters pertaining to the Permanent Fund for your consideration.

Finally, we trust that you have received a copy of the Committee's brochure, "The Role of the Permanent Fund in Alaska's Future." If you'd like additional copies to distribute, please let us know. The number is limited, but, if the response makes it necessary, we may have additional copies printed.

Sincerely,

Mike Doogan
Administrative Assistant

Enclosures

2

REMARKS ON THE ALASKA PERMANENT FUND

by

GEORGE HOHMAN, STATE SENATOR
CHAIRMAN, SENATE PERMANENT FUND COMMITTEE

IN THE BROADEST SENSE THE PERMANENT FUND QUESTION CAN
BE DIVIDED INTO TWO PARTS:

I. ASSESSMENT AND PRIORITIZING OF ALASKAN GOALS AND
OBJECTIVES.

HERE THE SENATE COMMITTEE IS DETERMINING WHAT SPECIFIC
GOALS AND OBJECTIVES THE FUND WILL BE DIRECTED TOWARD ACHIEVING.

II. PLANNING AND IMPLEMENTING A DELIVERY SYSTEM.

HERE THE COMMITTEE IS PLANNING AND PROVIDING FOR THE
IMPLEMENTATION OF A STRUCTURE TO PUT PERMANENT FUND DOLLARS INTO
THE ECONOMY IN A WAY THAT WILL MAXIMIZE BOTH REALIZATION OF GOALS
AND OBJECTIVES, AND MAINTAIN A CONTINUING VIABILITY OF THE FUND.

THE COMMITTEE WORK PLAN CAN BE BROKEN INTO FOUR AREAS:

I. A STUDY OF EXISTING STATE TREASURY PRACTICES FOR
MANAGING ALASKA'S MONEY.

HERE WE ARE INVESTIGATING FOUR SUB-TOPICS:

1. PRESENT TREASURY INVESTMENTS.

WHAT IS ALASKA'S MONEY INVESTED IN TODAY?

2. TREASURY INVESTMENT STRUCTURE.

HOW DOES TREASURY MAKE AND IMPLEMENT INVESTMENT DECISIONS?

3. STATE LOAN STRUCTURE.

HOW DOES THE STATE MAKE AND IMPLEMENT DECISIONS ON
LOANING MONEY TO ALASKANS?

4. STATE LOAN FINANCING.

WHAT STRUCTURES AND METHODS DOES THE STATE USE TO
PROVIDE MONEY TO FINANCE ITS EXISTING LOAN PROGRAMS?

II. A SECOND MAJOR STUDY AREA HAS BEEN AN OUTREACH TO OTHER
STATES ON THREE OF THE SUB-TOPICS I REFERRED TO PREVIOUSLY:

1. TREASURY INVESTMENT STRUCTURE.

2. LOAN STRUCTURE

3. LOAN FINANCING.

- III. A THIRD STUDY EFFORT HAS BEEN THE COMPILATION AND
ASSISSMENT OF ALASKAN GOALS AND OBJECTIVES WHICH MIGHT
BE FACILITATED THROUGH THE USE OF PERMANENT FUND INVESTMENTS.

HERE THE COMMITTEE IS ENGAGED IN THREE ACTIVITIES:

1. COMPILATION AND ASSESSMENT OF THE PUBLIC INPUT WORK
BEING DONE BY THE ALASKA PUBLIC FORUM, THE HOUSE PERMANENT
FUND COMMITTEE, AND OTHERS WORKING ON THE QUESTION.

2. IN ADDITION WE HAVE SENT SPECIFIC QUESTIONNAIRES TO
THE FOLLOWING GROUPS:

- | | |
|---------------------------------------|-----|
| 1. RURAL QUESTIONNAIRES | 668 |
| 2. CHAMBER OF COMMERCE QUESTIONNAIRES | 750 |
| 3. BANKERS QUESTIONNAIRES | 18 |

3. FINALLY, WE PLAN TO SURVEY ALASKAN TEACHERS AND PUBLIC
EMPLOYEES REGARDING THEIR FEELINGS TOWARD ALTERNATIVE
USES OF THEIR RESPECTIVE PENSION FUNDS:

- | | |
|----------------------------------|-------------|
| a. TEACHERS PENSION FUND BALANCE | 180 MILLION |
| b. PUBLIC EMPLOYEES FUND BALANCE | 200 MILLION |

IV. THE FINAL STUDY AREA IS ANALYSIS AND ANSWERING OF THE
FOLLOWING SPECIFIC QUESTIONS:

1. WHAT ARE THE DEFERRED CAPITAL PROJECT NEEDS OF ALASKA?
2. WHICH OF THESE DEFERRED CAPITAL NEEDS ARE THE STATE'S
DIRECT RESPONSIBILITY?
3. WHERE IS THE STATE'S LONG RANGE CAPITAL PROGRAM AND
FINANCIAL PLAN? (THERE IS NONE AT PRESENT)
4. SHOULD WE MAKE REVENUE PROJECTIONS BEYOND 1985, SINCE
PRUDHOE BAY OIL IS SCHEDULED TO BE COMPLETELY PUMPED
IN 24 YEARS?
5. WHAT ARE THE AVAILABLE FUND BALANCES IN THE GENERAL
FUND UNDER THE FOLLOWING CIRCUMSTANCES:
 - a. THE DEFERRED CAPITAL OUTLAY NEEDS ARE MET?
 - b. AFTER THE DECLINE IN PRUDHOE BAY TAKES PLACE?
6. SHOULD THE STATE ANTICIPATE MORE EXTENSIVE OIL FINDS
IN PLANNING FOR THE NEXT 30 YEARS?

WITH THE PRECEEDING THOUGHTS IN MIND I'D LIKE TO TAKE A FEW
MINUTES TO DISCUSS YOUR ANSWERS TO THE QUESTIONNAIRE I SENT TO YOU.

FIRST, I WOULD LIKE TO THANK YOU FOR TAKING THE TIME TO
ANSWER. I AM ESPECIALLY PLEASED THAT MANY OF YOU TOOK THE OPPORTUNITY

TO GO BEYOND THE QUESTIONS I ASKED AND WROTE TO ME ABOUT SPECIFIC PROBLEMS AND IDEAS THAT YOU HAVE.

REVIEWING THE RESULTS, I AM IMPRESSED WITH YOUR UNIFORMITY OF ANSWERS AND COMMENTS IN THREE SPECIFIC AREAS:

1. AVAILABILITY OF LONG TERM INVESTMENT CAPITAL,
2. PERCENTAGES OF PERMANENT FUND PRINCIPAL THAT SHOULD BE BE INVESTED IN VARIOUS CATAGORIES, AND
3. RECOGNITION OF THE SPECIAL FINANCIAL CIRCUMSTANCES OF RURAL ALASKA.

FIRST, ALMOST ALL OF YOU INDICATED THAT YOU ARE HAPPY WITH YOUR ALASKAN BANKERS. THIS DIDN'T SURPRISE ME WHEN I SAW THAT MORE THAN 90% OF YOU HAVE APPLIED FOR AND RECEIVED LOANS FROM ALASKAN BANKERS. BEHIND YOUR OBVIOUS SUCCESS IN OBTAINING ALASKA MONEY HOWEVER, YOU INDICATED A SYMPATHETIC UNDERSTANDING AND ACCEPTANCE OF YOUR BANKERS INABILITY TO PROVIDE CERTAIN KINDS OF LOANS THAT YOU FEEL ARE IMPORTANT TO ALASKA'S ECONOMIC GROWTH. SPECIFICALLY, YOU ARE UNDERSTANDING AND ACCEPTING OF THEIR INABILITY TO MAKE LARGE, LONG TERM, LOW INTEREST LOANS AVAILABLE TO YOU. THESE ARE THE LOANS THAT WOULD PROVIDE MONEY FOR STARTING NEW ALASKAN BUSINESSES, FOR EXPANDING EXISTING BUSINESS FACILITIES, AND FOR EXTENDING HOUSING LOAN AVAILABILITY TO ALL ALASKANS.

WITH YOUR STATEMENT OF THE PROBLEM BEFOR US, THE SENATE PERMANENT FUND COMMITTEE WILL ATTEMPT TO ADDRESS YOUR NEED FOR THESE TYPES OF LOANS; TO FIND WAYS TO MAKE LARGE, LONG TERM, LOW INTEREST LOANS AVAILABLE TO YOU.

SECOND, I WAS STRUCK WITH THE UNINIMITY OF YOUR RECOMMENDATIONS ON WHAT PERCENTAGE OF THE PERMANENT FUND PRINCIPAL SHOULD BE ALLOCATED TO DIFFERENT INVESTMENT CATAGORIES. IT WAS INTERESTING TO NOTE THAT YOUR RECOMMENDATIONS PARALLEL, WITHIN 5%, SIMILAR RECOMMENDATIONS BY THE INVESTMENT ADVISORY BOARD, THE BANKERS OUR COMMITTEE HAS QUESTIONED AND THE RURAL ALASKANS WE HAVE HEARD FROM.

THE SPECIFIC PERCENTAGES YOU RECOMMEND ARE:

43.0% TO BE INVESTED IN HIGH GRADE STOCKS, BONDS, AND FEDERAL PAPER

9.0% TO BE INVESTED IN NEW LOAN PROGRAMS

12.5% TO BE INVESTED IN HOUSING LOANS

11.0% TO BE INVESTED IN EXPANDING EXISTING STATE LOAN PROGRAMS

10.5% TO BE INVESTED IN COMMUNITY DEVELOPMENT

8.0% TO BE INVESTED IN TECHNOLOGY DEVELOPMENT LOANS (ENERGY)

6.0% TO BE INVESTED IN OTHER INVESTMENTS

FINALLY, I WAS PLEASED TO FIND AN AGREEMENT ON YOUR PART THAT THE LEGISLATURE HAS AN OBLIGATION TO USE PERMANENT FUND DOLLARS TO MEET SOME OF THE UNIQUE RURAL AS WELL AS THE COMMON URBAN/RURAL ECONOMIC PROBLEMS BEING EXPERIENCED IN ALASKA TODAY.

THE NEED FOR LARGE, LONG TERM, LOW INTEREST LOANS WAS RECOGNIZED AS A COMMON URBAN/RURAL NEED. A LARGE NUMBER OF YOU HOWEVER, WENT BEYOND THIS COMMON NEED AND COMMENTED ON THE SPECIAL NEED FOR RURAL COMMUNITY DEVELOPMENT MONEY.

ON WEDNESDAY OF THIS WEEK I WAS IN BETHEL MAKING A PUBLIC PRESENTATION ON THE PERMANENT FUND. DURING THE COURSE OF THE PRESENTATION TWO ISSUES WERE RAISED THAT ILLUSTRATE THE SPECIAL RURAL COMMUNITY DEVELOPMENT PROBLEMS YOU REFER TO. FIRST, THE MATTER OF HOME OWNERS INSURANCE. THIS TYPE OF INSURANCE IS MORE AND MORE AN IMPOSSIBILITY IN RURAL COMMUNITIES. THE PROBLEM LIES IN A DE FACTO INABILITY RATHER THAN AN INTENTIONAL REFUSAL TO WRITE SUCH POLICIES. ELIGIBILITY FOR THESE TYPES OF POLICIES IS BASED ON AVAILABILITY OF INFRASTRUCTURE SUPPORT. WITHOUT ADEQUATE SEWER, WATER AND POWER SYSTEMS IT IS UNLIKELY THAT RURAL ALASKANS WILL EVER QUALIFY FOR HOME OWNERS POLICIES. BASED ON YOUR GENERAL RECOGNITION OF THE SPECIAL NEED AND MY PERSONAL KNOWLEDGE OF AT LEAST ONE RURAL AREAS PROBLEMS THE SENATE PERMANENT FUND COMMITTEE IS ATTEMPTING TO FIND WAYS TO USE PERMANENT FUND DOLLARS TO HELP RESOLVE THIS AND OTHER SIMILAR PROBLEMS.

A SECOND SPECIFIC COMMENT I HEARD WAS THAT ALASKAN CONTRACTORS ARE UNABLE TO COMPETE WITH OUTSIDE FIRMS BECAUSE OF PROBLEMS IN SECURING CONTRACTORS BONDS. AGAIN, WITH YOUR RECOGNITION OF THE SPECIAL NEED AND MY KNOWLEDGE OF THE SPECIFIC PROBLEM THE SENATE COMMITTEE WILL ATTEMPT TO FIND WAYS

OF USING PERMANENT FUND DOLLARS TO ASSIST ALASKAN CONTRACTORS IN SECURING THE BONDING NECESSARY FOR THEM TO COMPETE ON AN EQUAL BASIS FOR ALASKAN JOBS.

WHAT I HAVE BEEN DISCUSSING WITH YOU ARE SOME OF THE MAJOR AREAS OF OBVIOUS CONCERN AND AGREEMENT YOU EXPRESSED IN YOUR ANSWERS TO THE QUESTIONNAIRE I SENT YOU. THE COMPLETE QUESTIONNAIRE RESULTS ARE AVAILABLE TO YOU AFTER THIS MORNING'S MEETING. I ENCOURAGE YOU TO REVIEW AND CONSIDER THEM AND TO LET ME KNOW WHAT YOU THINK AND EXPECT AS OUR INTERIM WORK CONTINUES.

THANK YOU

PLEASE NOTE: THE FOLLOWING PAGES WERE TREATED
AS A UNIT IN THE ORIGINAL DOCUMENT.



Pouch V
JUNE 1978 ALASKA
99811

Alaska State Legislature

#138

Senate Committee
on the
Permanent Fund

To: All Members
Senate Committee on the Permanent Fund

From: George Hohman, Chairman

Date: August 29, 1977

Re: Transmittal #2

Enclosed please find:

- First Interim Report
- Banker's Questionnaire
- Chamber Questionnaire
- Rural Outreach Questionnaire
- Bibliography
- Synopses and Analyses
- Project Work Sheet
- Schedule of Projected Needs

Please feel free to contact my office at 465-3880 for additional information.

I. INTRODUCTION

This Interim Report of the Senate Permanent Fund Committee outlines those areas which have been under study or on which further work and study will take place through January 9, 1978.

Our initial effort has been to outline the tasks to be undertaken if meaningful information is to be made available to the Senate for its decision making process. Thereafter, to determine which committees and agencies have produced studies and reports that are useful, acquire same and reduce the material to a summary form for the convenience of the Senate committee members.

A review of past and existing contracts was made to avoid duplication. Contact with other legislative committees and the administration was made and will be maintained, again in an effort to avoid duplication.

Where additional information was needed, an effort to acquire the material has been initiated (refer to outline). This data, as well as other material from other legislative committees and the administration, will be added to subsequent interim reports.

The study effort can then be summarized into the following categories:

1. What investments should be made from the Permanent Fund, and to what extent will loans to Alaskans be a part of these investments?
2. Determine how the investment effort and the loan programs should be organized.

The results of the completed studies and those being undertaken will provide assistance in this decision making process--but only the legislature can make the final decision.

After various policy options are presented to the Senate Permanent Fund Committee and direction given by a majority of the committee, legislative alternatives will be drafted.

II. ANALYSIS OF STUDIES

A. Previous Studies (through 5/31/77)

B. New Studies (dated after 6/ 1/77) (attached)

1. Thinking About the Alaska Permanent Fund: A Cautious Approach
for Alaska Policymakers
2. Economic Considerations in Establishment of Alaska's Permanent
Fund

C. Contractual Studies--Senate Permanent Fund Committee

1. F.L.Orth, Sea Grant Program, University of Alaska
 - a. review implications of foreign investment in expansion
of Alaska's bottomfish industry
 - b. investigation of fishing cooperatives, PCA's, and potential
advantages of establishment of a development bank for fisheries
in Alaska
 - c. completion date October 10, 1977
2. M. DeMan, Alaska Native Foundation
 - a. provide assistance in developing work plans for Permanent
Fund research
 - b. completion date November 30, 1977

D. Bibliography

1. Updated to August 22, 1977 (attached)
 - a. various materials and publications requested to be
added to future bibliography updates

E. Synopsis of Each

1. All previous studies, new studies and contractual studies to
be summarized
2. Completed synopses (attached)
 - a. Structuring Decisions for the Alaska Permanent Fund (1976)
 - b. Report to the State Investment Advisory Committee re:
Domestic, National and International Banks (1976)
 - c. A Prospectus of the State of Alaska's Finances and Its
Development of Economic Diversity (1976)
 - d. The Alaska Series--The Alaska Permanent Fund in Perspective (1977)
 - e. The Alaska Series--The Alaska Permanent Fund and Other
Significant World Funds (1977)

II. E. Synopses (cont.)

- f. Thinking About the Alaska Permanent Fund: A Cautious Approach for Alaska Policymakers (1977)
- g. Economic Considerations in Establishment of Alaska's Permanent Fund (1977)
- h. Report to the State Investment Advisory Board re: Development Banks (1976)
- i. State of Alaska Permanent Fund Investment Objective Options (1976)
- j. Citizen Feedback #2, Rowan Group (1977)

III. ANALYSIS OF EXISTING LOAN PROGRAMS

A. Schedule of Existing Loan Programs

- 1. 13 state loan programs identified for further investigation
- 2. 8 federal loan programs identified for further investigation

B. Description of Existing Programs

- 1. Primary information gathered from administering agencies,
 - Alaska Administrative Code and Alaska statutes
 - a. statutory authority
 - b. administrative regulations, if promulgated
 - c. eligibility criteria
 - d. loan amount limits and repayment terms
 - e. implementation
- 2. Information requested of Division of Loans-State of Alaska
 - a. number of loans outstanding in all programs
 - b. dollar amount of loans granted in all programs
 - c. employment generated by loans in all programs
 - d. no response to date
- 3. Primary information request regarding federal loan programs operating within Alaska
 - a. responses
 - (1) Small Business Administration (SBA)
 - (2) Bureau of Indian Affairs (BIA)

C. Organization, Staffing and Cost of Operations - state loan programs

- 1. Request Budget and Audit Committee to Provide Information
 - a. staff member assigned to project
 - b. projected completion date September 30, 1977

III. D. Program Compliance With Legislative Directives

1. Request Budget and Audit Committee to provide information
 - a. staff member assigned to project
 - b. projected completion date September 30, 1977

IV. INVENTORY OF SUGGESTED PROGRAMS

A. Schedule of Inquiry and Scope of Inquiry

1. Questionnaire to banks and other financial institutions in

Alaska (attached)

- a. business loans - urban/rural
- b. personal loans - urban/rural
- c. mortgage loans - urban/rural
- d. loan denial factors - urban/rural
- e. areas of perceived credit scarcity - urban/rural
- f. comment on state loan programs
- g. comment on federal loan programs
- h. comment on Permanent Fund role
- i. mailed August 15, 1977
 - (1) 15 banks, savings/loan associations, financial institutions in Alaska

2. Rural outreach questionnaire (attached)

- a. business ownership
- b. consideration of business ownership
- c. granted/denied business or home loan
- d. comment on perception of bank consideration of loan application
- e. other sources of loans considered
- f. comment on availability of capital in rural Alaska
- g. familiarity with state loan programs
- h. impressions of state loan programs
- i. comment on interest charged by state loan programs
- j. familiarity with federal loan programs
- k. comment on areas of possible Permanent Fund loans
- l. mailed August 22, 1977
 - (1) 87 village councils
 - (2) 200 village corporations
 - (3) 12 regional corporations
 - (4) 10 agricultural policy task force members
 - (5) 138 miners/mining companies
 - (6) 44 fishing associations
 - (7) 176 holders of Alaska business licenses in various occupations

IV. A. Schedule of Inquiry and Scope of Inquiry (cont.)

3. Chamber of Commerce questionnaire (attached)
 - a. refer to IV.A.2. sections a-k
 - b. comment on areas of possible Permanent Fund loans/investments
 - c. mailed August 18, 1977
 - (1) to be distributed by D. Dickey, President, Alaska State Chamber of Commerce, to 750 individuals throughout Alaska
4. Governmental National Mortgage Association information request
 - a. explanation of association's procedures and practices as secondary market for housing loans
 - b. statistical data for last five years' activity in Alaska
 - (1) number of units financed
 - (2) dollar amount of mortgages written
5. State Department of Labor information request
 - a. method of cost of living indices formulation
 - b. existence of cost of construction indices compiled at state or federal level
6. Commerce and Economic Development Departments of other 49 states information request
 - a. types of loan programs
 - b. terms of loans
 - c. interest rates
 - d. publications describing loan programs
 - e. mailed August 24, 1977

B. Schedule of Responses

1. Bank/Financial institution questionnaire
 - a. no response to date
2. Rural outreach questionnaire
 - a. no response to date
3. Chamber of Commerce questionnaire
 - a. response requested by September 15, 1977
 - b. no response to date
4. Governmental National Mortgage Association
 - a. no response to date
5. State Department of Labor request
 - a. informal meeting with research staff member
6. Other states' Commerce and Economic Development information request
 - a. no response to date

IV. C. Inventory of Capital Improvement Needs of Alaskan Communities (attached)

1. Type of project
 - a. description of needs
 - b. cost per unit
 - c. estimated population to be served
 - d. estimate direct construction costs
 - e. estimated total costs
 - f. expected funding sources
 - g. mailed August 23, 1977
 - (1) 8 boroughs
 - (2) 11 home rule cities
 - (3) 21 first class cities
 - (4) 107 second class cities
 - (5) 1 federal reservation
2. Project work sheet (attached)
 - a. for familiarization with cost projection components
 - b. mailed August 23, 1977
 - (1) refer to IV.C. 1.g. (1)-(4)

D. Schedule of Responses

1. Municipal League member cities (50)
 - a. response requested by October 15, 1977
 - b. no response to date
2. Non-member cities
 - a. response requested by November 15, 1977
 - b. no response to date

V. ORGANIZATION

A. Inquiry of State Treasurers as to Organization of Treasury Management

1. Letter of inquiry to selected state treasurers
 - a. management of state funds
 - (1) general fund-temporary investment
 - (2) dedicated/trust funds with protected principle
 - (3) organizational/staff operational charts
 - (4) accomodation of management of fund size of Permanent Fund
 - (5) suggestions, comments, observations

B. Schedule of Responses

1. Michigan

V. C. Inquiry of Organization and Operation, Treasury Division, State of Alaska

1. Prior audit reports
 - a. refer to bibliography Audit Reports section
2. Consultant review
 - a. Lombard and Wall
 - b. preliminary reports generated by September 2, 1977

D. Inquiry of Method of Financing Program

1. Other states
2. State of Alaska and agencies

VI. FINANCIAL PROJECTIONS

A. Acquire Present Projections

1. Permanent Fund and Revenue Projections
Legislative Affairs Agency, July 1977
 - a. general and permanent fund balances 1978-1985
 - (1) low income-high expenditure model
 - (2) medium income-medium expenditure model
 - (3) high income-high expenditure model
2. Permanent Fund Revenue Projections
Department of Revenue, January, 1977
 - a. general and permanent fund balances 1976-1985
 - b. estimated petroleum revenues 1976-1985

B. Analysis of Present Projections

C. Request Projections be made for 10-year increments after 1985; 1999, 2005

D. Analysis of Projections through 2005

VII. PROGRAM RECOMMENDATIONS - OTHER

A. Outline Source of Program Recommendations

B. Outline Specific Recommendations and Sources of Same

VIII. PROGRAM ALTERNATES - STAFF

- A. Outline Programs Suggested for Inclusion
- B. Outline Specific Recommendations and Sources of Same

IX. ORGANIZATION

- A. Outline Organization Methods - Present
- B. Outline Organization Recommended by Various Studies and Consultants
- C. Provide Alternates Available for Consideration and Selection by

Senate Permanent Fund Committee

- 1. Continue with present system of intermediary and direct programs under the executive branch with the Permanent Fund functioning as an intermediary
- 2. Same as 1. but the Permanent Fund control within the Treasury Division
- 3. Streamline all programs and Permanent Fund within the Executive branch with legislative overview and checks/balances concerning compliance with legislative mandates reinforced

X. SPECIFIC LEGISLATION - BASED ON DIRECTIVE OF SENATE PERMANENT FUND COMMITTEE

- A. Draft Alternate Bills as Directed

- 1. Preliminary drafts of statements of intent

- B. Present Alternate Bill at January Meeting Prior to Session's Opening

January 9, 1978

Banker's Questionnaire

Sent to main branches of all banks in Alaska on August 18, 1977.

Senator George Hohman, Chairman
Senate Permanent Fund Committee
Pouch Y
Juneau, AK 99811

QUESTIONNAIRE

1. Assuming that Anchorage, Fairbanks and environs are urban, would you supply the following information concerning your loan portfolio?

	Urban	Rural	Total
Dollar amount			
Business loans	_____	_____	_____
Personal loans	_____	_____	_____
Number of loans			
Business loans	_____	_____	_____
Personal loans	_____	_____	_____
Mortgages			
Conventional	_____	_____	_____
Federally insured	_____	_____	_____

2. What are the averages concerning these loans?

	Urban	Rural
Business loans		
Length of loans	_____ months	_____ months
Average interest rate	_____ %	_____ %
Range of interest rates	_____ %	_____ %
Personal loans		
Length of loans	_____ months	_____ months
Average interest rate	_____ %	_____ %
Range of interest rates	_____ %	_____ %

Page 2
QUESTIONNAIRE

2. (cont.)

	Urban	Rural
Conventional Mortgages		
Length of mortgage	_____ months	_____ months
Average interest rate	_____ %	_____ %
Range of interest rates	_____ % to _____ %	_____ % to _____ %
Federally insured mortgages		
Length of mortgage	_____ months	_____ months
Average interest rate	_____ %	_____ %
Range of interest rates	_____ % to _____ %	_____ % to _____ %

3. What is the approval rate (number of approvals ÷ number of applications) for:

	Urban	Rural
Business loans	_____	_____
Personal loans	_____	_____

4. What factors are most important in loan denials in urban/rural areas? Please rate from 1 to 10, 1 being most important factor.

	Urban	Rural
Lack of applicant capital	_____	_____
Undeveloped nature of local economy	_____	_____
Poor credit record of applicants	_____	_____
Lack of applicant experience	_____	_____
Lack of applicant education	_____	_____
Difficulty of servicing loan	_____	_____
Lack of local support services	_____	_____

Page 3
QUESTIONNAIRE

4. (cont.)

	Urban	Rural
Lack of government infrastructure	_____	_____
Out of bank service area	_____	_____
Other (urban) please specify:		

Other (rural) please specify:

5. Which types of credit do you think are insufficiently available to urban Alaska?

Housing _____	Development _____
Business venture _____	Other (please specify) _____
Business expansion _____	_____
Research _____	None _____

6. Which types of credit do you think are insufficiently available to rural Alaska?

Housing _____	Development _____
Business venture _____	Other (please specify) _____
Business expansion _____	_____
Research _____	None _____

Page 4
QUESTIONNAIRE

7. Please comment on your impressions of the role played or potentially played by the state loan programs in the Alaska economy.
8. Please comment on your impressions of the role played or potentially played by the federal loan programs in the Alaska economy.
9. What do you perceive as the main credit availability problems in Alaska today?
10. What role should the Alaska Permanent Fund play in addressing these problems?

Page 5
QUESTIONNAIRE

11. How should the Permanent Fund invest its capital?

- A. High grade stocks, bonds and federal paper _____%
- B. Certificates of deposit in Alaska banks _____%
- C. Alaska loan programs
 - 1. New loan programs _____%
 - 2. Housing loans _____%
 - 3. Expansion of existing loan programs _____%
 - 4. Community development _____%
 - 5. Technological development loans
(energy, arctic construction, etc.) _____%
 - 6. Other (please specify) _____%

Please return completed questionnaire to:

Senator George Hohman, Chairman
Senate Permanent Fund Committee
Pouch Y
Juneau, AK 99811

Attention: Banking Questionnaire

May we contact you personally or by telephone at a later date?

Yes _____ No _____

Name _____

Address _____

Telephone number _____

Chamber Questionnaire

Distributed via Don Dickey's office, Alaska State Chamber of Commerce, to all Chamber Members. We supplied him with 750 copies on August 18 and requested response prior to September 15, 1977

Chamber of Commerce
Questionnaire

- 1) Do you own or manage or have you owned or managed a business in Alaska?

☐ Yes

☐ No

- 2) If you answered "yes" to Question No. 1, what type of business?

☐ Retail

☐ Services

☐ Other

Explain in more detail if necessary.

- 3) If you checked "no" to Question No. 1, have you ever thought seriously of entering business for yourself or with partners, or corporation?

☐ Yes

☐ No

Please explain the type of business that would be of interest to you.

- 4) Have you ever applied for a bank loan for home construction or small business?

☐ Yes

☐ No

- 5) If you answered "yes" to Question No. 4, was the loan denied or granted?

☐ Granted

☐ Denied

If denied, why?

- 6) Was bank consideration of your application:

☐ Satisfactory

☐ Unsatisfactory

Please explain.

Chamber of Commerce
Questionnaire
Page 2

7) Have you ever attempted to get business loans from sources other than commercial banks?

☐ Yes

☐ No

If "yes", from which source?

☐ State Loan
☐ Federal Loan
☐ Credit Union

☐ Friends or Family
☐ Personal Sources
☐ Other (please specify)

8) Do you think small business credit is adequately available to Alaska businesses?

☐ Yes

☐ No

Please explain.

9) Which types of credit do you think are insufficiently available?

☐ Housing
☐ Venture
☐ Expansion

☐ Research
☐ Development

10) With which of the following state loan programs are you familiar?

☐ Veterans
☐ Small Business
☐ Child Care
☐ Agriculture
☐ AK State Development Corp
☐ Senior Citizen Housing
☐ Small Business Development Corp

☐ Commercial Fishing
☐ Water Resources
☐ Tourism
☐ Fisheries Enhancement
☐ AK Housing Finance Corp
☐ Student Financial Aid

11) Please comment on your impressions of the state loan programs.

12) With which of the Federal loan programs are you familiar?

☐ Housing Loans
☐ Agricultural Loans
☐ Natural Resources Loans
☐ Environmental Quality Loans

☐ Business Loans
☐ Disaster
☐ Employment Training Loans
☐ Other (please specify)

13) Please comment on your impressions of the Federal loan programs.

Chamber of Commerce
Questionnaire
Page 3

14) How should the Alaska Permanent Fund invest it's capital?

- | | |
|--|-----------|
| A. High Grade Stocks, Bonds, Federal Paper | _____ % |
| B. Alaska Loan Programs | |
| 1. New loan programs | _____ % |
| 2. Housing loans | _____ % |
| 3. Expand existing state loans | _____ % |
| 4. Community development | _____ % |
| 5. Technological development loans | _____ % |
| (Energy methods of construction, etc) | _____ % |
| C. Other (please specify) | _____ % |
|
TOTAL |
100 % |

Please return this questionnaire to:

Senator George Hohman, Chairman
Senate Committee on the Permanent Fund
Pouch V
Juneau, Alaska 99311

Attn: Chamber Questionnaire

May we contact you by phone or personally at a later date?

___ Yes

___ No

Your Name _____

Address _____

Phone _____

RURAL OUTREACH MAILING LIST

- 87 Village Councils
- 10 Agricultural Policy Task Force Members
- 200 Village Corporations
- 13 Regional Corporations
- 138 Miners/Mining Companies
- 44 Fishing Associations
- 176 Business License Holders in the area of: Agriculture, Forestry,
Building Trades, Food Processing, Lumber & Wood Products, Local
Transportation, Water Transportation, Air Transportation, Retail Trade,
and Retail Food Stores.

668 TOTAL

The packet included 2 questionnaires (attached) and a transmittal letter.

Sent out on August 22, 1977.

RURAL OUTREACH QUESTIONNAIRE

1) Do you own or have you owned a business in Rural Alaska?

___ Yes

___ No

2) If you checked "yes" on the above, what type of business do you or have you owned?

___ Retail Sales (grocery, boats & motors, snow vehicles, etc)

___ Services (cafe, restaurant, movie theater, etc)

___ Other (agricultural, logging, fishing, etc)

Explain in more detail if necessary.

3) If you checked "no" to Question #1, have you ever though seriously of entering business for yourself or with partners?

___ Yes

___ No

Please explain the type of business enterprise you would be interested in.

4) Have you ever applied for a bank loan for home construction or small business?

___ Yes

___ No

5) If you checked "yes" to Question #4, was the loan granted or denied?

___ Granted

___ Denied

If denied, why?

- 6) Was bank consideration of your application: ☐ Satisfactory
☐ Unsatisfactory

Please explain.

- 7) Have you ever attempted to get business loans from sources other than commercial banks.

☐ Yes

☐ No

If "yes", from which of the following?

☐ State Loan

☐ Friends or Family

☐ Credit Union

☐ Personal Resources

☐ Federal Loan

☐ Other

Please give any details you feel are relevant.

- 8) Do you think small business loans are adequately available to rural Alaska?

☐ Yes

☐ No

Please explain.

- 9) We would appreciate any further statement or information you may wish to give relevant to opportunities and credit in rural Alaska.

10) With which of the following state loan programs are you familiar?

- | | |
|--|--|
| ☐ Veterans | ☐ Fisheries Enhancement |
| ☐ Commercial Fishing | ☐ AK State Development Corp |
| ☐ Small Business | ☐ Water Resources |
| ☐ Small Business Development Corp | ☐ AK Housing Finance Corp |
| ☐ Child Care | ☐ Senior Citizen Housing |
| ☐ Tourism | ☐ Student Financial Aid |
| ☐ Agriculture | |

11) Please comment on your impressions of the state loan programs.

12) What rate of interest do you believe the state should charge for the loan programs and the Permanent Fund loans?

13) With which of the following Federal loan programs are you familiar?

- | | |
|---|--|
| ☐ BIA | ☐ Small Business Administration |
| ☐ Farm Home Administration | ☐ Other (please specify) |

What are your impressions of the federal loan programs?

14) In which areas would you like to see the Alaska Permanent Fund make loans available?

- | | |
|---|---|
| ☐ None | ☐ Education |
| ☐ Housing | ☐ Environment |
| ☐ Small Business | ☐ Other (please specify) |

Page 4
Rural Outreach Questionnaire

If you have any personal ideas or suggestions regarding the Alaska Permanent Fund, please write or call. We will very much appreciate your input as we begin formulating the legislation to determine the working of the Permanent Fund. Thank you for your cooperation.

May we contact you personally or by phone?

☐ Yes

☐ No

Name _____

Address _____

Phone _____

The Capital Needs Survey Materials (Project Work Sheet and Schedule of Projected Needs) mailed on August 24, 1977 to all 1st and 2nd class cities, to all boroughs, all home rule cities and federal reservations (Metlakatla).