

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 86 / 2

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regional planning efforts, to me this strikes a very great disservice and injustice to areas of Alaska that have been left out over many, many decades. I was going to get into a number of other points, but I would probably just say that probably to me, it has to be re-addressed more than anything else.

I was going to get into things like how does that again measure the effectiveness of the utilization, the regionalization of utilization of the fund? Well, certainly it would more enhance the possibilities for decision-making, the possibilities for effectiveness measurement, the development of innovative and creative ideas as to how utilize rural areas of Alaska. I happen to be from Deering, Alaska, which is up by the Arctic Circle; and I certainly recognize there are resources in that area, renewable and non-renewable, that have not been tapped, that could be tapped, that certainly will be tapped--either through good, sound planning or through a process forced upon the regional corporations that are there now because of their non-involvement in a windfall fund like this.

What I'm saying is the state of Alaska certainly has an opportunity to guard its environment, to guard its integrity in all areas: streams, its wildlife, fish, to guard also culture that is fast disappearing. These are assets that

cannot be regained, cannot in any manner be brought back. What I'm hoping is that we will look at this fund in a different sense than we look at just another dollar or two in our pocket. What I'm hoping is that we can, in some manner, incorporate all of Alaska into this planning and utilization of these dollars. I think the regionalization of planning efforts certainly bring about a more in-depth review of what is there and has ever been done before. It will not only identify the resources that are there, renewable and non-renewable, but also the resources in human kind.

Too many times, asininely I have to say, we assume so much. Assume that we have no resources of the human kind out there. We assume that they are having yet language problems, problems of identifying with the different cultures, problems of getting to work on time, well you hear that from biased, judgemental, prejudiced and sometimes bigoted individuals. You'll hear that whether or not the rest of Alaska catches up and even surpasses the majority of society. You'll hear that from the natives as well as the non-natives. You'll hear that from the blacks as well as the Hispanics. You'll hear that from everyone when they have a problem of identification and a problem of realization that we are one. You'll hear that all the time.

What I'm saying is that this is an opportunity to do

away with a lot of those problems. This is an opportunity to incorporate planning endeavors and planning opportunities for other groups that are not now in the planning that's going on, who have not been asked to participate; yet have 40 plus million acres that they're going to have to incorporate to your system, their own system, simply because they're citizens of the state, citizens of the country. How are you going to say to them that you don't have to pull out your oil, you don't have to pull out your gas now, when they know they do have to now. Because the society is forcing upon them their own rules of the game, forcing them to become involved in the 20th century capitalist system overnight, which is the system I believe in, by the way, even though I feel that cooperatives certainly will, most likely, work best in rural Alaska for many years, because the communal system inbred into our people to do away with it very quickly for a capitalist system.

I guess what I'm trying to say is that I don't see how we can plan for the fund utilization until we have identified more clearly and more fluently who, in actuality, is going to administer the fund; because if you identify the areas by regions of the state of Alaska, and I view Alaska as six states not one, six areas of Alaska that are somewhat separate from each other. If you do identify those areas for planning purposes, you will identify how the fund will be utilized.

You have no real commonality between Southeastern Alaska and Northwest Alaska. One is fishing and timber industry base area and the other is a subsistence area. The two are not in any manner similar. The only similarity might be in the fact that some communal systems still work in both parts of Alaska. If we then recognize that there are different parts of Alaska that need to be taken into consideration in our planning endeavors and in the utilization of this fund, we then certainly must recognize that the administration and the utilization of the dollars and the actual expenditures and how they are best put to work for Alaskans, how they will best incorporate more equity into our lifestyle and how they will better do away with the inequities that cause prejudices and fears and the misinformation and the wasteland that sometimes we don't even like to think of and the fact that we do many times disallow each other a good lifestyle simply because we are different.

I think that we need to re-evaluate what we're doing with these dollars. We need to re-evaluate in the sense that we need to take into consideration that we can't, as one group of people sitting in Juneau, dictate for all of Alaska a system that will be compatible to all of Alaska. Simply because there has never been a time when anyone has really looked at my part of Alaska, for instance, and never really

been a time when anyone has looked at other parts of Alaska. It's an opportune time. It's an opportune time to make a pact with the national government on D2 lands. We should not actually determine what the D2 lands are going to be until Alaska has had the opportunity to utilize some of its new-gained wealth to evaluate our state, to thoroughly recognize what's under the ground before we determine what it should be called on top. I think that's something we should look at--some of the things that we need to fairly evaluate. A gentleman made the comment that the educated are moving into Alaska. I hope they're not coming from places like New York and places where it has been shown that their system has failed miserably.

BERGMAN: Let's not have any bigotry here.

BLACK: This is not a racial statement whatsoever. I'm hoping that what we have in Alaska is a start of a new planning effort that can incorporate more Alaskans on a regional basis. I hope that you gentlemen don't take this as a personal thing that I don't believe that the legislature should be by itself in handling these dollars. I think that the legislature has great wisdom, but I do believe the people out there can plan and have some policy control over these dollars. I would certainly agree that they should be involved in the final determination.

GRUENING: Thank you, Cliff. Can you stay for questions? Is there a question of Mr. Black? Representative Meekins.

MEEKINS: Cliff, I am wondering what you think about where would the greater benefit be, I suppose this is contained in your comments, but I wanted to ask you directly, if you think there would be greater benefit in an Alaska, Inc. type proposal where the income from the fund is directly distributed to people in the rural areas, for instance, or if you think a development bank concept with planning agencies and regionalized, as you have talked about, would be preferable.

BLACK: I haven't really made up my mind seriously on Alaska, Inc. Whether or not I could go beyond the distribution of funds beyond the retirement level so that Alaskans who have lived here all their lives don't have to leave the state to retire. I think that's a tragedy. They have lived here all their lives, then they retire, then are forced by economics to leave our state, simply because we lose their expertise, we lose their knowledge in vast areas that cannot be gained overnight. Only

those people who have lived here for many, many years understand Alaska. We are losing them very rapidly. I would say that the majority of dollars be put into, not the majority of dollars because I cannot even comprehend that kind of money, but a good amount should be put into the development of really significant homes for the aged, take care of them and keep them in the state so we can utilize their expertise. Beyond that, I have still to make up my mind. I would certainly have made up my mind further had I been more comfortable with who would be administering the fund in the long haul.

GRUENING: Senator Rodey.

RODEY: Cliff, could I ask you another question in regard to administration? I'm as concerned as you are. Do you favor a method of electing members to the Permanent Fund board or an appointed mechanism such as has been embodied in the governor's bill?

BLACK: Well, elected representation is always good if it is on a regional level. If you put it into a state level, a good portion of Alaska is left out of any major decision-making possibility. I view the Permanent Fund in the sense that it's

an opportunity for a full type of revenue sharing that would incorporate the different costs in Alaska. For instance, if you buy a dozen eggs in Barrow right now, it'll cost you \$2.00 or more. The cost of service, the cost of product, the cost of anything that happens in Barrow is tremendously different from the cost in Anchorage.

What I'm saying is simply that if there's a revenue sharing device used for the distribution of these dollars, it incorporates very clearly the different cost of living differentials and it is distributed in that sense, then I could see a regionalization utilization based on election processes and very well could even see it go beyond that to dictate that a particular community would be represented and a person from each community could be represented on the regionalized board. So that way you wouldn't have to have any communities left out in the process.

RODEY: Your main concern is to ensure that some of the areas of Alaska which have a smaller population are represented on whatever Permanent Fund administrative body is finally formed. Is that what you mean?

BLACK: I guess my concern is--I'll go back to comments about the federal system in Alaska, the paternalism system

that has for many, many years placed it's hand on our head and said, "we will do it this way," and have never reached the point where they've done anything that we've wanted them to. They've always gone and done things as they've wanted to do them.

What I'm saying is that in this case I would like to see, since we're all citizens of the same state, since we are all part of the same state, that there be some manner where all Alaskans will determine the direction and utilization of these funds.

GRUENING: Thank you, Mr. Black. Are there questions from the audience? We have panelist here; we want to keep them on their toes. If you have some questions. Representative Chatterton.

CHATTERTON: Thank you, Mr. Chairman. Can you hear me alright? Mr. Chairman, I want to congratulate you on getting this group together, I can assure you it has been stimulating and very thought provoking. I hope you'll keep up the good work because the total picture can only be seen once all the various, however conflicting they might be, parts of the picture come before you. Keep up the good work.

GRUENING: Thank you, Chat. I didn't ask for that plug.

CHATTERTON: I really have two questions for

the panel, that developed this morning, but I can't help feel a little bit facetious. There was a person who testified here a little earlier this afternoon and made a suggestion as to how to use some of the Permanent Fund funds. I felt I should provide you also with a corollary suggestion for their use. Instead of buying all the federal lands that are put up for oil and gas leases or along with that, I suggest that we buy the national interest land and thereby immediately solving the D2 question.

Mr. Chairman, through you I would like to ask the panelists or anyone that would care to comment--we did hear earlier comments about: 1. loaning money; 2. investing money. It was even suggested earlier--there was some comment about investing in a pipeline or a petrochemical plant--state funds. My question to the panel and to the economists--if they have any background on this, would they care to comment--does the potential for a conflict of interests develop when a taxing entity becomes a participant in the profitability of a taxable entity?

My next question is--is there a degree of parallelism, at least in some facets, between what is before you, Mr. Chairman, with this Permanent Fund and what had to be before the U. S. Congress some years ago when they were faced

with seeing that each and every native Alaskan got a fair share out of the Alaska Native Settlement Act? Is there a parallelism? That's my second question. Thank you, Mr. Chairman.

GRUENING: I'll leave that up to the panelists, the economists, anyone who wants to speak up.

GORDON: I am really no expert on the problems of taxable entities. The notion that some of the investment proposals put forth recently here remind me very much of where I now live. I happen to have moved to Canada in the last few months. In Canada, there are truly an astounding number--they talk about free enterprise like everybody--there's just an astounding number of what they call their Crown Corporation, Federal Crown Corporations, and Provincial Corporations.

Now when you say is there a conflict of interests, they attempt, at least, by this device called a Crown Corporation, to make the Crown Corporation totally operate like an individual enterprise, despite the fact that the state or the province or the nation owns all the shares--sometimes not all the shares, most of the shares. I think if you survey the record of those Crown Corporations, that it is dismal. They have a Crown Corporation selling what Westinghouse sells--

atomic reactors. They got involved in a little bribery, but the most significant thing is they managed to sell two of their atomic reactors to Argentina at a loss of \$130 million.

The Province of Alberta has something called Alberta Heritage Fund. They're visably in the business of setting up businesses that otherwise wouldn't be there--irrigation facilities, food packing plants, huge petrochemical operations. The other thing they're doing is providing more services than otherwise would be the case and lower taxes. They're the lowest tax province in Canada by some piece. The result is that an enormous number of people are leaving the rest of the country and going there. The wages are lower there than they are where I happen to live in British Columbia, but people are moving there--that's where the jobs are. Rents are going up. Land is getting scarce. I see very little merit, what apart from the conflict of interest problem.

GRUENING: Is there any comment on the second half of the question, which was--was there any parallel between the Native Land Claims and what we might be trying to do with the Permanent Fund? Mr. Love.

LOVE: Well, it is my understanding that in British Columbia, under the New Democratic Party, there's a lot of acquisitions in terms of the Crown Corporations. As a result, partially because of their policy for rapid acquisitions, there's a problem with the insurance industry that the New Democratic Party was defeated and replaced by the conservative government of Mr. Bennett. It's also my understanding that Mr. Bennett's conservative government has not divested themselves of any of the acquisitions made by the NDP and that most of them, in fact, are now on the whole profitable. Is that in accurate summation? Just as a parallel to the experience the Federal Crown Corporation as looking to British Columbia where you teach.

GORDON: No, not entirely. You see, to describe the present government as conservative is, I think, quite incorrect. We have two kinds of parties in British Columbia. One is socialist and the other is more socialist. It is not true that those have become profitable. It's not true--they've all been losers. In fact, if you investigate in the theories of finance they teach in business schools, it is extremely difficult to lose money consistently by investing. The NDP did not succeed in doing so. But more serious, some of their acquisitions, a distressing number of their acquisitions, have lost money.

They perhaps could have been defended on the grounds that they had some social purpose. There's a great dispute about what the social purpose was and whether it helped anybody significantly.

I'd say in Canada, there's all kinds of conservative government of another province in far east. New Brunswick. They bought all kinds of things, setting up another conservative government. They got into an endless stream of business--nearly all of which went bankrupt. The one advantage, incidentally, of the Crown Corporation is it isn't like many of the corporations into which the British government bails people out. When they set up a corporation, it is like a private corporation. When it goes bankrupt, it's bankrupt. So it doesn't continue forever. It's just draining off the public purse. That is a legal device which, I think, is of some usefulness.

I think there's a great parallel; it's a little hard to classify political opinion. It seems to be so simple that a liberal, radical person interested in the poor and egalitarianism should be for one thing. And that is give the money to everybody, if they could, and they can't. Okay. Invest it as good income as possible, and give that good income to the people. That would do more for the world

of Alaskans. It would be an immediately equalizing phenomenon. I cannot think of one thing that has been proposed here that is going to do nearly as much for the poor in Alaska as that kind of proposal.

LOVE: Which you stated on several occasions.

GRUENING: I think we've got the different philosophy pretty well outlined here. Is there any comment on the second half of that questions? Or another question from the audience?

HAVELOCK: I think the answer to Mr. Chatterton's second question is yes.

GRUENING: Okay. That's the kind of answer I like. Mr. Dave Hickok, did you have a comment?

HICKOK: I agree with John. I think the answer is very definitely yes.

GRUENING: I believe this gentlemen in the red shirt wanted to ask a question. Could you identify yourself please.

WICKS: No specifically a question or even an answer. My

name is Alan Wicks. I'm a recently retired teacher, in the Anchorage School District for the past 20 years. I came to Alaska initially in 1940, working for the Territorial Department of Health. At that time, I supported our Chairman's grandfather, Governor Gruening of the Territory of Alaska, in his efforts to roll back an unseemly rate increase by Alaska Steamship Company and have been more or less a Gruening supporter ever since.

One thing that is lacking in all of this commentary and discussion as to profits investment management--there's one thing lacking, because it seems as if everybody is making an effort to play God for everybody else. While we like our benefits and we like our dividends, and I like them as well as anybody else and have been lucky, and like the Wall Street Journal has said "nothing succeeds like dumb luck." A little bit of that can go a long way if you're on the lucky end. I want to put a diagram on that board. As a teacher, I just can't resist the opportunity. Then I'm going to come back and make a couple of comments about it and then a question at the end.

GRUENING: Okay. It's getting a little late. We want to keep everyone interested.

WICKS: I didn't need the eraser. I didn't want to wipe off the rest of that. There again, somebody made allusions and maybe I'm, well no, I'm not, just reiterating what a couple other people said. We've arrived at a place in international affairs. I'll flash back to pre-World War II and depression times. We've arrived now with technology and science and my background is basically biological science--we've arrived now at a place where humanity with it's science and technology doesn't really know where it's going. But I submit to you, and this is an independent, personal formulation, I won't give the blame to anybody else; but unless and until humanity arrives at a umbrella concept, and that's what that is, of first basic, foremost environmental, ecologic concern before the fund, before the investment of the fund, before the applications from the return from the fund. What I'm saying is that civiliziaton and humanity, at this juncture is up against it. If we don't learn or haven't learned what the aborigines, the native peoples, learned long ago, was to live and operate in concert with nature, with earth. Not as it's master, not as God who says, "I'll scrape it, I'll build it, I'll erect the edifices in my own way and to my own needs and beliefs and likes." Now I'm going to leave that idea, but I think it's the one that needs the most emphasis, first and before just about anything else.

I'd like to turn to the panel, and while I respect and admire Dr. Lindauer's views, he is a relatively new and accurate able observer of the Alaskan scene. I'd like to ask him how he discriminates on one hand between the need for application for funds to this or that industry or development, to get to a specific point, or the abhorrence of the use of the funds because they would be an economic magnet to people elsewhere to come to Alaska, but on the other hand, my, and I'm tickled to death I've got it, my 5¼% FHA, if it is made available to them, it's not going to just be a drove, a horde, who are attracted to the magnet of 4% or 5% or 7% Alaskan-style FHA. We're not going to be able to differentiate between those things in any way.

LINDAUER: That's really an excellent question.

One could easily say that you could do the same, for example, with Alaska, Inc. as using eligibility for loans for business. It could, in fact, be those people who are here now and could have such time variety for qualification or w0 years, and you pick the number in order to qualify. It wouldn't really qualify that they'd be eligible. What we'd assume the utility serving a native village would

be instantly qualified. We'd assume a long-term Alaskan would be instantly qualified. The question is where do you draw the line. That wouldn't seem to be that difficult.

BERGMAN: Let me ask a question about Alaska, Inc. Suppose you have two kids born the same day, and one of them is the child of a long term resident and the other is the child of someone who is not a long-term resident. Are you going to give one of them the Alaska, Inc. payment and not the other?

GRUENING: The governor isn't here to defend himself. The more you get into the Alaska, Inc., the more difficult it is to exactly define who an Alaskan is or who is the beneficiary. It doesn't mean it's impossible. But obviously if it's going to be a meaningful program, you've got to draw the line somewhere.

BERGMAN: I understand that you might be able to draw it with adults, but I think if what you're trying to do is enfranchise only those who are here now and their descendants, you've got a tough row to hoe. I don't think you can do that.

GRUENING: Alaska, Inc. does have a residency. The child isn't really eligible until it's been here a certain number of years.

LINDAUER: What would, for example, require 18 year residency, at least, so an 18 year old can enter into contract. So whatever is the legal age for entering contracts, that means every child will be eligible if they've lived here long enough. As would be anybody who arrived.

HAVELOCK: It's not going to stand up constitutionally though.

GRUENING: I know that's being studied. I'm sure there's some way you can find a way, but we're not here to discuss that. Somebody who hasn't made a comment yet. Mr. Hickok, would you like to follow up?

HICKOK: I'd like to say a couple things that tie in on this subject. My name is Dave Hickok. I'm the director of the Arctic Environmental Information and Data Center at the University of Alaska, currently the president of the Alaska Division in the American Association for the Advancement of Science. I think there's two or three items that seem to me have not been covered.

One of the things the economists appears to have said is that the need on the curves is a function of economics

alone. I'd like to say that I don't think it is. I'd like to give a few examples of what's happened to history in Alaska. One of the needs trends that has determined what has happened in Bush Alaska has been, for example, many years ago, in the Arctic latitudes here, we did a lot of research on ionospheric scatter and so on. We were able then to develop satellite communication systems for these latitudes which was not a possibility under existing technology of lower latitudes. Now what has happened here is because communication was available to Bush Alaska, technologically, and because there was a political decision made by very, very few people for the sale of the Alaska communications system about 1970, the whole need trend for communication and development for this kind of thing in rural Alaska changed. Not by virtue of economics, but by virtue of technology and science and by virtue of political decision.

There also have been a number of other of these kinds of things. In the health field, two doctors made the breakthrough in tuberculosis following World War II here in Alaska. The highest incident rate in the world in the early 1950's of birth rate and death rate in rural Alaska---beat the Kalahari Desert in Africa and everywhere else--were brought down by science and technology. The application of money, in that sense, of the political decision to stamp out disease.

These things make aspirations. These things make needs that are not just driven by the common market place. I would suggest, in addition to the economics of capital investment and so on, there are at least three or four other items that are driving the need co-efficient and that is law and politics, which I put in despite Mr. Havelock's qualms, hand in glove, science and technology and perhaps a population expansion. These things are making change in Alaska. The need curve is escalating at a tremendous rate despite what happens in economics.

The aspirations of the Bush communities, where there are hundreds of them, have no water, no sewer, no schools. These aspirations are real. They are going to drive a demand for public expenditure funds to satisfy these problems. I would certainly agree with John Havelock that the Statehood Act called for the expenditure of tax revenues and so forth to support a burgeoning new state. I would also suggest to you that the Alaska Native Land Claims Act also had the same effect. The one thing that Alaska has not recognized, or several things it hasn't recognized, but one thing it hasn't recognized is that rural Alaska should not pay the price for the public services that everyone else in Alaska enjoys in the urban settings. Through their compensation dollars that came under the Native Land Claims Act, they are entitled to the

same public services as anyone else. I guess that's about enough.

GRUENING: Thank you, Dave. Would you mind remaining for a minute in case the economists or the legal field would like to responds.

BERGMAN: I'm the one that introduced the word and when you started talking, I instantly regretted it. Then I recall that I had put quotes around it. I actually agree with you that there is no such thing as absolute need. You can't take a certain desire and say this particular desire is a need and this particular desire is not a need. What I'm trying to point out here, though, is that if the population were to grow, just to maintain a certain level of services would require a growing trend of revenues, which is an entirely different point.

HICKOK: I think you're right. But regardless of that, the need curve, the demand curve, perhaps, of social aspiration, human aspiration, is escalating at a tremendous rate, regardless of the economics of the state. Because of broader expansion in health, in education, in other factors.

BERGMAN: Well, I think what you're saying is what some other

people have said--that perhaps it would be more reasonable to use the oil revenues for this kind of purpose. Use them all for this kind of purpose--setting up schools, setting up water supplies, setting up electrification plants, instead of either sending it to these much maligned New York brokers to be kept for future generations or perhaps for giving concessional loans to people of Anchorage. That, I think, is a matter of simply social policy. You've got to fight it out. That's not a matter of economics. That's a matter of what you can get the people of the state to spend their income on. I feel that the Supreme Court had said schooling had to be provided throughout the state in a more or less equal way. There's a famous California case on that.

HICKOK: Well, we had one here in Alaska too.

BERGMAN: So I don't quite understand the fact that it hasn't been done already.

MEEKINS: Doctor, are you saying that expectations or needs, whatever you want to call it, are not related to the economics?

HICKOK: I think they're related, but I think there are a number of external forces that make new aspirations.

Prior to the research on ionospheric scatter and so on, that made possible high altitude communication systems, there were no aspirations for it because nobody knew it could be done. There are a lot of these kinds of sayings. Before you could put a sanitation system in Arctic permafrost, you have to know how to do it. Then by virtue of it being able to be accomplished, there's aspiration for it.

MEEKINS: I think that's the common denominator between the two. Because when you have money, it's, therefore, possible to build things, it's, therefore, possible that weren't before. It's the possibilities that seem to feed the needs.

HICKOK: No, the possibility may fuel the need, but not necessarily money. In the case, for example, of the communication situation here in Alaska that wasn't a function of money.

MEEKINS: I'm not limiting it to money.

HICKOK: It's research of science and technology and a political decision to sell the Alaskan communication system away from the military and to put it into modern science.

MEEKINS: Just to clarify--I'm not limiting it to money.

I'm saying that things being possible is the common denominator between technology and economics in your scenario, because even if the technology made it possible to have telecommunications, if we didn't have the money, even if we had the political will, we wouldn't have it.

HICKOK: Then, I would to back to Tussing's scenario. I think what Tussing is saying is that the private sector, the private demand for these things is running, and we have a large sector of private money, by virtue of Native Land Claims and the growth of the Alaskan economy.

GRUENING: Thank you, Mr. Hickok. Okay, in the waning hours, are there any more questions? Sure, you're welcome to ask again, if there's anybody who hasn't had a chance to ask...

FISKE: I'm Lieutenant Colonel Fiske--Retired. I'd like to say first that I strongly support Dr. Lindauer's position on adequate investment of Permanent Fund in Alaska and for the lowerest, reasonable interest rates, and where present Alaskans can enjoy the benefits of employment, social amenities, health services, recreation, etc., etc., and etc.

I'm interested in providing something to occupy the leisure time of the many small communities, particularly during long

winter hours. Something that involves all ages, both sexes, from youth to octogenarian. Most of our rural communities have churches, bars, but many have little else to occupy the people when they're not busy at making a living or subsisting. It seems to me that an excellent way to use some of the earnings and possibly some of the Permanent Fund would be to develop a program to provide indoor recreation facilities--I'm referring to curling, skating, and I'd like to draw a comparison with what the Canadian government has done. Many, many of their small communities have been funded to build curling, skating facilities, which also provide a place for the community to assemble for all kinds of things. I believe that if the Permanent Fund and the native regional corporations get together, many of these small communities could be provided with something that would knit the communities together. Their needs, then, would be brought forth as a community requirement. I think, it would do much to knit the communities together throughout the state of Alaska. I would suggest that all of the other comments today have been primarily on what to do with the fund. I submit that this is just one idea that might be considered in providing for Alaskans who can enjoy it through all ages. Thank you.

GRUENING: Thank you. In bringing this to a close, I want to ask the audience once again if there's any questions they'd like to ask the panel?

HAVELOCK: I'd like to make a comment on that last statement. I think that if the Permanent Fund committee does adopt some sort of internal investment policy as part of the Permanent Fund, you should be careful at the same time to keep a count of the public costs that are going to be associated with that private investment. Perhaps, Dr. Gordon could comment on what kind of ratios those are. It's clear you're going to be giving money for loans for small business, that you are going to kick off at the same time a lot of pressure for public amenities to go with that. If you haven't taken proper account of that, you're going to create substantial social unrest.

GORDON: I can't really answer that. I would be very surprised, however, if you could make some generalization about that. If you subsidize investment on the private sector, it might entail a considerable amount of public spending outside of that. In other cases, perhaps a very much smaller amount. I think you'd have to investigate each on a case by case basis.

GRUENING: Mr. McCutcheon, you were going to ask the last question.

MCCUTCHEON: It will probably turn out to be a rhetorical question. There are several things here I'd like to state. Professor Gordon, you challenged Paul Fuchs's estimation of the greater return on investment of Prudhoe Bay. I don't necessarily share Mr. Fuchs's view of what should be done. I thought that you might possibly give us some idea of your estimation of the greater return on Prudhoe Bay, and maybe you could start with by getting to the size of the reservoir, the amount of recovery under current production practices, the amount left in the ground, the amount of additional recovery through secondary treatment, what will be the value of oil, price of oil on the West Coast, what will be the value of oil delivered at the West Coast, what is the value of the investment that's going to be happening? What are the profits contributable to tax relief, tax loopholes?

GRUENING: May I just interject here? These are very interesting questions. I think they, at least have some relevance to the Permanent Fund...

GORDON: I'd like to answer that. In the first place, nobody can rate that question. Anybody who thinks they can tell you the price of oil ten years hence, as has been suggested around here, is engaged in witchcraft. Let me explain one other thing. What I wanted to do was find out how this Prudhoe Bay figure came

out \$98 billion, and I happen to know that's the sum total of all American corporations from ma and pa ones up to Exxon--all over the whole world in any one year, after taxes.

RODEY: On behalf of the Senate Permanent Fund Committee and the chairman, Senator Hohman, I'd like to thank the House for putting this symposium on. This is the first in a series of meetings that the Senate and the House will be participating in. The House effort is more visable here in Anchorage because Chairman Gruening has done a very good job of getting the committee's work planned and accomplished. The Senate Committee's work is being done primarily in Juneau at this point; and we are trying to work in conjunction with the House to provide as much possible information on the Permanent Fund as we can before our January deadline of drawing up legislation. If there are questions or concerns, I know either the House or the Senate would be happy to address them.

SCOMM

#9:193

HOUSE SPECIAL COMMITTEE ON THE ALASKA PERMANENT FUND

Friday, July 15 1:30 p.m.
Saturday, July 16 9:00 a.m.

4th floor Jury Assembly room
Alaska Court Building
303 K Street
Anchorage, Alaska

AGENDA

FY 1977 Financial Report
Consultant Reports:
 Arlon Tussing
 Belden Daniels
Publication discussion and revision
5-year Revenue projections
Report on current Permanent Fund investments
Interim budget and plan of operations
Discussion of Permanent Fund proposals

#193

These transcripts were taken from tape recordings. They have been edited for the purpose of clarity. The original recordings are in the possession of the committee and may be heard upon request.

Proceedings
of
The House Special Committee on the Permanent Fund

COMMITTEE MEETING

July 15, 1977

Anchorage

Rep. Clark Gruening, Chairman

Rep. Terry Gardiner, Vice Chairman

Rep. Ernie Haugen

Rep. Russ Meekins

Rep. Bill Miles

Rep. Leo Schaeffer

Rep. Rick Urion

PRESENT: Clark Gruening, Chairman; Terry Gardiner, Vice
Chairman; Bill Miles, Russ Meekins, Leo Schaeffer;
Hugh Maline; John Rader; George Hohman.

TUSSING: I am not going to read the paper, nor am I going to go through it point by point. Frankly, it is a little too heavily steeped in jargon and it is hard for me to get back and read it through a couple of weeks after I have done it and exorcise all of the economist catch phrases and financial catch phrases.

GRUENING: Arlon, give us a little bit of your background. There may be a few people who haven't heard of you.

TUSSING: I know almost everybody here. If they don't know me, maybe it is their hard luck. I am a adjunct professor of economics at the Institute of Social and Economic Research at the University of Alaska. I have been connected with the university in one way or another for eleven years. With the short study requested by Representative Gruening to cover some of the background of economic issues that the committee felt had not been really treated before the committee got into looking at the organization in terms of the permanent funds. I have read Dr. Daniel's paper, and let me assure you that until this morning I had never met him and we did not cooperate or collude in any way. So I found nothing in his paper that I could disagree with and a great deal I could

agree with.

GRUENING: I might just introduce the committee. I am the chairman of the House Permanent Fund Committee and sitting next to me is George Hohman, the chairman of the Senate Committee on the Permanent Fund. Two members of the Senate committee are here in attendance, the president of the Senate, John Rader. At the end of the table, Senator Pat Rodey, from the Senate. On my left, from the House, is Representative Terry Cardiner who is Vice Chairman, and Representative Bill Miles. Going down on the right side, Representative Russ Meekins and Speaker of the House Hugh Malone who is not a member of the special committee, but has an interest in the Permanent Fund.

TUSSING: Let me emphasize one issue in particular which is mentioned in my paper but does not have---does not really focus on as much as I would like to focus on. That is that the investment policy of the Permanent Fund will have far less influence on the rate and shape of economic development in Alaska than the amount of money in the general fund and the way the general fund money is spent. For one thing, the general fund is going to be much larger than the Permanent Fund according to the kind of numbers we are talking about, as far as revenue dedications to the Permanent Fund.

A Department of Revenue projection issued in February of this year, assuming a 25% contribution revenue to the fund projected in 1985 Permanent Fund balance of \$1.8 billion and a general fund

balance in the same year of \$6 billion, as based on the projections of existing programs and the anticipated gross rate in state spending. That \$6 billion is surely not going to accumulate in the general fund. There is going to be enormous pressure to spend it. But the general fund---the money available in the general fund will be much greater than the money available in the Permanent Fund. For another reason the general fund will have more influence is that its expenditures in general move directly into a spending stream in the state's economy through payrolls and procurement while the Permanent Fund money, much of it will be invested outside and, as I will explain in a moment, probably all of it will be in effect invested outside no matter what the investment policy the Permanent Fund is.

Thirdly, the Alaska demand for Permanent Fund investments is extremely low. There is very little additional demand in terms of potential income earning projects which can be funded by the Permanent Fund which would not be funded through existing financial sources and much of my paper is devoted to this. An examination of the question of whether or not there is a capital shortage or not---in other words whether or not the existing financial institutions are sufficient mechanism to bring capital into the state.

My conclusions are this: Major industrial ventures in Alaska, and this includes ventures in fish processing, mining

timber, major agriculture developments, major tourist operations, are very adequately served by existing financial institutions. That there is no financial obstacles to their continued rapid development in the state. The obstacles that exist tend to be problems of resource location and marketing regulatory problems including state leasing and permitting and federal leasing and permitting. But they are not financial problems, for the kind of large industrial venture that would significantly diversify the state's economy, or the kind of large industrial venture that would be piggyback on our oil and gas industry like petrochemical. These investments will be made by large national or multi-national corporations drawing on their regular sources of finances. For those that are independently developed within Alaska, the new ventures with new enterprises, there are a large variety of institutions in the capital market that are interested in the financing required investment.

I will give an example of this from my personal experience and involved in a new fishing port in a remote totally undeveloped site in Western Alaska. The preparatory work putting together of the land leases and getting the engineering design on the port facilities had just barely begun and we have made no public announcement of this, yet within a few weeks after this started we had been approached by three major outside banks---one New York bank, one California bank and one Canadian bank, who were very interested in putting together a financing package for this venture which is

just a beginning of a conception. All of these banks have specialists to deal in Alaska and there is no lack of information to prevent them from going and looking for more information and looking for investment opportunities. They are as aware of anybody in Alaska or as aware as the managers of the Permanent Fund of the opportunities that the expansion of U. S. National Fisheries jurisdictions and the growing world demand for protein and the opportunity that it will create for bottom fisheries and other fisheries in Alaska. One of these major New York banks has a specialist who is heading up a whole team dealing with these problems specifically.

Another experience we had was that directors of the new firm were immediately inundated with approaches from friends who had invested and who were looking for places to put venture capital. High risk, high potential return ventures with large tax write offs. People come in and say I have got \$29 million I have to place during this tax year, or I have got a problem. They want a potential rate of return but most of these big development ventures aren't terribly sensitive to the small differences and the amount they pay per capita. A major venture, a big venture, that where there are millions of dollars involved, those millions of dollars can carry a great deal of investment research and exploratory work on the part of either the ultimate investor or the financial intermedior, the insurance companies or brokerage houses.

So my conclusion with respect to major industrial venture, not only is there no problem, no specific problem, but that Permanent Fund investments in these ventures will essentially displace capital that would come in from the outside. So from the point of view of impact, the point of the impact in Alaska's economy, or the impact in diversification of Alaska's economy is going to be very little. A concentration on these ventures might on the other hand affect the security of the quality of the loan portfolio of the Permanent Fund because, in a sense, you are putting all your eggs in one basket called Alaska and the very thing that may make your regular revenue fall may make these investments in Alaska enterprises particularly risky.

Move on to another area in which the Permanent Fund probably has no role and no particular effect, and that is the commercial loans in the urban areas of Alaska. There is no capital shortage here. The existing financial institutions, the commercial banks, thrift institutions, factors, mortgage brokers, etc. and both the commercial and residential, it is the same way in Alaska as in the rest of the country---there is no substantial interest rate differential between Anchorage and communities of comparable size in the rest of the United States. There seems to be a greater availability of loan money, partly because the people in some of the outside financial institutions have a great faith in Alaska because the growth is assured. There is no problem, there is no capital shortage to be filled by the Permanent Fund in the area

of equipment financing, the kind of item trucks, construction equipment, generators, compressors, aircraft, etc., which are movable where the financing is available from vendor to manufacturer, from equipment financing companies, from banks and smaller units from credit unions and the like. No matter where you are in Alaska, if you need a backhoe and you've got something useful to do with it, and a prospect of some income, you can finance a backhoe. There is no capital gap for the Permanent Fund to fill here. The question of utilities and other utility type interest subsidy investments is often raised and I see quite a bit of talk about the Permanent Fund providing credit to the Alaska Power Authority or to the Susitna project. This could be done but it is another incident where the Permanent Fund would probably simply be displacing money that would be available from outside. If the Susitna project is viable, if it can prove that it can pay its debts or can be financed conventionally, and the reason that---there are several reasons why the Permanent Fund should probably not be involved in financing the long term debt of the Susitna project.

First is that the Alaska Power Authority can issue tax exempt bonds, while at the same time the Permanent Fund can invest in taxable corporate bonds, for example, or federal securities that get a higher rate of return than the Alaska Power Authority or any solidly based Alaskan utility would have to pay. It makes no sense for the Permanent Fund to be

getting a low rate of interest on its investments than it can get in the open market while at the same time the Alaska Power Authority doesn't get any break on the cost of capital.

Now, conceivably, the Permanent Fund could be used as a source of equity capital for joint ventures. However, going through most of the major categories of the capital market in Alaska, these are either areas which are adequately served by the existing financial institution or ones in which the Permanent Fund could probably not make a useful contribution anyway.

One area does stand out as an area of opportunity and in this very preliminary survey it seemed to me that the one capital market that is not serving its constituents well is that serving small community business, medium size business in the small communities and in the Bush in Alaska. The urban commercial banks in Alaska just don't reach out far enough. The cost of information gathering, of servicing loans, the cost of collections and repossessions, foreclosures, resale and things are just too much. Outside institutions don't deal with them. The demand is too sparse. So the tourist oriented business or a local store or a small locally owned fish processing venture or something on that order may not be able to borrow, or, for that matter, to obtain any sort of capital on terms comparable with a similar venture---a venture with similar early expectations in a major community. And so I think there is an area in which the state could look at the formation of regional development. Probably a statewide development bank would be too

big and would be too far from the---the problem in the Bush and the small communities have people on the scene oriented to problems of the particular community. I would suggest looking at the possibility of setting up a state-chartered regional development bank in each of the regional corporation areas and working together with the regional corporations, or having the regional corporations participate in these rural development banks, but having a professional management supervised by the Permanent Fund using Permanent Fund money. The problem here is that I doubt whether the aggregate demand for capital from all of these banks would be greater than forty or fifty million dollars at the present time. A great number of people in smaller communities in the Bush who feel that they are not well served by the existing banking system. But the total amount of real business they would generate is relatively small and you are not talking about billions of dollars---you are talking about tens of millions most likely. Just think of what it is in the Calista region which has induced the Calista Corporation to put its money outside of the region. How much potential private investment that could be locally developed does exist? How much opportunity is there in the Calista region? It is nothing like the kind of funds we are talking about with the Permanent Fund. So I would say by and large the potential role for the Permanent Fund money in altering the shape or

character of Alaska's economy on a business-like basis is rather small.

I go on to say the Permanent Fund is not a very promising tool for short economic stabilization. I am not sure how many people really think that it could be but I've heard it referred to as something that could feed money into the economy in a slump period and slow down the investment activity in a boom period. Now as far as dealing with the regular business cycle that lasts two or three years, there is a number of reasons why Permanent Fund is not a promising tool.

In the first place, its impact is less and slower than that of the general fund. The impact of the Permanent Fund investment policy is going to be very, very minor compared with what is done with the general fund. The general fund expenditures are direct injections into the state's economy. They occur now and secondly because Permanent Fund investments---many of them will simply be displacing capital which would otherwise come in but there is another fundamental problem that, even if these were not ---even if these previous problems were not involved, there is another problem that would probably make it impossible to use the Permanent Fund or general fund appropriations for that matter as a significant stabilizing force. That is by the time it takes the management to recognize that we are in an overheated boom situation that something out to be done about, we may well be approaching a turning point. So it takes some time to recognize something ought to be done. Then you have to implement the policy. And by the

time the loans are made and the people or concerns who receive those loans start paying construction workers, it is very likely that we are going to be on the other part of the cycle. But the effect of the Permanent Fund---or for that matter the effect of the legislature---trying to use the capital budget as a stabilizing device is that you are going to zig when you ought to zag.

There is a very good persuasive case on the part of some economists that the federal reserve has been more often ---that the effect federal reserve policy nationally has been more often wrong than right. We could build a business cycle model of the Alaska economy and give legislators in the--- give them say \$4 billion on a computer to play with. We will start the thing off at 1964 after the earthquake and see whether there is any---see what you can do on the basis of the effect on unemployment, building starts, on gross products if you have gross products, and things like that. See what happens as you try to influence the economy with this. My intuitive guess is that it would create---no matter what you did trying to do it would create oscillations in the economy that wouldn't have existed before. I just don't think that it can be done.

There is another problem. It is a practical, political one. That is, when the money is available, when you are in a recession situation, when the money is available there is

resistance to spending it. You are in a boom, no matter how high the rate of inflation and how great the pressures that boom is creating on public facilities. It is going to be very hard to get anybody, whether it's in administration, legislature or managers of the Permanent Fund, to say we ought to turn off the water when the revenue is more available than it has ever been before and the needs are growing by leaps and bounds because of this boom and population influx. If you are skeptical about that, look at what happened to all the talk about stockpiling of public works projects until after the pipeline construction is over. It just is not going to happen.

Nevertheless, the Permanent Fund can be an important long-term stabilizing influence. That long-term stabilizing influence as the main intention of the people in voting the Permanent Fund and the legislature for establishing one. That is the result of the fact that state spending is the main engine of growth in Alaska. It determines in the long run the level of employment and level of population and determines the needs for government service. The principal influence of the Permanent Fund on growth and on the size of the state's economy is the amount of money it takes out of the general fund.

The Permanent Fund is going to influence the rate of growth of the state's economy, but not on the supply side. It is going to have almost no impact on the rate of growth by the way it spends.

money, or the way it invests money. It will have a gigantic impact in terms of the amount of money that is dedicated to the fund because, for every hundred million a year that goes into the Permanent Fund, there is a hundred million that is not in the general fund for current operations and for state capital expenditures or for current consumption. In the next decade or two, the legislature is going to determine the rate of employment and population growth in the state and it is going to determine the rate at which the need for state services increases by the way in which it spends the money. It makes some difference whether this money is spent in tax reductions, in transfer payments such as Alaska, Inc. or welfare, on regular operations of government or on construction.

It would be worthwhile to have a comprehensive fiscal model of the state's economy so that you can look at what the differences are, but the differences aren't as important as similarity. The more you spend, the bigger the economy is going to grow, the more population we are going to have in the state and the greater the need for state services are going to be a year or two or five years down the line. So the more money that is not available for this process today, or the more money that is not spent, the smaller the employment and population base and the smaller the needs will be.

What the Permanent Fund does and its principal function

and principal predictable function is that it slows down the development of the state by diverting money from current expenditure. There is hope that it creates enough income and it grows to the point where it can sustain the state expenditures that sustain the rest of the civilian economy of Alaska in those days after the oil money is gone or when the oil money levels off or when the oil money stops increasing in amount as fast as the perceived need for population are increasing.

So if you take this revenue bubble and put it in the future, you stabilize the economy. I have two final points on this. The eye of the legislature ought to be much more on the amount of money that goes into the Permanent Fund than it is now, and probably a little less on dividing up the---or deciding what kind of portfolio the fund should have. And that the 6%, say 25%, does not solve the problem, it does not---25% of the nonrecurring oil revenue going into the Permanent Fund does not do away with the revenue excess, nor does it do away with the use of this oil money to create here in Alaska an economy.

It is just not when the oil money runs down and the oil runs out, that will be a long time, but when the rate of growth of state revenue starts to slow down. So putting 25% just means you got 75% left there with an enormous growth in those years when you have got a lot of revenue and very little when the revenue stops coming. So it seems to me we ought to start thinking in terms of what kind of formula for contributions to the Permanent

Fund will stabilize or create stable growth over the long term in the general fund and to do this you have to get some view---have some philosophy of growth for the state. That is, how rapidly should the state's economy grow. As I said, the legislature is going to determine how fast the state is going to grow by the amount of the money spent.

So you need some sort of formula and it should not be a fixed percentage. It should be something on the order of after your studies have determined the 6% or annual rate of growth, the real value of the general fund expenditures is what you need to sustain the reasonable growth in the standard of living in Alaska and a reasonable rate of population growth.

So, as far as what needs to be known, the research ought to be done. I think the legislature ought to look very heavily at just what are going to be future revenue needs. What is the projected income from other sources. And just how much of that gap is going to have to be filled from mineral royalties. Assuming that Prudhoe is the last big field and put in some speculative reserves and making assumptions about the price of oil and the rate of other resource development, and you say at what point are current revenues not going to be enough to sustain the level of government, the level of population, the standard of living that we want to maintain, and that will

tell you at what point you are going to have to start drawing out of the surplus in the capital fund to maintain this economy. If people are lucky, the growth will have a sufficient momentum that you will have future oil discoveries and you can keep putting off that day of reckoning, so that you may never have to draw on the accumulative surplus, much less the capital. But the principle remains the same. The most effective use of the Permanent Fund is to control what is available in the general fund, to make less available now and more available in the future. What should be in the general fund probably is the most important to know in setting up the Permanent Fund.

GRUENING: Thank you very much, Arlon. As usual, you have raised a few questions.

TUSSING: In summary, I think most of the investments of the Permanent Fund in Alaska will simply displace money that will come from somewhere else. Now it is possible to increase investment of various industries by subsidization or making loans available cheaply. The problem is that most of the ventures that would take advantage of them are ones that would be viable in any case. Both Dr. Daniels and I made the point that most new ventures, their feasibility is not very sensitive to interest. I mentioned in here that a new venture probably that expected to be able to be

written off in five years or so, which means a growth cash flow is in 30 to 50% of investment capital, and when you have got to have cash flow of that magnitude, a couple percentage points difference from what you are paying for, capital is not a crucial factor.

Well, I admit there might be some cases---in fact I was going to---there will for certainty be some cases which a prudent Permanent Fund manager might reasonably deem to be a prudent investment and managers of other outside financial institutions might not. Those marginal cases are probably so limited compared to the number of---if you are going to cover those, you are probably going to be giving money at subsidized interest rates or giving higher leveraging to a lot of other people who don't need it, and in those other cases you are simply giving away potential earnings from the Permanent Fund and for the propose of backing out capital which would otherwise be there. There may be some such cases at the margin, but I am very skeptical, first, about how many there are, and too the volume in terms of capital demand, and secondly, the ability of the Permanent Fund managers to discern those. I would ask why it is if these are trustworthy investments that can earn a market rate of return and the risks are not too great, why it is that some combination of investors and lending ---why the promoters who are putting it together haven't been able to package it attractively enough that somebody will

finance it in view of the enormous diversity of capital market. As I say, there is the availability of the insurance company money in large amounts for wealth secured investments of the availability of high return---high cost, high capital for the others and there is everything in between, I would just ask the question in this case, why is it that the Permanent Fund manager thinks it is so much better than the investment and there may be some---there may be some---but most of them are limited by resources or by the local interest structure or something of that nature.

GRUENING: I think Terry has a question here.

GARDINER: I have got a couple. What is the advisability of the Permanent Fund financing the El Paso gas line?

TUSSING: Well, it seems to me that the talk of the Permanent Fund financing is a political gimmick to get some support outside. There may be some resistance in Congress, the federal loan guarantees and if the State of Alaska will undertake those guarantees, maybe the Congress or somebody...

GARDINER: Are you saying that...

TUSSING: Well, I said in the past, I am skeptical about financing

viability of any of the gas pipeline projects in standing on their own two feet. That is, there is an enormous danger that the full cost of service of moving the gas from Alaska to the lower 48 is more than the gas is worth in the lower 48.

If there is a national decision that we ought to have a gas pipeline from---how do you cover the risk of that possibility? The financial market---that is, the bond houses and the insurance companies who are lending other people money are not going to be satisfied with a three-to-one probability the thing is financially viable, let alone only one-in-three possibility. So people are trying to come up with ways of providing that backstop. Now the pipeline companies essentially propose the consumers provide that backstopping simply by rolled in pricing, which means that the gas utilities use the fact that they have got a lot of gas that they hang on old long term contracts at regulated prices lower than the value of the gas to---they use that to subsidize the fact that Alaska gas will go into the market at more than it's worth, more than the consumers are willing to pay. You have rolled in pricing and you have the so-called all events tariff where the gas utilities, the buyers of the gas, will sign a contract saying we will pay for it, no matter how much it costs, and even if it is interrupted. We will pay the debt service on the pipeline. We will guarantee the debt service and will sock our consumers

for that debt service by adding it to the price of the other gas they get, you know, the gas that doesn't come from us.

Well, the notion of a state loan guarantee is just another attempt to find a gimmick to---or another backup for the fact that these things probably will not stand on their own feet economically. Now if there is a national decision to build a pipeline, there will be the national federal government finding some way of guaranteeing the financing. If consumer guarantees are not enough, there will be federal loan guarantees---and I really can't see Alaska coming up with a proposition that it wouldn't guarantee the bond of El Paso is going to have any effect on national decision. In fact, we may well be setting ourselves up to be sandbags on this if the commissioner of revenue comes back here and says that Secretary Blumenthal and Governor Brown and these people are going to support El Paso if we do it. And you rush it through the legislature in a special session before September 1st and the president makes his decision for Alcan on September 1st. Then they come back and say, well you lost your virginity, now we want you to do the same for the Alcan line.

The Treasury Department has been saying all along Alaska is the principal beneficiary of the pipeline. Alaska ought to be putting in the loan guarantees. Alaska ought to take the risks. And now they have got you. But what have you got? You've tied up a lot of Permanent Fund money at a public utility rate of return in a risky

investment that---I want to know on these loan guarantee programs the seniority of the state's guarantee; that is, if the pipeline can't pay, if it's revenue can't pay its debt obligation, who is it---is it Alaska that gets stuck first, or is it somebody else? If Alaska is going to be hit at the bottom of the list; that is, if somebody else is going to be hit first, it is not going to have much effect on the cost of financing the pipeline in its feasibility. If Alaska is going to be hit first, we have got a very expensive continued liability on the Permanent Fund.

GRUENING: I would like to just follow that up with---do you intend to follow that question up? I just wanted---before we got off---there has been a rumor around that there is some plan to suggest the Permanent Fund get into financing the gas pipeline. But assuming there are some business risks involved, does that---would that reflect on the reason there is a cause that the producers or the lessees of that gas had not come forward to finance a line?

TUSSING: I don't see any reason why a producer should want to finance it. They are not in the gas business, they are not financial intermediaries and the cost of capital---is maybe 20% or 25% after taxes. That is their opportunity

cost. Now why should they acquire a contingent liability against capital that can be invested that way but limits what they can do with it. The most they can get from money invested in the gas pipeline system is the public utility rate of return. The cost of the capital to them is much greater. ARCO cannot go out and borrow money as a public utility at the kind of rate the public utility can. If the income is not guaranteed the---proposing to set up companies to guarantee the gas pipeline their revenue, have consumer guarantees, etc. ARCO and Exxon didn't have any guarantee of revenue. And so, from their point of view, I would regard it as an outrageous suggestion. They are not going to---of the notion before the Federal Power Commission that they are going to be that enormous beneficiary from the sale of the gas. Who knows what the price is going to be and whether it is going to be a great boom. It is very minor compared with the oil revenue. If the president adopts the FCC's proposed pricing scheme, that is to price the gas at Chicago on the basis of the price of No. 2 fuel oil, to set the price at \$2.25 in Chicago and subtract the cost of transportation from it, the oil companies really don't have a great interest in building that pipeline, or in helping build the pipeline.

MEEKINS: Yeah, but on the other hand, if they are concerned about, you know, increasing the wellhead and the state's case would

be similar, there might be---really don't know---there might be a motivation of an extra benefit that guarantees a substantial portion of the debt would reduce not only the interest cost but the---maybe the debt equity ratio and that might possibly, I understand, decrease the---it would lower the cost of service and increase the wealth.

TUSSING: Well, it might be, but the people who are advocating this approach are those who were saying a few months ago that the cost of service would categorically have no effect on a wellhead price. As I say, when the figures came out showing that El Paso would result from the highest cost of service, they said, well the cost of transportation has no effect on the wellhead price. Now you have the same people turning around and saying, well now let's commit our Permanent Fund money to lower the cost of service to El Paso and we will more than get it back in increased wellhead price. For the same people to make both of them is not credible.

MEEKINS: I agree.

GRUENING: OK, if we can get off the reality gap...

MEEKINS: I have another question. You were talking about the various economic growth of...

...and so the question is, when you are looking at it, did you come across anything that you felt could create, whether Permanent Fund or not, could create economic growth in the state that would be real economic growth in the sense that it doesn't necessarily increase population in the state but increases real economic activity...

TUSSING: Real economic activity increases population. The mechanism is you create jobs and people come in to fill the jobs. There are people coming to Alaska and leaving all the time. It is not a question of attracting people. What happens is the higher the unemployment rate here the more of them leave after... It is essentially the same question. Now, what industries you get may affect---and others---you know, they may have a higher average wage, but of course that will affect if they have a relatively high component of skilled and technical personnel and professionals they will attract and---the people who are qualified for those. No, I don't see how over the long run you can have a large effect on the---you can't create any real economic growth in Alaska unless you know, economic activities---the rest of the United States.

Oh, economic growth is proceeding in Alaska at a very rapid rate. Alaska economy is growing faster than that of any other state in the country. We are increasing in the sense we still have the same unemployment rate, or greater, and, you know, the people

after the pipeline---know what our average incomes show, but basically, we have got a bigger pie, but it is the same pie. And so what I am saying---you know, that is why I say, can you create real economic growth in the sense that people might be better off here, but it is still the same amount of people.

Well, what is better off, to reduce the seasonality? I think part of the extreme seasonality in the economy comes from the weather in the first place, but it happens because people like it. They want to go outside in the winter and they don't like to work construction in the winter. And things like that. It may be you can stabilize by spending the money on salaried state employees to work the year round in nice comfortable office buildings. That is one way of doing it. And you get...

GRUENING: Are there any other questions?

RODEY: You mentioned the Permanent Fund and financing those projects that normal private institutions won't finance. How can you avoid what Mr. Daniels called---that is Permanent Fund getting all that bad debt portfolio. There seems to be a consistent danger we are going to face as we develop some scheme for investing money.

TUSSING: If you look at the history of development bank

type institutions, of special lending funds in Alaska, look at EBA, FBA, BIA loan programs, etc. If you instruct the managements to make loans only to those ventures that can't get money otherwise, you are asking them to invest in those who are, by definition, high risk ones, and you are going to have a lot of bad loans and portfolios. That is the way it is going to be. If that is alright---if this is the way of spreading the money around, well fine. When the money first started coming in, the government purchased all the land in a city and then sold it back to the people at lower prices. That is the way of getting money into the---it was an urban development program. If you want to get the money into people's hands, that is one way of doing it. You get a lot of---projects that can't get financing when you got too much money. If you are going to give away, well there are all sorts of ways to do that.

No, I don't think you are going to avoid that. I would like to see a real audit of loan quality in the existing state revolving loan program. And what the real subsidy is. When you take into account---when you classify these loans the way the banks are suppose to classify their loans and write off the ones that are really no good and write down the ones that are only partially collectable and then add the administrative costs, and say what have we got from the agricultural---for the small business loan. It frightens me to set up a multi-billion dollar---without taking a

hard look at what went wrong with the other loan programs. And taking a hard look at all these EDA projects, the EDA financing of industrial parks, the BIA industrial park projects and infra-structure projects that we were supposed to encourage in rural areas.

GRUENING: Hugh, did you have any questions?

MALONE: Thank you, Mr. Chairman. In the report that you prepared for the committee, in discussing the accumulation of surplus balances in the state general fund, it states that one way to make use of general fund balance would be to reduce the personal income tax. It says that the analysis showed a significant reduction in the general fund balance of a highly stimulative effect by the increase of disposable income increased demand, but it says that if additional revenues would be generated it would not be sufficient to maintain constant per capita at government expenditures. General fund balance would be depleted more rapidly than initial calculations indicated. It concludes by saying if the Permanent Fund is interpreted as a fund to benefit Alaskans the expansion generated by the income tax---I believe that would be the reduction of the income tax---could be the worst possible use of the general fund money. The question I have is---the next page at the

bottom there, discussed an idea that has been brought up from time to time, the transfer of payment directly to individuals. That would provide an economic increase in private---my question is, would the same considerations apply to that transfer distribution of monies to some form of Alaska, Inc., would apply to an income tax cuts. That is to say that you would generate additional revenues but you generate government costs that exceeded those additional revenues in that you might have a case where the expansion generated could be the worst possible use of general fund money and would you care to comment on that?

TUSSING: OK, as I said before, we can model the different impact tax deductions of Alaska, Inc., welfare payments, increases in state operating expenses, and there would be significant differences because they will be distributed differently throughout the population by income level and by region and some would have larger impact outside the state than others and it would be worthwhile to compare them. What we are saying here is all of these things do have impact and those that feed cash directly into the economy might well have more impact---or likely to have a greater effect on the management of state services than on the secondary ability to adapt to the time at which you couldn't maintain the services of the population you created. You may be asking---you said one of these uses may be worse, probably should say among the worst, from the point of view of stabilizing the growth. It could apply to the others as well.

GRUENING: Mr. Malone.

MALONE: Thank you, Mr. Chairman. Generally, one of the ideas was discussed when the various legislation creating Permanent Fund was under consideration. One of the ideas was that there would be some sort of buffer against the decline in state revenues with the dropoff in production of mineral resources. Does that make any sense to save money for a rainy day, or is that only a question of considerations. Can you put that into perspective?

TUSSING: Alright, you can model the situation. Assume that the demand for state services is going to remain constant in per capita dollars and you can add to say---increase 2% a year and you are aiming for a population growth rate of 2% or 5% a year, something like that. Then you can put it into your model and can see how much revenue is necessary. Then you can project how much your regular taxes would maintain the same structure of personal taxes in the state, the nuisance taxes, the gasoline tax, etc., how much that rate---and how much you are going to need from supplemental sources which would be either current mineral leasing revenues or Permanent Fund income. For every rate of contribution in the Permanent Fund you can show where the lines are going to cross, the point

at which the growth of the amount---the current revenue plus Permanent Fund income wouldn't be enough to sustain that level of service. Now for some amount of Permanent Fund contributions you may find that that point never comes. That the Permanent Fund may---and that you will always be able to maintain---well, your rate of increase in state services may be growing at 5% a year and the Permanent Fund's spendable income may be at 7% or something like that. It is entirely conceivable. But you would get that result only with very large early contributions, trying to minimize the budget growth---trying to keep growth in the next decade to a very low level.

If you spend 75% of the oil revenues every year, you are going to get to the point where the state's economy and the state government can no longer sustain the needs created and get to that point much faster. The model is very useful for that. The model did some preliminary projections on the basis of 25% contribution on the basis of various assumptions as to what happens to the general fund, but you can put together whatever assumptions you want. You can test various formulas for Permanent Fund contributions and come out with a theoretical golden path, where each year you assure that at least for 20 years, maybe for 30 or 50 years, there is always enough surplus revenue in the Permanent Fund to meet the requirements of the growth. But that can be accomplished only on the basis of an assumption as to what your goal is for population growth or growth of state gross income.

GRUENING: Are there any further questions of Dr. Tussing?

RADER: Doctor, in regard to the trans-Alaska gas pipeline, you are saying that if it is a viable economic project that money would be available to us at a public utility rate through normal public utility sources throughout the United States. It is possible that Alaska, in order to get in its royalty gas to tidewaters the trans-Alaska line would have an interest rate---would be justified in financing a line which would not be financable at a normal utility rate in order to have that option of 25 years of recall of our gas?

I have no idea of what the value of that option is. But I am only assuming, first of all, that you could establish going in, that the ability of Alaska to tax and the ability of Alaska to---the desirability of keeping that option of tidewater availability of oil and gas. Is there room for argument that we could participate in that situation in a project that a New York investor would not be interested in?

TUSSING: It depends how much it is worth to you to get to tidewater.

RADER: How do you think of that 25 year option with the gas pipeline? What do you think?

TUSSING: I don't think it is worth very much, myself. I think that we are going to have a lot of oil and gas explorations in the Gulf of Alaska or Cook Inlet, and there are presently uncommitted gas resources in Southern Alaska. If the state builds a spur from an Alaskan highway pipeline to Cook Inlet, for example, it is much more likely that the gas would go north on that spur than south. It is conceivable the cost situations may change sufficiently to make the Inlet area or Prince William Sound an inviting area for industrial development, based on the gas. No study has yet indicated that that is in the offing. There is no evidence for it and there is no serious argument anywhere that there is a petrochemical or major gas using industry waiting to be established because of the availability of gas at tidewater in southern Alaska. Any sacrifice the state makes now, either in gas revenue or in Permanent Fund earnings, speculating on what is going to happen five years from now, is that thing that happens 25 years from now has got to be awfully big at compound interest to justify the sacrifices made now.

The gas on the North Slope probably should not come to tidewater in southern Alaska. There is very likely to be a big surplus of gas in southcentral Alaska, the Gulf of Alaska, lower Cook Inlet, out the chain, etc. and it is going to be extremely difficult to market.

The trans-Alaskan gas pipeline is an idea, it is a vision, it's very little else in terms of the prospect for further development. It is a big payroll boom and that's why it is so attractive. Do we want another big payroll, big construction boom for the difference between the El Paso and Alcan in terms of the payroll. How much are we to pay?

How much is it worth to pay to get gas directly to Glennallen. Wouldn't it be a lot cheaper to give them the money to haul propane in for free, or something like that? I know how much it is worth but a lot of this discussion takes it completely out of economic reality. It has become a religious thing and I don't know how much it takes.

GRUENING: Now that we are into religion, can we get back to Permanent Fund? Do you have any other questions?

RADER: I have a couple of others, if I could, Mr. Chairman. During the discussion of Permanent Fund, it has been brought up from time to time that Permanent Funds can be used as a vehicle. You touched on this during your discussion and I apologize for not having read your paper. I assure you I will. It has been suggested that the Permanent Fund be used as a vehicle to handle the transition of Alaska non-renewable resources to renewable resources and I assume inherent to that would be that we would take the Permanent Fund and use it to

subsidize what would apparently be non-economic agricultural products or fishing ventures perhaps on the Continental Shelf and the 200 mile limit or something else, I don't know. To use---I don't know really---I am not one of those who made that argument. It was made that this fund could be used as a vehicle to get us from a non-recurring resource revenue to a recurring resource revenue. Do you really see that?

TUSSING: How long are we going to subsidize them and compare the cost of continuing subsidy to just how much income you could bring in by investing that money at the highest rate of return and using it to sustain normal state activity. I am no more sure than you are what the people who talk about this mean. I would like to see what kind of venture and what kind of subsidy is involved. Suppose the Permanent Fund contributes free half the money to establish a processing plant for bottom fish. Over long term the operating cost---or the revenue to cover the operating cost and the depreciation---are you going to just keep feeding in money from somewhere to keep that project going if it's not otherwise viable, and if you have to do that what do you want it for? Does this make the state's economy any less precarious than it was based mostly on oil? I don't quite understand the argument myself.

RADER: I don't either. I thought maybe...

TUSSING: Let me say, I have faith in the ability of the fish processing industry and of Alaska-based fisheries to grow and make enormous investment in the next two or three years or in the next five or ten years, and there is virtually nothing that can stop this aside from state and federal regulatory policy, but the pace and shape of that development is not going to be determined by the cost or availability of venture capital. That will be there if the projects can show that they are worthwhile. There may even be too much because there are a lot of Japanese and Korean companies who are writing down and writing off their previous investments in processing plants back home and who will want to get involved at almost a non-economic basis in Alaska industries and may want to get a foothold now and will invest at less than, you know, it thinks a prudent investor might hesitate at. That is true, we have another source of capital in the native corporations who have been doing that, too.

RADER: A different line of inquiry. Have you given any thought as to the governmental structure that you would recommend? You and I are both aware to some degree at least of our past, in the way we handled the past lending activities and whether they have been economic. I am like you. I have some question about the management ability of some of our agencies. Have you given any thought as to how the fund should be structured

for an executive and legislative oversight but with a view towards insulation from legislative pressures and public pressures, etc.?

TUSSING: Not enough to spend time on my prejudices.

RADER: That concludes my question.

GRUENING: Thank you, Senator Rader. Are there any further questions of the committee? Representative Meekins.

MEEKINS: Dr. Tussing, you were talking about providing some loans for small and medium enterprises in the rural area and that private institutions don't provide the capital needs there. Is it your view that in order to do that that we would have to set up regional development banks or some sort of development banks and that that wouldn't be possible or preferable to work through the financial institutions?

TUSSING: Well, I think most investments in Alaska should be done with or through or in partnership with existing financial institutions. I haven't given a great deal of thought to how this would be structured, but I would see the regional development banks being formed in some sort of cooperation between the Permanent Fund and existing financial institutions and the regional corporations. For example, they might joint venture, which would be utilizing the services and get money from the existing financial institutions. Might guarantee them and sell bonds---have a correspondent relationship---there is just many ways of doing it and I simply haven't devoted a lot of thought to its structure. It will be a

difficult problem. It is not an easy thing to work out.

GRUENING: On that line, Mr. Belden Daniels, who is our next witness, will give a little more thought to that. Are there any further questions from the committee? I want to thank you very much for a very thought provoking presentation. Thank you. I would like to call our next witness because I would like to wrap most of this up today. I think he is in the audience. Mr. Belden Daniels from Harvard University has submitted a very, I think very, comprehensive report and I would like to hear your initial comments, Belden. You have a resume here that looks pretty impressive. I know you are pretty modest and maybe you could summarize it for us.

DANIELS: Thank you, Clark. I am a lawyer, a former international banker. I teach development finance at Harvard and I am actively involved in putting development banks together in a number of places in Asia, Europe and in the United States. That provides me with a very good point of departure because I suppose that in the last 18 years of working in development banking and in the last 13 years or so in working specifically with regional and community economic development problems that I have read several hundred development banking acts and draft bills and I participated in drafting and having passed and funded a dozen or so myself.

I begin with a very strong feeling of genuine excitement about the quality of work which the State Investment Advisory Committee has already invested in this issue and which the consultants for the state, Price Waterhouse, White Weld and Bob Richards here in Alaska, have contributed. It is much easier for someone in my position to offer refinements and additions and clarifications on a draft which I think is essentially very sound. I am speaking specifically about House Bill 298 and I think somewhat improved version of that House Bill 300, which are the two that I have looked at in some detail.

I have about eight points, if I could kind of quickly go down them and make them fast, and then open it up to your discussion as much as possible. I guess I want to say one or two more preliminary things. I confess to being somewhat overwhelmed by both the potential size and scope of the Permanent Fund and also by the size and nature of the Alaskan economy in relation to your population base and I feel very cautious about wanting to be too quick in making judgments about the relevance of my own experience in many other parts of the world because, as Arlon Tussing has point out, you are faced with an absolutely unique situation. There are really no comparable situations in my experience in either Asia or Europe or in the United States which combine the particular concentration of extraordinary resources, capital and natural, in such a vast area with such a limited population. So I would like

to reserve the ability to be somewhat tentative in---as an outsider in offering too much advice and council about how you should proceed here.

I do think that there are at least three major areas in which that experience is relevant to you and useful to you; that is, the world wide experience is relevant and useful to you, without presuming what your goals are. And they get, Senator Rader, to some of your questions.

One, I think there is a way that you can look at your problems or your opportunities---a great deal of learning with regard to structure that is worth your careful consideration and I am mindful that having read all of the minutes of the Advisory Committee and the reports of your previous consultants, that through Price Waterhouse and White Weld you have had a rather thorough consideration of lots of that international development banking experience.

In the third area that I would offer some comment on, related to Representative Meekins' question, is the specific applicability of regional and community development experience to some of the structural problems that you are facing. The title of my paper I believe in very strongly and that is that I would urge caution on all of you in several levels. One I think, it is very important for all of us to recognize the very real limit on the capacity of any state government to influence profoundly the course and direction of economic

development within its boundaries and this is one of the areas which Arlon and I certainly share---one of the many areas in which we share a common kind of sense of caution.

Secondly, I think that all of us need to be extremely cautious in anticipating too much impact on the economic development of the state from the Permanent Fund. And, in my eight points that I would like to make, Clark, I think I can bring out the specifics of that in, I hope, at least quick conference. The punchline, of course, in suggesting this caution with regard to the role of the state in economic development and the role of Permanent Fund in economic development is that you have the opportunity of enormous scale, either to waste these tremendous capital resources that you have or to husband them very carefully, both in terms of the maintaining the value of the capital itself and invest in ways which will at least marginally contribute to the overall economic development of the state.

Point One: No development bank, no financial intermediary, can create any economic activity that isn't there in the first place. Development banks and any financial intermediary operate only on the supply side of the economic equation. If there is real economic activity for which there is not available capital, then the intervention of the Permanent Fund can affect that positively and can add economic value to the state. But if there isn't a market, if there aren't sufficient---if the costs of production are too high, the intervention of the Permanent Fund is not going to

affect that at all. Specifically, it is my understanding that at the present time petrochemical industries is not viable on a world-wide basis. The cost of production of petrochemicals in Alaska are too high to be competitive on the world-wide market. Now that may change and then maybe things that will lower those real economic costs. But there is nothing that the Permanent Fund can do to intervene in order to lower the costs sufficiently to compete in the world-wide market. Now that is very, very important, I think, in terms of lots of thinking about the Permanent Fund.

That means, for instance, in terms of Point Number Two, that subsidies are not the issue. We have a very interesting case in point in Massachusetts right now where we have very rapidly growing, high technology companies, between \$50 and \$100 million in sales, that are between 20% and 40% profitable and growing, and growing at the rate of 20% to 40% a year, which have a great deal of difficulty accepting capital in either equity or debt form for their needs. But these companies could be financed on Master Charge, and I think that that is a critical idea. In fact, there may be circumstances where you want to increase the price of capital in the Permanent Fund because it discourages non-economic activity and you want to discourage all of the dogs that will be attracted to the Permanent Fund if there is subsidy available. The issue is the availability of capital.

Point Number Three. The general fund is far more important--- and I am saying this in emphasis to Arlon's point---the general fund is far more important in terms of its impact on the overall economic development of the state than the Permanent Fund. I devote time to this in my paper, and I don't want to repeat any of that now, but the issue of expenditure policy, tax policy and regulatory policy will more profoundly affect economic development than the Permanent Fund. But the key punchline in Point Number Three is that you have got to operate your expenditure policy, your tax policy, your regulatory policy, and the use of the capital resources of the Permanent Fund as part of a coherent economic development effort in the state. If you don't the opportunities for sound investment on the part of the Permanent Fund will be less, the jeopardy of Permanent Fund investments in the state will be greater, and the likelihood of your general expenditure policy through the general fund and your investment policy operating against each other, I think, are very great. I suggest that there is extraordinary opportunity right now for the State of Alaska to think about a coherent overall economic development approach that recognizes the limits of all of its policies, individually and collectively, to affect the economic development of the state, but still is operated in combination, will have a much greater impact than operated separately. Just a simple illustration.. A couple of the issues that I have had the pleasure of talking about the last couple of days is from some of the native corporation areas

and with---in specific projects, one in the Aleutians, one in the Kotzebue area. You can't begin to talk about a significant fisheries project that is going to be sound unless you get the concrete in there for the pier first. And so, obviously, the infrastructure decision made through general fund investments has got to be made side-by-side with the Permanent Fund.

Point Number Four. The private market needs to be used first in terms of solving both market and capital issues within the state, and all of your planning and development in terms of any financial intermediary specifically that might be set up within it have got to be planned in collaboration with the private market and implemented in collaboration with them. This is essential if you are to husband your resources properly, both in terms of lowering the risk in which state funds are invested, and also lowering the cost. And I would suggest that ---and I will cite some specifics before we finish---that there are lots of opportunities for that kind of collaboration which are mutually attractive to the market sites, to the population of Alaska, and to the state government. And therefore, specifically, in the case of regional development banking subsidiaries of the Permanent Fund to deal with some of the problems of capital availability in the regions, I strongly support Arlon's position that they should be a collaboration between the native corporations, between the private market

place, and between the Permanent Fund. I will give a few specific cases in a moment. Without knowing in great detail the operations of the present revolving loan funds, what little I know confirms the experience in many other states and many other places that those funds which are in collaboration with the marketplace have a portfolio which is not only financially of better quality but in terms of the economic impact has a greater impact within the state.

Point Number Five. What are the potential areas for use of the Permanent Fund and how might the Permanent Fund be organized in order to deal with them? I think there are four that deserve very careful consideration by you and I will try to highlight those points which are either extending on a point that Arlon has made or in addition to them. First of all, in terms of large scale economic activity in the state, the very efficiency and consolidation which is taking place in money and capital markets on a worldwide basis means that there is capital available for those large enterprises and I think you should ask very carefully what the market imperfection is, either in terms of the private market or financial market, which would lead you to be asked to undertake either an equity investment in or a debt loan to or specifically a debt guarantee of a large activity which you should presume can be handled by the marketplace. Now, I would like to introduce another issue with regard to large scale enterprise. At the present

time large scale enterprises in Alaska are primarily being developed by resources from outside Alaska and you may want to ask yourself the question whether or not there is a reason to intervene in order not to change the underlying economic viability of the project, which is presumed to be sound, but to change the ownership, both in terms of who is bearing the risk and who is bearing the reward for that particular large scale undertaking. I am going to suggest a number of points a couple of models around the world which your---which the previous consultants of the state were not asked to look at because they were asked to look primarily at international development banking experience. There is very close to you a model that deserves your careful consideration in terms of this issue of shifting ownership for very large scale enterprises and it is the Canada Development Corporation.

Canada Development Corporation was created in 1971, I might note after a 10 year debate. I don't mean to suggest that this process may go on for a while, but I am fascinated that it did take 10 years to do it in Canada. It was created with an initial public investment by the federal government of Canada of a quarter of a billion dollars. Three years later it was able to have the largest public offering in the history of Canada, \$150 million public offering, primarily by small individuals in Canada, primarily because of the soundness of the investments which it had made. It now has total assets in

less than a 6 year period of over a billion dollars and is producing a significant return on investments and has repurchased a number of rather large corporations which were originally under foreign ownership, primarily American ownership. Now, it is a mixed success, depending on the standards that one uses. But it is one alternative form of use of the Permanent Fund in which you would be operating on a market basis but with a somewhat different public purpose.

Second, in terms of uses. There are on a world-wide basis--- there are problems of the availability of intermediate long term capital for small and medium size businesses generally and particularly in remote areas. Now it is very important to note that this is not an Alaskan problem. This is a world-wide problem. And the question then that you have to ask yourself is whether or not you have an economy that is in some way particularly dependent on those kinds of enterprises for economic growth and therefore there is warranted on the part of you and the Permanent Fund some intervention. In Massachusetts, for instance, we are a particularly dependent economy on small and medium size businesses. We are also particularly dependent on the creation of new high value added and high technology companies, which, as I mentioned earlier, have difficulty of access to the capital market. Therefore, we have created a series of new development banks in Massachusetts, two wholly privately owned and several that have a mixed and private capital in order to deal

with that problem. Very critical point. That activity must be undertaken, planned and implemented in collaboration with your existing commercial banks and thrift institutions both federally and state chartered in order to create a mode of investment that is sound, from a risk standpoint, spreads the cost and builds those institutions more deeply into the economy on a sounder basis.

There are a number of models that warrant your careful consideration. One, again, is the Connecticut Development Authority, which in my judgment is the soundest of the intermediate and longer term joint ventures between public capital and private capital. Every European nation, every Canadian province, almost every state in the lower 48, has this kind of intermediary. This one just happens to be the best of them. OK. Third. There is a particular problem that deserves your attention in terms of support for regional and small community economic development and I would say on the basis of my experience in Appalachia, my experience in New England, and my experience with regional economic development efforts in Europe, that without knowing precisely the nature of your own economic situation in the---outside of the major cities, that this is a very serious problem, as Arlon has already noted, and that---but I think the extraordinary thing is you have a resource that does not exist in any other state, and that is the existence of the native corporations. -

What I think is worth your serious consideration is the regionalization of parts of the Permanent Fund to deal on a joint venture basis with the native corporations. And I would like to note that this is the one case in which I think, underlined many, many times, that there may well be a sound economic and financial reason for the Permanent Fund to take a significantly lower rate of return, and that is this: The native corporations have a very high need to produce at the highest rate of return at the lowest risk on a worldwide basis as they can in order to husband their own resources and protect their stockholders. They are therefore naturally looking to investment opportunities in the Anchorage area, Fairbanks area and outside the state, as they should, I think---because of their opportunity costs. I think that they are essential to the sound investment in their region. It is not sound for them to have all of their economic eggs in their local basket, or even in the basket of Alaska as a whole, but that development will only take place if in fact the Permanent Fund is willing to compensate for their opportunity costs. This will require much more careful consideration and analysis, but I think in principle the idea is sound. I just, in fact, had the opportunity to sit down and talk in more specific terms about a specific project in Kotzebue where I think this is true. The project will be financed but it may well not be financed as soundly as is good for the project in order to have the shopping mall to get started in Kotzebue.

Once again, there are very good models for your consideration, some new and some old, in terms of this kind of collaboration. One set that deserves your further attention is the British Columbia Central Credit Union, which has had an enormous impact on regional and small scale community development in an economy which I would presume is not radically different from the Alaskan economy in terms of its overall construction, political dimension and demographic dimension and underlying economy. Related to that is an extraordinary institution in Germany called the DG Bank, known as the largest bank in the world, starting from small scale community development, now investment opportunities on a worldwide basis. A new institution in Massachusetts not yet operational but I think conceptionally very sound, the Community Development Finance Corporation is an institution that I think deserves consideration by you in the planning. I might note a small kind of example of refinement I would suggest for consideration in HB300, and I know this---I think it is a mistake in the community development of units of the Permanent Fund to limit the form of investment to only debt and debt guarantee. I think equity is essential for community and regional economic development and the Permanent Fund should have the opportunity of making those kinds of equity investments on a joint venture basis in a minority position with the native corporations in the kind of case that Leo and I just had an opportunity to talk about.

Fourth and finally, in terms of uses of infrastructure investments. Be wary, be cautious. There is an enormous body of experience on a worldwide basis of public investments made in anticipation of private market investments following and those public investments are lying in the fields. Now, where there is the opportunity for a market investment like a fishery, like a fish processing plant and in the Aleutians, but an infrastructure investment needs to be made first, then we have---in order to realize the private investment---then there is a very great need for collaboration between general fund infrastructure investments and Permanent Fund income producing investments.

Point Six. Without having access to either private market projections for the economy or the university's projection, or the government's projection, under no circumstances in my judgment will there be the capabilities for absorbing substantial amounts of Permanent Fund resources in any of the above four categories over the foreseeable future. And it is interesting that I arrived at the need to make private market investments, not from the standpoint of security, not from the standpoint of evening out the long term ups and downs in the cycle of state government revenue, but from the standpoint of development banking. And I very much support the language of 298 and 300, which say no less than 40% in terms of investment grade security and---but no more than 30% in community development, or no more than 30% in productive private enterprise

Now, Point Seven I have already covered and that is good. There are other models in addition to the ones which you asked the original consultants to look at that are worthy of your consideration. There is no need for any kind of activity that you might undertake with the Permanent Fund to reinvent the wheel. Somebody has been there first and made plenty of mistakes and finally of all there were times creative models ---models are available for your use and should be used.

Eight. Looking at the structure of the development bank and is proposed in 298 and 300. A general proposition first, very important. Some members of the committee, I think, will be a little sick of hearing me stress this. There is one great strength in a development bank and one great weakness. The great art in design is to maximize that strength and minimize the weakness. The strength is that it is the most efficient mechanism for making a public capital investment that is sensitive to market conditions in order to contribute to economic development. It beats setting up a bureaucratically administered fund in terms of both equity and efficiency by a very long distance, and it beats tax expenditures and tax incentive by a very long distance, which are the two other principal forms of public investment. But the price that is paid is the price of accountability to a public purpose, both to the executive and to the legislature. There is a history of development banks