ALASKA LEGISLATURE COMMITTEE FILES 1993-1994 8672
8470 SENATE STATE AFFAIRS

crime, had acquired their last crime handgun at a gun store. Of those, about one quarter had stolen the gun from a store; a large number of the rest, Wright and Rossi suggested, had probably procured the gun through a legal surrogate buyer, such as a girlfriend with a clean record. For the few remaining felons who actually did buy their own guns, the purchase might have been lawful because the purchaser as yet had no felony record.

The survey further indicated that 56 percent of the prisoners said that a criminal would not attack a potential victim who was known to be armed. Seventy-four percent agreed with the statement that "One reason burglars avoid houses where people are at home is that they fear being shot during the crime." Thirty-nine percent of the felons had personally decided not to commit a crime because they thought the victim might have a gun, and 8 percent said the experience had occurred "many times." Criminals in states with higher civilian gun-ownership rates worried the most about armed victims.

Since criminals can never be entirely sure which burglary targets may or may not contain a homeowner with a gun, or which potential robbery or rape victims may be carrying a concealed firearm, the ownership of firearms by half of American households provides a general deterrent to crime that benefits the entire population.

How Guns Prevent Crime

Consistent with the reports of criminals, ordinary citizens also report that gun ownership plays an important role in preventing crime. Professor Kleck estimates that handguns are used approximately 645,000 times for defense against an attacker every year in the United States.

The figure, ironically, is based on data from a survey conducted on behalf of the pro-control National Alliance Against Violence (NAAV). NAAV hired Peter Hart, a leading Democratic pollster, to survey Americans on guns, asking, among other things: "Within the past five years, have you yourself or another member of your household used a handgun, even if it was not fired, for self-protection or protection of property at home, work, or elsewhere, excluding military service or police work?" Six percent answered "yes." Follow-up questions revealed that 3 percent of the respondents had used the handgun against a person, 2 percent against an animal, and 1 percent against both. That 4 percent said "yes" to defensive gun use against persons meant that about 18 percent of households where a handgun was owned for protection had actually used the handgun for protection.

Carter's researchers found no persuasive evidence that any of America's gun-control laws had reduced criminal violence.

Kleck's analysis started with the 4-percent "yes" from Hart's data. Kleck made the conservative assumption that each "yes" related to only one gun usage in the last five years—that no household used a firearm for self-defense two or more times in the five years. Thus, 3,224,880 households reported self-defense usage. Kleck then divided by five (since the question had asked about usage in the last five years) to arrive at an estimate for the annual number of uses of a handgun for self-defense: 644,976—or roughly once every 48 seconds.

Since Kleck's estimate is based on responses to a pollster it should be emphasized that the 645,000 figure is necessarily imprecise. The original question posed by Peter Hart could have elicited a "yes" answer from an insecure gun owner who had perceived a criminal threat that did not in fact exist. Kleck partly controlled self-defense inflation from false "yes" answers by assuming that no "yes" answer related to more than one defensive use. In addition, the 645,000 estimate applies only to handguns; the original question did not ask about defensive use of rifles or shotguns.

In 1990, Professor Gary Mauser, of Canada's Simon Fraser University, asked Americans about use of a handgun or a long gun for self-defense; the responses suggested approximately 691,000 annual defensive uses of guns of all types. Accordingly, we may conclude that guns are used defensively at least half a million times a year.

Of course, the fact that a gun is used for defense does not mean that a shot is fired, or an attacker wounded or killed. About 95 percent of self-defense usage, says Kleck, involves merely the brandishing of a weapon to deter a perceived attack.

While the majority of defensive handgun use is simply brandishing a weapon to frighten away an attacker, Kleck suggests that 1,700 to 3,100 homicides a year are actually justifiable homicides committed by citizens using a firearm to defend themselves or another person against violent attack.

One Bullet at a Time

While most Americans believe they have a right to own a gun, and believe that guns can be protective, even many gun owners are baffled at the gun lobby's apparent intransigence in its refusal to accept a ban on so-called assault weapons or a waiting period on gun purchases.

The assault-weapon issue, however, turns out to involve much less than meets the eye. First of all, it should be emphasized that most people who own semi-automatics support strong controls on actual machine guns. Ever since the National Firearms Act of 1934, acquisition of real machine guns—guns that continue to fire bullets repeatedly as long as the trigger is held down—has required a difficult-to-obtain federal license. The NRA did not oppose the restrictive machine gun law when it was enacted, and has never indicated any desire to repeal the law.

While machine guns do have a unique capacity for rapid fire, what we know as assault weapons do not. Although most of the public believes that assault weapons are machine guns, the guns in question simply look like military weapons. Appearances notwithstand-

UPI/Bettmann

The waiting period promoted by Sarah Brady would not have stopped John Hinckley from shooting her husband Jim.

ing, the guns fire just as every other common American gun does: squeezing the trigger fires one, and only one, bullet. According to Martin Fackler, former director of the Letterman Army Institute of Research, assault weapons are actually less lethal than many firearms commonly associated with hunting, such as an old-fashioned 12-gauge Winchester shotgun. The Bureau of Alcohol, Tobacco, and Firearms states that no guns available for sale to the public can be easily converted to fire automatically.

Hard to Convert

The fact that semiautomatic assault weapons differ from other guns only cosmetically is one reason why legislative bodies have had so much trouble defining them. Since the guns do not fire faster than other guns, legislative definitions sometimes focus on extraneous features, such as the presence of a bayonet lug—as if we were suffering from a rash of criminals bayonetting people.

Other definitions are merely a list of particular guns with a military appearance. Among the guns targeted by assault-weapons legislation are the M1 Carbine; the AKS Rifle; the Uzi Pistol and Carbine, the Colt AR-15 H-Bar Rifle; the Springfield Armory 4800 Rifle; the M10 Pistol and Carbine; and the AK-56 rifle. Yet some of these guns are in no way distinguishable from many other guns not on the lists, such as the popular hunting rifles made by Winchester, Remington, and Ruger. As former Attorney General Richard Thornburgh noted, the main characteristic of an assault weapon seems to be that it has a black plastic stock rather than a brown wooden stock.

In practical terms, the legislative definition of assault weapon amounts to "the largest number of guns that a given legislature can be convinced to ban." The New Jersey assault-weapon prohibition even outlaws BB guns.

While assault weapons have been claimed to be the "weapon of choice" of criminals, such guns constitute a very small number of the crime guns seized by the police. The Florida Assault Weapons Commission's 1990 report found that assault weapons were used in 17 of 7,500 gun crimes in the years 1986–1989. The Washington, D.C. director of the police firearms section stated in early 1989 that not one of the more than 3,000 weapons the Washington police confiscated in 1988 was a semiautomatic assault rifle.

While some gun-prohibition advocates have claimed that a record number of police are being murdered by assault weapons, police-officer deaths in the line of duty are at their lowest level since 1968. The percentage of police homicides perpetrated with assault weapons is about 4 percent, a figure that has stayed constant over the last decade. The FBI's Uniform Crime Reporting Program, which collects extensive data on all murders of police officers, reports no instance of a drug dealer ever killing a police officer with an Uzi.

That assault weapons should appear so rarely as crime guns seized makes sense. Street criminals need concealable weapons, and a Colt or a Kalashnikov rifle is pretty difficult to stick in a pocket. Indeed, rifles of all types constitute a tiny percentage of crime guns. According to the Washington, D.C., Metropolitan Police Department, rifles are used in less than one-tenth of 1 percent of armed robberies in the District. Nationally, only about 4 percent of the weapons used in homicides are rifles.

Occasionally, so-called assault weapons are used in gruesome mass murders. In Stockton, California in January 1991, Patrick Purdy used a Kalashnikov-type semiautomatic rifle to fire 105 shots in about four minutes at a schoolyard full of Cambodian immigrant children. Thirty-five people were wounded, six of whom died. Purdy's rate of fire could have been duplicated by

UPI/Bettmann

Children praying for their slain schoolmates in Stockton, California. The media's innaccurate description of the murderer's gun enabled the California authorities to escape censure for having freed this dangerous man.

anyone with an old-fashioned bolt-action rifle or simple revolver, and autopsies of the victims showed that the wounds were approximately equal in severity to wounds associated with a medium-sized handgun, which explains why 29 of the 35 people who were shot survived.

Thus, Purdy could have committed the same crime using many other types of guns. But the national media incorrectly told the American public that Purdy had used an automatic AK-47 rifle, and that such guns could be bought over the counter.

Lost in the media frenzy over Purdy's gun was Purdy himself, who committed suicide with a pistol at the end of his spree. Purdy perpetrated his crime after he had told a state mental-health worker that he though about committing a mass murder with a gun or a bomb, and even though a parole report called him "a danger to himself and others."

Purdy had a lengthy history of crime and arrests, including a robbery in which a 55-year-old woman was seriously injured, receipt of stolen property, criminal conspiracy, possession of illegal weapons, and assault of a police officer, all reduced to misdemeanor charges. His crime career began when he was 14 years old and continued unabated for the next decade, until he killed himself at Stockton. Not one of Purdy's two-dozen encounters with the law ever led to more than a few weeks in prison. The media's hysterical focus on Purdy's gun enabled California's decrepit criminal-justice bureaucracy to escape public censure for allowing Purdy to roam the streets, free to commit his final, horrible crime.

"Cooling Off"

The waiting period, like the assault-weapon ban, becomes considerably less attractive when examined carefully. While the waiting-period initiative is often called the "Brady Bill," it would not have prevented John Hinckley from shooting Ronald Reagan and Jim Brady. When Hinckley bought two handguns in October 1980, he had no felony record, and no public record of mental illness. The simple police and mental health records check proposed by the Brady Bill would not have turned up anything on him. And since Hinckley bought the guns more than five months in advance, a one-week wait would not have made any difference to him.

Indeed, a "cooling-off" period for handgun purchases requires a number of unlikely assumptions in order to work. First, the potential murderer—denied a handgun immediately—must then decide not to buy a rifle or a shotgun, which the Brady Bill would allow him to do. Then, he must not know how to buy a handgun on the black market, or how to obtain one from friends, relatives, or acquaintances. In addition, the type of murder he intends must not be one for which readily available alternative weapons, such as knives, automobiles, or bare hands will work. Finally, the person who was literally ready to commit a murder on day one of the waiting period must calm down by day seven, and stay calm from that day forward.

This scenario, while implausible, is not impossible; it is at least theoretically imaginable that a waiting period could "save at least one life." But a waiting period can cost lives, too.

"I'll Be Dead by Then"

Even a short waiting period will inevitably prevent people from protecting themselves against criminal attack during the wait. When Los Angeles citizens went to gun stores to buy firearms to protect life and property during the recent riots, they were told to come back 15 days later, to comply with California's waiting period on all guns.

After Hurricane Andrew, Florida's looters did considerably less damage than their California counterparts, in part because Florida has only a three-day handgun waiting period, and no wait at all on long guns.

Nor are waiting period victimizations confined only to periods of civil disorder. In September 1990, a mail carrier named Catherine Latta of Charlotte, North Carolina, went to the police to obtain permission to buy a handgun. Her ex-boyfriend had previously robbed her, assaulted her several times, and raped her. The clerk at the sheriff's office informed her the gun permit would take two to four weeks. "I told her I'd be dead by then," Latta later recalled. That afternoon, she bought an illegal $20 semiautomatic pistol on the street. Five hours later, her ex-boyfriend attacked her outside her house, and she shot him dead. The county prosecutor decided not

to prosecute Latta for either the self-defense homicide or the illegal gun.

A Wisconsin woman, Bonnie Elmasri, was not so lucky. On March 5, 1991 she called a firearms instructor, worried that her husband—who was subject to a restraining order to stay away from her—had been threatening her and her children. When she asked the instructor about getting a handgun, the instructor explained that Wisconsin has a 48-hour waiting period. Elmasri and her two children were murdered by her husband 24 hours later.

Waiting periods that appear reasonable in a legislative chamber may become unreasonable through administrative abuse. Although New Jersey law requires that the authorities act on gun license applications within 30 days, delays of 90 days are routine; some applications are delayed for years for no valid reason. In Maryland, where an appeals process exists, the police are overruled on 78 percent of the denials that are appealed.

Instant Records Check

If it is determined that the way to keep criminals from getting guns is to impose background checks on retail handgun sales—a questionable determination—a mandatory instant records check makes sense. The same technology that allows a store to receive verification of credit card validity within a few minutes can also allow firearms dealers to dial a state government registry and verify that a gun buyer has no felony record.

Polling data suggests that most Americans prefer the instant check to the waiting period, particularly when presented with the choice of mandatory immediate check (the NRA proposal) versus a waiting period with no requirement than any check be conducted (the Brady Bill). In recent years, many states have made major progress in bringing their criminal-records histories online. Thus, an instant check should become feasible in the near future.

And if records are not sufficiently accurate to support an instant check, they are also not sufficient to support a check with a one-week wait. Former Attorney General Thornburgh's task force found that even if there were no improvement in state criminal records, an instant check would be just as accurate as a check that could be completed in one week.

Unfortunately, if adequate safeguards are not in place, the instant check, like the waiting period, can be misused by police departments to create a registry of gun owners. In 1991, California admitted that it had used the state's handgun waiting period to create a list of handgun owners, even though nothing in California law authorizes the compilation of such a list.

Although the federal gun-control debate talks almost exclusively about retail handgun sales and the Brady Bill, the most effective method to deal with criminals obtaining guns might be to focus on the major source of criminal guns: the black market. A sensible first step in dealing with the black market would be to increase penalties for fencing a gun known to be stolen. In some states, theft and sale of a $75 gun amounts only to petty larceny. Selling a "hot" $75 pistol ought to be a more serious offense than selling a "hot" $75 toaster-oven.

NRA's Reform Proposal

While Congress has spent most of its gun-control effort debating new restrictions on gun acquisition, the discussion in many state legislatures has shifted to the carrying of firearms. The Second Amendment refers to a right "to keep and bear arms," and if the text is read consistently with original intent and judicial interpretations of the following century, the government cannot require that citizens ask for permission to carry an unconcealed gun in public.

But in many states, the right to carry has been obliterated by laws that require a police license to carry, and by police administrators who give out carry licenses only to the political elite. In New York City, crime victims who will testify at a forthcoming trial, and who are receiving death threats from the criminal's friends, are denied carry permits—while politically powerful citizens are routinely granted them. While New York's abuse of licensing discretion is notorious, the licensing systems in many other cities are also skewed against people without some kind of clout.

Based on a literalist reading of the Constitution, Second-Amendment advocates should lobby for repeal of all laws requiring a license to carry a gun. But instead, the NRA suggests only reform of easily abused gun licensing systems.

The NRA proposal requires that applicants for a permit to carry a protective firearm must undergo safety training and must submit to a police background check. Then, if the applicant passes the safety class and background check, he or she is to be granted a license to carry. The bureaucratic discretion to deny permits to qualified citizens simply because the bureaucrat does not like guns would be removed.

Every 48 seconds, an American uses a handgun for defense against an attacker.

Progress in the Gunshine State

Carry reform was first enacted in Florida in 1987, amidst vociferous cries from gun-control supporters in the legislature that blood would run in the streets as Floridians shot each other while jostling in line at fast-food restaurants. Florida would become the "Gunshine State," it was warned.

Today, those same critics have admitted that they were wrong, and that they regret the harm done to Florida's reputation by the histrionic campaign against carry reform. Indeed, while the murder rate has risen 14 percent nationally from 1986 to 1991, it has fallen 20 percent in Florida. The state's total murder rate was 36 percent higher than the U.S. murder rate in 1986, and is now 4 percent below the national average. In the same

AP/Wide World Photos

Bans on semi-automatic "assault weapons" are based on the misconception that they fire rapidly like machine guns. They actually fire like every other common gun—one bullet per squeeze of the trigger.

period, robbery rose 9 percent in Florida, and 21 percent nationally.

There has been no research proving that Florida's carry reform was part of the reason for Florida's relative improvement in recent years. But the experience of Florida, and of other carry reform states such as Oregon, Montana, Mississippi, and Pennsylvania, demonstrates that people who are already good citizens and who are willing to pass through a licensing process do not suddenly turn into murderous psychopaths when granted a permit to carry a firearm for protection.

Interrupting a Mass Murder

While tragic mass murders are frequently used by the pro-control lobby to push restrictive laws, evidence suggests that laws prohibiting firearms carrying may be costing innocent lives.

In October 1991 in Killeen, Texas, a psychopath named George Hennard rammed his pickup truck through the plate glass window of a Luby's cafeteria. Using a pair of ordinary pistols, he murdered 23 people in 10 minutes, stopping only when the police arrived.

Dr. Suzanna Gratia, a cafeteria patron, had a gun in her car, but, in conformity to Texas law, she did not carry the gun; Texas, despite its Wild-West image, has the most severe law in the country against carrying firearms. Carry-reform legislation had almost passed the state legislature, but had been stopped in House Rules Committee by the gun-control lobby.

Gratia later testified that if she had been carrying her gun, she could have shot at Hennard: "I know what a lot of people think, they think, 'Oh, my God, then you would have had a gunfight and then more people would have been killed.' Unhunh, no. I was down on the floor; this guy is standing up; everybody else is down on the floor. I had a perfect shot at him. It would have been clear. I had a place to prop my hand. The guy was not even aware of what we were doing. I'm not saying that I could have saved anybody in there, but I would have had a chance." Hennard reloaded five times, and had to throw away one pistol because it jammed, so there was plenty of opportunity for someone to fire at him.

Even if Gratia hadn't killed or wounded Hennard, he would have had to dodge hostile gunfire, and wouldn't have been able methodically to finish off his victims as they lay wounded on the floor. The hypothetical risks of a stray bullet from Gratia would have been rather small compared with the actual risks of Hennard not facing any resistance. But because of the Texas law, Gratia had left her gun in the car and couldn't take a shot at Hennard. Instead, she watched him murder both her parents.

Two months later, a pair of criminals with stolen pistols herded 20 customers and employees into the walk-in refrigerator of a Shoney's restaurant in Anniston, Alabama. Hiding under a table in the restaurant was Thomas Glenn Terry, armed with the .45 semiautomatic pistol he carried legally under Alabama law. One of the robbers discovered Terry, but Terry killed him with five shots in the chest. The second robber, who had been holding the manager hostage, shot at Terry and grazed him. Terry returned fire, and mortally wounded the robber.

Twenty-three people died in Killeen, where carrying a gun for self-defense was illegal. Twenty lives were saved, and only the two criminals died in Anniston, where self-defense permits are legal. Yet while Anniston never made the network news, Killeen did, and is used to this day as supposed proof of the need for severe gun controls. Precisely because lives are saved, instances of citizens using firearms carried on their persons to defend themselves and others rarely make the national news, even though such defensive acts occur with great frequency, as the research of Professors Kleck and Mauser demonstrates.

Emphasis on Gun Safety

Gun control, properly conceived, is not simply a matter of passing laws, or adding to the paperwork involved in retail gun purchases. Gun control needs to involve people control, or more precisely, helping people take control of their own actions. In this regard, the NRA's gun safety programs rank as America's most successful gun-control efforts.

The National Rifle Association was founded in 1871 by Union Army generals dismayed at the poor marksmanship displayed by Union forces during the recent war. The NRA always has placed heavy emphasis on its mission to train American citizens in responsible and effective firearms handling.

Happily, the fatal gun accident rate is now at an all-time low. In 1945, for every million Americans, there were about 350,000 firearms and 18 fatal gun accidents. Today, the per-million rate is 850,000 and 6 accidents. As the gun supply per capita more than doubled, fatal accidents fell by two-thirds.

NRA safety programs implemented by the 32,000

instructors and coaches who have earned NRA Instructor certification have played an important role in the accident drop, and will become even more important in coming years as more and more women choose to own handguns. Since women gun owners are more likely to own for protection, and less likely to have been initiated in sport shooting by an older male relative, safety training for these new gun owners is especially worthwhile, and the NRA has, accordingly, set up a program offering free safety training to women.

The number of fatal firearm accidents for children aged 0–14 has fallen from 550 in 1975 to 250 in 1988. While the NRA always has had junior shooting and hunting programs that emphasize the development of safe sporting gun use under adult supervision, in 1988 the organization launched a safety campaign aimed at the millions of children who never have any exposure to the shooting sports.

The NRA's Eddie Eagle Elementary Gun Safety Education Program is geared for children in pre-school through sixth grade. Using teacher-tested materials such as an animated video, cartoon workbooks, role-playing, and fun safety activities, Eddie Eagle teaches the simple lesson: "If you see a gun: Stop! Don't Touch. Leave the Area. Tell an Adult."

To date, the Eddie Eagle program has reached almost 4 million children and their parents through schools, law-enforcement programs, and a variety of youth programs. Unfortunately, it has been excluded from some urban schools by administrators who refuse to allow pupils to contact anything related to the NRA, even though the Eddie Eagle curriculum does not discuss political issues.

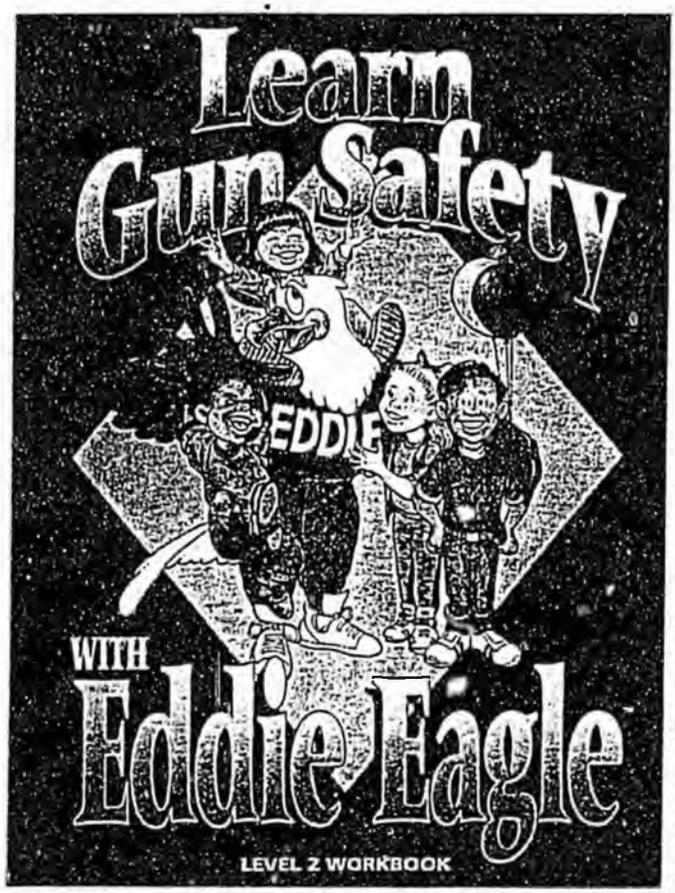

photo courtesy of the National Rifle Association

Thanks to such gun-safety programs as the NRA's Eddie Eagle, fatal firearm accidents among children 14 and under have fallen from 550 in 1975 to 250 in 1988.

Controlling Criminals, Not Guns

The NRA's most controversial recent effort is the organization's CrimeStrike program, which takes aim at aspects of the criminal justice system that the NRA considers too lenient. In pushing for laws allowing greater pretrial detention of violent repeat offenders, the NRA adheres to its conservative roots, to the chagrin of some its libertarian supporters, who are unwilling to protect the Second Amendment by weakening the Eighth Amendment right to bail.

Other aspects of CrimeStrike, such as support for victims' rights laws, cause no dissent within the pro-Second Amendment coalition, and offer an opportunity to improve a criminal justice bureaucracy that sometimes lets the desire to process cases overshadow the necessity to do justice to the criminal *and* the victim.

NRA CrimeStrike strategies, like NRA lobbying, rely heavily on grassroots pressure. In a recent Texas case, Charles Edward Bruton had been sentenced to two 10-year terms for shooting at a woman and for committing a heinous sexual assault against her 11-year old daughter. Having served only three years, Bruton was up for parole last September. After the shooting victim asked CrimeStrike for assistance, NRA members were notified through NRA magazines destined for Texas; the Texas Board of Pardons and Appeals was flooded with calls and letters; the parole was denied.

CrimeStrike will not single-handedly fix the criminal justice system, nor will safety education eliminate all accidents, nor will carry reform wipe out all street crime. But each of these efforts will improve public safety for all citizens, whether they own guns or not. Everyone benefits from a prison system that keeps violent felons off the streets; everyone benefits from reduced risks of gun accidents; and everyone benefits from street criminals facing increased odds of victims resisting successfully.

Today, rather than merely opposing poorly conceived gun-control legislation, right-to-keep-and-bear-arms supporters are working in positive ways. These efforts will enhance not only the rights of the 50 percent of American families who own guns, but also the safety of the 50 percent who do not.

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THE LAST WORD

GEORGE F. WILL

Are We 'a Nation of Cowards'?

JEFFREY SNYDER'S TIMING IS EITHER PERFECT OR PERFECTLY awful. Just as there seems to be a coalescing consensus that the keys to controlling violent crime are more police and fewer guns, along comes Snyder to trouble the conscience of anyone who thinks so. In his essay "A Nation of Cowards" in The Public Interest quarterly, he argues, with a potent blend of philosophy and fact, as follows:

"Crime is rampant because the law-abiding, each of us, condone it, excuse it, permit it, submit to it. We permit and encourage it because we do not fight back immediately, then and there, where it happens ... The defect is there, in our character. We are a nation of cowards and shirkers."

Strong words, those, but not stronger than his argument, the gravamen of which is that the crime problem cannot be addressed without confronting the moral responsibility of the intended victim. Taking responsibility for one's life, family and community requires fighting back when threatened with violence. How? By possessing and mastering the means of resistance. The means is an "equalizer"—a handgun. A responsible citizen, he says, "will be trained in the use of his weapon, and will defend himself when faced with lethal violence."

EXAMINING THE ARGUMENT FOR AN ARMED CITIZENRY

Before examining his argument for an armed citizenry, consider the freshest evidence of the nation's quickened concern about crime.

On Election Day voters in liberal Washington state gave emphatic (75 percent) approval to the "three strikes ... you're out" initiative which mandates life imprisonment without parole for people convicted of three major felonies. California, although tax-phobic, nevertheless voted to make permanent an existing tax to provide $1.5 billion for public safety—more police and firemen. (Arson has made fire a facet of California's anxiety about crime.) Fiscally conservative Texas endorsed a $1 billion bond issue to build more prisons and mental health facilities.

The day after the elections the House of Representatives, with a familiar mixture of posturing and false advertising, passed yet another crime bill: this one purporting to subsidize the hiring of 50,000 police officers. It probably would fund fewer. The Senate promptly pumped up the money. For 40 years Congress has passed a crime bill in every two-year session, except the last one. The criminal class has not been impressed.

The day after the elections the president held a ceremony to push the bill that would require a five-day waiting period for the purchase of a gun. The attention given to this "Brady bill" seems disproportionate, given that 93 percent of the guns obtained by violent criminals are not obtained through lawful transactions that are the focus of most gun control legislation.

More interesting, the day after the elections Sen. Pat Moynihan proposed whopping tax increases on various kinds of handgun ammunition. He even favors a 10,000 percent tax on the Winchester 9-mm hollow-tipped Black Talon cartridge. ("Penetrates soft tissue like a throwing star—very nasty," boasts an advertisement.) That tax would make 20 cartridges cost about $1,500. In large portions of Moynihan's New York City people are slain by stray—that's right, stray—bullets. Moynihan says: Guns do not kill people, bullets do. We have a 200-year supply of guns and a four-year supply of ammunition, so concentrate on the latter.

Snyder, an attorney in Washington, where the mayor begs for military help against crime, demurs, comprehensively. America, he says, is wrongly called an "armed society." He thinks we would be better off if it were. Most of the guns owned by law-abiding citizens are kept at home, but 57 percent of violent crimes occur outside the home. The constantly armed portion of the community consists primarily of the police and violent criminals. Multiplying the former cannot make us safe from the latter.

Self-respect: It is, says Snyder, foolish and craven to expect police to perform as personal bodyguards. The existence of police does not relieve individuals of all responsibility for self-protection. That judgment has both prudential and moral dimensions. Gun owners like to say, "Call for a cop, call for an ambulance and call for a pizza. See which comes first." The Department of Justice reports that in 1991, for all crimes of violence, only 28 percent of calls to the police were responded to within five minutes. And it is now more likely that an American will be injured by violent crime than that he will be injured in an auto accident.

Feminists, says Snyder, rightly insist that rape is not about sex but about domination. What is at issue in crime is not just property but dignity. Crime, he says, always violates the victim's dignity, which can hardly be said to exist if the victim does not deem it worth fighting for. Crime is "an act of enslavement" and a personal readiness to resist it should be regarded as a prerequisite of self-respect, properly understood. He notes that "self-respect," which implies standards by which one judges oneself, has been supplanted in public discourse by the locution "self-esteem," which simply means having warm feelings about oneself. Repeating the shibboleths of the gun control movement makes many people feel good about themselves. Snyder's argument should disturb their peace.

Much gun control advocacy is directed against normal citizens, who are depicted as at best benighted and at worst barbaric. Gun owners are routinely characterized as uneducated, intolerant, possibly paranoid rednecks—people urgently in need of re-education and "consciousness-raising" from the liberal agenda. In Mario Cuomo's depiction, gun owners are "hunters who drink beer, don't vote and lie to their wives about where they were all weekend." (Cuomo quickly recanted this. Gun owners do vote.) Actually, the gun-owning population is pretty much like the general population because approximately one of every two households has a gun.

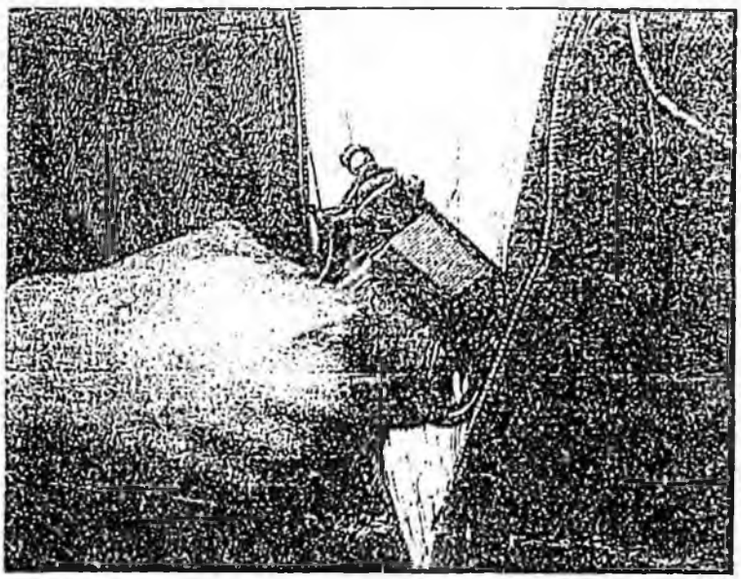
Now, Snyder is right that the gun control movement often radiates distrust of average citizens, whose supposed mental and moral deficiencies are such that "only lack of immediate access to guns prevents the blood from flowing in the streets." Nevertheless, it is reasonable to wonder whether a nation whose citizens cannot

(Continued on page 93)

(Continued from page 94)
program their VCRs and who increasingly will not respect stoplights (surely you have noticed the increasing lawlessness of drivers) is a nation whose citizens are insufficiently dexterous and too aggressive to be safely armed.

Snyder says the idea that only the police are qualified to use firearms is akin to saying that "only concert pianists may play the piano and only professional athletes may play sports." The flaw in Snyder's analogy is that if you play the piano unskillfully, you neither kill nor wound anyone. However, Snyder has evidence more powerful than his analogy.

In 13 states citizens who wish to carry arms may do so, having met certain requirements. Consider Florida, which in 1987 enacted a concealed-carry law guaranteeing a gun permit to any resident who is at least 21, has no record of crime, mental illness or drug or alcohol abuse, and who has completed a firearms safety course. Florida's homicide rate fell following the enactment of this law, as did the rate in Oregon after the enactment of a similar law. Through June 1993, there had been 160,823 permits issued in Florida. Only 330, or 0.33 percent, of the applicants have been denied permits. This indicates that the law is serving the law abiding. Only 16 permits, less than 1/100th of 1 percent, have been rescinded because of the commission, after issuance, of a crime involving a firearm.



RON LEAV—GAMMA-LIAISON

Equalizer: *Is this a citizen taking his responsibility seriously?*

Ninety percent of violent crimes are committed by persons not carrying handguns. This is one reason why the mere brandishing of a gun by a potential victim of violence often is a sufficient response to a would-be attacker. In most cases where a gun is used in self-defense, it is not fired. Can the average citizen be trusted to judge accurately when he or she is in jeopardy? Snyder answers that "rape, robbery and attempted murder are not typically actions rife with ambiguity or subtlety." Furthermore:

"Florida State University criminologist Gary Kleck, using surveys and other data, has determined that armed citizens defend their lives or property with firearms against criminals approximately 1 million times a year. In 98 percent of these instances, the citizen merely brandishes the weapon or fires a warning shot. Only in 2 percent of the cases do citizens actually shoot their assailants. In defending themselves with their firearms, armed citizens kill 2,000 to 3,000 criminals each year, three times the number killed by the police. A nationwide study by Don Kates, the constitutional lawyer and criminologist, found that only 2 percent of civilian shootings involved an innocent person mistakenly identified as a criminal. The 'error rate' for the police, however, was 11 percent, more than five times as high."

'CRIME IS RAMPANT BECAUSE THE LAW-ABIDING SUBMIT TO IT'

Concerning what we may call "the running of red lights syndrome" in contemporary America, I put the point to Snyder and he fired back a fax:

"Regarding your observation about our society's general level of aggressiveness and disregard for rules, you may wish to consider Robert Heinlein's famous dictum that 'An armed society is a polite society.' Knowing that one's fellow citizens are armed, greater care is naturally taken not to give offense. The proposition is, of course, difficult to prove, but you can find some support for it in English literature. Observe the polite formality with which strangers address each other in inns in, for example, Fielding's 'Tom Jones' or (with comedic exaggeration) in Dickens's 'Pickwick Papers.' While no doubt attributable in part to England's class structure and the education received by the aristocracy, I would hesitate to say that it had nothing to do with the fact that gentlemen generally were armed."

Or as is famously said in American literature, by the hero of Owen Wister's "The Virginian," "When you call me that, *smile!*" Such was politeness in the armed society of 19th-century Wyoming.

Finally, there is the matter of the Second Amendment. This Republic's Founders constitutionalized, which means they made fundamental, the right to possess firearms, and they did not do so unreflectively. They placed that right second in the Bill of Rights, yielding precedence only to rights pertaining to speech, worship and association, and they did that for philosophically serious reasons. The philosophy of classical republicanism recognizes a crucial relationship between personal liberty and possession of arms by a people prepared to use them. Snyder believes that the Second Amendment is as much a product of this philosophy as of the Revolutionary War experience or the exigencies of frontier life: "To own firearms is to affirm that freedom is not a gift from government . . . As the Founding Fathers knew well, a government that does not trust its honest, law-abiding, taxpaying citizens with the means of self-defense is not itself worthy of trust."

Yes, and yet . . . no society can be called successful where violence is so prevalent and random that lawful citizens must go about prepared to dispense violence in self-defense. No one wants to live, raise children and grow old in such a society. But government is constituted to provide, first and foremost, domestic tranquillity sufficient to make unnecessary the sort of personal measures that Snyder recommends. If such measures are becoming necessary, do not blame Snyder.

Snyder writes that "the association of personal disarmament with civilized behavior is one of the great unexamined beliefs of our time." Not anymore it isn't. His searching examination of it may not compel your assent—I remain unpersuaded—but it must shake some soothing assumptions regarding crime and civic responsibilities. I am among those whom Snyder faults, civilly but firmly, for insufficient rigor in reasoning about these matters. I find being reproved by him a bracing experience because it enlarges my understanding while subtracting from my certainties. I salute him and thank him.

THE RIGHT TO KEEP AND BEAR ARMS

PRO-GUN LAWS— THEY WORK!

Now that the law-abiding citizens of several states legally have the right to defend themselves, even anti-gun officials have admitted that they are safer states to live in than before the passage of a concealed weapons carry law.

■■■

By Marion P. Hammer

A 33-year-old Miami cab driver was among the first to apply for and receive a concealed weapons license under the new concealed weapons licensing reform law that went into effect in Florida on October 1, 1987.

A few short months after receiving his license, Miami police reported that on March 5, 1988, he became the first license holder to be involved in a shooting.

Forced to defend himself, the driver shot and killed a robber who pointed a firearm at him, demanded money, then after taking the money told the moonlighting cab driver he was going to kill him.

The robber, a 29-year-old ex-convict with a history of attempting to kill police officers, tried to fire a Smith & Wesson 9mm semi-automatic handgun at the cabby at point-blank range. But he had forgotten to disengage the safety. In those few split seconds when the robber was distracted the cab driver pulled and fired his own gun—a Colt .45-caliber semi-automatic handgun—mortally wounding the attacker. Pronounced

"The bottom line is that Florida is a safer place to live because of the law...."

dead at the hospital, the robber still had the cabby's wallet in his pocket.

The ex-convict's past included arrests for armed robbery, gun violations and attempted first-degree murder of a police officer. In 1981, he shot out the windshield of a Hialeah patrol car, which then crashed. He also shot at Miami Spring police during a chase. He was sentenced to 12 years in prison, but seven years later he was on the street pulling the trigger on a law-abiding cab driver.

The criminal justice system failed to protect the cabby by not keeping this violent criminal in prison to serve out his time. But Florida's new concealed weapons licensing law made it possible for him to protect his own life. As reported in a newspaper following

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the incident, the cab driver "used the weapon correctly to defend himself. Without the law in effect, he would be a dead man this morning."

While this incident was reported to be the first involving a concealed carry permit holder, it has not been the last justifiable self-defense shooting involving law-abiding license holders. No one likes to see headlines filled with bloodshed, but all sane and reasonable Americans must surely applaud when a terrible crime is thwarted and an innocent citizen saved. In this case a quiet, hard-working and honest cab driver prevented his own death at the hands of a criminal with a history of brutal violence.

The Miami police sergeant on the scene told reporters that the incident "sends a message to the rest of the robbers out there." I think the incident also sent a message to those who worked against the passage of the

"The issue is, and has always been, one of the right of self-defense."

concealed carry reform law.

The media have always been quick to report the emotional, inflammatory hysterics of the anti-gunners any time the subject of firearms emerges, and slow to report positive results of firearms ownership. During the fight for passage of the licensing reform legislation, it was commonplace to read and hear a steady media drumbeat about Dodge City, frontier-style justice, the O.K. Corral for guns, an invitation to a Wild West mentality, blood on the hands of those who vote for passage, etc. Some editorials, like the Suntattler's, got a little more creative, declaring: "...a state law that welcomes virtually everyone to pack a rod would increase lawlessness—and death. Forget that a pistol-packing citizenry will mean itchier trigger fingers...Forget that South Florida's climate of smoldering fear would flash like napalm when every stranger totes a piece, and every mental snap in traffic could lead to the crack of gunfire."

Now, four years after implementing the concealed carry reforms in Florida, the critics and doomsayers have been forced to recant their hysterical predictions. They have been forced to abandon the parade of horribles they contrived in the heat of debate.

Those of us who labored for seven

years to reform the nightmarish patchwork of concealed weapons ordinances found in Florida's counties are proud to point to its record of success. The new concealed carry permit law is working well.

Before passage of the reform law, our hodgepodge of laws either disregarded the Constitution's Second Amendment, were interpreted locally or were left up to bureaucratic whim. There was no uniform procedure in Florida's 67 counties and citizens were subject to varying criteria depending upon where they lived.

Now this very basic right no longer vacillates according to local politics or the authority of a powerful few. We now have a state agency that handles applications and issues licenses based on statewide statutory criteria, and the license is valid statewide—not just in a particular county as in the past.

A year after the law took effect, Willis Booth, executive director of the Florida Chiefs Association, told the press, "The minute the bill was passed, we asked our chiefs in the state to be particularly alert for any cases in their jurisdiction that would give us knowledge of the fact that there was some abuse. At this point, it would appear the law is working very well. There are no horror stories that can be attributed to the passage of the law."

John Fuller, general counsel for the Florida Sheriff's Association, agreed. "I haven't seen where we have had any instance of persons with permits causing violent crimes, and I'm constantly on the lookout," he said.

A Florida Department of Law Enforcement spokesman has told reporters that the new law hasn't affected firearms violence in Florida, indicating that any increase in crime is attributed to the growing drug problem, not the concealed firearms law.

FLORIDA CONCEALED WEAPONS LICENSING: STATISTICS TO DATE

Applications received:	104,249
Applications denied:	743
Denied for incomplete application:	301
Denied for criminal history*:	442
Licenses revoked for offenses after licensure:	61
Revoked for offense/firearm present**:	10
Revoked for other reasons*:	51

*Majority of offenses were nonviolent crimes such as DUIs, worthless checks and controlled-substance convictions.

**DUIs, reckless display included.

NOTE: This chart contains official statistical data from the Florida Department of State, Division of Licensing.

Even Robert Creighton, agent in charge of the U.S. Bureau of Alcohol, Tobacco and Firearms (BATF) in Florida, acknowledged that the popular concealed weapons permits aren't a factor in crime, adding, "The criminal element has no permits."

Anti-gun groups and the media predicted an outbreak of shootings in the Sunshine State. But, since passage nearly four years ago, this fair and more uniform concealed carry law simply hasn't shaken the foundations of the Florida legal system or created "an Old Wild West, "O.K. Corral" or "GUNshine State," as doomsayers predicted.

But the media have been unenthusiastic about reporting the success of the law and rarely report incidents when license holders defend themselves with a firearm, or simply bury a very short report somewhere in the back of the paper. Nonetheless many Floridians are alive and well today because we stuck with it for seven years and passed a law that they credit with saving their lives.

Take the case of a Miami attorney who believes he and his wife are alive today because of passage of the law. He and his wife returned home from a basketball game late on the evening of February 24, 1991. After opening the door for his wife to enter the home he turned around in the garage to get a leash to walk his dog. He was confronted by two attackers standing in his garage, wearing ski masks and carrying guns. He ducked behind the door as one attacker fired a shot, pulled his .45-caliber semi-automatic handgun and opened fire through the doorway. The attackers ran from the garage and fled in a waiting vehicle driven ay a third person.

The attorney said if the concealed weapons law had not passed he would not have been armed, and surely would not be alive to read the brief 2-inch-long story—buried inside the newspaper—reporting the incident.

Clearly, the law has worked as we said it would, proving what those of us who supported it said all along. Statistics from the Florida Department of State—the agency handling applications and issuing licenses—are graphically clear. They prove that applicants are conscientious citizens concerned about and taking responsibility for their personal safety. The issue is, and has always been, one of the right of self-defense. Law-abiding Florida citizens do not wish to harm anyone. Yet neither do they feel they should suffer harm at the hands of the lawless. It is patently obvious from the accompanying chart that license holders are everyday, law-abiding people who simply want to be able to protect themselves and their families should the need arise.

That should come as no surprise. A study conducted by the St. Louis University School of Law found that armed citizens were exceedingly responsible in carrying handguns on the street. The study found that while police were successful in shooting or driving off criminals 68 percent of the time, private citizens succeeded in 83 percent of their encounters. Most importantly, while 11 percent of the individuals involved in police shootings were later found to be innocents misidentified as criminals, only 2 percent of those in civilian shootings were so misidentified. In light of the fact that in urban areas private citizens encounter and kill up to three times as many criminals as do law enforcement authorities, the track record of the private citizen is very impressive indeed. Florida's experience simply proves it once again.

David Register, Director, Div. of Licensing, Florida Dept. of State (left), and Florida Sec. of State Jim Smith (right) present "Concealed Weapons License Number 1" to Marion P. Hammer under Florida's new concealed weapons licensing law. Ms. Hammer, representing the NRA and Unified Sportsmen of Florida, helped write and pass the self-defense legislation.

Law-abiding Floridians who choose to protect themselves by carrying a concealed firearm may apply for a license—and receive it—if they meet the standardized criteria. Sate law mandates that a license be issued within 90 days from receipt of a completed application if the applicant is 21 years of age or older, has been a resident of Florida for six months, has no criminal record, can document knowledge or training in the safe use

continued on back page

and handling of a firearm, has no record of alcohol or drug abuse, no record of mental illness or mental incompetency, no physical infirmity that would prevent safe handling of a firearm and desires to carry a concealed firearm for lawful self-defense.

The state must issue the license or prove the individual is disqualified based solely on the statutory criteria. There is no arbitrary or subjective discretion by anyone, and rule-making authority that could alter the intent of the law is specifically prohibited.

Three years after passage, in November 1990, the press revisited the issue in an interview with State Representative Ron Silver. Silver, an ardent supporter of Handgun Control Inc., and the organization's chairwoman, Sarah Brady, told the press, "There are lots of people, including myself, who thought things would be a lot worse as far as that particular situation [people being licensed to carry firearms for protection] is concerned. I'm happy to say they're not."

Silver also said that Florida has a long way to go to rid itself of its Wild West reputation and the "GUNshine State" label that he and HCI helped create with their emotional predictions of misuse and abuse. He added, "All of us are trying to do away with that image."

The bottom line is that Florida is a safer place to live because of the law, as Silver admitted. So it's time for the anti-gun organizations to back off. The statistics are in. The proof supports our position. The law is working very well. And decent people are alive today as a result of its passage.

Other states (Idaho, Mississippi, Montana and Oregon) have already used the Florida concealed weapons licensing law as a model and have passed similar legislation. Perhaps it's time for your state to do the same.

Besides being a mother of three and a grandmother, Ms. Hammer has been active both as a sportswoman and as a political force working on behalf of firearms rights. Currently, she is a National Rifle Association board member and holds a seat on the NRA Legislative Policies Committee and the NRA Membership Committee and is chairperson of the NRA Ethics Committee. As a strong supporter of the NRA/ILA, she has been a media spokesperson on behalf of our 2nd Amendment rights, giving over 700 interviews in the past four years for national television, radio and the print media. For the past 12 years, Manon P. Hammer has held to post of Executive Director of Unified Sportsmen of Florida 206 S. Monroe St., Suite 5, P.O. Box 6565, Tallahassee, FL 32314.

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Fla. Klock

Steve Humphries
October 1991

Florida State criminologist
shoots down gun-control myths

TALLAHASSEE, Fla.--A criminal without a gun is more likely to hurt you than a criminal with one. You're less apt to be robbed, or to be hurt in a robbery, if you have a gun for defense.

And an assailant is no more likely to kill you if he has a gun than if he doesn't.

Those findings are contained in a new book, "Point Blank: Guns and Violence in America," by Gary Kleck, a criminologist at Florida State University.

"It appears that the net effect of gun availability on crime is just about zero," said Kleck. "Victims with guns may depress crime a little and offenders with guns may increase it a little. My research indicates they cancel each other out."

The 500-plus-page book, due out Nov. 5, notes that guns are used for defense in this country about the same number of times each year as they are used to commit crimes -- and usually with no one getting hurt.

"In a robbery, people who use guns in self-defense avoid injury 83 percent of the time and in most cases they don't have the crime completed against them," Kleck found. "The results are similar for assaults and rapes.

"It turns out you're less likely to be hurt if you resist with a gun, even compared to doing nothing at all to resist. This shouldn't be surprising. If a gun works in committing a crime, why wouldn't it also work in preventing one?"

Kleck found that people who do nothing to protect themselves are injured in 25 percent of robberies, while those who use a gun for protection are hurt only 17 percent of the time.

He said would-be victims thwart many crimes by carrying a gun, and assailants often find just flashing a firearm can keep the situation from escalating into a fight.

"You are actually less likely to be injured if a robber

-more-

has a gun than if he doesn't," he said. "And you're less likely to be injured if you have a gun.

"It's actually safer if either party has a gun."

Kleck, a professor in the FSU School of Criminology and Criminal Justice, studied 19 types of gun control and found that almost none -- including waiting periods and owner registration -- had any effect on crime rates. Banning guns, he said, is no longer an option.

"This country has 200 million guns, minimum, in private hands," he said. "To think of some method that works by controlling the overall supply of guns is hopeless. We passed that point long ago."

Instead, Kleck says, background checks should be instituted to make it harder for convicted violent offenders to buy guns and penalties should be strengthed for those caught with them. Laws also should be passed to more closely regulate the carrying of guns, he said, to decrease the number of opportunistic robberies.

Kleck bases his recommendations on data that show most violent offenders are not average citizens who become enraged, pick up a gun and commit a crime.

"Repeatedly violent offenders account for most cases of domestic violence and practically all homicides," he said. "There aren't many average-Joe, honest-to-God, they-did-it-out-of-nowhere killers. It's a wonderful media myth -- the average Joe killer."

Kleck said 70 percent of all homicides in the United States are committed by someone with at least one prior arrest.

"Point Blank," published by Aldine de Gruyter, is a first in at least two respects.

It is the first to use nationally representative samples of violent incidents -- from minor threats to homicides, including those reported and those not reported to the police -- to distinguish between attack, injury and death as outcomes of violent situations. It also is the first to combine national data on both fatal and non-fatal violent incidents to study how weapon use affects death rates.

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Dr. Kleck can be reached at (904) 644-4050. Audio tapes containing actualities by Dr. Kleck, and videotapes and photographs of Dr. Kleck, can be obtained by calling the FSU Media Relations Office.

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The Pacific Institute for Public Policy, in February 1990, published a Policy Briefing entitled GUNS, MURDERS, AND THE CONSTITUTION; a Realistic Assessment of Gun Control, by Don B. Kates, Jr.

The author does an excellent job of addressing the issue of gun control laws, giving the pros and cons and comparing the actual facts with the assumptions of the various attitudes which are prevalent.

Two positions are attached here for your information:

1. Sagecraft Summarized

2. Police Protection vs Capacity to Defend Oneself

1. Sagecraft Summarized

Lest the sagecraft concept seem unduly harsh, I will briefly review five particularly insupportable anti-gun claims (they and others are further detailed in the body of this paper):

a) *The claim that homicide is predominantly a matter of "ordinary law-abiding people" killing a relative or acquaintance because a loaded gun happened to be available during a moment of anger.*

This claim is contradicted by all national and local studies of homicide, which uniformly show that murderers are not "ordinary law-abiding people." Rather, murderers (like gun accident perpetrators) are highly aberrant individuals, characterized by felony records, alcohol and/or drug dependence, and life histories of irrational violence against people around them.[10]

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[8] Bruce-Briggs, above.

[9] Tonso, above, applying concepts based on F. Znaniecki, *The Social Role of the Man of Knowledge*, 72-74 (N.Y.: Harpers, 1968).

[10] Straus, "Domestic Violence and Homicide Antecedents," 62 *Bull. N.Y. Acad. Med.* 446 (1986); cf. Bruce-Briggs, "The Great American Gun War," 45 *The Public Interest* 37, 40 (1976):

> The calculation of family homicides and accidents as costs of gun ownership is false. The great majority of these killings are among poor, restless, alcoholic, troubled people, usually with long criminal records. Applying the domestic homicide rate of these people to the presumably upstanding citizens whom they prey upon is seriously misleading.

See also Kates, "Firearms and Violence: Old Premises, Current Evidence," in T. Gurr (ed.), 1 *Violence in America*, 203-204 (1989) (hereinafter cited as "Current Research"); Kleck, "Policy Lessons from Recent Gun Control Research," 49 *Law & Contemp. Probs.* 35 (1986) (hereinafter cited as "Policy Lessons") at 40-41, and studies there cited.

b) *The claim that (though banning all guns may not be politically feasible) banning only handguns would save lives because gun attacks are more lethal than knife attacks.*

In a recent National Institute of Justice survey among about 2,000 incarcerated felons, well over 80 percent of those who had often misused handguns said that if handguns were unavailable they would turn to long guns (rifles or shotguns) instead.[11] Thus, a crucial issue in any handgun ban is that, while handgun wounds are 1.3 to 3 times more lethal than knife wounds, a rifle or shotgun wound kills 5 to 11.4 times more often than a handgun wound. Far from decreasing homicide, if a handgun ban caused only 30 percent of handgun attackers to turn to long guns, the homicide rate might nearly double; if 50 percent switched, homicides could more than triple.[12] Astoundingly, not one academic who argued that banning handguns would save lives (because knives are less deadly) even mentioned the necessary corollary that not controlling long guns would cost lives because rifles and shotguns are far more lethal.

c) *The claim that comparing American statistics to those of selected gun-banning foreign countries proves that guns cause crime and that banning them reduces it.*

Differentials in international crime rates reflect basic socio-cultural and economic differences that have nothing to do with gun laws. First, Western Europe has not only far less gun violence but also less violence of all kinds *per capita*. Second, this difference between the United States and Western Europe was even greater before the latter's gun laws were adopted in the 1920s and 1930s. Third, those laws were adopted to control political violence–to which those countries have always been far more subject than the United States. Fourth, as American violence skyrocketed from the mid-1960s on, violence rates increased even more rapidly in the gun-banning countries (particularly gun violence). And fifth, in such equally crime-free countries as Switzerland, Israel, and New Zealand, there is even more gun availability than there is in the United States.[13]

d) *The claim that guns are generally not useful and not used for self-defense.*

Gary Kleck recently has found that, while handguns are used in vast numbers of crimes annually, they are used even more often by good citizens to repel crime

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[11]. J. Wright & P. Rossi, *Armed and Dangerous: A Survey of Felons and Their Firearms* 221, table 11.3 (N.Y.: Aldine, 1986) (hereinafter called NIJ Felon Survey).

[12] Policy Lessons at 48-50, Lizotte, "The Costs of Using Gun Control to Reduce Homicide," 62 *Bull. N.Y. Acad. Med.* 539, 541 (1986).

[13] See discussion in Current Evidence at pp. 200ff and below in this paper.

(approximately 581,000 crimes vs. about 645,000 defense uses annually).[14]

e) *The claim that there is no individual right to arms because the Second Amendment to the U.S. Constitution protects only the states' right to arm the militia.*

Though mere control is constitutional, wholesale prohibition and confiscation is not; the Constitution precludes laws barring responsible, law-abiding adults from choosing to own guns for self-defense. Sanford Levinson, a leading constitutional scholar (who personally opposes gun ownership), recently dismissed academic obliviousness to this clear fact in a paper fittingly entitled "The Embarrassing Second Amendment."[15]

1. Police Protection vs. the Capacity to Defend Oneself

Perhaps the single most common argument against freedom of choice is that personal self-defense has been rendered obsolete by the existence of a professional police force.[69] For decades, anti-gun officials in Chicago, San Francisco, New York, and Washington, D.C., have admonished the citizenry that they don't need guns for self-defense because the police will defend them. This advice is mendacious: when those cities are sued for failure to provide police protection, those same officials send forth their city attorneys to invoke

> [the] fundamental principle of American law that a government and its agents are under no general duty to provide public services, such as police protection, to any individual citizen.[70]

Even as a matter of theory (much less in fact), the police do NOT exist to protect the individual citizen. Rather their function is to deter crime in general by patrol activities and by apprehension after the crime has occurred. If circumstances permit, the police should and will protect a citizen in distress. But they are not legally duty bound even to do that nor to provide any direct protection—no matter how urgent a distress call they may receive. *A fortiori* the police have no duty to, and do not, protect citizens who are under death threat (e.g., women threatened by former boyfriends or husbands).

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[68] All discussion of gun-armed self-defense in this paper is directed to handguns because they are infinitely more efficacious for defense than rifles or shotguns. In contrast to the unwieldy long gun, the short-barrelled handgun is much easier to bring into play at close quarters and much harder for an assailant to wrest away. Consider the situation of a woman holding an intruder at bay while trying to dial the police. With a rifle, this is difficult and hazardous at best. Given only the two-inch barrel of a snub-nosed handgun to grasp, not even the strongest man can lever it from a woman's grip before she shoots him. M. Ayoob, *The Truth About Self-Protection* (N.Y.: Bantam, 1983) 332-33, 341-42, 345-55.

[69] Thus Ramsey Clark denounces precautionary gun ownership as an atavistic insult to American government: "A state in which a citizen needs a gun to protect himself from crime has failed to perform its first purpose"; it is "anarchy, not order under law—a jungle where each relies on himself for survival." R. Clark, *Crime in America* 88 (1971). For similar views, see also Wills, "Handguns that Kill," *Washington Star*, Jan. 18, 1981; "John Lennon's War," *Chicago Sun Times*, Dec. 12, 1980; and "Or Worldwide Gun Control" *Philadelphia Inquirer*, May 17, 1981; editorial: "Guns and the Civilizing Process," *Washington Post*, Sept. 26, 1972.

[70] *Warren* v. *District of Columbia*, 444 A.2d 1 (D.C. Ct. of Ap. 1981). For similar cases from New York and Chicago, see *Riss* v. *City of New York*, 22 N.Y. 2d 579, 293 NYS2d 897, 240 N.E. 2d 860 (N.Y. Ct. of Ap. 1958); *Keane* v. *City of Chicago*, 98 Ill. App.2d 460, 240 N.E.2d 321 (1968). See also the cases cited in the next two footnotes and *Bowers* v. *DeVito*, 686 F.2d 61 (7 Cir. 1982) (no federal constitutional requirement that state or local agencies provide sufficient police protection).

An illustrative case is *Warren v. District of Columbia* in which three rape victims sued the city under the following facts. Two of the victims were upstairs when they heard the other being attacked by men who had broken in downstairs. Half an hour having passed and their roommate's screams having ceased, they assumed the police must have arrived in response to their repeated phone calls. In fact, their calls had somehow been lost in the shuffle while the roommate was being beaten into silent acquiescence. When the roommates went downstairs to see to her, as the court's opinion graphically describes it, "For the next fourteen hours the women were held captive, raped, robbed, beaten, forced to commit sexual acts upon each other, and made to submit to the sexual demands" of their attackers.

Having set out these facts, the District of Columbia's highest court exonerated the District and its police, because it is "fundamental [in] American law" that the police do not exist to provide personal protection to individual citizens.[71] In addition to the case law I have cited, this principle has been expressly enunciated over and over again in state law.[72]

The fundamental principle that the police have no duty to protect individuals derives equally from practical necessity and from legal history. Historically, there were no police, even in large American or English cities, before the mid-19th century. Citizens were not only expected to protect themselves (and each other), but also legally required in response to the hue and cry to chase down and apprehend criminals. The very idea of a police was anathema, American and English liberalism viewing any such force as a form of the dreaded "standing army."[73] This view yielded only grudgingly to the fact that citizens were unwilling to spend their leisure hours patrolling miles of city streets and were incapable even of chasing fleeing criminals down on crowded city streets--much less tracing and apprehending them or detecting surreptitious crimes.

Eventually, police forces were established to augment citizen self-protection by systematic patrol to deter crime and to detect and apprehend criminals if a crime should occur. Historically, there was no thought of the police displacing the citizen's right of self-protection. Nor, as a practical matter, is that displacement remotely

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[71] 444 A.2d at 6; see also *Morgan* v. *District of Columbia*, 468 A.2d 1306 (D.C. Ct. of Ap. 1983). To the same effect, see *Calogrides* v. *City of Mobile*, 475 So. 2d 560 (S.Ct. Ala. 1985); *Morris* v. *Musser*, 478 A.2d 937 (1984); *Davidson* v. *City of Westminster*, 32 C.3d 197, 185 Cal. Rptr. 252, 649 P.2d 894 (S. Ct. Cal. 1982); *Chapman* v. *City of Philadelphia*, 434 A.2d 753 (Sup. Ct. Penn. 1981); *Weutrich* v. *Delia*, 155 N.J. Super. 324, 326, 382 A.2d 929, 930 (1978); *Sapp* v. *City of Tallahassee*, 348 So.2d 363 (Fla. Ct. of Ap. 1977); *Simpson's Food Fair* v. *Evansville*, 272 N.E. 2d 871 (Ind. Ct. of Ap.); *Silver* v. *City of Minneapolis*, 170 N.W.2d 206 (S. Ct. Minn. 1969); and the other authorities cited in the footnotes preceding and following this one.

[72] See Cal. Govt. Code §§ 821, 845, 846, and 85 Ill. Rev. Stat. 4-102, construed in *Stone* v. *State*, 106 C.A.3d 924, 165 Cal. Rptr. 339 (Cal. Ct. of Ap. 1980); and *Jamison* v. *City of Chicago*, 48 Ill. App. 567 (Ill. Ct. of Ap. 1977) respectively; see generally 18 *McQuillen on Municipal Corporations*, sec. 53.80.

[73] See generally 82 *Mich. L. Rev.* above at 214-16. and F. Morn, "Firearms Use and the Police: A Historic Evolution of American Values," in D. Kates (ed.), *Firearms and Violence* (1984).

feasible in light of the demands a high-crime society makes on the limited resources available to police it. Even if all 500,000 American police officers were assigned to patrol, they could not protect 240 million citizens from upwards of 10 million criminals who enjoy the luxury of deciding when and where to strike. But we have nothing like 500,000 patrol officers: to determine how many police are actually available for any one shift, we must divide the 500,000 by four (three shifts per day, plus officers who have days off, are on sick leave, etc.). The resulting number must be cut in half to account for officers assigned to investigations, juvenile, records, laboratory, traffic, etc., rather than patrol.[74]

Doubtless the deterrent effect of the police helps ensure that many Americans will never be so unfortunate as to live in circumstances requiring personal protection. But for those who do need such protection, police do not and cannot function as bodyguards for ordinary citizens (though in New York and other major cities police may perform bodyguard services for the mayor and other prominent officials). Consider just the number of New York City women who each year seek police help, reporting threats by ex-husbands, ex-boyfriends, etc. To bodyguard just those women would exhaust the resources of the nation's largest police department, leaving no officers available for street patrol, traffic control, crime detection, apprehension of perpetrators, responses to emergency calls and so forth.[75]

Given what New York courts have called "the crushing nature of the burden,"[76] the police cannot be expected to protect the individual citizen. Individuals remain responsible for their own personal safety, with police providing only an auxiliary general deterrent. The issue is whether those individuals should be free to choose gun ownership as a means of protecting themselves, their homes, and their families.

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[74] See the extended discussion in Bowman, "An Open Letter," *Police Marksman*, July-Aug. 1986.

[75] Silver and Kates, "Handgun Ownership, Self-Defense and the Independence of Women in a Violent, Sexist Society," in D. Kates (ed.), *Restriction Handguns* at 144-47. Prof. Leddy, formerly a N.Y. officer, cites personal experience:

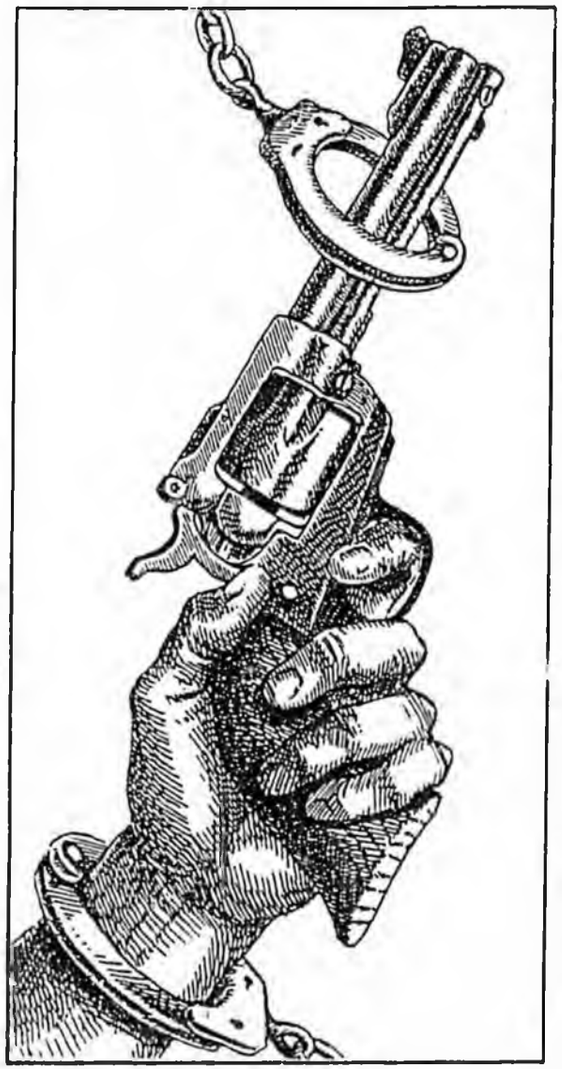
> The ability of the state to protect us from personal violence is limited by resources and personnel shortages [in addition to which] the state is usually unable to know that we need protection until it is too late. By the time that the police can be notified and then arrive at the scene, the violent criminal has ample opportunity to do serious harm. *I once waited 20 minutes for the New York City Police to respond to an "officer needs assistance" call which has their highest priority.* On the other hand, a gun provides immediate protection. Even where the police are prompt and efficient, the gun is speedier.

From "The Ownership and Carrying of Personal Firearms," forthcoming in *Int'l J. Victimol.* (Emphasis added). Cf. the Riss and Silver cases cited above, as well as *Wong* v. *City of Miami*, 237 So.2d 132 (Fla., 1970). All emphasize the need for judicial deference to administrators' allocation of scarce police resources as a reason for denying liability for failure to protect.

[76] *Wiener* v. *Metropolitan Transit Authority*, 433 N.E. 2d 124, 127, 55 N.Y. 2d 175, 498 N.Y.S. 2d 141 (N.Y. App. Div. 1982).

FORUM / LETTERS

Concealed weapons protect victims, not criminals



COMPASS
POINTS OF VIEW FROM OUR COMMUNITY

Let's get one thing straight at the beginning: Police don't protect. Period. In fact, they are required by law to react after a crime is either in progress or is over. Police retaliate.

The illusion of police protection is one of the great myths that I, as a self-defense for women instructor, have to overcome. One of the other myths is that if a woman pulls a gun on a bad guy, he will summarily take it away from her and use it on her. That doesn't happen either.

But back to the police. They have been very good at finding ways to protect themselves. The concern that C.E. Swackhammer, Ron Otte and Brian Porter have about HB 351 (the bill to allow concealed carry of firearms) is that the passage of this bill might make it more dangerous for police officers. It might, but it definitely would make it more dangerous for the criminals.

Supporters of this bill have pointed to the Florida experience as a way of demonstrating what the passage of this bill means.

In total, there are 13 states that allow concealed carry. To date, there has been no research on the effects of concealed carry that includes all of these states.

But information has been developed about the Florida experience by Florida State University criminologist Gary Kleck. According to his data, approximately 1 million times a year an armed citizen defends himself or his property. Ninety-six percent of the time, he merely brandishes the weapon or fires a warning shot. In 2 percent of the cases, the citizen actually shoots the assailant. While defending themselves with firearms, the armed Florida citizen ended up killing between 2,000 to 3,000 criminals each year since 1987 when the law was enacted. This is three times the number killed by police during the same time-frame.

In a nationwide study, Kates found that about 2 percent of civilian shootings involved the injury of an innocent citizen mistakenly identified as an assailant. The error rate for police, however, was 11 percent.

The difference in the "identification" problem is fairly easy to understand. If a citizen is standing at the bus stop of life and a bad guy comes up, pulls a knife and says, "Your money or your life," it is pretty obvious that a crime is in progress. Police, on the other hand, are usually not privy to that kind of exchange. They retaliate, after the fact, and try to sort out who did what to whom.

Self-defense laws, in general, favor protection of the police, the criminal justice system, and those who make their living off of those institutions. In short, if a citizen is going to act in self-defense, he must first try to run away. Failing that, he cannot escalate past what is being done to him (e.g., if the bad guy is unarmed, the good guy cannot start hitting the bad guy with a 2-by-4).

Then, once the bad guy is on the ground, the good guy must stop, wait for the bad guy to get up and present himself as a danger again before the good guy can act again. Additionally, the good guy can only use lethal force if he can prove to a jury that he was in fear of losing his life (or he was preventing another from losing his/her life).

If I had followed these guidelines as I fought my way through my early life, I wouldn't be alive today. Combat strategies that actually work will not fit neatly into those restrictive guidelines.

The fact is: Only the intended victim of a crime is in a position to: 1) establish that a crime is in progress, and 2) prevent that crime from occurring. No one else is in any position to do much of anything else except pick up the pieces — after the fact.

Another fact is: The handgun is the most powerful tool for prevention and protection that there is. A woman, trained in the use of a handgun, stands a good chance against the rapist, the estranged husband or boyfriend, the mugger, etc. FBI statistics say that in less than 1 percent of the cases reported did the assailant take a woman's gun away from her and use it on her. Again, compared to police giving their gun away, the citizen did better.

What does happen is that women are fully capable of defending themselves from violent attack:

- 92-year-old, wheelchair-bound Bessie Jones shot her assailants (USA Today, Nov. 10, 1993);
- After being blindfolded and raped, Madeline Morehouse reached the gun in her purse and held her rapist at gunpoint while she called the police (Seattle Times, May 13, 1993);
- "Woman Feeding Baby At Home Shoots Intruder" (San Antonio Express News, Aug. 10, 1993);
- "Widow of Police Chief Shoots Intruder" (Sacramento Bee, April 22, 1993).

The experience of the armed citizen is not that gun owners are homicidal, emotionally deranged, sub-human throwbacks who are just looking for an excuse to blow somebody away. They are, rather, decent, law-loving people who accept the fact that only they, the intended victims, can prevent crime.

J Bruce Bibee is a seventh-degree black belt. He is the owner of Kung-Fu San Soo Center, and he has been teaching women's self-defense classes since 1976.

NEWS ARTICLE

Move legislature to Wasilla

The new capital designation which is coming onto the ballot in the general election in

has been spent. Why not let those who misappropriated our money personally return it. Gov. Hickel, then-Attorney General Cole, Barnes, Halford and the rest of the legislature

SB 242

FISCAL NOTE

STATE OF ALASKA
1994 LEGISLATIVE SESSION

BILL NO. SB 242

Revision Date:
Dept. Affected: All State Agencies
Title: "An Act relating to office hours of State agencies." BRU:
Component:
Sponsor: Taylor
Requestor: (S) Sta
COMPONENT SERI/ NO.

Expenditures/Revenues (Thousands of Dollars)

OPERATING EXPENDITURES	FY95	FY96	FY97	FY98	FY99	FY00
PERSONAL SERVICES	0.0	0.0	0.0	0.0	0.0	0.0
TRAVEL	0.0	0.0	0.0	0.0	0.0	0.0
CONTRACTUAL	0.0	0.0	0.0	0.0	0.0	0.0
SUPPLIES	0.0	0.0	0.0	0.0	0.0	0.0
EQUIPMENT	0.0	0.0	0.0	0.0	0.0	0.0
LAND & STRUCTURES	0.0	0.0	0.0	0.0	0.0	0.0
GRANTS, CLAIMS	0.0	0.0	0.0	0.0	0.0	0.0
MISCELLANEOUS	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0
CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
CHANGE IN REVENUES ( )	0.0	0.0	0.0	0.0	0.0	0.0

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts	0.0	0.0	0.0	0.0	0.0	0.0
1003 GF Match	0.0	0.0	0.0	0.0	0.0	0.0
1004 GF	0.0	0.0	0.0	0.0	0.0	0.0
1005 GF/Program Receipts	0.0	0.0	0.0	0.0	0.0	0.0
1006 GF/MHTIA	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0
Total	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of current year (FY94) cost: none

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

ANALYSIS: (Attach a separate page if necessary)

Assumes that State agencies will continue to periodically assess the preferences and needs of clients with respect to accessing State offices.

Prepared by: Kevin Ritchie, Director
Phone: 465-4430
Division: Personnel/OEEO
Date:

Approved by Commissioner: Nancy Bear Usera
Date: 2/16/94
Agency: Administration

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(Rev. 10/93) ni 2/16/94

SB 244

Alaska Permanent Fund Corporation
P.O. Box 25500 Juneau, Alaska 99802-5500
(907) 465-2047

MEMORANDUM

DATE: April 12, 1994

TO: Senator Loren Leman
Chairman, Senate State Affairs Committee

FROM: William H. Scott
Executive Director

SUBJECT: **Senate Bill 244**

Senate Bill 244, introduced at the request by the Board of Trustees, would amend current law with respect to equity investing. Specifically, it would allow the Permanent Fund to purchase – under certain conditions – more than five percent of the stock of a corporation.

The bill sets out general policies and guidelines for alternative asset investing. The purpose of the alternative asset investment program is to prudently employ a modest percentage of Permanent Fund assets to alternative investments to produce a well-diversified, profitable portfolio which will enhance the Fund's total return. The goals of the program are: (1) to achieve superior total returns compared to traditional asset classes; and (2) to diversify away from traditional capital market risks.

Even though alternative investments as an asset class are employed by hundreds of public and private corporations and institutions around the country, including universities and state retirement systems, they would represent a new type of investment for the Permanent Fund. As such, it is understood that a significant amount of education will be required both within the Corporation and within the legislature before such investments would be initiated, even on a limited basis.

To begin the educational process, I am enclosing the following six attachments:

Attachment #1 is draft language for a proposed committee substitute for SB 244. This language, rather than focusing on the transaction mechanics of the new investments, more properly addresses alternative investments as simply a new asset class to be made available to your Fund managers for investment under the very stringent guidelines set forth by the Prudent Investor Rule. It is important to recognize that the particular selection criteria for each of these investments will most likely evolve and be adjusted over time as a result of the interaction between the staff, the Board and our consultants.

Attachment #2 is the Board of Trustees resolution dated December 6, 1993 in support of the original legislation. The Trustees adopted this resolution by a vote of five to one.

Attachment #3 contains excerpts from the minutes of the December 6 Board meeting in which Trustee Brady made the case for the proposed change.

Attachment #4 is the Executive Summary from the "1992 Survey of Alternative Investments by Pension Funds, Endowments and Foundations." This document indicates that investment by our peers in the asset class of alternative investments is widespread, significant and growing. For example, the top 200 funds in the U.S. and Canada currently have $36 billion invested; this represents 3.6 percent of the assets of those funds that allocate dollars to alternative investments.

Attachment #5 is a reprint from the Spring 1994 issue of *The Journal of Investing*. The headline of the featured article is "Alternative Investments Grow Rapidly at Tax-Exempt Funds." Interestingly, this article indicates that it is the largest funds which are most the active in alternative investing. In fact, of the 33 $10 billion-plus funds surveyed, more than 80 percent participate in at least one alternative investment asset.

Attachment #6 is a copy of a letter from Dave Rose, the Fund's previous executive director, stating his support for the legislation and his reasoning, as well as some thoughts about the specific prohibitions included in the proposed committee substitute.

The bottom line is that the Board wishes to have the authority contained in this amendment because we are convinced it will help us to do a better job protecting and enhancing the Permanent Fund. I would ask for your support and stand ready to provide additional information at any time.

#1

Be it enacted by the Legislature of the State of Alaska:

*Sec 1.AS.13.120.(g) is amended by adding a new paragraph to read:

(21) Notwithstanding 37.13.120(i), equity investments may comprise more than five percent of the stock of a corporation only through an interest in a partnership, or ownership in a collective investment vehicle, under the following conditions:

(A) the Fund shall not own more than a 60% interest in a partnership or collective investment vehicle;

(B) the aggregate investment of the Fund under this paragraph may not exceed five percent of the total investments of the Fund:

(C) at no time may the Fund own directly or indirectly, through a corporation, partnership or collective investment vehicle, more that 5% of any entity which has substantial oil and gas operations in the State of Alaska;

(D) appropriate policies and procedures for investments under this section shall be reviewed and approved annually by the Board of Trustees.

Attachment #2

RESOLUTION OF THE BOARD OF TRUSTEES OF THE ALASKA PERMANENT FUND CORPORATION PERTAINING TO LEGISLATIVE CHANGES IN THE ALASKA STATUTES RELATING TO ALTERNATIVE INVESTMENTS BY THE ALASKA PERMANENT FUND CORPORATION

RESOLUTION 93-12

BE IT RESOLVED, THAT the Board of Trustees directs staff to seek legislative changes to provide that, notwithstanding any other provision of law, but subject to the prudent investor provisions, the Alaska Permanent Fund Corporation may invest in the category of "Alternative Investment Strategies."

PASSED AND APPROVED by the Board of Trustees of the Alaska Permanent Fund Corporation, this 6th day of December, 1993.

Chairman, Board of Trustees
Alaska Permanent Fund Corporation

ATTEST:

Corporate Secretary

CHAIR SEEKINS: Yes. Mr. Brady.

MR. BRADY: I'm going to follow our senior Trustee's example of trying take the floor for a while and stand up here and talk to you about this subject. No offense, Mr. Freeman. I think Mr. Surz's presentation highlighted an opportunity here that wasn't presented necessarily by his presentation, but presented to you in the fashion of understanding of something that sounds to be very complicated and possibly even beyond the grasp of most of the activities we do, in your mind.

I probably am the one responsible for all of this today and it has to do with a number of things. Firstly, we've all concluded one way or another, I believe, that the strategy of diversification through asset allocation is the primary key to our success. As a matter of fact, I don't know how many of you saw this article in Forbes Magazine recently, with which I don't agree, but which basically asks why spend a lot of money with money managers because, if you just bought into S&Ps and saved all that money, you'd end up with approximately the same results? I don't concur that, over a long period of time, this is true.

If we're going to continue to grow in profit in the style and manner at which we've set our objectives, this horizontal development of asset allocation, I think, is very important to all of us. If we don't, that pyramid in the middle, our bonds, keeps getting bigger and bigger and we have a shallower horizontal allocation. I think that, to continue to diversify, we've got to continue to do this. We're in alternative investment strategy right now. That's all real estate is. We're betting on Pete and Llewellyn and others to find the deals that make the most sense. That's an alternative investment strategy. I don't want to confuse this with venture capital or with the other investment funds that the State of Alaska does. This is not building a water pipeline to California or buying into a gold mine. I think we're looking at here a strategy that would allow us to do some of the things that we're currently prohibited from doing.

For example, we're limited to the extent of 5% on any publicly traded equity. This summer, when all this started, I met some very bright fellows. We've heard over and over and over that the key to a lot of this is the people you find for your partners. I think that's true in any successful entrepreneurial enterprise. These guys and gals have rates of return that are phenomenal. They're doing partnerships with people like ourselves. If we had an alternative investment strategy of 5%, whether we fund it or not, by resolution we can restrict it however we wish. Let's say we don't want to do timber, although that's been very successful recently, we don't want to do dairy farms, we don't want to do gold mining, and we don't want to even get into

some of the IPOs or some of the other things that are happening. But, let's say that we wanted to partnership with some people who buy what they feel are undervalued small-cap, publicly traded companies, for whatever reasons. They can either influence the board or put themselves on the board or do things to maximize their rates of return that otherwise aren't happening. It may be that there's one senior shareholder that's got a large percentage of it and you can recapitalize, do all the things that need to be done to fix the company, and get the rates of return that company is likely to get being fixed, if you will.

Bill Scott and I met with these folks. These kinds of people are real interesting. I think this is something we ought to do. I don't think we should take 1% and throw it out there for a home run, but I think we should take some percentage as we broaden our diversification and look at opportunities with people and companies that are successful at making a lot of money.

By the way, although I know this doesn't carry a lot of weight with you, Mr. Freeman, almost everybody else is doing this. It is not just the swingers, the universities, and the colleges, but the public entities, the states, and the corporations are in this category. I got a sampling of this myself and over 100 entities similar to ourselves have an alternative investment strategy. That doesn't mean we take 5% of our money and threw it at the wall and say, "Do deals, whatever they are, and we just trust you." That's not the suggestion I have here. The suggestion I have here is that we pass a resolution that allows us to incorporate, in our legislative package, the ability to invest in alternative categories. Then, through our own means and devices, such as limitations as we talked about with real estate, we control through resolutions what it is we want and wish to do. I don't have anybody in mind. There's not many Duracell deals floating around. Those come around once in a while. There are, however, a lot of small-cap companies and other situations that come along that are good. The rates of return some of these people are generating are really good. As our oil revenues go down and other things take place, you could create a scenario that we ought to have other opportunities and ways to make money around here.

Having said that, the example that I tried to lay out here to do this is prohibited because, in many instances, we may find ourselves in a partnership wherein we would own more than 5% of a specific stock. We can't do that. But, if we had an alternative investment category and we invested with partners and it was understood that these investments, made from time to time, in most cases, we would find ourselves in a situation where we would have 20% to 30% of this partnership that would own 30% to 50% of a publicly traded company.

We just flipped over the edge. What I want to do is convince you, as best I can, that through our asset allocation and diversification, we should have this category. Once we have this category and the authority to do these sorts of things, then we come back and we look at the opportunities through presentations to learn the history, the track records, the benchmarks, and all the things we talked about earlier that we need and want to have to feel comfortable about this. Then, if we choose to do this, we can do it. Mr. Surz said it and Mr. Stone said it. Not just because everybody else is doing it. I do believe it's a missed opportunity, if we don't have ourselves positioned so that we can take advantage of these kinds of opportunities as they continue to come along.

With $80 million to $120 million a month coming in, the pyramid keeps getting bigger and we're shallower on our diversification. That's why I feel, after having learned a little bit about this from reading stacks of information and discussing those with Commissioner Rexwinkel, it's something we should be doing. The other board Commissioner Rexwinkel sits on is going to do it. We're not throwing something at the wall, closing our eyes, and looking out the corner to see what's going to happen. This is something that's got some premeditated thought to it and some pre-examination. I feel very strongly that this is something we should have in a resolution to be able to incorporate. I've got a copy of the New York statute, if anybody wants to see what they did. They just authorized up to "X" percent of their allocation for that category.

That doesn't force us into any position to have to do anything. It would just allow, if the timing is such that we can convince the Legislature we're right about this, the passage of legislation to authorize us to engage in these different opportunities, as they come along. Thank you.

CHAIR SEEKINS: Are there any comments? Mr. Freeman.

MR. FREEMAN: I would assume from your remarks, Mr. Brady, that a change in legislative authorization would be necessary for what you want to do?

MR. BRADY: I think so, only as respects, from what I understand, the potential of intentionally going out and having an indirect, but real, ownership in more than 5% of a publicly traded company. That's where the Legislature would have to come into play.

MR. SCOTT: If you can't do that, then you can't accomplish the types of private buy-outs involved here. If you can't own more than 5%, then you can't effectively operate in this arena.

It's interesting to me, and it may be just of incidental help, that it's been demonstrated over the years that higher tax rates dry up entrepreneurial capital. The only reason I make that point is that we're going into a period of higher tax rates, unless Congress and Clinton change their minds, and we're going to see a drying up of entrepreneurial capital and it may very well be that also demonstrates an opportunity for the institutional investor to take the place of some of that.

CHAIR SEEKINS: Commissioner Usera.

COMMISSIONER USERA: I'm wondering what is your experience in terms of the necessity of having staff involved. Did you feel that the Washington and Oregon funds felt it was necessary to staff up to do oversight of this process?

MR. STONE: It was interesting that, at the time we got involved, staff did it all. There was no outside expertise. To be honest with you, I don't think they increased their staff at all with respect to what they were doing. That's not true. In Washington, they added one person who was specifically involved in alternative investments.

COMMISSIONER USERA: The impression I get is that you do have to know what you're doing. You have to be tuned into it and not, like with passive investments, say that you'll check back in six months or a couple of years. Certainly, it requires close monitoring and having a sound communication system between the funds, as well as the gatekeeper and the company that's going to be a parent. If I'm hearing you right, what they're doing is saying they're in agreement and they collectively, as partners, are going to insure the success of this company by using these very best and brightest people who are going to go in and add value to the investment.

MR. STONE: That is true, to a certain degree. Let me add this. John was mentioning Paul Saylor earlier with respect to real estate. He is very well know and very good. Surprisingly, in this area there are some very good people. We found some excellent, if you will, Paul Saylor types who could monitor this and have done a very good job for Washington and Oregon.

COMMISSIONER USERA: They were on a contract basis?

MR. STONE: Yes. I'm not recommending adding staff. This guy talked earlier about smart people. There is some real talent out there in terms of companies who are overseeing this as consultants and advisors who do a wonderful job.

COMMISSIONER USERA: Mr. Chairman, could I ask just one other question? What is the competition for the good deals?

MR. STONE: What we found to happen is, in the 1980s, this asset category got flooded with money. I think that is one of the reasons you've got so many problems. What has happened now is a lot of that money has pulled back. That's in the form of insurance companies. Banks can't do it any more because the regulations have changed and they can no longer be involved in this type of asset category. So, the number of good deals have increased dramatically with the available dollar that's out there. The funds are having potential deals go across their table that are very attractive.

COMMISSIONER USERA: Do the deals come to you or do you go out and look for the deals?

MR. STONE: They come to the fund.

COMMISSIONER REXWINKEL: Mr. Chairman, I have a question. Do we have legislative authority to do some of these that Mr. Surz pointed out on page 2 of his presentation, which include hedged funds, market neutral, and managed futures?

MR. BRADY: No.

COMMISSIONER REXWINKEL: None of them?

MR. SCOTT: We can hedge individual positions, but not on a speculative basis.

CHAIR SEEKINS: Mr. Freeman.

MR. FREEMAN: I suspect that my feelings and position on this and my lack of enthusiasm doesn't come as a surprise to Mr. Brady. I don't want to make a long-winded pitch on the merits of it. I'll be a little more practical than that. I asked the question whether you thought this was going to require legislative approval and a change in the statute and I'm sure that it will. From a practical standpoint, how do I put that? One of the lessons I learned in politics is, once in a while, you try to do something you think should be done, but it's very unpopular politically. Even though something is unpopular, if you can get it done, it's a lose/win situation, as far as politics is concerned. But anytime you tackle something that's very unpopular and don't get the job done, all you've done is diminish your credibility, harmed your reputation politically, and haven't accomplished anything other than that.

From a practical standpoint. 1994 is an election year and you know, as well as I do, the concern that our politicians have for reaction from the public as far as tampering with the Permanent Fund. The chances of accomplishing the changes in the law that you need are just about nil. If you're not going to accomplish that and can't get the job done, I think it's harmful to the Permanent Fund with regard to the feelings of the public as far as the Permanent Fund Board of Trustees is concerned to attempt it, if you can't get the job done. You can do as you wish, but whether this is good or bad, there are a lot of people in the Legislature today that I served with years ago and were there when the Permanent Fund was created. They are well aware of the background, the history, and the philosophy all along the line and most of those people have enough seniority that they're in positions of reasonable influence today. When I have serious thoughts about the Permanent Fund, I don't hesitate to talk to them and I have a pretty good idea what are some of their feelings. Regardless of the merit of what you're trying to do, it's not going to happen. My suggestion would be to discuss it and whatever you want to do, but I wouldn't put my foot on the line to get it done. That's just my opinion.

MR. BRADY: Mr. Chairman.

CHAIR SEEKINS: Mr. Brady.

MR. BRADY: Mr. Freeman, I respectfully disagree. You know better than I the evolution of the investment strategy of this Fund. At one time, we didn't have a real estate portfolio. At one time, we didn't invest in stocks. We simply started with some bonds and some cash. I think that the Fund was late in making the proper decisions in those investment strategies. The results will bear that out.

Having said that, I don't think this is an attempt to hoodwink the Legislature. I'm attempting to, as convincing as I can be, go back to our asset allocation strategy and I think we can make awfully good sense to all of our legislators that the success in our Fund has been largely due to that, to date. I think we need to continue to broaden that. I don't know what's going to be coming next. You said $10 billion and I think it's more than that. Whatever it is, there are hedging opportunities through diversification that we're foolish to ignore. I believe this is one we should give very serious consideration and we should move forward in a continued asset allocation through diversification, if you will. What we end up purchasing, at the end of the day, remains to be seen. The fact is, the timing is here. As I spoke at the last Fund meeting when I said I wanted to bring this up, I said I wanted to bring in somebody who could try to explain that

this isn t something that is novel, new, or unique to one or two private investors, but this is something that's going on in lots of ways with lots of funds with lots of money.

The interesting thing is that this concentration of money is not in the traditional risk-takers. I say traditional risk-takers are typically colleges and universities. I guess they figure, if they lose some money, they can go back and get some more and have it replaced. They do swing more than the state retirement funds. Having said that, it's not just the colleges and universities, it's universal. I'm sorry that maybe we haven't had a work session prior to this to go through and exemplify some of the activities with proven results. I've had the opportunity of having done that and have seen those results. I see the future here and it's very clear to me that we're amiss, if we don't do this. If it's a gamble at this point in time because of politicians going off and being re-elected, I'm prepared to take that gamble because I feel that it's important to this Fund to be able to have this diversification. Then we can sit down and decide where it makes the most sense to go forward.

CHAIR SEEKINS: Mr. Brady, if you perhaps want to bring some action, you might want to do that during New Business.

MR. BRADY: I intend to do so.

CHAIR SEEKINS: Thank you very much. We are one-half hour behind on our agenda.

MR. SCOTT: Mr. Chairman, because we are one-half hour behind, could I intercede here? I have checked with Mr. O'Leary and he could switch to a point later on in the agenda. We do have Capital Guardian here to address you and one part of their presentation is going to be a conference telephone hook-up. Those people are ready and waiting and, if it's all right with you, I think we should go on to that one next.

CHAIR SEEKINS: We would like to then go ahead with **Capital Guardian**, who is right on time.

MS. YORBA: They had to go out and place a quick telephone call.

CHAIR SEEKINS: So, we will have two new items under New Business. One will be a real estate resolution and one will be dealing with alternative investments.

Mr. Scott, would you introduce the next presenters on the agenda, please?

Attachment #4

1992 Survey of Alternative Investments

By Pension Funds, Endowments and Foundations

Goldman, Sachs & Co. and Frank Russell Company
October 1992

Executive Summary

The 200 largest pension funds, endowments and foundations in the United States and Canada currently have $36 billion invested in alternative investments

Pension funds, endowments and foundations have invested significant assets in alternative investments(1) -- the top 200 funds in the United States and Canada(2) have invested $36 billion. This represents 3.6% of the assets of those funds that allocate dollars to alternative investments.

Alternative investments have, until recently, been the province of a small group of investors; participation is broadening significantly:

- 54% of all respondents participate in alternative investments
- Over 80% of funds with greater than $10 billion in assets participate in alternative investments

Buyout funds and venture capital have been the predominant investment strategies.

Limited partnerships are the most common investment vehicle; 80% of all alternative investment dollars are channelled through them.

There is a strong appetite for alternative investments *going forward:*

- 71% of all respondents plan to increase commitments to alternative investments
- Venture capital continues to dominate investor interest

(1) "Alternative investments" are defined as non-traditional investments that are illiquid and have a substantial equity component. See p.22 for a more complete definition.
(2) See p. 2 for a breakdown of institutions surveyed. A smaller survey of 72 of the top 100 pension funds in the U.S. and Canada was performed by Goldman Sachs in 1991.

#5

THE JOURNAL OF INVESTING

A PUBLICATION OF INSTITUTIONAL INVESTOR, INC.

VOLUME 3 NUMBER 1 SPRING 1994

ALTERNATIVE INVESTMENTS GROW RAPIDLY AT TAX-EXEMPT FUNDS

Reprinted from the Spring 1994 issue of The *Journal of Investing*
488 Madison Avenue, New York, NY 10022

Alternative Investments Grow Rapidly at Tax-Exempt Funds

THOMAS J. HEALEY

is head of the Pension Services Group at Goldman, Sachs & Co. in New York. He joined Goldman in 1985 in charge of real estate capital markets and became a partner in 1988. Mr. Healey was previously the assistant secretary for domestic finance at the U.S. Treasury Department in Washington. He holds an A.B. degree from Georgetown University and an M.B.A. from Harvard.

DONALD J. HARDY

is the director of Private Investment Services at the Frank Russell Company in Tacoma, Washington. He has been with Frank Russell since 1977. Mr. Hardy has more than twenty-five years of investment experience, and has previously been a fund manager, a securities analyst, and a trust officer. He holds a B.S. from Boston University and an M.B.A. from the University of San Francisco.

When interest rates on U.S. Treasury bills dipped below 3% last summer to their lowest level in thirty years, investors and the public alike were caught by surprise.

But no one was more alert to this drop than pension fund managers. These specialists knew that the continuation of this trend could make it difficult to match the high investment returns of the 1980s.

One look at the figures illustrates the problem: between the end of 1991 and the end of 1992, total returns on equities dropped from 33.0% to 9.0%; on cash, from 5.75% to 3.61%; and on fixed-income investments, from 16.1% to 7.6%.[1]

NEW ASSET CLASSES IN SPOTLIGHT

Tax-exempt funds, appropriately, are exploring new ways to increase returns. One result is greater interest in categories like alternative investments, which have a strong potential for higher returns.

A number of studies have shown that private U.S. equities produced returns of 18% or 19% during the latter part of the 1980s, while some leveraged buyout funds did considerably better.

Of course, the illiquidity of these private investments makes them subject to greater due diligence and oversight. But the results can be worth it, especially when other potentially high-yielding asset classes like real estate are still under water.

Additionally, with traditional sources of capital like insurance companies and banks facing major constraints, tax-exempt funds find themselves in a new role — providing a much more active source of capital. They are offered a much wider range of private investment opportunities at extremely attractive returns.

Yet this asset category still suffers from one major problem, along with its potential cyclicality and relative youth: Very little systematic data are available. Funds traditionally have been secretive about their most successful alternative investments, and the variety of strategies involved has made it hard to develop useful benchmarks.

To start building a more accurate picture,

Goldman, Sachs & Co. and the Frank Russell Company joined forces last summer to launch the first truly comprehensive study of this investment category. The study requested data on alternative investment participation from the 228 largest tax-exempt funds in the U.S. and Canada (assets ranging from $500 million to $68 billion).

194 (85%) of the 228 funds contacted responded, a remarkably high response rate (Exhibit 1). The results of the study, entitled "1992 Survey of Alternative Investments by Pension Funds, Endowments and Foundations," were released in the fall of 1992.

STRONG PARTICIPATION IN ALTERNATIVE INVESTMENTS

This article discusses the findings of the survey, using the terms tax-exempt fund and investor interchangeably to refer to respondents. Percentages are rounded in the text and shown to the nearest tenth of a percentage point in the exhibits.

The survey defines alternative investments (AI) as illiquid private investments that have not been registered with the Securities and Exchange Commission. It focuses on eight different types of strategies within the asset class, strategies typically grouped together under the rubric of "alternative investments."[2]

These strategies are buyout funds, venture capital, mezzanine financing, oil and gas programs, distressed companies, targeted investments, timberland (and/or farmland), and other. All strategies involve an equity or equity-like component (Exhibit 2).

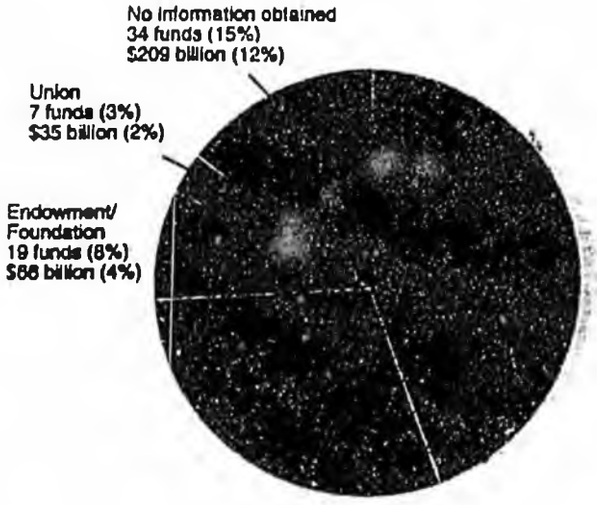
LARGEST FUNDS MOST ACTIVE IN THIS MARKET

One of the most impressive findings of the survey is the fast growth rate of this asset class. The assets held by tax-exempt funds have tripled over the past six years.

More specifically, in 1986 about one-third of the respondents in the survey held $12 billion in this investment category (Exhibit 3). Today over half (54%) have invested a total of $36 billion in alternative investments. This is a compound annual growth rate of 20%.

The survey reveals that the largest funds are most active in alternative investing (Exhibit 4). These investors dominate the asset category. By and large, they are the ones that have committed professional staff and developed consistent strategies within this

EXHIBIT 1
SURVEY PARTICIPATION: BREAKDOWN OF FUNDS SURVEYED



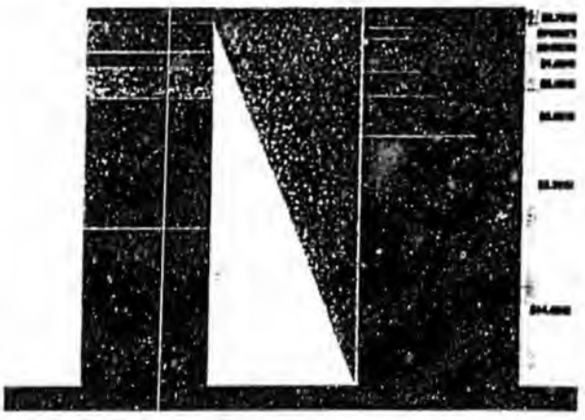
Total Funds Surveyed = 228, representing $1.7 trillion assets
Total Funds Responding = 194, representing $1.5 trillion assets

investment category.

Over 80% of investors with assets of $10 billion or more participate in at least one alternative investment asset. Put another way, thirty-three funds with assets of $10 billion or more account for 69%, or $24.6 billion of all alternative investment assets.

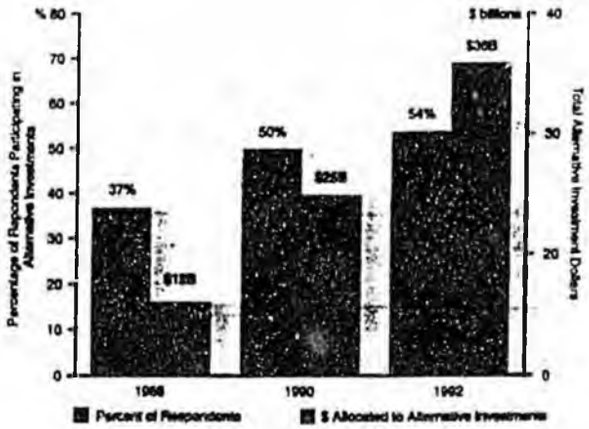
Among the remaining funds, those with assets from $5 billion to $9.9 billion account for only

EXHIBIT 2
ASSET ALLOCATION



Sources: *Pensions & Investments*, Goldman Sachs/Frank Russell 1992 Survey.

EXHIBIT 3
Estimated Growth of Alternative Investments



17.9%, or $6.4 billion, while funds with under $5 billion have 13%, or $4.8 billion, in AI assets.

The largest funds certainly have significantly greater resources to investigate opportunities in this market. They also have the potential to obtain better returns and gain more control than smaller players. Furthermore, large funds can make significant investments in private equity without exceeding their asset allocation guidelines.

For example, funds with over $10 billion in assets commit, on average, $750 million to AI assets, versus a mere $106 million for funds under $4 billion (Exhibit 5). Yet alternative investments comprise only 3% of total assets for these giants, compared to 5% for the funds with under $4 billion in assets.

EXHIBIT 4
Participation in Alternative Investments by Fund Size

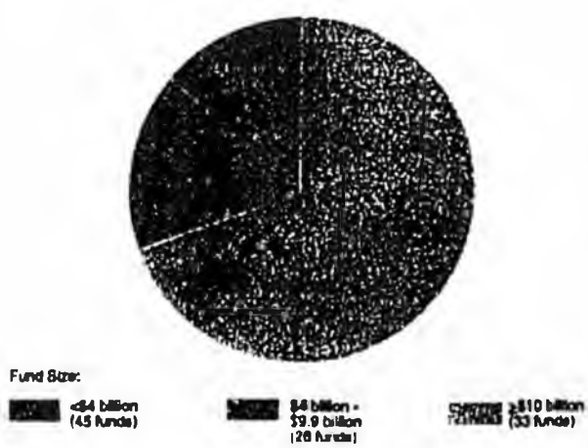
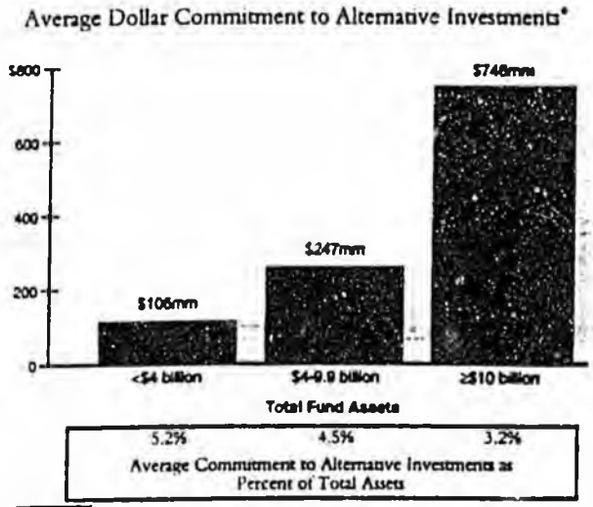


EXHIBIT 5
Average Allocation to Alternative Investments by Fund Size



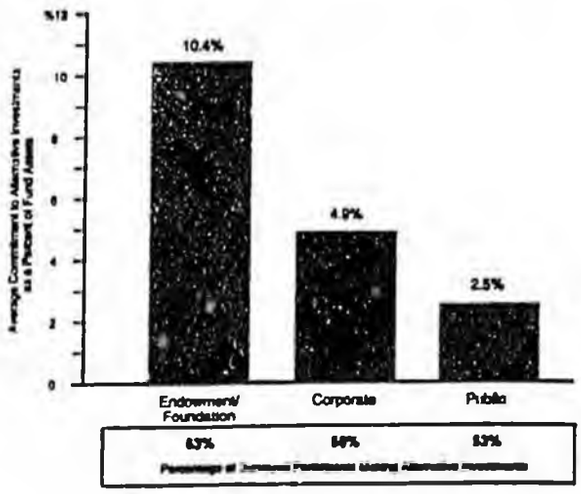
*Includes all funds committed whether drawn down or not.

This does not mean that smaller funds cannot invest efficiently in alternative investments. It just means that when they do, the investment usually involves a larger portion of their asset allocation. And it usually means that they invest more heavily in certain types of AI investment than do their larger peers.

BEHAVIOR DIFFERS BY FUND TYPE

The historical behavior of tax-exempt funds differs not only by fund size, but also by fund type (Exhibit 6). Endowments and foundations were the

EXHIBIT 6
Alternative Investments by Fund Type



first to enter this market, investing steadily in the 1970s and 1980s. This early involvement probably stemmed from the long-range thinking of their boards, as well as a shorter chain of command. Even today, these funds are the most committed to alternative investing, keeping 10% of their assets in AI funds versus only 5% for corporate funds and 3% for public funds. Despite their smaller size, endowments and foundations continue to commit a greater portion of their assets to alternative investments than corporate or public funds.

Corporate and public funds did not start participating heavily in this market until 1982. Today their total investment in this asset class far surpasses the others. This fact is probably more a function of their size than a greater commitment.

In fact, corporate funds today lead their public fund peers, although the public funds appear to be catching up. With the possible exception of targeted investments (assets with a special component such as a social or geographic imperative), union pension funds that flirted briefly with the idea of alternative investing seem to be sitting on the sidelines. This may be the result of membership constraints.

THE EIGHT MAJOR INVESTMENT STRATEGIES

Our study breaks alternative investments into eight different investment strategies (Exhibit 2). Some of these, like venture capital and oil and gas programs, have been around for years, and thus have solid track records.

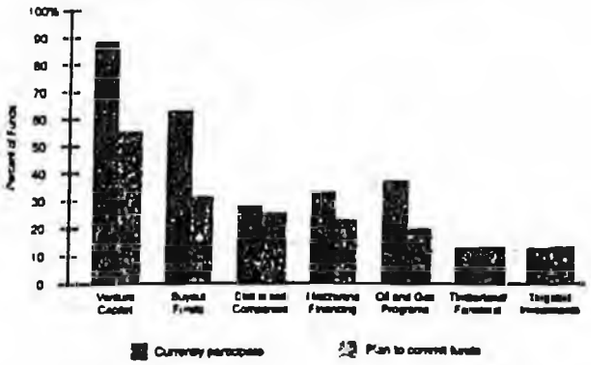
But others came of age in the 1980s. These include several corporate finance-related strategies such as leveraged buyout equity funds (LBOs), mezzanine financing (subordinated debt), and distressed companies (restructuring or bankruptcy funds). The remaining strategies include farmland and/or timberland and "targeted investments."

The alternative investment assets of respondents that did not provide a detailed breakdown were assigned to the "other" category. Coinvestments and project financings are likely to be among the investments in this category.

Inclusion of these newer strategies dramatically expands the AI category. This expansion has given AI assets more importance in the overall asset mix and is probably the reason why alternative assets are considered such an important, newly recognized asset class today.

EXHIBIT 7
FUND PARTICIPATION BY INVESTMENT STRATEGY

Percent of Funds that Participate in Each Investment Strategy and Plan to Commit Initial/Additional Funds



FUNDS DIFFER IN THEIR INVESTMENT MIX

When tax-exempt funds first consider AI investing, they usually start with venture capital, complementing it with one or two other strategies. Within this structure, most investors do not seem to have one preferred plan for AI asset allocation.

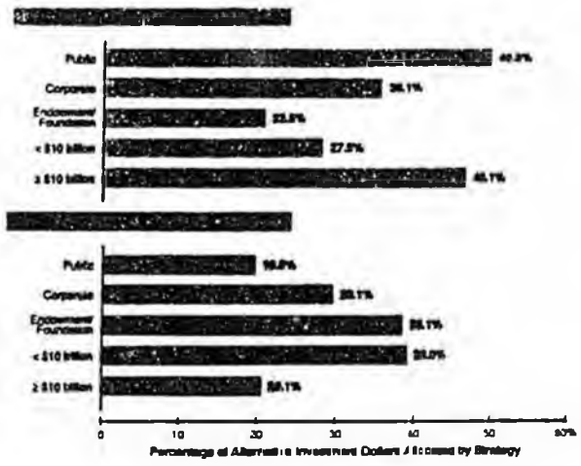
Given this pattern, it is no surprise that venture capital is the most popular asset on a participation basis (Exhibit 7). Almost 90% of the funds with alternative investments have allocated some dollars to this strategy. Investors also report that they are more interested in investing in venture capital in the future than in any other investment strategy.

Even though venture capital attracts more participants, however, it attracts far fewer dollars than leveraged buyouts (Exhibit 2). Investors have invested $9 billion in venture capital versus $14 billion in buyout funds.

LBOs represent 41% of all AI assets, which makes them the largest AI investment component (Exhibit 2). Venture capital comprises 26% of all AI assets, while mezzanine financing accounts for 10%. These top three strategies represent 77% of all AI assets. Of the remaining 23%, investors have put 7% in oil and gas programs, perhaps because these have been around the longest, 4% in distressed companies, 3% in targeted investments, 2% in timberland or farmland, and 6% in "other."

The popularity of LBOs is related to the size of each investment. Despite the attraction of venture capital, it is difficult for investors to commit large amounts of assets to these deals because of the small

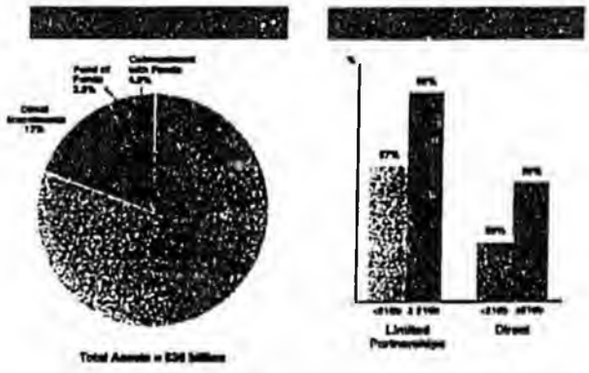
EXHIBIT 8
LEADING STRATEGIES: INVESTOR PROFILES



size of individual venture investments.

Leveraged buyouts, however, give equity investors an opportunity to commit large dollar amounts in far fewer deals. In doing this, the investor usually purchases significant control of a company. Given the asymmetry between the two most popular AI strategies, it is not surprising that large investors and public funds, in particular, gravitate toward buyout funds, while smaller investors, endowments, and foundations focus on venture capital (Exhibit 8).

EXHIBIT 9
INVESTMENT PROCESS — VEHICLES*



*Limited partnerships and other commingled vehicles.

Coinvestment/Add-on Investment with Funds: The investor invests in parallel with or in different securities from the Limited Partnership.
Fund of Funds: A multiple-manager vehicle with investments in more than one fund.
Direct Investments: The investor does not use an intermediary such as a Limited Partnership or Fund of Funds.

The largest funds keep 46% of their AI assets in buyout funds, while public funds keep 50%. On the other hand, smaller funds have 39% of their assets in venture capital, while the largest invest only 20% in that strategy.

REASONS FOR INVESTING IN THIS ASSET CLASS

The study examines the main reasons funds invest in alternative investments. Predictably, 63% said they were looking for superior returns. But another 33% said their main motive was diversification. This is understandable because the volatility of this asset class has a low correlation with other asset classes. Of the remaining participants, 2% said they are looking for an inflation hedge, while 2% believe these assets enhance their reputation.

The lack of information about alternative investing has made it difficult to understand the investment process itself. To clarify this, the study looks at three different aspects of the process: the choice of investment vehicle; organization and decision-making; and monitoring and measurement.

THE POPULARITY OF LIMITED PARTNERSHIPS

Limited partnerships are by far the most popular investment vehicle, accounting for 80% of all alternative investment dollars (Exhibit 9). Direct investment accounts for 13%, while coinvestment with funds represents 4% and fund of funds are 3%.

With limited partnerships, investors can rely on outside experts for assistance in making their investment decisions. This is particularly helpful for smaller investors with limited staff.

Although many investors reported seeking out coinvestment opportunities with general partners, only the largest funds have been able to do this on a consistent basis. To date, coinvestment attracts approximately $1.6 billion.

The study shows that limited partnerships have been, and will likely continue to be, the primary vehicle for alternative investing (Exhibit 9). But it also reveals that certain pressures are changing the typical partnership structure. As pension funds gain more experience in alternative investing, they want to take a more active role.

For instance, investors rank negotiating terms and conditions as the most important contractual issue. Additionally, investors are putting pressure on

partnerships to establish priority returns and to reduce the carry from the traditional 20%.

While some investors do not emphasize these cost issues, they do search for general partners that put their own capital at risk rather than relying solely on investors' capital. Overall, the bottom line seems to be a trend toward selecting a general partner with whom the investor can forge long-term partnerships.

Although direct investment is the second favorite investment vehicle, with 13% of alternative investment dollars, it is difficult to gauge whether more funds are going to move toward this vehicle in the future. There is no consensus on the subject.

Clearly, the largest and most experienced funds are those that do the most direct investing. They are also the ones that plan to do the most direct investing in the future (Exhibit 9). For example, 50% of the investors with over $10 billion in assets plan to commit additional funds through direct investing, compared to only 25% of the smaller funds.

Direct investing allows the larger funds to avoid the fees charged by general partners. Many smaller funds say they would like to do more direct investing, but they simply do not have the resources, time, or staff to do the necessary groundwork.

DECISION-MAKING

Participation in alternative investments brings with it a unique set of risks and rewards. As private investments, these assets are much less liquid than traditional stocks and bonds. Thus the due diligence process is different, more complex, subjective, and more judgmental. In addition, investments must be held longer than many others to yield the expected results.

To determine whether investors handle this category differently, the study looks at who is responsible for the decision-making process, including the initial decision to participate in alternative investments; allocation by strategy; and, finally, selection of individual investments.

The study shows that top-level management exercises unusually strong control over this entire three-tier process. The investment committee or board of directors maintains total control over the first two decisions virtually 100% of the time. They maintain control over the selection of individual investments about two-thirds of the time. When they do give up control, the board or investment committee delegate the third tier of decisions to the chief investment officer or other professional staff 29% of the time and to an outside consultant 6% of the time.

Nearly half (49%) of the investors use outside consultants to help evaluate or manage this asset category. The study defines consultants as external advisors who provide either non-discretionary advice or handle selection and oversight of investments on a discretionary basis.

Looking at the specific functions performed by these advisors, survey respondents said they use consultants in an advisory capacity (22%), to handle due diligence (18%), to take on the entire decision-making process (6%), and as Qualified Plan Asset Managers (QPAMs) (3%).

MONITORING AND MEASUREMENT

There is no consensus among respondents about how to measure performance in this asset category. Although 52% report using a benchmark, there appears to be little consistency. Many funds consider their benchmarks to be proprietary information.

When it comes to measuring actual performance, most investors report turning this task over to the internal staff or the trustee bank. The respondents are split on measurement methods. 53% use internal rate of return as their primary method; 48% use time-weighted rate of return; and 16% use cash on cash.

A large majority of respondents (84%) say they would welcome development of generally accepted performance measurement standards for this asset class.

THE FUTURE OF ALTERNATIVE INVESTMENTS

Looking toward the future, 71% of the funds say they intend to expand their alternative investment assets in the future. This answer suggests a strong appetite for these investments. More specifically, the funds selected four strategies as most popular going forward: venture capital, buyout funds, distressed companies, and mezzanine financing.

Investors were also asked which *single* investment strategy they would favor if they were just starting out. The three top choices were venture capital (39%), buyout funds (16%), and mezzanine financing (8%), in that order.

However, when asked to select *three* investment strategies, investors still rank venture capital first (81%), but mezzanine financing is second

(56%) and buyout funds third (52%). This suggests that venture capital and mezzanine financing may be the leading alternative investment strategies in the future.

GREATER OPPORTUNITIES FOR INVESTORS

The timing seems right. Today, the economy has started to expand. Yet many traditional lenders are still relegated to the sidelines until they solve their own capital adequacy and loan problems.

In the meantime, pension funds, endowments, and foundations are filling this gap. These tax-exempt investors have suddenly become a much more important source of capital to the economy as a whole. Thus, they receive a much larger flow of more sophisticated transactions to evaluate and select from. And many of these transactions fall into the alternative investment category.

To evaluate and track these transactions may take more expertise than other investments. But with the potential for double-digit returns, clearly the rewards justify the extra effort.

It is clear today that alternative investments offer investors an unusual opportunity. By investing in these strategies, tax-exempt funds may achieve both the higher returns and the diversification they will need in the 1990s to succeed in the new, lower-return investment environment.

ENDNOTES

The authors wish to thank for their assistance with the research and preparation of this article: W. Blair Garff, Matthew A. Bernstein, and Jill Byatt of Goldman, Sachs & Co.; Sharon L. Hammel, Holly F. D'Annunzio, Heide L. Berger, and Sandra M. Sullivan of The Frank Russell Company; and April W. Klimley of Klimley Communications.

[1]Sources for these figures: equities, the Russell 1000 index; cash, ninety-day Treasury bills; fixed-income, the Lehman Brothers Long-Term High Quality Government/Corporate Bond Index.

[2]Following is how the study defines the eight strategies commonly considered alternative investments:

Venture capital: Equity investments in companies that have undeveloped or developing products or revenue.

Buyout funds: Equity investments in public or private companies that result in the purchase of a significant portion or majority control of the company.

Distressed companies: Investments made through the purchase of debt or trade claims in companies that are in financial distress, restructuring, or bankruptcy.

Mezzanine financing: Investment in the subordinated debt of privately owned companies. The debtholder participates in equity appreciation through conversion features such as rights, warrants, or options.

Oil and gas programs: Investment in the exploration for oil and/or gas reserves or in the development of proven reserves.

Timberland or farmland: Investment in land to harvest timber or farm commodities.

Targeted investments: Investments that have a special component, usually related to geographical, economic, or social issues. These investments are sometimes referred to as "ETIs," or "economically targeted investments," and include investment in minority-owned businesses and state-financed housing.

Other: This category is a catchall that includes assets that respondents did not break down into individual strategies. Coinvestments and project financings may be among the investments in this category.

#6

Alaska Permanent
Capital Management Company

900 West Fifth Avenue, Suite 701
Anchorage, Alaska , 99501

Phone: (907) 272-7575 Fax: (907) 272-7574

February 2, 1994

Mr. Carl Brady, Jr.
Board Member
Alaska Permanent Fund Corporation

VIA COURIER

Dear Carl:

Thank you for providing a copy of the Permanent Fund Trustees' Resolution 93-12 which sets in motion a legislative request to authorize Alternative Investment Strategies. Thank you, also, for a copy of the proposed legislation and the analysis thereof.

At the outset, allow me to comment that this proposal appears to have been well thought out. The Trustees started with the broad concept of Alternative Investments (which could have involved everything from investments in timber, agricultural land, and venture capital) and quickly narrowed it down to investments in corporate stock.

Having established that focus, certain important investment parameters were wisely established:

1. **Other institutional co-investors are required** This insures that additional participants—institutional investor peers— scrutinize each transaction.

2. **A significant level of other institutional participation is established.** When the Fund started real estate investing, it used the same approach and it provided for the important useful exchange of information between large funds. It also provided a needed comfort and confidence level and "eased" us into investments and relationships over time. This gave us an opportunity to expand our knowledge, increase our returns and revise and establish policy over a long protracted period.

3. **A cap is placed on the amount of such investment.** This is wise as it controls the amount of non-diversification which could occur and restricts the Fund to activity in the small and medium capitalization company field. You won't be able to join in the Paramount takeover under this legislation; and you shouldn't!!

COPY

FISCAL NOTE

STATE OF ALASKA
1994 LEGISLATIVE SESSION

BILL NO. Senate Bill No. 244

Revision Date:

Dept. Affected: Department of Revenue

Title: "An Act relating to investments of the permanent fund in certain limited partnerships each of who principal purpose is investment in securities of public or private companies; and providing for an effective date."

BRU: APFC

Component: APFC

Sponsor: Senate Rules Committee by Request.

Requestor: SenateState Affairs.

COMPONENT SERIAL NO. 109

Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY95	FY96	FY97	FY98	FY99	FY00
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL	200.0	206.0	215.0	223.0	232.0	240.0
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	200.0	206.0	215.0	223.0	232.0	240.0
CAPITAL						
REVENUE FUND SOURCE:						

FUNDING: (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other (Corporation Receipts - 1022)	200.0	206.0	215.0	223.0	232.0	240.0
TOTAL	200.0	206.0	215.0	223.0	232.0	240.0

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year (FY94) Impact: $ -0-

ANALYSIS: (Attach a separate page if necessary) The Corporation intends to begin expending money for due diligence relating to these investments on July 1, 1994. These costs will include a "gatekeeper" fee similar to current real estate advisory fees; and will increase annually at the 3.75% inflation rate.

Prepared by: William H. Scott, Executive Director — Phone: (907) 465-2047
Division: Alaska Permanent Fund Corporation — Date: April 12, 1994

Approved by Commissioner: Darrel J. Rexwinkel, Commissioner — Date:
Agency: Department of Revenue

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4. An effort is made to specifically exclude companies in the oil and gas sectors who may operate in Alaska. This, too, is prudent in that it would be wise to avoid even the appearance of involvement in this sector in an oil and gas state.

I think that you and the Trustees have done a fine job and that the request for the legislation is reasonable and well thought out. You are to be commended on reaching for the opportunity to increase bottom line yield and the passage of the legislation will permit that.

Finally, allow me to observe that the current legislative draft is adequate and will permit you to do the job. It is not as artfully written as I would have preferred because it appears to be preoccupied with the business form of how a transaction might be put together rather than the investment itself. Each transaction is different and it could be a limited partnership, a joint venture, a corporation, etc. Each venture might use a financial adviser, a consultant, a brokerage merger and acquisition team, etc. If I had a chance to rewrite the legislation, I would dwell on the investment, not who pulls the deal together and how it is organized.

I have taken the liberty of enclosing my view of more focused legislative verbiage.

As always, thanks for giving me an opportunity to comment. I enjoy being "kept in the loop" and hope that I have been constructive.

Please give my regards to the other Trustees.

Sincerely,

David A, Rose
Chairman

PERMANENT FUND

BOARD: Board of Trustees of the Alaska Permanent Fund Corporation

BOARD IDENTIFICATION NUMBER: 076

DEPARTMENT: Department of Revenue

AUTHORITY: AS 37.13.040

STATUS: Active

REQUIREMENTS: Financial Disclosure

PROHIBITIONS: Conflicts of Interest - Ownership of interest in entities in which corporation assets are invested; public members may not hold any other state or federal office/position except as a member of the armed forces.

TERM: 4 years

DESCRIPTION: 6 members appointed by Governor: 4 public members (may not hold any other state or federal office, position or employment, either elective or appointive, except as member of armed forces) with recognized competence/wide experience in finance, investments, or other business management-related fields; 2 heads of principal departments, 1 being the Commissioner of the Department of Revenue; board elects chair; vacancies to be filled promptly; terms of public members shall be staggered so that no more than one term of a public member expires each year.

FUNCTION: Manage and invest the assets of the permanent fund and other funds designated by law.

CHAIR: Board elects.

SPECIAL FACTS: Quorum - 4 members; may be removed by the Governor with a written explanation; report (by September 30) to Governor/Legislature/public.

COMPENSATION: Standard Travel and Per Diem. Public members receive honorarium of $400 per day.

MEETINGS: 8 times per year; 10 days total.

FOR FURTHER INFORMATION CONTACT: Mr. William H. Scott, Executive Director, Alaska Permanent Fund Corporation, P.O. Box 25500 M/S 0401, Juneau, AK, 99802 5500, Phone: 907 465 2047, Fax: 907 586 2057

STATE OF ALASKA
Boards and Commissions

Membership Roster
PERMANENT FUND (076)

Member	Appointed	Reappointed	Term Exp.
Nancy Bear Usera Commissioner/Principal State Department Comm/DOA/P.O. Box 110200 Juneau, AK 99811-0200	11/27/91		
Carl F. Brady, Jr. Public 2100 Atwood Drive Anchorage, AK 99517	02/01/91	07/01/92	07/01/96
Oral E. Freeman Public 2743 Third Avenue Ketchikan, AK 99901	02/01/91		07/01/94
John T. Kelsey Public P.O. Box 527 Valdez, AK 99686	03/06/87	07/01/91	07/01/95
Darrel J. Rexwinkel Commissioner/Revenue Comm/DOR/P.O. Box 110400 Juneau, AK 99811-0400	10/01/91		
Ralph C. Seekins Public -- Chair 1625 Old Steese Highway Fairbanks, AK 99701	02/01/91	07/20/93	07/01/97

(Revised December 23, 1993)

FISCAL NOTE

STATE OF ALASKA
1994 LEGISLATIVE SESSION

BILL NO. Senate Bill No. 244

Revision Date:

Dept. Affected: Department of Revenue

Title: "An Act relating to investments of the permanent fund in certain limited partnerships each of who principal purpose is investment in securities of public or private companies; and providing for an effective date."

BRU: APFC

Component: APFC

Sponsor: Senate Rules Committee by Request.

Requestor: SenateState Affairs.

COMPONENT SERIAL NO. 109

Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY95	FY96	FY97	FY98	FY99	FY00
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL	200.0	206.0	215.0	223.0	232.0	240.0
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	200.0	206.0	215.0	223.0	232.0	240.0
CAPITAL						
REVENUE FUND SOURCE:						

FUNDING: (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other (Corporation Receipts - 1022)	200.0	206.0	215.0	223.0	232.0	240.0
TOTAL	200.0	206.0	215.0	223.0	232.0	240.0

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year (FY94) impact: $ -0-

ANALYSIS: (Attach a separate page if necessary) The Corporation intends to begin expending money for due diligence relating to these investments on July 1, 1994. These costs will include a "gatekeeper" fee similar to current real estate advisory fees; and will increase annually at the 3.75% inflation rate.

Prepared by: William H. Scott, Executive Director — Phone: (907) 465-2047
Division: Alaska Permanent Fund Corporation — Date: April 12, 1994
Approved by Commissioner: Darrel J. Rexwinkel, Commissioner — Date: 4/14/94
Agency: Department of Revenue

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(Rev 11/92) 93fisno xls/DBR

'ermanent Fund changes asked

BRIAN S. AKRE
ASSOCIATED PRESS

The Alaska Permanent Fund ard of trustees wants legislative rmission to invest a portion of e state's oil-wealth savings ac- unt in limited partnerships.

But one trustee questions the sdom of putting hundreds of mil- ons of dollars into limited part- erships, an area of investments e considers too broad and risky.

The trustees also are asking awmakers to lift the restriction hat prevents the fund from invest- ng in more than 40 percent of any uilding or other real estate.

Supporters say the changes would allow the fund to adapt to a changing investment market and continue bringing in high returns that lead to larger dividends for Alaskans.

The two changes are in Senate Bills 244 and 245, introduced on behalf of the board. Both are scheduled to have their first hearing Friday before the Senate State Affairs Committee.

SB244, the limited partnership bill, is expected to generate the most debate.

Limited partnerships are investments usually sold through brokerage firms. Investors put up cash that typically goes toward real estate, stock or major developments, such as oil and natural gas drilling projects.

The limited partners risk only their investment, while the general partner who puts the deal together assumes the legal liability. In return, investors can receive income, capital gains and tax benefits.

The board wants legi ative permission to invest some of the state's savings in limited partnerships, which carry a higher return but also a higher risk.

Under state law, the Permanent Fund invests only in domestic and foreign stocks, government bonds, real estate, mortgage securities and Treasury bills.

SB244 would only allow investments in limited partnerships that are principally invested in corporate stocks. It would require the general partner to have at least five years experience managing large securities investments. The fund could contribute no more than 60 percent of the capital for the investment.

Total investment in limited partnerships could not exceed 5 percent of the Permanent Fund, or about $750 million under the fund's current value.

The legislation has been narrowed for legislation that would allow investments in the far broader category of "alternative investment strategies," which also includes leveraged buyouts, oil and gas projects, and commodities such as timber.

The board, on a 5-1 vote, approved a resolution directing its staff to seek such legislation.

But the staff "toned down" the legislation in light of trustee Oral Freeman's objections, research officer Jim Kelly said.

"It was just too wild. He didn't think in an election year the Legislature would give the board the authority, basically, to do anything it wants to do."

There initially were concerns that the change was being pushed as a way to get the fund to invest in the trans-Alaska natural gas pipeline, which Gov. Walter J. Hickel has promoted for years.

But SB244 would specifically prohibit investment in limited operations in Alaska.

Freeman cast the only dissenting vote on the alternative investment resolution. He still opposes the narrower legislation that resulted, saying the term "limited partnership" is too vague.

Freeman said Monday that while limited partnerships pro ise greater returns, they al come with greater risk of big losses.

Senate President Rick Halford, R-Chugiak, referred both bills to four committees each – a long path to travel through one chamber. He did not return phone calls for comment Friday and Monday.

Rep. Terry Martin, R-Anchorage, said the Legislative Budget and Audit Committee introduced the bill Friday simply to open up the issue for discussion. He, too, doubted it would go far.

SB245, which would remove the provision in state law that says the fund cannot own more than 40 percent of any real estate investment, has a better chance of gaining passage, Martin said.

The fund began investing in real estate in 1983. The 40 percent limit was intended to reduce the risk of being a novice investor by allowing the fund to use the expertise of experienced partners.

In a recent memo to the board, Pete Jeans, the fund's real-estate

SB

245

Alaska Permanent Fund Corporation
P.O. Box 25500 Juneau, Alaska 99802-5500
(907) 465-2047

MEMORANDUM

DATE: December 27, 1993

TO: William H. Scott
Executive Director

FROM: Pete Jeans
Real Estate Investment Officer

SUBJECT: Elimination of 40% restriction on real estate acquisitions

This memorandum should be attached to the memorandum dated November 18, 1993 to the Board of Trustees as additional information.

The following three investment opportunities are examples that were lost by APFC during the past three months due to the 40% restriction on real estate acquisitions.

1. Park 227
Industrial Property
Kent, Washington

This proposal was received from the L & B Group. The proposed investment included 39 acres with 5 industrial buildings, 100% leased. The total purchase price was $26,500,000 and the initial cash on cash was 9% after fees.

After preliminary review, APFC decided to move forward and hired Saylor Capital to perform in-depth due diligence. APFC was considering 40% and the Public Employees Retirement Association of Colorado (PERA) was considering the remaining 60%. The due diligence was completed by both APFC and PERA and the decision was made to proceed with documentation. During this process, APFC and its attorneys could not negotiate acceptable buy-sell arrangements and were forced into backing out of this investment. PERA is proceeding to do 100%. The interesting thing on this investment is that it was presented to the APFC first, and we recommended PERA to the L & B Group as a potential partner.

2. 278 Post Street
San Francisco, CA
(Retail Property on Union Square)

This proposal was received from LaSalle Advisors. The property is being converted to Nike Town and other upscale retail. The cash on cash is projected to be over 9% after the renovation. The total investment was $34,600,000. The same situation occurred as above and PERA is doing 100%.

3. Sequoia Station Shopping Center
Redwood City, CA

This proposal was received from TCW Realty Advisors. The total purchase price was $33,725,000. The initial cash on cash after fees was 9.33%. The proposal was presented to APFC toward the end of October and the seller required a closing by December 15, 1993. We looked at the property and were interested in proceeding. TCW was unable to locate co-investors that could close by the December deadline. As a result, we lost the opportunity to consider this investment.

As more institutional dollars are made available for real estate, it is going to become more and more difficult for APFC to become involved in the better investments unless we can control the investment. In order to do this, we need to have the flexibility to go up to 100% on some of the smaller investment opportunities.

Alaska Permanent Fund Corporation
P.O. Box 25500 Juneau, Alaska 99802-5500
(907) 465-2047

January 6, 1994

The Honorable Randy Phillips
Chairman, Legislative Budget & Audit
Room 103, State Capitol Building
Juneau, AK 99801-1182

Dear Senator Phillips:

As you requested last week, please find enclosed proposed draft legislation (Attachment #1) which would amend the Permanent Fund's list of authorized investments to provide for up to 100 percent ownership in real estate investments. I would suggest the bill be titled, "An Act relating to real estate investments of the permanent fund; and providing for an immediate effective date."

I appreciate the opportunity to appear before the Legislative Budget & Audit Committee next week to request introduction of the bill. For the information of the members, I am enclosing a number of supporting documents which collectively present the rationale for seeking this legislative change.

Attachment #2 is the Board of Trustees resolution dated December 6, 1993 in support of this proposed change. The Trustees adopted this resolution unanimously.

Attachment #3 is a memorandum dated November 18, 1993 addressed to the Board of Trustees from our Real Estate Investment Officer, Pete Jeans. It explains the need for the change from an historical perspective.

Attachment #4 is a letter dated November 9, 1993 addressed to Mr. Jeans from the Corporation's outside real estate consultant, Paul Saylor. This letter provides the consultant's fiduciary opinion in support of the change.

Attachment #5 is a letter dated November 16, 1993 addressed to Mr. Jeans from the Corporation's real estate legal counsel, Morrison & Foerster, which also provides a fiduciary opinion in support of the proposed change.

Finally, Attachment #6 is a copy of an article which appeared in the July 1993 issue of *The Institutional Real Estate Letter.* The article, I think, makes a compelling case from an uninterested but expert third-party perspective that the concept of co-investing as currently practiced by the Alaska Permanent Fund Corporation is not necessarily in the Fund's best long-term interest.

We are seeking this change primarily because we are convinced it will help us to do a better job protecting and enhancing the Permanent Fund.

Thanks very much for your willingness to support this proposal, and we look forward to addressing this issue at the upcoming LB&A meeting on January 12.

Sincerely,

William H. Scott
Executive Director

WHS:JK:ly

Attachments

DRAFT LEGISLATION FROM DEPARTMENT OF LAW:

Section 1. AS 37.13.120(g)(16) is amended to read:

(16) equity interests in, and debt obligations secured by mortgages granting a first lien on, real estate improved by completed and substantially rented buildings and located in the United States [, IF THESE INVESTMENTS ARE MADE

(A) IN A CORPORATION, PARTNERSHIP, TRUST, OR OTHER ENTITY IN WHICH, AT THE CONCLUSION OF EACH INVESTMENT TRANSACTION, AT LEAST 60 PERCENT OF THE BENEFICIAL OWNERSHIP INTEREST ARE HELD BY OTHER INSTITUTIONAL INVESTORS, AND WHICH IS ORGANIZED AND OPERATED FOR THE PURPOSE OF MAKING REAL ESTATE INVESTMENTS BY A BANK, INSURANCE COMPANY, OR OTHER MANAGER OF INSTITUTIONAL FUNDS THAT HAS HAD AT LEAST FIVE YEARS OF EXPERIENCE IN THE MANAGEMENT OF REAL ESTATE INVESTMENTS OF INSTITUTIONAL INVESTORS; OR

(B) WITH CORPORATIONS, PARTNERSHIP, TRUSTS, OR ENTITIES IN WHICH, AT THE CONCLUSION OF EACH INVESTMENT TRANSACTION, AT LEAST 60 PERCENT OF THE BENEFICIAL OWNERSHIP INTERESTS IN THE CO-INVESTING ENTITY OR ENTITIES AS A WHOLE ARE HELD BY INSTITUTIONAL INVESTORS, AND IF

(i) AT THE TIME OF INVESTMENT THE FUND HAS NO MORE THAN A 40 PERCENT BENEFICIAL OWNERSHIP INTEREST IN THE REAL ESTATE INVESTED IN AS A WHOLE;

(ii) THE RIGHTS AND OBLIGATIONS OF THE FUND ARE SUBSTANTIALLY SIMILAR TO THOSE OF THE OTHER INSTITUTIONAL INVESTORS, EXCEPT FOR THE PERCENTAGE INTEREST IN THE PROPERTY; AND

(iii) THE PROPERTY IS MANAGED AND OPERATED BY AN ENTITY THAT HAS HAD AT LEAST FIVE YEARS OF EXPERIENCE IN THE MANAGEMENT OF REAL ESTATE INVESTMENTS OF INSTITUTIONAL INVESTORS];

Attachment #2

Alaska Permanent Fund Corporation
P.O. Box 25500 Juneau, Alaska 99802-5500
(907) 465-2047

RESOLUTION OF THE BOARD OF TRUSTEES
OF THE ALASKA PERMANENT FUND CORPORATION
PERTAINING TO LEGISLATIVE CHANGES IN THE ALASKA STATUTES
RELATING TO REAL ESTATE INVESTMENTS BY THE
ALASKA PERMANENT FUND CORPORATION

RESOLUTION 93-11

WHEREAS, the Fund is limited in directing business decisions on real estate investments as a 40% participant; and

WHEREAS, the Alaska Permanent Fund Corporation is impaired in its ability to reach its targeted real estate asset allocation within current parameters; and

WHEREAS, the Alaska Permanent Fund Corporation has lost opportunities to acquire high return, low risk real estate investments;

NOW, THEREFORE, BE IT RESOLVED, THAT the Board of Trustees unanimously directs staff to seek legislative changes to provide for up to 100% ownership in real estate investments.

PASSED AND APPROVED by the Board of Trustees of the Alaska Permanent Fund Corporation, this 6th day of December, 1993.

Chairman, Board of Trustees
Alaska Permanent Fund Corporation

ATTEST:

Corporate Secretary

Attachment #3

Alaska Permanent Fund Corporation
P.O. Box 25500 Juneau, Alaska 99802-5500
(907) 465-2047

MEMORANDUM

DATE: November 18, 1993

TO: Board of Trustees
Alaska Permanent Fund Corporation

FROM: Pete Jeans
Real Estate Investment Officer

THROUGH: William H. Scott
Executive Director

SUBJECT: Recommended Legislative Changes, Real Estate

I am recommending a change to Title 37, Chapter 13, Section 37.13.120, the Alaska statute that authorizes the Fund's investments in real estate. The reference to real estate investment responsibilities of the Board of Trustees will be changed to read:

(g)(16)	equity interest in, and debt obligations secured by mortgages granting a first lien on, real estate located in the United States.
(16)(A)	deleted
(16)(B)	deleted
(16)(B)(i)	deleted
(16)(B)(ii)	deleted
(16)(B)(iii)	deleted

This change removes the 40% restriction on real estate acquisitions. The real estate "investment list" is stricken from the Statute and transfers to the Board of Trustees, the responsibility for establishing prudent investment standards and guidelines through the annual real estate resolution.

In order to justify this recommendation it is necessary to give a brief description of the Fund's real estate experience over the past ten years, along with my views on the changes that are taking place in the industry.

In 1983, the year the Alaska Permanent Fund Corporation made its first investment in real property, the Board of Trustees had allocated 6% of the $3 billion Fund to real estate. The Board of Trustees hired a real estate consultant to assist

in selecting three real estate advisors. From 1983 through 1987, the Fund took a passive role in real estate investing and relied almost exclusively on the recommendations of the consultant and advisors. Additionally, the 40% co-investment requirement created a high comfort level for the Trustees. By co-investing with larger, more sophisticated pension funds and endowments, the Permanent Fund took advantage of their expertise and leadership in real estate investing. During this period, control and involvement in property decisions were not priorities for the APFC.

In the later part of the 80's, there was a turnover in Permanent Fund real estate staff. Soon after, the Fund employed new real estate consultants and attorneys, all of which resulted in a more directive approach to real estate investing. The Fund has become more involved in the real estate investment process, from requiring certain controls and buy-sell arrangements on each real estate transaction to initiating disposition activities. Even as a 40% player, the Fund has been able to negotiate either equal or favorable terms and receive coequal treatment from larger investors.

Historically, market conditions played an important role in negotiations for favorable terms. During the recent market decline in the industry, many pension funds sat on the side lines, offering little competition for deals. Now that the market has shown signs of recovery, pension funds are re-entering the markets. Like the APFC, our institutional partners are gaining knowledge and confidence in their abilities to control investments and they no longer allow us to participate as an equal partner in a 40/60 deal. The only way to secure the same level of control that the Fund historically obtained with past investments is to acquire an equal or majority interest.

Control is by far the greatest benefit of holding a majority position in an investment. Timing of major capital events, such as a property sale or the funding of a mall redevelopment designed to head off new competition, is often crucial to enhancing returns on a property. The inertia of some institutional partners has caused numerous missed opportunities for the Permanent Fund in the past.

Other advantages also exist. The real estate asset allocation set by the Board of Trustees will be more easily attainable. Unless a single deal is exceptionally large, the acquisition of a single property will not materially affect the diversification strategy. Through resolution, the Board of Trustees will continue to maintain control over the diversification goals.

Legal costs will be reduced substantially by eliminating or decreasing the negotiations over control issues in partnership agreements. Complications in replacing investment advisors are directly correlated with the number of partners in a deal. The replacement process is simplified in a 50/50 to 100% investment.

By having the option to take 100% of an investment, we anticipate an increase in deal flow. With only one or two investors involved, advisors will be more likely to propose acquisitions to us, particularly those with short closing time frames.

This proposed change to the Statute will give the Board of Trustees the flexibility to direct the real estate staff by board resolution. Attached is a letter from our legal counsel and real estate consultant recommending these changes.

SAYLOR PROPERTY CAPITAL, INC.
EIGHT PIEDMONT CENTER
SUITE 320
ATLANTA, GEORGIA 30305
TEL. (404) 261-8049
FAX: (404) 261-0271

PAUL H. SAYLOR

NEW YORK OFFICE
437 MADISON AVENUE, 40TH FLOOR
NEW YORK, NEW YORK 10022-7380
TEL. (212) 754-6260
FAX (212) 754-6264

Attachment #4

November 9, 1993

Mr. Pete Jeans
Investment Officer
The Alaska Permanent Fund Corporation
801 West Tenth Street
Suite 302
Juneau, AK 99801

RE: Proposed Legislation

Dear Pete:

You have asked that I give a few thoughts why I am in favor of a legislative change to allow you to take up to a 100% interest in an investment.

1) *Control*

Although co-investment documentation is evolving to the point where a minority investor will not necessarily be disadvantaged as to influence or control, there is no such thing as a 40% gorilla. In other words, it would be preferable for the APFC to invest on a basis that would allow it to control major investment, management and divestment decisions in its own best economic interests, rather than be influenced by one or more investors which may, at least over time, have differing objectives.

While I believe the APFC has been advantaged by retaining discretion over major investment, management and divestment issues, it is currently required to be totally aligned with one or more partners in order for activities which best serve it to occur. Examples include the inability to close recent transactions because of (what I consider) minor differences with a 60% partner, and your lack of influence in matters associated with Boston Real Estate Counsel assets in a situation where at least one of your partners was lethargic and bureaucratically hamstrung from acting in all partners' best interests.

2) *Maximum New Opportunities*

As property markets turn back in favor of sellers, the APFC will receive

increasingly fewer high quality investment opportunities, as investment managers will be less in need of the APFC's capital and wish to conclude transactions with either one investor or a commingled format over which they have discretion. Currently, it is relatively complicated for a transaction originator to identify an asset for the APFC with the condition the APFC will only pursue due diligence or the consummation of a transaction once a compatible investment partner has been identified. Recently, transactions have gone elsewhere to avoid this process.

Additionally, there are increasing concerns regarding potential incompatibility of APFC requirements with those of certain other active investors. Although the multi-asset co-investment opportunity which we have collectively pursued for the last several months will go a long way to establish levels of overall compatibility among several investors and standardized processes, sellers or transaction originators generally attempt to avoid the unknowns associated with due diligence and documentation requirements of multiple investors.

3) *Management Changes*

Since the APFC appropriately exercises rights of management oversight, it is more likely to recognize management program weaknesses and to move to correct them than most other institutional investors. Existing assets and portfolios need to be intensively managed in order to improve their performance and occasionally to position assets for sale. Managers who are ineffective should be replaced, and manager replacement is most difficult to accomplish for the APFC as a minority investor especially since most partners of the APFC are required to live with an "approved list" of investment managers.

I do not at all advocate that the APFC should only pursue acquisition of full interests in individual assets and portfolios, but I believe a change of legislation to allow you to do so is most important. It is my view that the immediate effect of such change will not be termination of your co-investment programs, but rather a gearing up of the process contemplated by your co-investor conference this past April. Your ability to be a major partner, rather than (always) a minor partner is most important to the achievement of your objectives set forth for the asset class of real estate and to your competitiveness in the marketplace.

Yours very truly,

Paul H. Saylor

CC: Llewellyn Lutchansky

Attachment #5

MORRISON & FOERSTER

LOS ANGELES
SACRAMENTO
ORANGE COUNTY
PALO ALTO
WALNUT CREEK
SEATTLE

ATTORNEYS AT LAW

345 CALIFORNIA STREET
SAN FRANCISCO, CA 94104-2675
TELEPHONE (415) 677-7000
TELECOPIER (415) 677-7522
TELEX 34-07154 MRSN FOERS SFO

NEW YORK
WASHINGTON, D.C.
DENVER
LONDON
BRUSSELS
HONG KONG
TOKYO

November 16, 1993

DIRECT DIAL NUMBER
(415) 677-7048

VIA FACSIMILE

Mr. Pete Jeans
Real Estate Investment Officer
Alaska Permanent Fund Corporation
P.O. Box 25500
Juneau, Alaska 99802-5500

Dear Pete:

You have asked us to review the proposed legislative amendments to Section 37.13.120(g) of the Alaska Statutes in the context of our experience as investment counsel for the Alaska Permanent Fund Corporation (the "APFC"). We understand that the legislative amendment to be reviewed by the Board would modify subsection (g)(16) of Section 37.13.120 to provide:

> (g) Subject to the limitations contained in this section, the board may invest fund assets at the competitive national market rates or prices that are applicable to each investment only in
>
> . . .
>
> (16) Equity interests in, and debt obligations secured by mortgages granted a first lien on, real estate located in the United States.

We believe that this proposed amendment would be beneficial in carrying out the investment policies of the APFC for several reasons. First, it would allow the APFC to effect real estate investments that fulfill its investment objectives without imposing legal constraints that may not be relevant to ensuring that the investments are prudent. Second, the existing provisions of Section 37.13.120 that would remain unchanged by this legislative proposal ensure that sufficient fiduciary safeguards are present in connection with the acquisition of real estate by the APFC. Third, and perhaps most significantly, the proposed

amendment would allow the APFC to invest in real estate on terms that are comparable to the terms available to ERISA-regulated corporate and Taft-Hartley (union) retirement plans and a majority of governmental retirement systems. By adopting the standards utilized by most tax-exempt institutional investors, the APFC will be poised to compete more effectively with such investors for real estate opportunities and to exert the degree of control that many of such investors have viewed as conducive to maximizing return and minimizing risk in their real estate portfolio investments.

The current provisions of Section 37.13.120(g)(16) include specific limitations that mandate, among other requirements, that the APFC not hold greater than a 40 percent beneficial ownership interest in a real estate investment at the time of acquisition, that the real estate investment is improved by completed buildings and that such buildings are substantially leased. These types of restrictions are typically referred to as "legal list" statutes and were commonly used in state statutes applicable to public and private retirement plan investments prior to 1974.

The enactment of the federal ERISA statute in 1974 eliminated the applicability of these legal list statutes to private corporate and union retirement plans. ERISA imposed general fiduciary standards applicable to all types of investments. The foundation of these fiduciary standards is the prudence and diversification rules of Section 404 of ERISA. These rules are incorporated into Sections 37.13.120(a) and (c) of the Alaska Statutes and are fully applicable to the APFC's real estate investments.

The drafters of ERISA abandoned the legal list statutes in favor of general rules of prudence and diversification for two reasons. First, to the extent that a restriction found in a legal list is a restriction appropriate to effecting a prudent and diversified investment, the legal list restriction is merely duplicative with the general fiduciary standards. Moreover, to the extent that the restriction was unnecessary to ensuring that appropriate fiduciary caution was exercised in effecting an investment, the legal list restriction was viewed as impeding the plan's ability to pursue prudent acquisition opportunities.

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Since the enactment of ERISA, a majority of public retirement systems have adopted legislative changes that substitute general fiduciary standards for legal list statutory restrictions. The rationale underlying these changes has been similar to the legislative intent of Congress in enacting ERISA, that the legal list restrictions are either duplicative with the general standards of prudence and diversification, are obsolete interpretations of such standards or are general examples of such standards that may not be appropriate in specialized investment contexts.

It would be beneficial to the APFC to pursue investment opportunities in real estate under standards similar to the fiduciary standards applicable to the majority of institutional investors competing for these investment opportunities. Because the APFC will be fully obligated to pursue real estate investments that satisfy the prudence, diversification and other standards applicable under Section 37.13.120, to the extent that the legal list restrictions of current subsection (g)(16) are appropriate to ensure prudence or diversification, these restrictions will still apply to real estate investments of the APFC. Thus, for example, if a purchase of more than forty percent of the beneficial ownership of a particular real estate investment would not be consistent with the standard of maintaining a reasonable diversification among investments, the "forty percent rule" would continue to apply. If, however, it was not only prudent and consistent with diversification standards to invest in a larger percentage of a particular real estate investment, but would allow greater controls with respect to operating budgets, leasing decisions and other control features determined relevant to enhance the APFC's investment return, the forty percent rule would operate to limit potential investment returns in the APFC real estate portfolio.

In summary, the legal list restrictions of subsection (g)(16) are generally redundant with the prudence and diversification standards of sections (a) and (c) of Section 37.13.120. In those instances where these restrictions do not duplicate the general standards, but provide more onerous restrictions, it is difficult to justify rules that do not further the standards of prudent real estate acquisitions or may impede such acquisitions.

It is widely recognized that the current real estate acquisitions market demands a greater scrutiny of

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current income opportunities than was the case in years where capital appreciation in real estate could be more easily projected. It is significant to note that the APFC's ability to control decisions that are economically relevant to both income and potential capital appreciation is limited by its current inability to acquire a majority interest in its real estate investments. By allowing the board and, to the extent delegated by the board, the APFC staff, the ability to balance the economic benefits of control against the costs of such a percentage acquisition, the APFC will be able to maximize its investment objectives in a context relevant to each particular investment opportunity it reviews for potential acquisition.

Please contact me if we can be of further assistance in this matter.

Very truly yours,

Rachel Markun/pmd

Rachel Markun

RM:pmd

Attachment #6

THE INSTITUTIONAL REAL ESTATE LETTER

The Information Source For Industry Insiders

Volume 5, Number 7 ISSN 1044-1662 July 1993

PROSPECTUS

SECURITIZATION by Steve Bergsman

REITs On a Tear

Déjà Vu—Have We Been Here Before?

Real estate investment trusts have been on a tear. For the first quarter of 1993, REITs posted returns of 19.1 percent, easily outdistancing the S&P 500 which only managed a 4.3 percent return. This was an even faster start than in 1992 when REITs

blistered the market for a 20.7 percent return, again showing up the S&P 500 which only notched a decent 7.7 percent return.

It's not just the market performance of REITs that has caught the eye of the investor—last year, the REIT market raised $6.6 billion, nearly $2 billion greater than the previous record year of $4.8 billion. More than half of that $6.6 billion was raised by existing REITs which were extremely active in the real estate market, acquiring $2 billion worth of properties. REITs suddenly became the Japanese of the Nineties. The paradox is, after mugging the U.S. real estate market with a seemingly inexhaustible supply of capital, the Japanese have disappeared. Will the same thing happen

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CO-INVESTMENT by Steve Bergsman

The Dark Side

Co-Investment May Be Trendy, But It's Not All Wine and Roses

The concept of co-investing has been around for decades, but recently, it seems to have become the "in" thing to do. Increasingly, over the past three years, investors and investment managers alike have been dressing their portfolios up with

co-investments—the institutional investment community's analog of the "grunge" look.

The "grunge look"—ripped jeans and flannel shirts—may be popular in some circles today, but it certainly isn't for everyone. Neither is co-investment. Even if co-investment is particularly well-suited to the needs of your fund, there are numerous issues which must be considered to make sure your beneficiaries don't end up in rags and tags.

Like the grunge look, the trendsetter for co-investment came out of the Pacific Northwest. Since the mid-1980s, the **Alaska Permanent Fund**—a $15 billion endowment organized for the benefit for

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COVER STORY

Co-Investment

Trendy, But It's Not All Wine and Roses

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all the citizens of Alaska and funded by taxes on mineral extraction revenues—has been the leader in the U.S. co-investment movement.

The reason? As always, necessity is the mother of invention. By statute, the maximum interest the Permanent Fund can hold in any single property is 40%. This means that, in order to make separate account investments work—and the Alaska Permanent Fund's Real Estate Investment Officer, **Pete Jeans**, very much wants his fund to be a separate account investor—the Fund has no choice but to co-invest (join with other tax-exempt funds to make a purchase).

As a result, for the last eight years, Jeans has made co-investment after co-investment, bringing into his real estate plays more than 100 pension fund investment partners. The approach has worked well for the Alaska Permanent Fund, and now Jeans has come south to spread his gospel throughout the "Lower 48." (More than 40 pension, foundation and endowment funds recently attended a private conference on co-investment in Dallas, sponsored by the Alaska Permanent Fund and its advisors.)

Obviously, Jeans is having some success spreading the word. He credits this success to the discontent so many pension plans have been feeling over the real estate investment programs in which they invested during the early to mid-1980s. During those formative years, Jeans explains, the institutional investor community enthusiastically embraced the concept of blind pool commingled fund investing. With this approach, a group of tax-exempt investors would invest their capital in a specified group trust, insurance company separate account or limited partnership organized and managed by an investment manager in order to enable those investors to acquire a diversified portfolio of real estate assets. The problem with these funds, says Jeans, is that investment decisions and management responsibilities were left in the hands of a third party who had ultimate discretion over the funds—and who almost always had significant conflicts of interest. To make matters worse, when the real estate market collapsed, funds trying to escape the calamity discovered they were blocked by poorly-conceived exit strategies.

Today, pension plans, still tangled in the webs of commingled funds but anxious to get in on the buying opportunity of a lifetime, are looking for new paradigms—alternative forms of real estate investment that can offer greater control and liquidity. Of course, the ultimate control results when a pension fund acquires properties directly with no partners. Some funds are unable or disinclined to go that route, however, which, according to Jeans, is what makes co-investment so appealing today.

If one considers investment structures on a continuum, notes **Allen Andersen**, a Principal with the Dallas office of **Arthur Andersen Real Estate Service Group**, they will fall somewhere between sole ownership and commingled funds. Where on the continuum co-investment lies—especially in regards to the control issue—is still subject to debate. Andersen, for one, says he would place co-investment closer to commingled funds on the spectrum, rather than placing it squarely in the middle.

Of the many forms of co-investment, the least popular have been those which require advisors, operating partners or developers to put their own capital at risk alongside the investors.

Of the many forms of co-investment, the least popular have been those which require advisors, operating partners or developers to put their own capital at risk alongside the investors. While some investors now require such arrangements, others shy away because of the obvious inherent conflicts of interest. (As **Bob Burke**, a Principal of **AMB Institutional Realty Advisors** likes to point out, the investment management industry appears to have come full circle. The real estate investment management industry really took off, explains Burke, when the Employee Retirement Income Security Act of 1974 [remember ERISA?] mandated that pension funds interject a fiduciary between pension plan assets and deal promoters. Today, notes Burke, pension funds requiring their advisors to co-invest effectively are requiring them to become promoters—creating, once again, precisely the kinds of conflicts the provisions of ERISA sought to eliminate.)

An examination of many of these structures also will reveal that the advisor/developer/operator often stands to receive back in fees during the first few years of the investment, an amount equal to or exceeding the capital it generally committed to the partnership. In such cases, the pension fund's coinvesment "partner" may have little or no capital at risk after the first few years.

To make matters worse, warns Allen Andersen, when the other partner is not a tax-exempt fund there usually is a disproportionate level of investment. The tax exempt investor typically funds something akin to 90-95% of the investment and the advisor, 5-10%. Those kinds of splits don't really do what the pension fund wants them to do.

When pension funds do require their investment managers to put their own capital at risk in the deal, adds **Jim Curtis**, a Principal with San Francisco-based workout specialist **The Bristol Group**, they typically are seeking to align the interests of their partners with their own. The hope, explains Curtis, is that, by having their capital at risk alongside the pension fund's capital, the operating partner will be more attentive to the management of the pension fund's investments. "That's the hope,"

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notes Curtis. "We've learned, however, that people can make equally as bad investment decisions with their own money as with somebody else's." Clearly, therefore, having capital at risk is no guarantee that things will go well.

Curtis also cautions that frequently the partner doesn't even have its own capital at risk. "They raise it from other sources or they borrow it. The problem is, when the capital contributed is non-recourse, the investment manager or promoter really isn't at risk at all. In such cases," warns Curtis, "all that these co-investment requirements really create is the *illusion* of comfort."

In addition, an incompatibility of incentives often exists in these types of investments, according to **Ron Karp** of the Summit, NJ-based consulting firm **Ronald A. Karp & Associates**. Karp notes that there is a mismatch in the long-term stability and financial staying power of the pension plan versus the investment advisor or operating partner. "If the investment gets into trouble, who is going to fund the losses? Obviously, it's going to be the pension plan. And that is going to create a problem when it comes to decision-making."

. . . co-investments . . . are nothing more than a commingled fund warmed over.

The most popular form of co-investment, however, is between similar investors with similar objectives and resources, such as two or more pension plans. Even here, however, there are variations and concerns. One type of co-investment, for example, relies on an advisor who brings together investors with a common investment strategy. The advisor then executes transactions accordingly. A second type of co-investment occurs when investors unite under their own initiative—when the co-investment is investor-driven, rather than manager-driven.

The principal feature of every co-investment, however, is that it involves more than one investor (the typical co-investment involved between three to five investors). Therein lies co-investment's strength—and its weakness.

For a smaller pension plan, co-investment offers the opportunity to participate in transactions larger than those the plan otherwise would be able to execute on its own. "Small funds may not be able to invest in large projects simply because their allocation is insufficient," explains **Terry Ahern**, a Principal with the Cleveland-based **Townsend Group.** It also enables a larger investor to achieve more diversification than otherwise would be possible by investing directly. According to its Chief Real Estate Investment Officer, Grayson Sanders, for example, the Ameritech Pension Trust has assembled a roughly $1.2 billion real estate portfolio over the past ten years. Sanders notes, however, that because it has acquired much of that portfolio by co-investing with other tax-exempt funds, Ameritech's $1.2 billion position is covered by a portfolio of more than $14 billion in real estate assets.

Investors who have done co-investments often say they like being involved with other participants with similar goals because there is a comfort with being associated with other entities that have the same investment strategy. Or, as **Andy Smith**, President of **L&B Real Estate Counsel Inc.** says, "There is a warm and cozy feeling about doing a large investment with others." Why? For one thing, there is a lot more due diligence, explains Smith. Each partner gets to scrutinize the deal; there are more checks and balances so it's less likely there will be any surprises.

Despite the lack of surprises, there also is going to be a lot more work—and fiduciary liability—for the co-investors. By co-investing rather than commingling, for example, tax-exempt investors not only have to review the potential investments, but also must participate in the decision to acquire. In addition, they must be involved in decisions concerning the ongoing management of the property, and when and how eventually to divest. The problem is, without a third party fiduciary to share the risks, a pension fund subject to ERISA provisions must shoulder the fiduciary liability associated with making these decisions alone.

Despite the extra work and liabilities, however, this is precisely the kind of control that was lacking in the commingled funds, and precisely the kind of control that many tax-exempt investors now want. When investors were passively investing in commingled funds, advisors and managers made those decisions. When advisors became promoters, and began structuring funds as partnerships to avoid being subjected to fiduciary liability under ERISA, they still made the decisions, but investors no longer enjoyed any insulation from fiduciary liability. When investors realized they weren't going to receive any fiduciary insulation, they started questioning why they should give up control. This issue, and this issue alone, is the primary driving force behind the co-investment trend. "Investors were very concerned about the lack of control in commingled funds," explains Alaska's Pete Jeans. "They wanted to be part of the process. Co-investment gives the investor more control."

Or does it?

LESSONS LEARNED

The old axiom of real estate used to be "location, location, location." But, counters **Tim Getz**, Investment Officer with the **Ohio Public Employees Retirement System**, the axiom really should be "control, control, control. You're not going to get that control," warns Getz, "by sharing your decision-making power." Getz speaks from experience—his fund was a pioneer in both the early commingled fund and co-investment movements. "One of the lessons that we learned from commingled funds was that the investor didn't make portfolio decisions. The decisions were always being made by someone else. When things got difficult, it was impossible to achieve consensus." Getz warns that the problem is no different with co-investments, which he says are

"nothing more than a commingled fund warmed over."

As noted before, one of the strengths of co-investment is the added layer of scrutiny. This also is a weakness, however, because it often can be difficult if not impossible to get multiple parties to come to a decision. And, since co-investors don't always have equal shares, by definition, someone is bound to end up with a minority interest. Obviously, that can be a real problem if the majority investors have a different point of view than the minority investors.

"Co-investment complicates every single aspect of a transaction," says **Susan Hudson-Wilson**, Director of Portfolio Strategy for Boston-based **Aldrich, Eastman and Waltch**. "All of a sudden there are two or more parties—very interested parties—that need and ought to be satisfied on every single aspect of the investment." As Hudson-Wilson points out, however, a hot button for one co-investor may not be so hot for another. This can make it extremely difficult to structure a transaction.

Once a co-investment has been completed, however, there essentially are five decisions upon which co-investors have to agree: leasing; capital improvement; budget; sale; and an exit strategy. In a co-investment, the way for the investors to feel their way through those processes, says L&B's Smith (who has been putting together co-investment deals since the 1970s) is to make sure that one participant never has more than 50 percent of the vote. To make a co-investment program work, explains Smith, a reasonable level of democracy must be established.

Michael Evans, National Director with **Ernst & Young**'s Real Estate Advisory Services in San Francisco, counters that co-investment adds another, unneeded level to problem solving over the life of the asset. "When there are decisions to be made by different investors who have changing objectives and strategies, there is always going to be the potential for conflicts of interest."

Hudson-Wilson concedes that co-investment may be a great way for a small pension plan to participate in larger investments, but reiterates that, "there is true lack of control when you need it most." At the point when you most need and want to do something big—like invest more or reduce the size of your investment—you discover that your options aren't much different than if you had invested in a commingled fund.

A FORMULA FOR SUCCESS

Co-investors typically try to avoid the problem of potential conflicts of interest by finding other investors with similar investment objectives. "The big key to success in co-investment is picking your partners," admits Jeans. "It does little good to find a partner who wants to hold properties for the long term, if you want to sell after three years."

Cab Grayson, Managing Director of **CB Commercial Realty Advisors**, feels that establishing a pre-existing association for co-investment can greatly enhance the success of the co-investment. "These associations of like-minded investors agree in advance to a defined real estate investment strategy, acquisition process, standardized contracts covering the decision-making powers of investors and transferability of interests, and pre-negotiated investment management fees that are performance-based and aligned with the investors' interests. The associations and the predefined process allow the investment manager to move quickly and to better negotiate with the seller." CB completed its first co-investment in 1981 and has created an active co-investment association of like-minded investors. **Scott Tracy**, Grayson's partner at CB Commercial, adds that, "The association prompts the co-investors to address most of the issues beforehand, and minimizes the difficulties in gaining consensus. Investors agree that, once the initial acquisition decision has been made, the advisor is given a defined level of discretion on operating decisions, thereby reducing disputes.

When constructing the co-investment, it is critical that the rights of the co-investors be stated clearly and definitively. "You must have a mechanism for resolving disputes among the participants," warns **Jim Snyder**, President of **Kennedy Associates Real Estate Counsel**, a Seattle-based advisor that has been putting together co-investments for the past 15 years. Snyder explains that the problem-solving process among the co-investors should be formalized as a general part of the co-investment agreement. Sometimes the process could be as simple as a majority vote among the co-investors, but it also should include a way to allow an unhappy investor to exit the co-investment. As noted, liquidity is one reason why pension plans are looking at co-investment. Investors, therefore, need to be assured that there is an easy out if they want to leave.

"Our experience," says Jeans, "has been that, if we're having a problem or disagreement with a partner, we call a meeting and sit down together face-to-face. Ninety-nine percent of the time we can solve the problem. In those few instances where it absolutely doesn't work out, the partner can leave." According to Jeans, that usually means the other partners will buy out the disgruntled party.

The **New York State Teachers Retirement System** also has been involved in co-investment transactions in the past, but none recently. "We're not saying we won't do anymore, but when we have a choice, we prefer to invest on our own," notes **Jim Campbell**, Assistant Real Estate Officer at NYSTRS. The Fund wants to control its own destiny, Campbell explains, and it is tougher to do that when hooked into other investors. "It can be frustrating to be in a deal with an investor who has a shorter term horizon or is handicapped by political decision-making processes."

The bottom line is, co-investment is a little like "the Force" —that wonderful source of power that Luke Skywalker discovers in George Lucas' Star Wars. Like the Force, co-investment can be either of great benefit, or great harm to the user—depending on how you approach it. And, as with all sources of power, investors must not forget that co-investment has its dark side. ❖

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January 13, 1994

Senator Randy Phillips
Legislative Budget & Audit Committee, Chairman
State Capitol Building, Room 103
Juneau, AK 99801-1182

Dear Senator Phillips:

Thank you for providing us with Ibbotson's report on the asset allocation of the Alaska Permanent Fund Corporation (APFC). We are pleased to provide this initial response to the report. Communication on this issue will continue as the board commences its annual review of APFC's asset allocation at the February 3 meeting in Juneau.

Since April 1993, the APFC has been involved with a significant portfolio restructuring program under the direction of the Board of Trustees. Upon completion, the APFC will place significantly less emphasis on passive investment and more on active management of the equity securities portfolio. This program has been undertaken with our investment consultant, Callan Associates, Inc. (Callan), providing recommendations and advice at each step of the program. Once completed, a number of the issues mentioned in the Ibbotson Associates Asset Allocation study will have been addressed.

After reading the Ibbotson report, Callan made the following observations:

1. Recent performance has been good because the board and staff have done a good job of adopting sound strategic allocation policies and employing good managers.

2. Movement toward current strategic targets at an accelerated pace may be particularly important since much of the strong performance over the past several years is attributable to extraordinary bond returns which are unlikely to continue given the current low level of interest rates. Obviously, we all agree with this

assessment and you, through significant funding of global portfolios in recent months, have already essentially reached the strategic target allocations.

3. Diversification within the domestic equity portfolio could be improved with a greater commitment to the small and mid-cap sector. Callan shares this view and your staff recognizes the under-representation in this area and plans to address it through the hiring of two small/mid-cap domestic equity managers in the first half of 1994.

4. Diversification within the fixed-income portfolio could be improved with explicit allocations to major segments such as mortgages. As discussed at length at our recent meeting, the effects of statutory limitations on fixed-income management must be carefully considered. The use of derivative securities, lower-rated bonds and non-US$ denominated bonds are all influenced by current (statutory) restrictions. In addition, managing liquidity to meet annual dividend requirements is increasingly affecting the fixed-income portfolio. Nonetheless, broader diversification of the fixed-income effort warrants further discussion and already has been scheduled for the upcoming board meeting. As an aside, I was pleased to see that Ibbotson recognized the fee savings and good performance that has been achieved to date. It also is important to note that at least over the past several years an allocation to mortgages would have hindered performance.

5. Ibbotson's expected equity returns are extraordinarily high relative to the firm's expected bond returns. While I sincerely hope that they are correct, the very large premiums and the high absolute levels may result in an underestimation of near-term risk associated with more aggressive strategies. Relatedly, we, staff and the board have all acknowledged that heavier equity commitment would result in greater expected returns over the long run but we all also recognize that shorter-term consistency in returns is particularly important to the Fund since the annual dividend is potentially at issue. Finally, it is important to note that the "aggressive" alternative suggested results in full utilization of the statutory equity maximum of 50%.

6. Ibbotson very clearly advises that the board control asset allocation at a more micro level than it has in the past. Specially, the study advises that the board set specific allocations within the fixed-income and domestic equity areas and make extensive use of specialists in the international area. The directions suggested are contrary to the board's movement toward providing less restrictive guidelines to its managers, particularly the global managers. I think that this is an important issue that already has been discussed at length during 1993 and warrants continued close monitoring

and review as we gain experience with the current structure. My current view is that the board's basic asset allocation plan, while theoretically vulnerable to the actions of the managers, will not be adversely affected. Each manager has indicated that it is highly unlikely that they would make sudden dramatic shifts from domestic to international portfolios. We, therefore, will be able to identify any potential problem before it undermines the program. You are continuing to use some specialists internationally and are planning to add specialists in domestic mid-cap securities. In sum, Ibbotson's management structure comments are important and I agree that the structure, particularly the domestic structure, should be on the board's agenda for 1994.

The staff of the APFC agree with Callan's remarks. Should the Legislative Budget & Audit Committee (LB&A) like to discuss in greater detail these conclusions, we recommend that myself and a representative of Callan Associates, Inc. be invited to appear before the Committee. The APFC would be pleased to make the necessary arrangements.

We would like to express our appreciation for LB&A's efforts and those of Ibbotson in conducting this review. It is always helpful to receive more than one independent view of this most important subject of asset allocation. In addition, we would be pleased to have Ibbotson present their report to the Board of Trustees at its meeting on February 3, 1994 at the APFC offices in Juneau.

Sincerely,

William H. Scott
Executive Director

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MEMORANDUM

DATE: February 1, 1994

TO: Senator Loren Leman
Chairman, Senate State Affairs Committee

FROM: William H. Scott
Executive Director

SUBJECT: **Senate Bill 245**

In response to the concerns you voiced at last Friday's committee meeting, here are two workable amendments to SB 245.

1. Remove the 40% ownership limitation on all real estate investments under $50 million (thus providing the Fund with the flexibility to go up to 100% on those investments).

2. Change the 40% ownership limitation on all real estate investments to a 67% ownership limitation on real estate investments in excess of $50 million.

These changes are less than we would like, but we recognize the Legislature's prerogative to exercise control over the Permanent Fund's investment authority. *We would like to make it clear, however, that even though these amendments would be an improvement over the status quo, the Alaska Permanent Fund Corporation would prefer that the committee move the bill as originally introduced.*

Why should the Legislature eliminate the current 40% limitation?

The primary reason your Fund managers are seeking changes to the existing real estate statute is to gain increased management control over the Fund's real estate investments – both for the old as well as the new investments which the Fund will make in the future. A 40% ownership