ALASKA LEGISLATURE COMMITTEE FILES 2007-2008 STRA 12785

The Alaska Marine Highway is one of two routes in Alaska that have earned the distinction of being named a National Scenic Byway by the United States Department of Transportation. In September of 2005, the Federal Highway Administration upgraded this designation to an All-American Road. Only 26 other roadways in America have received this title. Being called such, means that the Alaska Marine Highway has features that do not exist elsewhere in the USA and are scenic enough to be tourist destinations unto themselves.

The genesis of the Alaska Marine Highway System occurred in the late 40's when Steve Homer of Haines together with Robert Sommers and Associates started a commercial ferry service on Lynn Canal. Mr. Homer and Ray Gelotte, converted a surplus World War II. LCT-Mark 6 landing craft which they christened the *M/V Chilkoot*. The Chilkoot Motorship Lines operated from Tee Harbor in Juneau to Haines-Port Chilkoot and Skagway. Their business was purchased by the Territorial Board of Road Commissioners in 1951.

The *Chilkoot* continued to operate for another 6 years while the territorial government decided to build a new, but smaller ferry. Named the *M/V Chilkat*, this distinctive ferry was painted blue and gold and almost instantly dubbed the "Blue Canoe." This vessel began daily service between Juneau and the communities on the Lynn Canal in June of 1957. After Alaska became a state in 1959, voters approved bond issues totaling $18 million to expand the ferry fleet. The first of the new ships to go into service was the *Malaspina* in January of 1963 when it sailed the Inside Passage to Ketchikan. That community and the rest of Southeast Alaska had been without regular passenger ship service for nearly a decade when the Alaska Steamship Company stopped such service in 1954. The Alaska Marine Highway System (AMHS) became official in 1963. The system is under the auspices of the Alaska Department of Transportation and Public Facilities (DOT/PF).

Today there are a total of eleven vessels serving in the Alaska's Marine Highway fleet. Over the years this ferry system has expanded to include additional routes between Whittier and Valdez, to Kodiak, Seward, Homer, along the Aleutian chain, Prince Rupert in British Columbia, and between otherwise isolated Native villages.

I should note that in 1967, the southernmost terminus was in Seattle, but moved to the Port of Bellingham, Washington in 1989. This port is a world class facility and AMHS's direct access point to the lower 48. The ferry terminal itself is a multimodal facility that offers shuttle services to the airport, train, bus, and taxi service besides ferry services to Alaska, Victoria, British Columbia and the San Juan Island ferry transportation.

I've given the readers this very brief history of the System because I think it's important to know how something was developed and nurtured, especially when it comes to judging the value of this or any such organization.

The Alaska Marine Highway is part of the National Highway System (NHS), an interconnected system of routes that serve important national functions, e.g., security, commerce, and travel. The NHS is comprised of Interstate and defense routes, other principal arterial routes, and routes connecting to major intermodal facilities such as airports, ports, and ferry terminals. Our marine highway is an integral component of the intermodal system here in Alaska.

The AMHS also falls under the mission and vision of the Federal Highway Administration (FHWA), in that this agency's goals include the protection and enhancement of the natural environment, and the communities affected by transportation which include mobility, safety, productivity, and national security.

The AMHS has historical significance as the main transportation link between many of Alaska's small, isolated coastal communities. Some consider the marine highway as their "life blood" to other areas of the state. This is particularly significant for those towns and villages that aren't connected by any roadway to the mainland. A healthy marine highway system has given every one of those communities the opportunity to expand the commerce of their region and provides a vital link for families, schools, and cultures to flourish. There have also been numerous studies (including the study cited below) that have provided empirical and statistical data demonstrating how the AMHS contributes significantly to the economies of the Railbelt region of the state.

In May of 2002, a study was released entitled: *Sustainability of the Alaska Marine Highway System*, which was prepared for the Southeast Conference by the McDowell Group. Two of the conclusions reached, speak volumes as to why AMHS is in trouble. One of the key issues expressed was that "the current operating model is outmoded and no longer adequately meets the needs of the users." Another conclusion stated that "the existing management structure may not be sufficient for the future..." The study also asserted that the AMHS had an economic impact statewide estimated at $171 million in 1995. This lends credence to the arguments surrounding how important the AMHS is to local economies.

Federal law requires Alaska to provide for consideration and implementation of projects, strategies, and services that will among others:

1. Increase accessibility and mobility of people and freight
2. Support the economic vitality of non-metropolitan areas
3. Improve the quality of life
4. Enhance the connectivity between communities

More often than not, our waterways are the shortest distance between two communities, even though they might be on the same island or landmass. Because of the fusion of Alaska's geologic formations, roadways can be impractical for connecting two or more communities. This isn't an argument about the marine highway vs. a gravel or paved roadway – quite the contrary. This is simply stating fact. Many communities will never

be connected by a hard surfaced road for a multitude of reasons. For their economic stability and harmony, they deserve no less than a reliable transportation service.

I would argue that a safe and reliable transportation is an underpinning of any basic government responsibility. Without a dependable transportation system, you will not have a consistent work force, and people will not have access to basic education, much less higher learning. Their pursuit of life, liberty and happiness is at risk because they have been denied equal access, and may be deprived of proper health care as well.

Sarah Palin
GOVERNOR

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

March 29th, 2007

ADMINISTRATIVE ORDER NO. 233

I, Sarah Palin, Governor of the State of Alaska, under the authority of art. III, secs. 1 and 24, of the Alaska Constitution, and in accordance with AS 44.19.145(c), establish the Alaska Marine Transportation Advisory Board (board) in the Department of Transportation and Public Facilities (department).

PURPOSE

The purpose of the board is to provide recommendations to the governor and the commissioner of the department on the department's exercise of its marine transportation functions assigned by law.

DUTIES OF THE BOARD

The board's duties are to:

(1) meet at the call of the chair to carry out its advisory functions;

(2) hold public hearings as necessary or use other means to solicit information from the public for the development of the board's recommendations; and

(3) prepare and submit to the governor and the commissioner of the department recommendations concerning the department's marine transportation functions assigned by law.

MEMBERSHIP

The board consists of nine members appointed by the governor, to serve at the pleasure of the governor. The governor will appoint the members as follows:

(1) a member representing labor unions of employees of the Alaska Marine Highway System;

(2) a member from Northern Southeast Alaska representing the municipalities of

Haines, Juneau, Sitka, and Skagway;

(3) a member from Southern Southeast Alaska representing the municipalities of Ketchikan, Ketchikan Gateway Borough, Metlakatla, Petersburg, and Wrangell, and the cities and communities of Prince of Wales Island;

(4) a member from Southeast Alaska representing the cities of Angoon, Hoonah, Kake, Pelican, and Tenakee;

(5) a member from the Prince William Sound/Kenai Peninsula area representing the cities of Cordova, Seward, Valdez, and Whittier, the City and Borough of Yakutat, and the communities of Chenega Bay and Tatitlek;

(6) a member from the Southwest Alaska/Aleutian Chain/Alaska Peninsula area representing the cities of Akutan, Chignik, Cold Bay, False Pass, Homer, King Cove, Kodiak, Port Lions, Sand Point, Seldovia, Unalaska, and Dutch Harbor; and

(7) three other members appointed by the governor.

Board members must be persons with an interest or background in marine transportation matters in this state.

The governor will designate the chair of the board. The board may elect other officers as determined necessary.

ADMINISTRATIVE SUPPORT

The department shall provide administrative support for the board.

GENERAL PROVISIONS

Board members do not receive compensation as a member of the board. Members of the board who are not state or federal employees are entitled to per diem and travel expenses in the same manner permitted for members of state boards and commissions. Per diem and travel expenses for members of the board who are a representative of a state or federal agency are the responsibility of that agency.

To reduce costs, the board may use teleconferencing or other electronic means, to the extent practicable, in order to gain the widest public participation at minimum cost.

Meetings of the board shall be conducted, and notice of the meetings and hearings provided, in accordance with AS 44.62.310 and 44.62.320 (Open Meetings of Governmental Bodies).

Records of the board are subject to inspection and copying as public records under AS 40.25.110 - 40.25.220.

This Order takes effect immediately.

DATED at Juneau, Alaska, this 28th day of March, 2007.

Sarah Palin

STATE OF ALASKA
OFFICE OF THE GOVERNOR

Press Release

FOR IMMEDIATE RELEASE 07-124

Governor Palin Fills Marine Transportation Advisory Board

May 14, 2007, Juneau, AK – Governor Sarah Palin today announced the appointment of several Alaskans to the Marine Transportation Advisory Board (MTAB). The Alaska Marine Transportation Advisory Board advises the state on issues related to the Alaska Marine Highway System. The nine-member advisory committee is made up of representatives from communities served by state ferries. MTAB was re-authorized under Administrative Order No. 233 by Governor Palin on March 28, 2007.

Captain William Hopkins of Ketchikan will represent employee labor unions of the Alaska Marine Highway System. Hopkins retired from the Alaska Marine Highway System (AMHS) in January 2007, after thirty years of service. He has piloted Southeast, Southwest and Puget Sound on all AMHS vessels, except for the Wickersham and high-speed craft. Hopkins served eight years as permanent master of the M/V Aurora and another eight years as permanent master of the M/V Kennicott. He is the author of two books including, "Wrangell Narrows, Alaska," a mile-by-mile guide for mariners navigating the Inside Passage.

Robert Venables of Haines will represent northern Southeast Alaska. Venables has worked for the Haines Borough since 2000 – first as the Borough's Economic Development Director and later as the Borough's Manager, a post he has held since 2004. He is a former member of MTAB and former chair of the Southeast Conference. Venables is active in the Haines and Alaska State Chambers of Commerce, and has been a board member of the Haines Borough Fire District #3 since 1988.

John (JC) Conley of Ketchikan will represent southern Southeast Alaska. Conley is the owner of Service Auto Parts, a locally owned auto parts store he has been with since 1979. He served three terms on the Ketchikan Gateway Borough Assembly, and served twice as chair of the Ketchikan Chamber of Commerce and Southeast Conference. Conley is the former chair of MTAB.

Maxine Thompson of Angoon will represent the cities of Angoon, Hoonah, Kake, Pelican, and Tenakee. She is the president of Thompson Management Services, Inc., DBA Angoon Oil Company, a post she has held for over twenty years. Thompson served on the Angoon City Council from 1994 to 1997, and served one term as Mayor from 1997 to 1999. She is a lifelong Alaskan.

Clay Koplin of Cordova will represent the Prince William Sound region. Koplin has served as the Manager of Engineering and Operations for the Cordova Electric Cooperative since 1988. He worked with the Prince William Sound Economic Development Group and the Cordova Chamber of Commerce to develop a marketing strategy for the M/V Aurora and the M/V Chenega. Koplin is a self proclaimed, "Enthusiastic Alaskan."

Shirley Marquardt of Unalaska will represent Southwest Alaska, the Aleutian Chain, and the Alaska Peninsula. She was elected mayor of Unalaska in 2004, and served the previous ten years on the Unalaska City Council. Marquardt is the Port Operations Manager for Samson Tug and Barge in Dutch Harbor. Since 1999, Marquardt has been a member of the American Seafoods Community Advisory Board. She also serves on the Alaska Municipal League Finance Committee and is a member of the Fisheries Committee for Southwest Alaska Municipal Conference.

Murray Walsh of Juneau will serve as an at-large member. Walsh has served as the Executive Director of Southeast Conference since 2006. He is also the Principal in Walsh Planning and Development Services, a private planning practice he has operated since 1996. Walsh has been preparing comprehensive site plans for communities and clients since 1974. He earned a Bachelor of Arts degree in Urban Planning in 1971 from the University of Washington.

Cathie Roemmich of Juneau will serve as an at-large member and as the chair, designated by the Governor. She has served as the executive director of the Juneau Chamber of Commerce since 2006. Roemmich was the assistant port manager for Southeast Stevedoring in Sitka from 1985 to 1996. She also spent four years as the service manager for Willie's Marine, Inc. Boat Sales and Service in Juneau. Roemmich is a lifelong Alaskan.

Mike Korsmo of Skagway will serve as an at-large member. Korsmo captains a 100-foot tug boat for Amak Towing, a subsidiary of Southeast Stevedoring. He has served as a Skagway City Council member since 2002, and is a member of the Southeast Conference Board of Directors where he chairs the Transportation Committee. Korsmo also serves on the Alaska Municipal League Public Works and Infrastructure Committee.

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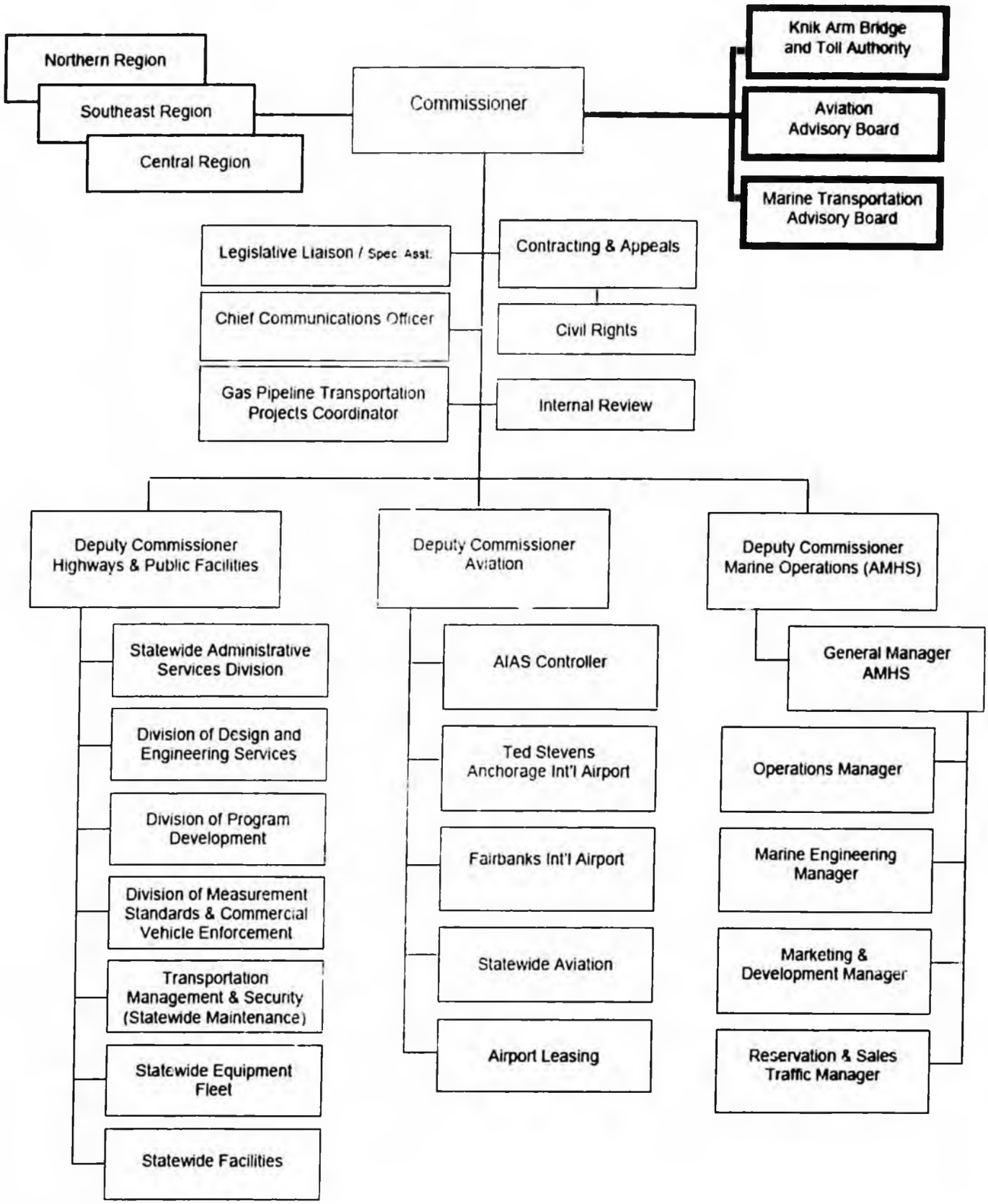
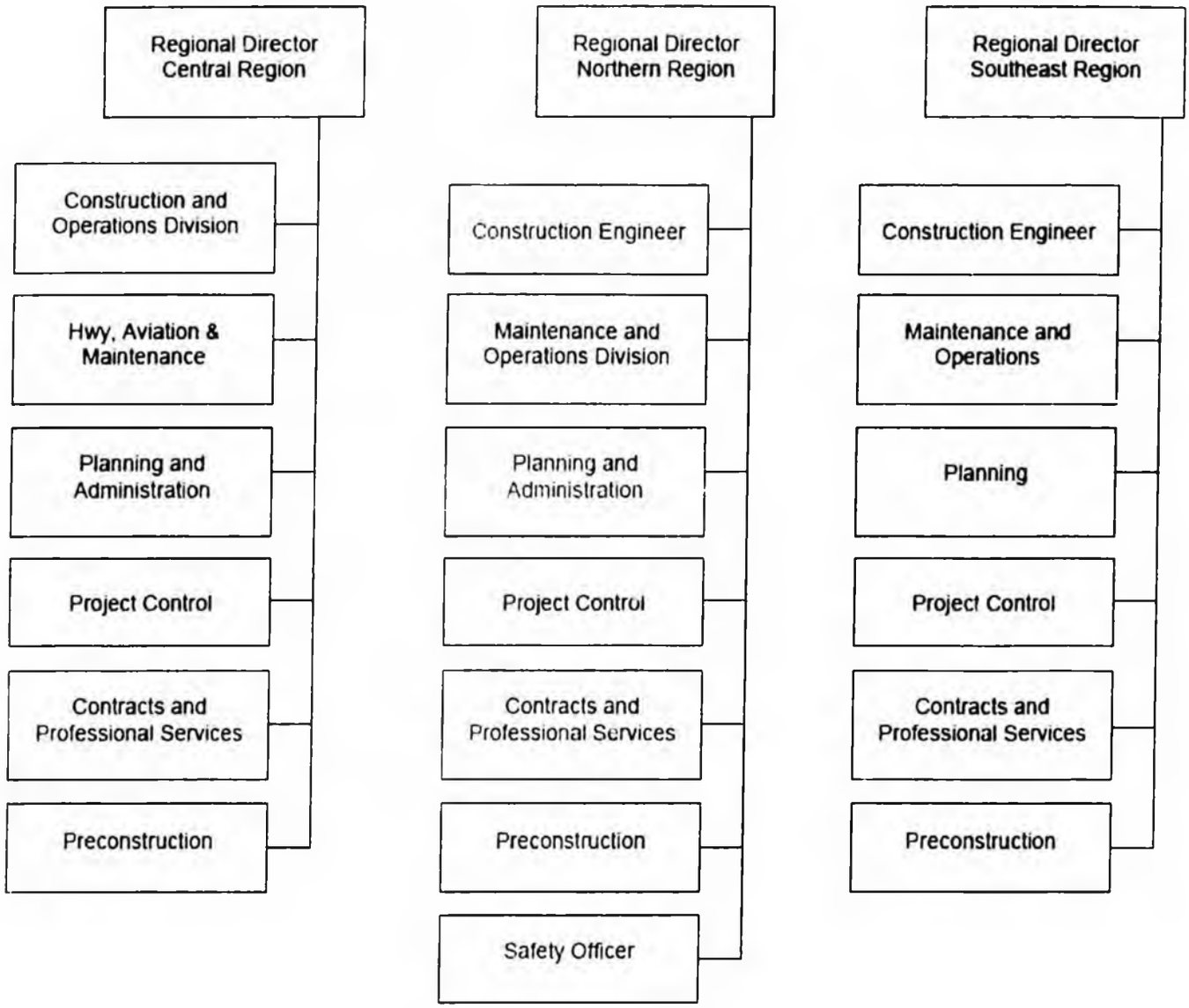


Department of Transportation and Public Facilities



Vessels

There are currently eleven vessels in the AMHS fleet. The newest are the Fast Vehicle Ferries Fairweather and Chenega. They are the first vessels of this type to be built in the United States.

AMHS Vessel Fleet

M/V Aurora (AUR)
M/V Chenega (CHE)
M/V Columbia (COL)
M/V Fairweather (FWX)
M/V Kennicott (KEN)
M/V LeConte (LEC)
M/V Lituya (LIT)
M/V Malaspina (MAL)
M/V Matanuska (MAT)
M/V Taku (TAK)
M/V Tustumena (TUS)

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M/V Aurora

The **M/V Aurora** was built by Peterson Shipbuilders in Sturgeon Bay, Wisconsin, and began service in 1977. The Aurora is 235 feet long, and can transport 300 passengers and 34 vehicles (20' lengths) at a service speed of 14.5 knots. Because the Aurora is used for short runs, staterooms are not available, although food service and a solarium are provided.

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M/V Chenega

The **M/V Chenega** is one of the new Alaska Marine Highway Fast Vehicle Ferries. Built by Derecktor Shipyards of Bridgeport, Connecticut at a cost of $34.5 million, she began service in summer of 2005. The Chenega's designer is Nigel Gee & Associates (NGA), a British naval architecture firm that has many years of high-speed ship design and build experience. The Chenega is powered by four diesel engines and four water jets. The hull form is a 235-foot catamaran that has been shown to provide the highest transport efficiency of any high-speed ferry of this size. The Chenega operates in Southeast Alaska during the winter months and in Prince William Sound during the summer. Photo by Ed Lien

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M/V Columbia

The **M/V Columbia** is the largest vessel of the Marine Highway fleet. Launched by Lockheed Shipbuilding in Seattle in 1974, the Columbia is 418 feet long, with capacity for 499 passengers and 134 vehicles (20' lengths). Its 103 total cabins include 44 four-berth units, and 56 two-berth units, 3 of which are wheelchair accessible. The Columbia boasts both a fine dining room and a cafeteria. The gift shop, cocktail lounge, solarium, and forward observation lounge round out the passenger amenities. Photo by Captain Jack Meyers

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M/V Fairweather

The **M/V Fairweather** is one of the new Alaska Marine Highway Fast Vehicle Ferries. Built by Derecktor Shipyards of Bridgeport, Connecticut at a cost of $36 million, she began service in summer, 2004. The Fairweather's designer is Nigel Gee & Associates (NGA), a British naval architecture firm that has many years of high-speed ship design and build experience. The Fairweather is powered by four diesel engines and four water jets. The hull form is a 235-foot catamaran that has been shown to provide the highest transport efficiency of any high-speed ferry of this size. The Fairweather normally operates in Southeast Alaska. Photo by Peter Metcalfe

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M/V Kennicott

The **M/V Kennicott** was built by Halter Marine group of Gulfport, Mississippi at a cost of over $80 million, she began service in the summer of 1998. Designed by Halter Marine, and the Glosten Associates of Seattle, Washington, the Kennicott is 382 feet long, 85 feet wide, with nine decks. She is driven by two 6,690 HP Wartsilla 32E diesel engines, and has a service speed of 16.75 knots. The vessel is ocean certified and is also designed to serve as a command and logistics center during an oil spill or other natural disaster. The ship has a capacity for 499 passengers, provides 109 berthing accommodations, and has space for 80 standard automobiles. There are 48 four-berth cabins (3 wheelchair accessible) and 56 two-berth cabins (2 wheelchair accessible). The observation lounges and the enclosed, heated solarium give excellent vantage points from which to enjoy Alaska's scenic splendor throughout her voyage. Photo by Frank Scigliano

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M/V LeConte

The **M/V LeConte**, launched in late 1973 by Peterson Shipbuilders in Sturgeon Bay, Wisconsin, joined the fleet in 1974 The LeConte is 235 feet long, with capacity for 300 passengers and 34 vehicles (20' lengths), and operates at a service speed of 14.5 knots. The LeConte is used for shorter runs, so it does not have staterooms, but food service and a solarium are provided. Photo by Cathy Brown

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M/V Lituya

The **M/V Lituya** was designed by Coastwise Corporation of Juneau in 2001, built by Conrad Shipyards in Morgan City, Louisiana, and was launched in April of 2004. The $9.5 million vessel provides daily ferry shuttle service between Metlakatla and Ketchikan. Lituya . The 180-foot, roll on/roll off steel ferry accommodates 18 cars and 149 passengers with an average speed of 10-12 knots.

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M/V Malaspina

The **M/V Malaspina** carries 499 passengers, and provides 46 four-berth and 26 two-berth cabins, one of which is wheelchair accessible. The vessel was built in Seattle in 1963 at the Lockheed Shipbuilding yards, then lengthened and renovated in 1972 at the Willamette Iron and Steel Company shipyard in Portland. The Malaspina is now 408 feet long, with capacity for 88 vehicles (20' lengths), and a service speed of 16.5 knots. Passenger services include a cafeteria, gift shop, cocktail lounge, solarium, and forward observation lounge. Photo by Rodney Stitt

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M/V Matanuska

The **M/V Matanuska** was built by Puget Sound Bridge & Dry Dock Company of Seattle and began service in 1963. In 1968 the vessel was lengthened and renovated. It now carries 499 passengers and provides 4 four-berth, 21 three-berth, and 80 two-berth cabins. One two-berth cabin is wheelchair accessible. The Matanuska is 408 feet long, with capacity

for 88 vehicles (20' lengths), and has a service speed of 16.5 knots. Passenger services include a cafeteria, gift shop, cocktail lounge, solarium, and forward observation lounge. Photo by Rodney Stitt

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M/V Taku

The **M/V Taku** was built by Puget Sound Bridge & Dry Dock Company of Seattle and began service in 1963. Renovated in 1981, the vessel is 352 feet long, with capacity for 69 vehicles (20' lengths), and operates at a service speed of 16.5 knots. It can carry 370 passengers, and has 9 four-berth, and 33 two-berth cabins, two of which are wheelchair accessible. Passenger services include a cafeteria, gift shop, cocktail lounge, solarium, and forward observation lounge. Photo by Peter Metcalfe

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M/V Tustumena

The **M/V Tustumena** was built at Sturgeon Bay, Wisconsin in 1964, sailed Alaskan waters for five years, then was renovated in San Francisco in the winter of 1969. The vessel is 296 feet long, with capacity for 36 vehicles (20' lengths), and operates at a service speed of 13.5 knots. It can carry 174 passengers, and has 8 four-berth, and 17 two-berth cabins (one wheelchair accessible). Passenger services include a cafeteria, cocktail lounge, solarium, and forward observation lounge.

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State of Alaska, AMHS Web Manager, DOT&PF Employee

Communities on the Alaska Marine Highway

view video

Main Port Menu

Inside Passage/ Southeast	Southeast Feeder Communities	Southwest Alaska	Aleutian Islands & Alaska Peninsula
Bellingham (BEL)	Angoon (ANG)	Chenega Bay (CHB)	Akutan (AKU)
Haines (HNS)	Hoonah (HNH)	Cordova (CDV)	Chignik (CHG)
Juneau (JNU)	Kake (KAE)	Homer (HOM)	Cold Bay (CBY)
Ketchikan (KTN)	Metlakatla (MET)	Kodiak (KOD)	False Pass (FPS)
Petersburg (PSG)	Pelican (PEL)	Port Lions (ORI)	King Cove (KCV)
Prince Rupert (YPR)	Tenakee Springs (TKE)	Seldovia (SDV)	Sand Point (SDP)
Sitka (SIT)		Tatitlek (TAT)	Unalaska /Dutch Harbor (UNA)
Skagway (SGY)		Valdez (VDZ)	
Wrangell (WRG)		Whittier (WTR)	
Yakutat (YAK)			

Other popular destinations visited by many Alaska Marine Highway travelers include Anchorage, Denali National Park, Fairbanks, and the Matanuska-Susitna Valley. For information about more Alaskan towns and cities, see the Alaska Department of Community and Economic Developments' list of every community in Alaska and the Alaska State Chamber of Commerce Web site.

Southeast Alaska / Inside Passage

The Inside Passage is a protected waterway on the northern Pacific coast of North America, replete with spectacular rain forests, mountains, and glaciers. AMHS's service through the Inside Passage is served from road connections at Bellingham, Washington and Prince Rupert, British Columbia, in the south to Haines and Skagway, Alaska, in the north.

Bellingham

Bellingham, Washington, southernmost terminus of the Alaska Marine Highway System, is 1-1/2 hours north of Seattle and one hour south of Vancouver, British Columbia. It is the traditional gateway to the San Juan Islands and Alaska. Bellingham's new multi modal facility offers train, bus, Alaska, Victoria and San Juan Island ferry service, all in one location. The ferry terminal and visitor information center are adjacent to the historic Fairhaven district. Shuttle services are available for travel between the terminal and major airports. See the Port of Bellingham for information about this multi modal facility, and the Bellingham Convention and Visitors Bureau Web site to find out about activities and events in Bellingham and Whatcom County.

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Haines

Haines connects the Inside Passage with the Alaska Highway at Haines Junction, in Canada's Yukon Territory. While in Haines, visit historic Port Chilkoot, the Native arts center, or camp within sight of glaciers at Chilkat State Park. The highlight of autumn is viewing the largest gathering of bald eagles in the world at the Chilkat Bald Eagle Preserve just outside the town. Many travelers board the ferry at Haines

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and sail to nearby Skagway, birthplace of the Klondike Gold Rush. See also Haines Visitor Bureau Home Page.

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Juneau

Juneau, Alaska's bustling capital and gateway to Glacier Bay, nestles between towering mountains and the Gastineau Channel. Although a modern city, Juneau wears its romantic Gold Rush past proudly. Exhibits, museums, and enchanting performances are waiting to entertain you. The Mendenhall Glacier and U.S. Forest Service Visitor Center offers programs, a naturalist to answer questions, trails and nature walks, and a panoramic view of the glacier face. Nearby Admiralty Island National Monument shelters the largest brown bear population in Southeast Alaska. See also The Juneau Web and Juneau Convention & Visitors Bureau.

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Ketchikan

Ketchikan is Alaska's southernmost major city. Its waterfront buildings rise above Tongass Narrows supported by a forest of pilings and joined together by a picturesque boardwalk. Visit the world's largest collection of totem poles at Saxman, Totem Bight, and the Totem Heritage Center. See also Ketchikan Visitors Bureau web site.

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Petersburg

Petersburg is off the beaten path of cruise ships and is famous for its Norwegian heritage which shows so beautifully in the decorative designs found on its homes and shop fronts. Local tours await you, too, offering spectacular views of the LeConte Glacier, the southernmost tidewater glacier in North America. See also Petersburg Visitor Information provided by Petersburg Chamber of Commerce.

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Prince Rupert

Prince Rupert, British Columbia, is an ideal starting point for drivers wishing to cruise up the Inside Passage. Take an archaeology tour, or visit the Museum of Northern B.C. with its carving shed and settlement history of the B.C.'s north coast. Tour the North Pacific Cannery Village Museum, a restored heritage site which offers a live performance to highlight its history. See also B C Ferries Corporation for sailings to Prince Rupert from other Canadian ports.

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Sitka

Sitka was the seaside capital of Russian America and a visit here is like stepping back in time to the 18th century. Visit St. Michael's Cathedral, one of the finest examples of rural Russian architecture. Stroll through the town's quaint shops and enjoy performances of Russian dancing. All of this entertaining history is presented under the shadow of stately Mr. Edgecumbe, a 3,201-foot-high, Fuji-like extinct volcano. See also Sitka Convention & Visitors' Bureau.

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Skagway

Skagway, the "Gateway to the Yukon," owes its birth to the Gold Rush of '98. The U.S. Park Service and the City of Skagway have made this one of the best historic sites in Alaska. The Klondike Highway follows part of the White Pass route and connects with the Alaska Highway at Whitehorse, Yukon Territory. See also Skagway Visitor Information.

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Wrangell

Wrangell, a half-mile walk from the Wrangell Ferry Terminal, is Alaska's fourth oldest city and its only community to have existed under four nations: the Tlingit, Russian, British, and American. Its even more ancient history is revealed by mysterious, centuries-old petroglyphs that are easily seen along the beaches at low tide. You will also enjoy the Chief Shakes Community House with its many totem poles, the replica tribal Chilkat blanket, and other historic items.
Wrangell is the "Gateway to the Stikine River", the fastest free-flowing navigable river in North America. Wrangell also hosts the largest springtime concentration of bald eagles in the world. Local tours are available to both the river and the Anan Bear and Wildlife Observatory. See also City of Wrangell Web Page.

Yakutat

Located on the scenic Gulf Coast of Alaska, and surrounded by Wrangell-St. Elias National Park and Tongass National Forest. Yakutat attracts a wide variety of outdoor enthusiasts to hike beaches, float rivers, explore bays and passages, climb mountains, view glaciers, snowboard, and surf remote breaks. Yakutat Bay provides some of the finest saltwater sport fishing in Alaska. See also the Yakutat Chamber of Commerce Web Page.

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Southeast Alaska Feeder Communities

Angoon, Hoonah, Kake, Metlakatla, Pelican, Tenakee, and Hollis (connected by road to several other Prince of Wales Island communities) are all linked to mainline AMHS ports by connecting vessels. Cultural sites complement a variety of outdoor activities and excellent wildlife viewing opportunities.

Angoon

Angoon, located on Admiralty Island some 60 miles south of Juneau, is surrounded by miles of picturesque waterways noted for fishing, hunting, and sightseeing opportunities.

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Prince of Wales Island

Prince of Wales Island, about 45 miles west of Ketchikan, receives ferry service at Hollis. It connects Craig, Klawock, Hydaburg, Thorne Bay and Coffman Cove. This area is noted for the good hunting and fishing along the roadways. Visitors will be particularly entranced by the many local examples of authentic Indian heritage.

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Hoonah

Hoonah was once the major village of the Huna Indians, a offshoot of the Tlingit tribe. Fishing boats line the harbor, and seafood processing is the major industry. Pleasure fishing in the area is excellent for Silver and King Salmon, as well as Cutthroat, Rainbow, and Dolly Varden trout.

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Kake

Kake is named for the tribe of Tlingit Indians which has occupied Kupreanof Island since prehistoric times. It is the site of the world's largest totem pole -- 132.5 feet high -- and enjoys a brisk logging and fishing trade.

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Metlakatla

Metlakatla is located on Annette Island, at the southern tip of Alexander Archipelago in Southeastern Alaska. Originally a religious colony, Metlakatla's population first consisted of 800 Tsimshian Indian converts who had moved from British Columbia. The native name means, "a passage joining two bodies of water."See the Metlakatla Tours/Metlakatla Indian Community Site for more information.

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Pelican

Pelican, in the mid 1930's, was nothing more than two large barges serving as cold storage for locally-caught salmon. Pelican grew with the fishing industry, and now consists of a main boardwalk and a cluster of weather- worn buildings that cling to the side of Chichagof Island. Besides great fishing and beautiful scenery, Pelican's main attraction is Rosie's bar, where fisherme have been carving their initials in the ceiling since the first beer was served. See the Pelican Web site for up-to-date information.

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Tenakee Springs

Tenakee Springs was once a leading Alaska spa, with early miners coming from around the Territory and the Yukon to "take the waters" of its warm mineral springs. Today, the year-round residents are joined by summer visitors who still come to "take the waters" but who have also discovered the excellent saltwater fishing in the area.

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Southwest Alaska

AMHS' Southwest Alaska route serves communities in Prince William Sound and on Kodiak Island. These routes are served by road connections at Valdez, Homer, and Whittier (via the Alaska Railroad).
See also Southwest Alaska trip planning information.

Chenega Bay

In 1996, the Alaska Marine Highway began "whistle-stop" service to the small communities of Tatitlek and Chenega Bay, made possible by the construction of new docks to provide staging areas for oil spill response capabilities in Prince William Sound.

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Cordova

Cordova is a fishing port where you can watch commercial fishermen bring in their catch or try your hand at Alaska-style sportfishing. Tour the salmon canneries, visit the famed "million dollar bridge", walk on Sheridan Glacier, or ride the chair lift to the top of Eyak Mountain. The activities and adventures are endless.
Cordova Chamber of Commerce Web Page.

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Homer

Homer sports a lively recreation scene along the 5-mile long, world-famous Homer Spit, and offers travelers an unbelievably spectacular view of Kachemak Bay. The harbor is lined with charter boats for hire, and fresh halibut, crab and shrimp can be purchased from seafood shops along the docks. For more information, go to the excellent Homer Chamber of Commerce site.

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Kodiak

Kodiak was the first capital of Russian America (1783-99), and remnants of the Russian occupation are still evident today. Kodiak also harbors Alaska's largest commercial fishing fleet and is home to the mighty Kodiak Brown Bear. Close to 3,000 of these giant bears live in the Kodiak National Wildlife Refuge. Visit the Kodiak Chamber of Commerce and Convention & Visitors Bureau site for more information.

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Port Lions

Port Lions, in Settler Cove on the northeast coast of Kodiak Island, offers the amenities of larger destinations such as full-service hunting and fishing lodges, the beauty of waterfalls tucked away in spruce-filled coves, beach combing, and sea kayaking through the still, blue waters of Kizkuyak Bay.

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Seldovia

Seldovia is accessible only by air or water and, therefore, has been able to maintain many of its age-old Russian traditions. Seldovia offers a view of Alaska's fishing industry with vessels moving in and out of Kachemak Bay, fresh catches in live tanks and fish processing at a local salmon plant. See also the Seldovia Chamber of Commerce site.

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Tatitlek

In 1996, the Alaska Marine Highway began "whistle-stop" service to the small communities of Tatitlek and Chenega Bay, made possible by the construction of new docks to provide staging areas for oil spill response capabilities in Prince William Sound.

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Valdez

Valdez began as a trading station in the early 1890s and served as a port of entry for gold seekers bound for the Klondike. The old city was destroyed by the 1964 earthquake, but its spirit lives in a new Valdez. This ice-free, saltwater port is the terminus of the 800-mile trans-Alaska pipeline, which carries oil from the North Slope. See also Valdez Convention & Visitors Bureau Web page.

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Whittier

Whittier is nestled between the glacier-capped Chugach mountains and Prince William Sound. Built by the U.S. Government during World War II as a hidden port, today Whittier is the gateway to a recreational wonderland. In May of 2000, a highway from Whittier to the Interior opened to the public. This spectacular drive from the edge of Prince William Sound through the Chugach mountains winds through a series of tunnels, and connects Whittier to Anchorage only 45 miles to the south. Travelers also have the option of taking the famed Alaska Railroad from Whittier all the way to Fairbanks.

Passengers traveling to and from Whittier, and especially those departing on the M/V Bartlett from Whittier, are advised to check the Whittier Tunnel web site for a schedule of when the tunnel is open to vehicle traffic. *You may be unable to make your sailing if you do not arrive at the tunnel at a time when it is open.* Bicycle and foot traffic is prohibited through the tunnel, and there are vehicle size and other restrictions of which you should be aware before traveling through the tunnel. For a recording of the base schedule, call the Whittier Tunnel toll-free at (877) 611-2586.

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Aleutian Islands and Alaska Peninsula

The Aleutian Islands and Alaska Peninsula sweep more than 1500 miles from Cook Inlet toward Asia. This region sits atop the "Ring of Fire," a string of volcanoes along the Pacific Rim, and boasts several wildlife refuges. The harsh weather precludes ferry service in the winter, but each spring the Alaska Marine Highway resumes its regular sailings to the seven westward communities of Chignik, Sand Point, King Cove, Cold Bay, False Pass, Akutan, and Unalaska/Dutch Harbor.

Akutan

Akutan is located in the center of some of the most productive fishing grounds in the world, and huge amounts of seafood products -- primarily crab, halibut, cod, pollock -- are processed in the shelter of its deep bay and at a large shore-based processing plant. Although the Aleut population of the local village remains at 90-100, it grows to about 1,000 during certain fishing seasons.

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Chignik

Chignik is actually three villages: Chignik Lake, Chignik Lagoon, and Chignik Bay, where the State ferry docks at one of two canneries at its first stop on the run out the Aleutian chain. Like the other Aleutian Island communities, Chignik provides a fishing lifestyle for its residents in a rugged but beautiful environment. In the Aleut language, "chignik" means "windy".

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Cold Bay

Cold Bay, located 634 air miles from Anchorage, is surrounded by the Izembek National Wildlife Refuge. Abundant seabirds and waterfowl, as well as caribou and brown bear, make it a popular spot for sportsmen and naturalists. Two active volcanos provide a spectacular backdrop for the community.

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False Pass

False Pass is a picturesque Aleutian community in a strategic location. The town sits on the south side of Isanotski Strait, the shortest transit route between the Gulf of Alaska and the Bering Sea. Its economy is based on fisheries: mostly for salmon, herring, halibut and crab.

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King Cove

King Cove rests on a sand spit and adjacent uplands which are located at the north end of a natural bay nestled between high mountain ridges. The community of 1,000, mostly Aleuts, has developed around one of the largest fish processing centers in the United States.

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Sand Point

Sand Point was originally founded as a cod fishing station in 1887, and today it continues to support the regional fishing industry. The city's harbor is home to a locally based fishing fleet, and is also heavily used by transient vessels during and between fishing seasons. Its population is mostly of Aleut and Scandinavian descent.

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Unalaska/Dutch Harbor

Unalaska/Dutch Harbor, at the end of the Aleutian Chain, is also its largest community, with over four thousand residents. A busy fishing and seafood processing port, Dutch Harbor is also a tourist destination, with sportfishing, bird and wildlife viewing, cultural and historical exploration, or hiking and beachcombing awaiting the adventurous traveler. Visit the Unalaska/Port of Dutch Harbor Convention and Visitors Bureau home page for travel information, events, weather, and more.

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MARINE HIGHWAY TRANSPORTATION IMPROVEMENT STUDY – PART I

SUSTAINABILITY OF THE ALASKA MARINE HIGHWAY SYSTEM

PREPARED FOR:

SOUTHEAST CONFERENCE
JUNEAU, ALASKA

PREPARED BY:

McDowell GROUP

JUNEAU • ANCHORAGE

MAY, 2002

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PRELIMINARY CONCLUSIONS AND RECOMMENDATIONS

Southeast Conference has contracted with the McDowell Group to assess the potential benefits of commissioning a comprenensive, independent study of the future of the Alaska Marine Highway System. The task of identifying the key components of such a study is not yet complete. However, the need for it, as the AMHS approaches its 40th anniversary next year, is compelling.

Alaska's Marine Highway System (AMHS) is entering a period of profound change. With its financial reserves exhausted, vessels in need of major refits or replacement, an intractable cost structure and waning political support, cuts in service seem imminent. Yet the communities it serves are heavily dependent on reliable marine transportation. The next five years will see the system navigate one of three courses:

- **Steady decline in service.** The gap between operating costs and state funding has widened each year since 1995. If the system and its users are unable to muster the political support to alter this trend, service levels cannot be maintained. Further, it is not clear that the additional financial resources needed to modernize the system will be available.

- **Abrupt restructuring.** Radical new management models proposed in this and prior legislative sessions might be imposed, though without any real understanding of whether these models will be able to solve the problems facing the system.

- **Transition to a new, well-conceived management and operations model.** With interim financial support and careful planning, operations and service levels may be aligned with available, secure funding sources *over the long-term.*

Why is "fixing" the system so difficult? The Alaska Marine Highway operates in an environment with market, political and operational challenges unlike those anywhere else in the world. Its service mandate is broad, its markets small and diverse, and its political support increasingly fragmented. Typically, annual appropriations fall approximately $10 million short of what is needed to sustain operations. The balance has come from a now-depleted reserve fund. Success over the long-term will require a carefully crafted combination of management, operations and funding strategies (and execution).

Yet the value of the system is clear. In addition to providing transportation to communities with no other options and infrastructure for several regional economies, Alaska's Marine Highway System has an annual economic impact estimated at $171 million in 1995.

Conclusions

This preliminary study identified the following key issues concerning the sustainability of ferry service in Alaska:

- The Marine Highway continues to serve critical infrastructure needs in coastal Alaska.
- The system is in financial crisis.
- The issue of how to make the Marine Highway system financially sustainable has not been resolved.
- The current operating model is outmoded and no longer adequately meets the needs of users.
- The Southeast Alaska Transportation Plan holds promise, but leaves many important questions unanswered.
- The existing management structure may not be sufficient for the future, and other management models exist that are worthy of consideration.
- Proposed legislation leaves some key issues unaddressed.

The Marine Highway serves critical infrastructure needs. Even more now than when it was conceived half a century ago, the system is a socio-economic lifeline for its communities. A number of smaller communities are extremely dependent on the AMHS for the movement of basic goods. In addition, it provides the basis for regional trade and may be key to addressing new seafood markets. The system is also a critical element in the visitor industry statewide.

The system is in financial crisis. A reserve fund that peaked in 1995 at $46 million, is now fully depleted. While earned income has been relatively steady at 54 percent of operating expenditures, general fund appropriations to the Marine Highway Fund have declined from 49 percent of expenditures during the late 1970s and 1980s to 37 percent of expenditures during the past five years. Confronted with proposed FY03 funding that is $6.6 million below the AMHS request, managers have outlined a program of service cuts and vessel lay-ups. Even if next year's funding is restored, the gap between earned income and operating expenses is expected to remain at roughly $40 million per year until the SATP is substantially implemented (currently projected in 2008). Even with planned improvements, however, expenses are projected to outstrip earned income by $32.7 million in 2010 according to AMHS planning documents. This is $4.5 million more than the average annual general fund appropriation over the past decade.

The issue of how to make the Marine Highway system financially sustainable has not been resolved. A formal evaluation of alternative financial models and their implications for Alaska has never been performed. Some long-term, acceptable balance of public funds and earned income must be achieved, yet none has yet been proposed.

The current operating model is outmoded. The operating model on which the AMHS has been based since its inception clearly is no longer acceptable. Both vessels and cost structure are inflexible. The system is unable to meet users' highest priority need: regular and convenient schedules.

The Southeast Alaska Transportation Plan holds promise, but leaves many questions unanswered. A new Alaska ferry operations model is articulated in the Southeast Alaska Transportation Plan (SATP): faster ships, shorter runs, smaller crews. In fact, regional self-sufficiency is an explicit goal of the SATP. However, the Plan does not specify how self-sufficiency is to be achieved, and critical elements remain either

unknown or undefined. While fast catamaran vehicle ferries are increasingly used worldwide, they have not been tested in Alaska service. Further, critical elements of the SATP are either in limbo or have been added or dropped in ad hoc fashion in the years since the plan was first developed. These include key road links, location of terminals, the structure of individual routes, and whole vessels, for example to provide mainline service not envisioned by the original SATP, but subsequently determined to be desirable.

SATP financial projections are not sufficiently detailed to generate confidence in the financial performance of the system in actual operation. The potential response of AMHS's largest market segment, the visitor market, to SATP-type service is unknown and largely untested. Given what has been learned from the *Alaska Marine Highway Marketing and Pricing Study (2000)* and other recent analyses, do the load factors projected in the SATP still seem reasonable? If not, what is likely to be the impact on fares and service? Finally, with the legislature reluctant to authorize GARVEE bonds for construction of new vessels, how will the SATP be implemented and over what period of time?

The existing management structure may not be sufficient for the future, and other models exist that are worthy of consideration. Community testimony about ferry service and the role of the Department of Transportation and Public Facilities in providing it continually echoes themes of confusion and frustration about how decisions are made and enacted. For its part, the department is caught between demands for better service at lower prices, growing pressure to cut costs, and equipment and labor contracts that largely preclude either. With no clear agreement or direction about how to resolve this dilemma, is it any wonder that AMHS decisions often appear to emerge from an inscrutable "black box?" Yet the question of whether there are better ways to manage the system in the future has not been systematically addressed.

Ferries and many other types of mass transit in the US are commonly organized as "authorities." While Alaska's needs are unique, aspects of this model may help address the seemingly inherent conflict in designing a system that is responsive to user needs and also autonomous enough to operate efficiently. Preliminary research into this type of structure indicates that it holds promise. For example, the Inter-Island Ferry Authority recently inaugurated independent ferry service between Ketchikan and Prince of Wales Island. However, significant questions remain. There is neither another ferry system nor a transportation authority in the US that approaches the geographic scope of Alaska's Marine Highway. Further, authorities are typically based on a predictable revenue stream that makes them relatively independent of annual appropriations. The mechanism by which this would occur system-wide in Alaska has not yet been identified. Other public/private hybrids that may be relevant include selective privatization and public/private partnerships.

Proposed legislation leaves some key issues unaddressed. Two bills introduced this legislative session – SB 130 and SB 271 – proposed sweeping changes to the structure of AMHS. However, neither addressed fundamental questions about how service levels should be determined or on what basis they should be funded. Two characteristics of the Alaska Railroad – relative insulation from the political process and a portfolio of revenue-producing real estate and other assets — hold promise for ferries as well. However, merging the two systems, as SB 271 proposed, does not seem a good solution. Neither is it clear that the type of board structure envisioned in both bills will work well for a system the size and complexity of AMHS.

Recommendations

The Alaska Marine Highway System is at a critical juncture. It cannot continue with business as usual because the funding is not available. It may be able to buy time to implement a new operating model. However, the Marine Highway Fund has been used to buy time since 1995 to the tune of $46 million. The new system (as described in the SATP) is still several years away and to some extent undefined. As time erodes so do options and the chance to act in a deliberate and thoughtful way. With Alaska's coastal infrastructure needs heavily wagered on the SATP model, the stakes are high.

McDowell Group therefore recommends that the following broad questions be examined in order to better identify the Marine Highway that will best meet the future needs of Alaska:

- What entity or combination of entities is most likely to operate the Marine Highway System in a way that achieves the best possible mix of cost control, service provision (passengers and freight), and revenue generation? Possibilities include:
  - A government department (current method)
  - One or more public corporations or "authorities," for example, similar to the Alaska Railroad or the Inter-Island Ferry Authority
  - One or more private corporations
  - Some combination of the above
- What is the financial performance of the SATP as currently conceived likely to be? What capital and operating decisions are most critical to that performance? On what basis and by whom should those decisions be made?
- What mix of public (federal, state, and local) funding and earned income will provide the most stable basis for Alaska's marine transportation infrastructure and how can it be achieved? This is the most pressing issue for the system, since none of the other improvements can be implemented unless this problem is solved.

Related issues include how to balance statewide, regional and local needs and interests, and the how ferry service will be integrated with other transportation infrastructure.

This White Paper presents limited, preliminary research into alternative approaches to marine highway service in Alaska. It is not intended to provide answers to these difficult questions. Rather, it suggests avenues for further investigation and analysis.

The paper discusses why this is a critical opportunity for the Marine Highway and outlines steps to help ensure that the opportunity is not lost. Attachments include a preliminary framework for evaluating management models and descriptions of a few of the relevant management and operational structures to be found in and outside Alaska.

Situation Overview

Role of the Marine Highway

Of the 32 Alaska communities currently served by state ferries, only a handful are connected to the road system, and just a dozen have jet service. For the others, small planes, private boats and an occasional barge are the only outside links. Regionally, the Marine Highway System provides the only reliable transport between most of these communities. Airplanes – both small and large – are expensive, weather dependent, and capacity constrained. The Alaska Marine Highway provides a surrogate road system and a foundation for regional trade.

For the state as a whole, the Marine Highway System is both a key visitor access point and one of the state's best known and most popular destinations. The system carries approximately 50,000 non-resident visitors per year either into or out of the state. These visitors stay in Alaska an average of more than two weeks. All told, approximately 140,000 visitors travel each year on the Marine Highway at some point during their visit. They travel widely, with nearly half (47 percent) visiting Anchorage.

As a recreational attraction, the Marine Highway has few parallels. Ninety-three percent of summer travelers – visitors and locals alike – rate their overall experience on the Alaska ferries good or very good. Nearly all summer passengers use the ferries primarily for pleasure and to experience the Inside Passage, Prince William Sound and other coastal waterways in a special way. Two thirds of summer passengers do not consider another alternative when making their trip plans, and only 7 percent consider traveling by cruise ship.[1]

Mission of the AMHS

The formal mission of the AMHS is not entirely clear, a condition that has contributed to the volume, if not the quality, of debate on the system. According to Legislative Research Report 02.016 (December 14, 2001), the published mission of the Alaska Marine Highway System is "to provide safe, reliable, and efficient transportation of people, goods and vehicles among Alaska communities, Canada and the 'Lower 48,' while providing opportunities to develop and maintain a reasonable standard of living and high quality of life, including social, education and health needs."

The *AMHS 2000 Traffic Volume Report* articulates a mission "to serve Alaskan communities by providing passenger, freight (van) and vehicle transportation service between communities without land highway connections. This service helps meet the social, educational, health and economic needs of Alaskans." The Southeast Alaska Transportation Plan (SATP) reinforces a view of the Marine Highway as necessary infrastructure. The Plan, which largely concerns itself with ferry service, offers as one of its six formal goals to "support local economic development and strength through the provision of adequate and affordable transportation...."

[1] *Alaska Marine Highway System Marketing and Pricing Study*. McDowell Group, 1999-2000.

Residents of AMHS-served communities often cite the system's designation as part of the national highway system as evidence that it is intended to meet the same essential needs as a land road, and with the same expectation of public subsidy normally associated with highways. However, according to the Legislative Research Agency, "the phrase "essential service" was not mentioned in the AMHS enabling legislation." The agency suggests that "... legislators may have acted under the assumption that the AMHS would eventually become self-supporting, as one pre-statehood report predicted."[2]

Historical Performance

In AMHS's early years, the new services and vessels were warmly welcomed and became, by default, the benchmark against which expectations were measured. Prior to 1975, the whole system ran on $20 million per year, about two-thirds of which was earned income. By 1985, operating costs had nearly tripled, to approximately $62 million per year. They have continued to rise at about half the rate of inflation[3], to the current level of $80 million.

Ridership has trended somewhat differently. After rising more or less steadily into the early 1990s to a high of 420,000 annual passengers, ridership declined. In 2000 351,000 people rode the Marine Highway, about 20,000 fewer than in 1985.

The most often cited reasons for the increase in operating costs are labor contracts and new Coast Guard regulations. Law makers have also accused the AMHS of being "top heavy" in management. However, the *Marketing and Pricing Study* of 2000 noted that certain management capacity considered critical to private sector marine operations – namely marketing, customer relations and reservations – was woefully inadequate at AMHS and, further, that this was a significant cause of the system's declining ridership.

If there is "excess" management at AMHS, it seems more likely to lie in the cumbersome contracting and oversight mechanisms that may be inherent in public services. For example, a 2001 *Ferry Operations and Service Study* of northern Southeast Alaska routes added an 11 percent premium to its estimates for new vessel construction to account for the difference between historical state contracting costs and those typical of the private sector. The state's lengthy dispute with the builders of the Kennicott, which cost nearly $80 million, seems to bear out that approach.

Current Financial Situation

Declining state support together with failure to raise fares and market effectively during a decade of rising costs have left Alaska's Marine Highway System (AMHS) on a precipice and without a net. Although the system typically earns more than half the amount of its operating expenses, this leaves a significant gap. For reference, the Washington State Department of Transportation ferry system, with much simpler routes and a much larger market, earns only about 60 percent of its operating costs.

The AMHS has been demonstrably in financial crisis since 1995. At that time its operating reserve in the Alaska Marine Highway Fund reached a peak of $46.3 million and began to decline. Ostensibly established (July 1, 1991) to see the system through short-term and emergency expenditures, the fund's reserve balance has not functioned for that purpose. Rather, it has been used to fill an ever-widening gap between the sum

[2] Legislative Research Report 02.016
[3] Based on the national Consumer Price Index

of AMHS earned income plus annual legislative appropriations and the system's actual operating expenditures.

Since FY 1996 operating revenues have increased slightly from around $39 million to $42 million. Legislative appropriations have held between $27 and $29 million. However operating costs have trended steadily upward since 1998. The gap between revenues and expenses is now in the neighborhood of $10 million per year.[4]

Reserve funds were exhausted during FY 2002. As a result, a recent proposal by the legislature to fund AMHS at $6.6 million less than its requested level for FY 2003 is projected by DOT/PF to result in service reductions for three vessels and the accelerated retirement of two others, also resulting in less service. Unless the system is drastically reconfigured or receives substantially more public funding, it seems clear that routes must be permanently cancelled and vessels idled.

The Alaska Marine Highway Vessel Replacement Fund was also designed as a "savings account" for the system, this one to provide for repair and replacement of aging vessels. Most of these capital expenses have been covered by federal highway and transit funds. The balance of the Vessel Replacement Fund is currently zero.

Summary of AMHS Operating Budget (in $millions)
1991 to 2000 with 2001 and 2002 Projected

Fiscal Year	AMHS Fund Beginning Balance	AMHS Revenue to AMHS Fund	General Fund Subsidy to AMHS Fund	AMHS Operating Expenditures	AMHS Fund Ending Balance
1991	0.0	40.5	70.5	70.5	40.5
1992	40.5[5]	44.1	30.7	69.7	45.6
1993	45.6	42.2	30.0	71.6	46.1
1994	46.1	41.7	28.7	71.1	45.4
1995	45.4	43.6	28.4	71.1	46.3
1996	46.3	39.0	28.3	69.5	44.0
1997	44.0	38.6	28.6	69.9	41.4
1998	41.4	37.4	26.9	68.0	37.7
1999	37.7	38.8	27.3	74.0	29.8
2000	29.8	40.3	27.1	75.2	22.0
2001	22.0	42.7	27.9	80.1	12.5
2002	12.5	42.6	28.8	80.5	3.5

Source: Legislative Research Report, December 14, 2001, Report #02.016

[4] Amounts are approximate and based on analysis and projections prepared during FY 2001 by Legislative Finance Division.
[5] The AMHS Fund became effective July 1, 1991. It was capitalized with $40.5 million from prior year AMHS revenue.

Source of the Gap between Revenues and Costs

In fiscal year 2000, ferry system revenues covered 54 percent of operating expenditures, and no capital costs.[6] While it is the norm for public transportation to cost more than it brings in, AMHS operating costs of approximately $1.25 per passenger mile are high.[7] Excess capacity, inefficient vessels, unprofitable routes or schedules, inflexible labor costs, and inadequate peak prices and off-peak price differentials are the main drags on operating margins. Historically, labor costs have represented approximately 70 percent of the AMHS operating budget.

Revenues

Market studies have identified lack of consistent, convenient scheduling and a responsive reservations system as the biggest barriers to increasing local ridership. A combination of 24 hour crewing, tidal restrictions and long, complex routes makes it difficult to spread service evenly over the week or month and impossible to schedule arrivals and departures at convenient times of day. Telephone hold times on the reservations system have improved recently, but historically have exceeded industry standards by a factor of five or more.

Simple follow-up target marketing has been identified as the most effective way to increase business, but, until recently, the system has lacked the capacity to execute it. Years of administrative downsizing together with a general lack of private-sector visitor industry experience and orientation have resulted in steadily declining visitor sales during a period of rapid expansion in the cruise industry. Alaska arrivals via AMHS declined 37 percent overall from 1989 to 1999. During the same period cruise ship arrivals increased by 200 percent.[8]

This suggests that management structures designed to respond to a market model could make a major contribution to the sustainability of the ferry system. A more market-oriented system could employ the profit incentive and shed political constraints to reach more optimal capacity, vessel and service configurations, routes, service schedules, labor schedules and costs, and pricing.

Costs

The same factors that hamper the system's ability to respond to market needs combine to leave current ferry management with few options for cost control beyond large cuts in service. Labor and fuel cost are the two significant variables in vessel operations efficiency. Both are largely pre-determined by existing vessels and routes. When vessels operate for more than 12 hours in succession, as AMHS vessels do, the Coast Guard requires that they carry a fresh crew aboard to assume operations at or before the 12-hour deadline. The Coast Guard also sets requirements for the number and type of crew that must be aboard depending on the type of vessel and service.

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[6] Table 2, *A Summary of the Legislative and Fisc ' History of the Alaska Marine Highway System*, Legislative Research Report No. 02.016, December 14, 2001.

[7] For comparison, operating costs for BC Ferries in 2001 were approximately $0.95 per passenger mile.

[8] McDowell Group, Alaska Marine Highway System Marketing and Pricing Study, 2000. Vol I, page 49.

To the extent that there has been room within Coast Guard regulations to institute labor savings, the AMHS has had little success in the past obtaining labor contracts that accomplish this. In 1997, an attempt to take a hard negotiating stance with the three AMHS unions – the Marine Engineers Beneficial Association, the Masters, Mates and Pilots union, and the Inland Boatman's Union – ended with little change in the system's cost structure, according to Legislative Research Report 02.016. The current three-year contracts end in 2003.

This leaves the AMHS with only one real cost-control option, cutting voyages and laying-up vessels. The option is not attractive since layup produces no revenue and labor inflexibilities limit cost savings. The fundamental problem is that the units of adjustment consist of large vessels and long routes. This means that capacity cannot be matched to demand using reasonable incremental adjustments. Any cost-saving measure big enough to be effective has a draconian impact on service.

Challenges to Continued Operation

The Alaska Marine Highway System is confronted with a funding crisis so severe that its ability to meet basic needs is in doubt. Service cuts are already being planned for this summer. Although a new operating model – faster ships with smaller crews on shorter routes – has been designed (the SATP), it is not clear that there is the political will to implement that system. Neither is it clear that the current management structure – resource-thin and battered from years of political wrangling – is the best choice to operate it. Finally, it has not been demonstrated publicly that the new system will, in fact, be financially sustainable.

Limits of Past Planning

Unknowns in the SATP

The Southeast Alaska Transportation Plan (SATP), developed over the past decade, recognizes many of the shortcomings of today's AMHS. It identifies a new service paradigm consisting largely of faster ships, smaller crews and more direct routes. However, to implement these recommendations without also looking hard at the operating entity charged with making them work and the financing mechanisms that will keep them solvent is to set the stage for failure. The SATP, itself, was developed within the system that produced the current malaise and may be expected to reflect that system's limitations. These include limited understanding of markets and marketing, susceptibility to political pressure and a general lack of private sector experience in setting and achieving financial performance goals.

Most critical, the SATP was not designed to be financially sustainable. It calls for vessels and routes that should, in theory, be more economical. However, it does not identify either a funding mechanism or an operating rationale to ensure stable, sustainable service. In fact, the plan represents something of a "Cadillac," with its combination of fast point-to-point service and continued mainline routes supplemented by occasional Inter-Island Ferry Authority (IFA)-type vessels.

Shortcomings of Other Planning

Ferry system planning to date has, to the study team's knowledge, been conducted in sound, workmanlike fashion. However, it suffers from a systemic shortcoming: the agenda and scope of work in nearly all cases have been determined by DOT/PF. *The Socio-Economic Impacts of the Southeast Alaska Transportation Plan on Petersburg* (2000) is something of an exception. However, it, too, was funded by the Department.

A result of DOT/PF's approach to planning is that, by and large, the objective has been to identify the most cost-effective alternative, including the "status quo" or "do nothing" alternative. Not generally included, however, are attempts to identify the most financially sustainable alternative, or to re-think the fundamental rationales behind service provision.

Further, the world of ferries, especially fast ferries, is changing rapidly. This evolution is being tracked on many fronts. The US Transportation Research Board currently catalogues more than 50 recent studies pertaining to ferries, ranging from new ways to project ridership to environmental impacts, to analysis of how public decisions are made. The Board is undertaking its own National Ferry Study on the evolution and current status of US ferry systems.

Ferry transportation in many other countries is more advanced than in the US. However, little is known about the financial structure of these operations because most of them are private companies. An attempt by independent consultants to learn more in this regard was largely unsuccessful, according to AMHS management.

Limits of Proposed Solutions – SB 130 and SB 271

Bills to alter the structure of the Marine Highway and, specifically, to create a ferry system "authority," have been introduced in the legislature since the mid-1990s. The current legislative session is considering two proposals. SB 130, sponsored by Senator Robin Taylor of Wrangell and co-sponsored by Senators Austerman and Cowdery, proposes to create a separate authority to manage the system. It's seven-member board would consist of the commissioner of DOT/PF and six citizens appointed by the governor, two of whom represent ferry system unions. Two board members must have private sector experience and others must represent the public in various specified ways.

A second bill, SB 271, sponsored by Senator Jerry Ward of Kenai and co-sponsored by Senators Austerman, Cowdery and Taylor, is similar in many regards. In its first draft, it called for state ferry service to be combined with the Alaska Railroad under a single authority charged with operation of both. A committee substitute was offered, eliminating the combination with the Railroad. The new entity would reflect the current Alaska Railroad Corporation model in that real estate holdings would be managed in such a way as to subsidize operations, at least to some extent. The new authority would be authorized to select 500,000 acres of land conveyed to the state under the Alaska Statehood Act. The bill does not address the type or location of the land, why this particular amount was chosen, or what revenues the authority would be expected to generate with it.

The bills are similar in that:

- Both amend AMHS enabling legislation with language that indicates increased state commitment to the system's financial and service stability. SB 130 goes farther, noting that the system is an "essential part of the state transportation system and that it warrants continued and predictable state support."
- Neither provides a mechanism for ensuring certain relevant expertise in the governance body. For example, no board members are required to have experience operating a profitable marine transportation system.
- The bills require the legislature to fund the system in "an amount that is consistent from year to year and is the amount necessary, after consideration of gross revenue, to provide stable services to the public consistent with the provisions of AS 19.65.050 (b) (4)" i.e., predictable and stable service. However, they do not describe a means by which to establish service or revenue expectations.
- Similarly, the bills call for vessel schedules to "optimize" the frequency of service to all ports, but do not describe how the number and choice of ports is to be determined nor on what basis frequency is to be optimized.
- Both bills also authorize management to conduct independent labor negotiations, and both provide for labor to be represented on the governing board.

Unanswered Questions

Before we risk condemning any future ferry system to the same funding, operational, and management demons that afflict this one, it makes sense to ask some basic questions.

- Will the construction and working capital to implement the Southeast Alaska Transportation Plan (SATP) be forthcoming?
- If implementation of the plan is delayed, what will happen to day-to-day ferry operations now that the Marine Highway Fund is exhausted?
- Is there a package of fair and sustainable financial support that can meet the long-term operating and capital needs of Alaska's ferries, and make the system less vulnerable to annual budget trade-offs?
- What set of routes, vessels and services would maximize the potential of the system to earn income?
- Can the system be designed so that basic operating decisions about who gets service and how often avoid becoming mired in political turmoil? What can we learn from other systems in this regard?
- What management and governance structure is most likely to succeed at meeting the system's dual mandates of basic transportation infrastructure and income generation while demonstrating a standard of efficiency that makes it financially justifiable. Again, what models might provide guidance?

In simplest terms:

What mix of service, management and funding will make for a ferry system that is stable, sustainable and that best meets state and regional needs?

A Vision of Sustainability

In the words of the Alaska Legislature's Legislative Research Services, AMHS's ... "self-imposed mandate – to provide basic transportation services to Alaskan communities – has been the source of much controversy and debate in the legislative and public arenas."[1] No one has ever defined "basic transportation" nor identified a mechanism by which to determine appropriate funding. This is not uniformly the case for other Alaska public "enterprises," however.

Other Alaska Models

The State has used its resources to subsidize other activities that are normally viewed as a less essential government activity than provision of transportation. The Alaska Housing Finance Corporation ("AHFC") has received more than a billion dollars to subsidize interest rates to homebuyers. The Alaska Industrial Development & Export Authority ("AIDEA") at one time had $388 million in capital contributed by the State to subsidize business loans. Hundreds of millions were spent by the State to subsidize power production and distribution by building the Bradley Lake and Four Dam Pool hydroelectric facilities and the Railbelt Intertie.

Approximately $190 million ($100 million from the Constitutional Budget Reserve and about $90 million from sale of the Four Dam Pool hydroelectric facilities) has been used to endow the Power Cost Equalization program, which subsidizes rural electric rates. $100 million was appropriated to the Alaska Science & Technology Foundation to promote scientific and technology development.

The Future of AMHS

The programs just mentioned differ from the Alaska Marine Highway System in one important respect. Each was designed, after a start-up period, to reach a level of financial sustainability after which continued large infusions of cash would not be required. While this may have been an intention on the part of legislators who authorized the start-up and evolution of the AMHS, it has not been an explicit operating goal.

Yet it is within the realm of possibility, indeed necessity, for the Marine Highway System to provide "basic transportation" while requiring no more than a generally acceptable level of operating subsidy. "Necessity" because infrastructure that is annually at risk of curtailment due to lack of funding cannot be the basis for a healthy regional or statewide economy.

The critical elements of sustainable service are discussed in the following section.

[1] *A Summary of the Legislative and Fiscal History of the Alaska Marine Highway System*, page 4.

Three Elements of Sustainability

Each of three critical elements of the system must be in place and coordinated with the other two:

- Management
- Operations
- Finances

Past ferry studies, including the Southeast Alaska Transportation Plan, have focused on operations. At best, this is enough to build a one-legged stool, and even that leg is not clearly drawn.

Management and Governance Planning

The attachment "Evaluation of Potential Management Models" discusses three broad management approaches: public, private and some combination. Each type has strengths and weaknesses with respect to the Alaska Marine Highway System. Purely public entities tend to be more subject to political pressures and less skilled at business tactics. Private sector firms may not be responsive to public needs and may not have access to certain types of funding. Public/private hybrids are possible, but require careful structuring and monitoring.

Preliminary analysis suggests that the "authority" model, variously used for ports, transit systems, bridges, tunnels, ferries and airports, offers some advantages for Alaska's ferry system. Authorities are overseen by a board of directors charged with meeting both service and financial goals. They typically are able to act more independently than government line agencies (departments).

Placing the ferry system in the hands of an authority is not a panacea, however. The degree to which it is publicly responsive depends on the makeup of its board and the nature of its mission. Extending this line of reasoning to its logical extreme suggests that responsiveness might be maximized under multiple sub-regional authorities similar to the IFA. The mechanism by which those bodies might work together to provide an efficient whole is by no means clear, however.

Further, an authority's independence relies heavily on its ability to cover its own costs. Authorities are generally designed so that the sum of their operations makes them self-supporting. Within a port or transit authority, for example, bridge tolls may be used to subsidize ferry service.

Further analysis of a range of potential management entities is warranted. Entities should be evaluated on the extent to which they are able to:

- Control operating costs
- Generate revenues
- Access appropriate public funds
- Engage in effective contracting negotiations

- Make timely, well informed business decisions
- Understand and respond to local, statewide and visitor market needs
- Meet the requirements of vessel and port operations
- Manage effectively all the assets of the system

Operations and Service Planning

There is no need to replicate the planning process undertaken for the SATP. It is generally accepted as having been reasonably thorough and most of its fundamental findings are not at issue. However, is the SATP a financially sustainable operations plan? The answer is that no one knows. Sustainability was not a goal of the SATP process. Rather, the plan sought the "best balance of cost and service," a quality that clearly depends on one's perspective. Financial projections for the SATP demonstrate that it compares well with other operating options *at a particular level of service*. However, the projections do not provide guidance with respect to how service can best be modified, should financial considerations demand.

The Inter-Island Ferry Authority (IFA), on the other hand, is predicated on sustainability, that is, on fares covering operating costs. Whether this will prove achievable is not yet known. Although its scope of operations is tiny compared to AMHS, IFA may be an instructive case study.

The IFA-type vessel is another variable. The SATP identifies a number of advantages to small passenger vessels built under Subchapters T and K of Coast Guard regulations. However, it leaves their potential deployment in Southeast Alaska unspecified. Further analysis is needed to understand the financial implications of using these vessels for day and, possibly, 24-hour service, or day service with the vessels overnighting in outports, depending on scheduling demands.

Other unresolved SATP issues include decisions about certain key road links and terminal locations and about the nature and cost of ground transportation needed between proposed terminal sites.

To address these issues, the SATP must be translated into a business plan. It must specify the degree to which each of its services is expected to contribute to net revenues. It must define the best *sustainable* balance of cost and service system-wide. This means that, if an unprofitable service is to be pursued, the source of its subsidy must be identified, whether that source is earned or unearned income. It also means that effort and expertise must be invested in maximizing profits, or at least contribution margin, throughout the system.

This type of analysis was performed for a recent BC Ferries study – *Review of BC Ferry Corporation and Alternative Uses for the Fast Ferries* (2001). The author concluded that the BC system could not realistically expect to implement its own operating plan. The report recommended a thorough re-examination of BC Ferries' management with the goal of "de-politicizing" decision making. While Alaska's Marine Highway is not faced with the Canadian dilemma of what to do with expensive new vessels that have been deemed unusable for their intended purpose, politically motivated decisions have taken their toll here as well.

Financial Planning

Identifying the composition of a fair and sustainable financial plan is the single most important step needed to secure the Alaska Marine Highway's role in the future. This is precisely because operating all runs on a break-even basis is unrealistic. Like any public infrastructure, coastal marine transportation must have a package of funding that is generally accepted at the federal, state, regional and local levels as practical, fair and reasonable. Here, again, we must address a continuum. Stability will likely result from a combination of operating and capital revenue sources that includes earned income, and federal, state, regional and local funds.

Earned Income

Based on past market studies, it is clear that the system could increase its level of earned income significantly. This, in turn would reduce public subsidy and pass more costs along to users, ideally in return for value delivered. There are at least five general sources of earned income:

- Regular/Local tariffs – Management should understand how – and have the authority – to set regular tariffs in a way that maximizes net revenue per route. If some other rationale is used to set tariffs – such as "everyone pays the same" – then some subsidy must be identified to make up the difference.
- Seasonal/Visitor tariffs and tours – As studies have pointed out, it is critical in the travel business to be able to charge according to what the product is worth to individual market segments. This means seasonal pricing, package pricing and pricing based on reservation and trip timing. The airline model of price discrimination and load management may not be desirable, but many of its fundamental characteristics are.
- Concessions and licensing – Lack of management capacity, entrepreneurial incentives, and seed money, together with restrictions imposed by labor agreements, have prevented the system from exploring concession and licensing opportunities. While not likely to be big business, these can contribute to a sustainable system.
- Freight tariffs – Freight service has long been a kind of homeless child of the AMHS. Not wanting to compete with private firms, the system has underplayed its freight services to the point where many potential customers do not take them seriously. A sustainable ferry system will need a business strategy that takes advantage of its capacity to serve the niche that lies between barge and air freight services.
- Asset management – Income from managing, leasing, trading, etc. of system assets is a relatively unexplored avenue for AMHS. Assets may be land, financial instruments, vessels, even expertise and information.

Federal Funds

In addition to funds specifically designated for ferry systems, AMHS has been eligible in the past for federal highway and safety funds and, to a lesser extent, public transit funds. Another federal funding rationale that might be applied to ferry service is the Essential Air Service program, which currently subsidizes air service for approximately 100 smaller rural communities, one quarter of which are in Alaska.

State Funds

In addition to annual appropriations, state mechanisms used to fund ferry operations elsewhere include gasoline excise taxes and highway taxes. Funding for particular functions, such as marketing for private ferry service that serves public and visitor needs, has also been provided by some states.

Regional and Local Funds

Local funding mechanisms used elsewhere to subsidize ferry service have included sales taxes, bridge and tunnel tolls, airport revenues,[10] and real estate taxes. Bed/head taxes on visitors is another potential source of local funding.

Summary of Options

Management and Governance

Key Question: What management structures and skills will be most successful at operating in a way that meets consumer needs, minimizes costs, maximizes earned income and acts as a vehicle for other funding as appropriate?

Structures	Line agency, public corporation/authority, public/private partnership
Skills	Vessel operations, sales and marketing, customer service, political skills, financial management, yield management, partnering

Operations and Service

Key Question: What combination of routes, vessels and other services will meet regional and statewide needs most efficiently?

Routes	Long-distance, shuttle, hub & spoke, road links
Vessels	Size, speed, capacity, operating cost
Schedules	Timing and incidence of service
Other services	Freight, tourism, reservations, retail sales,

[10] Tunnel tolls and airport revenues are generally part of a mix of revenue typically available to larger metropolitan authorities.

Finances

Key Question: What combination of earned and unearned income will sustain the Alaska Marine Highway System in a manner commensurate with the services it provides to its local, statewide and visitor constituencies?

Earned Income	Local fares Visitor fares and tours Concessions and licensing Freight tariffs Asset management (real estate, investments, vessels)
Federal Funding	Highway and transit funds Essential service funds Other federal programs
State Funding	Taxes for local / regional infrastructure Visitor industry support Other state programs
Regional/Local Funding	Bed tax / Head tax / Sales tax Other local programs

A Preferred Ferry Management Model

At this preliminary stage, it is not clear that any particular management structure is an obvious choice for the Alaska Marine Highway. The attributes, advantages and disadvantages of various structures are discussed in the attachment "Evaluation of Potential Management Models."

A sustainable model must combine responsiveness to community needs with responsiveness to market demands. In many cases, these may be at odds. For this reason, a desirable model must also offer access to public funding mechanisms. Four basic choices exist:

- **A line agency of government** (current system)
- **A statewide public corporation** (for example, Alaska Housing Finance Corporation)
- **A regional quasi-public corporation** (such as the Inter-Island Ferry Authority)
- **A public/private partnership** (wherein some management functions are performed by public employees and some contracted to the private sector. Note that this arrangement may be a subset of either a statewide or regional public corporation. The barriers to incorporating private contracts into line agency management are more significant.)

A purely private operating model is unlikely to be satisfactory unless service expectations by users are substantially adjusted. Many routes do not have enough ridership potential in the foreseeable future to be profitable at current service levels or in all seasons. Vehicle and freight van service, in particular, are difficult to provide to smaller communities on the basis of positive marginal revenues.

ATTACHMENTS

The ability of a management structure to move AMHS towards sustainability can be evaluated in terms of the scope of management authority, operational efficiency, external controls on management, and access to capital.

1. Does it have the authority to make the necessary decisions?
2. Does it have the incentive to operate efficiently?
3. Is it responsive to local and statewide needs?
4. Does it have access to necessary funding?

Structures that offer the greatest latitude to management to determine the services provided and the prices charged, and control costs will have the best hope of reaching sustainability. With respect to services provided, what ability will management have to determine capacity, vessel configurations, routes, and service schedules? In the near-term, flexibility in regard to service is limited by the fleet configuration. Access to capital, as well as market economics, will constrain the long-run.

Possible management structures for AMHS range from pure public sector to pure private sector, to some mix in between. Decentralization of management is another dimension to be considered. Decentralized operations could involve a mix of public and private structures. Statutory guidance and standards for the process of decentralization would be needed.

Decentralizing ferry management can be a force for sustainability. For one thing, the limited geographic scope of management limits the opportunity for cross-subsidization of routes. It also limits access to general tax and financial resources of the State or other communities that might be used for subsidies. It helps ensure that services are tailored to market demand.

Key Management Measures

Operating Authority

An *Alaska Marine Highway System Marketing and Pricing Study* documents the failure of AMHS to raise fares, even to keep up with inflation, for a period of ten years from 1991 to 2000.[11] This is a strong signal that management's current scope is unduly confined by political and bureaucratic pressures.

Labor is currently the largest cost of AMHS operations. In fiscal year 2001, it represented 65 percent of AMHS operating budget. Services provided and the fleet make-up build in a lower threshold for labor costs. But, beyond the effects of service decisions, to what extent can management control manning and staffing, work hours and rules, or compensation? A study of the British Columbia ferry system[12] identified the following as collective bargaining issues that significantly affect efficient operations:

- Inflexibility in work rules, hours, and contracting out

[11] *Alaska Marine Highway System Marketing and Pricing Study, Volume 1*, McDowell Group, , September 2000, page 34.
[12] *Review of BC Ferry Corporation and Alternative Uses for the Fast Ferries*, page 14.

- Promotions based on seniority, rather than merit
- Above-market compensation
- Overtime policy as a disincentive to on-time performance
- Ability to set crew levels and pay on new vessels

Will management have a free hand in pricing and the resources to effectively market ferry services? The *Alaska Marine Highway System Marketing and Pricing Study*[13] demonstrates how reservation and marketing resources and market pricing could go a long ways towards getting AMHS on its own two feet.

AMHS currently operates under a number of administrative procedures to provide accountability and public control and protect the public interest. These include:

- Executive Budget Act
- Administrative Procedures Act
- State Personnel Act
- State Procurement Act

These procedures should be compared to those under alternative management structures to shed light on management's relative ability to determine services and prices and control costs.

Does the management entity have the power to issue debt, at least in the case where it is supported solely by system revenues? Would it have the power of eminent domain?

Operating Efficiency

Balancing customer expectations with cost-effective operation is the fundamental challenge in any business. It is a much greater challenge when the business involves a public service such as transportation. The private sector can use a simple, easily quantified measure of efficiency: profits. However, public service is measured by an almost infinite spectrum of often vague, even mutually exclusive expectations.

To be useful, then, management measures of operating efficiency must combine financial and public service goals. Past ferry system planning documents have not directly addressed what a desirable balance in this area might be, nor even how to go about finding one.

A more complex question is "does the current system operate as efficiently as it can." To this, one must assume that the answer is "yes." Public employees cannot profit personally from inefficient operations, for example, by making "deals" that are in their own financial interest. Therefore, they must do the best they can within the constraints and incentives imposed by the system in which they work. It is these constraints and incentives that warrant further study.

The internal dynamics that cause AMHS or DOT/PF to operate the way they do also have not been formally analyzed. The issue was addressed in a limited way by the *Marketing and Pricing Study*, which noted that improving the *financial* performance of AMHS sales and reservations staff would be much easier if standard industry pay incentives could be employed. Private sector firms often take this principle farther, for example by offering cash rewards to employees who identify cost-saving measures. The

[13] *Alaska Marine Highway System Marketing and Pricing Study.*

most efficient management structure for the Marine Highway will be one that understands how, *and has the authority*, to align individual staff incentives with this goal.

Responsiveness to Local and Statewide Needs

Where statewide or local management is governed by a public corporate form, careful attention would need to be given to the make-up of the board and the approvals required, if any, from local municipalities or electorates, as under the Alaska Port Authority Act.

Responsiveness to statewide needs suggests the continued need for an overall statewide management entity. The Alaska Mental Health Trust Authority has potentially useful elements of a management structure for determining services in coordination with available statewide funding, even though it does not operate services itself. A similar ferry entity could operate services and also be responsible for devolution of services to be operated by subsidiary entities, either public or private, on a decentralized basis.

Access to Funding

Where an essential public service is provided to communities and that service is known to require a financial subsidy, does management have access to a reasonable and secure level of public funding? The management structure must be eligible to participate in a program of pubic funding mechanisms that is capable of supporting the desired level of public service.

Ferry transportation also requires large capital investments. Access to capital markets or government aid for capital improvements will be critical in the long run. If operations are not sustainable, a ferry will also need an outside source of funding for operating subsidies.

A management structure could need access to federal, state, or municipal support. Given the predominance of federal highway aid (both formula programs and Discretionary Ferry Boat funding[14]) and mass transit aid for capital improvements, legal, institutional, and political barriers, or competition for these funds need close examination.

Access to the public debt and private equity markets may also be important for capital funding. The ability to use tax-exempt borrowing would be important if there is any possibility of debt financing supported by ferry revenues. Revenue debt can require net cash flows that are 25 percent or more greater than debt service. This would be a far greater challenge than sustainability of operating costs, given that cash flows currently barely covering half of operating costs.

If a ferry operation can use tax-exempt financing, State or municipalities might provide additional credit support. This could include general obligation bonds ("GOB's"), limited-GOB's, moral obligation bonds, lease-financings, and GARVEE or other bonds supported by a particular government revenue stream.

[14] Section 1207, TEA-21.

Public Sector

Line Agencies

Ferry systems can be operated as a **line agency** of a government. This is the current structure of AMHS. It is a division of the Alaska Department of Transportation and Public Facilities ("DOT&PF"). It is governed by the appointed officials in the chain of command from the Governor, to the DOT&PF Commissioner, and on down, subject to various State laws and administrative procedures, labor agreements, and Federal regulations.

Enterprise Funds

While still a line agency, ferry systems can be structured as an **enterprise fund** within the government's accounting system. An example of this is the International Airports System within DOT&PF.

Generally accepted accounting principles[15] define the purpose of enterprise funds as:

"...to account for operations (a) that are financed and operated in a manner similar to private business enterprises—where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through users charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes."

Enterprise funds are often used to meet the disclosure and accountability necessary to issue revenue bonds. This is the case with the International Airports System.

AMHS statutes have created two funds—the Alaska Marine Highway System Fund and the Alaska Marine Highway System Vessel Replacement Fund—that provide something similar to enterprise fund accounting. But, they are accounted on the State's books as part of the general fund, a governmental fund.

One of the principal differences between enterprise and governmental funds is that only enterprise funds report long-term assets and liabilities on their balance sheets. Also, full accrual accounting is required only of enterprise funds. These differences would require an accounting of AMHS capital assets and annual charges for depreciation.

The Governmental Accounting Standards Board is phasing in requirements that will move even governmental funds closer to an enterprise model. The Board's Statement 34 will require accounting for infrastructure asset values and annual depreciation or maintenance charges.

[15] National Council on Governmental Accounting Statement No. 1, Governmental Accounting and Financial Reporting Principles.

Public Authorities

Public authorities are another type of governmental structure. They have a legal existence independent of the state or municipal government—usually, they are created by law as public corporations. They may still be administratively lodged in departments of government— for example, AHFC is part of the Alaska Department of Revenue—to facilitate oversight, budget coordination, or other administrative functions.

They also typically have a different governance structure, usually a board of directors, either appointed, ex officio, elected, or some mix. They may be created with statewide, regional, or municipal scope, for any purpose. They typically have administrative procedures similar to government, but often with greater flexibility.

Authorities may be given the power to tax or issue debt. Authority debt may receive various forms of credit support or guarantees from the parent government.

Authorities can provide a degree of independence from electoral politics. But, they also run the risk of becoming captives or advocates of users or suppliers of the services they administer. A degree of financial independence in terms of budgetary approval or retention of earnings may shift authorities closer to market-driven incentives. Endowment with financial resources can encourage an orientation to bottom-line results, but can also encourage assaults by interest groups that lead to the ruination of the commons.

Private Sector

Private sector management assumes that the State would exit the ferry business altogether, or on selected routes during selected times of the year. It denotes leaving the decision to the market as to what, if any, ferry service will be provided. Private ferry operations are common, particularly in Europe. In the US, public entities often eschew potential profits in favor of private operations. For example, when a study projected that a fast ferry operating between Gloucester, Massachusetts and Shelburne, Nova Scotia could be profitable, the City of Gloucester actively courted private sector interest in the route.

Private sector management structures would most likely take the form of **for-profit corporations**. Unlike public corporations, they can issue stock to raise capital, finance acquisitions, or reward employees. Significant capital investment would normally weed out other structures such as non-profit corporations that do not provide a return on risk capital. Business and other risks would rule out proprietorships or partnerships that do not provide limited liability. Small business structures that do provide limited liability such as limited partnerships, limited liability corporations, or subchapter S corporations can be cumbersome for obtaining outside capital or providing equity participation incentives to employees.

System Divestiture

The geographic scope of private sector ferry operations could be system-wide or confined to selected routes. The current deficit in AMHS operations suggests that **system-wide privatization** would severely truncate routes and service. If a private sector operator had to recover capital costs, it would create great uncertainty about what, if any, routes or services could sustain themselves. This would be true whether a private operator acquired existing AMHS assets or purchased new vessels or terminals.

Even if AMHS donated its existing assets to a private sector operator, the continuation of many routes and services would be in doubt. In addition, federal regulations may restrict the terms of transfer of assets funded from federal aid, or require repayment to the federal government of the proceeds of any such asset sales.[16]

No AMHS assets have been financed with tax-exempt bonds. If they had been, IRS regulations governing private-activity bonds could create problems with transferring assets to a private entity. Looking forward, private owners could face higher capital costs because of lack of access to tax-exempt financing for future capital improvements.

Service Shedding

Rather than abandoning the system to the vagaries of the private sector, AMHS could indulge in selective **service shedding**. AMHS could solicit proposals for providing service for selected routes, seasons, etc. that cover, or could reasonably be expected to cover, their costs.

Divesting any service that made money for AMHS would deepen the System's operating deficit. In theory, bids should represent the capitalized value of the routes' future earnings stream. If earnings were potentially greater under private operation, bids would more than compensate for aggravated future deficits.

Regulation of Competition

Where AMHS relinquishes service, some encouragement could be given to private ferry operations by limiting competition. AMHS could award **franchises** for particular areas as part of the bidding process. Alternatively, public utilities-style regulation could be established, requiring **certificates of convenience and necessity**.

[16] Executive Order 12803 from 1992, Executive Order 12893 from 1994, and the current federal highway aid statutes, as amended by TEA-21 would need to be examined.

Public/Private Partnerships

Where both the public and private s tors are involved in providing a good or service, the operation is frequently referred as a **"public/private partnership"**. In actuality, this seldom takes the legal form of a partnership or joint venture. More often, "public/private partnership" is a term used to garner popular support for either public financial support to private sector operations or contracting out public sector services to the private sector.

For example, Wisconsin's ferry service across Lake Michigan is essentially a private operation. However, the state has shown a willingness to provide such things as start-up support for new routes, marketing support and assistance for capital projects.

Partnerships

Partnerships, in the true sense of the word, denotes **legal partnerships, joint ventures, or corporations,** in which there are both public and private equity investment and joint governance, if not management and operation. Conflict could be expected between profit incentives and government mandates to provide ferry services. The joint operating agreement or articles of incorporation would have to spell out strictly the scope of services and equitably allocate costs, profits, and risks.

Public Financial Support

Public financial support for private or subsidiary public ferry operations can take many forms. But, the most critical element is what control or assurances of service the government obtains in return. A **laissez-faire approach** leaves determination of what services will be provided to the private sector or subsidiary entity. Financial support could include:

- subsidies or prizes, awarded for example on a passenger-mile basis
- dedicated or shared revenues, also based on some performance measure
- tax incentives or exemptions with respect to income, property, sales, or fuel taxes
- credit support or financing guarantees for assets used in Alaska ferry operations; or
- lending for ferry assets

With a **public services approach**, government would retain control over the services provided. But, ownership of assets and operation of service would lie with the private sector. Financial support would be provided in the context of a contractual relationship that sets out routes, schedules, or capacity of services provided. The types of support mentioned above could be provided, but there would be more flexibility to negotiate fixed payments or obligations, as well as performance-based ones. In addition, support could include:

- capital contributions in the form of equity or grants
- endowment of ferry operations

A study of the British Columbia ferry system[17] suggests that if a process for privatizing routes were established,

> "Even for operations where there is little present appetite in the private sector, the very conduct of the process and the accompanying pre-commercialization activities will ultimately result in further commercialization opportunities."

Private Sector Contracts

In addition to privatizing ferry operations on specific routes, "public/private partnership" could include contracting out specific functions in running a ferry operation. For example, the cabin housekeeping or ship operations of vessels might be contracted to a private firm. Restaurant or bar operations might be provided on a concession basis.

Administrative or shoreside operations that might be contracted out include:

- management/administration
- marketing
- reservations
- dock operations
- layup

AMHS already depends to a great extent on private firms for planning, design, and construction of capital improvements. But, in addition to acquisition of capital assets, AMHS might be able to lease vessels or terminals or pay usage or port fees for the use of terminals. Of course, AMHS could contract with municipalities, public authorities or agencies, or non-profits as well as the private sector.

[17] *Review of BC Ferry Corporation and Alternative Uses for the Fast Ferries*, Fred R. Wright, December 2001, page 25.

Current AMHS Model

AMHS operates nine vessels on routes that cover 3,500 miles of Alaska and British Columbia coastline between Bellingham, Washington and Dutch Harbor. It serves 32 Alaska communities plus Bellingham and Prince Rupert, British Columbia. The system has always been operated as an agency of state government. In 1997, the legislature ordered the that AMHS be reorganized and merged with the Department of Transportation and Public Facilities.

The primary management units at AMHS are general administration, financial administration, reservations, vessel operations and port operations. Recently, authorization was obtained for a single marketing position. General planning and contracting are handled by other DOT/PF units. The director of Southeast Region for DOT/PF is also active in ferry system issues and sits on the ferry committee of the national Transportation Research Board.

Decision-making is handled as with any State department. There is no special mechanism or body to provide representation for the communities served by the system. Funding is prioritized through the same Statewide Transportation Improvement Program (STIP) that determines other DOT/PF project funding. An often-discussed issue is whether the STIP is an effective way of addressing the ferry system's strategic needs. For example, the first two fast vehicle ferries are slated for service between Sitka and Juneau and in Prince William Sound. However, it is not clear from existing planning documents that these are the routes that present the greatest opportunity for revenue enhancement or system-wide service improvements as a result of the new vessels.

Since 1990, ferry system finances have been funded through the Alaska Marine Highway Fund and the Alaska Marine Highway Vessel Replacement Fund. Both are sub-funds of the state's general fund. The Alaska Marine Highway Fund receives revenue from operations and annual appropriations by the legislature. Appropriations do not lapse at year-end. However, the fund meets Alaska's constitutional prohibition against dedicated funds because it is at all times subject to legislative appropriation for any purpose. The fund provides AMHS an increase in financial autonomy over the pre-1990 arrangement whereby the system was operated directly from the general fund by annual appropriation.

The Vessel Replacement Fund was to act as a "savings account" to meet vessel-related needs. To date $19.5 million have been appropriated to the fund, all of which has been spent or committed. Since 1995, the vast majority of vessel refurbishment and replacement projects have been funded through the National Highway System Designation Act and the Transportation Equity Act for the 21st Century. This includes $31 million for the first fast vehicle ferry, authorized in 2000.

Alaska Railroad Corporation

The Alaska Railroad Corporation is a public corporation, legally independent from the State. It cannot issue stock (AS 42.40.300). Organizationally, it is a political subdivision of the State Department of Community and Economic Development.

Notably, operation of the Railroad is declared to be an essential government function (AS 42.40.010). At the same time, it is mandated to generally operate on a self-sustaining basis (AS 42.40.100 (3)). Statutory provisions exist for requesting and receiving State subsidies for particular services. But, no subsidies have ever been requested. The statutes would require subsidies to be calculated in a specific manner, as prescribed by the United States Interstate Commerce Commission, now the Surface Transportation Board. Revenue and profits, if any, are retained by the Railroad for railroad purposes (AS 42.40.530).

The Railroad has been endowed with substantial amounts of land, both along railroad rights-of-way and elsewhere. In part, this is to assure unobstructed, efficient rail operations. But, revenues from non-rail uses of land also provide financial independence from State politics. They can cover variations in operating earnings that might otherwise require the Railroad to go hat in hand to the Legislature to maintain essential services.

Historically, the Railroad's rail operations have shown a profit, sufficient to recover depreciation. In 2001, they only covered operating expense. About half of the Railroad's $306 million in assets have been funded from Federal grants and earmarked appropriations. $79 million in retained earnings have funded another quarter of the assets.

Eighty-three percent of total rail revenues of $96.2 million in 2001 came from freight; fourteen percent came from passengers. Net income of $6.6 million from real estate accounted for all of the Railroads net earnings in 2001. The Railroad actively manages its real estate. It has had a real estate department since the mid-1990's. Still, of some 18,000 leasable acres, only about 2,500 are under lease or permits.

Privatization is a possible goal for the Railroad. A number of rail services do not pay their own way and would most likely be jettisoned under private operation. AS 42.40.260 requires an annual report that analyzes the potential for sale of the corporation to private owners. Annual costs and income by category of service are included in the annual report. The Governor may also lease the Railroad under certain conditions (AS 42.40.940). The Railroad has privatized some passenger services via "pull" contracts for railcars owned by Princess and Holland America and relies on private contractors for the bulk of its capital improvements.

A seven-member board of directors governs the Railroad. The board includes two State commissioners and five public members. The majority of public members enhances the board's political independence. The public members must be appointed by the Governor and confirmed by the Legislature. Two members must have railroad expertise and one member is a Railroad employee bargaining unit member. Terms are staggered, but members serve at the pleasure of the Governor, potentially undermining continuity and independence.

The scope of the board's management authority is broad. It includes service levels and routes, rates, labor agreements, and budgets. Its budget is not subject to approval by the Governor or Legislature. With approval of the Governor, the Railroad may exercise the power of eminent domain.

There are a number of external limits on management's authority in these matters. The Railroad is deemed a common carrier subject to the jurisdiction of the Interstate Commerce Commission (AS 42.40 060 (b)(2) , now the Surface Transportation Board. Rates must conform to the requirements of the Alaska Railroad Transfer Act of 1982 (AS 42.40.250 (14)). Legislative approval is required for the Railroad to issue bonds. There are no provisions for the State to make its credit available for Railroad debt obligations.

The Railroad is generally exempt from the State's Administrative Procedures Act, State personnel and collective bargaining statutes, and the State procurement code. But, there are Railroad statutory provisions relating to adopting rules, collective bargaining, and procurement. About 80 percent of Railroad's 670 employees belong to one of five unions. The Railroad and interest on its debt are exempt from State and municipal taxes (AS 42.40.910), as well as Federal taxes.

As a corporation, the Railroad's liability is limited to its own assets or revenues. Railroad obligations create no rights against the State (AS 42.40.500). The Railroad's land is exempt from taking by adverse possession (AS 42.40.450).

Alaska Industrial Development & Export Authority

The Alaska Industrial Development & Export Authority ("AIDEA") is a public corporation, legally independent from the State. It also is a political subdivision of the Department of Community and Economic Development.

The main purpose of AIDEA is to provide financial assistance to business enterprises. AIDEA does so by purchasing loan participations, issuing loan guarantees, and owning and operating economic development projects. Economic development projects are often transportation infrastructure facilities.

These activities have been funded through State capital contributions of cash and existing State business loans; proceeds of AIDEA taxable and tax-exempt bond issues; and earnings on loans, investment securities, and development projects. Earnings on loans include loan commitment and guarantee fees charged to borrowers, as well as interest earnings.

AIDEA is essentially mandated to cover its costs. Interest rates on loans are statutorily set at AIDEA's cost of funds, including overhead. Bond-funded economic development projects must be able to meet debt service. AIDEA is authorized to charge fees for the projects it owns to provide a return on investment. This mandate, combined with a contribution of almost $300 million from the State, now produces substantial earnings—over $40 million in fiscal year 2001. This helped prompt a statutory provision that AIDEA pay an annual dividend to the State.

The oil price crash of the mid-1980's caused large loan losses for AIDEA, and limited demand for new loans into the 1990's. As a result, AIDEA's net worth grew little during this time. But in the last ten years, AIDEA's equity has grown from $643 million in 1991 to $878 million in 2001. And, this is after paying a cumulative total of $91 million in dividends to the State from 1996 to date.

A five-member board of directors governs AIDEA. The board includes three State commissioners and two public members. The Governor appoints the public members. There are no expertise or experience requirements for any members. Except for two ex-officio State commissioners, members serve two-year terms.

Even with a majority of State executive branch cabinet members on its board and short terms for public members, AIDEA has remained profitable. Business-like management has played a role. But in large part, AIDEA's profitability is due to statutory privatization of the underwriting decision.

Private lenders determine what loans will be made to business enterprises. AIDEA by statute (AS 44.88.155) may only purchase participations (up to 80 percent) in loans that are originated by private lenders. Further protections are contained in statutory underwriting criteria for these loans, such as loan-to-value ratios.

For economic development projects, AIDEA statutes limit bond financing to projects that are economically and financially feasible (AS 44.88.095 (d)). The statutes allow projects to be subsidized by the State (AS 44.88.173 (b)). But, primary reliance on bond market financing enforces profit-oriented decision-making.

The scope of the board's management authority is rather limited. Statutory and financial market underwriting criteria ensure funding only for viable enterprises and projects. Of course, there is still a lot of judgment and discretion that must be exercised by the board with respect to individual projects. Interest rates and fees on loans are limited by statute.

AIDEA's operating budget is subject to the Executive Budget Act. AIDEA is generally not subject to the State's Administrative Procedures Act or personnel statutes. Legislative approval is required for AIDEA to issue bonds in excess of $10 million for economic development projects. Until 1989, AIDEA could issue moral obligation bonds of the State. Authority to issue any bonds other than refunding or conduit bonds sunsets July 1, 2003.

AIDEA is exempt from Federal, State, and municipal taxes, though it often negotiates payments in-lieu of taxes on economic development projects. Interest on its debt is exempt from State and municipal taxes (AS 44.88.140), but some private activity bonds are subject to Federal taxation.

As a corporation, the AIDEA has limited liability and cannot obligate the State.

Inter-island Ferry Authority

The Inter-island Ferry Authority ("IFA") is a public, legally independent, corporation organized under the Municipal Port Authority Act (AS 29.35.600-730). It is a political subdivision of the municipalities that created it.

Petersburg, Wrangell, and Prince of Wales ("POW") out-port communities—those not on designated National Highway System ("NHS") ferry routes—created the IFA to improve AMHS ferry service between their communities and with Ketchikan. Parallel ordinances adopted by each participating municipality, and approved by their voters, created the IFA. A Memorandum of Understanding was executed between the AMHS and IFA to transfer responsibility for POW ferry service to IFA.

Under the Municipal Port Authority Act, each participating municipality had to approve an IFA development plan for the specific project that it would operate. Under the plan, IFA has financed the construction of two ferries and terminal improvements from the proceeds of IFA revenue bonds, guaranteed by the Ketchikan Gateway Borough and issued through the Alaska Municipal Bond Bank, earmarked Federal appropriations passed through the Federal Transit Administration, Federal and State aid to highways, and other sources.

Unlike some port, bridge or other types of authorities elsewhere in the U.S., authorities under the Alaska Municipal Port Authority Act do not have the power to levy any taxes. Nor are they entitled to receive any dedicated government revenues. Alaska port authorities are designed for self-sustaining operations.

In addition, formation of port authorities requires local initiative. This requires that there be a perceived need for improved or lower cost services. It reinforces realistic assessment of market demands, or the value of any services that might be subsidized.

A seven-member board of directors governs IFA. Each participating municipality appoints one director and the board ordinarily then appoints an at-large director from nominations made by participating municipalities. Terms are staggered.

IFA expects to cover all operating cost from the farebox and concessions. No provisions have been made for any subsidized operations. It expects a profitable operation, even though fares and employee wage and benefit levels[18] are comparable to AMHS.

IFA's ability to provide improved services on a profitable basis stems from four operating characteristics:

- dayboat operations cuts work hours from 24 to 12;
- smaller vessels[19] reduce excess capacity and crew requirements;
- eliminating cabin services reduces crew requirements and increases fuel efficiency; and,
- food and beverage operations are privatized.

IFA has substantial political and budgetary independence. As long as it does not require subsidies, approved IFA projects do not need budgetary approval by participating municipalities or other outside parties. Unlike AMHS, it is not subject to the State's Executive Budget Act and the associated statewide budgetary politics of legislative and gubernatorial approval.

IFA is not subject to the State Administrative Procedures Act or Procurement Act. It had the option to exercise the power of eminent domain within its designated boundaries, but chose to renounce it. Authorities under the Municipal Port Authority Act can issue bonds payable from authority income and receipts, or payable by another party if secured by lease or agreement.

In October, 2001, IFA opted out of the State's collective bargaining statutes[20] and IFA employees are not unionized. As a result, it is subject to the National Labor Relations Act. It can designate masters and mates as management supervisors under the Wage and Hour laws, thereby exempting them from collective bargaining. This ability of IFA (and other Title 29 authorities) to operate unencumbered by existing bargaining units is key to keeping its cost structure manageable. Shuttle operations have benefited local employment and employee morale, because crew return home each night.

As a non-profit, municipal corporation, IFA remains eligible to receive Federal highway and transit funds. It has limited liability and is tax-exempt, though it may negotiate payments in-lieu of taxes.

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[18] IFA employees participate in the State's Public Employees' Retirement System ("PERS"), have Blue Cross/Blue Shield health insurance, and are covered under Social Security, rather than the State's Supplemental Benefits System ("SBS").
[19] IFA vessels are regulated under U.S. Coast Guard Subchapter K. Subchapter K applies to vessels under 100 gross tons. Coast Guard manning requirements increase dramatically for vessels over 100 tons. Subchapter K vessels can have more than 150 passengers, subject to safety and stability requirements.
[20] Public Employment Relations Act (AS 23.40.070–260).