

HOUSE/SENATE FINANCE COMMITTEE MINUTES - 1967-1982 2815

In his closing remarks Mr. Yould recommended addition of language permitting development of oil or gas-generated energy in areas not possessing other natural resources, and deletion of the Director of Budget & Management from the Power Authority directorship because this individual also serves on the governor's budget review committee.

Senator Dankworth replaced his prior motion to move the Finance committee substitute for SB 25 from committee with individual recommendations.

Senator Sackett objected for the purpose of amendment. He moved that a new subsection (C) be added to page 4, line 17:

"(C) on fossil fuel in the event none of the above are economically feasible."

He advised that the above amendment will "take care of rural areas which do not have renewable hydroelectric energy." These areas are "going to be stuck with diesel-generated energy."

No objection to the proposed amendment having been voiced, it was adopted.

Senator Dankworth moved to amend page 1, deleting lines 20 through 26, replacing the Director of Budget and Management with the Commissioner of Community and Regional Affairs as a director of the Alaska Power Authority. No objection to the amendment having been voiced, it was adopted.

Senator Sackett moved to incorporate the two foregoing amendments within a redo of the Finance committee substitute rather than effect the changes in amendment form. No objection to the above motion having been raised, the above amendments were incorporated within the Finance committee substitute.

Senator Sackett then moved for passage of the Finance committee substitute for SB 25 with individual recommendations. No objection having been voiced, the Finance committee substitute passed from committee--all members signing do pass.

Senator Ferguson then moved that the Finance committee substitute for SB 26 pass from committee with individual recommendations. No objection having been raised, the Finance committee substitute passed from committee--all members signing do pass.

ADJOURNMENT

The meeting adjourned at approximately 10:00 a.m.

SFC-81 #10, Side 2, (604-end)
SFC-81 #11, Side 1, (000-672)

SENATE FINANCE COMMITTEE

March 6, 1981

9:05 a.m.

(Tape SFC 81, # 11, Side 1, 672-815)

CALL TO ORDER

Co-chairman Bennett called the meeting to order at 9:05 a.m.

PRESENT

All members of the committee were present with the exception of Senators Sackett and Stimson. Also in attendance were Administrative Assistant to Senator Bennett, Judy Johnston; Administrative Assistant to Senator Dankworth, Kathy Martinson; and Senator Parr.

BILL ASSIGNMENT

Co-chairman Bennett made the following bill assignment:

SB 244 - Dankworth

SENATE BILL NO. 150

Co-chairman Bennett stated that the committee would consider Senate Bill No. 150 (An Act making a special appropriation to the Department of Transportation and Public Facilities for improvements to the Steese Highway; and providing for an effective date).

Co-chairman Bennett stated that most of these improvements would be in Senator Sackett's area. He said that the highway had originally been built years ago with virtually no standards; consequently, there had been many unnecessary accidents. He said that the \$1,800,000 appropriation would enable DOTPF to realign the culvert and bring the highway up to standard. He added that this funding had been intended to go in last year's budget. He asked for comments and/or questions from the members.

Senator Sturgulewski asked if this wasn't in the Governor's original request. Co-chairman Bennett stated that it was. Senator Sturgulewski commented that therefore, this would continue to be a priority. Senator Eliason pointed out that this type of thing should be a priority anywhere in the state.

Senator Sturgulewski moved and asked unanimous consent that Senate Bill No. 150 be passed from committee with individual recommendations. There being no objection, it was so ordered. All present members signed the committee report "do pass".

SENATE BILL NO. 133

Co-chairman Bennett stated that the next order of business would be consideration of Senate Bill No. 133 (An Act relating to memorials to Alaskan veterans; and providing for an effective date). He requested that one of the sponsors to the bill, Senator Parr, come forward to testify on the legislation.

Senator Parr stated that though other states (he gave the example of Hawaii) have monuments to their war veterans, Alaska does not. He stated this to be the reason for the bill. He said that the Denali State Park was chosen for its statewide significance, and that it would be placed adjacent to the Parks Highway so that people could see it. He stated that the original bill had been modified in the State Affairs Committee to include veteran's of all the different areas of service, and that he did not object to the changes.

SENATE BILL NO. 134

Senator Parr stated that this bill would provide the funding for the above memorial. Co-chairman Dankworth requested an explanation of the fiscal note for CSSB 34. Senator Parr said that he felt the FY 82 \$30,000 planning and design figure was rather high, but added that he did not think that the Department of Military Affairs would actually use that much.

Senator Sturgulewski commented that she would like more people to realize that the Denali Highway is a "Blue Star" highway.

SB NO. 133 AND SB NO. 134 - BILL PASSAGE

Senator Eliason moved and asked unanimous consent that Committee Substitute for Senate Bill No. 133 (SA), and Committee Substitute for Senate Bill No. 134 (SA) be passed from committee with individual recommendations. There being no objection, it was so ordered. The committee report was signed as follows: Co-chairmen Bennett and Dankworth and Senators Eliason and Sturgulewski signed "do pass", and Senator Ferguson signed "no recommendation".

ADJOURNMENT

The meeting adjourned at 9:15 a.m.

(Tape SFC 81, # 11, Side 1, 672 - 815)

SENATE FINANCE COMMITTEE

March 10, 1981

8:45 a.m.

(Tape SFC 81, # 11, Side 2, 000 - end)
(Tape SFC 81, # 12, Side 1, 000 - 516)

CALL TO ORDER

Co-chairman Bennett called the meeting to order at 8:45 a.m.

PRESENT

All members were present with the exception of Senator Ferguson. Also in attendance were Dr. Milton Lipton and Mr. Dick Kilgore of W.J. Levy Consultants; Administrative Assistants to Co-chairman Bennett, Judy Johnston and Judy Noe; Administrative Assistant to Co-chairman Dankworth Kathy Martinson; Legislative Fiscal Analyst Milt Barker; and members of the press Joe LaRocca, Rosemary Alexander and John Matthews.

BILL ASSIGNMENTS

Co-chairman Bennett made the following bill assignments:

SB 6 - Bennett
SB 168 - Sturgulewski

DR. MILTON LIPTON

Co-chairman Bennett stated that the next order of business would be testimony from Dr. Milton Lipton of W.J. Levy Consultants, and tax issue advisor to the State of Alaska. Present with Dr. Lipton was Mr. Dick Kilgore, also of W.J. Levy Consultants. Co-chairman Bennett then requested that Dr. Lipton come forward to speak to the committee.

Dr. Lipton stated that he would use the time to touch upon the tax issues that have been brought to the fore by the court suit against the State's corporate income tax, and that he would like to use as much time as possible for discussion with the committee and discuss only briefly what he felt were the implications of the State's position at the present time. He said that he felt there were the following four things worth considering in this light:

1. Legal Challenge to Separate Accounting Under the Corporate Income Tax Statute (windfall tax aside) - This is the legal challenge to the principal of corporate income tax accounting resulting from the latest amendments to the corporate income tax law, which provides for separate accounting of taxable

income for oil companies that produce and transport oil and natural gas in the state.

2. Policy Questions Raised for the State and the Legislature - Under the Alaska Statutes, taxable income is assessed and the corporate income tax rate is applied to the portion of the gross revenues received by producing companies. These companies in turn pay a windfall profits tax to the federal government on the same gross revenues. This is separate and apart from the principal of separate accounting.
3. Fiscal Implications - This point is applied to the continuing of the present system, or to making certain amendments.
4. The Overhang of Uncertainty - Dr. Lipton felt that this was the most important aspect of the present situation, which threatens the interests of both the State and the industry.

Dr. Lipton stated that he would elaborate briefly on each of the above four points, emphasizing the fourth point, as he did not feel that it had been adequately covered to date.

THE FOLLOWING IS A VERBATIM TRANSCRIPT OF DR. LIPTON'S TESTIMONY TO THE SENATE FINANCE COMMITTEE

1. Separate Accounting - Under the Alaska income tax law, this is the basis of taxable income and income tax liability for companies engaged in production and/or transportation in the oil industry. This is an "either/or" principal for the State. There is no question (and this goes back to the earliest sessions of the Legislature that considered it), that under the previous corporate income tax law, there was an inappropriate allocation of taxable income to the State of Alaska under the apportionment formula that then existed. There was no question about that. As a result of going to separate accounting, you have very significantly increased the taxable income subject to your corporate state income tax law. Now, for the State, this is "either/or". If you revert from separate accounting, and go back to the old forms, in effect you probably miss about 3/4 of the income which is thrown up by oil producing operations in the United States. Obviously, there is a lot of money involved. And there is no escaping this. There are legal issues that are raised which will be adjudicated by the courts, and I wouldn't presume to say how that is going to come out. But the fact that there is a lot of money involved and legal issues posed, is not going to be escaped by trying other devices. That is to say, if you can see, or if you back away from separate accounting, there are alternatives. One is to go to an apportionment formula, and in the hope of recovering the taxable income and the taxes that you would lose, you may try to alter the factors in the apportionment formula. But if you do that, you do not avoid the legal uncertainties. Because by whatever device you may be able to improve the

allocation of income to the State for tax purposes, if you turn to various devices, you back away from the standard formula. And as you back away, in one sense or another, you raise the same questions that the industry has provoked to take to court the questions of double taxation, separate identification of the industry (treating them differently from other industries, etc.). So I put it to you without judging the legal issues, that for the state, the ability to identify, to isolate and to tax the incomes generated in this state through the production of oil and gas depends on some form of taxation, whether its separate accounting or some deviation from it. And so long as that much money is involved, there can be legal issues raised. I don't think we can avoid legal issues. I can't say whether the State will win or lose at this point, but I put it to you that if you search for alternatives, the alternatives that you find will also be subject to diverse legal interpretation - for exactly the same reasons as separate accounting. If you feel it is appropriate to identify and tax producers income, the device you have chosen, which is separate accounting, is appropriate to the purpose. Whether or not it will stand up in court, I don't know. So it is an either/or situation. Nor is it true that only the multi-state companies who are producing in Alaska are the only ones subject to separate taxation. I put it to you that any all-Alaskan company that operates only in the state of Alaska, whether its oil operations or other industries, accounts to the Department of Revenue on the basis of separate accounting for its income. Now let me pass away. This has to do with the separate accounting issue per se and the implications for the State. The revenue implications are tremendous, and there is no way of avoiding it. Because virtually all of the work we have done, and I think its paralleled by all the work the companies have done, and that is why so much money is involved, indicates that under the apportionment system, as you have it in your previous income tax, only about 25% roughly of the income generated by...was in fact identified and apportioned to the State of Alaska. Now there is an entirely different problem raised by the windfall profit tax.

2. Windfall Profits Tax - This has been added to the legal attack on the corporate income tax law. But regardless of whether it is a legal issue, it certainly is a policy issue for the State. And I think the State and the Legislature has to address itself to that subject. There is no way which you can avoid the policy implications of what is happening. Your state corporate income tax as it now stands never really envisioned that the State would be taxing as profit generated in the State of Alaska, a portion of the gross revenues of the producing companies which they are unable to keep. That was certainly not the intention, nor was it written into the state law. It transpired by a sequence of events, which by the same time, favorably effected the State's taxable income and the State's tax revenues. That was the decision of the Administration, as of January 1, 1980, progressively to

remove price controls from domestic crude oil. When that was done, this immediately increased the profitability of all producing operations in the U.S., and as a result, under your separate accounting bill, also increased taxable income within the State of Alaska. Within 2 months, Congress passed a windfall profits tax which said that not all of these higher prices shall be retained by the producing industry. A portion of it, for producers in the category of those say, in Prudhoe Bay, would have to pay 70% of the increased prices, above the tax-free level, to the federal government. In the conference committee of the Congress of the U.S., it was stated that the windfall profits tax was an excise, or severance tax on domestic oil producers and royalty owners. And they further concluded...the committee believed that this would reduce profits of oil producers and royalty owners. So in a sense, you are taxing, without intention but inadvertently, as a result of congressional decisions, you are taxing as income, income which producers here in Alaska are not able to retain. Whether you do anything or not about it is your own decision. I put it to you that if the Legislature does not act on this decision, it becomes a positive decision of the Legislature. It will everywhere be interpreted as a positive decision however inadvertent it may have been when your income tax law was amended. This issue having been raised and no action being taken, this then becomes interpreted as a positive decision that the State of Alaska in effect will assess corporate income taxation against the windfall tax revenues which are received by the federal government. And I think this is a policy decision you must consider before you make your final judgement. Again, legalities aside, it is a positive decision because it has implications both within Alaska, for the industry and in Washington D.C. as to how the State goes about taxing. It is not a matter of revenue. This did not become an issue until the windfall profits tax was passed as effective March 1, 1980. It effects your revenues only for a portion of the calendar year of 1980, which accrue at the present time, and for 1981, and would effect your revenues in the future through probably October 1990, when the windfall profits tax is scheduled to expire. Whether it expires or not remains for future congresses to decide. But the implications then are there because the federal government in many respects, has taken special cognizance of the circumstances of Alaska - the entitlements treatment of Prudhoe Bay oil, at a time when Prudhoe Bay wellhead prices had been very depressed and the fact that Congress in its finite wisdom, decided that the excess profits tax shall not be applied to future production north of the Arctic Circle. So, dollars and cents apart, however, you may regard the fiscal implications of the tax on wellheads profits tax - the tax upon the tax. And you may decide the revenue is essential or not, but there is a special issue involved in the form this taxation takes.

3. Fiscal Implications - You have of course, as a result of your whole tax regime and as a result of the way in which it is

applied by the Department of Revenue, certain revenue expectations. And you also have certain revenue projections, predicated upon the whole set of forecasts which are made about levels of productions, future prices, future tax revenues, royalties, etc. Both your revenue expectations and your revenue projections are obviously critical to the way in which the Legislature handles the affairs and the way in which the administration handles its budgeting. But, I would put it to you that there is nothing sacrosanct about a series of budgeting projections. Series of budgeting projections by themselves are little more than an arithmetic computation based upon somebody's assumptions. If you made revenue projections for calendar year 1980, you made them in 1979, what would your revenue projections have shown? Would you have anticipated the level to which world crude oil prices have increased? Never. Would you have anticipated that by an act of the then President, that de-control was going to be phased in over the course of time supposedly to end as of October 1? Neither would you have anticipated at that time that there was going to be a wellhead windfall profits tax. So all your revenue projections are predicated at the time when you make it, and then the changes that take place in the interim. So the fact that you now have a series of revenue projections, for example, what will accrue to the State, what will accrue to the federal government, to the private oil companies by time Prudhoe Bay has been exhausted. There is nothing magic about these revenue projections. And I put it to you, that with or without the tax on the windfall profits issue, I suspect that all your revenue projections in the long run are going to be on the low side - and hardly indicative of what the total profitability in the State's share in the profits will be. So again, I think that your criterion, is dependent upon the State's perspective on its revenue needs, and its capability of raising revenues, and how you want to spend your money. All these fall within the purview of the Legislature and are inappropriate to any decision you make on taxation. But I don't think that it is essential even for your own purposes, that "willy nilly", not one dollar of future projected revenues shall ever be foregone.

4. Issue of Uncertainty - The uncertainty that faces you as a result of the case before the courts is a costly over-hang for the State of Alaska. You face an extremely large future liability if it turns out that the law is declared unconstitutional. This liability accumulates year by year - windfall tax aside. The simple difference between the way in which you assess and collect a corporate income tax now, and what you would go back to if your amended law is declared unconstitutional, accumulates a tremendous potential liability. It could cause the State of Alaska an incredible economic "wrench" if somehow your expectations are frustrated by an adverse court decision. And I suspect that if this uncertainty hangs over the heads of the State of Alaska for five or more years where the decision goes through a series

of court findings, that it will probably effect the Legislature in its approach to virtually every revenue and spending bill that comes up over the intervening years because in the back of your minds you will be thinking, "my god, what are we thinking?". But I put it to you that the overhang of uncertainty that confronts the industry is as serious as that for the state. Its easy to think well what does the industry have to lose? They can only gain. If they lose the court case, they have paid the money in already. What do they have to lose? I think they have a tremendous amount to lose, particularly if they win the case. If they win the court case - from now until five years while the industry is awaiting the same decision you are waiting for, they are confronting uncertainty. But the worst uncertainty for the industry would come if they win the case. Let five judges, good and true, decide through their interpretation of the law, that the income tax statute is invalid. What then? Do the five judges say to the State, "within 30 days you have to pay \$7-8 Billion back to the industry."? How does the State do that? Or, do the judges say to the industry and to the state, "come and tell us what kind of relief". So then you enter into the whole problem as a matter of equity and as a matter of practical consequence - how is the legal decision of the state to be enforced and to be effected? Is the State, having been imprudent in the intervening five years, going to be confronted with bankruptcy because of the need to pay this kind of money? How can the State with 1.5 million barrels out of Prudhoe Bay, and with the aggregate after tax profits at that time with the changing the law, running \$10, \$11, \$12 dollars a barrel - how can a state like that face bankruptcy? Or does the industry say, "Hey, we give it to you, this is a real problem. We will now be gentlemen. We were buggers when we took this to court, but we will now be gentlemen. You can pay us back, not in dollars, but as a credit to our future tax liability over 12 years." And then do they sit content that the Legislature will do nothing for all these years, while they accumulate credits against future taxation, or will this Legislature or some subsequent legislature say, "We will see that your tax liability is high enough so that we don't have to pay you back anything over the next 10 or 12 years." Now, what a horrible situation for an industry to operate under. If today they argue to you that the levels of taxation are creating an uncertainty which threatens incentives to investments in the State, which I do not believe is the case - but if they argue that - what are the odds that you can continue with exploration and development in Alaska with the uncertainty of the court decision overhanging. And then even if its favorable to the industry, not knowing under what kind of a tax regime, what kind of a settlement the industry has to operate for the next 5-6 years after. I think the risks and the uncertainties confronting the industry are just about as high as those confronting Alaska, which suggests that for heavens sakes, both sides really ought to get rid of these uncertainties.

And then finally, what directions for a solution? I suggest that there are three things I suggest that there are three things that are pivotal in the picture.

1. I think that there are amendments called for in your income tax law. It was debated I think carefully by the Legislature for many years, and the industry's expressions of opinion was listened to. The industry was loud, I'm not sure they were that clear. But certainly their opinions were expressed over many years. But the final income tax amendment was passed in the final days of the legislative session at a time when the legislature and the administration were compromising in the legislature all kinds of compromises were being worked out from different perspectives of legislators. So obviously, there are things in this law that could stand amending. We could discuss those if you want, but I think the first part of the compromise is to get rid of some of the encumbrances which are most an anathema to the industry. And that has nothing to do with the dollars and cents computation.
2. Lets look at the fiscal aspects of it. Particularly with respect to the windfall profits tax. There are costly implications for the industry and there are windfall profits to the State, which it had no reason particularly to anticipate or to build into its revenue projections. But the fiscal implications breakdown - there are the fiscal implications for the year past. That is, 1980 has gone by. And the tax liability has accrued. And this is money the State had every reason to expect under the law as it stood. There are fiscal implications for everything you are wrestling with for the year ahead. And then there are fiscal implications for if you do have or don't have the windfall profits tax covered for 10 - 12...for the years in the future until the law expires. And it seems to me that there ought to be room for compromise on which of these shall not necessarily require payment, which can be voided for the future. So in a sense, the policy implications of continuing to tax the federal windfall profits tax receipts can be avoided, but the compromise is struck on what the fiscal implications are and certainly through your severance tax amendment, if you want to go that route without establishing onerous and impossible levels of taxation, one can go ahead and strike a reasonable balance on the fiscal effects.
3. The third, of course, is to get rid of the overhang, by agreement that the cases will be removed from the courts. I think in a sense Alaska and the industry was fairly close to that two years ago when it was just a legality of separate accounting that was in dispute. Now you have the added question of windfall profits tax. But if there can be agreement on the essentialities of the law through amendment, and if there can be a compromise on fiscal implications I would think that both sides would be happy to have the overhang of uncertainty removed. I'm at your disposal.

STURGOLEWSKI: You told us that we went from one method to another. If we went to some form of apportionment, that we would stand the same risks of legal issues being raised. So that didn't seem to offer too much comfort. You haven't really talked about the basis of the charges under the present case - the interstate commerce, the due process, the equal protection issues. As an advisor to the Legislature, would you suggest that we do certain things to determine the strength of our case prior to somehow following your suggestion of getting rid of the overhang? How do we get rid of the overhang if we can't go this way because we have other problems, and we are going to settle it more as you say, on the fiscal basis rather than on the issues. I have a real problem. How do we handle this?

LIPTON: Senator, let me say. Obviously, the State will want the best possible legal advice as long as the case is pending. Obviously. I think the best possible legal advice has to do with how you protect your interests in the courts. I don't think anyone is competent to give you legal advice that "yes, you are going to win the case, or no, you are going to lose the case." Therefore, given the fiscal, and particularly the overhang of uncertainties, it seems to me that nobody gains by pursuing the case through the courts. The one way in which you can avoid the whole issue is by passing a new amendment to the income tax law and going back to the old law. The companies were very very happy with the old law. They were happy with the old law not because it was a better law, or an equitable law, not because it gave you fair taxation. It was a good law because it taxed them less. That made it a good law. As a matter of fact, I put it to you, that all these issues of equity you select the industry for special taxation here in Alaska which you do to nobody else. These questions of equity and fairness - there was nothing so unfair as your previous income tax law. And to understand that, you have only to look at the submissions that the industry has made. The industry made submissions to prove that they were paying so much money to the State of Alaska. But virtually every example which they gave proved that the producers at Prudhoe Bay were each paying taxes under the apportionment formula which was different from their share of the profitability in Prudhoe Bay. Now what is less equitable than that? As a matter of fact, Standard of Ohio would pay a disproportionately high tax compared to ARCO or compared to EXXON. That is terribly unfair, but the industry wouldn't make an issue of it, because they are all paying lower taxes than otherwise. So fair is fair, and unfair is unfair, but it depends really upon dollars and cents. Now, I put it to you that the interest of the state in an appropriate level of corporate tax income requires something else rather than the standard formula. That is what I am saying. But I don't think any alternative which throws up three to four times more, has essentially got....The minute you start deviating from what the industry has been accustomed to, then you raise the question of legality. And I put it to you also, that its not just a matter that every time you have separate accounting by a state, that per se is unconstitutional or illegal or violates all the strictures of the state's rights. Because the industry itself

has desperately tried to get separate accounting in states where it would lower their taxes. But, I can't predict the outcome of the legal question. But I think the State has to face up to it that if the State purports to get the levels of income from the industry, and I don't think that all the industries arguments notwithstanding, that they pay too much taxes, that they pay a disproportionate share of the taxes, that there are disincentives. You put it all together and I think this is a matter of how the industry sees it, this is a matter of the citizens of the State of Alaska and how they want to tax enterprise within the State. I make no grief for higher or lower taxation, but if this is your purpose, then you are going to have to live with a corporate income tax structured somewhat like it is at the present time. And to resolve the uncertainties you have to resolve them on a pragmatic basis before the legal uncertainties do violence to the interests of both the state and the industry.

DANKWORTH: How many ways do we have besides an income tax and a severance tax, to adjust - if its the political or whatever type of decision you call it that we feel that our percentage figure - take Prudhoe Bay we will say is 30% - if that is the figure - if we can find the tools to get to that. With the present things in place. The only two we have discussed are the income tax and the severance tax. I don't know of any other two besides that. How many states have this separate accounting?

LIPTON: I believe it is Alaska only that has separate accounting for oil producing and transportation operations. But there is a reason for that. There is nothing magic about one of the reasons that we in a sense not really recommended but pointed up the implications of separate accounting in the State of Alaska. It has to do with the circumstances of the State of Alaska. The State of California is very happy with an apportionment formula (it is a modified apportionment formula), because you have a tremendous concentration of headquarter property, of refining marketing, petrochemical service stations - all of which are heavy in property in California, all of which involve large payrolls in California, all of which involve large sales in California. So that the apportionment formula throws up for California a relatively attractive level of taxable income. The circumstances of Alaska are very different. So I think there is a reason - and incidently, every state does look, whether its on apportionment or not, even under apportionment, for that particular variation of the formula which best serves its interests. But I want to get to the other part of your question - what are the other alternatives? I think there are other alternatives. One of the alternatives you also use, but which we think involves unduly heavy taxation so long as your corporate income tax and severance tax are inviolate, is your advalorem property tax. You have exempted certain aspects of the industry's property from the advalorem property tax and you include others. Now if you want to supplement your incomes and your yielding on the income tax, then you can go to the advalorem property tax in ways you are avoiding at the present time. At

one time you went to the reserve tax. And incidently, the reserve tax involved a degree of separate accounting which was fantastically more involved and more complicated and more forward looking than any income tax, because if you talk about the value of reserves in the ground you have a forecast over how many years they are going to be produced, what prices are going to be in the year 2000, net it down to present value and put a tax on it. Reserve tax is a possibility. We had discussed in this Legislature, when the issue, the failure of the old income tax law to do its job - you discussed many alternatives, you discussed the franchise tax, you discussed the net proceeds tax, all kinds of alternatives. But the minute you start going to round-about ways, you may have the legal questions, but more importantly, and this is why I think your question is such a good one, you can have many different taxes that develop revenue for the State, but they all have different implications for incentives, for the industry and for the future. Because today, you reckon the effect of alternative taxes by what it will bring in - essentially from the Prudhoe Bay operation. Because this is what you are looking at. So you say, if we go a advalorem tax we may get the same thing or if we go to the severance tax we may get the same thing for a year or so. But they all have different implications for the future. Because its not just Prudhoe Bay you are looking at. And as a matter of fact, I think you tailored your severance tax very carefully to give help to some producers in Cook Inlet at the same time as you were raising the level of taxation on the more prolific Prudhoe Bay. But all of these taxes have different effects on the incentive to explore for and develop the potential resources of Alaska. And I put it to you that the corporate income tax, insofar as it accurately identifies the level of producing profits in the State of Alaska is one which yes, hits particularly hard the prolific and very good oil fields. But it is so sensitive a tax that it provides incentives for people to look for and even develop marginal oil field because then their low level of profitability is not intensively hit by the State of Alaska income tax. And I can visualize under the old apportionment formula that a company would pay a damn sight more tax on its income here if it happened to have big profits outside of the State of Alaska and operated a marginal oil field here in Alaska. So there are alternatives. But when you judge the alternatives, please do not judge them just by whether or not Prudhoe Bay pays the same amount of money, but judge them by what their effects may be on all the incentives for exploration and development.

DANKWORTH: Under the severance tax - I believe its a 15% on the severance tax is all that can be deducted against the federal tax. What happens, if we were to raise the severance tax, and lets pick a hypothetical figure, say 16 or 17% (where its now 12.5%), what would get involved when we step above that 15% mark?

LIPTON: Very simply - at the present time, the tax free component of a Prudhoe Bay producer's revenue from the production and export of crude from Alaska - under the windfall profits tax - is roughly about \$14.5 dollars. The first \$14.5 dollars of

that he doesn't pay any windfall profits tax on. Now that \$14.5 dollars goes up quarter by quarter by inflation. But the law also says that any increase in the severance tax liability up to the level of 15% will be added on to this tax free component, so if you go from 12.25% to 15%, you are adding about 2.75% gross to your severance tax - well they wouldn't pay any windfall profits tax on that additional severance tax. In other words, the federal government has done for your severance tax what you have not done for their windfall profits tax. Now if you go to 16% or 17%, that additional severance tax which they pay to you will be counted by the federal government as gross wellhead receipt and will be taxed at the rate of 70%.

KILGORE: One other point, it would be some offset of course because the additional windfall profits tax would be deductible from federal tax purposes.

LIPTON: Sure, and the additional severance tax would be deductible both from your own corporate income tax and from the federal income tax. But in answer to your question, up until the point of the 15% severance tax, the company is protected against paying any windfall tax liability on that additional tax payment to the state of Alaska.

DANKWORTH: What is the highest severance tax?

LIPTON: 12.5% at the present time.

DANKWORTH: Of course we know the Montana coal case - now I think 30% severance tax on coal in Montana. How that case relates to Alaska oil when we are talking about 16.5%, 17%. How significant do you think a decision would be in the Montana case as it relates to Alaska's case? We have a tendency sometimes...I hear in conversations that that case is going to impact greatly the increase of severance tax in Alaska. Do you view that as a...?

LIPTON: Well, there are two different legal aspects to the severance tax. One has to do with your own state courts and your own constitution. At what point does your own taxation become confiscatory? Fix this, I think, as an important criteria in your mind - that your production tax that we refer to as a severance tax, is a percentage of gross wellhead value, and if you have two oil fields for each of which the gross wellhead value is say \$25 dollars a barrel, you tax them both at the same severance tax rate. But one, on \$25 dollars a barrel may be making \$10 dollars a barrel profit, and the other may be making \$2 dollars a barrel profit because its a very high tax. So, as you raise severance taxes it becomes doubly onerous to people who are engaged in marginal productions. So, somewhere along the line, one has to worry about the tax becoming confiscatory. But if you look at the alternatives, you see, there is no real reason why a severance tax has to be based on gross wellhead value. You could put a severance tax on net wellhead value. Now, if you actually compute all the costs to be deducted from gross to reach net, you are coming close to an income tax. But you don't have

to do that. You can allow companies to take notional deductions. Whether or not their costs are that high, they can take notional deductions, and you end up with what is, in a sense an imputed net wellhead value, not a marginal profit, an imputed net wellhead value, and then you can go to different tax rates, and one of the advantages of that is, that you can make it more sensitive. That is to say you can have a relatively high severance tax rate on the gross...which effects the more prolific...you have so many different things that can be done. I don't think the State is at loss for recourse if in fact it is the judgement...again, I put aside revenue considerations. Its in your mind and you have to make those decisions. The level of the taxation that you believe is appropriate to the industry. And there are ways of going beyond the pail - very obviously - but I think you must be concerned also, not only do we have the instruments available to use to reach our revenue objectives, but also what are the other consequences of alternative taxation?

DANKWORTH: If we wanted an objective of 30% of return of Prudhoe Bay in revenue, what is the advantage, if we have these alternatives. Why is it not practical for them - if you say its bad for the oil companies and the State to be in court for five years - why is it not practical for us to go ahead and address these alternatives now and try to solve these problems as soon as possible if its politically our decision to reach this 30%, or is that what you are saying that we probably should do?

LIPTON: Well, really, what I am saying in specific answer to your question is that I think there is a very great danger for the state in writing tax laws for Prudhoe Bay. I know its the biggest operation in the state, and I know its the source for now and for some time to come for the biggest revenue for the State, but I don't think its appropriate - I shouldn't say that - I think there is a danger to the state in writing tax laws for Prudhoe Bay because you have other operations in the state which are ongoing. In Cook Inlet for instance, which is very very different - some are profitable and some not so profitable. And I put to you, if you are talking about 9 billion barrels of recoverable left in Prudhoe or whatever the figure may be - and you are looking for 12 to 15 years production out of Prudhoe Bay - that within that period of time, the odds are that Alaska could discover billions of barrels of additional reserves with different cost conditions, different degrees of profitability - some close in with not such difficult transportation problems, whatever the case may be. But if you write a tax law specifically for Prudhoe Bay you have to worry about what this may do for all of the incentives for all the exploration and development elsewhere. And a lot of implications for other types of industry in the State. So that how much money you get out of Prudhoe Bay is not a matter of defending the industry's interests, or denegrating for the State's ability to raise taxation for an ongoing and profitable operation. But its highly preferable to do it through a tax regime, which is consistent with so many other purposes within the State. And there are so many taxes which are productive and creative and forward looking,

and there are taxes which tend to be backward looking. And we've got Prudhoe Bay, and here we go, and all we are concerned about is how much revenue we get out of it. So the answer to your question basically is not so much, can't we do it in easier ways, but rather do you want to do it in ways which are not attractive to the State and the industry in terms of what the next 10 - 20 years may bring to Alaska?

STURGULEWSKI: It would be very helpful and perhaps this is not the appropriate place, if you could see that the members could get a little more detail on the amendments to the law that you spoke about. It seems to me that what you are telling us, apart from protecting the current law as we can, that we ought to get into a situation of negotiation to get the matter settled out of court. Is that correct?

BEGIN NEW TAPE, SFC 81, # 12, Side 1, 000 - 516)

LIPTON: Well, sure. Obviously, we didn't come up here with a brainstorm that negotiation and resolution is better than dragging this thing through the courts. Obviously, this is...negotiations and conversations are going on. The only thing we can do is to try to set this thing in a broader perspective. In particular I think the appreciation on the part of the State that the industry is as much hung on the horns of a dilemma by pursuing this case as the State is. Which means that the bargaining position on the part of the State isn't all that bad. But I think that certain types of amendments to your income tax law are called for in any case. Now, are there criteria? I would say, yes, there are criteria that you yourself can judge - by your own statute. There was a basic purpose when the battle of the income tax law was fought out. And everybody focused on that basic purpose. Now, a lot of other baggage got thrown into the law. And if you jettison some of that baggage I think you've got a better law and a stronger one. Quite apart from the legal...the legal contest on the case - if the industry wins a court decision on any one aspect of this law, which by your own statute is separable from the rest - if they say...trying to get the facilities and the payrolls associated with the offshore operations out of the apportionment formula - that is illegal, throw that out the side. You are still left with what is essential - that is separate accounting. The industry really achieves its objective, which is lower tax liability, only if they overthrow separate accounting. The rest of this baggage is not essential to your purpose. It confuses your statute. And I think the State is better off without it, if it cleans up the law. I think this is a tremendous interest to the industry also. And whether separate accounting is negotiable, I leave up to you to judge. That has been discussed with the industry for several years. And I think up until the new issue of the windfall profits tax, it looked to be a negotiable item.

STIMSON: On the fiscal implications, I am not clear, if we use a general guide of roughly 30% as the overall income we receive from the industry - are you saying that as we analyze this

through that we shouldn't be hung up on this 30%? When you speak of revenue projections and tell us that shouldn't be a primary factor in our considerations, I find it difficult to step back away from that. Can you help me put that in perspective a little better?

LIPTON: I'll speak my piece, whether it puts it in better perspective or not, I'll leave to you to judge. I don't think there is anything magic about the 30%. As a matter of fact, I would say to get hung up on a matter like that does a disservice to you. In other words, you can't spend 30%. You can only spend dollars. 30% of what? And what is the criterion of 30%? The comparable figure to 30% I guess would be about 20% left to the producers after all is said and done. I don't know exactly. Now, 30% for Alaska, 20% for the industry. Is that a reasonable criterion to use? Again, is it just Prudhoe Bay you are talking about? If 20% of the residual profits is reasonable for Prudhoe Bay that is because that 20% represents so many dollars of income relative to so much capital investment. And therefore, for these companies, not only in retrospect to Prudhoe Bay but looking forward, that that kind of an expectation is enough to keep exploration going. But there is nothing magic about the 30% per se. For example, would you have said when the net back on Prudhoe Bay oil looked to be \$2.65 a barrel at the wellhead, that the State could take 30% and leave 19 or 20% for the industry? I think how much you can get, or how much you can expect to get depends also not only on the profitability of an enterprise that has been brought to completion but what expected profitability for an ongoing exploration. I think to get hung up on 30% as though its a magic number - there may be cases where the State ought to get more than 30% and other cases where the State will have to yield a lot less than 30%. It depends on overall profitability. And if you use Prudhoe always as the touchstone as to what is good, bad, right, wrong, appropriate, inappropriate, and then write your tax legislation to insure that, I think you are being backward looking instead of forward looking. Now, there is nothing wrong with 30% under certain circumstances, but to use it as though it has a magic rationale all its own I think is dangerous.

ELIASON: I suspect if we did find the magic formula that did produce this 30% figure we are talking about, that since we are dealing with such vast amounts of money that we would be subject to litigation no matter what course we chose. So obviously our responsibility is to chose the safest course as it pertains to the revenues to the State and to the people of the State of Alaska. However, unfortunately, the emphasis is on the 30%. Could you give us an overview of the profits of the oil companies? Lets look at it from their aspects. What kinds of profits are they enjoying this particular period in time?

LIPTON: Your own revenue department must have made some pretty careful calculations. I would hate to give you an off the cuff answer. But I would say that the producers at Prudhoe Bay must be netting after all taxes at the present time upwards of \$6 per

barrel. And I don't know how meaningful that is even. All I know is its a lot less than they expected to make. Three years ago...its a lot more than they expected to make three years ago. But on the other hand, the State of Alaska is getting a lot more out of Prudhoe Bay than they expected to get three or four years ago. But you know, the incredible change which is taking place in recent years has to do with an unexpected and dramatic increase in world oil prices. Which, to a very considerable extent, carries down here - though not entirely. And this has increased tremendously the profitability of the Prudhoe Bay operations and has increased tremendously the federal government's revenues from all forms of taxation to Prudhoe Bay and also yours. Now what it does to the 30% and so on, or whether \$6 is good, bad or indifferent - this is why in a way, your income tax law, which is plagued by uncertainties, is we think, one of the most appropriate elements of a tax policy here because it will give the state higher revenues when profitability increases. It will leave the companies with higher profits after taxes as the value of their oil production goes up. And it is sensitive to production outside Prudhoe Bay to the degree of how prolific other oil fields are, what their costs of production are, etc. This is where the State gets its biggest increments, its adjustment - where it foregoes revenue when profits are low, where it gets the incremental revenues when the oil operation is profitable. So that I don't think it makes sense to jettison what is one of the key elements of your tax regime if it can be avoided.

BENNETT: What do you think will happen to the price of oil in the next year or 18 months?

LIPTON: The price of oil on the average in world markets is going to be going up despite the overhang of surplus in the world over the next year or two years. Thats for the mainstream of oil production. But with surpluses around, the prices of oil around the rims will be suffering discounts. So that the highest price of oil today will probably be going down somewhat, while the lowest prices and the average prices will be going up. That means that for Alaskan crude oil which is marketed in the lower 48 states, and has to be equated with other domestic crude, but mostly with foreign oil imports, the bulk of Alaskan crude will be competing with imported crude that will be going up in price. But just as the foreign crude faces problems around the perimeter, you know the incremental barrel gets...so too, some of the Prudhoe Bay crude, which should all ideally be marketed in District 5 because you get the best net back and sell on, you may find that some of it has to take inferior markets, can't quite swing the same deal of exchange with a District 5 producer who has other alternatives, or carry...transportation. So on the average, the value of your crude will be going up with the average value of your foreign crude. But around the perimeter there may be problems. I would not like to be a speculator who cannot actually use a barrel of Prudhoe Bay crude and starts lifting it on July 1, 1981, and pays over \$3 premium above the royalty value. He may have problems. On the other hand, I would

like to be that winner of royalty crude if there is another crisis in the Middle East.

KILGORE: We would also like to say that if there is another crisis in the Middle East, our basic forecast changes as well about what happens to the mainstream of crude prices.

DANKWORTH: Just to touch on Senator Eliason's question on 30%. I can't help but believe if 70% is received off Prudhoe Bay for example, is divided between the federal government and the producers - with 34% on the producers, and about 36-37% by our figures on the federal government, Alaska takes 30%. Its nice to say - I could see setting up a tax structure where we don't get involved in the shares at all, just forget that, and come up with something. I've lost you somewhere about how we would go about as owners - we are in a rather unique situation in the sense that we own the oil. The people of Alaska. Normally, some fellow out there owns the oil and the land - like in Texas. And perhaps the question becomes a little different. But one, we take our hat off as legislators and put another on as a manager of a resource. I don't know, it just seems like to me they are relative, as to what the producers are making and what the government is taking and distributing in the United States - all states are getting 37% of our oil revenue now. Its not a very effective system, but the federal government is supposed to distribute these funds by going through the federal government to the oil of the states in their shared wealth. I don't know of any other way than to look at our present system and to say do we think 30% and the producers and the federal government take 70% - is 29 or 30% fair for Alaskans? And then try to find the tools to accomplish that. That is why I was interested in the alternatives, and I was pleased to hear that there were more than just what we were looking at. But, if you were to take those guidelines away from me, and say "I think you ought to just sit down and don't tax Prudhoe Bay, tax oil in Alaska for future things", that creates a real problem I think.

LIPTON: Senator Dankworth, I hope I'm not interpreted as having said "don't tax Prudhoe Bay". The only thing I've been saying really is that the sole criterion of the decisions you make on taxation ought to take into account the implications for other producing areas and for potential exploration and development as well. Now, its true of course, that the federal government, and therefore 49 other states, as participants in our union, get a very appreciable benefit out of the profitability of Alaskan oil operations. But you know, when the State of Alaska as owner of land, put up the acreage for exploration on the North Slope, that acreage was very poorly regarded by virtually everybody who was involved. And if you will remember, the amount of bonus income the State of Alaska got for the leases which are now producing in Prudhoe Bay was very very small. What you have got of course is the royalty and out of the profitability of the right to produce. But the prospects were not exciting prospects in 1965, 1967 and 1968. They only became exciting in 1969. Now the willingness of companies to invest and take risks in Alaska was made possible by

the fact that they were getting profits remaining to them and untaxed by other states in the United States. It was profits on Texas, California and Oklahoma production which made possible the risk-taking and production in Alaska also. So I think its correct not only to view Prudhoe Bay as an obvious and important income source to Alaska, and to take into account also the profitability of Prudhoe Bay. And I think that no one, not the industry and certainly not the State of Alaska can close its eyes to the fact that this is a major source of profitability within the State. California is a big oil producing state, but its got manufacturing industry and its got agriculture. And Texas is the biggest oil producing state in the United States and it has a relatively low level of taxation on oil for all kinds of reasons, but incidently, has one of the most prolific agricultural bases, and its the sunbelt for all kinds of defense industries and everything else in it. Well, Alaska "willy nilly" so far is looking at the income of Prudhoe Bay, not just because it is a major oil producing income, but also because it is a major source of income generated in the State of Alaska. But whether or not...I'm not saying the 30% is wrong. What I'm saying is its not a magic figure, and I think you ought not to hang all your decisions on it. There is nothing magic about it.

STURGULEWSKI: The major criteria you have talked about is that we need to look to other developments, other exploration, etc., as a criteria. Do you have other criterion you think we should look at as we judge the magic or lack thereof of our present system?

LIPTON: Yes, but that goes back to part of your whole tax regime. We have in the past pointed out that you judge different kinds of taxes by different criteria. For example, I would certainly judge the quality of the ad valorem property tax by whether its discriminatory or not. I would judge the adequacy of severance tax by whether or not its consistent on the one hand with the practices in other states, and with the levels of prices and how prolific the oil fields in Alaska are. I think one of the greatest contributions you have made in your whole approach to taxation in the State of Alaska, is by making your severance tax sensitive to levels of well producability. I think that is a tremendous improvement in the whole concept of severance taxation. And I think, for what its worth, that one of the biggest improvements you have made in your corporate income tax, is to get off the apportionment formula and to get on to separate accounting. Despite that its very costly to the industry.

ELIASON: You said the net profit is \$6 per barrel - that would be \$1 billion per year over a period of 10 or 20 years. It seems to me that in itself is an incentive. But also, increased value - we know its going to go up. Doesn't that create further incentives?

LIPTON: The incentive to invest in oil exploration in Alaska is a function of two things: 1. What the prospects are - the better the prospects, the more someone can swallow as far as

onerous taxation. These things have to be balanced off. 2. The other thing is not to measure the profitability of Prudhoe Bay against whether it is more or less than is required for an incentive. Look you, as Alaska moves to broaden out to more intensive exploration, there are going to be more and more dry holes drilled in Alaska and there are going to be more and more costly aborted exploration opportunities. And everybody who is taking the risk has to expect that when he finds a bonanza, a good part of that bonanza is left to him because, if its not, how the hell is he going to cover all that unsuccessful exploration? Which you must have if you are going to have successful exploration. If this were an industry with less uncertainty and if the only time you drilled a well it was going to be successful - no problems. But you can't broaden out exploration in Alaska without increasing the cost of unsuccessful exploration. Which means the successful guys have to be left with something to finance the whole business. And when you look at Prudhoe Bay, hell, you are looking at one of the most successful exploration efforts ever achieved in North America. No two ways about it. And if that doesn't return a more profitable operation than the average, then the industry's incentives don't make sense any more. If the most successful isn't left with a very much better than average return then the candle isn't worth the burning.

END OF VERBATIM TRANSCRIPT

OTHER COMMITTEE BUSINESS

Co-chairman Bennett thanked Dr. Lipton and Mr. Kilgore for their testimony, and confirmed that Dr. Lipton would be available to the Senate Finance Committee the following morning at 9:15 a.m. to testify on the gas pipeline in Alaska. The co-chairman further stated that the Senate Finance Committee would meet at 8:30 a.m. to consider Senate Bill No. 205 and Senate Bill No. 244.

ADJOURNMENT

The meeting adjourned at 9:55 a.m.

(Tape SFC 81, # 11, Side 2, 000 - end)
(Tape SFC 81, # 12, Side 1, 000 - 515)

SENATE FINANCE COMMITTEE

March 11, 1981

8:45 a.m.

Tape SFC-81, #12, Side 2 (000-end)

Tape SFC-81, #13, Side 1 (000-431)

CALL TO ORDER

Co-chairman Don Bennett convened the meeting at approximately 8:45 a.m.

PRESENT

All committee members were present with the exception of Senator Sackett who arrived shortly after the meeting convened. Also attending portions of the meeting were Senator Bettye Fahrenkamp; Terry McGuire of the Alaska Power Authority; Dave Hutchens of the Alaska Rural Electric Cooperative Association; Kent Dawson; Beverly Ward; Milton Lipton of W. J. Levy Consultants; Fiscal Analysts Elmer Lindstrom and Milt Barker; committee administrative assistants Maria Converse and Judy Johnston; and representatives from the press including Joe LaRocca.

BILL ASSIGNMENT

Co-chairman Bennett made the following bill assignment:

SB 264 - Senator Ferguson

SENATE BILL NO. 205

Co-chairman Bennett moved that SB 205 (AN ACT MAKING A SPECIAL APPROPRIATION TO THE FAIRBANKS NORTH STAR BOROUGH FOR THE NORDIC SKI CLUB OF FAIRBANKS AND THE NORDIC SKI CLUB OF ANCHORAGE) be brought on for discussion. Co-chairman Dankworth advised that Senator Fahrenkamp, prime sponsor of the bill, was present to testify.

Senator Fahrenkamp stated that the legislation seeks \$35,000 to partially fund the cost of sending 32 Alaskan skiers (20 from Fairbanks and 12 from Anchorage) to the Junior Olympic Games. Due to snow conditions in Alaska, the skiers were unable to raise sufficient funding to finance the trip. They thus contacted the legislature seeking help, and conversations between Senators led to the subject legislation.

The Junior Olympics were scheduled for February 25 through March 5 at Lake Placid, New York. Because skiing conditions at Lake Placid were ruined by three days of rain, the Olympic Games were moved to Steamboat Springs, Colorado. According to newspaper reports, a number of Alaska's young skiers won their areas of competition.

The \$35,000 will not cover the full (approximately \$45,000) cost of attending the Games. Senator Fahrenkamp advised of her belief that the students and coaches should be responsible for raising a portion of the needed funding as an educational experience.

(Senator Sackett arrived at the meeting at this time, 8:50 a.m.)

Senator Dankworth moved that SB 205 pass from committee with individual recommendations. No objection having been raised, SB 205 passed from committee--Senators Sturgulewski, Ferguson, Sackett, Dankworth, and Bennett signing do pass, Senators Stimson and Eliason signing no recommendation.

SENATE BILL 244

Co-chairman Bennett moved that the committee next take up SB 244 (ACT PROVIDING FOR THE FORGIVENESS OF CERTAIN LOANS AUTHORIZED BY LAW AND BY THE ALASKA POWER AUTHORITY FOR POWER PROJECTS AND REDESIGNATING THE LOANS AS GRANTS FOR POWER PROJECTS).

Senator Dankworth advised that he had hoped to have provisions contained in SB 244 "in place" when the committee discussed SB 25 and 26. SB 244 relates to forgiveness of loans for power projects, converting funding for projects included in SB 26 from loans to grants.

Senator Dankworth stated that he was advised by legislative drafters that inclusion of the above provisions within SB 25 or SB 26 would render the bills "too clumsy." "Clean up" provisions have thus been placed in separate legislation.

Senator Dankworth requested that Terry McGuire of the Alaska Power Authority testify concerning the bill. Senator Dankworth added that following Power Authority testimony, he wished to offer an amendment to the legislation.

TERRY MC GUIRE, ALASKA POWER AUTHORITY

Mr. McGuire advised that SB 244 is consistent with the intent and purpose of SB 25 and 26 and provides direct funding through grants for power development projects originally funded as loans from the water resources revolving loan fund (1976-77), Department of Revenue (1977), and Alaska Power Authority (1977-78). The above funding provided for studies, some engineering design, and in some instances construction on the following projects:

Green Lake
Terror Lake
Swan Lake
Lake Tye
Port Lyons

Each section of the bill refers to a separate appropriation--a separate loan.

Referring to the amendment earlier mentioned by Senator Dankworth, Mr. McGuire directed committee attention to page 5, Sec. 17 of the bill, lines 14, 15, and 16, advising of the need to delete "and loaned by the Alaska Power Authority to the Thomas Bay Power Authority" from bill language. He further stated that the word "redesignated" on line 16 should be changed to "designated," advising that because the allocation within an appropriation which funded Lake Tyee was treated as a capital project, there are no loan documents associated with the project. Mr. McGuire further advised that the effective date of SB 244 is "coincident" with SB 25, should it pass.

Senator Sturgulewski spoke to her understanding that funding set forth in SB 244 becomes grants when SB 25 passes, but it again becomes loans in 1986 if total funding for SB 25 has not been appropriated. Mr. McGuire concurred in Senator Sturgulewski's understanding, advising that should the total \$5 billion appropriation not be made, the loans are to be paid back at an interest rate of 7%. He further stated that the legislation provides no term (length of time) on the loans.

Discussion ensued concerning the rate of interest and whether all loans must be paid back at the 7% rate or at the rate originally made (Green Lake's loan is for 35 years at an interest rate of 6%, loans for Terror and Swan Lakes are at 5%, and loans to Port Lions are at 7% and 8.6%). Senator Eliason advised of his feeling that projects should not be required to pay a higher rate than the rate at which the loan was originally made. Senator Dankworth advised that the rate of 7% was proposed to encourage deposit of the \$5 billion in the fund. He added that since the legislation speaks specifically to grants, perhaps it would not be wise to add language permitting loan repayment at the original rate and repayment of remaining funding at 7%.

Mr. Dave Hutchens, of the Alaska Rural Electric Cooperative Association appeared before committee advising that under SB 25 the 7% rate of return would not convert funding to loans. Funding would represent a direct investment by the Power Authority and would earn a return on the state's investment of 7%. In actuality the above rate equates to a much lower rate of interest.

Senator Ferguson inquired concerning the total in general funds relative to SB 244. A brief recess was called while the figures were compiled.

RECESS, 9:06 a.m.

RECONVENE, 9:10 a.m.

Upon reconvening Senator Dankworth advised that the bill totals \$49,960,000. This amount was subtracted from amounts set forth in SB 26 when SB 26 was drafted.

Responding to a question from Senator Sackett concerning the rate of return included in SB 25, Mr. Hutchens expanded his earlier statement, advising that under SB 25 if \$5 billion has not been appropriated to the Power Project Fund by July 1, 1986, projects financed through the fund at that point would have to return to the Power Authority a rate of 7% per year on the investment made in them. This does not represent a return of principal plus 7% interest, but an annual rate of return on the state's investment in the projects.

Responding to a question from Senator Stimson concerning the relationship between SB 244 and SB 26, Senator Dankworth advised that SB 26 would have increased had the \$49 million in funding already advanced to the above listed projects been included. Legislative bill drafters advised that it would be difficult to include forgiveness and redesignation provisions within an appropriation bill, so separate bills were drafted and funding set forth in SB 244 was subtracted from SB 26 when SB 26 was drafted.

Senator Ferguson moved that SB 244 pass from committee with individual recommendations. Senator Dankworth moved that the amendment designating the \$15 million previously-appropriated to Lake Tye as a grant (earlier mentioned by Mr. McGuire) be adopted. No objection to the amendment having been raised, it was adopted. Senator Ferguson replaced his previous motion, and SB 244 as amended passed from Senate Finance--Senators Stimson, Eliason, Sturgulewski, Dankworth, and Bennett signing do pass, Senators Sackett and Ferguson signing no recommendation.

RECESS, 9:15 a.m.

RECONVENE, 9:20 a.m.

When the committee reconvened, Milton Lipton of W. J. Levy and Associates appeared before committee to speak on the Alaska gas pipeline.

GAS PIPELINE

Dr. Lipton advised that it is difficult to discuss the problems of the Alaska Northwest natural gas pipeline at this time. Most of the problems stem from the difficulties of financing, and to repeat and reiterate what the financing problems are adds to the difficulty (certainly in the minds of the lenders). It is a "Catch 22" situation for pipeline participants. On the other hand, it does no good to slough over the nature of the difficulties and the uncertainties.

Dr. Lipton stated that he would not dwell on but simply repeat some of the problems of financing and then move on to something commanding closer committee attention which is not whether or not the pipeline eventually can be financed and whether the price of gas can cover the costs of service, but "whether the candle may be worth the burning" if in fact the costs of building the

pipeline rise astronomically and begin to take up a major part of the value of the gas, if and when it is finally delivered.

Costs of Financing

Two things multiply one against the other. The first is the obviously increasing capital costs of the operation. The second is the risks which begin to cumulate and become aggravated as the capital costs "go very much higher." The basic question, from the beginning and the question which remains unanswered, is, who will be the ultimate bearer of the risk. As pipeline costs mount (the figure now being discussed is perhaps \$30 billion, give or take \$5, \$6, \$7 billion--a wide margin), the risks multiply also. Although there are ways of trying to minimize the risks (for example to make sure that the ultimate costs are covered in the initial contribution of capital or that a secondary fund is accumulated for reasons of contingency in case there are overruns even above the first accumulation or first commitment of capital), as these things go up the lenders are inevitably left with the basic question "Okay, you have protected us against the failure of completion, but there are many things that can interfere with the flow of gas even after completion, and if the flow of gas is interrupted and there is no cash flow of tariffs to fund the debt, who is responsible for repayment?" It then becomes a matter of shifting the risk from the lender to somewhere else. The risk eventually has to fall upon someone. It is either going to fall upon the pipeline participants who obviously don't have the financial resources to commit repayment of debt if they don't have throughput in the natural gas pipeline. Will the lenders assume that final risk? There is a very great reluctance, obviously, for lenders to do so. The third alternative is that the buyers of the gas assume the risk. But, where do you find buyers who are prepared to guarantee the funding of debt even if the gas is not delivered to them or if the gas is interrupted for any considerable length of time (the pipeline is finished, there is a one-year delay before initial throughput for a variety of possible reasons, or there is a pipeline break and all of the environmental factors come to play and even after repair there is a long hiatus). This is a very basic problem. To the extent that pipeline participants try to move the risk, for example to suppliers, through not valuable price contracts but fixed price contracts, all of these devices--anything which minimizes someone's risk--also tends to increase the cost. Because if someone else assumes the risk, he wants the repay, somehow, in the price which he receives. So, you have accumulation of costs. Essentially this is the problem. Further, by statute and by federal decision, the producers, who have a keen interest in seeing that the gas can be produced and disposed of, are inhibited or prohibited from having an equity position in the pipeline. As things now stand, they only have "this wonderful opportunity of being one of the contributors of debt capital with all of the risk." The fact that the federal government, at least to this point, says it will not assume any further support for the pipeline, leaves on the governmental side essentially the State of Alaska.

Dr. Lipton cited two additional points:

1. The run-up in costs. Dr. Lipton advised that he has "no idea whether \$30 billion is even in the ballpark; it may be substantially lower; it may be higher. But the run-up in costs means in fact that the cost of service in the pipeline and the profit that accrues to pipeline participants, related to these higher capital costs, will make the first claim on whatever revenues the sale of gas in the Lower Forty-eight States generates. The question is, "When the gas reaches the Lower Forty-eight and is sold to contractual buyers, will the price that the buyers are prepared to pay cover the cost of service, including the pipeline participants' profit on the escalating capital construction costs." The answer is possibly "yes," maybe even probably "yes," because the value of the gas is mounting year by year in relation to the run-up in competitive oil prices. Had competitive oil prices remained at the levels of 1978, even 1979, there would have been a very grave question whether the gas value would cover costs of transportation to the Lower Forty-eight. But, with the increase in prices, crude oil prices, and the competitive value of the natural gas, there is a good chance the value will cover the cost.

2. The second, more difficult, question is, "Is the candle worth the burning." If a pipeline can be completed and the gas sold and it turns out that the bulk of the gas sales revenues are required to repay the costs of the pipeline and the profits to the pipeline participants, what's left in terms of the wellhead value of the gas. If very little is left in the wellhead value of the gas, there are two parties of interest who must raise questions in their minds. One party is the producers--the gas producers. If in fact they produce and commit the gas to the pipeline, and it's sold, and what comes back to them after all the pipeline costs, includes for them under current arrangements no more than a rate of interest on the capital they commit, then there must be a question in their minds as to whether it makes any sense to commit the gas since the netback is so low, unless there are no alternatives. What they would prefer is that if the pipeline were to be built that they have an equity position in it, in which case their capital contribution would at least allow them to participate in the profits of natural gas transportation. If that were the case, then, even if the transportation segment of the value of the gas is very large (and, of course, the profit on the transportation goes up the higher the cost of construction of the line) at least there would be some offset for them in getting a lower wellhead price for the gas. But this, of course, depends upon whether or not they can get an equity position or even upon whether they might get a variable rate of interest on their lending to the pipeline, depending upon what the equity owners get; there are various combinations. That leaves the State of Alaska, essentially, with nothing left except its economic interest in the wellhead price of the gas, which economic interest becomes less and less the more the transportation cost depresses the value of the gas at the point of production.

The basic question, then, is not only whether the economic value of the gas can cover the costs of construction, but "whether the candle is worth the burning, if in fact the costs of construction eat up so much of the value of the gas." The answer depends upon alternatives. Dr. Lipton advised that he suspected there are alternatives, and alternatives are being considered in the minds of the producing companies. The State of Alaska ought to concern itself too.

Alternatives

If the line fails of completion, or if costs are so high that "the candle is not worth the burning," the alternative that all of the gas at the point of production at Prudhoe Bay be converted to liquids should be considered. The legislature is already contemplating the possibility (and Dr. Lipton added that he understands it is the legislature's hope and expectation) that both the State's royalty share of the natural gas liquids and a contribution of natural gas liquids from the producing companies will move southward through a liquids line and be available for petrochemical processing in Alaska. The legislature has, in a sense, given a franchise for a feasibility study to the Dow Chemical group in that respect.

There is a further possibility that not only the liquids extracted from the natural gas, but the remaining methane that otherwise would move through a relatively high cost natural gas pipeline through Canada can be converted to liquid methanol. And that, then, the natural gas liquids, together with the methanol (in effect no natural gas remains) move south to tidewater through an all-liquids, all-Alaskan pipeline, with the NGL (natural gas liquids) available for petrochemical processing, and the methanol available for a variety of uses both in Alaska and by export because the water movement of methanol is a relatively straightforward movement as is the pipeline movement of methanol. Dr. Lipton advised that he is not suggesting the above as something that ought to be immediately pursued, but advised of his belief that the alternative should be a serious consideration by all parties, particularly the State of Alaska, because in the end the state would suffer most by the diminution--the depression--of the wellhead value of the gas by the run-up of natural gas pipeline costs. It has another value because even if the state has pipeline movement of natural gas liquids on the order of magnitude of 150,000 barrels a day (producers' and royalty liquids committed), the per barrel cost of moving those liquids 800 miles from Prudhoe Bay to tidewater is going to be relatively high. If you move in conjunction both methanol and natural gas liquids, the unit cost of transportation is substantially reduced. This is something that ought to be seriously considered as an alternative. The state is fairly soon going to have to make certain basic decisions. Dr. Lipton stated that he is "convinced beyond a shadow of a doubt that one of the major contributors to the natural gas pipeline--contributors of debt capital--if the pipeline is going to be built will be Alaska." The state will be asked in "one guise or another" to

make a major contribution. At that time the administration and the legislature will have to make a "very, very, sober decision." He stated that the state made a decision two years ago and advised of his understanding that the state is "very, very, happy" it didn't commit itself to a billion and a half dollars before anybody else had subscribed the first dollar of capital to the line. The state is going to be asked again (and it is going to be asked to be one of the earlier lenders) to commit itself to the final decision. When this decision is upon the legislature, it is going to have to assess whether or not this is something the State of Alaska wants to support. Dr. Lipton advised that he suspected that if there is no other alternative, the State of Alaska is so much a party of interest that it is going to be hard to say no. Because the production of that natural gas, which depends upon the ability to move it and dispose of it, is vital to the interests of Alaska. So, if there are no alternatives and the final time of decision-making is upon the state, it's going to be very very difficult. When the state is contemplating or debating the decision the administration and legislature should at least know whether there are alternatives other than shutting in the gas and not being able to produce it at all. The investigation of alternatives, both modes for transportation and for disposition, should be relatively high on the state's agenda. In the end the state may have to find out anyway, but it seems better to have at least some kind of a fix on what the alternatives are before the state is faced either with a yes/no decision on which the fate of the pipeline may hinge, or find out that even with the state's contribution the deal cannot be made, the pipeline goes down the drain and one starts from "home plate--from square zero"--and begins working ahead.

At this point Dr. Lipton concluded his presentation and the floor was opened to questions from committee members.

Senator Dankworth advised of prior legislative concern because the state has "no backup plan." He added he was pleased to hear Dr. Lipton set forth alternatives. He then asked if the oil companies (the producers) aren't conducting extensive studies to determine the cost of the line. He added that conversations with "top people in Houston companies, top people in the Regan administration," top people who will "have anything to do" with the pipeline indicate that there is not going to be a gas pipeline, or if there is, it will be some years away because a number of factors are precluding it. Senator Dankworth advised of concern when reliable individuals say there will not be a pipeline, while the Alaskan economy continues to rely on its eventual construction.

Dr. Lipton stated that serious studies are being conducted, not only concerning the cost but the "range of probable costs upon which all financing plans would have to be based." Financial advisors to Alaska are participating in this operation, but it is unfortunate that it is only now that this kind of cost study is being done, and that serious cost studies were not done so long ago. This is one of the "misadventures" involved in the project.

(Change Tape, SFC-81, #13, Side 1, 000)

Dr. Lipton stated that if the gas pipeline is completed by 1986, the state should be considering what "kind of gas is going to be rolled-in" because the longer one goes, the greater the decline in the available flow of all gas which may or may not be under price control at that time. The lower the price and the greater the volume, the greater the effective roll-in, and the better the chance of absorbing the high cost of Prudhoe Bay gas when it is delivered. There are going to be changes in law. The Natural Gas Policy Act of 1978 is not going to be on the books in 1984 or even 1983. Within a year there are going to have to be revisions. If those revisions take the form of lifting price controls on various categories of gas, including phasing out some of the old gas and letting it go to market price by 1985, 1986, 1987, then there is a problem in roll-in. It may be that by 1986, 1987, at least in the early years of production and delivery of Prudhoe Bay gas it's going to have to stand on its own feet with very little economic support from roll-in. The state should be concerned about this.

Responding to a question from Senator Dankworth concerning his understanding that if the state or federal government does not become involved in the pipeline the chances of it being built are greatly diminished, Dr. Lipton stated "I give it to you as an uninformed opinion, but I think you've this from many more informed people, that it looks very very unlikely that, given this level of cost and the risks still associated, that the total package of financing can be put together without the State of Alaska or the federal government being parties to the ultimate bearing and sharing of the risk."

Responding to a statement by Senator Dankworth concerning lack of federal participation, Dr. Lipton responded "To my mind there are never any absolutes. There is never a never. Change the circumstances and who knows whether or not the federal government out of a sense of responsibility to its treaty commitment to Canada who is very badly out on a limb with the Trudeau government having exposed itself to incredible political risks within Canada for having decided to go ahead with the 'prebuilt' on the basis of 'a smile and nod' from the United States without a firm commitment of support." In the end, the federal government, for a combination of reasons, may enter a treaty commitment. There may be various forms and it may even be possible to get a measure of federal support without even changing the law, i.e. if the commitments or guarantees are not to the pipeline but to lenders or consumers who bear the ultimate risk.

Senator Sturgulewski inquired concerning the role of the producers on the North Slope, owners of the oil vis-a-vis owners of the gas. Is it to their interest to utilize that gas? Dr. Lipton stated that there is no question but what all of the producers have a fundamental interest in seeing that Prudhoe Bay gas is produced--both the associated gas and in due course the

"gas cap" gas is produced and generates revenues over and above costs, against the alternative of continuing reinjection with the costs involved in reinjection and with the adverse impact that this may ultimately have upon oil recovery. From an economic standpoint, Dr. Lipton advised that he had no doubt whatsoever that all of the owners of Prudhoe Bay gas would like to see a plan or decision moving ahead which permits them to produce the gas, and in one way or another generate revenues from production of the gas. Further responding to a question from Senator Sturgulewski concerning costs involving wellhead price, reinjection, etc., Dr. Lipton advised that reinjection is a clear cost to the producer, nothing but a cost. In effect, it diminishes the value of the oil they produce.

Responding to a question from Senator Stimson concerning circumstances surrounding selection of Northwest Pipeline, Dr. Lipton stated that pursuant to Congressional Statute, when the Presidential office made the selection among competing proposals, every proposal except the Northwest alternative stipulated that some kind of governmental financing would be necessary to complete transportation. It was Northwest alone that stipulated it could be financed entirely by the private commitment of capital. And that must have been at least one consideration that bore upon the decision to select the Alaska Northwest project as an alternative to Arctic Gas Consortium or the El Paso proposal.

Senator Stimson then asked, "Who takes the initial step in all of this? The producers have been waiting for the state and the state is waiting to see whether the pipeline is an investment it wishes to participate in. The whole time the federal government has attempted to "stay out of it." Can the project progress without federal government participation? It doesn't appear feasible. Dr. Lipton referred once again to the "Catch 22" quality of the project. So long as the participants in the Alaska Northwest project are trying to put together a privately-financed package of capital, to talk about public (federal or state) participation too much induces every possible private participant to say, "Hey, let's not go too fast on this, let's hold back and see what we can get in terms of government support like loan guarantees and so on." So if one is trying to put together a private package, there is a reluctance to talk about too much governmental support. On the other hand, if at the end of the day one is unable to put together a privately-financed package, and one has explored all alternatives, then the project is either abandoned or one goes to the various governments concerned and says, "Let's participate."

The same problem exists in Canada. There the bulk of the Canadian line from the Alaskan border down into Alberta will probably require a considerable amount of governmental support. But this is less of a problem in Canada because natural gas pipeline construction in Canada has a long history of governmental support. The Alberta Gas Trunk (natural gas corporation) which is now a major participant in the foothills section of the Alaska Highway Natural Gas Pipeline was originally

a crown corporation of the Province of Alberta and was originally financed entirely by the Province and has since gone to private ownership. TransCanada Natural Gas Pipeline which links Alberta Gas with Eastern Canada and the United States essentially had a tremendous amount of Canadian federal government support.

Senator Eliason inquired concerning alternatives available if the overriding factor by which Northwest was originally selected (private financing without government support) is no longer controlling. Is an all-Alaskan line again an option? Dr. Lipton advised of difficulty in answering the above question. Decision may be made by the federal government because of what it feels are strong political commitments that if the Alaska Natural Gas Pipeline cannot be built without federal support, that federal support must be given. Alternatives may not be considered because of the political commitment. From the standpoint of Alaska, whether or not Alaska provides financial support should be contingent not only on the dire straights of that particular natural gas pipeline, but on what the state considers to be viable alternatives. It may be that a natural gas pipeline through Alaska with the transportation of liquefied natural gas thereafter which is sort of an El Paso thing, still faces the problem of the high cost of natural gas transportation through Alaska. It's either 800 miles from Prudhoe to the Canadian border, or it's 800 miles from Prudhoe to tidewater. Dr. Lipton advised that he did not wish to appear negative about the above proposal; it is a possibility. He added that the methanol alternative is also something the state should be looking at.

Co-chairman Bennett inquired concerning the effect of a state decision to take a liquids line to tidewater upon the economics of the Northwest project. Dr. Lipton responded that "if you take out all of the liquids, you raise the cost of transportation of the methane through a natural gas pipeline." There would be a substantial impact because in effect the state would be diminishing the throughput. You are also reducing the average BTU content of what's delivered at the other end. It will have an effect upon the unit cost of transportation in a natural gas pipeline as well. There have been cost estimates made of what that effect would be. It depends upon what proportion of the liquids are taken out and a lot of other things. Of tremendous interest to Alaska is the fact that every increase in the cost of transportation through a natural gas pipeline reduces the the wellhead value. But, when it reduces the wellhead value, it improves the economics of alternative use, and the higher the cost of moving a BTU of energy through the line, the greater the value of the molecule left for internal use in Alaska. That is to say that the rising costs of natural gas transportation improve the potential prospect of utilizing the natural gas liquids--not necessarily for their BTU's but for their molecules. Rising costs improve the economics for internal transportation and use of the natural gas liquids.

Responding to a question from Senator Dankworth concerning the U.S. natural gas market in terms of supply and demand, Dr. Lipton

advised that at the moment it is in surplus. Illustration: Canada just approved the increased export of natural gas to the United States (when the prebuilt is finished) on the order of about a billion cubic feet a day which is about a 30% increase in their authorized exports. At the present time, the U.S. is not taking all of the gas which has already been authorized. Partly this is due to the pricing of Canadian gas, but essentially it is because we now have, temporarily, in the United States a surplus of immediately-available gas--the "gas bubble"--compared to current consumption. Dr. Lipton advised that he does not believe the above situation is a factor to be concerned with for 1986 and onward.

Senator Dankworth raised questions concerning construction of an all-Alaska gas pipeline much like the El Paso proposal given the lack of market on the west coast. Dr. Lipton responded that El Paso representations were that Alaskan gas would not necessarily compete with alternative gas in California, but the west coast would be using the regasified Prudhoe Bay gas, displacing other sources of gas which then would move into midwest and eastern U.S. markets. Dr. Lipton advised, "If I were you, without regard to the pros and cons of the El Paso suggestion, I would always think of gas available to the United States from whatever source (whether it's Mexican gas at the Texas border, Canadian gas coming down the west coast or into the midwest, Alaskan gas however it comes, imported, liquefied natural gas from Algeria, or from Indonesia) always think of that as a net contribution to the total gas availability of the United States. It really doesn't have to be justified in the market closest to where it enters the United States. What you have then is a reshuffling of available gases. The economics of competition will determine where the gas goes. In effect it's not an NCF of gas competing with an NCF of gas. It's six NCF's of gas competing with a barrel of fuel oil which is imported."

ADJOURNMENT

The meeting adjourned at approximately 10:00 a.m.

SFC-81, #12, Side 2 (000-end)
SFC-81, #13, Side 1 (000-431)

SENATE FINANCE COMMITTEE

March 12, 1981

8:45 a.m.

(Tape SFC 81, # 13, Side 1, 435 - end)

(Tape SFC 81, # 13, Side 2, 000 - 776)

CALL TO ORDER

Co-chairman Bennett called the meeting to order at 8:45 a.m.

PRESENT

All members of the committee were present. Also in attendance were Senators Fahrenkamp and Ray; Representative Oral Freeman; Jay Hogan, Director of Legislative Finance Division; Ron Lehr, Director of Division of Budget and Management; Administrative Assistant to Senator Bennett, Judy Johnston; Administrative Assistant to Senator Dankworth, Kathy Martinson; Barbara Walker of the Alaska Nurses Association; and members of the press.

BILL ASSIGNMENTS

Co-chairman Bennett assigned Senate Bill No. 54 to Senator Sackett.

SENATE BILL NO. 4

Co-chairman Bennett stated that the next order of business would be consideration of Senate Bill No. 4 (An Act relating to health care services and the coverage of the services of nurse midwives under the insurance laws of the state), and requested that Senator Sturgulewski present the bill to the committee.

Senator Sturgulewski moved and asked unanimous consent that the committee consider Committee Substitute for Senate Bill No. 4 (Finance) (same title). There being no objection, it was so ordered.

COMMITTEE SUBSTITUTE FOR SENATE BILL NO. 4

Senator Sturgulewski pointed to back-up on the bill in the file, and added that Barbara Walker from the Nurses Association was present to testify before the committee. She stated that the bill basically provides for coverage of nurse midwives practice under health and disability insurance policies that pay for maternity care, and adds it to the list of coverages for Medicaid. She stated that the Committee Substitute makes two changes from the original bill. There had been questions from the American Council of Life Insurance Providers (represented by Mike Thomas) regarding the effective time of this coverage for outstanding insurance policies. So sections 1 and 27 reflect conversations between Senator Sturgulewski, Mike Thomas and Don

Koch of the Division of Insurance on the effective date of the coverage. She stated that the industry as well as the Administration agreed that this was an appropriate way to implement the legislation. She stated that there is firm support for the bill (that Representative Rogers had indicated his support on the House side), though there had been some concern, particularly by the Fairbanks medical community, on the relationship between the parts of the professions (between OB's, GN's and general practitioners). She concluded by saying she felt it was a good bill and stated that she was available to answer any questions the members might have.

Senator Eliason noted that the bill carried a zero fiscal note and asked why the bill was in committee. Senator Sturgulewski stated that though the legislation would not entail further cost, it would allow that private insurance companies pay for midwife services, and would also make it an allowable category under Medicaid.

Senator Sackett requested that the Nurses Association representative Barbara Walker come forward. He stated that his question related to nurses, but not necessarily midwives. Representatives from villages in his districts had informed him that the nurses had changed the regulations and/or the law on whether or not Public Health Nurses could treat acute or emergency cases. He asked for her comments. Ms. Walker stated that the regulations had not been changed, and that to her knowledge it was not a recommendation of the Nurses Association. She stated that possibly Senator Sackett was referring to changes in the Department of Health and Social Services with regard to nurses working in remote areas, or that possibly it was in reference to Senate Bill No. 238 which was a complete revision of the Nurse Practice Act. She added though that there were no provisions in the revision that would prohibit nurses from giving aid or assistance.

Co-chairman Bennett asked Senator Sturgulewski if midwives could set up their own billing procedures and their own practice per se if this legislation were to pass. Senator Sturgulewski asked that Ms. Walker respond. Ms. Walker stated that it was her understanding that the nurse midwife could be reimbursed directly; presently the physician is the only person reimbursed. But, yes, a nurse midwife could set up her own practice. Co-chairman Bennett expressed the worry that this particular level of practice could then be carried out unrelated to and uncontrolled by a physician. Ms. Walker stated that would not be the case, as the nurse midwife by law cannot practice without a collaborative relationship with a physician. The Boards of Nursing and Medicine in January of last year adopted regulations governing the practice of all advanced nurse practitioners (nurse midwives are one category under "advanced nurse practitioners"). One part of the regulations states that the nurse midwife must present to the Board documented evidence of an established collaborative relationship with the physician actively licensed in the state. She said this was the case in all states. The

only "so called" midwives who work on their own are the "so called" lay midwives who usually have no medical education and work in the community and assist women with home deliveries. But nurse midwives usually do their deliveries in the hospital and follow the mother through the pregnancy state, and if there is a medical complication, the physician is called in to collaborate.

Senator Sturgulewski pointed to a memo in the file to her from the Family Health Section of the Department of Health and Social Services which speaks to the difference between the "lay" midwife and the "nurse" midwife. She confirmed that there are governing regulations that make the physician solely responsible. Ms. Walker added that the nurse midwife is also solely responsible for her practice. She cannot go out and practice without a collaborative relationship with the physician.

Senator Stimson asked what the practical aspects of the collaborative relationship would be. Ms. Walker responded that the nurse midwife and the physician would decide between themselves at what point the nurse midwife would consult the physician. There would be an agreement on what was a normal pregnancy; any deviation from that would require a physician to be present. It was established that in normal pregnancies, a physician would probably never be consulted unless the physician made a practice of routinely seeing the patients.

Co-chairman Dankworth moved and asked unanimous consent that the bill be moved from committee with individual recommendations. There being no objection, it was so ordered and the committee report was signed as follows: Co-chairman Dankworth signed "no recommendation"; Co-chairman Bennett signed "do not pass"; and Senators Sackett, Stimson, Sturgulewski, Eliason and Ferguson signed "do pass".

SENATE BILL NO. 17

Co-chairman Dankworth requested that Senate Bill No. 17 (An Act amending the Executive Budget Act to provide for agency budgeting in place of program budgeting; and providing for an effective date) be considered at this time. He stated that this legislation would amend the Executive Budget Act by removing certain references to terminology related to budgeting by program category. It would make clear that future budgeting would be done on an agency basis. Budgeting by program was recommended in the early 1970's as a method to reveal the full cost of program objectives within an agency; since then this method has not proven to fulfill those objectives. It lacks accountability of department heads that would otherwise be available under agency budgeting. He stated that he would like to have previous Finance Committee chairmen speak on the issue, but first asked Representative Oral Freeman, Vice Chairman of the House Finance Committee to come forward with testimony.

Representative Freeman stated that he was delighted to have an opportunity to say a kind word for the proposed legislation. He

stated that he originally felt that if he just worked "harder and harder at it" he would eventually understand "better and better how program budgeting worked". But, he said after six years, he had almost given up hope. He had considered introducing similar legislation in the past, but felt that he should wait until both Finance Committees agreed on the issue; he said that he felt the timing was right at present. He said that he had spoken with the House Finance Committee Chairman, and with his agreement, a duplicate House version of the bill had been prepared and introduced. He said that for several years he had the subcommittee on the Transportation category budget, and that it was virtually impossible to really understand exactly what was going on. He said that years ago with agency budgeting, one could go through a budget line by line and determine who did what, how much it cost, and whether or not Alaskans were getting their moneys worth. In conclusion, he stated his full support for the bill before the committee.

Discussion and questioning ensued on the practical aspects of the legislation, how it would be instituted. Comments were made regarding specific department positions being spread out among the categories, making a very cumbersome program budget, one too time-consuming and difficult to really digest and evaluate in the legislative session. The need was expressed for getting each department budget in "one stack", so that an overall picture would be possible. Senator Ferguson asked Representative Freeman if he felt that with program budgeting there were duplications of service and possibly even "double dipping". Representative Freeman stated that he felt that was definitely so, but that he simply did not have the time, the knowledge or the expertise to find these situations. He said that if the Legislative Finance fiscal analysts - who do have the expertise - work on the budgets all year and can't find all the duplications and double dipping situations, a legislator here for only a few months doesn't have a chance.

Co-chairman Dankworth requested that Senator Sackett speak on the legislation, and added that certainly Senator Sackett was one of the most knowledgeable and experienced persons on the issue.

Senator Sackett stated that when he first came to Juneau in 1967, the budget was arranged by department. In addition, the total budget was only just over \$100 million, so things were a little more simple. After the change to program budgeting, he felt that it took him between 6-8 years before he felt confident that he understood where everything was located in the different categories. He stated that with agency budgeting, there would be many less layers of procedure as far as the departments were concerned. He stated that certain departments were adding new budget concepts to the present program budget concept, and gave the example of the Department of Natural Resources, which last year added a management by objectives concept. All of this is very difficult for a legislator coming to the capitol for a short time, and eventually there is runaway budgeting and absolutely no control. He stated also that after going through all the various

programs in the categories, the budget goes back to the specific department and the programs are run from that department. The Legislature never really has the opportunity to see the department as it functions as one entity, even though in reality that is what it does. He concluded that for all the problems program budgeting creates, he did not feel that it was a valuable budgeting concept, particularly for the Legislature working with it on a short term basis.

Further discussion ensued. Senator Sturgulewski expressed the possible need for some kind of review for programs that do cut across agency lines, and still get the advantages of the agency budget. Senator Sackett stated that by "re-shuffling" what is in the total budget back to the specific department, the goals and objectives, management techniques and the programs themselves would still be visible. Duplication of effort is also an aspect of administering programs, which is the basic responsibility of the administration.

(BEGIN SIDE 2, SFC 81, Tape # 13, Side 2, 000 - 776)

Co-chairman Dankworth then requested that Senator Ray, who was a member of the Legislature before and after program budgeting was instituted, come forward and speak to the committee on the proposed legislation.

Senator Ray stated that he had been on finance committees for 14 of the 17 years he had been in the Legislature and had been Chairman of both the House and the Senate Finance Committees. He stated that he had worked with both the agency budget concept and the program budget concept. His feeling was that if the Legislature wants to trace the full monies and find out "who is doing what", it would have to return to agency budgeting. He repeated the worry about duplication of effort, and said that it was the old game of "they hide the money, and we try to find it". He felt that with the agency budget, the Legislature would at least have 50/50 opportunity to win at the game.

Co-chairman Dankworth then requested that Ron Lehr, Director of the Division of Budget and Management, come forward to testify on the legislation. Mr. Lehr stated that he would recommend against the bill, and would offer an option. He stated that his objection to the bill was not because it would be easier for Budget and Management to continue program budgeting, as it would actually be easier with agency budgeting because they could deal with one agency at a time. But, he said, his objection was due to a change in focus. Right now with program budget, the focus is on the services that are being delivered to the public. By going to agency budget, there would be a much more introspective focus - whereby each commissioner would do what was most administratively convenient, as opposed to what would be the best services to produce. Mr. Lehr disagreed that program budgeting does not allow legislators to see what the different agencies are actually doing. He said that agency budgeting would show what activities the departments are involved in, but that the services

to the public should actually be more important. As far as duplication of effort went, Mr. Lehr felt that with agency budgeting the problem would become more profound than it is under the present system. Generally speaking of the problems the budget as a whole presents to the Legislature, he agreed that the sheer size of the budget was almost too much, even for those working with it on a year-round basis. But, he felt that a budget summary such as the one Budget and Management uses (a "policy budget" or a "preliminary budget") might make the system more manageable for the legislature, still concentrating on services to the public. He felt that the program budget concept forces the different departments to recognize which other departments are providing the same services so that there will be no duplication of effort. Without program budgeting, he did not feel departments would work cooperatively on similar services. He felt that with agency budgeting, Budget and Management would not be able to provide the Legislature with as much information on specific programs as they are able to provide with program budgeting. He used the example of the Bottomfish Program that had previously been mentioned by Senator Sturgulewski.

Co-chairman Dankworth agreed that was the design of program budgeting, but after speaking with various legislators, he felt program budgeting was not doing what Mr. Lehr said it was doing. He said that it makes good rhetoric, but doesn't work for laymen who come here for 60-90 days to deal with a budget for several billion dollars. He used the Bottomfish Program as an example of a budgeting problem that would be improved by agency budgeting. He reiterated the need stated by Senator Sackett to have a grasp on the departments as whole entities.

Senator Sturgulewski, using the Bottomfish Program, stated that she can only go by what the Department of Fish and Game says about the program, though she knows nothing about the portions of it that are being handled by the Departments of Community and Regional Affairs or the Department of Commerce. It seemed to her that the big problem is with how the information is presented to the Legislature. She asked how many programs there were that cut across agency lines. Mr. Lehr stated that there are about 15-20. Senator Sturgulewski stated that these programs would be separated from each other in any case, and stated a need for a way to get the programs reviewed. Mr. Lehr stated that there is that accountability in program budgeting even at the lowest level. Senator Sturgulewski asked why the administration cannot provide the information in an agency format and also present the program information by using the computers. Mr. Lehr stated that it could simply be done mechanically by rearranging the budget books. Discussion continued on possible budget formats.

Co-chairman Dankworth reiterated that from his point of view, the agency budgeting would be preferable. He asked for further questions and/or discussion.

Senator Stimson brought up the Bottomfish Program again. He stated that the program, included in the Department of Fish and

Game, the Department of Community and Regional Affairs, the Department of Education, the Department of Commerce and Economic Development, and the Department of Labor. He stated that all of that is Operating Budget but its coming through the Capital Budget. He said that he had requested the agencies to bring that up in the Operating Budget, and the response seems to be that they will not do it. The rationale given was that the Governor has a ceiling on the Operating Budget. He said that of the \$6 million in the Capital Budget request, only about \$2 million was legitimate Capital expense, with the remaining \$4 million undoubtedly surfacing next year in the Operating Budget. Mr. Lehr stated that he had directed the Bottomfish Program to put these things in the Operating Budget, but it had not been done. He agreed that the items requested in the Capital Budget were clearly Operating Budget items.

Senator Sturgulewski stated that at least with the program budgeting concept, problems like the above show themselves. Senator Sackett pointed out that however, these situations were an exception to the rule by a great percentage. He added that having more than one department work on the same objective is in itself inefficiency. But he said 98% of the departments have functions and responsibilities by department. Senator Sturgulewski stated that she hoped to devise some way to use an agency budgeting approach, but to also receive some kind of a report on these 15-20 overlapping programs.

Co-chairman Dankworth then requested that Mr. Jay Hogan, Director of the Legislative Finance Division, come before the committee for testimony, and specifically requested the history of program budgeting in Alaska as well as the portions of the concept that were not fulfilled.

Mr. Hogan pointed to the bill file where was located an executive summary of a series of reports prepared to implement program budgeting in 1971 and 1972. It passed as an Act in 1970, as a piece of model legislation that was introduced by the then Governor. The implementation of program budgeting fell to the next administration. Management Analysis Center, Inc. was the firm selected by the administration in 1971 to prepare the format for beginning program budgeting. He stated that the advantages of the concept were outlined in the white pages of the executive summary, with the final report printed on pink pages. He stated that the concept was designed around the eventual reorganization of state governments along program category lines. What happened was that Alaska never went the last step. He pointed to another bill in the file, House Bill No. 676, introduced in 1972 by the total membership of the House Finance Committee, that would have accomplished this reorganization; that bill never passed. The original concept was based on the desire that people responsible for the programs should be identifiable and should have control over the programs within the entire program category. However, what Alaska has now is program budgeting "super-imposed" on an organizational structure. In some cases, its not a bad arrangement because one finds most of the department's functions.

But in other programs, certain departments virtually lose their identity as they are so scattered.

Mr. Hogan stated that the whole budget in its abbreviated format is on the computer and it would not be difficult to sort it one way or another. So if the BRC would feel more comfortable reviewing the budget by program, the computer could sort it that way. On the other hand, if the Legislature feels more comfortable reviewing it by agency, then the computer can sort the budget that way.

Senator Sturgulewski asked Mr. Hogan what he felt the Finance Committee's role in reviewing programs would be if we were to go to agency budgeting. Mr. Hogan responded that in many cases programs would be properly combined under the agency. He felt there were two ways to approach it. There could be cross-references in the budget to identify those programs that cover more than one agency, and subsequently get a programmatic presentation of those key 15-20 areas. Another way would be to utilize the computer to sort budget documents either way. Senator Sturgulewski asked Mr. Hogan what he would have the administration do in preparing their analysis that comes to the Legislature. Mr. Hogan responded that over the years as he has worked with the Legislature, the Legislature seemed to prefer to hold an administrative officer accountable for a program. There seemed to be a more comfortable feeling about that, as the Legislature does not have time to devote their full attention to the budget even during the session. To Mr. Hogan himself, that issue was not so important as he has time all during the year to "ferret out" the problems. In the analysis of the budget as far as Legislative Finance was concerned, it did not matter to Mr. Hogan which method would be employed. But in the execution of the budget as far as the agency was concerned, it does operate on an agency level. When the appropriations are made, some of the advantages of program budgeting do not materialize as the agencies are in charge of the things that are legally placed with them. Further discussion ensued as to the semantics of the problem, and of the practical application of the proposed legislation.

SENATE BILL NO. 6

Co-chairman Bennett informed Senator Fahrenkamp that since the hour was late, the committee would not be able to take up Senate Bill No. 6 (An Act establishing the Alaska Administrative Journal) at this meeting and that it would be rescheduled for the following morning.

RETURN TO SENATE BILL NO. 17

Senator Eliason asked Mr. Hogan, if the Legislature returned to agency budgeting and "red-tagged" the programs that cross agency lines, would it be easier to understand the budget as a whole better than with program budgeting. Mr. Hogan responded that he felt the work of reviewing budgets would be the same, but that

committees would assign agencies with some sense of balance - the larger agencies would be assigned to one person and some of the smaller agencies would be grouped together. Special area programs like the Bottomfish Program would stand out just as well as with program budgeting.

Senator Ferguson moved that Senate Bill No. 17 be moved from committee with individual recommendations. Co-chairman Dankworth requested that Senator Ferguson hold his motion as there were proposed amendments in the file relating to the supplemental appropriation budget, and since the committee had not had sufficient time to peruse the material he wished to hold the bill over. Senator Sackett agreed that this would require a great deal of discussion. Senator Ferguson withdrew his motion.

Co-chairman Dankworth moved that the bill be held over until the March 17, 1981 meeting. There being no objection, it was so ordered and the bill was held over in committee.

ADJOURNMENT

The meeting adjourned at 9:50 a.m.

(Tape SFC 81, # 13, Side 1, 435 - end)
(Tape SFC 81, # 13, Side 2, 000 - 776)

SENATE FINANCE COMMITTEE
March 13, 1981
8:40 a.m.

SFC-81, #14, Side 1, (000-696)

CALL TO ORDER

Co-chairman Bennett convened the meeting at approximately 8:40 a.m.

PRESENT

All committee members were present. Also in attendance were Senator Bettye Fahrenkamp; Christopher Noah, Executive Director of the Alaska Council on Science and Technology; and administrative assistants to Senate Finance Kathy Martinson and Judy Johnston.

BILL ASSIGNMENT

Co-chairman Bennett made the following bill assignment:

SB 276 - Dankworth

SENATE BILL 6

Co-chairman Bennett moved that SB 6 (ACT ESTABLISHING THE ALASKA ADMINISTRATIVE JOURNAL) be brought on for discussion. Senator Fahrenkamp appeared to testify on behalf of the legislation. She advised of her preference for the Judiciary Committee Substitute over the original bill, advising that the purpose contemplated by the legislation has been before the legislature under various names for a number of years, and similar legislation "made it as far as House Rules last year.

The Alaska Administrative Journal as envisioned in SB 6 would be similar to the Federal Register. It would compile state information within a single publication.

The Judiciary Committee in effecting its committee substitute wished to make clear to the public that whether the Journal is printed by a state agency or private firm, the publisher is not liable for errors and omissions. The Department of Law felt previous legislation was too general. It is necessary to identify areas to which the "code" applies. Senator Fahrenkamp presented an amendment to the Judiciary Committee substitute for consideration, advising that the amendment adds "a number of sections which were left out." It also shifts responsibility for the Journal from the Lt. Governor's Office to the Department of Administration--the Lt. Governor has said that he will personally see that the Journal is published.

Senator Fahrenkamp added that it is hoped the Journal will not require a Fiscal Note after the first year or so. At that time, subscription from the public should cover costs.

Responding to a question from Senator Stimson concerning who would be using the Journal, Senator Fahrenkamp advised that it would be helpful to "anybody in the business world" trying to keep up with state happenings, those in the construction field, contractors interested in state bids--basically the same individuals interested in the Federal Register.

It is difficult to estimate "how long" the Journal will be, given the unpredictability of regulation lengths, etc. There will probably be about 1,000 subscribers.

Senator Stimson asked if state agencies would use the Journal. Senator Fahrenkamp stated that she didn't know whether agencies would subscribe to the service, but copies would be given to libraries.

Senator Sturgulewski moved for adoption of the amendment previously presented by Senator Fahrenkamp which would add additional agencies and change responsibility from the Lt. Governor's Office to the Dept. of Administration. No objection to the amendment having been voiced, it was adopted. Senator Sturgulewski then moved that Committee Substitute for SB 6 (Judiciary) pass from committee with individual recommendations. No objection having been raised, Committee Substitute for SB 6 (Judiciary), as amended, passed from committee--Senators Sackett, Stimson, Sturgulewski, Bennett, and Eliason signing do pass. Senator Ferguson signed no recommendation.

SENATE BILL 48

Co-chairman Bennett moved that SB 48 (ACT RELATING TO GRANTS FOR NORTHERN TECHNOLOGY) be brought on for discussion.

Senator Eliason advised that the above legislation "is a Governor's bill." He further advised that Mr. Chris Noah, Executive Director of the Alaska Council of Science and Technology was present to testify.

Mr. Noah stated that the Governor's transmittal letter, accompanying the bill, explains "what the council is trying to do."

Mr. Noah presented the following bill analysis:

Section 1 increases allowable grant funding from \$5,000 to \$7,500 due to inflation and a desire to offer greater technical assistance to inventors.

Section 2 changes the definition of "northern technology." Mr. Noah stated that the council previously had seven categories within its function: energy generation, waste

disposal, recycling, food production, transportation, building design, and industrial enterprise. The council would like to include medicine as a possible grant area. Further, the Alaska Energy Center has taken over energy grants, so the council has decided to concentrate on other areas like food production and waste disposal, hence the request for a broader definition of "northern technology."

Senator Sturgulewski advised of her concern regarding a lack of follow-up on behalf of the council. Mr. Noah responded that the program is relatively new, but of the 20 individuals funded in 1979, only one person has "not produced," or told us why he hasn't come through. The council has granted extensions in some instances because its grants are made to average Alaskans who design experimental devices on a part-time basis.

Upon commencement July 1, 1979, the council used a portion of its operating budget to get funding to people by September. Progress is currently running about six months behind due to shipping problems, etc.

Mr. Noah agreed that the program "needs some monitoring/fiscal tracking."

He advised of a recently completed film which explains the council's function, shows recipients working on grant projects, and highlights innovative successes.

Senator Sturgulewski asked how one would find out about an invention developed through a council grant. Mr. Noah responded that the council issues a final report which is given to libraries, the Governor's office, legislative offices, and the press. The council attempts to make others aware of successful inventions, and if an individual wishes to inquire further, he is directed to the inventor.

Senator Stimson inquired further concerning accountability for grant funding and evaluation of the final product. Mr. Noah advised of reports issued at various stages (progress reports). In three months, the council will issue its final report which lists project successes and failures for 1979-80. This report, along with the names and addresses of grantees, will be given to libraries around the state. As a sample project Mr. Noah cited the instance of a grantee in Anchorage who has extended the growing season four months--two months in the spring and two months in the fall--through design of a special greenhouse.

Responding to a question from Senator Stimson concerning contracts and terms relating to grants, Mr. Noah explained that the council requires prospective grantees to submit a proposal setting forth their goal and a time period within which it will be accomplished. This proposal becomes the contract between the council and grantee when the grant is made. The council has not set up strict time frames because each project is different.

Referring to the fact that the bill contemplates an increase in grant amounts but bears a zero fiscal note, Senator Stimson asked if the grant increase would be covered in the council budget. Mr. Noah responded that the increase would be covered in the upcoming budget--the council has requested \$260,000 for grants.

Senator Sturgulewski advised of her original intent to amend the bill to call for review of projects and increased dissemination of information. It would cost approximately \$50,000 to effect the change. She advised that after discussion with Mr. Noah and Senator Eliason she decided not to effect the amendment but requested instead that correspondence be directed to committee concerning the manner in which the council will follow up on accountability and dissemination of information with existing staff. Then, next year, the legislature can check council progress and follow-up.

Senator Ferguson advised that he does not support the council's program, terming it a "rip-off." He further advised that he would not support the grant increase from \$5,000 to \$7,500 since he feels the council is unable to justify the amount it currently issues. He inquired concerning the number of grant projects in rural areas, and Mr. Noah advised that the council has funded an innovative farming project in Ruby, a waste reclamation project in Dillingham, and a waste heat project in Hoonah.

Senator Eliason advised that he became interested in the grant program when dealing with new forestry concepts in the Sitka area. He advised of difficulty encountered by "laymen" in understanding and interpreting research information issuing from the University. He added that the council's grant program is at times a "gamble," but even if the council experiences 99 failures and 1 success, such a success may be of great help and benefit to the people of the state.

Senator Ferguson strongly restated his feeling concerning the program, advising that it represents an opportunity for certain people "to rip-off the state for \$5,000." He concluded his remarks stating, "I think this program stinks."

Senator Sackett concurred in Senator Ferguson's objection to increasing the grant amount without review of the names of grant individuals, dollar amounts, and descriptions of projects authorized. He added that in theory the grant program "sounds good, but in practice it has not been good."

Mr. Noah advised that he would furnish the above information to committee staff.

Advising of his understanding that grant funding is applied to materials and equipment rather than a salary for the inventor, Senator Stimson stated that the program appears cost effective since the grantee furnishes "the sweat." He directed committee attention to the Governor's letter highlighting grant projects such as a smoke alarm for bush environments and use of Alaskan

red algae against herpes. Contrary to previously expressed opinion that such research should be conducted through the University, Senator Stimson advised of his support for "creative individuals who can come up with ideas that impact society." He also further advised that the program must be accountable to the legislature. The legislature understands there will be failures, but it must know that work accomplished through the grants is of value to the state. Information must also receive wider distribution than merely "passive dissemination."

Senator Sturgulewski advised of her enthusiasm for the program as well as her concern for needed "standardized follow-up." She moved that the bill be held in committee pending receipt of additional information. No objection to the motion having been voiced, SB 48 was held in committee.

Co-chairman Bennett directed Mr. Noah to compile a list of grantees, dollar amounts involved in the grants, and project descriptions and return to committee in approximately ten to fourteen days. Senator Ferguson requested that Mr. Noah also furnish a list of council members and their backgrounds. Mr. Noah agreed to furnish the above information, advising that the council currently consists of two staff individuals and two hundred volunteers.

ADJOURNMENT

The meeting adjourned at approximately 9:14 a.m.

SFC-81, #14, Side 1, (000-696)

SENATE FINANCE COMMITTEE
March 16, 1981
8:40 a.m.

(Tape SFC 81, # 14, Side 2, 000 - end)
(Tape SFC 81, # 15, Side 1, 000 - 652)

CALL TO ORDER

Co-chairman Bennett called the meeting to order at 8:40 a.m.

PRESENT

All members of the committee were present. Also in attendance were Alison Elgee, Division of Legislative Finance Fiscal Analyst; President of University of Alaska, Dr. Jay Barton; other University of Alaska officials, Dr. Cutler, Dr. Harrison, Dr. Carter, Dr. O'Rourke, Dr. Dhingra, Dr. Paradise, Dr. Biggerstaff; Administrative Assistant to Senator Bennett, Judy Johnston; Administrative Assistant to Senator Dankworth, Kathy Martinson; and members of the press, including Joe LaRocca and Patty Ginzburg.

BILL ASSIGNMENT

Co-chairman Bennett assigned to himself Senate Bill No. 214 (An Act making a supplemental appropriation to the Department of Commerce and Economic Development for a mining loan fund).

DR. J. BARTON - UNIVERSITY OF ALASKA BUDGET OVERVIEW

Co-chairman Bennett requested that Dr. Barton come forward to present a University of Alaska budget overview to the committee. Dr. Barton stated that he would make some brief opening statements and then remain available for questions. He stated that he still felt the same enthusiasm regarding the University of Alaska as when he took over the Presidency a little over a year ago. He thanked the committee for the support it has given to the university, both directly and indirectly. He felt that the strong ties the university is beginning to forge with the state are indicating that the university is worthy of support. He stated that he would like to speak at this time on the four following topics:

1. The University plan for FY 82 is reasonable and realistic.
2. The plan is indeed a plan for action.
3. The plan is responsive to the needs of the State.
4. The plan reflects the concern of the University for full accountability to the State, and for sound and prudent leadership and management.

Dr. Barton proceeded to discuss the above four items:

1. He stated that he felt the UA budget this year is truly realistic and reasonable. The needs for higher education in Alaska have never been greater. Last year, more than 40,000 people each semester have been involved in one or more programs of the university, both credit and non-credit. More than 30,000 of those were in credit courses. He pointed out that was almost 10% of the State's population in terms of the total individuals touched by the programs of the University. He pointed to a March 3 article in the Wall Street Journal by Peter Drucker regarding coming changes in our school system which he felt were relevant to Alaska. He stressed the importance of education for our future.

Dr. Barton stated that he was "a little chagrined to note" that the proportion of funding allocated to the University of Alaska from the State's Operating Budget for the last few years has been declining. In 1980, 9.8% of the State's Operating Budget was dedicated to investment in knowledge capital. In FY 1981, it was 7.7%, and in FY 1982 (as proposed by the Governor's budget) it was 6.8%. This was a comparison by agency, though the same downward trend would be reflected if it were compared by category. In fact, he said that this year's recommendation for the University ranks the lowest in percentage of any component of the Operating Budget - a 10.3% increase. Even if the University plan were funded as it was requested, it would still rank second lowest of all the components proposed in the Governor's Budget Request. He asked that the Senate Finance Committee reconsider that relative standing, and to continue to invest a significant portion of the State's Operating Budget in the University of Alaska.

Dr. Barton discussed the budget planning process for the University, who was involved, and the fact that the planning essentially begins with the professors and teachers within the university system. He stated that he felt this grass roots planning process was beginning to work very well. He spoke of strategies for the future developed from planning assumptions. As an example he pointed to results of planning for education to the fisheries industry of the State of Alaska.

2. Dr. Barton expressed that the University feels it is responsive to the needs of the people of the State of Alaska. He stated that if the University does nothing else, it would like to inculcate in its students "habits of the mind" so that they can "go on learning again". This perhaps is the biggest investment in knowledge that the State could make. He stated that the programs this year stress a shift of interest from some of the liberal arts and fine arts programs to much more "practical" programs. Though they intend to inform all their programs with the "wisdom and insight" that the liberal arts offer, they also intend to respond to the interests of the State by developing business and public administration, agriculture and land resource management,

environmental and marine science programs, vocational/technical instruction, and engineering programs (including an engineering program for the University of Alaska at Anchorage. He said that he felt the plan this year was more responsive to the needs of the State for renewable and non-renewable resources.

Dr. Barton continued by speaking of new approaches for use of knowledge in relation to problems in the State, such as in the fisheries and in agriculture, especially in relation to the world food problems. He spoke of linking engineering and technology to productivity as being areas where the University has demonstrated its competence in experience and direction.

3. He stated that he felt the plan this year was more responsive to the needs of Alaskans for greater access and learning opportunities. He stated that the University would like to provide more counseling and advising, as well as to pay more attention to student record systems and transcript systems, to better serve the students. He said the University is looking more seriously at telecommunications and computer based education. Finally, the cross-cultural program in bilingual and rural education would require a significant increase in funding for its full support. Funds were also being requested to improve coordination and management services, and to increase the University's accountability to the State.
4. Dr. Barton stated that he had earlier informed committee members that this year, for the first time in recent history, the University's external audit resulted in a "totally clean and unqualified opinion". In January the University went on line with a financial accounting system that reports to the Legislature in the fashion earlier requested by the Legislature. There will be monthly statements that show expenditures in the same format which other State expenditures are shown. He stated that he would like very much to increase the overall accountability to the State.

In the area of Capital Construction, Dr. Barton stated that the plan is appropriate to the program needs of UA in its present stage. UA has asked for about \$12 million in this area for instructional equipment, research equipment, for on-line record systems, funds to support a modest marine training vessel in Valdez, and a whole series of activities that would be immediately fundable and not require a tremendous amount of time and construction. They are capital improvements in the technical sense of the State's budget system.

Dr. Barton stated that about \$13.7 million has been requested for handicapped barrier removal, to repair the Seward Pier; develop a coal handling facility in Fairbanks; repair and renovate classrooms across the State; and for roads, streets and parking, etc. These are funds also that could be delivered to the

economy just as quickly as the plans are taken from the drawing board and would not require elaborate planning as do buildings.

Finally, Dr. Barton stated, about a half dozen major facilities have been requested for \$52 million, in addition to the geophysics building in Fairbanks, a classroom building for UAA, a core marine building for Juneau, and other structures that are literally large scale capital improvements.

Dr. Barton stated that these were reasonable plans for the Committee's review. The basic UA request for about \$27 million for repairs and alterations and for equipment were straightforward. He wished to conclude by saying that the building of a "great university", one worthy of the State of Alaska, is a task of the University students, faculty and staff, and of the Governor, the Regents and the Legislature. He stated that this achievement would require rising above regionalism and partisan politics. He cited what he termed a "dramatic quotation" from Thomas Jefferson, "If a nation expects to be ignorant and free, and in a state of civilization, it expects what never was and never will be." He concluded by saying that he would like very much to plan with the Legislature how "we might build a great university in a great land, beginning in FY 82."

Co-chairman Bennett thanked Dr. Barton for his testimony and subsequently asked for questions and/or discussion from the committee members.

Senator Ferguson pointed out that 70% of the UA budget goes for salaries, and specifically pointed to two positions in Kotzebue - one for \$64.5 and one for \$81.6. He asked Dr. Barton if anyone was worth \$81.6. Dr. Barton responded that he was not at all sure anyone was. He stated that UA plans for Kotzebue were totally up in the air - the Regents, the Education Committee and the Community College Committee met on this issue just last week and will be making recommendations to the full Board. He stated that the University hopes to re-think its whole position in that area.

Senator Sturgulewski stated that there had been a great deal of talk about the University and the "role of excellence". She asked how that was quantifiable and if the University was looking into measures showing whether or not it is "on to" that goal. Dr. Barton stated that quality control programs for a university has to look partly at outcomes - how do students do on standardized exams in comparison to other institutions, how do they do in the marketplace, what is the reaction of employers to students, what is their own feeling of satisfaction once they have tested their learning against the realities of the world of work, etc. He provided a sample of these kinds of outcomes. The nursing program at UAA has produced a graduating class that annually takes the national nursing exam. This year, all the students scored above the national median. The class average as a whole was two standards above the national median. The

performance of UA engineers in Alaskan companies has been excellent. Both ARCO and SOHIO are convinced that they will "hire anybody the UA can produce". He stated that the medical technology program at ACC has also scored significantly higher than the national average on national exams. He stated that that is the kind of information the University of Alaska is looking at to determine if it is reaching its own goals. Senator Sturgulewski asked if the UA was institutionalizing those measures for the entire UA system so that someone from outside the system can "audit" UA accountability. Dr. Barton stated that the UA is developing a Quality Assurance Program, but pointed out that each of the measures he had referred to cannot be applied to all programs.

Senator Stimson expressed concern about the way community colleges fit into the University system. He pointed to a study done recently by the Post-secondary Education Commission and the fact that it recommends the community college system have a president reporting directly to the Board of Regents. He asked what Dr. Barton's as well as the Board of Regents' reaction to that was. Dr. Barton responded that at least the study had not recommended total separation. He said that he felt there were better ways to support and integrate the community college system than the approach developed by the "little subcommittee". He felt there were other ways to give the community college more leverage. He did not comment on the Boards' reaction.

Senator Ferguson asked about plans for a four-year engineering school in Anchorage. Dr. Barton stated that he had recommended to the Board last fall that the last two years of the civil engineering program be developed so that there would be a baccalaureate program at UAA. The final decision has been delayed pending one further review by a man recommended by the Engineering Accrediting Association - Dean William Sanctor of the School of Engineering at the George Institute of Technology. The report is on the way, but he has tentatively answered "yes" to the following questions.

1. Can an accreditable excellent program in civil engineering be developed at UAA?
2. Can it be done without hurting the program at UA Fairbanks?
3. Should it be done? Is the effort, the cost and the benefit worth the benefits that are involved?

Dr. Barton said with that and with the full report on the way, he would recommend again to the Board in March that they proceed with the development of a civil engineering program at UAA.

Senator Ferguson asked if there were plans for a law school. Dr. Barton responded that there were no such plans. He said that there had been short discussions concerning law education in Alaska. The general consensus was that in this stage of U.S. development, an additional law school is probably not needed.

The nation has enough lawyers and enough law schools. He stated that he did not feel, with the large number of attorneys in Alaska, an Alaskan law school could not be justified. Educational opportunities for citizens in the State who need to study law could be offered through a WICHE or WAMI program. He added that he felt there was a strong need in Alaska for continuing education in law, especially for subjects not well covered in a law curricula such as public land issues.

Senator Ferguson asked about private enterprise supporting a dorm or family unit in Anchorage. Dr. Barton responded that there has been informal discussion and plan more in-dept conversation on dormitory policy next week. They have identified need for student housing in Juneau, modest need for student housing in Anchorage, and need at a number of community colleges such as Kenai. Whether these needs can best be met by leasing private facilities or by developing relationships with private owners, or by building state subsidized programs has not yet been determined.

Senator Sackett asked Dr. Barton if there were any supplementals coming in this year. Dr. Barton stated that there were a small number coming in - one is for the ACC negotiated salary settlement, another is for sewer cost increase at UA Fairbanks, and the other is for intercollegiate athletics at Fairbanks, for a total of \$520,000.

Senator Sackett asked how much of the above mentioned capital improvements projects were actually in the Governor's recommendation. Dr. Barton responded that about \$5 to \$6 million out of a total of \$78 million was included. Senator Sackett requested that he (as well as the other members) be provided with a list of these projects in Operating and Capital.

Senator Sackett asked for the total UA request, over and above the Governor's request - both Operating and Capital. Dr. Barton responded that it was about \$6.8 more in Operating and about \$70 million more in Capital.

Senator Sackett asked if Dr. Barton anticipated any additional requests, and Dr. Barton responded that he did not. He added that "given your generosity last year, we have been fairly hard on requests for supplementals."

Senator Sackett pointed out that Dr. Barton had indicated a new area of emphasis, which was the vocational/technical area, and asked that Dr. Barton elaborate on that. Dr. Barton stated that of the requests for funds to increase educational opportunities in the State, the biggest single item had to do with additional vocational/technical instruction. This includes programs that extend from Police Academy Training at ACC to additional petroleum education at Tanana Valley CC and Kenai CC. He added the Marine Technology program in Ketchikan. Senator Sackett stated that he was more interested in what Dr. Barton had meant by "emphasis".

Senator Eliason requested that Dr. Barton elaborate on UA intentions as far as fisheries go. Dr. Barton stated that they have tried to create the land grant model for fisheries of increased instructional support to turn out the kinds of people needed in the fisheries effort, technology transfer efforts that would be analogues to agricultural experiment stations, and marine advisory agents who would be analogues to the county agent. The basic management needs according to UA advisory groups stress the business management side just as much as they do the biological management of the fisheries resource. UA hopes to develop the basic fisheries management program in Juneau supported by the instructional programs already in place in Fairbanks. Supporting that would be a technology transfer center in Kodiak primarily concerned with applying new technologies to food processing and to fishing technology by the training of individuals and training as well as increasing the marine advisory group across the State. He stated that they want to do more in quality control and food processing. In summary he said that they were talking about a center in Anchorage for the economic, social and legal aspects of the fishery industry.

Senator Sturgulewski commented on the single appropriation level - down from the 25 or so appropriation levels used last year. She complimented the UA on its more recent accountability and accounting issue, but she felt the single appropriation approach was going a bit too far. Dr. Barton responded that this had been discussed with the Governor some months ago - not as a fiscal management concept - but more as a matter of changing the locus of decision-making on detail budgets. He did not want the committee to feel that their judgement was less than his, but he felt that covering the needs for the entire State of Alaska without allegiance to any particular region would ultimately be a superior method. It would offer the Legislature some "insulation" from lobbying. Many Legislatures in the nation have taken this single appropriation approach.

Senator Ferguson asked for the names and locations of UA Board of Regents members. Dr. Barton named them as follows:

Juneau	-	Mr. Abel Mr. Beadle Ms. Banfield
Anchorage	-	Mr. Kito Mr. Rasmuson Mr. Shively Mr. Lang
Fairbanks	-	Dr. Fate Mr. Cook Mr. Miklautsch Mr. Tim Burgess (student regent)
Kodiak	-	Ms. Hall

Senator Ferguson noted that this certainly was not a state-wide coverage. Dr. Barton pointed out that for example Regent Cook doesn't owe his re-nomination to what he does for Fairbanks, but rather his carrying out of the trust for the entire State. Senator Ferguson stated that this would be natural, but that it would also be natural to put most of one's emphasis in the town one is from. He suggested that the Board of Regents be statewide, and specifically represent certain districts. Dr. Barton stated that then the Board of Regents would be just as partisan as the Legislature. Senator Ferguson stated that was not the point - the point was that most of the Board is comprised of people from Anchorage and Fairbanks, and that is where the emphasis is, no matter who one is.

Senator Sturgulewski stated that in any case, she was not prepared this year to "go a single appropriation". She did feel, nevertheless, that the university has come a long way in financial responsibility. She also felt that the trend to cut down on the number of appropriation levels was appropriate, but possibly only to 10 to 15 levels rather than just one. She requested that Dr. Barton provide her with a list showing 10 - 12 appropriation levels.

Senator Ferguson asked if it wouldn't be better to have a group other than the UA Board of Regents controlling the community colleges. Dr. Barton stated that he did not feel the need in the State of Alaska could be "fractured up" into a whole series of constituencies. The community colleges, except for three, are primarily extension operations of the University; they are very small. The ability to deliver effective and appropriate instruction and service throughout the State depends upon the University involvement. The linkage the University has with the community colleges could be analogous to the extension agent/county agent kind of thing in the lower '48. It is the 21st Century analogue of what used to be a concentration on agriculture and is now a concentration on knowledge - and its that linkage that helps. He felt that the ability to respond would decrease were they to be fractured. Senator Ferguson asked Dr. Barton if he believed in local control. Dr. Barton responded that he believed very strongly in local control; the programs offered in a particular region ought to reflect precisely what is needed there. The strength of a land grant campus is strongly dependent on local control. Senator Ferguson stated that he did not believe this theory was being acted out. He said that he felt if there were local control in the Kotzebue school system for instance, they sure wouldn't put all the money in salaries. Dr. Barton stated that a university system must be "people intensive", so that in order to present quality education to an area, money must be invested in staff. Therefore, 70% is not an outrageous amount to commit to salaries.

Senator Sackett asked what the status was of the court case with the State of Alaska on University land. Dr. Barton stated that the attorneys are meeting with the AG to see what changes might be involved in the suits.

(BEGIN NEW TAPE, SFC 81, # 15, Side 1, 000 - 652)

Dr. Barton said that they did not go so far as to say that the State can't take University land at all, but they did stress the compensation aspect. There are some areas they still don't understand as the courts have not yet ruled on the general case.

Senator Eliason requested that, in respect to the fact that 70% of University appropriation goes to salaries, a salary schedule be provided to the Senate Finance Committee. Dr. Barton stated that it would be provided.

Co-chairman Bennett requested that Dr. Barton provide him with a brief synopsis of proposed research as well as on-going research in the fisheries. He asked that locations and missions be identified. Dr. Barton stated that such a synopsis would be provided.

Senator Sackett commented that after 9 years and millions of dollars, the present accounting system is pretty good. He added though, that it was unfortunate to have been in the situation to begin with. Dr. Barton stated that he felt the problem went back even further; he felt that there was no recognition of the fact that in order to run a university there is a need for working capital. He said that compounded with the mismanagement ultimately led to the crisis.

Co-chairman Bennett thanked Dr. Barton and requested that he direct members of his staff to testify before the committee. Dr. Barton stated that Chancellor Cutler from the University of Alaska at Fairbanks would speak next.

DR. HOWARD CUTLER, CHANCELLOR, UNIVERSITY OF ALASKA, FAIRBANKS

Dr. Cutler stepped forward and thanked the committee for the opportunity to inform them of the programs at UA Fairbanks. He stated that their three main areas are in basic instruction, research and capital support. He said that growth at UAF has been 7% compounded per year, and that increase in hours taught has been 8% compounded per year. He stated that UAF is the only university teaching native language in the world. He said the most pressing items in their budget request are for rural teaching development, petroleum studies, business management and more salary funds for their summer programs. He said that they are also experiencing an increase in the number of transfer students as well as an increase in the need to evaluate credentials so that students can be properly placed in the university structure. Since the biggest enrollment is in the freshman class; however, he said he would like to increase transfer enrollment in the upper division classes. Dr. Cutler proceeded to comment on the quality of instruction at the University of Alaska, Fairbanks. He stated that faculty "quality" has increased from 4 PHD's to 14 PHD's in the

accounting area. He said that they are not asking for "salads and deserts", but rather for "bread and butter".

Dr. Cutler stated that the gathering of information and the dissemination of that information is their basic mission in the research area. Areas of reasearch at UAF for which they are requesting funding this year concern problems relative to Alaska - coal conversion, seafood processing, interfacing between oceanography and fisheries, study of the sea and study of climatic conditions in terms of the cycle of fish development. Specific requests center around building up the equipment, and increasing staff and competition for funds available from the federal government.

Dr. Cutler then commented on requests in the Capital Budget area. He centered his comments around building facilities and equipment for the students on campus.

Dr. Cutler informed the committee on the budgetary procedure at UAF. He concluded by saying that the Fairbanks campus is the lowest in support within the university system. He added that he felt they had an "exciting" group of students to serve in an "exciting" environment within Alaska. He made himself available to answer any questions from the members.

Senator Sturgulewski referred to information earlier requested by Senator Sackett regarding to amount of capital that was not included, and on cuts in the Operating Budget. She asked Dr. Cutler if the \$7-8 million cut in Operating was partly for the summer program, or if he just felt that more of a priority should have been placed on the summer program. He stated that he was saying the latter. Senator Sturgulewski asked if there was a possibility of readjusting within the existing budget before the committee. Dr. Cutler commented on historical and internal changes in the summer program that warranted his request. Senator Sturgulewski requested that Dr. Cutler provide further information on the summer program, as well as methods for salary payment to faculty.

Further questioning and discussion ensued on such subjects as research at the university and whether or not it was duplication of what has already been done in other institutions. Senator Eliason was specifically concerned about research in the fisheries in the above regard, as well as how the information is disseminated to people in the fisheries.

Co-chairman Bennett stated that the committee would continue to hear from the chancellors the following morning at 8:30 a.m.

Senator Sturgulewski asked that chancellors be prepared to talk about telecommunications and how it fits into the university system, particularly in rural Alaska.

ADJOURNMENT

The meeting adjourned at 9:55 a.m.

(Tape SFC 81, Tape # 14, Side 2, 000 - end)
(Tape SFC 81, Tape # 15, Side 1, 000 - 652)

SENATE FINANCE COMMITTEE

March 17, 1981

8:40 a.m.

SFC-81, #15, Side 2 (000-end)

SFC-81, #16, Side 1 (000-222)

CALL TO ORDER

Co-chairman Bennett convened the meeting at approximately 8:40 a.m.

PRESENT

Present were Senators Bennett, Eliason, Sackett, and Sturgulewski. Senator Dankworth arrived later in the meeting. Also in attendance were Dr. Jay Barton, President of the University of Alaska; Dr. Howard Cutler, Chancellor of the University at Fairbanks; Dr. Edwin L. Biggerstaff, Campus President, Anchorage Community College; Dr. Patrick O'Rourke, Chancellor Community Colleges, Rural Education and Extension; Dr. Ashok Dningra; Bill Zybach, Director, Alaska Statewide Student Association; Dr. Theresa Nangle Obermeyer; administrative assistants to the Finance Committee, Judy Johnston and Kathy Martinson, and representatives from the press including Joe LaRocca.

BILL ASSIGNMENT

Co-chairman Bennett made the following bill assignments:

SB 69 - Ferguson
SB 120 - Bennett
SB 140 - Eliason
SB 141 - Eliason
SB 214 - Bennett
SB 263 - Dankworth

UNIVERSITY OF ALASKA - DR. CUTLER

Co-chairman Bennett asked that Dr. Cutler first appear before committee to respond to questions resulting from testimony given at a previous committee meeting.

Responding to a question from Co-chairman Bennett concerning teaching positions in petroleum engineering, Dr. Cutler stated that classes in this field are "going well." There are approximately 30 to 40 students in the class. The University expects to receive approval of a Bachelor of Science Degree in Petroleum Engineering from "the Board," and expects a Masters program to be forthcoming soon in the Anchorage area.

Responding to an additional question from Co-chairman Bennett concerning a controlled burn and loss of a building, Dr. Cutler stated that the building was old and its destruction long overdue. The University needs new buildings in this area and will be "bringing in a request for this in conjunction with growth in the area of agricultural research."

UNIVERSITY OF ALASKA - Bill Zybach

Mr. Zybach, Director of the Alaska Statewide Student Association, next appeared before committee, advising that the association represents local student government on campuses throughout the University system. The association concluded a two-day statewide conference March 1, resulting in a united position in unanimous support of the University budget as requested, with additional funding for libraries. Mr. Zybach stated that over the past four years, the student organization has consistently come to the legislature asking that specific items be included in the University budget. The era of students coming to the legislature may be approaching an end. The association has "done a good job of educating fellow students regarding University needs," and by developing such organization has made inroads within the University itself as far as the decision-making process is concerned. Most association success has occurred during the past year when the role of students within the University was expanded. If the above situation continues, the students feel their needs will be met by the University, and it will no longer be necessary to come to the legislature in order to be heard. The association objective is to get students involved in all areas of the University at both the local and statewide level. President Barton has greatly assisted student involvement at the statewide level. There has also been greater representation and response on the part of the Board of Regents. Because of the foregoing changes, the student association voted unanimously for full funding of the University budget. The association also advocates additional funding for University libraries.

(Senator Dankworth arrived at the meeting at this time, 8:50 a.m.)

UNIVERSITY OF ALASKA - Dr. O'Rourke

Dr. Patrick O'Rourke next appeared before committee, advising that he presides over 10 community colleges, 11 extension centers within the cooperative extension system, the Alaska Native language program, national bilingual center, and telecommunications.

The community college system is career designed, accommodating transfer students and offering the first and second year of a Bachelor program, vocational training, and community service courses. These offerings are not statewide but limited to geographic area.

Extension centers offer programs similar to community colleges but more program specific--smaller in scope. They also provide

upper division or graduate services as needed in cooperation with the University.

Cooperative extension programs function in combination with the University, state, and federal agencies to offer programs for people in particular areas. This service delivered programs to 162 different cities and villages across the state.

Dr. O'Rourke advised that he implemented a system of resource reallocation when constructing his budget. Resource reallocation is based on:

1. A belief that over a period of time "stuff" occurs in a budget which needs to be "weeded out."
2. Resources could be better distributed throughout the division.
3. A need to stimulate requests from units for new programs which are needed more than what is currently being offered.

A number of statewide programs such as the statewide associated nursing degree program (offering fall and spring semesters at local colleges and twelve weeks during the summer in Anchorage for a two year period) have been implemented through the statewide community college instructional component.

In an effort to deliver competent personnel to the industry, petroleum-related courses have been offered at Kenai, Tanana Valley, and the Alaska Skill Center.

Through the cooperative engineering program, courses may be offered in small areas where such learning might otherwise be unavailable. The community college system is also "looking into" statewide fisheries, air traffic control, coordinated services to the military.

Dr. O'Rourke advised that in his budget he attempted to stimulate vocational education throughout community college units, "boost" the cooperative extension system, and "bring small campuses up with increased faculty." The budget also reflects greater emphasis on part-time faculty. The media center at ACC also received budget emphasis since the center services the entire community college system as well rural education, UAA, and Alaska Pacific University.

Less glamorous needs include clerical support, registration clerks, rental space, etc.

A recent accreditation evaluation recommends:

1. Improved student services staffing at Ketchikan
2. Expanded faculty at Mat-Su, Prince William Sound, and Northwest.

3. Improved library/media service facilities at Northwest.

Dr. O'Rourke stated that since the capital budget was compiled in an off-year for G.O. bonds, new facilities fell to the lowest priority. Capital items in order of priority are:

1. Instructional and administrative equipment.

2. Life safety items.

3. Removal of handicapped barriers.

4. Facility repair.

5. Campus improvements

6. New facilities, including an extension facility at Galena and an administrative building in Anchorage.

Dr. O'Rourke stressed the need for University equipment, advising that \$100,000 is currently to be divided between 10 community colleges and 11 rural education centers. Funding so distributed will not go very far. He stressed the need to upgrade on a regular basis to remain current, adding that \$2.7 million could be utilized within the community college system. He mentioned specifically the need for \$500,000 for aviation equipment in Anchorage, and funding for two mobile vocational units. These would consist of semi tractor trailers with changeable internal components. One would function out of Sitka and could be put on the ferry to service rural areas. The other would service Tok, Delta--the interior region.

In addition, \$600,00 is requested for administration and records to provide a better record system for students.

In concluding his remarks, Dr. O'Rourke advised that the community college teachers' association (ACCFT) has agreed to extend the current contract for a year rather than renegotiate. This will require \$175,000 this year and \$900,000 next year.

UNIVERSITY OF ALASKA -- Dr. Biggerstaff

Dr. Biggerstaff identified himself as the president of Anchorage Community College and presented committee with a rundown of the planning and review process involved in preparation of University budgets. He advised that he had not before encountered the resource reallocation approach implemented by Dr. O'Rourke, but that the process "makes very good sense."

Dr. Biggerstaff advised that ACC provides high quality education for the first two years of a four-year program. It offers career training, and an evening schedule of community-oriented courses. Spring enrollment of 8,100 represents a 12% increase over last year. Eighty percent of the students are part-time, 50% are transfers, 40% are enrolled in occupational courses, and 10% are

enrolled in community-directed programs. The average age is 30 years, and the student population is 60% female and 40% male.

The college wishes to better penetrate the community and reach 10 to 12% of the people not presently reached. The budget request through the University to the board of regents to the Governor's office provided for a 12% increase; it was 8% when it left the Governor's office.

Dr. Biggerstaff stressed the need for capital projects such as completion of Phase I of the Aviation Complex and commencement of Phase II, the need for the applied science facility and specialized classrooms for educational programs and media services.

Dr. Biggerstaff concluded his remarks, advising that FY 80 at ACC ended with a balanced budget. Additional operating funds were used to remove debt service.

At this point Dr. O'Rourke advised that community college institutions are "open institutions." One need not have a high school diploma to attend. Throughout the system part-time attendance ranges from 22% to 92%, depending upon location of the college. These schools cater to people wishing to "pick up education on the side."

Dr. O'Rourke stressed the need for telecommunication implementation and computerized instruction which can deliver instruction to areas not before being served. "Telecommunication is like a road system in other states, it brings people closer together."

Responding to a question from Senator Bennett concerning community college labor relations, Dr. O'Rourke pointed to the fact the teachers' contract has been extended rather than renewed as an indication that relations have improved. The number of grievances filed is also less this year than last. Dr. O'Rourke advised, however, of tension between labor leadership and the administration.

Senator Dankworth asked Drs. O'Rourke and Biggerstaff if they could identify areas of needed vocational education not currently being met by community colleges. Dr. Biggerstaff advised that there is no doubt but what vocational education is on the "upswing." The market is there. Employers are looking for well-trained people in the areas of aviation, electrical work, automotive work. The nursing program is "moving to cover the state. The more programs which can cover the state the better."

Dr. O'Rourke stated that most often vocational needs are met in one way or another throughout the state. The question is, How close to home is the training. How far should the community college system extend training? Needed training is most likely available in one place or another throughout the state. Dr. O'Rourke advised, however, that what the community college system

is not doing well is training at lower levels such as retail sales, short-order cooking, etc. Senator Dankworth advised of his desire to "see" such training for "the little guy who does not want to become a great brain but wants to go beyond high school."

Responding to questions from Senator Sturgulewski concerning telecommunication operations, Dr. D'Rourke advised of a Memorandum of Agreement between the University and DOT for establishment and operation of a statewide audio and instructional T.V. network. The University also has a Memorandum of Agreement with the state Department of Education, relating to decision-making and program time.

Responding to questions from Senator Sturgulewski concerning the aviation maintenance program, Dr. Biggerstaff advised that the \$500,000 in equipment was not recommended by the Governor. He further spoke to the need for \$190,000 for costs and support of two maintenance teachers requested by the University but cut by the Governor. At this point the University has the facility but needs capital equipment and teachers. Senator Sturgulewski requested that a memorandum relating to the above situation be furnished committee members by University staff.

Responding to a question from Senator Sturgulewski concerning the relationship between ACC and UAA, Dr. Biggerstaff advised of problems which are normal when two institutions "split off." Some of the problems are "rooted in fantasy. There seems to be an inclination to hang onto ghosts of the past." Dr. Biggerstaff allowed that there are some problems with program articulation, joint-use facility problems, some confusion regarding fees, some course duplication which can be "rooted out." The basic problem is between the purpose of a community college and a university. The separation will take time in terms of promotion to the public. The past year has seen faculty interchange, scheduling improvements, and joint programs such as the Bartlett memorial lectures. The transition will require time and patience; it has only been a year and a half.

Co-chairman Bennett complimented University staff on the job which has been done, given Alaska's extensive geography and scattered population.

At this time Dr. Theresa Obermeyer addressed the committee as a public citizen, requesting that she be permitted to air a grievance against the University. She then proceeded to read a prepared statement which she distributed to committee members (copy attached to these minutes).

Upon conclusion of her statement, Co-chairman Bennett advised that, while he sympathized with her wish to publicly air her complaint, budget hearings before the Finance committee do not represent a proper forum for her grievance, since the grievance is not pertinent to the University budget. Co-chairman Dankworth agreed that the Finance Committee did not constitute a proper

forum for Dr. Obermeyer's complaint. He added that as a legislator he felt an obligation to see that she gets a fair hearing and is treated properly. He thus volunteered to take the complaint to the Attorney General's Office and report back to Co-chairman Bennett concerning the appropriate manner of handling the problem. Dr. Obermeyer expressed apprehension that, based on prior experience, she would not be accommodated by the A.G.'s office. Senator Sturgulewski stated that Senator Dankworth's offer of assistance represents a "good faith" effort on the part of the legislature since the committee is not in a position to hold hearings on the matter.

ADJOURNMENT

The meeting adjourned at approximately 9:50 a.m.

SFC-81, #15, Side 2, (000-end)
SFC-81, #16, Side 1, (000-222)

F O R I M M E D I A T E R E L E A S E

Finance Committee
University of Alaska Budget
Juneau, Alaska
March 17, 1981

I am Dr. Theresa Nangle Obermeyer. I do not want to take up much of your time today but I feel that after almost three years of my efforts to resolve the damage that has been done to my career and reputation that this time is important to our mutual efforts to work together toward improvement of public higher education in the State of Alaska.

I would very briefly like to summarize my appeals to be treated in a legal manner by the State of Alaska agencies and the Attorney General's Office.

I am an American citizen. I have a Ph.D. and thirteen years of experience in various parts of the United States in education. I have been an administrator at four institutions of higher learning before coming to the State of Alaska. I also am a judge's daughter and five members of my immediate family are attorneys. I feel that I have a firm grasp of legal matters but I find that every principle that I have revered in my life has been made a mockery by the University of Alaska.

I came to Anchorage Community College of the University of Alaska in 1978 to find that my subordinate, Jon Baker, admitted to me the first month of my employment that he had accepted at least one bribe for an Associates Degree. I acted in a responsible manner about this criminal admission by alerting the chain of command including Patrick O'Rourke immediately about what I had been told by Jon Baker who was responsible for all national testing at that time. Then, I was terminated and locked out of my office with no explanation. I to this date do not know what the reasons were for the illegal treatment I have received. I have never been afforded the most basic right I as an American citizen have under the Constitution of the United States; that of due process. I have found that the Attorney General's Office has shown gross negligence by doing nothing about the allegations I brought before the Criminal Division almost a year and a half ago.

Now, I am compelled to bring this matter before you not only for myself and my career but for the lives of many students who have no alternative but to attend the University of Alaska.

I feel that we must work together to make certain that children in the State of Alaska are able to learn the skills that they need and deserve in order to become productive citizens of our state.

The charges that I have been sending you correspondence about as Alaska State Legislators for a number of years have been attested to as truthful because of the inaction and deliberate negligence of those in authority. I feel very strongly that the attorneys in the Alaska Attorney General's Office as well as the Regents and the chain of command have intentionally implicated themselves in wrongdoing and criminal activity by doing absolutely nothing to investigate the details of this matter which has been pending for all of this time.

I know that each of you value a person's word. What would you think if the Chief Justice of the Alaska Supreme Court who is supposed to be the embodiment of truth and law reneged on his word to you? This is exactly what Chief Justice Rabinowitz did twice to me. My husband and I met with Judge Rabinowitz on May 21, 1980 at which time I was informed by Judge Rabinowitz that he would contact the Regents and arrange for my reinstatement. Nothing happened until I received a letter from the Chief Justice stating that he would bring this situation before the State Supreme Court for review. He went back on his word a second time as I was informed by Judge Rabinowitz on October 16, 1980 that he had not done what he had written to me he would do.

I would like to praise some of the good and well-meaning educators employed in the University of Alaska system who are at a loss to know how to work constructively to improve this unwieldy bureaucracy. I believe it is the system itself that creates the overwhelming problems that the University of Alaska now faces.

As I look around this room and see Mr. Rasmuson, the Regents, and administrators of the University of Alaska, I honestly and sincerely believe that if some of these men could know how destructive the University of Alaska is on young lives that they could not in conscience allow their names to be involved in this folly that is being labeled higher education.

In conclusion, I would like to respectfully ask you now what you might propose to me in resolution of this matter so that I may restore my career and reputation in order that I may work positively toward the improvement of higher education in the State of Alaska.

Page 2 of 2

3000 Dartmouth Drive
Anchorage, Alaska 99504
278-9759

SENATE FINANCE COMMITTEE

March 18, 1981

8:35 a.m.

(Tape SFC 81, # 17, Side 1, 000 - end)

(Tape SFC 81, # 17, Side 2, 000 - 237)

CALL TO ORDER

Co-chairman Bennett called the meeting to order at 8:35 a.m.

PRESENT

All members were present with the exception of Senators Sackett and Stimson. Senator Eliason arrived at 9:00 a.m., and Senator Sturgulewski arrived at 9:05 a.m. Also in attendance were Jay Hogan, Director of Legislative Finance; President J. Barton of the University of Alaska; other UA officials, Chancellor Harrison and Chancellor Paradise; Administrative Assistant to Senator Bennett, Judy Johnston; and a member of the press Joe LaRocca.

SENATE BILL NO. 17

Co-chairman Bennett stated that Senate Bill No. 17 (An Act amending the Executive Budget Act to provide for agency budgeting; and providing for an effective date) would be taken up at this time. He requested that Co-chairman Dankworth (to whom the bill had been assigned) present the bill to the committee.

COMMITTEE SUBSTITUTE FOR SENATE BILL NO. 17 (FINANCE)

Co-chairman Dankworth Stated that at the March 12, 1981 meeting it had been decided to hold the bill over so that members could peruse the proposed amendments. These amendments were subsequently incorporated into a Senate Finance Committee Substitute, and it was established that the committee was presently considering COMMITTEE SUBSTITUTE FOR SENATE BILL NO. 17 (Finance) (An Act relating to the Executive Budget Act; and to state agency programs; and providing for an effective date). Co-chairman Dankworth stated that one of the amendments would set time limits for the Governor to submit supplemental appropriations by the 45th day, and budget amendments no later than the 75th day. The second amendment had to do with sunset provisions under the proposed agency budgeting. He then requested that Jay Hogan, Director of Legislative Finance explain both amendments.

Mr. Hogan stated that the clean-up amendment would change the existing law that sets out the sunset audit schedule for agency programs (AS 44.66.020). In regard to this amendment, he pointed to a letter in the file from Merle Jensen, Legislative Auditor. At present, Legislative Audit has a statutorily prescribed schedule for completing certain sunset audits, and that schedule

is written in the language of programs. An amendment changing program names to agency names would be appropriate if the budgeting law is changed; that is simply what the amendment would do.

Co-chairman Dankworth moved and asked unanimous consent that the above amendment (already included in the Senate Finance Committee Substitute) be adopted. There being no objection, it was so ordered.

Mr. Hogan stated that the second amendment would in effect replace what is now Section 6 of the original bill. The existing Section 6 would be entirely deleted. The new language would limit the time for submission (or review) of supplemental appropriations submitted by the Governor, and budget amendments submitted by the Governor. As an example, Mr. Hogan stated that in this week's listing of supplemental appropriations, the Governor's supplementals are before the Legislature. If it were the Legislature's desire to turn supplemental appropriations down, obviously if they come in this late in the session, the Legislature is somewhat more restricted in dealing with them because there is less time left in the fiscal year to appropriately turn a supplemental down. He stated that this was not a new problem for the Legislature, but rather, it has been a problem over the years. This amendment would provide that the first 45 days of the Legislative session be reserved for delivery of supplemental appropriation requests.

Co-chairman Dankworth asked that Mr. Hogan explain the avenue the Governor could take in the case of an emergency. Mr. Hogan stated that the amendment would really instruct the Legislature not to pay attention to Governor's messages submitted after these dates. Nowhere is there reference to restriction on the Legislature. Individual legislators are free to be persuaded by the Governor to introduce a bill that would accomplish the same thing. It really restricts the formal submission of Governor's documents; it in no way restricts the ability of the Legislature to decide they wish to add something to the budget or to decide they wish to introduce a bill that is effectively a supplemental appropriation.

Co-chairman Dankworth moved and asked unanimous consent that the amendment (also already incorporated in the Senate Finance Committee Substitute) be adopted. There being no objection, it was so ordered.

Senator Ferguson moved and asked unanimous consent that COMMITTEE SUBSTITUTE FOR SENATE BILL NO. 17 (Finance) be moved from committee with individual recommendations. There being no objection, it was so ordered and the committee report was signed as follows: Co-chairman Dankworth and Bennett and Senator Ferguson signed "do pass", and Senators Eliason and Sturgulewski signed "no recommendation".

CONTINUATION OF UNIVERSITY OF ALASKA BUDGET OVERVIEW

DR. FRANK HARRISON, CHANCELLOR, UNIVERSITY OF ALASKA, ANCHORAGE

Dr. Harrison stated that the University of Alaska at Anchorage has only been in existence for four years, and was created by a division of the former Southcentral region of the Senior College in Anchorage and Anchorage Community College. He stated that the mission is appropriate to a 4-year institution situated in the largest population center of the State. Concentration is primarily on the health sciences, social sciences, business and public administration, and engineering. He said that the faculty was young, aggressive and spirited. The student population is growing rapidly; over the past five years on a fall-to-fall annual increase, credit hours have gone up 16%. At the end of the past fall semester there were 3,800 students. He stated that he was pleased to say that the increase in the number of full-time students at UAA has been significant - 30% last fall. This indicates a growing acceptance of UAA being the premiere public institution in southcentral Alaska. He was also pleased to say that the students take part in various activities including the governing structure at UAA.

Dr. Harrison stated the following as being the goals at UAA (along with the goals of the statewide system:

1. academic excellence
2. accountability
3. balance - with growth at UAA that combines academic and non-academic areas to effect mutual development of athletics and academics to develop a solid root structure for the institution in the years ahead.

Dr. Harrison moved on to the FY 82 budget request for UAA. He stated that they were principally concerned with developing the campus, the buildings, laboratory space, and classroom space. Their top request in the Capital Budget for FY 82, apart from some instructional equipment, was for a classroom building for \$13.8 million. This would carry the classroom space problem through the 1980's. In the Operating Budget, in keeping with the institutional goal of a balanced growth between academics and administration, the Board of Regents has approved 31 line items representing \$1.6 million of new money. These line items are divided mainly between instruction and some essential kinds of positions in administration. Dr. Harrison stated that the budget increase, apart from the continuation level, which represents the increased cost of doing business, is 10% FY 82 over FY 81. He wished to stress the importance of the new building for the campus, as well as the growth and development of UAA since it is only about 4 years old.

Senator Ferguson asked if this budget overview wasn't conservative compared to the statements Dr. Harrison had made to the Chamber of Commerce recently. Dr. Harrison replied that the \$100 million he had mentioned at that time was related to a

funding forecast made for development of the University of Alaska, Anchorage over the next 6 years. Senator Ferguson asked if they were "in line" with the present budget to meet that need. Dr. Harrison replied that the \$13.8 million classroom mentioned earlier during this meeting would put them in line. Their plan, approved by the Board of Regents, indicates that between now and 1989 they need to put about one building or a major parking structure on line every year if the plan is to be achieved by 1990. Senator Ferguson asked if they would have objection if the process were speeded up, to which Dr. Harrison replied, "we certainly would not".

Co-chairman Dankworth asked about the relationship between ACC and UAA. Dr. Harrison responded that he was "strongly in accord" with Dr. Biggerstaff's comments made a few days previous. He added that he felt the two institutions had made remarkable progress in relating to one another, given the differences in missions, though there are problems from time to time. He stated that there are quite enough students and need for both institutions in southcentral Alaska.

Co-chairman Dankworth stated that the infra-structure in education in Alaska should be viewed along with the infra-structure in Alaska in energy development, dams, hydroelectricity, etc. He added that he wanted the University to really stand for something. Dr. Harrison stated that he felt it did stand for something, for example, the research institute has an international reputation. Further comments were made about the image of the university. Co-chairman Dankworth stated that he would like to guard against making the university a "welfare department for intellectuals", and against accepting unnecessary studies.

Senator Ferguson stated that his question would be directed to Dr. Barton. He stated Alaska needs research into the following:

1. Acoustics for protection of arctic marine species
2. Frostbite
3. Impact of pack ice on man-made islands
4. Molecule break-up of hydro-carbons in arctic waters

He asked what UA policy was as far as the Arctic Research Lab in Barrow.

DR. J. BARTON, PRESIDENT, UNIVERSITY OF ALASKA

Dr. Barton stated that the Arctic Research Program at the University has been involved, and continues to be, especially in the Outer Continental Shelf studies. He stated that over the past few years, the problems Senator Ferguson mentioned above have been addressed - ice physics, pollution, oil spill emergency measures, etc. He said that Arctic Lab in Barrow has been used much, much less in the past five years than ever before. The Navy has pulled out its research and the role of that Laboratory as a base for university studies (UA, other universities and

other institutions) has gone downhill. He said that the University has been very much concerned with arctic research policy and stresses the need for continuing work on precisely those areas. The long term future of the Naval Arctic Lab as a research base was, he felt, probably fairly small, but the long term future for arctic research he thought was very good. Research would be based in a number of locations across the State.

Senator Ferguson commented that the Navy research was cut back not because of a declining need for research, but because of the fiscal restraints placed on it by the federal government. He felt that every effort should be made to save whatever facilities are there so that some service can be provided in that area. Dr. Barton responded that there was a "very strong interest and dedication" in Washington and in Alaska to maintain Arctic research - to look at just problems of the North Slope and western coasts of Alaska. He said that he had found that there isn't an agency in Washington that is willing to "pick up the pieces"; the basic reason is that the costs of simply maintaining the laboratory, aside from carrying out any research, are very high. The Navy has been spending \$9 -11 million per year "just to keep the doors open". If UA streamlines the facility, the maintenance costs could drop to one half; however, Dr. Barton felt that the money could more effectively be applied to research projects temporarily located in Prudhoe Bay, Barrow, Kotzebue, Nome, Fairbanks and Anchorage.

Senator Ferguson asked if a study has been conducted to evaluate the premises. Dr. Barton stated that there has been on on-going evaluation partly by university people and partly by federal people. A two-year study has been mandated for the Department of the Interior to determine the long-term future of the land, its resources and the facilities themselves. The UA will participate in that.

Senator Sturgulewski asked if evaluations had been made for the \$7 million cuts in the UA Operating Budget. Dr. Barton stated that incremental impacts would be provided to her within the day.

Further discussion ensued on off-campus student housing and/or private student housing. Co-chairman Bennett requested that Chancellor Paradise of the University of Alaska, Juneau come forward with his budget overview.

DR. PARADISE, CHANCELLOR, UNIVERSITY OF ALASKA, JUNEAU

Dr. Paradise provided a history of the University of Alaska, Juneau. He said that UAJ has grown 287% since 1973. This year growth will cost 10%. Student body is over 12% minority, 62% women, 46% are married, 35% are 30 years old or older, almost 10% are over 40. He noted that all university institutions in Alaska assist to alleviate the high unemployment rate in Alaska. Dr. Paradise proceeded to emphasize the following programs at UAJ:

1. The jail program
2. The vocational teacher education program
3. The outreach education program in Southeast Alaska
4. The fisheries program

Dr. Paradise stated that the UAJ budget presented to the Board of Regents and the Administration was an extensive one. He stated that he thought their requests had been too severely cut.

BEGIN NEW SIDE, Tape SFC, # 17, Side 2, 000 - 237

In regard to their capital portion of the budget, Dr. Paradise stated that earlier Senator Sackett had stated a need for some kind of plan for vocational and technical education. He said that the Governor had not recommended one single item in the Capital Budget for major construction projects, and yet 2/3 of the capital construction budget was strictly related to vocational/technical education. He said that the site between Harris and Aurora boat harbors belonged to the University, and that they had plans for some time to develop that into a technical/vocational center as this area was so much in need of such a facility, but the Governor did not recommend the funding for the building.

Dr. Paradise continued to describe budgetary needs in areas such as fisheries ecology, and how these requests related to Southeast Alaska. He also stated the need to coordinate more closely with other Southeast community colleges.

Senator Dankworth asked for the total enrollment at UAJ. Dr. Paradise stated that last semester over 8,000 students were served. Of that number, about 5,000 students were in special courses, most of those being non-credit classes. There were 712 full-time equivalent students last semester. He qualified that this is a significant number of students considering limited facilities at UAJ as well as the fact that these students come from a small population.

Co-chairman Bennett asked for further questions; there being none, he thanked Dr. Paradise for his testimony. Dr. Barton stated that the UA budget overview presentation was completed.

Co-chairman Bennett made a comment he thought would have an impact on the various chancellors. He stated that several times during the presentation he had heard that UA would be more interested in bonding aspects next year. He stated that he thought the UA should take a close look at what interest rates are for bonds right now. The interest rate for bonds is 15% and 16%, where the permanent fund and other State investments are getting from 11% to 12%. He did not feel that it would make a lot of sense to go the bonding route, and just wanted to throw that out for consideration by the UA staff and the Board of Regents. Dr. Barton stated that he thought they all shared that perception, but that they are also cautious not to presume on the legislature's prerogatives as to how these things get funded. He

added that the tradition has bond issues every alternate year; however, he was in "precise agreement" with Co-chairman Bennett.

Co-chairman Bennett stated that the committee would meet the following morning at 8:30 a.m.

ADJOURNMENT

The meeting adjourned at 9:40 a.m.

(Tape SFC 81, # 17, Side 1, 000 - end)

(Tape SFC 81, # 17, Side 2, 000 - 237)

SENATE FINANCE COMMITTEE

March 19, 1981

8:40 a.m.

SFC-81, #17, Side 2 (237-end)

SFC-81, #18, Side 1 (000-075)

CALL TO ORDER

Co-chairman Bennett convened the meeting at approximately 8:40 a.m.

PRESENT

Senators Bennett, Dankworth, Eliason and Sturgulewski were present when the meeting convened. Senator Ferguson arrived later in the meeting. Senators Sackett and Stimson did not attend. Also in attendance were Dr. Sherman Carter, Executive Vice President, University of Alaska; Ashok Dhingra; Representatives from Matthews and Wright of New York; Fiscal Analyst Alison Elgee; and administrative assistant to the finance committee, Judy Johnston.

BILL ASSIGNMENTS

Co-chairman Bennett made the following bill assignments:

SB 37 - Stimson
SB 178 - Sackett
SB 222 - Sackett
HB 140 - Bennett

MR. BENOIT - MATTHEWS AND WRIGHT

Co-chairman Bennett informed committee members of the presence of visiting financial experts from the Wall Street investment firm of Matthews and Wright, advising that he had asked that they speak to committee regarding interest rates and the national economy.

Mr. George Benoit appeared before committee, advising that Matthews and Wright is a nationwide investment banking firm specializing in municipal finance. Representatives from the firm are visiting Alaska (Cordeva, Yakutat, Anchorage, Juneau, and Ketchikan).

Mr. Benoit stated that when he started in the investment business, tax exempt interest rates in the short end were at 1-1/2%. The prime rate was between 4 and 5%, and by law long-term treasuries couldn't be sold any higher than 4-1/4%. With that, we went into a series of monetary and economic crises starting in 1966 and ending up with a phenomenon called "magic 5's." The government promised after that to stem the tide of inflation. That lasted until 1967-70 when we went into another era where

interest rates were up around 8%. In the early 1970's we ended up with wage and price controls. That lasted for another three or four years, and we ended up with another crisis in 1974-75. Again we had a period where a little of the pressure was off, and we ended up in the next era (the one we're now in) the 1979-80-81 period. There is a phenomenon there and perhaps a lesson to be learned in that in August of 1979 Mr. Volker took over the Fed. If you have read any of his speeches, his speeches said that if you continue to spend money in Congress, I only know one thing I can do to offset it, and that is to raise interest rates and squeeze inflationary expectations.

On October 6, 1979, he caused a dramatic rise in interest rates. We ended up with a totally destabilized financial capital market. The prime rate went up to 20%. We had a brief respite from March to June last year where government officials were afraid that the bond markets would collapse; we'd have financial panic. They put in credit controls and other devices to force interest rates down. We continued to inflate the economy by having a larger and larger deficit. We are now at the point where interest rates have risen again to the 21-1/2% level, and interest rates are now falling for the first time since last June--falling in a rapid and definable pattern.

Mr. Volker has said that he doesn't want interest rates to fall until the economy weakens. Every time they tried to fall, he pushed them back up again. In the last month and a half he has not attempted to push interest rates higher. He has let them go lower. He has served notice on everyone that if they get too low, he will artificially push them up again.

We are right now at a point where we are running and will continue to run a sizable federal deficit. Mr. Volker has made it clear and the people in the administration have supported him, that interest rates will remain at a relatively high level until we see some basic changes in the economy. We have seen interest rates come down (and I'm not talking about the prime rate, because the prime rate now is a follower not a leader). Short term interest rates have been as high as 18-19% in real terms and are hovering somewhere in the 12-1/2 to 13-1/2 range. The prime rate is sure to follow; it should move down at least another 2% to get in line with everything else. I think we'll see in the near term the fed act again to stop the decline of interest rates until the congressional outcome is known--whether we are going to get the spending cuts the administration has proposed.

If we do not get the spending cuts, there is no doubt in my mind that the chairman of the fed will attempt to push interest rates higher--sharply higher--and may do so as a warning to Congress. I would anticipate that interest rates are going to remain relatively high, that you will continue to see destabilized markets with wide swings. We have a swing in the marketplace now where in one day we get more market move than we used to get in a year or a year and a half. The financial markets have learned to cope with that; it really isn't the upsetting thing it was about

a year and a half ago. There is no doubt in my mind that interest rates are in a relatively high pattern. A chart of recent rates looks like stepping stones. Each time we get up to a higher plateau. We are on a plateau now, and I wouldn't look for interest rates to go a lot lower than they are now. Short term interest rates will probably stay in the plus 10% range. Long term interest rates will probably be up above that for quite some time. The era of cheap money is over as far as interest rates go. The state should factor that into its plans.

Mr. Benoit advised that he understands the state is currently considering spending money and deciding what to do with surpluses. Alaska has a unique opportunity to borrow money in the bond markets at (using fictitious rates) tax exempt rates of 10% and take state surpluses and reinvest them at 13-14-15-16-17%. It gives the state a unique opportunity to issue self-supporting debt, reinvest surpluses at higher rates, and come out with "your money--more money--at the end. You will not have spent your surpluses, and you will have initiated self-supporting programs that will in the long run not be costing Alaska any money."

Senator Sturgulewski stated that many of the bills being considered by the legislature, the payoff on bonds, defeasance, property tax relief, etc. are exactly contra to the advice given by Mr. Benoit when he suggests leveraging. She stated that she believed there to be a great deal of merit in Mr. Benoit's suggestions, but the legislature is "getting a lot of pressure to do just the other--pay cash today, don't worry about the fact that you might need to bond tomorrow, and be able to establish yourself in the bond market." She advised that she appreciated Mr. Benoit's comments.

Mr. Benoit stated that the bond markets have a "long memory." If you do not act responsibly, and you end up acting irresponsibly, they remember for a long time.

Senator Sturgulewski inquired concerning market reaction if the state were to pay off as many bonds as possible (How would the market look at Alaska in the long term?). Mr. Benoit guessed that thinking people would say "I don't really know what they have in mind. It seems to me that this is a way that we under the same circumstances would not go." He added that he believes the market would wonder and be puzzled by the state's actions. One learns in the capital market that when one has a 5-1/4% mortgage, you don't pay those off because you can take that same dollar and reinvest it at 10-12-14%. The state is in the same position.

Responding to questions from Senator Dankworth concerning the interest rate in the bond market, Mr. Benoit responded that interest rates have changed dramatically in the last week alone. Short-term treasuries that were selling at 14-1/2 ten days ago are now trading at 12-3/4.

Senator Dankworth raised questions concerning the bond market attitude toward Alaska if the state pays off its bonds and does not buy additional bonds but instead uses its surplus, would this action be viewed as irresponsible? Mr. Benoit responded "No, I don't think it would be viewed as irresponsible; it would be viewed as strange." Senator Dankworth responded, "Well, it is a strange situation, Sir, there is no state in the union that's got this strange situation here where we've got billions to spend in a short period of time. Is it irresponsible to not resolve some of these financial problems we've got when in a short term here we're going to get an awful lot of money. I've been told by bond council that if we don't buy bonds we're going to be seen as irresponsible and I guess you're confirming that." Mr. Benoit responded that he believes the state can issue debt responsibly, use its surpluses in other ways, and in the long run come out ahead.

Senator Dankworth attested to pressures upon legislators concerning use of state money--pressure to see that such money remains within the state. Pressure from the public which owns the money is at odds with advice given by financial experts. Mr. Benoit advised that he didn't have all the answers and didn't pretend to. One thing the state might consider is taking moneys the state has now and investing it in Alaska, so that Alaska twenty years from now is a better place to live, and has a stronger economy. This can be done through investment in "productive facilities"--not "government facilities."

Senator Eliason asked if the economy will ever "get back in the real world of low interest rates." Mr. Benoit responded that they are "a thing of the past." Low interest on a taxable basis will be around 10%. "Running \$50 billion deficits at a crack" is not going to help the inflation rate. It is just not possible to go back to 5 or 6% interest rates.

Concerning the national economy and financing for large corporations, Mr. Benoit stated that 20 years ago the federal government and long-term debt was probably somewhere between 15% of the market. The federal government is now about 50% of the market. The federal government has squeezed out the small and marginal borrower, and by the need to borrow has forced interest rates to high levels. Thus, the government in its sacrocant way has said to everybody, "you should cut down," but they're the ones who have forced interest rates to a level because they have squeezed other people out of the market, and there is only a finite number of dollars. Those dollars react to market pressures. If there is more demand for money, the price goes up.

Mr. Benoit concluded his remarks at this time and left the meeting.

The committee next directed its attention to the University of Alaska in order to continue budget review, and Drs. Sherman Carter and Ashok Dhingra appeared to testify.

UNIVERSITY OF ALASKA -- DR. CARTER, DR. DHINGRA

Dr. Dhingra advised that the University request totals \$127.2 million while the Governor's recommendation is \$121.1 million. He delivered to committee members a handout highlighting the University request, the percentage increase over last year, the Governor's recommendation, and the percentage increase of the Governor's recommendation (copy attached).

(Senator Ferguson arrived at this time, 9:10 a.m.)

Distributed with the handout was a priority listing of University capital projects (copy attached), totaling \$78.2 million. The Governor allowed \$5.5 million. The major item of priority concern is \$5.5 million for instructional equipment for which the Governor allowed \$500,000.

Dr. Carter mentioned that one item not shown in the short form is a prioritization of the operating budget. By the 25th of this month the University intends to have a prioritized listing of both operating and capital items for committee review. The University budget includes approximately 1/3 of what the individual chancellors requested. The priority listing should facilitate budgeting in the event a cut-off line has to be drawn.

Referring to the handout setting forth University and the Governor's figures and percentages of increase for each, Senator Ferguson requested that a "run" be made at an across-the-board increase of 10% over FY 81.

Dr. Dhingra stated that the Governor's budget represents a 12% increase over the prior budget--9% for inflation and 2.2% for growth to meet increasing demand. Senator Ferguson advised that the only thing he is willing to do at this time is vote on a 10% increase. Senator Dankworth advised of his interest in seeing University figures at 10%, adding that the committee is "looking at all budgets, not just the University."

Dr. Carter stated that the above requested figures would be furnished with prioritized operation and capital programs on March 26.

Co-chairman Bennett specifically requested that he be provided information on costs involved in reinstating the welding class at Tanana Valley Community College (the college is currently below 10% funding at 8.5%). He stated that competent welders will be needed for construction of the gas pipeline.

Responding to a question from Senator Ferguson concerning the separate budgeting of Chuckchi Community College, Dr. Dhingra advised that it was so budgeted because it was not budgeted last year. Senator Ferguson advised the University to continue to show Chuckchi in its budget even though he intends to transfer it over to the Department of Education.

Senator Sturgulewski commented on the need to take a look at a number of University budget categories, adding that "right now it's a single appropriation."

ADJOURNMENT

The meeting adjourned at approximately 9:25 a.m.

SFC-81, #17, Side 2 (237-end)

SFC-81, #18, Side 1 (000-075)

**FY 82 BUDGET REQUEST
BUDGET REQUEST UNIT SUMMARY**

General Fund and
General Fund Match Only

University of Alaska
Operating Budget

	<u>FY 81 Auth.</u>	<u>FY 82 Contin.</u>	<u>FY 82 Increments</u>	<u>FY 82 Total Request</u>	<u>% Increase FY 82 over FY 81</u>	<u>Governor's Recommendation</u>	<u>% Increase Gov. Rec. over FY 81</u>
Regents & Statewide Administration	\$ 8833.2	\$ 9603.3	\$ 679.5	\$ 10282.8	16.4%	\$ 9945.8	12.6%
Organized Research	11349.7	12642.2	906.6	13548.8	19.4	12835.7	13.1
UA/Fairbanks	33597.8	36653.6	2459.9	39113.5	16.4	36983.6	10.1
UA/Anchorage	15050.1	16826.5	1597.8	18424.3	22.4	17534.6	16.5
UA/Juneau	5697.9	6249.6	762.9	7012.5	23.1	6547.3	14.9
Comm. Coll, Rural Ed. & Extension	32764.4	35694.7	3107.5	38802.2	18.4	36612.4	11.7
CC-Statewide	2257.5	2448.0	584.2	3032.2	34.3	2607.6	15.5
Anchorage Community College	12679.2	13594.6	801.3	14395.9	13.5	13839.6	9.2
Kenai Peninsula Community College	1886.6	2033.9	196.3	2230.2	18.2	2056.8	9.0
Ketchikan Community College	1069.0	1199.1	139.3	1338.4	25.2	1250.5	17.0
Kodiak Community College	1169.7	1338.5	63.2	1401.7	19.8	1379.8	18.0
Kuskokwim Community College	2836.9	2765.2	--	2765.2	(2.5)	2765.2	(2.5)
Mat-Su Community College	923.8	1032.1	198.2	1230.3	33.2	1161.2	25.7
Northwest Community College	873.4	1106.0	187.2	1293.2	48.1	1106.0	26.6
Prince William Sound Community College	436.8	567.1	231.1	798.0	82.7	676.9	55.0
Sitka Community College	717.6	812.3	59.5	871.8	21.5	812.3	13.2
Tanana Valley Community College	3137.0	3382.8	201.3	3584.1	14.2	3407.6	8.6
Rural Education	2068.7	2364.1	174.1	2538.2	22.7	2407.9	16.4
Cooperative Extension Service	2708.2	3051.0	271.8	3322.8	22.7	3141.0	16.0
TOTAL UNIVERSITY OF ALASKA	<u>107293.1</u>	<u>117669.9</u>	<u>9514.2</u>	<u>127184.1</u>	<u>18.5</u>	<u>120459.4</u>	<u>12.3</u>
Chukchi Community College	4.6	5.1	666.3	671.4	--	671.4	--
Total						<u>121130.8</u>	

3/19/81

PRESIDENT'S CAPITAL PROJECT PRIORITY LIST

FY 82

		<u>Location</u>	<u>Amount</u>	<u>Gov. Recomm.</u>
1.	Handicapped Barrier Removal	Statewide	\$2,724.4	500.0
2.	Fire Pumper - UAF	Fairbanks	120.0	120.0
3.	Physical Plant/Water Treatment	Fairbanks	650.0	650.0
4.	Seward Pier/Roof Repair - UAF	Seward	564.0	564.0
5.	Complete HOF Spine - UAA	Anchorage	280.0	280.0
* 6.	Instructional Equipment - CCREE	Statewide	2,783.0	*500.0
* 7.	Instructional Equipment - UAF	Fairbanks	1,418.2	
8.	Working Capital Fund	Statewide	2,500.0	2500.0
9.	Statewide Admin. Equipment/Computer	Statewide	518.1	
10.	On-Line Student Records System	Statewide	600.0	
11.	Land Acquisitions - UAJ	Juneau	400.0	
* 12.	Equipment - UAJ	Juneau	470.0	
13.	Coal Handling Facility & Hose Dry Tower	Fairbanks	965.0	65.0
14.	Building Repair/Renovation	Statewide	4,465.6	300.0
15.	Statewide Administration Building	Statewide	9,780.0	
16.	Core Marine Building - UAJ	Juneau	5,395.0	
17.	Elvey Building Addition	Fairbanks	17,660.0	
* 18.	Instructional Equipment - UAA	Anchorage	825.6	
19.	Research Equipment - UAF	Fairbanks	1,865.5	
20.	Mobile Classrooms CCREE	Sitka & Rural Ed.	312.2	
21.	Marine Training Vessel - CCREE	Valdez	84.7	
22.	Saltwater System II	Juneau	200.0	
23.	Administration Equipment - CCREE	Statewide	178.1	
24.	Equipment - UAA	Anchorage	210.8	
25.	Roads, Streets, Parking	Statewide	3,404.0	
26.	Office Building - CCREE	Anchorage	4,300.0	
27.	Galena Classroom Building - CCREE	Galena	1,430.0	
28.	Classroom Building - UAA	Anchorage	13,800.0	
29.	Electrical Feeder Upgrade	Fairbanks	200.0	
30.	Admin. Computerized Regist.	Fairbanks	81.0	

TOTAL \$78,185.2 \$5479.

* { Gov. recommendation of \$500.0
Includes funding for instructional equipment for UA system
requested under priority # 6, 7, 12 & 18 in an amount \$5496.8

10/28/80

3/19/81