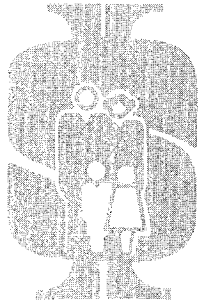


ACTION PAPER

RESOURCE
REVENUES
AND
STATE SPENDING
**ALASKA'S
GOLDEN
OPPORTUNITY**



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**RESOURCE REVENUES
AND
STATE SPENDING**

A REPORT BY
COMMONWEALTH NORTH

Prepared by the Resource Income Committee

December 1980

ALASKA'S GOLDEN OPPORTUNITY

A Commonwealth North Report

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Anchorage, AK 99501

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THE COMMONWEALTH NORTH RESOURCE INCOME COMMITTEE

On October 16, 1979, the Board of Directors of Commonwealth North established the Resource Income Committee to study how best to husband and use the state's projected revenues. Bill Sheffield, President of Sheffield Hotels, was named chairman of a team of fifteen including two former Commissioners of Revenue, two former state legislators and the ex-Director of the Office of Management and Budget of the Anchorage Municipality.

For many months the committee met weekly, heard from key legislators, members of the state administration and representatives of the private sector.

In February 1980, five of the committee testified on the Permanent Fund legislation before the legislature. In March, nearly all of the committee travelled to Juneau to meet with members of both the Senate and House Finance Committees.

In April, as the legislature was finalizing its income tax repeal bill, telegrams were sent to the Governor and every legislator calling for outright tax repeal.

After studying the laws passed by the 1980 legislature as well as the state budget for Fiscal Year 1981, the committee spent weeks hammering out the recommendations included in this report.

Those interviewed by the committee included Governor Jay Hammond, Revenue Commissioner Tom Williams, Senate Finance Chairman John Sackett, Senators George Hohman, Bob Mulcahy, Bill Sumner and Ed Dankworth; House Finance Chairman Russ Meekins, and Representatives Oral Freeman, Ernie Haugen and Hugh Malone; Chairman of the Trustees of the Permanent Fund Elmer Rasmuson and Dean Olsen, trustee of the Alaska Renewable Resources Corporation.

This "Action Paper" includes an examination of a wide range of issues. The result is an analysis of the best ways to invest Alaska's resource revenues for the long-term benefit of the state.

The members of the committee are as follows:

William Sheffield, Chairman
Sheffield Hotels

Robert E. Baer
Totem Realty, Inc.

Bertram B. Beneville
Merrill Lynch Pierce
Fenner & Smith

Edith Bullock
Retired Businesswoman
Former Legislator

David Chatfield
Alaska USA Federal
Credit Union

Harry Donahue
Independent Consultant
Former Director Office of
Management and Budget
Municipality of Anchorage

David Heatwole
Anaconda Copper Company

Max Hodel
Alaska Sales and Service

John Mlakar
Denali Fuel Company

Ron L. Rettig
Alaska Mutual Savings Bank
Former State Senator and
Alaska Commissioner of
Revenue

William Scott
Peat Marwick Mitchell

Judge James Singleton
Appellate Court, State of
Alaska

Paul Wilcox
Paul S. Wilcox Law Firm
Former IBEW Legal Counsel

Renee Murray
Scott Wetzel Services, Inc.

Eric Wohlforth
Wohlforth & Flint
Former Alaska Commissioner
of Revenue

FOREWORD

TRANSCENDING A COLONIAL ECONOMY

Historically, Alaska has always been capital short. Poverty in rural areas sometimes is more bitter than in the villages of India. Sewer, water, electricity and transportation systems are frequently either non-existent or primitive. Our cost of living is the highest in the nation.

Ironically, the most northern state in the union has more in common with the "southern" undeveloped nations of the Third World than it does with the contiguous 48 states. Like the developing nations, Alaska's economy is essentially colonial, characterized by a dual dependence on government expenditure and the export of resources largely in their natural state.

We recommend therefore that our resource revenues be used primarily in a coordinated effort to transcend our colonial economy and hasten the day when Alaska can join its more fortunate sister states in the benefits which a broad-based market economy brings.

To realize this goal, a basic infrastructure must be built. Now, for the first time, with Alaska's resource income, this economic backbone can be put in place. The components should include hydro power projects, a transportation system to reach our people and our natural resources, and ports and harbors to better respond to the opportunities available through international trade and Alaska's resource rich coastal shelf.

While each of the individual recommendations which follow can be defended on its own, they should not be viewed in isolation. Rather they should be seen as component parts of a program of progressive development to a mature and integrated private economy.

CONCLUSIONS

The following points summarize the conclusions of this study:

1. Alaska must free itself from its traditional "colonial economy", an economy characterized by its dependence on the federal government and the export of unprocessed natural resources.
2. Resource revenues must be used skillfully to enhance an integrated market economy sustained by private investment, a healthy local industry and worldwide commerce.
3. To avert a false sense of unlimited wealth, the state should immediately develop and publicize a series of projections illustrating anticipated growth in both state revenues and expenditures.
4. A five- to six-year Capital Improvement Plan, updated on an annual basis, is an urgent priority. This plan will contribute to a more coherent use of state revenues and assist legislative judgement as to annual contributions to the Permanent Fund.
5. In order to strengthen Alaska's private sector, tax burdens must be reduced.
6. Further tax reductions will not only help individual Alaskans but should reduce the size of the bureaucracy and the cost of government.

7. Alaska corporations should be exempted from income taxes on the first \$250,000 of taxable income. This action will help over 90 percent of Alaska's businesses.
8. Municipal taxes, such as sales taxes and real property taxes, should be replaced with state revenue but only if such action is coupled with a lid on local government spending.
9. Corporate income tax and business property tax relief will help the consumer. This action will result in better services, stabilized prices, more employment, and improved facilities for all Alaskans.
10. Transportation fuel taxes for highway, marine and air travel will cost Alaskans an estimated \$28,000,000 in fiscal year 1982. These state taxes are not needed and should be repealed.
11. If the tax repeals recommended above are implemented, some \$278 million will remain with the people each year instead of going to government. Although this will help the people immensely, this sum amounts to less than 4 percent of the projected revenues for FY '82.
12. Companies doing business in Alaska should be encouraged to reinvest their profits in the state. Investment tax credits should be established for this purpose.
13. The windfall profit tax paid by the oil companies should be permitted as an allowable deduction in determining state income taxes to eliminate double taxation.

14. The growth of state and local government operating budgets should be limited by law or by constitutional amendment. The best formula ties government expenditures to the annual fluctuation in personal income of the non-governmental work force.
15. Permanent Fund monies should be invested so that the income from and the value of these dollars keeps pace with inflation. The current Permanent Fund legislation should be amended to allow investments in appreciable assets.
16. In order to finance large, self-liquidating projects, such as ports, harbors, and hydroelectric facilities, an Alaska Investment Fund should be established, along the same lines as the Permanent Fund.
17. Projects built with this Investment Fund will provide the infrastructure needed to move Alaska away from its economic dependence on the rest of the nation. They can be used as collateral for revenue bonds if the state finds itself short of cash in the future.
18. The state government should not jump into the banking business. Loan programs are best administered by existing private lending institutions.
19. State loan programs must be divorced from the temptations of political abuse. Strict accountability through independent audit systems must be established.

SECTION I

THE SIZE OF THE SURPLUS

In order to make wise decisions on the best use of Alaska's revenues, it is imperative that accurate projections are made regarding the state's potential income and predicted expenditures.

According to a November 5, 1980 memorandum by the staff of the legislature's Budget and Audit Committee, there will be \$5,927,600,000 available for appropriation by the legislature for FY '82.

General Fund surplus predictions for the year 2000 range as high as \$184 billion. But the actual surplus (or deficit) will depend on the level of inflation and state spending as well as on the investment policies of the state and the market price of oil and gas.

The state should immediately develop a series of projections illustrating anticipated growth in both government revenues and expenses. These projections should be widely publicized in simple, understandable form.

A false sense of unlimited wealth could badly distort the judgement of the Alaskan people.

Recommendation for Action

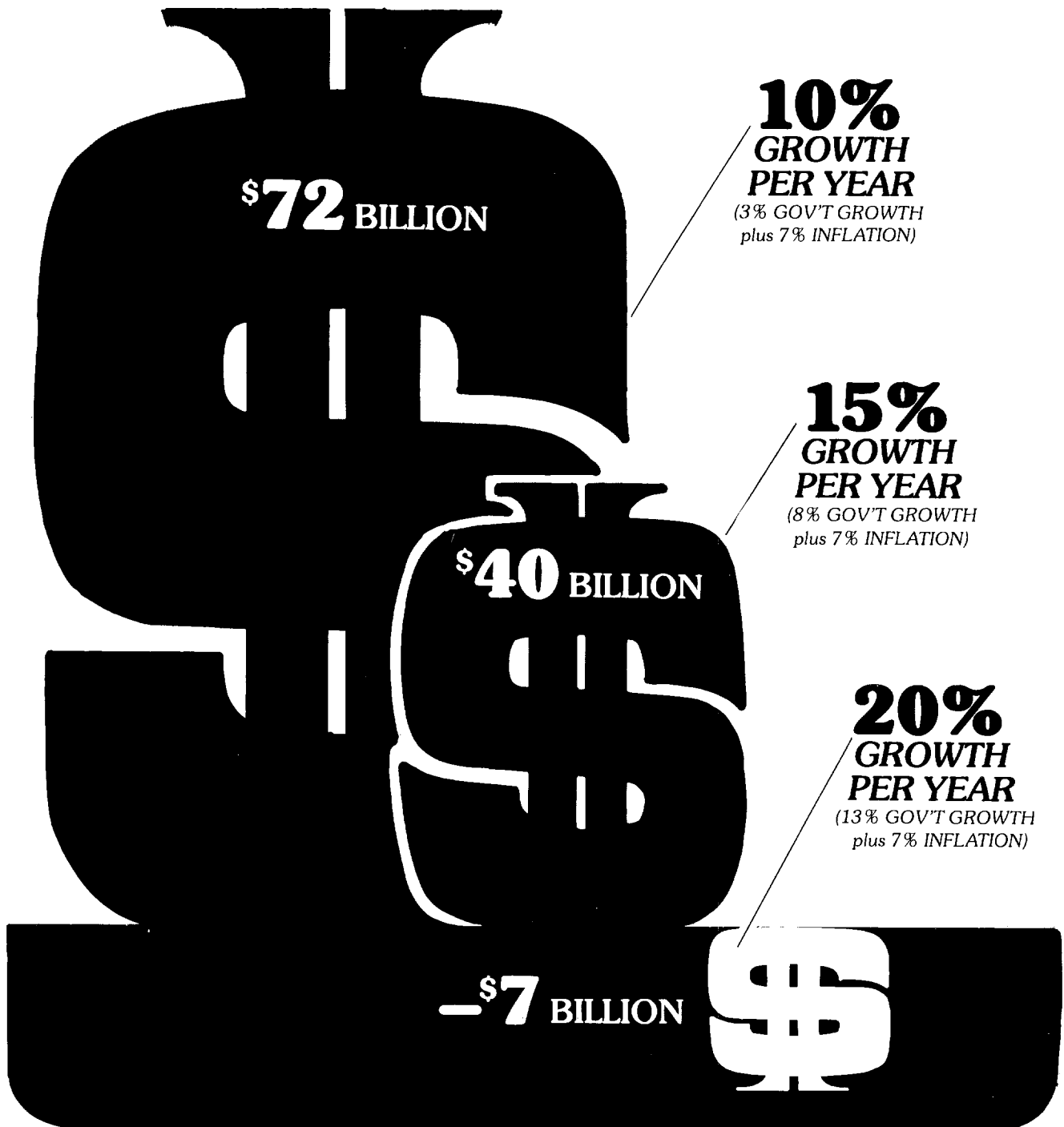
The state should immediately develop a series of projections illustrating anticipated growth in both government revenues and expenses.

Such information is necessary to avert a false sense of unlimited wealth which could badly distort the judgement of the Alaskan people and their leadership and to provide some touchstones for gauging the effect of state spending decisions.

Figure A

1995

Shrinkage of the size of the projected General Fund by 1995 if government growth is not contained.



COMMONWEALTH NORTH CHART

DATA SOURCE: State of Alaska Legislative Working Document Budget Forecasting Model February 20, 1980