

HOUSE FINANCE COMMITTEE
March 22, 2004
1:42 P.M.

TAPE HFC 04 - 62, Side A
TAPE HFC 04 - 62, Side B
TAPE HFC 04 - 63, Side A
TAPE HFC 04 - 63, Side B

CALL TO ORDER

Co-Chair Williams called the House Finance Committee meeting to order at 1:42 P.M.

MEMBERS PRESENT

Representative John Harris, Co-Chair
Representative Bill Williams, Co-Chair
Representative Kevin Meyer, Vice-Chair
Representative Mike Chenault
Representative Eric Croft
Representative Hugh Fate
Representative Richard Foster
Representative Mike Hawker
Representative Reggie Joule
Representative Carl Moses
Representative Bill Stoltze

MEMBERS ABSENT

None

ALSO PRESENT

Bob Bartholomew, Chief Operating Officer, Alaska Permanent Fund Corporation, Department of Revenue; Bruce Tangeman, Fiscal Analyst, Legislative Finance Division; Cheryl Frasca, Director, Division of Management & Budget, Office of the Governor; Pete Ecklund, Staff to Representative Williams; Tom Wright, Staff to Representative Harris; Kim Garner, Director, Division Of Finance, Department Of Administration; Sue Stancliff, Staff to Representative Pete Kott; Tamara Cook, Director, Legislative Legal and Research Services; Mr. Bill Sherrill, Transportation & Infrastructure Committee, U.S. Congress.

PRESENT VIA TELECONFERENCE

Billie Jo Han, Wasilla

SUMMARY

HB 494 An Act relating to the disbursement of money by
 the state, including employment compensation,

unemployment payments, and permanent fund dividends, and to bank investments and deposits by the state; and providing for an effective date.

CSHB 494(FIN) was REPORTED out of Committee with a "do pass" recommendation and seven new fiscal impact notes.

HJR 26 Proposing amendments to the Constitution of the State of Alaska relating to and limiting appropriations from and inflation proofing the Alaska permanent fund by establishing a percent of market value spending limit.

HJR 26 was heard and HELD in Committee for further consideration.

HB 298 An Act relating to the distribution of appropriations from the Alaska permanent fund under art. IX, sec. 15(b), Constitution of the State of Alaska, and making conforming amendments; and providing for an effective date.

HB 298 was heard and HELD in Committee for further consideration.

HJR 9 Proposing amendments to the Constitution of the State of Alaska relating to an appropriation limit and a spending limit

HJR 9 was heard and HELD in Committee for further consideration.

HB 236 An Act imposing a tax on employment; and providing for an effective date.

HB 236 was heard and HELD in Committee for further consideration.

#HB494

HOUSE BILL NO. 494

An Act relating to the disbursement of money by the state, including employment compensation, unemployment payments, and permanent fund dividends, and to bank investments and deposits by the state; and providing for an effective date.

Co-Chair Harris MOVED to ADOPT Work Draft Version Q of HB 494 dated 3-17-04. Co-Chair Williams OBJECTED for purposes of discussion.

MS. SUE STANCLIFF, STAFF TO REPRESENTATIVE PETE KOTT, explained the changes in Version Q. She noted that there

was discussion during the last hearing of the provision in Section 19 that required the departments to do electronic disbursements. This version makes it optional and suggests that the departments use electronic disbursement. The change in Section 14 relates to stale dating and unclaimed property and it was recommended by the Department of Administration.

Ms. Stancliff continued, Version Q deletes the section that repealed the word "warrant" and inserts "warrant" because warrants would be issued and should be kept in statute. The Alaska Railroad recommended the last change. She explained that the Railroad is not required to do electronic disbursements because it is exempt under current statutes, so the work draft removed the Railroad to avoid changing two other parts of the bill.

Co-Chair Harris noted that every year at budget time the Legislature takes up the stale dated warrants, and he asked if the bill addresses that issue. Ms. Stancliff deferred to the Department of Administration.

MS. KIM GARNERO, DIRECTOR, DIVISION OF FINANCE, DEPARTMENT OF ADMINISTRATION, stated that last year the Legislature amended Title 37.05.180 that affects stale dated warrants. She explained that starting last year the warrants became part of unclaimed property. The unclaimed property program holds the money until the claim has come forward instead of letting it lapse into the General Fund and waiting to get a new appropriation in the stale date process. She said that it works well, and that there wouldn't be further stale dated warrant legislation.

Ms. Garnero also noted that last year the Legislature amended the miscellaneous claims portion that is the two-year-old bills. She said that these currently only come before the Legislature if they are large and the agency couldn't pay for them out of the current budget.

Representative Foster MOVED to report CSHB 494 out of Committee with individual recommendations and the accompanying fiscal notes. There being NO OBJECTION, it was so ordered.

CSHB 494(FIN) was REPORTED out of Committee with a "do pass" recommendation and seven new fiscal impact notes.

#HJR26

HOUSE JOINT RESOLUTION NO. 26

Proposing amendments to the Constitution of the State of Alaska relating to and limiting appropriations from and inflation proofing the Alaska permanent fund by establishing a percent of market value spending limit.

Co-Chair Harris MOVED to ADOPT Work Draft Version U of HJR 26 dated 3/19/04. There being NO OBJECTION, it was so ordered.

PETE ECKLUND, STAFF TO REPRESENTATIVE WILLIAMS, explained the incorporation of Representative Stoltze's Amendment #1 in Version U. He said that it simply shortened and amended the title of the resolution.

In response to a question by Co-Chair Williams, Mr. Ecklund commented that Amendment #2 is not in Version U.

Co-Chair Williams announced that he would move HJR 26 to the bottom of the agenda until Representative Stoltze arrived to address it.

#HB298

HOUSE BILL NO. 298

An Act relating to the distribution of appropriations from the Alaska permanent fund under art. IX, sec. 15(b), Constitution of the State of Alaska, and making conforming amendments; and providing for an effective date.

Co-Chair Harris MOVED to ADOPT Work Draft Version V for HB 298 dated 3/19/04. There being NO OBJECTION, it was so ordered.

MR. PETER ECKLUND, STAFF TO REPRESENTATIVE WILLIAMS, explained the changes by comparing Version V with the previous version, House Special Committee on Ways & Means Version U. In Version U, on page 3, lines 5 and 8, the word "average" was changed to "annualized," at the request of the Permanent Fund Corporation. On page 3, line 6, "10 calendar years" was changed to "10 fiscal years" to match the other calculations based on fiscal years.

On page 3, line 21, after the word "inflation" the remainder of that subsection (1) and (2) is deleted after the words "for a specific fiscal year by," The new language was inserted in Version V, page 3, lines 20- 26 was a change requested by the Permanent Fund Corporation.

MR BOB BARTHOLOMEW, CHIEF OPERATING OFFICER, ALASKA PERMANENT FUND CORPORATION (PFC), DEPARTMENT OF REVENUE explained the change in Version V starts on line 24 of page 3. The PFC has recommended a simpler way to calculate the annual inflation rate, using the Consumer Price Index (CPI). The Corporation has always used the CPI, and would now look at the change in one 12-month period instead of from month to month. It is a technical simplification.

Mr. Ecklund addressed Representative Croft's questions from the last hearing on the bill, referring to page 3, lines 17-18 of the Ways & Means Version U. The language states, "50 percent may be appropriated to the general fund" and "50 percent may be appropriated to the dividend fund". The new Version V states: "not more than 50% may be appropriated to the general fund" and "not more than 50% may be appropriated to the dividend fund." He explained it was in response to questions of whether "may be appropriated," meant that 60% or 40% could be appropriated. The new language sets more of an upper cap. The way it is written allows future legislatures to decide a cap of zero to 50% on either the general fund or the dividend.

Mr. Ecklund referred to page 3, line 14, Work Draft V subsection (b), "The legislature may appropriate from the fund for each fiscal year the amount for costs of the corporation associated with operating and investing the fund." The current costs of operating the Fund are between \$45 and \$50 million annually. Those operating costs would be taken off the top, and then 50% would be distributed to dividends, and 50% to the General Fund.

Mr. Ecklund referred to page 3, line 22, subsection (d) noting that the previous version was silent on when the transfer of money would occur from the Permanent Fund to the dividend fund and the General Fund. The new language states that the transfer would occur "within 14 days after the effective date of the appropriation."

Mr. Ecklund referred to a change in Version V on page 4, Sec. 5, which now states, "The operating budget of the corporation shall be included in the state's operating budget under AS 37.07 (Executive Budget Act)." He said the Corporation is agreeable to the language change.

Representative Chenault asked if the Corporation has any problem with the change to 14 days.

Mr. Bartholomew commented on the timing of the distributions. The dividend distribution historically ranges from a \$500 million to \$1 billion lump sum distribution that is needed within the first week of October. It is a policy call if the money resides in the General Fund or the Permanent Fund for that period. It has been transferred in July, so this change is in line with how the Corporation handled the dividend this year. The new language providing an allocation for state services would require discussion on whether to pay a lump sum at the beginning of the fiscal year, or on a quarterly or monthly basis. He said that when there is a steady cash flow, it is easier for the Fund to plan to do a recurring payment rather than a lump sum. A lump sum requires determining how many securities to sell or

how to raise the cash. However, Mr. Bartholomew said that the Fund could make it work as written for a \$1.2 billion transfer on that date. He asked the committee to consider approaching the state services portion from a cash flow standpoint with either a quarterly or monthly distribution. He said it would work as written.

In response to a question by Co-Chair Harris, Mr. Ecklund explained that language was removed from Section 10 of the previous Version U, and confirmed it now provides one effective date of January 1, 2005 if voters approve the constitutional amendment.

Co-Chair Harris MOVED to amend Amendment #1 by adding the words "not more than" before (1) and (2) to incorporate the change in Version V. Co-Chair Williams OBJECTED.

Co-Chair Harris explained that his Amendment #1 would change the 50-50 allocations to the General Fund to not more than a 40% appropriation to public education, and not more than a 60% appropriation to the dividend. He said that his reasoning is to ensure that the public would accept the measure, and would understand that the Legislature wouldn't take any more of the dividend money than is necessary for the operation of the public education portion of general government. He remarked that education is the most highly supported service by the public. He submitted the amendment hoping that it would help to pass the bill and the constitutional amendment.

The amendment to Amendment #1 reads:

Page 3, lines 19-20:

Delete all material and insert:

- "(1) not more than 40 percent may be appropriated for public education;
- (2) not more than 60 percent may be appropriated to the dividend fund"

Vice-Chair Meyer commented that the 60-40 split is closer to what the "Conference of 55" had recommended. He agreed that 40% is appropriate for public education, but expressed concern that 50% could also be appropriated for education in the 50-50 split. He thought that 50% would get the Legislature closer to the amount needed for education. He thought the discussion would center on the 40-60 split or 50-50 split. He indicated that he's inclined to leave it at 50-50 but would agree to change public education to 50% in (1) of Amendment #1.

Representative Hawker agreed with Vice-Chair Meyer's thinking. He drew attention to the new fiscal note from the Department of Revenue, dated 3/22/04 at 12:30 pm. The

analysis gives current projections of appropriations available to the Legislature's discretion under the adoption of the 5% POMV in a constitutional amendment. He noted that in FY 2006, the 50-50 split breaks out Public Services and Per Capita Dividend at \$641 million each. It climbs to about \$800 million each in FY 2011. Combining the two figures totals about \$1.2 billion in FY 06 and \$1.6 billion in FY 11. Looking at immediate need, the proposed amendment would increase the amount appropriated by 10% from 50% to 60% for an approximate additional \$120 million into dividends and away from public services, and perhaps education.

Representative Hawker discussed the attempt to increase education funding by about \$90 million a year for all future years, asking where it will come from. He doubted that the current \$30 per barrel oil price would be sustained. As that price declines, he said the state would have to "scratch" to meet the recurring budget requirements. He voiced reluctance to designate that extra 10% or \$120 million to dividends when it is needed for schools. He noted that the schools need an additional \$30 million to \$40 million above the \$90 million each year. He calculated that \$120 million in a per capita dividend for 600,000 residents has a net effect of \$200 each. He noted that public testimony this year predominantly asked the Legislature to pay for schools first and expressed support for using some of the state wealth for state programs. He was not inclined to support the amendment.

Representative Croft spoke against Amendment #1 for different reasons. He said that it would amend a statute, and it doesn't matter what those two sections are because they give a false perception to the public as long as the words "may be appropriated" are used. It's a statement that these percentages could be used for public education or dividends or for anything, and different numbers could also be used. The language doesn't put any substantive restrictions on what the Legislature can and cannot do. Different percentages wouldn't guarantee the result, or restrict the power of appropriation. He doubted that the amendment makes the difference the sponsor intended, and said that it gives a false impression.

Co-Chair Williams asked how the change from 50% to 40% for state services, amounting to about a \$200 million reduction, would affect the cash flow for payout.

CHERYL FRASCA, DIRECTOR, DIVISION OF MANAGEMENT & BUDGET, OFFICE OF THE GOVERNOR replied that she perceived the issue to be the amount of shortfall over the next 5 to 6 years. She said if the assumption is flat spending, it averages between \$700 and \$800 million in each of the next 5 or 6 fiscal years based on the fall forecast. The pending

increase in K-12 funding raises it by another \$85 million. She said that 50% helps a lot in filling the gap, and 40% helps "not quite as much."

Co-Chair Harris agreed with Ms. Frasca if the intention is to fill the gap only with Permanent Fund earnings. He argued that 40% plus other revenues from the gas line or an income tax would achieve the goal. The budget could easily be balanced on 100% of the earnings of the Fund. Ms. Frasca responded that is correct but she said that she "based it on what has been passed so far."

Co-Chair Williams agreed with Representative Croft that the split can be "dressed," but he observed that spending on education is a selling point for the public. He expressed that the state can't afford a "wish list" of a gas line, an income tax or high oil prices with a fiscal gap of \$600-700 million a year. He said, the Permanent Fund is a rainy day fund, and "It's raining out there, and I don't want to get wet." He spoke for taking care of state services, and said that he strongly opposed the amendment.

Co-Chair Harris questioned adding "shall" rather than "may" and asked if it would cause a legal problem.

MS. TAMARA COOK, DIRECTOR, LEGISLATIVE LEGAL AND RESEARCH SERVICES, explained that fundamentally it wouldn't matter in the context of the two provisions. The lead-in language is mandatory, which states "appropriations for a specific fiscal year are limited as follows." With the insertion of the language, "not more than," some discretion is built in, whether "shall" or "may" is used. The language says the Legislature can go up to a certain percentage for a certain purpose. In any case, statutorily the Legislature cannot dedicate revenue. Ms. Cook said, from that point of view, it may be that this provision would not be enforceable, depending on the form of the constitutional amendment when it's adopted. She hastened to remind the committee that the current allocation in AS 37.13.145 repealed in this bill is also not enforceable as a dedication. She expressed that it has been very potent in explaining the behavior of the Legislature with respect to the use of Permanent Fund income. To that extent, she concluded, there is no reason to suspect that the new provision 143 [Sec. 37.13.143] would have less political force.

Co-Chair Williams asked for clarification that currently the Legislature may use the Permanent Fund in any way it wishes. Ms. Cook affirmed, saying that the Legislature is restricted to the use of the Fund income, but there is currently no restriction in the Constitution regarding how that income can be used. The Legislature statutorily has elected to distribute it under a formula providing for dividends and inflation proofing. She said it has mathematically resulted

over the years in an accumulation of additional money in the earnings reserve account. She noted that that statute also could not be enforced as a dedication, and it has been adhered to by the Legislature because of the public policy decision it makes every year.

Co-Chair Williams asked if the Legislature has ever used any part of the Permanent Fund earnings for state services. Ms. Cook thought that once or twice small amounts from the earnings reserve or income account were used to reimburse litigation expenditures of the Department of Law when it was at fault in litigation. She said there might have been other isolated instances involving very small amounts.

Representative Hawker noted that over the last 8 years since 1996, the Legislature has appropriated over \$238 million from Permanent Fund earnings for other purposes. Appropriations to the Department of Corrections through provisions in statute allow taking dividends from felons to use for the department's operations. Supplemental social service benefits are paid to recipients who also receive dividends. The Legislature has also funded administrative costs of the Departments of Revenue, Public Safety, and Law.

In response to a question by Representative Stoltze, Representative Hawker affirmed that it is money already appropriated for dividends that has been redirected.

Ms. Cook agreed that Representative Hawker is correct. She cited AS 37.13.145, the distribution system that puts a set formula amount into the dividend fund. She clarified that in the dividend fund statutes, the Legislature also identified some appropriations that are taken out of the dividend fund, not for the distribution, but for the purposes Representative Hawker has itemized. It is part of the dividend program.

Co-Chair Harris commented that constitutionally, 25% of oil royalties go into the Permanent Fund automatically, so it was felt that 25% or more can toward the operations of oil and gas to help perpetuate and build up the Fund.

Co-Chair Williams noted that the Legislature hasn't used the Permanent Fund earnings since enactment. Ms. Cook agreed that it is fundamentally true. As the earnings have accumulated, the Legislature has swept the additional earnings back into the principal of the Permanent Fund through a special act of appropriation.

Co-Chair Williams commented that if this measure passed right now, it would be difficult to change the numbers up or down. He recommended that the Legislature can always pay more to the dividend distribution, but it can't lower the dividend amount.

A roll call vote was taken on the motion to adopt the amendment to Amendment #1.

IN FAVOR: Chenault, Foster, Harris
OPPOSED: Stoltze, Croft, Fate, Hawker, Joule, Meyer, Moses, Williams

The MOTION FAILED (3-8). Amendment #1 was not adopted.

Vice-Chair Meyer agreed with Co-Chair Harris in dedicating money to education in statute. He proposed a conceptual Amendment #2 using the 50-50 split that would state, "50% may be appropriated for public education."

Amendment #2 reads:

Page 3, line 19:

(1) not more than 50 percent may be appropriated for public education;

Amendment #2 was adopted without objection.

HB 298 was heard and HELD in Committee for further consideration.

#HJR9

HOUSE JOINT RESOLUTION NO. 9

Proposing amendments to the Constitution of the State of Alaska relating to an appropriation limit and a spending limit.

Co-Chair Harris MOVED to ADOPT Work Draft 23-LS0435, Version Z dated 3/19/04. There being NO OBJECTION, it was so ordered.

MR. PETER ECKLUND, STAFF TO CO-CHAIR WILLIAMS, explained that line 7 in Section 16, would change the average to three of four fiscal years from an average of two of four fiscal years in the previous version. He said that it is an attempt to smooth out the starting point between fiscal years, which Mr. Tangeman could explain, and he noted the chart (copy on file) showing it in visual format.

MR. BRUCE TANGEMAN, FISCAL ANALYST, LEGISLATIVE FINANCE DIVISION stated that the previous version included one base year two years prior in order to get an accurate base year. He explained that it was because last year, or our current FY 04, does not yet include supplemental appropriations. The problem was that it could allow a stair-step of the appropriation: if the Legislature doesn't appropriate the

full limit one year, but does the following year, there would be a gap causing a stair step in future years.

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Mr. Tangeman continued stating that the change smoothes out the low years when less than the full limit is appropriated.

Mr. Ecklund continued discussing the changes in Work Draft Version Z. The change to Section 16(b) on page 1, line 16, would provide that if a future Legislature desired to exceed the spending limit, it could do so by two methods. Exceeding by 2% would require a 2/3 vote of both houses, and exceeding by a further 2%, for a total of 4%, would require a 3/4 vote of both houses.

Mr. Ecklund explained that the change on page 2, line 7, in the last part of (b) states that any exceeding of the limit must be done in a separate appropriation bill. A future Legislature wishing to exceed the spending limit by, or up to, 2% or 4% would have to introduce separate legislation and get a 2/3 vote for 2%, and a 3/4 vote for 4% increases.

Representative Croft questioned whether the change on page 1 would recreate the supplemental problem in the new draft by using the earliest 3 of the 4 preceding fiscal years. Mr. Tangeman clarified that FY 04 would be skipped, and FY 01, FY 02 and FY 03 would be averaged.

Representative Croft asked how the "anti-log rolling" section would work if the operating and capital budgets both passed but exceed the limit by 4%, and which of the two would require the 2/3 vote. He asked if it would be similar to the Constitutional Budget Reserve special vote provisions. Mr. Ecklund replied, with a limit that used the prior three fiscal years averaged and adjusted for half of the population and the income increase, that would be the limit for the operating and capital budgets. To exceed that limit- to go over 3.5%- for capital or operating spending, a separate piece of legislation would have to be introduced and voted on.

Representative Croft continued discussing a hypothetical situation and reiterated his question of which appropriation would stand alone. Mr. Ecklund clarified through example that if the cap were \$3.5 million, the operating and capital budgets could not exceed it. As the budgets were developed, if it appeared that they would exceed the cap, items would be pulled and put in a separate piece of legislation. The intent was to highlight and separate the exceeding of the limit instead of burying it in the operating and capital budgets requiring a lot of successive votes. The intent was to make it less confusing.

Representative Croft questioned how it would work in practical effect, if the budgets run up to the cap in every fiscal year. He said that a separate appropriation might be needed each year to assure the gap in the operating budget would be filled. Mr. Ecklund replied that it is hard to anticipate future events, but the concept is based on a hard limit that can't be exceeded. The intent is to build in a safety valve to highlight what the percentage exceeding the limit is, and to conduct separate votes on separate pieces of legislation.

Co-Chair Williams commented that he and Representatives Stoltze and Hawker, and Mr. Ecklund worked with Ms. Frasca to draft the changes.

Mr. Ecklund continued discussing the changes. On page 2, line 21, the debt service of General Obligation (GO) Bonds was added to the exemptions from the limit. On page 3, line 1, (12) the new language mirrors that in statute, in order to include an exception such as the Kodiak Launch Facility. He explained this is intended not to penalize the Facility for getting more business income. In Section 30 on page 3, the language stating the ballot proposition would come up again in 2010 wasn't changed. He explained that a "yes" vote means the voter wants to keep the spending limit, and a "no" vote means the voter rejects it.

Representative Hawker commented that the base indexing is the average annual percentage rate change for state population and personal income. One factor that is not in the index is the inflation factor or Consumer Price Index (CPI). He asked the sponsor's and committee's thoughts on whether the CPI ought to be in the base indexing. He referred to a chart by Legislative Finance (copy on file) which shows that population and income projected from the base year of 1996 is a higher number than combining population and the CPI.

Representative Stoltze offered that his original intent was not to have any indexing at all. He agreed to use the Governor's Office formula of personal income. He was open to hearing the committee's thoughts.

Representative Hawker MOVED to ADOPT Amendment #1. Co-Chair Williams OBJECTED for purposes of discussion.

Amendment #1 reads:

Page 2, line 12:

Delete "of Alaska permanent fund income"
Insert "from the Alaska permanent fund"

Representative Hawker explained that the amendment involves an addition to the exemptions not subject to the spending limit. The Permanent Fund money dedicated to dividends should be exempted. On page 2, line 12, the language reflects the current statute in which dividends are paid from Permanent Fund income, and Amendment #1 would make the language more encompassing: to appropriations from the Permanent Fund for payments of dividends. He believed that the language would accommodate either a POMV or the current statute, depending on what the public decides.

Representative Stoltze asked if the spending limit would allow for money to come out of the Permanent Fund principal by the nature of this language. He asked for guidance from legal counsel.

Ms. Cook did not think it would create the concern that Representative Stoltze articulated. She did not see subsection (c) as granting authority to make any particular type of appropriation. It simply states that an appropriation would not be counted toward the spending limit. She said that the extent of the power of the Legislature to make an appropriation will be handled under the constitutional provision for the Permanent Fund in Section 15, whether it is amended or not. Ms. Cook pointed out that if it is not amended, and HJR 9 were to pass, obviously any appropriation from the Fund would have to be from income. She continued, if it is amended, and HJR 9 were to pass, obviously there would be no distinction between income and principal, but any appropriation made would be subject to a limit based on Percent of Market Value.

Representative Stoltze expressed that if HJR 9 were to pass, the legislative record would be very important. He asked Ms. Cook to provide her comments as a legal opinion to the committee. Ms. Cook replied that she would.

There being NO further OBJECTION, Amendment #1 was adopted.

Co-Chair Williams MOVED to adopt Amendment #2. Representative Stoltze OBJECTED for the purposes of discussion.

Amendment #2 reads:

Page 3, line 7, following "**Section 30.**":

Insert "**Contingent Effect and Effective Date;**"

Page 3, line 7:

Delete "(a) The"

Insert "(a) The 2004 amendment relating to an appropriation limit (art. IX, sec. 16) takes effect only if

a 2004 amendment relating to and limiting appropriations from the Alaska permanent fund based on an averaged percent of the fund market value (art. IX, sec. 15) is approved by the voters and takes effect. If the 2004 amendment relating to an appropriation limit (art. IX, sec. 16) under this subsection takes effect, it takes effect on the effective date of the 2004 amendment relating to and limiting appropriations from the Alaska permanent fund based on an averaged percent of the fund market value (art. IX, sec. 15).

(b) If the"

Page 3, line 8, following "(art. IX, sec. 16)":

Insert "takes effect under (a) of this section, it"

Page 3, line 10:

Delete "(b) Notwithstanding Section 1 of Article XIII,"

Insert "(c) If it takes effect under (a) of this section,"

Page 3, following line 15:

Insert "(d) To the extent this section conflicts with Section 1 of Article XIII, this section prevails."

Co-Chair Williams explained that Amendment #2 basically states that if the POMV doesn't pass, this measure doesn't pass.

Representative Joule commented that it would be asking the voters to approve two constitutional amendments, but Amendment #2 would link one to the other. He questioned what would happen if the voters chose only one, and he asked if their votes don't count.

Vice-Chair Meyer agreed with Representative Joule. He suggested that the spending limit should move forward because if some new sources of revenue were passed, the Legislature would want to guarantee a limit to spending. If the voters were to approve HJR 9, that is also what they would want, regardless of passage of the POMV. He objected to the amendment.

Representative Hawker agreed that the spending limit amendment would stand on its own merits. The real impetus for the sponsorship of HJR 9 was to avail of some of the Permanent Fund earnings for general government so that the public would have confidence that future legislatures would not spend the money frivolously. He stated that HJR 9 was originally brought forth as part of a fiscal legislation package, and he felt that there is strong merit to having them linked. Representative Hawker said that he didn't feel

this disrespects the individual voter who might adamantly prefer one to the other. He has listened to the counsel from the Minority Leadership who require a comprehensive fiscal package that will work for future years. He concluded that he supports Amendment #2.

Representative Stoltze expressed that passage of the POMV will require building the trust of the voters. He did not think that tying HJR 9 with the POMV would build that public confidence. He thought that both measures should prevail or fall on their own merits. He did not want to lose votes on his measure. He stated that he did not support Amendment #2 although he respected the motivations of its sponsor.

Representative Croft commented that it prohibits the dividend protection as a spending cap. He thought that a logical approach would be to spend no more money than is available and not touch the revenue source, which is the type of limit that individuals impose on themselves. He voiced concern with the proposed approach while commending the process presented by Representative Stoltze. He said that Amendment #2 precludes the people from choosing the alternative form of spending cap. He stated that if the public rejects dividend protection, they don't get a spending cap, and the public will get neither if they vote down the POMV.

Representative Croft pointed out the tenor in Amendment #2 is that the Legislature can be trusted to manage the Permanent Fund, but it cannot be trusted on spending in future years. He expressed concern that the POMV and the spending cap should not be tied together. He felt that constitutional amendments must be done thoughtfully and carefully because they remain in effect for a long time. He worried that it is inappropriate to say, "if you don't let us take half your dividend, we won't promise to be good with your money."

Co-Chair Williams commented that he has heard talk that the only way he would support the POMV is if a spending cap was put on it. He stated he has been, and remains, opposed to a spending cap because he believes it goes against the Constitution to give up the Legislature's right to appropriate. He expressed concern that the way the bill is currently written, a 2% increase requires 27 votes, and a $\frac{3}{4}$ vote on 4% would put the Legislature in the same position that it's in at the end of session with the $\frac{3}{4}$ vote [CBR]. He expressed that he does not distrust the electorate and he supports the amendment,

A roll call vote was taken on the motion to adopt Amendment #2.

IN FAVOR: Fate, Foster, Hawker, Williams

OPPOSED: Chenault, Croft, Joule, Meyer, Moses, Stoltze, Harris

The MOTION FAILED (4-7). Amendment #2 was not adopted.

HJR 9 was heard and HELD in Committee for further consideration.

#HB236

HOUSE BILL NO. 236

An Act imposing a tax on employment; and providing for an effective date.

Co-Chair Harris MOVED to ADOPT Work Draft 23-LS0921, Version X dated 3/19/04. There being NO OBJECTION, it was so ordered.

Representative Hawker announced that Representative Wilson was unable to attend the hearing and that Mr. Ecklund would explain the changes in the proposed committee substitute.

MR. PETER ECKLUND, STAFF TO REPRESENTATIVE WILLIAMS, noted that Version X deletes from Version W the lines 13-28 on page 2, subsection (d). He explained that this deletes two triggers: one where the tax would go into effect if the CBR is less than \$1 billion, and the other where the trigger goes off when the CBR goes higher than \$2.5 billion.

Mr. Ecklund noted a change adding new language requested by the Department of Revenue on page 2, lines 30-31. It states "The Department of Revenue may, if it will result in cost savings for the state in the administration of the tax, for employers in the administration of the tax, or for both." Mr. Ecklund explained that the Department of Labor receives federal funds with restrictions on how the monies can be used, and the department wanted to ensure that the Legislature would not require it to cooperate in ways that didn't make sense.

Representative Hawker expressed that the sponsor, Representative Wilson, is in concurrence with the proposed changes.

Representative Croft asked what difference the word "may" makes when the department can do whatever it wants. Mr. Ecklund affirmed that the Department of Revenue asked for the language. Representative Croft also questioned the meaning of the words, "or for both."

Representative Croft asked why the trigger was removed from Version X. He noted that the billion dollar minimum amount in the Constitutional Budget Reserve has been important in

the discussions of both Governor Murkowski and the Conference of 55.

Co-Chair Williams replied that this would generate \$42 million a year, and to start up a process and then stop it would cost more. The people of the state are asking for this type of tax.

Representative Croft MOVED to ADOPT Amendment #1. Co-Chair Harris OBJECTED.

Representative Croft explained that his office talked to the National Conference of State Legislatures (NCSL) about every state's income tax structure. He noted that 35 states have some kind of income tax that is graduated, but none have graduated it downward, or charged a higher percentage for poorer people. These 35 states adopted the concept that wealthier people should pay a higher percentage of their income on an income tax. If each person was taxed \$100, as you go up in income level, it becomes a smaller and smaller percentage of that income. If a person is extremely wealthy, it is a miniscule percentage of that income. He is not proposing any substantive amendments to the bill but feels it should be titled correctly. He said it should be known as the only regressive income tax in the nation.

Representative Hawker stated that this bill is known as a head tax, and he asked the sponsor of the amendment to consider changing his proposed language to "We've All Got a Stake in the Future of Alaska Act." He said that's the point of this bill. It is not designed as a comprehensive income tax, but as an ante up for participating in the bounty of Alaska.

Co-Chair Harris asked Representative Croft when the state passed a school tax and if it was \$10 per year for everyone regardless of income level. Representative Croft affirmed that it was \$10 for everyone. Co-Chair Harris asked if he thought this is different. Representative Croft said that at the time, there was a progressive income tax included, so this is an alternative minimum.

Co-Chair Williams commented that he had suggested a \$100 school tax last year when this was introduced.

Representative Croft commented on "class responsibility." He felt that there is nothing fundamentally unfair about the idea of upper incomes paying proportionately more. Conservatives make the argument for a flat tax. He noted that only regressive ideas are on the table--proposals that would take from the poorest members of society. He said that this title is at least honest about what this bill does. He didn't want this measure to be a "trick" for some

later tax. He thought that this is the only regressive tax in the nation and it deserves further discussion.

Co-Chair Harris agreed that there's no doubt that the bill is based on people who earn income. He discussed current user fees and taxes, noting that poor people pay the same amount as do rich people. Everyone benefits from education; he expressed concern that the Legislature can't mandate that this will go to education, just as it can't dedicate the Permanent Fund to education. It can be called an education fund but Co-Chair Harris said that it doesn't guarantee it will be appropriated to education. It's a user fee.

Representative Hawker commented that the characterization of this as a regressive device intrigued him. He pointed out that the bill was crafted to create a huge exemption for folks who have no jobs and exist purely by subsistence or public welfare or retirement income. The State is looking at a basis to generate earnings to support public institutions, and in this case, the base is the people who are working.

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Representative Hawker continued, in aggregate it is a substantial contribution to education. It seems a reasonable approach and looks at value for value. It asks working people to give a small amount back to the state.

A roll call vote was taken on the motion to adopt Amendment #1.

IN FAVOR: Croft

OPPOSED: Fate, Foster, Hawker, Joule, Meyer, Moses, Stoltze, Chenault, Williams, Harris

The MOTION FAILED (1-10). Amendment #1 was not adopted.

Vice-Chair Meyer said he would not make an amendment without the bill sponsor being present. He noted on page 5, line 6 where it says, "the legislature may appropriate the estimated amounts to be collected and separately accounted for" under this section for education. He appreciated that this would go to education. The Legislature has talked about inflation proofing education for some time, and he spoke in favor of a source of money to inflation-proof the Foundation Formula. He said he would like to change the word "may" to "shall" because it is a little stronger, even though money can't be dedicated. He would wait to discuss it with the sponsor.

Discussion ensued regarding whether the language change would carry any weight.

Vice-Chair Meyer stated his understanding that there would be legal concerns in charging out-of-state workers twice the amount charged to in-state workers, or \$200.

Representative Stoltze introduced **Mr. Bill Sherrill**, who works for the Transportation & Infrastructure Committee in the U.S. Congress.

BILLIE JO HANSEN, REPRESENTING SELF, VIA TELECONFERENCE, WASILLA, voiced opposition to the bill because she felt that it would penalize the retired person who moves off of social security to work part-time to make ends meet. She thought it would also penalize motivated youth in the workforce who may work only one day a week for eight hours. She felt there are other ways to do this, and it is not appropriate to call it an education tax. She suggested calling it a work permit tax and setting it on a percentage rate of income for the year. She would rather give \$100 to a school for her son's education than to the General Fund when it's not specifically appropriated to education.

HB 236 was heard and HELD in Committee for further consideration.

#HJR26

HOUSE JOINT RESOLUTION NO. 26

Proposing amendments to the Constitution of the State of Alaska relating to and limiting appropriations from and inflation proofing the Alaska permanent fund by establishing a percent of market value spending limit.

Co-Chair Williams again brought HJR 26 before the committee to discuss Work Draft Version U that was adopted earlier in the meeting. He noted that Amendment #1 by Representative Stoltze was adopted and incorporated into Version U.

Representative Stoltze MOVED to ADOPT Amendment #2. Representative Hawker OBJECTED.

Representative Stoltze explained the amendment reflects his concern about protecting the principal from invasion in the event a POMV is implemented in the Constitution. He had the amendment drafted after listening to testimony from the Mental Health Trust and Permanent Fund Corporation staff.

Amendment #2 reads:

Page 2, line 3:
Delete "five"
Insert "four"

In response to a question by Co-Chair Harris, Representative Stoltze explained that the amendment changes the percentage, on line 2, page 3 of the new version. It proposes to make it 4% of the value.

Representative Hawker agreed with the intent of the amendment to ensure protection of the value of the Permanent Fund over time. The issue has been given a great deal of technical analysis and consideration, but he was personally convinced that 5% would protect Fund over time. He discussed the ten-year rolling real rate of return for the Permanent Fund and why 5% is appropriate. He reminded the committee of statutory enabling language in HB 298 that provides that if the 10-year real rate of return drops below 5%, the Legislature would be limited to that lower number for draws. He concluded that there is a compelling argument to keep it at 5%. He noted that the constitutional amendment states "up to 5%." He could not support Amendment #2.

Vice-Chair Meyer commented that in the community meetings on POMV, people constantly returned to the 5%. He is comfortable with 5% and up to the 5%. He expressed that adequate safeguards are already in place.

Representative Croft commented that 4% is a more prudent number. He supported erring on the side of caution and conserving more for Alaska's children and grandchildren. He said 5% is defensible, but "on the outer edge of what most endowments take."

Co-Chair Harris expressed support for Amendment #2.

Co-Chair Williams stated that he objected to Amendment #2 for the reasons that Vice-Chair Meyer and Representative Croft expressed. After working on the Percent of Market Value for the past six years, he believes that 5% is a good and proven payout. He would vote against the amendment.

A roll call vote was taken on the motion.

IN FAVOR: Joule, Stoltze, Chenault, Croft, Harris
OPPOSED: Fate, Foster, Hawker, Meyer, Williams

Representative Moses was absent.
The MOTION FAILED (5-5) and Amendment #2 was not adopted.

Co-Chair Harris MOVED to ADOPT Amendment #3. Co-Chair Williams OBJECTED for purposes of discussion.

TOM WRIGHT, STAFF TO REPRESENTATIVE HARRIS, explained that Amendment #3 would establish an earnings reserve account to ensure that the corpus of the Fund would not be touched and would be a separate entity. Language was inserted on page

2, beginning on line 4, to provide a mechanism within this amendment to appropriate funds for the operation of the Permanent Fund Corporation. There is also language providing to distribute a program of dividend payments for state residents and public education after paying the costs of operation. Conforming language on page 2, subsection (b), line 19, provides that after the effective date, the costs up to June 30, 2004 prior to the passage of this amendment will be appropriated.

Co-Chair Harris asked if this constitutional language protecting the corpus of the Fund provides that if the earnings are less than 5%, the payout would be less than 5% for the first five of six fiscal years. Mr. Wright affirmed.

Amendment #3 reads:

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3/22/04

CS FOR HOUSE JOINT RESOLUTION NO. 26()

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - SECOND SESSION

BY

Offered:
Referred:

Sponsor(s): HOUSE RULES COMMITTEE BY REQUEST OF THE LEGISLATIVE BUDGET AND
AUDIT COMMITTEE
A RESOLUTION

Proposing amendments to the Constitution of the State of Alaska relating to the Alaska permanent fund, establishing the earnings reserve account, and permitting distribution from the account only for permanent fund dividends, costs of administering the permanent fund, and public education.

BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* **Section 1.** Article IX, sec. 15, Constitution of the State of Alaska, is amended to read:

Section 15. Alaska Permanent Fund. (a) At least twenty-five per cent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses received by the State shall be placed in a permanent fund, the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for permanent fund investments. **The earnings reserve account is established as a separate account in the fund.** All income from the permanent fund shall be deposited in

the earnings reserve account as soon as it is received. Appropriations may only be made from the earnings reserve account as provided in (b) of this section [GENERAL FUND UNLESS OTHERWISE PROVIDED BY LAW].

* **Sec. 2.** Article IX, sec. 15, Constitution of the State of Alaska, is amended by adding a new subsection to read:

(b) Appropriations from the earnings reserve account for a fiscal year may not exceed five percent of the average of the market values of the fund on June 30 for the first five of the six fiscal years immediately preceding that fiscal year. Appropriations from the earnings reserve account may be made only for the following purposes:

- (1) costs of administering the permanent fund;
- (2) a program of dividend payments for State residents established by law together with costs of administering that program; and
- (3) public education.

* **Sec. 3.** Article XV, Constitution of the State of Alaska, is amended by adding a new section to read:

Section 30. Transition. (a) On the effective date of the 2004 amendments relating to the Alaska permanent fund (art. IX, sec. 15), the unencumbered, unappropriated balance of the earnings reserve account established under AS 37.13.145(a) is added to the earnings reserve account established in the Alaska permanent fund.

(b) Section 15(b) of Article IX first applies to appropriations for fiscal year 2006. Appropriations from the permanent fund for fiscal year 2005 are subject to Section 15 of Article IX as that section read on June 30, 2004.

* **Sec. 4.** The amendments proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

Representative Croft asked if the language on page 2, lines 9-10 protects the current dividend structure in law. Mr. Wright clarified that it states a program of dividend payments for state residents, and it doesn't prescribe a percentage or an amount. In response to a question by Representative Croft, Mr. Wright said it would apply to the current statute.

Representative Croft asked if the Legislature could change the current statute on the dividend program under this language. Mr. Wright pointed out that the Legislature always has the authority to change the dividend program.

Co-Chair Harris explained that Amendment #3 would establish in the Constitution three things that the Legislature can do with the earnings of the Permanent Fund: pay the costs of administering the Fund, pay the dividend, and appropriate for public education. It doesn't give percentages.

Representative Croft commented that the amendment language looks like a dividend protection but it could be anything established by law.

Co-Chair Harris observed that the Legislature could spend all the earnings of the Permanent Fund if it so chose, but this amendment provides some small protection to the dividend.

Co-Chair Williams asked if Amendment #3 changes everything and gives a new direction to HJR 26. Co-Chair Harris replied that it's not a complete change, but it is a lot more specific.

Co-Chair Williams requested that the committee not vote on Amendment #3 at this time in order to have time to review it before the next hearing.

Representative Hawker asked Co-Chair Harris to consider dividing Amendment #3 into the two distinct issues embodied in Section 1 and Section 2 of the amendment.

Representative Joule commented that there is currently an earnings reserve account and he asked how this would be different. Mr. Wright pointed out the only difference is that this amendment states there is a separate earnings reserve account and places it in the Constitution.

Representative Fate MOVED to ADOPT Amendment #4. Co-Chair Williams OBJECTED for purposes of discussion.

Representative Fate expressed concern over the ability of the Legislature to fulfill its prime purpose of appropriating money. He expressed that any percentage is subject to a warranted change, and the ten-year rolling average has been well researched. He said he is one of the few members who can recall the Great Depression that lasted 12 years, with double-digit inflation. He reiterated that the prime responsibility of the Legislature is to appropriate, and if it can't, its function has been eroded.

Representative Fate explained that Amendment #4 changes six words. On line 2, instead of saying a percentage of 5%, it codifies in the Constitution that there will be a percentage determined by law.

Amendment #4 reads:

*Sec.2. Article IX, sec. 15, Constitution of the State of Alaska, is amended by adding a 01 new subsection to read:

02(b)Appropriations from the permanent fund for a fiscal year shall be
03 a percentage of [on may not exceed five percent of] the average of the

04 market values of the fund on June 30 for the first five of the six fiscal years

05 immediately preceding that fiscal year as determine[d] by law.

MR. BOB BARTHOLOMEW, CHIEF OPERATING OFFICER, ALASKA PERMANENT FUND CORPORATION, DEPARTMENT OF REVENUE, compared Amendment #4 to Work Draft U. The proposed work draft puts a spending limit on the Permanent Fund equal to the Board of Trustees' recommendation of no more than 5%. The proposed amendment maintains the concept of basing appropriations on market value, but states that the spending limit would be put into statute instead of the Constitution, on an annual basis.

Representative Croft noted previous discussions of the limit of 5%, which would allow lower appropriations but not higher. This amendment would allow higher appropriations. The trade-off for POMV is the spending limit discipline of 5% in good years in order to reserve for the bad. He expressed concern that in a year when oil prices and the market are up, the inclination to ignore an income tax or oil tax and the pressure to spend up to 6% or 7% might be irresistible. This amendment gets rid of the needed discipline.

Representative Hawker agreed with Representative Croft and expressed concern that Amendment #4 clearly allows overspending in the good years. He pointed out that it violates three of the five reasons the Permanent Fund Corporation argues for Percent of Market Value: maintaining the purchasing power of the Fund, preventing overspending in good years, and making payout amounts more stable from year to year. He observed that the purpose of the POMV set percentage is to stabilize the amount of appropriation from the Fund and give absolute guarantee of the long-term value of the Fund. He respectfully did not concur with the amendment.

Representative Fate informed the committee that his amendment was drafted in concurrence with the spending limit bill [HJR 9] before the Committee. For him, it does not come down to a short, or even a 25-year term consideration of the growth of corpus of the Fund. In his view, although he agreed with the concept of the measure, passage of HJR 26 would erode the prerogative and responsibility to appropriate by the Legislature. It is not his concern whether the Fund even grows, but putting from zero to 5% in the Constitution establishes an appropriation. He introduced the amendment because of the basic question of the functions and responsibilities of the Legislature, not in order to allow 7% or 8% in the future.

Co-Chair Harris asked if the fiscal note for \$700 thousand dated 3-16-04 is still in effect with the bill. Mr.

Bartholomew affirmed, and explained that there are two additions to the FY 05 budget that the Board of Trustees and Permanent Fund staff is requesting. Once the Legislature adopts the constitutional amendment, the Corporation would fall under the restrictions of the Alaska Public Offices Commission (APOC) on the authority to advocate. The requests in the operating budget are for additional authority to educate and advocate for Percent of Market Value; and if the Legislature supported that request, to be able use radio, television and print media to carry out those functions.

A roll call vote was taken on the motion to adopt Amendment #4.

IN FAVOR: Foster, Fate

OPPOSED: Hawker, Joule, Meyer, Stoltze, Chenault, Croft,
Williams, Harris

Representative Moses was absent.

The MOTION to adopt Amendment #4 FAILED (2-8).

Representative Croft questioned if the Fund would educate in a non-partisan manner or advocate for POMV. He asked how it would be found in a fiscal note. Mr. Bartholomew stated that in talking with the APOC, the definitions of education and advocacy are unclear. He said that if there were specific lines to draw, the PFC would work with legal counsel on the authority to comply, as well as the authority language. He noted that if the language in the operating budget did not pass, the PFC couldn't spend the \$700 thousand.

Co-Chair Harris thought that it would be a "slap in the face" to the public for the Permanent Fund Corporation, which is entrusted with the dividend to advocate for POMV. He questioned using \$700 thousand dollars of the Permanent Fund on advocacy when another entity could assume that role. Mr. Bartholomew agreed that it would be the preferred way. He explained that the "feed-back" from the public on the Percent of Market Value approach indicates that a broad segment of the public does not understand it. The public is educated through mass media. The Permanent Fund needs the authority to speak publicly. To reach the public, you must go after them, he said.

Co-Chair Harris voiced concern that the Just Say No campaign gets the message out to many Alaskans who may not be educated on the issue but are hearing the message. He asked if people would be "turned off" by the use of \$700 thousand of Permanent Fund money to tell Alaskans what they need to do. He asked if that had been considered.

Mr. Bartholomew replied that even as the request was written up, the Board discussed a negative public reaction.

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Mr. Bartholomew continued discussing the use of state money for advocating for the POMV, expressing that the Board of Trustees believes there is the obligation to educate and that the benefits outweigh the risks.

Vice-Chair Meyer pointed out that \$300 thousand is in the Supplemental Budget and asked if the \$700 thousand is additional. Mr. Bartholomew addressed the \$1.4 million advocacy, pointing out that the amount could be determined by campaign parameters. Costs would be split between FY 04-FY 05, with \$900 thousand in FY 05 and \$700 thousand derived from the fiscal note. He said that \$200 thousand would come from other parts of the budget. He expressed that the Board was very sensitive to the potential negative reaction and it urged the Corporation not to proceed without legislative guidance.

Vice-Chair Meyer asked if there would be other than public sources of funding available if there were only General Fund money. Mr. Bartholomew answered that the Corporation had not pursued other sources, and private groups had not contacted it. The Board would not seek private funding, and as a public entity, it wouldn't want to have "strings attached."

Vice-Chair Meyer noted that there are opposing groups raising private money. He suggested a grassroots effort to be a "Just Say Yes" group, but he acknowledged that it would be a challenge.

Representative Hawker referred to the fiscal note. He thought that the opposition groups would not be held to the same standard of truthfulness and impartiality of the Permanent Fund Corporation, and he commented that it is easy to tell people what they want to hear. He voiced concern over the Legislature's leadership role and responsibility, and said that if the Legislature lacks faith in its own convictions on the POMV being the right thing to do, an inappropriate message could be sent to the public. He expressed that the dialogue before the public should be objective, factual and truthful.

Representative Stoltze felt that there is no legitimate reason to use government money and it would erode public confidence. He recommended looking at it from a strategy point of view, and he lauded all the effort that has been expended.

Co-Chair Williams noted that he agreed with the Permanent Fund Corporation's approach. He stressed that this is an

important issue for the State of Alaska, and the public needs to make an informed decision.

Co-Chair Williams stated that HJR 26 would be HELD in Committee for further consideration.

#

ADJOURNMENT

The meeting was adjourned at 4:15 P.M.