

MINUTES
SENATE FINANCE COMMITTEE
May 06, 2004
8:05 AM

TAPES

SFC-04 # 109, Side A
SFC 04 # 109, Side B

CALL TO ORDER

Co-Chair Gary Wilken convened the meeting at approximately 8:05 AM.

PRESENT

Senator Lyda Green, Co-Chair
Senator Gary Wilken, Co-Chair
Senator Con Bunde, Vice Chair
Senator Fred Dyson
Senator Ben Stevens
Senator Lyman Hoffman
Senator Donny Olson

Also Attending: REPRESENTATIVE NORM ROKEBERG; REPRESENTATIVE MIKE CHENAULT; JANET SEITZ, Staff to Representative Norm Rokeberg; RUTH BLACKWELL, Realtor and Representative, Alaska Association of Realtors; PAT DAVIDSON, Director, Legislative Budget & Audit; BOB BARTHOLOMEW, Chief Operating Officer, Alaska Permanent Fund Corporation, Department of Revenue; STEVER PORTER, Deputy Commissioner, Office of the Commissioner, Department of Revenue

Attending via Teleconference: From Anchorage: CHARLES SANDBERG, Realtor, and Representative, Alaska Association of Realtors; HAROLD HEINZE, CEO, Alaska Natural Gas Development Authority; From an Offnet Site: DAVE OWENS, Owner, Owens Inspection Services; From Kenai: BILL POPP, Oil and Gas Liaison for the Kenai Peninsula Borough

SUMMARY INFORMATION

HB 418-REAL ESTATE COM'N/LICENSEE/HOME INSPECT

The committee heard from the sponsor and the real estate and home inspector industry. Four amendments were adopted and the bill

reported from Committee.

HB 417-AK NATURAL GAS DEV. AUTHORITY INITIATIVE

The Committee heard from the sponsor, the Department of Natural Resources, and the industry. The bill was reported from Committee.

HJR 26-CONST. AM: PF APPROPS/INFLATION-PROOFING

The Committee heard from the Department of Revenue and reported the bill from Committee.

HB 15-SOLICITATIONS/CONSUMER PROTECTION

This bill was scheduled but not heard.

HB 422-BUDGET RESERVE FUND INVESTMENT

This bill was scheduled but not heard.

HB 494-ELECTRONIC PAYMENT FOR STATE BUSINESS

This bill was scheduled but not heard.

HB 514-CHILD SUPPORT ENFORCEMENT/ CRIMES

This bill was scheduled but not heard.

HB 545-STATE REAL PROPERTY LEASE EXTENSIONS

This bill was scheduled but not heard.

HB 559-STEP PROGRAM CONTINUANCE

This bill was scheduled but not heard.

#HB418

SENATE CS FOR CS FOR HOUSE BILL NO. 418(L&C)

"An Act extending the termination date of the Real Estate Commission; relating to real estate; relating to home inspectors; relating to real estate licensees; and providing for an effective date."

This was the first hearing for this bill in the Senate Finance Committee.

Co-Chair Wilken stated that this bill, SCS CS HB 418 (L&C), Version 23-LS1548\Q, is sponsored by the House Labor & Commerce Committee and Representative Norm Rokeberg and would extend the Real Estate Commission until June 30, 2008. In addition, he noted that the bill would further clarify the State's Home Inspector law. He specified that a Department of Community and Economic Development fiscal note accompanies the bill.

JANET SEITZ, Staff to Representative Norm Rokeberg, the bill's sponsor, informed the Committee that in addition to extending the life of the Real Estate Commission until 2008, this legislation would clarify existing procedures regarding real estate licenses and notice procedures as recommended in the Alaska Division of Legislative Audit, Audit Digest #08-20023-03 [copy on file]. She explained that this bill would also change language to address issues arising from the enactment of the 2003 Home Inspector legislation, HB 9, as recommended by the Regulation Writing Procedure and the Home Inspector industry.

RUTH BLACKWELL, Realtor and Representative, Alaska Association of Realtors, informed the Committee that the Alaska Association of Realtors (AAR) supports extending the life of the Real Estate Commission. On another matter, she pointed out that AAR is in favor of a forthcoming amendment that would reduce the real estate surety fund award to a claimant from the \$20,000 level specified in the Senate Labor & Commerce (L&C) version of the bill to its current level of \$10,000.

Co-Chair Wilken asked which amendment would address the surety bond issue.

Ms. Seitz responded that it would be addressed in forthcoming Amendment #3.

Ms. Blackwell explained that with the exception of the year 2003 when the number of surety claims amounted to fourteen, the average number of claims has been three or five claims a year. She stated that during her most recent tenure as a Board member of the Real Estate Commission, it was noted that few surety claim hearings were heard due to the fact that the Commission has limited access to the lone surety fund hearing officer, who is shared with another entity. She stated that AAR recommends that the Committee continue the \$10,000 surety bond level and allow time for a process to be developed to "fix the system so that the public is served." She argued that increasing the surety bond to \$20,000 would result in an increase in the number of claims filed which would escalate the problem regarding the scheduling of hearings.

Ms. Blackwell informed the Committee that AAR has, in place for its members, a mediation, arbitration, and professional standards hearing system that has conducted 60 hearings within the last year. She voiced optimism that some manner of processing hearings to better serve the public could be developed through a cooperative effort between the Commission, the Department of Community and Economic Development, and the AAR.

Co-Chair Wilken stated that when Amendment #3 is discussed, AAR's support of it would be noted.

Senator Dyson asked whether AAR supports the licensing of home inspectors.

Ms. Blackwell affirmed that it does.

Senator Dyson asked the methodology used by AAR to reach this conclusion.

Ms. Blackwell explained that AAR conducted a poll of its various boards and that information was provided to the AAR Legislative Committee, which consists of a minimum of one member from each of the other AAR boards. She noted that AAR has monitored, discussed, and provided input regarding the Home Inspector bill for approximately four years.

Senator Dyson asked whether 99 percent or 60 percent of realtors support the licensing of Home Inspectors.

Ms. Blackwell responded that the answer would depend on the area being polled as, she disclosed, the City and Borough of Juneau and several other communities in the State do not have either licensed or unlicensed home inspectors. She commented that, Juneau, for instance, instead utilizes licensed engineers as, she noted, it is felt that "their license was better than ours." However, she disclosed that access to licensed inspectors would be acceptable as their service would be less expensive than that of a licensed engineer. In summary, she surmised that a minimum of 75 to 80 percent of the Association's members support licensing Home Inspectors.

CHARLES SANDBERG, Realtor and Representative, Alaska Association of Realtors, testified via teleconference from Anchorage, and informed the Committee that he, a realtor for 17 years, was formerly the National Director of the National Association of Realtors and is currently a member of the Professional Standards Committee on the national, State, and local Anchorage Board and Association level. He also disclosed that he is an arbitrator on the AAR Hearing

Panel. This panel, he shared, is a very effective system that resolves disputes between both consumers and consumers and between consumers and realtor members. He stated that the AAR Hearing Panel is less expensive to operate and is more efficient system than the system utilized by the Commission and, in addition, has a 95-percent resolution history. In contrast, he avowed that the Surety Fund claim process is slow and resolves less than 10 percent of the claims that are filed. He stated that none of the fourteen Surety Fund claims that were filed in 2003 were heard, as compared to the AAR process in which 60 claims were filed and processed. Furthermore, he noted that the AAR system usually addresses and resolves disputes in two to four months; whereas, the Commission's hearing system process might require several years. Echoing Ms. Blackwell's comments, he urged that the Surety Fund claim limit be rolled back, via Amendment #3, from \$20,000 to \$10,000, and allow the appropriate parties to review and determine a more effective manner through which to deal with the issues.

Amendment #1: This amendment inserts new bill sections into the bill on page two, following line 20. The new language reads as follows.

Sec. 3. AS 08.18.071(a) is amended to read:

(a) Except as provided in (d) and (e) of this section, each [EACH] applicant shall, at the time of applying for a certificate of registration, file with the commissioner a surety bond running to a state conditioned upon the applicant's promise to pay all

(1) taxes and contributions due the state and political subdivisions;

(2) persons furnishing labor or material or renting or supplying equipment to the applicant; and

(3) amounts that may be adjudged against the applicant by reason of negligent or improper work or breach of contract in the conduct of the contracting business or home inspection activity, as applicable, or by reason of damage to public facilities occurring in the course of a construction project.

Sec. 4. AS 08.18.071 is amended by adding a new subsection to read:

(d) A general contractor or specialty contractor who is in compliance with the surety bond or deposit requirements of (a) and (b) of this section is not required to file another surety bond or increase a deposit with the commissioner when the general contractor or specialty contractor applies to be a registered home inspector. However, if the general contractor or specialty contractor subsequently is neither a general contractor nor a specialty contractor and becomes only a

registered home inspector, the home inspector shall provide a surety bond or deposit in lieu of the bond in the manner and amount required for registered home inspectors under this section.

(e) An applicant for, or holder of, a certificate of registration as a home inspector may, in lieu of filing with the commissioner a surety bond or deposit that meets the requirements of this section, file evidence satisfactory to the commissioner that the applicant is employed by a registered home inspector who is in compliance with the surety bond or deposit requirements of this section.

Co-Chair Green moved to adopt Amendment #1.

Co-Chair Wilken objected for explanation.

Co-Chair Green noted that one issue not resolved by the passage of HB 9, was how to deal with home inspectors who are not employees of a city or borough and who conduct the majority of the home inspections.

Co-Chair Green informed the Committee that by restoring some of the original language pertaining to home inspections, the amendments she would be offering today would assist in alleviating the unintended consequences resulting from the passage of HB 9.

Co-Chair Green stated that Amendment #1 "would correct" provisions established by HB9 that require each home inspector to be individually licensed, to provide a surety bond, and to have a general liability insurance policy. These requirements, she continued, require an individual to acquire "multiple bonding and insurance requirements" in such situations as when a home inspector business owner employs one or more persons who are also registered home inspectors, or when a general or specialty contractor also wishes to be a registered home inspector. She voiced the understanding that the current requirements result in multiple layers of requirements that are unnecessary in that they would not provide any additional protection. She stated that Amendment #1 would change the provisions so that an owner/home inspector's coverage would not be duplicated.

Ms. Seitz informed the Committee that Representative Rokeberg supports Amendment #1, as it would address the "dual bonding" concern. She exemplified that currently a specialty contractor who also desires to be licensed home inspector is required to acquire two bonds, and she continued, this dual bonding requirement also applies to a owner/employee situation in which both the employee and the owner are currently be required to have a bond.

Senator Dyson asked whether there is a national home inspector association.

Co-Chair Green understood that there is; however, she would defer to the industry to provide further information.

Senator Dyson specified that he "did not agree" with the State being involved in the licensing of home inspectors and, voicing support for "eliminating that entirely." He asked whether this amendment would eliminate the licensing requirement and replace it with a registration requirement.

Ms. Seitz responded that the amendment retains the requirements established by HB 9 that specify that a home inspector be required to register in a manner "similar to a license, but it's not called a license, it's called a registration."

Senator Dyson asked whether meeting the standards of the national organization would serve to qualify someone as a licensed inspector.

Ms. Seitz stated that once the transitional licensing period, that allows someone to be qualified in the profession based upon a certain number of years' experience, has expired a person would be required to pass certain examinations.

Senator Dyson asked whether the examinations would be administered by the State or by a professional organization.

Ms. Seitz responded that the tests would be administered by professional testing agencies.

Co-Chair Green referred to language in Section 2, subsection (a) (1) (A) on page one, line 13 through page two, line two, of the bill that reads as follows.

(A) existing home is the examination offered by the American Society of Home Inspectors, [AMERICAN HOME INSPECTORS TRAINING INSTITUTE,] or National Association of Home Inspectors;

Co-Chair Green noted that this legislation would require an applicant to provide additional information as denoted in Section 2, subsection (a)(3)(B), located on page two, line nine, that reads as follows.

(B) accompanied by documentation that the applicant has completed continuing education requirements established by the

department;

Co-Chair Green clarified that this amendment does not address the registration requirements as they are addressed elsewhere in the legislation.

Co-Chair Green stated that forthcoming Amendment #2 would address other issues that have resulted from the enactment of HB 9.

DAVE OWENS, Owner, Owens Inspection Services, testified via teleconference from an offnet site and explained that his business conducts both residential and commercial inspections. He discussed the "stumbling blocks" that he and his business have experienced as a result of HB 9's licensing requirements, in that, in addition to the "problematic" dual bonding requirement, he, who has been accredited in the home inspection business for numerous years, was denied his license because he had not been tested in all applicable categories within a year prior to his licensing application.

Mr. Owens also requested that the AS 18.56.300(c) provision, as would be addressed in a forthcoming amendment, remain in Alaska Housing Finance Corporation (AHFC) statutes.

Mr. Owens asked the Committee to address the dual bonding issue as well as to determine a method through which the Department of Community and Economic Development could recognize qualifying certifications in lieu of when a test was undertaken.

Senator Dyson asked for clarification that while Mr. Owens remarks referenced licensing requirements in his remarks, he was, in fact, speaking to the registering requirements.

Mr. Owens concurred that he was speaking in regards to the registration requirements.

Senator Dyson commented that although he would not require further discussion at this time, he would be interested, at some time, in further clarification between the difference in registration, certification, and licensing.

Co-Chair Wilken removed his objection.

There being no further objection, Amendment #1 was ADOPTED.

Amendment #2: This amendment deletes "Section 44(e), ch. 134, SLA 2003, is" and replaces it with "Sections 41, 42, 44(e), and 47, ch. 134, SLA 2003, are" in Section 11, page five, line two.

Co-Chair Green moved to adopt Amendment #2.

Co-Chair Wilken objected for explanation.

Co-Chair Green explained that this amendment would reestablish the AS 18.56.300 (c) provision, as earlier mentioned by Mr. Owens, that was repealed by HB 9. She noted that a home inspection is required for either the purchase of home through AHFC or for the implementation of a housing loan for residential housing constructed after June 30, 1992 with AHFC. She noted that AHFC ascertains that this would apply to approximately "thirty to forty percent of the market share of mortgage lending for single family residential dwellings." Furthermore, she noted that subsection (c) limited the liability of a home inspector performing the requirements of subsection (b) to gross negligence and intentional misconduct. Therefore, she stated, removal of subsection (c) served to "expose home inspectors to greater risk of legal actions against them for which a prudent business owner would require professional liability or errors and omissions insurance." Furthermore, she informed that this insurance is unavailable in Alaska, as confirmed by the Division of Insurance. Therefore, she stated, HB 9 required home inspectors to seek an unobtainable product. She stated that the bill's sponsor concurs with this amendment.

Co-Chair Wilken removed his objection.

There being no further objection, Amendment #2 was ADOPTED.

Amendment #3: This amendment deletes "one year" and replaces it with "three years" in Section 2, subsection (3)(A), on page two, line seven of the bill. The amended language would read as follows.

(A) within three years after passing the examination required under (1) of this subsection; or

In addition, the amendment would delete Section 6, on page three, lines 12 through 22, which proposes changes to the claim level associated with the Surety Fund.

Co-Chair Green moved to adopt Amendment #3. She stated that the first portion of the amendment would address Mr. Owens' concern regarding testing and registration time limitation requirements by increasing the one-year time window to a three-year window.

Co-Chair Green noted that the second portion of the amendment has been suggested by various individuals and would serve to delete the Senate Labor & Commerce bill's language pertaining to the Surety Fund.

Co-Chair Wilken objected for clarification.

Co-Chair Wilken requested that Amendment #3 be divided into Amendment 3A and 3B.

There being no objection, Amendment #3 was divided.

Amendment #3A: This amendment deletes "one year" and replaces it with "three years" in Section 2, subsection (3)(A), on page two, line seven of the bill. The amended language would read as follows.

(A) within three years after passing the examination required under (1) of this subsection; or

Co-Chair Green moved to adopt Amendment #3A.

REPRESENTATIVE NORM ROKEBERG, the bill's sponsor, concurred with the proposed language.

Co-Chair Wilken removed his objection.

There being no further objection, Amendment 3A was ADOPTED.

Amendment #3B: This amendment deletes Section 6 which is located on page three, lines 12 through 22 of the bill. The language being deleted reads as follows.

Sec. 6. AS 08.88.470 is amended to read:

Sec. 08.88.470. Findings and payment. At the conclusion of the commission's consideration of a claim made under AS 08.88.460, it shall make written findings and conclusions on the evidence. If the commission finds that the claimant has suffered a loss in a real estate transaction as a result of fraud, misrepresentation, deceit, or the conversion of trust funds or the conversion of community association accounts under the control of a community association manager on the part of a real estate licensee, the commission may award a claimant reimbursement from the real estate surety fund for the claimant's loss up to \$20,000 [\$10,000]. Not more than \$20,000 [\$10,000] may be paid for each transaction regardless of the number of persons injured or the number of parcels of real estate involved in the transaction.

Co-Chair Green moved to adopt Amendment #3B.

Co-Chair Wilken objected.

Co-Chair Green stated that the Senate Labor & Commerce committee adopted this language, and that there has been support for continuing the \$10,000 surety fund level.

Senator Bunde, Chair of the Senate & Labor Committee, asked whether the removal of the entire section would serve to eliminate the Surety Fund in its entirety.

Ms. Seitz responded that removal of this section would serve to retain the current language of the section; specifically, she stated, its removal would assure the continuance of the \$10,000 Surety Fund claim level.

Representative Rokeberg commented that he supports this amendment, as it would address the concerns raised by AAR. He echoed the comments regarding the limited availability of the hearing officer, and characterized the situation as not being "very workable." He stated that currently the Surety Fund could be utilized to reimburse injured parties for cases involving misrepresentation, fraud, or deceit. He stated that were the limit to increase to \$20,000, the cases would be "more appropriately addressed by the judiciary system" due to the high cost involved. He also noted that claims at that level should be adjudicated in the Court System rather than via the hearing office system. Furthermore, he opined, increasing the level to \$20,000 might result in an increase in the number of claims. He noted that separate legislation is being considered that would increase the current damages amount allowable in Small Claims Courts.

Representative Rokeberg stated that the Surety Fund was originally developed to "simplify the process to the consumer, but he opined, the system is currently "more complicated and more expensive," and that, in the case of a "frivolous claims," the licensee is "required to expend a large amount of money for legal fees in order to defend himself and achieve a dismissal." He concluded that increasing the amount of the Surety Fund would be wrong in that, in reality, the entire "system needs to be reformed" rather than "making it more attractive to go the wrong way." He acknowledged the AAR hearing process that allowed 60 cases to be addressed and rectified in a short amount of time.

Senator Bunde stated that he respectfully disagreed and objected to the amendment. He provided Members with a handout on Surety Bonds titled "A Selection of Other States with State Administered Real Estate Recovery Funds" [copy on file], that compares Alaska to other states. He noted that Alaska with a \$10,000 Surety Bond requirement is one of approximately four states with the lowest level. Furthermore, he declared that the majority of other states

have an established level of \$20,000 or more, which, he attested, has not "destroyed" their real estate industry.

Senator Bunde declared that the Committee should pay more attention to the recommendations of the Legislative Budget & Audit division. He pointed out that as specified in the aforementioned Legislative Audit report in Recommendation #1, on page 11, the \$10,000 claim limit was established in 1974 statute. Furthermore, he noted that the Surety Fund statute language was amended in 1998 to specify that licensees would not be required to pay a Surety Fund fee greater than \$125 to support the Fund. He also noted that Statute requires a minimum Surety Fund balance of \$250,000 and a maximum fund balance of \$500,000, and that the Commission determines a fee level to support these amounts. In addition, he noted that during the auditing period, the Fund balance maintained a level close to \$500,000. He stated that the current \$30 fee is sufficient to support the statute requirements. He declared that increasing the claim level to \$20,000 would have minimal impact on the licensee, and that consideration should be equally given to the impact on the consumer, as he continued, while the last five successful Surety Fund claim payments were at the \$10,000 level, all of those alleged losses exceeded that amount. Therefore, he supported the Audit's recommendation to increase the level from \$10,000 to \$20,000. He reiterated his objection to the amendment.

Representative Rokeberg informed the Committee that while the primary purpose of the Surety Fund is to support awards to consumers, it's secondary use is to provide funds for educational purposes such as those associated with a restructuring of a licensing law. He stated that the Fund balance is healthy due to the manner in which the fund's fees are managed.

Senator Olson asked whether the amendment would result in costing the consumer more or might serve to make the claim process more complicated.

Representative Rokeberg replied that the amendment would result in neither of these concerns, as it specially pertains to the ceiling on the level of a Surety Fund award that might be determined.

Representative Rokeberg declared that the Surety Fund would also be available to support any claim awarded by the Superior Court that fits the Fund's established criteria. He stated that the fund is there to protect the consumer against such things as "a fly-by-night builder." He reminded the Committee that testimony has been provided attesting to the fact that a higher award level might attract people as it might be viewed as "a pot of money."

Senator Bunde respectfully disagreed. He contended that passage of this amendment would cost the consumer, as he noted that the legal cost associated with pursuing a claim via the Superior System would be expensive, and that increasing the limit to \$20,000 would allow the claims to be addressed via the hearing process. Furthermore, he noted that \$10,000 is a small percentage of the cost of a home in today's market.

Senator Olson asked whether the sponsor agrees with Senator Bunde's comments.

Representative Rokeberg stated that while he does not agree with Senator Bunde's comments, he would agree that the level has not been adjusted for some time.

PAT DAVIDSON, Director, Legislative Budget & Audit, spoke to Recommendation #1 which recommends increasing the claim limit from \$10,000 to \$20,000. She stated that this recommendation was based on a review of claims submitted through the hearing process during the four-year audit period. All of those claims, she stated, exceeded \$10,000 and all but one was less than \$20,000. She stated that the recommendation is also based on the fact that the limit had not been raised since its inception in 1974. These facts, combined with the health of the Surety Fund and the fee limit of \$125, which assure that no excessive costs would be borne by a licensee, support increasing the claim limit increased to \$20,000.

Ms. Davidson shared that, in addition to the \$10,000 individual transaction limit, the Audit's recommends that the overall maximum limit be increased from \$50,000 to \$100,000 due to the fact that a licensee could be involved in multiple transactions. However, she noted that, unlike the supporting history regarding the individual claim levels, there was no history regarding the overall maximum limit.

Representative Rokeberg suggested that in order to address the inflation factor concern and the Audit's concerns, the individual claim limit could be adjusted to \$15,000.

Amendment to Amendment #3B: This amendment retains Section 6 and reduces the maximum amount of a Surety Fund claim from \$20,000 to \$15,000, as specified on page three, lines 20 and 21 of that section.

Co-Chair Green moved to adopt Amendment #3B, as amended.

There being no objection, Amendment #3B, as amended, was ADOPTED.

Representative Rokeberg noted that this legislation and its amendments were necessitated in order to address regulatory making process requirements. He stated that while he did not agree with many of those interpretations, they required addressing.

Co-Chair Green thanked the sponsor for his assistance in developing this legislation as it has addressed numerous constituent concerns

Co-Chair Green moved to report the bill, as amended, from Committee with individual recommendations and accompanying fiscal notes.

There being no objection, SCS CS HB 418(FIN) was REPORTED from Committee with zero fiscal note #2, dated March 25, 2004, from the Department of Community and Economic Development.

#hjr26

CS FOR HOUSE JOINT RESOLUTION NO. 26(FIN)

Proposing amendments to the Constitution of the State of Alaska relating to and limiting appropriations from the Alaska permanent fund based on an averaged percent of the fund market value.

This was the second hearing for this bill in the Senate Finance Committee.

Co-Chair Wilken stated that this Percent of Market Value (POMV) legislation would propose an amendment to the Alaska "Constitution that would limit appropriations from the Permanent Fund to five percent of the average of the market value of the Fund." He stated that CS HJR 26 (FIN), Version 23-LS1006\Z, is accompanied by a Division of Elections' fiscal note.

BOB BARTHOLOMEW, Chief Operating Officer, Alaska Permanent Fund Corporation, Department of Revenue, noted that this resolution is the result of approximately six years of effort on the part of the Permanent Fund Board of Trustees to provide a simpler method "to determine how much is available for appropriation from the Permanent Fund."

SFC 04 # 109, Side B 08:52 AM

Mr. Bartholomew informed the Committee that The Alaska Permanent Fund Board of Trustees supports the Version "Z" committee substitute.

AT EASE 8:53 AM / 8:54 AM

The bill was HELD in Committee.

[Note: HJR 26 was re-addressed later in the meeting.]

#hb417

HOUSE BILL NO. 417

"An Act amending the definition of 'project' in the Act establishing the Alaska Natural Gas Development Authority; and providing for an effective date."

AT EASE 8:54 AM / 9:14 AM

This was the first hearing for this bill in the Senate Finance Committee.

Co-Chair Wilken stated that this legislation, HB 417, Version 23-LS1494\A, would change the responsibilities of the Alaska Natural Gas Development Authority (ANGDA) "to include a review of the economic viability of a gas line to tidewater at a point at or near Cook Inlet."

REPRESENTATIVE MIKE CHENAULT, the bill's sponsor, stated that this bill would allow ANGDA to investigate the possibility of a gas line route to tidewater at a point at or near Cook Inlet. He noted that the citizens of the State voted in support of providing ANGDA with the authority to investigate the viability of developing a gas pipeline from Prudhoe Bay south to tidewater on Prince William Sound. He stated that enlarging that authority to encompass a route to the Cook Inlet area is important, and he noted that increasing the scope of the project would not negatively affect the original routing evaluation, and would in fact, "enhance it."

HAROLD HEINZE, CEO, Alaska Natural Gas Development Authority, testified via teleconference from Anchorage in support of the bill. He attested that this legislation would expand the Authority's authority to analyze a direct route to Cook Inlet in addition to its original charge of getting gas to Cook Inlet via some method. Furthermore, he stated that the Authority's analytical "feasibility" study method would allow this study to be added to the Authority's mission in an economically sound manner. He informed the Committee that, "regardless of what happened here," the Authority would be considering this alternative, as it would fall within the scope of its work to consider direct and indirect

routings.

BILL POPP, Kenai Peninsula Borough Oil and Gas Liaison, testified via teleconference from Kenai, and stated that the Borough supports passage of this legislation as it is believed that it would enhance the responsibilities of ANGDA as an entity of the State by allowing ANGDA "to perform with due diligence" by investigating a direct route to Cook Inlet in addition of the line to a point on Prince William Sound and the Spur Line from Glennallen to a Southcentral Distribution Grid. He declared that a clear and detailed explanation of routing economics is important to the success of the project. He stated that the project is faced with numerous economic obstacles and that expanding the project would be beneficial in finding the most viable route to make this project "a reality if the economics support it.

Senator Bunde understood that the project "would fall within the parameters" of ANGDA's mission as currently established, and as such, no additional funding would not be required.

STEVE PORTER, Deputy Commissioner, Department of Revenue, agreed with Senator Bunde's comment.

Co-Chair Green moved to report the bill from Committee with individual recommendations and accompanying fiscal note.

There being no objection, HB 417 was REPORTED from Committee with zero fiscal note # 1, dated February 15, 2004 from the Department of Revenue.

AT EASE 9:21 AM / 9:56 AM

#hjr26

CS FOR HOUSE JOINT RESOLUTION NO. 26(FIN)

Proposing amendments to the Constitution of the State of Alaska relating to and limiting appropriations from the Alaska permanent fund based on an averaged percent of the fund market value.

[Note: This bill was heard earlier in the meeting.]

Co-Chair Wilken noted that this bill, which is referred to as the Percent of Market Value (POMV) bill, is again before the Committee. He stated that the bill proposes to place an amendment to the Constitution on a Statewide ballot that would, were it approved, limit the appropriation from the Permanent Fund to five percent of

the average of the market value of the Fund. He reminded that CS HJR 26(FIN), Version 23-LS1006\Z is before the Committee.

BOB BARTHOLOMEW, Chief Operating Officer, Alaska Permanent Fund Corporation, Department of Revenue, shared that the Permanent Fund's Board of Trustees worked for approximately six years to develop this proposal in order to prepare the Fund for the future, both from an investment management perspective as well as "from the perspective of how to make a stable and predictable amount of money available to the Legislature if they desire to appropriate it." He stated that this House of Representatives' legislation is representative of the language proposed by the Board of Trustees. He stated that the bill would establish "a spending limit of five percent of the value of the Permanent Fund on an annual basis." He exemplified that were this methodology in effect for the next fiscal year approximately \$1.3 billion would be available for appropriation from the Fund.

Mr. Bartholomew shared that were the current calculation methodology in affect, and were the Legislature to require additional resources, in excess of \$4 billion could be available for appropriation.

Mr. Bartholomew stated that this legislation would assure that "the Permanent Fund is invested in long-term assets" with a goal of trying to provide a stable and predictable payout. He pointed out that one of the Board's concerns was to assure, were fiscal concerns to be experienced in the future, that one of the State's largest assets could be as productive as possible to assist in that effort. He stated that inflation proofing has been conducted for 22 years. He stated that this would be inherent to the system, were the spending limit in place. He stated that the goals of limiting spending; protecting the fund against inflation; and granting the Legislature and the public have a predictable payout in the future, would be achieved by this legislation.

Senator Bunde stated for the record, that passing this legislation, "while it might be a pre-cursor to some future activity that would use some of the earnings for supporting State services, just passing this does nothing to determine how the funds are spent."

Mr. Bartholomew confirmed Senator Bunde's comment to be correct. He stated that, "there's two major public policy issues regarding the Permanent Fund that ... are being discussed in the Legislature this year." The first, he noted, is the legislation regarding the Constitutional amendment regarding the Board of Trust's POMV proposal. This proposal, he opined, would serve to identify the method through which to determine what is available and to protect

the Fund for the future. He clarified that the POMV proposal would not change how the funds would be used, but would rather specify the amount that could be used. He advised that a separate bill, HB 298, would address how the Permanent Fund's money would be spent. He stressed that these are two separate issues.

Senator Bunde responded that the POMV proposal, were it approved, would allow future Legislators to either designate all the earnings calculated by the five-percent methodology, "as dividends or to take all the earnings and put them into funding State services or some combination thereof."

Mr. Bartholomew agreed that, "this Constitutional amendment would limit the annual amount available, subject to the Legislature."

Senator Hoffman asked regarding the intent of a Board of Trustee's POMV advertisement that had recently appeared in the Anchorage Daily News newspaper. He also asked how the advertisement was financed.

Mr. Bartholomew responded that the advertisement was paid for via the Permanent Fund Corporation's operating budget. He stated that the intent of the advertisement was to assist in educating the public regarding the POMV proposal as, he noted, such things as surveys indicate that, "there's still a high level of confusion in the public as to what is the proposal." He stated that due to the fact that "there's a lot of awareness and interest right now" in regards to the Permanent Fund, the Board viewed this "as an opportunity to provide education in as neutral a fashion" as could be done. Therefore, he concluded that the intent was, "in a simple way," to explain the difference between the current process and "the Percent of Market Value (POMV) or endowment approach."

Senator Hoffman recalled a previous Finance Committee discussion regarding the Board of Trustees' request for in excess of one million dollars to inform the public about POMV. He stated that the response from the Committee was unfavorable and that the request had been denied. Therefore, he asked why the Board was furthering this endeavor.

Mr. Bartholomew responded that "the request for both the authority to do advocacy and for the funding to do the education and outreach on POMV was because of the rule changes that take place" were the legislation passed by the Legislature. He stated that it was understood that, were the POMV proposal approved by the Legislature, the Board's ability to advocate for a Constitutional amendment would be restricted. He stated that, in his discussions with the Board, it was not "linked" that advertisements prior to

the Legislative approval of the proposal would be prohibited.

Senator Hoffman asked for confirmation that it was not the intent of the Board to get the public to apply pressure on the Legislature to support POMV, by running the advertisement.

Mr. Bartholomew assured that the advertisement was not intended to be a tool through which to lobby or influence passage of this legislation. He assured that the Board understands that the issue must be presented in a balanced fashion. He stated that aside from working directly with the Legislature on issues, it would be "inappropriate" for the Board to indirectly lobby the Legislature. Therefore, he continued, the Board viewed the advertisement as an educational tool.

Co-Chair Wilken complimented Mr. Bartholomew as being "good soldier and he was glad he worked for the people of Alaska."

Senator Olson characterized the response to the advertisement questions as "somewhat confusing, at best, if not "questionable."

Senator Dyson referenced the Permanent Fund Corporation's April 2004, "Percent of Market Value talking points" handout [copy on file] and stated that in the subsection titled "how does POMV provide the solution?" it is stated that, "The Fund is invested for a 5-percent real rate of return after inflation." He noted that he had previously asked regarding whether the language in Section 2(b) of the bill on page two, line two, meant that it was "indeed" going to be after inflation.

(b) Appropriations from the permanent fund 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.

Senator Dyson stated that in subsequent conversations, he had been "reminded that the whole thing is a smoothing operation" in that it was a five-year average. He recalled that he had asked whether any language had been considered "that would make it clear that the five percent that we are making available for appropriation is protected against the year that we might have high inflation, and actually, in a given year might be appropriating part of the real value of the corpus." He noted that the response was to the affect "that anything that we did along that line must be carefully worded so that it was over a board period because it would vary from year to year." Therefore, he re-asked whether language could be included to clarify that in any given year, the amount being proposed would "not dip into the principal," as he stated that, in addition to

preserving "the value of the principal," the people of the State must be assured that the principal would "be intact."

Mr. Bartholomew replied that the issue regarding whether the POMV would allow for the expenditure of the principal or corpus of the Fund, has had a lot of discussion. He stated that it has been determined that there are two methods through which to protect against eroding the Fund. First, he communicated, the concept of the word principal is included in Constitution through the "number that is the sum of all the oil contributions, all the inflation proofing appropriations the Legislature has done, and special appropriations." This number, he specified, currently amounts to \$23.5 billion, and "only goes up." He communicated that "the Legislature would not be allowed to appropriate any money that would reduce the Permanent Fund below that level."

Mr. Bartholomew shared that an issue raised by the Board, regards those times when there might be short-term extreme downturns in the stock market that might reduce the value of the Fund down towards the principal level. He stated that the Board determined that in those times, "it would not be prudent for the economy" not to distribute a Permanent Fund Dividend to the citizens. Therefore, he continued, the Board proposed an endowment method of not just the principal of the fund, but of the entire fund. Therefore, he stated that in order to respond to the question of how to assure the public that the corpus of the Fund would not be attached, the House of Representatives' legislation before the Committee has adopted a statutory limitation through which the Constitution would allow a five-percent of the total market value to be spent in any one year.

Senator Dyson understood that the language specifies market value as opposed to principal.

Mr. Bartholomew confirmed, and stated that this would include the entire fund including the principal and the excess earnings. He stated that this currently amounts to \$27.5 billion dollars. He stated that it is expected that the total rate of return would be eight-percent, including a three percent inflation factor. Therefore, he stated the real earnings of five-percent, after inflation, would be utilized over time.

Mr. Bartholomew stated that in question is how to assure that public that the principal would not be spent. He stated that there is a provision in HB 298-DISTRIBUTIONS OF APPROPS FROM PERM FUND, that, states that every ten-year period would be reviewed by the Corporation to assure that the fund has earned five-percent above inflation. Were this not to occur, he continued, the spending limit would be lowered to the real rate of return. Therefore, he

recommended that the expenditure not be viewed on a year to year basis "as there have definitely be years that the Permanent Fund has not make money;" however, he attested, there has never been a ten year period in which the five-percent level was not exceeded. Continuing, he stated that over the 25-year period that the Fund has existed, it has earned six-percent over inflation. He referred the Committee to a PFC graph titled "Rolling 10-year real return - Fiscal year" [copy on file]. He stated that "the Legislature has not spent anywhere near the available funds."

Mr. Bartholomew stated that the statutory limitation addresses Senator Dyson's concern. He stated that were a higher rate of protection desired, a Constitutional amendment would be required as opposed to the statutory limitation.

Senator Dyson understood that while appropriate inflation proofing could not occur in a year of double-digit inflation; an appropriation of up to five percent of the market value could continue to be made. Doing so, he contended, might result in a net loss of three to five percent of the Funds' market value that year.

Mr. Bartholomew replied that while this is correct, what makes this "allowable and prudent" is the fact that the rate of return for fiscal year 2004, for instance, is going to exceed the rate of inflation by ten percent. He stated that adoption of the POMV would limit the expenditures to five percent of the market value, which in this case would have grown in excess of ten percent. This, he attested "would serve to carry that money forward and over time," he stated, it is "believed that the good years would outweigh the bad" years. He stated that limiting the spending in the good years to five percent by retaining those excess earnings via the implementation of a spending limit, would serve to protect the Permanent Fund.

Senator B. Stevens pointed out that on the effective date of the amendment that sweeps the Earnings Reserve Account (ERA) into the Principal, as specified in Section 3 of the bill, the ERA would cease to exist. He stated that HB 298 would allow the Legislature to change the distribution of the five percent by a simple majority vote. Therefore, he declared that the concept of the distribution of the earnings "would be at the full discretion of future Legislatures, just as it is now," with the only difference being that the ERA is swept into the principal.

Co-Chair Wilken asked whether this legislation would allow for an FY 05 CBR draw.

Mr. Bartholomew replied that, as drafted, the POMV program would

not allow for an appropriation until July 1, 2005, which would be the beginning of FY 06. Therefore, he concluded the October 2004 Permanent Fund Dividend, which would occur in FY 05, is accounted for in the FY 04 operating budget. He noted, that unless there was a need for other appropriations "as written," that would be no other appropriations from the Permanent Fund until July 1, 2005. At that time, he continued, the appropriation would be limited to five percent, were POMV enacted.

Senator Bunde reiterated that there are Alaskans who are concerned that with the adoption of POMR, the Permanent Fund "would go away." He referred to the aforementioned Ten-year look back chart, and stated that while the past few years' stock market performance was dismal, the Fund still made five-percent including the recent years' worst-case scenario. Therefore, he observed that were the POMV in affect for the past ten years, the corpus would not have been used and any appropriation would have been limited to five percent.

Mr. Bartholomew responded that this is correct, and were the POMV five-percent spending limitation in place for the entirety of the Fund's history, the expenditures would not have exceeded what the Fund had earned above the rate of inflation. He reiterated the importance of viewing the Fund over a ten-year period verses a year-to-year basis. He noted that HB 298 would provide "guidance to the Legislature" to reduce the five-percent Constitutional spending limit appropriation down to the real earnings level were the average earnings of the Fund to fall below that five-percent level.

Senator Bunde stated that the Legislature currently appropriates between three and five million dollars of earnings, on an annual basis, from the Permanent Fund to inflation proof the account.

Mr. Bartholomew agreed that the Legislature, on an annual basis, appropriates money from the Fund's earnings account into the protected principal. He stated that under POMV, the earnings would be protected by the five percent limit, but would not subject to a future appropriation.

Senator Bunde stated therefore, that were the Constitutional amendment approved, the State would crease to appropriate up to five million dollars of Fund earnings each year.

Mr. Bartholomew stated that is correct. He stated that POMV would eliminate the Board's current concerns regarding inflation proofing the Fund when there are other fiscal pressures such as the need to find additional funds to support such things as education and transportation.

Senator Bunde pointed out that while "many people say, 'don't' spend the Permanent Fund," they do not understand that the Legislature already spends money to inflation proof the Fund and provide "for the Permanent Fund Dividend itself." He stated that using the POMV method to provide funding for State programs and Dividend checks, "would not change significantly the amount" currently being utilized from the Fund were inflation proofing factored into that amount.

Senator Hoffman stated that the Legislature could assess the earnings from the ERA and "spend those dollars with a simple majority today, but we haven't." He attested that the Legislature has not done this, but has rather chosen to take "the more difficult road" of balancing the budget by accessing the CBR, which requires a three-quarter vote of the Legislature, because they are aware that spending the Fund would be perceived by the people as "tapping into... and threatening the Fund."

Senator Hoffman continued that were the POMV program adopted, the Legislature could interpret it to state that the people have granted them the authority to spend the five-percent as needed. He stated that the POMV would provide no protection to the Permanent Fund Dividend. He stated the participants of the Conference of Alaskans stated they went one-step above and beyond what they were charged to do by stating that the Permanent Fund should be protected in the Constitution. Therefore, he stressed that consideration of protecting the Permanent Fund be provided were the POMV "management tool" to be adopted.

Senator Bunde stated that people could protect their PFD by supporting a person to represent them in the Legislature.

Co-Chair Wilken asked for clarification regarding whether the five-percent value of the fund is the value of the fund at a certain point of time over the last five-years, as specified in the bill in Section 2(b).

Mr. Bartholomew responded that the applicable rules in this regard as included in statute. He stated that the value of the Permanent Fund would be determined on June 30th of each year as that is the end of each fiscal year. He stated that in order to accommodate the "ups and downs of the financial markets, it's prudent to take an average of the previous five years." Therefore, he stated that this proposal would mandate that, on June 30th, an average of the previous five-years' market value of the Fund, would be determined based upon Generally Accepted Accounting Principals. That value, he continued, would then be multiplied by five-percent in order to

determine the amount that would be available.

Co-Chair Wilken understood therefore that this would equate to "five June 30's divided by five."

Senator Bunde moved to report the bill from Committee with individual recommendations and accompanying fiscal notes.

Senator Hoffman stated that his not objecting to the motion does not mean that he supports the proposal.

There being no objection, CS HJR 26(FIN) was REPORTED from Committee with \$1,500 fiscal note #3, dated January 16, 2004 from the Division of Elections and new zero fiscal note #4, dated April 13, 2004 from the Department of Revenue.

RECESS TO THE CALL OF THE CHAIR 10:33 AM / 5:06 PM

[NOTE: Due to an audio malfunction, the adjournment of this meeting was not recorded]

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ADJOURNMENT

Co-Chair Lyda Green adjourned the meeting at 05:07 PM.