

**ALASKA STATE LEGISLATURE  
SENATE JUDICIARY STANDING COMMITTEE**

Kenai City Hall  
October 28, 2003  
7:00 p.m.

**MEMBERS PRESENT**

Senator Ralph Seekins, Chair  
Senator Scott Ogan, Vice Chair  
Senator Johnny Ellis (via teleconference)  
Senator Hollis French (via teleconference)

**MEMBERS ABSENT**

Senator Gene Therriault

**OTHER LEGISLATORS PRESENT**

Representative Mike Chenault  
Representative Kelly Wolf

**COMMITTEE CALENDAR**

**SENATE JOINT RESOLUTION NO. 18**

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

HEARD AND HELD

**SENATE JOINT RESOLUTION NO. 19**

Proposing amendments to the Constitution of the State of Alaska relating to the Alaska permanent fund.

HEARD AND HELD

**PREVIOUS ACTION**

SJR 18 - See State Affairs minutes dated 5/1/03 and 5/6/03 and Judiciary minutes dated 5/15/03 and 6/26/03.

SJR 19 - See State Affairs minutes dated 5/13/03 and Judiciary minutes dated 5/17/03 and 6/26/03.

**WITNESS REGISTER**

Mr. Bob Bartholomew  
Chief Operating Officer

Alaska Permanent Fund Corporation  
PO Box 25500  
Juneau, AK 99802-5500

**POSITION STATEMENT:** Explained the Alaska Permanent Fund Corporation Board of Trustees' percent of market value proposal

Mr. Preston Williams  
Kenai, AK 99611

**POSITION STATEMENT:** Expressed concern that no fixed percentage amount is required for the dividend payout

Mr. C.A. Short  
Nikiski, AK

**POSITION STATEMENT:** No position at this time

Ms. Ruby Kime  
Ninilchik, AK

**POSITION STATEMENT:** Disagrees that Alaska has a fiscal crisis and believes the problem is overspending

Mr. James Price  
Nikiski, AK 99635

**POSITION STATEMENT:** Suggested allowing voters to vote on a constitutional spending limit and the POMV proposal

Mr. Jack Dean  
Sterling, AK 99672

**POSITION STATEMENT:** Opposed to any changes to the permanent fund program

Ms. Vicki Pate  
Nikiski, AK 99635

**POSITION STATEMENT:** Opposed to the POMV proposal and suggested allowing voters to vote on both SJR 19 and the POMV proposal

Mr. Malcolm McBride  
Kenai, AK 99611

**POSITION STATEMENT:** Prefers SJR 19 to SJR 18

Mr. Fred Sturman  
Soldotna, AK 99669

**POSITION STATEMENT:** Opposed to SJR 18

**ACTION NARRATIVE**

**TAPE 03-56, SIDE A**

**SJR 18-CONST. AM: PF APPROPS/INFLATION-PROOFING**  
**SJR 19-CONST. AM: PERMANENT FUND INCOME**

**CHAIR RALPH SEEKINS** called the Senate Judiciary Standing Committee meeting to order at 7:00 p.m. Senators Ogan and Seekins were present. Chair Seekins noted that Senator Therriault was out of state and Senators French and Ellis were participating via teleconference. He asked Representatives Chenault and Wolf to join the committee at the table. He informed members that Senator Lincoln introduced SJR 19 and she was invited to participate. He then asked Mr. Bartholomew to address the committee and noted that members' packets contain a copy of Mr. Bartholomew's PowerPoint presentation.

MR. BOB BARTHOLOMEW, Chief Operating Officer of the Alaska Permanent Fund Corporation (APFC), told members he would provide an overview of what the permanent fund looks like today and how the rules governing the permanent fund work, and describe the proposal recommended by the APFC Board of Trustees.

MR. BARTHOLOMEW told members the current statutory and constitutional authority of the permanent fund says the fund should be a means of conserving a portion of the state's revenue from its resources to benefit all generations of Alaskans. The APFC believes the current system has worked very well for the last 27 years, but that some weaknesses need to be improved upon. He said the proposal before the committee will help do exactly what the purpose statement purports: to benefit all generations, both current and future.

MR. BARTHOLOMEW said the permanent fund, as of June 30, 2003, contained roughly \$24 billion. Over the last four years, the amount has ranged from \$22 billion to \$26 billion, with a \$24 billion average. The fund has had earnings and a distribution each year.

The \$24 billion fund is made up of two components: the principal and the earnings reserve account. The earnings reserve account is the portion of the fund that is available to the Legislature for appropriation. On June 30, 2000, the earnings reserve account contained \$3 billion. That amount was the balance after dividends were paid and the fund was inflation proofed. On June 30, 2003, the earnings reserve account contained \$100 million. He pointed out the difference shows the volatility of the stock market over the last few years. He noted in the last few months the stock market has gone up, so the earnings reserve account is now worth close to \$400 million. The Permanent Fund Board of

Trustees is concerned about the amount of movement in that account, and believes that changes to stabilize it should be reviewed.

MR. BARTHOLOMEW said in 1978, 100 percent of the permanent fund was invested in bonds. The original permanent fund statutes were written in 1978 and 1980. Since then, the permanent fund has become a very mature, institutional fund with large assets. Its current investments include stocks, bonds and real estate. The original bonds paid interest on a regular basis; that interest was received monthly, accounted for, and was deposited into the earnings reserve account. Only 35 percent of the fund was invested in bonds in 2002, 10 percent was invested in real estate and the remainder was invested in U.S. and foreign stocks and fixed income from other countries, The permanent fund grows differently today. Based on the rules written over 20 years ago, one investment might be a shopping mall in Washington, D.C. and, although that property has increased substantially in value over 15 years, that increase will not be reflected in the earnings reserve account until the building is sold. The trustees propose that when the assets are increasing in value, a different formula should be used to determine how much is available from the permanent fund. The fund has matured and evolved over 25 years, and the trustees and their advisors believe the rules governing the fund must mature and evolve also.

MR. BARTHOLOMEW said the trustees have proposed using a percent of market value, known as the POMV. The POMV would establish a 5 percent spending limit on the amount that can be taken out of the permanent fund each year. He said the proposal actually says "up to 5 percent." That amount was determined after reviewing a study of over 650 college and university foundations and endowments throughout the country. Over 84 percent of those foundations and endowments use some form of a percent of market value. The percent ten years ago was 50 percent. He said the trustees came to recognize 5 percent as the appropriate amount because its policy goal with permanent fund investments is to earn a total return from all assets of 8 percent. He pointed out that the permanent fund has earned as much as 12 percent in one year but also lost money in 2001 and 2002. The 5 and 10 year averages over the last 20 years show about a 9 percent return.

MR. BARTHOLOMEW repeated the Permanent Fund Board of Trustees is shooting for an 8 percent return. The current projection for inflation is 3 percent, so the objective of the proposal is to retain enough money in the permanent fund to cover the effects

of inflation. Today, that amount is appropriated from the earnings reserve account by the Legislature each year. Under the new proposal, 3 percent of the 8 percent return will be used for inflation proofing, leaving 5 percent. The board of trustees believes 5 percent is the sustainable amount that can be paid out from the permanent fund each year. Inflation will vary, but what tends to happen to the capital markets when inflation is high is that the total return of investments goes up also. The Board of Trustees still would expect the bottom line of what the permanent fund will earn, on average, to be 5 percent, in addition to inflation, which is why it is recommending the spending limit be set at 5 percent. The fund will continue to grow for two reasons: enough earnings will be retained to offset inflation; and oil money will continue to be deposited each year.

MR. BARTHOLOMEW said the permanent fund has earned on average 7.8 percent per year during the last 10 years. Inflation has averaged 2.5 percent, giving an overall average growth of 5.3 percent. The fund has earned over 6 percent over the last 20 years after inflation. The board believes this proposal is an improvement. It will protect the fund for the future generation and make sure the benefits reach the current generation. It is an improvement because today the principal and earnings reserve are accounted for separately, although the entire fund is invested in the same way. The board proposes to eliminate the distinction between the principal account and earnings reserve account and create one account that is protected by a 5 percent spending limit. He said the first major policy call for the Legislature and the public is whether 5 percent should be the amount of the limit. The second policy call is whether "principal" should be eliminated from the Alaska Constitution and replaced with a 5 percent spending limit.

MR. BARTHOLOMEW said, regarding the second policy call, the POMV method would be more protective of the fund because the current rules allow the Legislature to appropriate the amount in the earnings reserve. Therefore, when the earnings reserve contained \$3 billion in 2000, the entire amount could have been appropriated. The Trustees believes during the good years, more money should be retained in the fund, not spent. That way, a distribution will still be available in the "down" years. He said it would also protect the option of having an annual payout. The primary use of that payout historically has been for dividends and inflation proofing. Allowing spending in the near term would spend into the fund during the "down" years, but the economy would be negatively affected by no distribution and the

amount spent could be made up over time. In addition, a lot more would be retained in the permanent fund over time, more than the amount to cover. The board feels it is important to not only have a spending limit during the good years, but also not to let it go to zero in the bad years. The board believes that will provide better protection for the future because the spending limit will not allow the Legislature to spend more now, leaving some for future generations.

MR. BARTHOLOMEW referred to PowerPoint slide 5, which shows how the permanent fund works and a four-year history of the amounts made available for the dividend. Those amounts have increased from \$800 million in 1998 to \$1.1 billion in 2000. This past year, \$691 million was made available. The projection for two years from now is \$490 million. He said the board would like to get away from that much fluctuation because it is difficult for the fund to manage that large of a change in the distribution. The proposed payout would stay right in the middle. He stated:

When the stock market was booming in 2000, we shouldn't have paid out as much money as we did. If the stock market has gone down for three years like it has, we shouldn't take a big dive where the economy, whether you're using the money for dividends, whether you're using some of the money for public services, you don't want to have a dramatic change from year to year as part of the plan for - it's hard for the economy to absorb that change. So, we would recommend that by basing the payout on the full value of the fund, the volatility of that payment skews out. It doesn't go up a lot in the good years, and it doesn't go down a lot in the bad years. When we look around the country at the other funds, that's what they need for their planning purposes. They want their governing boards, whether it's the board of trustees of the legislature, to be able to say on a reasonable level, how much money is available.

And to put it in perspective, I explained how much was spent out of the fund for dividends over the last four years and it varies from \$1.2 billion three years ago to two years from now \$490 million. Under this proposal, how much would be available in total from the permanent fund on an average year is between \$1.2 billion and \$1.3 billion. That's 5 percent of \$24 billion. That number would vary - if it varies by \$50

million in any one year, that would be a lot so it's much more stable than the current formula.

And I think, in closing, the board of trustees does support SJR 18. There's a similar version of the bill that has been introduced in the House and that, as it's written today, it accomplishes what the board believes is the best way to protect the permanent fund. The Governor said at his first state of the budget speech that he was going to evaluate and ask the board to look at it again. They spent three or four months reviewing it and the Governor has recently come out in support of the percent of market value again as a way to protect the permanent fund.

SENATOR OGAN commented that when most people think of the permanent fund, they think of their dividend check. They don't see the check as a product of the earnings of the permanent fund. He asked what to say to people with the perception that legislators just want to steal their money to spend more on government. He said the APFC has an uphill battle ahead trying to explain its proposal to people. He asked Mr. Bartholomew to explain how the dividend is paid and how this change will affect the dividend check.

MR. BARTHOLOMEW said the simplest way to explain that is to explain how it works today and how it would work under the proposal. He said today, a statutory formula is used that bases the amount on the cash earnings, not the total value of the fund; therefore it would not reflect an increase in the value of stocks. Every year, the APFC calculates how much money is available from the permanent fund and each year the Legislature decides how that money should be spent. The Legislature has put in statute how it wants to spend it this year. It wants to pay an amount of the earnings to the dividend and it wants to account for inflation. The weakness in the formula used to determine how much is available is that it is volatile. It chases the market up and down. Each year, the Legislature has decided whether or not to pay a dividend and it has. Under the proposal, the decision on how the earnings are used will remain with the Legislature each year. What will change is how much is available; that would be calculated by simply saying the Legislature can only spend up to 5 percent. He stated, regarding how it will affect the dividend:

There [are] two things I would say. We're not proposing to change how much goes to the dividend.

That is a decision that has to be made by the Legislature. But what we think it does do for the dividend is it assures that there will be money available each year from the permanent fund. So currently, if we have another short term sharp drop in the market, and that sharp drop only has to happen on June 30<sup>th</sup> because June 30<sup>th</sup> is the one day - we look at the permanent fund one day a year and that is when the calculation is made for what's available. So, if for the month of June the stock market took a dive, under the current formula we would get to June 30<sup>th</sup> and the formula would say sorry, there's nothing available. Under the proposal, we would look at the value of the fund and say 5 percent is available. So, in essence, it protects the ability to make a payout so it can improve the chances that there's money available. Without change, it doesn't affect how much should go to the dividend; it's limited to no more than 5 percent.

SENATOR OGAN said he believes many people feel they have a constitutional right to a dividend. It is important they understand that whether people receive a dividend is at the whim of the Legislature. He noted the will of the people has generally been honored with the exception of trying to make a run on it several years ago when 83 percent of the voters said no. He said he foresees a huge uphill battle to explain and answer to that 83 percent. He asked if this proposal will simply change the amount that is available to spend, but not change the dividend program.

MR. BARTHOLOMEW said that is correct. This proposal will limit how much can be taken each year but it also changes the Constitution to make sure that money is still available in the bad years.

CHAIR SEEKINS pointed out that he was a member of the APFC Board of Trustees in the 1990s and during that period of time, the board encouraged the Legislature to deposit some of the excess earnings reserve fund into the principal of the permanent fund, which the Legislature did. He asked if about one-third of the principal of the fund today is made up of additional funds from the earnings reserve account that were deposited into the principal by the Legislature, over and above the amount for inflation proofing and deposits from the oil fields.

MR. BARTHOLOMEW said that is correct. He added since 1980, under the current formula used to calculate the amount available, in addition to the Legislature appropriating money for the dividend, it also appropriated \$7 billion from the earnings reserve and deposited it into the restricted account.

CHAIR SEEKINS maintained the Legislature acted responsibly to make sure it did not have a big pot of money to use for "wild haired projects."

MR. BARTHOLOMEW said when he looks back at the testimony and the bills that were passed, the Legislature was looking toward a time in the future when the state would need the money more than it did at the time. He said when one looks at whether the Legislature was looking to benefit the current and future generations, it decided that it wanted to benefit the future generation more because it had enough money at the time. That is how the permanent fund got to be worth \$24 billion.

CHAIR SEEKINS referred to page 6 of the document, Realized Income vs. Market Value, that Mr. Bartholomew distributed and said one thing he learned when he was on the Board of Trustees is that a trustee could actually play God with the amount of money that became realized income. When something was sold, it became realized income and went into the profit formula for distribution. He asked if he is correct that the Board of Trustees can instruct the managers regarding what and when to sell in order to accomplish the realized income.

MR. BARTHOLOMEW said that is correct. He said the chart shows the volatility of the income versus the size of the fund over time, and that the income has been much more volatile. There have been situations in the past where the Board of Trustees felt the best thing to do for the permanent fund was to sell certain assets for various reasons. Those sales have a dramatic effect on the formula. The Board feels that should not be the case; it does not want to make decisions about what is right for the fund that then have a dramatic effect on the amount that is paid out. The Board would rather make the decisions based purely on what the best investment is and keep the formula for what is available separate.

CHAIR SEEKINS asked:

Let's say that all of the fund managers, or a large portion of them, came to the Board of Trustees, or the internal management did, and said look, we've got a

lot of money in unrealized income out there in the fund and we think that, you know, that we're going to have another Black October and the stock market is gonna crash. We think we should sell now and profit take now and put our money in a more stable investment. If they did that, took that profit, under the current scenario because it's a wise move for investment on the fund, it goes into the distribution process. Is that correct?

MR. BARTHOLOMEW said that is correct but a different way to say that is when the stock market was rallying and it only happened one time, the permanent fund managers generally should not be involved in trying to time whether the markets are good or bad. The permanent fund is invested for the long term. He said in 1996 or 1997, the Trustees looked at the unrealized gains in the stock portfolio and decided to sell after three or four meetings so that the current generation would receive some of the distribution. About \$300 million in gains were realized from the stock portfolio. The Board, however, repurchased that stock in the next few months. The Board incurred some transaction costs but it felt they struck the best balance. He said the Board would have never made that decision under the new proposal. It would not have had to because part of that asset growth would be shared with the current generation because they would have received 5 percent of the total fund. He pointed out that is why he said the investing strategy has changed but the rules have not. The Board feels it is prudent to change those rules to make them match the change in investment strategy.

CHAIR SEEKINS said, according to statute, the trustees serve at the pleasure of the Governor. They are not confirmed by the Legislature and can be removed for any purpose at any time as long as they are notified in writing. He said he personally believes that is a dangerous situation for a trustee who has investment responsibility and can tell the managers to sell, as happened in 1996, to put money into the distribution system to pump up the permanent fund dividend. He said virtually one person could control, under the current formula, what becomes realized earnings, that being the Governor. He said Governor Murkowski broke the cycle of replacing board members when he took office. He retained the board members for their term of office, regardless of their political affiliation. He said he sees the volatility shown in the chart as politically driven, as well as market driven. He asked if it would be beneficial to limit the political volatility of the permanent fund.

MR. BARTHOLOMEW said yes but the Board of Trustees looks at it from an investment perspective and believes [the POMV] will limit the investment volatility. He said the political volatility is an issue that the Board has dealt with. Changing the formula could reduce the political volatility.

CHAIR SEEKINS commented that the statutory formula could be changed by the Legislature at any time with a 51 percent vote.

MR. BARTHOLOMEW agreed and said the Constitution requires a vote of the public. The statutes that describe how to determine the amount available can be changed by the Legislature.

SENATOR OGAN said to his recollection, the only thing the Legislature used permanent fund earnings for, with some very minor exceptions, was to give funds to the Department of Natural Resources to help get more oil developed.

MR. BARTHOLOMEW repeated the calculation of how much should be spent on the dividend is set in statute. Once that amount is calculated, the APFC makes two transfers. A transfer of approximately \$35 million goes to two or three state agencies to cover adverse effects of the dividend. Certain social service programs are based on income. The Legislature decided to hold people harmless. That amount comes out of the dividend calculation and is paid directly to people who lost some income because of the dividend. Then, 100 percent of all other spending out of the permanent fund has been on the dividend program. He said he believes the historical track record of the Legislature has been very good. He pointed out the Board is trying to look ahead five or ten years. The Board believes this proposal is important because the pressures on the finances and budget of the state are going to change. The state has used its constitutional budget reserve (CBR) fund to cover revenue shortfalls. That fund may be empty in four or five years. When the pressure comes, the Board is concerned that the funds used to inflation proof the permanent fund could be at risk. The board believes that when pressure comes to bear and there is no other reserve money to cover the budget, the Legislature will have to decide whether to inflation-proof the permanent fund or pay for education. The board wants a spending limit and inflation proofing before the Legislature determines what amount is to be spent to ensure that the fund is protected. He repeated this proposal is aimed at that future pressure.

CHAIR SEEKINS said the Senate Judiciary Committee passed a resolution supporting a constitutional spending limit. That

resolution is now in the Senate Finance Committee. The legislature would also like to see some sort of restraint on expanding the budget. He said, regarding the hold harmless clause, he is surprised that very few people understand that the dividend knocks some people off of the welfare roles because their income has increased. The Legislature sends three months of welfare payments to the federal government so that it will continue to send the welfare checks to recipients.

MR. BARTHOLOMEW said he believes those guidelines are in statute and under the purview of the Legislature.

SENATOR ELLIS, testifying via teleconference, asked the number of participants in the audience.

CHAIR SEEKINS estimated around 50 people.

SENATOR FRENCH, testifying via teleconference, asked if the return on the investments of the fund was zero percent for five years in a row, and five percent was paid out to the Legislature every year, whether the fund's value would decrease by 25 percent.

MR. BARTHOLOMEW said that is correct. He said if this proposal is adopted by a vote of the public and the investment return was zero percent for the next five years, the Legislature would have to decide annually how much it wanted to spend, up to five percent. If the Legislature spent five percent each year, the fund would decline.

SENATOR FRENCH said if 5 percent is paid out for inflation proofing and dividends, the fund would decrease by about 25 percent; therefore, in today's dollars the permanent fund would contain \$18 billion.

**TAPE 03-56, SIDE B**

CHAIR SEEKINS clarified the language on line 4 on page 2 says the amount may not exceed 5 percent. He said if Senator French saw that kind of trend and wanted to continue to spend five percent, he would have a hard time getting anyone to join him.

MR. BARTHOLOMEW said Senator French was pointing out that is one of the biggest public policy decisions to be made on this proposal. The Legislature will have to compare this proposal to the alternative, which is the status quo. Under

today's method, if, as Senator French described, the permanent fund earns nothing for the next five years, not one penny would be paid out of the permanent fund and it would still amount to \$24 billion. He said the Legislature could still have the POMV proposal, with the caveat of not removing the word "principal" from the Constitution. That would create the 5 percent spending limit on the upside so that the Legislature would not overspend in the good years, but there would be no benefit in the down years. He explained:

You would hit the zero mark, you'd have zero earnings, and there would be no payment from the permanent fund and if that was the will of the people, that's how the economy of Alaska would run. It would go good in the good years and it would be really bad in the bad years - and the Board struggled with that. When they first adopted this proposal four years ago, the word 'principal' was left in the Constitution. They studied it for two more years and it was the bad markets that changed their minds. They first adopted the proposal in the heydays, in the good years. They wanted a spending limit and that made sense but they didn't want to deal with the downside because 'principal' has become known as a very important thing for people - protecting the principal of the permanent fund. But they studied it for two more years, and they also felt that they looked around the country and how the big funds operate and having large endowments that don't pay out any money also has some negative consequences. They believe that the benefit of having the opportunity to spend money in the bad years, so that you didn't go to zero, outweighed that you could spend into the fund in the short term. They took a long-term view and believe two things.

One, as we said, over the last 20 years, we have reinvested over \$7 billion of earnings so we have not overspent in the good years. We've kept it. If it goes down the next three, four, five years, should we dip into the fund that we've saved for the last 20 years? That's an important policy call.

CHAIR SEEKINS interjected, "Or, we could cherry pick the fund in the bad years and still have realized income that's available for distribution. That's very easy to do." He said if the market was flat, the investments that have an unrealized gain could be cherry picked. That, in effect, would take money out of the fund by converting good investments into realized gains and holding those that have not been good investments.

MR. BARTHOLOMEW said that is correct. Under today's rules, selling assets could create income. The Board feels that is not a good position to be in.

CHAIR SEEKINS thanked Mr. Bartholomew for his presentation and took public testimony.

MR. PRESTON WILLIAMS, testifying on his own behalf, commented that he sees some benefit to imposing the 5 percent spending limit. He expressed concern that no portion of the 5 percent will be required to be set aside for the payment of dividends, such as 2 percent. He maintained that he would be more apt to support the proposal if it contained a fixed percentage for dividends. He noted, "Again, if you're in zero budgeting and you're losing money, then it would be zero that would be invested. I think the people realize if the permanent fund's not making money, they won't get a dividend." He again expressed concern that the proposal contains no guidelines to protect the dividend.

MR. WILLIAMS also noted that the Legislature will no longer be putting 50 percent [of royalty revenue] into the permanent fund. It will be depositing 25 percent, so the principal will not be growing as fast as it has since 1980. He asked how much that difference will be.

CHAIR SEEKINS said about \$40 million.

MR. WILLIAMS said his guess is that 3 percent of the 5 percent will be used to address budget constraints, along with the extra \$40 million. He said his second concern is that the permanent fund was originally created as a rainy day account and that a catastrophic event could occur, such as another earthquake. If this change is made in the Constitution, the Legislature could only spend up to 5 percent without another vote of the people. He cautioned that might not be wise.

MR. C.A. SHORT, a resident of Nikiski, testifying on his own behalf, said the argument in support of the proposal sounds good

but he would like more time to consider it. He said he would send the committee a letter with his position.

SENATOR OGAN told members he is probably one of the most mistrustful people when it comes to giving legislators more access to the permanent fund. He said the jury is still out in his mind on this proposal. Although the proposal makes sense, one has to consider the law of unintended consequences. He said legislators have had a history of wanting to get their hands on the excess earnings to fund more government. This proposal does not change the fact that the dividend will still be at the whim of the legislature.

MS. RUBY KIME, a resident of Ninilchik testifying on her own behalf, said the legislators and media have put a message out that the State of Alaska is short of money. She disagrees. As of 2001, according to the U.S. Census Bureau, the State of Alaska spent \$14,270.27 per person. The State takes in \$9,756.97, leaving a difference of about \$5,000 per person. She said elected officials never want to discuss that information. She noted the Census Bureau provides the same statistics for every state. The State of Alaska spends three times as much per person than the State of New York. She said the only way to reign in politicians is to take away their money. She further submitted that the State had its first budget in 1961. Roads were cleared, children learned in school, the state had a legal system. If one extrapolates that budget adjusted for inflation, \$257 spent in 1960 per person per person would equal \$1579 in 2003. She said the State is spending 10 times that amount of money now. She does not trust that the POMV is the way to go without requiring that the dividend and inflation proofing be paid. She suggested passing SJR 19 instead of SJR 18, because SJR 19 contains those requirements.

MS. KIME referred to pages 81 through 83 of a document entitled, 2001 Consolidated Annual Financial Statement, and said it shows 116 programs have cash in the bank. Of the 116 accounts, 39 are in the general fund. She said the remaining 67 other funds are never discussed. They all have money and that money should be used for state operations, it should not be "squirreled" away. Government is not a for-profit enterprise.

SENATOR OGAN commented, "God help us when Senator Stevens is no longer in the Senate because we're going to have a serious recession."

MS. KIME agreed that Senator Stevens brings a lot of money into the state but those funds always have strings attached. Those funds also create programs that never end.

CHAIR SEEKINS stated that \$5,000 per person equals \$3 billion per year and the state does not have a \$3 billion deficit, partly because federal funds are not accounted for in the state budget. He said the people of the state are not incurring an additional \$5,000 per person debt. He said the draw on the [constitutional budget reserve] account last year was a little more than \$300 million. He said the question will always be where to make the budget cuts.

MR. JAMES PRICE, a resident of Nikiski testifying on his own behalf, said he believes the POMV plan may work very well for universities and companies that rely on their investments as a funding mechanism. That is what he finds most frightening about a POMV plan for the permanent fund. He believes it will invite more legislative appropriation. He said he thinks the first year this plan is put into effect, the Legislature will immediately appropriate funds directly from the permanent fund. He does not believe that will ever cease or diminish. He has heard candidates say during every election campaign they would cut the budget and have a long-range budget plan. That has not happened in any meaningful way. He said the POMV plan would be wonderful if it contained constitutional protection against legislative spending. He said he has no problem with the current program because the principal is inflation proofed first. He said the dividend is currently calculated on a five-year average, which has removed some of the volatility. He sees the problem as more pressure on the Legislature from special interests, a result of legislation last session that allowed campaign contributions to double and changed the definition of lobbyist so that lobbyists can contribute to legislators. He said that has created a meaningful threat to getting any budget reductions or a long-range budget plan because of more influence by special interest groups. He said the POMV plan would be the death knell to the permanent fund and the dividend. He commended Representative Chenault for sponsoring HJR 3, which would constitutionally protect the permanent fund from legislative appropriation. He encouraged the Legislature to let Alaskans vote on both constitutional protection and the POMV plan.

REPRESENTATIVE CHENAULT pointed out that lobbyists cannot donate to any legislator outside of their districts.

MR. PRICE said the new definition of lobbyist is someone who lobbied for 10 hours in one month, a change from 30 hours.

[The committee discussed the changes to the lobbyist law and noted that Mr. Price was incorrect.]

REPRESENTATIVE CHENAULT said everyone talks about wanting to protect the permanent fund and he has not made his mind up on the POMV proposal. He sees some advantages to it simply because it will prevent the ups and downs and level out the amount of the dividend. He noted the Legislature decides right now whether to inflation proof the permanent fund every year. He said his concern is that at some point in time, if the Legislature does not look at a spending limit, does not institute any other revenue source, such as an income tax, the only pot of money that will be available is the permanent fund dividend money. He hopes that does not happen but fears it will if government is not curtailed or another revenue source is not established.

MR. JACK DEAN, a resident of Sterling testifying on his own behalf, thanked Mr. Bartholomew for his fine presentation. He said he was alarmed when Mr. Bartholomew said Governor Murkowski supports the POMV proposal. He said if Governor Murkowski supports this resolution, there is probably something wrong with it. He said he prefers to leave the permanent fund alone.

MS. VICKI PATE, a resident of Nikiski testifying on her own behalf, said in the year 2000, she opened up a Roth IRA in the S&P stock index fund and quickly lost money. She said her point is that she believes it is a good thing that the permanent fund value fluctuates up and down. She said a steady 5 percent would create a disconnect from the permanent fund: people would no longer worry about how well the fund is being invested. She agreed with Mr. Price that both the POMV proposal and SJR 19 should be put before the voters. That would give Alaskans an actual choice and foster good discussion.

MR. MALCOLM MCBRIDE, a resident of Kenai testifying on his own behalf, said he believes SJR 19 contains much better provisions than SJR 18. He recommends that members support SJR 19, not SJR 18. He said if the concern is the volatility of the stock market, the Board of Trustees might consider returning to less volatile investments. He said the permanent fund has not been broken, but if it is going to be fixed, he prefers SJR 19.

MR. FRED STURMAN, a resident of Soldotna testifying on his own behalf, said in his experience as a stockholder, he has never

seen anyone make a profit until a stock was sold so the 5 percent market value will not be a true representation of the profits made. He said he is opposed to the POMV proposal. If the permanent fund is not making any money, he does not think a dividend should be paid. He said although the Legislature deposited an additional \$7 billion into the permanent fund, that amount should have been closer to \$15 or \$20 billion. He said a lot of money is being wasted in Juneau and that he has suggestions about budget cuts.

SENATOR OGAN asked Mr. Sturman to forward those suggestions to his office staff.

MR. STURMAN said about 10 to 15 people spent almost 400 hours devising a list of budget cuts that they sent to the Governor and Lt. Governor. He was dismayed by the fact that no one has acknowledged receipt of that list.

CHAIR SEEKINS said he agrees with Mr. Sturman that a profit cannot be realized until an investment is sold. He asked Mr. Sturman if he is willing to let the six members of the Board of Trustees of the permanent fund decide when to sell an investment to realize a profit.

MR. STURMAN said that is the only choice available. He added:

I hate to see six men taking care of 26 or 25 or 28 billion bucks. I would rather see six men taking care of 5 or 6 billion, maybe a group taking care of the real estate, you know?

CHAIR SEEKINS said portions of that the money are parceled out to management firms and they report back to the Board of Trustees. He said he was a member of the Board of Trustees and knows that the board can decide when to sell to determine whether a profit is realized. Using the POMV proposal, they would still have to sell something to pay out that money. He said his concern is that he wants to remove the political volatility out of when the board converts something into a realized gain. He asked Mr. Sturman to get back to him with some comments on that problem.

REPRESENTATIVE WOLF asked Mr. Sturman to provide him with a copy of the list of budget cuts also.

MR. STURMAN told members how to get a copy and said the list also contained suggestions to increase revenue.

CHAIR SEEKINS noted as a car salesman, he knows that one can't make a profit until a sale is made.

MR. STURMAN said that is why he cannot see how Mr. Bartholomew can say that the payout could be 5 percent if there is no profit.

CHAIR SEEKINS said the proposal assumes an 8 percent profit.

MR. BARTHOLOMEW said that is food for thought but said he would like to use Ms. Pate's situation as an example. He noted that she invested in an S&P index fund with the hope that her investment would grow over time. Some of that growth would come from dividends and some would come from an increase in the value of the stocks. He said most people normally buy an index fund to hold. If Ms. Pate just held that investment for 30 years and it increased in value to \$10,000, under the rules of the permanent fund today, she could not take a penny of that. She might then be 75 years old and need \$200 per month to supplement her income. However, the rule says she must sell her index fund before she can take any money from it. Therefore, she keeps saving it until she's 100.

MR. BARTHOLOMEW said his point is that dividends could be kept in cash or reinvested and the value of the asset would increase. The Board is trying to find a formula that allows a benefit from both. In other words, Ms. Pate would be able to sell a portion of her index fund to generate cash. Whether that one year the index fund went up or down should not matter in the long term. He said the permanent fund managers are always buying and selling, and have made money overall. However, the Board has a long-term philosophy of holding assets so it does not want to have to always sell long-term investments. It might want to sell the poor performing investments to pay the dividend. He said the Board is looking for a formula that works not only when investments are sold. He agreed that if money is not made, it should not be paid out but that is why the constitutional amendment limits the amount to 5 percent. He said he truly believes that if the permanent fund lost money for 5 to 10 years in a row, legislators who voted to spend 5 percent during those years would be voted out of office.

**TAPE 03-57, SIDE A**

CHAIR SEEKINS explained that a good deal of the money in the permanent fund now came as the result of being invested in the

equity market. He said the Legislature was responsible for telling the Board of Trustees what the asset allocation of the permanent fund board could be. He said he was frustrated at times as a trustee because without any appreciable greater risk, the fund could have gotten a greater return but the Legislature has imposed a rather conservative investment philosophy. Over the years, the Legislature has allowed a larger percentage to be invested in the equities market. He noted that when the fund was invested only in government securities, there was virtually no growth.

MR. STURMAN asked if that will change if the Constitution is amended.

CHAIR SEEKINS said the Board of Trustees will still be constrained by the policy set by the Legislature. The bonds must be of a certain rating.

MR. BARTHOLOMEW said only 55 percent of the permanent fund is invested in stocks, which is less than most funds. He said the difference between investing 100 percent in bonds with an assured cash flow, is that the fund would get a lower return.

SENATOR OGAN noted that he voted against increasing the equity allocation to 55 percent when the Board of Trustees made that request to the Legislature.

REPRESENTATIVE WOLF told members he has not made a decision on the POMV proposal yet and attended the meeting to listen to others' comments.

REPRESENTATIVE CHENAULT told participants that he takes all comments seriously and appreciated their attendance.

SENATOR FRENCH also thanked participants.

CHAIR SEEKINS also thanked participants. He said his intent as a legislator is exactly the same as it was when he was a trustee, that being to return the greatest amount of profit to Alaskans through the investments that the permanent fund board makes. He said it is inherent within that system, through the political process, that legislators know how [the people] want that income to be distributed. He said the biggest responsibility of the trustees is to return the greatest amount of profit and the responsibility of the Legislature is to make the fiscal decisions. He said although the Legislature was tempted to use the earnings from the fund in the past, it acted responsibly but

he expressed concern that the situation will be different in the future. He then adjourned the meeting at 8:49 p.m.