

**ALASKA STATE LEGISLATURE**  
**SENATE JUDICIARY STANDING COMMITTEE**

February 27, 2004  
8:00 a.m.

TAPE(S) 04-10 & 11

**MEMBERS PRESENT**

Senator Ralph Seekins, Chair  
Senator Scott Ogan, Vice Chair  
Senator Gene Therriault  
Senator Johnny Ellis  
Senator Hollis French

**MEMBERS ABSENT**

All members present

**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.

MOVED CSSJR 18(STA) OUT OF COMMITTEE

SENATE JOINT RESOLUTION NO. 19

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

MOVED CSSJR 19(JUD) OUT OF COMMITTEE

SENATE JOINT RESOLUTION NO. 24

Proposing amendments to the Constitution of the State of Alaska to guarantee the permanent fund dividend, establishing the earnings reserve account, and relating to the Alaska permanent fund; and providing for an effective date.

MOVED CSSJR 24(JUD) OUT OF COMMITTEE

SENATE JOINT RESOLUTION NO. 32

Proposing amendments to the Constitution of the State of Alaska relating to appropriations from the Alaska permanent fund to be used for a program of dividends for all state residents and providing a conditional effect and effective date for the amendment.

MOVED CSSJR 32(JUD) OUT OF COMMITTEE

**PREVIOUS COMMITTEE ACTION**

BILL: SJR 18

SHORT TITLE: CONST. AM: PF APPROPS/INFLATION-PROOFING

SPONSOR(s): RULES BY REQUEST OF LEG BUDGET & AUDIT BY REQUEST

04/17/03 (S) READ THE FIRST TIME - REFERRALS  
04/17/03 (S) STA, JUD, FIN  
05/01/03 (S) STA AT 3:30 PM BELTZ 211  
05/01/03 (S) Heard & Held  
05/01/03 (S) MINUTE(STA)  
05/06/03 (S) STA AT 3:30 PM BELTZ 211  
05/06/03 (S) Moved CSSJR 18(STA) Out of Committee  
05/06/03 (S) MINUTE(STA)  
05/07/03 (S) STA RPT CS 1DP 3NR NEW TITLE  
05/07/03 (S) NR: STEVENS G, DYSON, GUESS;  
05/07/03 (S) DP: COWDERY  
05/13/03 (S) JUD AT 8:00 AM BELTZ 211  
05/13/03 (S) Scheduled But Not Heard  
05/14/03 (S) JUD AT 0:00 AM BELTZ 211  
05/14/03 (S) -- Meeting Postponed to 5/15/03 --  
05/15/03 (S) JUD AT 8:45 AM BELTZ 211  
05/15/03 (S) -- Meeting Rescheduled from 5/14/03 --  
10/28/03 (S) JUD AT 7:00 PM Kenai  
10/28/03 (S) CONST. AM: PERMANENT FUND INCOME  
10/29/03 (S) JUD AT 7:00 PM Mat-Su LIO  
10/29/03 (S) CONST. AM: PERMANENT FUND INCOME  
10/30/03 (S) JUD AT 7:00 PM Anch LIO  
10/30/03 (S) CONST. AM: PERMANENT FUND INCOME  
01/21/04 (S) JUD AT 8:00 AM BELTZ 211  
01/21/04 (S) -- Meeting Canceled --  
02/09/04 (S) JUD AT 8:00 AM BUTROVICH 205  
02/09/04 (S) Heard & Held  
02/09/04 (S) MINUTE(JUD)  
02/27/04 (S) JUD AT 8:00 AM BUTROVICH 205

BILL: SJR 19

SHORT TITLE: CONST. AM: PERMANENT FUND INCOME

SPONSOR(s): SENATOR(s) LINCOLN

05/02/03 (S) READ THE FIRST TIME - REFERRALS  
05/02/03 (S) STA, JUD, FIN  
05/13/03 (S) STA AT 3:30 PM BELTZ 211  
05/13/03 (S) Moved Out of Committee  
05/13/03 (S) MINUTE(STA)  
05/14/03 (S) STA RPT 1DP 3NR

05/14/03 (S) NR: STEVENS G, COWDERY, DYSON;  
 05/14/03 (S) DP: GUESS  
 05/16/03 (S) JUD AT 1:00 PM BELTZ 211  
 05/16/03 (S) Scheduled But Not Heard  
 05/17/03 (S) JUD AT 10:00 AM BELTZ 211  
 05/17/03 (S) Heard & Held  
 05/17/03 (S) MINUTE(JUD)  
 10/28/03 (S) JUD AT 7:00 PM Kenai  
 10/28/03 (S) Heard & Held  
 10/28/03 (S) MINUTE(JUD)  
 10/29/03 (S) JUD AT 7:00 PM Mat-Su LIO  
 10/29/03 (S) Heard & Held  
 10/29/03 (S) MINUTE(JUD)  
 10/30/03 (S) JUD AT 7:00 PM Anch LIO  
 10/30/03 (S) Heard & Held  
 10/30/03 (S) MINUTE(JUD)  
 01/21/04 (S) JUD AT 8:00 AM BELTZ 211  
 01/21/04 (S) -- Meeting Canceled --  
 02/09/04 (S) JUD AT 8:00 AM BUTROVICH 205  
 02/09/04 (S) Heard & Held  
 02/09/04 (S) MINUTE(JUD)  
 02/27/04 (S) JUD AT 8:00 AM BUTROVICH 205

BILL: SJR 24

SHORT TITLE: CONST AM: GUARANTEE PERM FUND DIVIDEND  
 SPONSOR(S): SENATOR(S) OGAN

02/04/04 (S) READ THE FIRST TIME - REFERRALS  
 02/04/04 (S) JUD, FIN  
 02/27/04 (S) JUD AT 8:00 AM BUTROVICH 205

BILL: SJR 32

SHORT TITLE: CONST AM: PERM FUND INCOME FOR DIVIDENDS  
 SPONSOR(S): SENATOR(S) ELTON

02/16/04 (S) READ THE FIRST TIME - REFERRALS  
 02/16/04 (S) JUD, FIN  
 02/27/04 (S) JUD AT 8:00 AM BUTROVICH 205

**WITNESS REGISTER**

Mr. Robert Storer  
 Executive Director  
 Alaska Permanent Fund Corporation  
 PO Box 25500  
 Juneau AK 99802-5500

**POSITION STATEMENT:** Answered questions about the percent of market value

Senator Kim Elton  
Alaska State Capitol  
Juneau, AK 99801-1182

**POSITION STATEMENT:** Sponsor of SJR 32

Mr. Mark Stopha  
Staff to Senator Lincoln  
Alaska State Capitol  
Juneau, AK 99801-1182

**POSITION STATEMENT:** Testified for the sponsor of SJR 19

Mr. Mark Gnadt  
Staff to Representative Croft  
Alaska State Capitol  
Juneau, AK 99801-1182

**POSITION STATEMENT:** Answered questions about SJR 19

Ms. Mary Griswold  
Homer, AK

**POSITION STATEMENT:** Supports SJR 18 and SJR 32 combined

Mr. Mark Newman  
Big Lake, AK

**POSITION STATEMENT:** Supports maintaining the status quo of the permanent fund

Mr. Roger Gay  
Big Lake, AK

**POSITION STATEMENT:** Opposed to inflation proofing the permanent fund

#### **ACTION NARRATIVE**

#### **TAPE 04-10, SIDE A**

**CHAIR RALPH SEEKINS** called the Senate Judiciary Standing Committee meeting to order at 8:03 a.m. All members were present. Chair Seekins announced that he planned to review all four resolutions before taking any action of them today and that SJR 24 would be heard first.

#### **SJR 24-CONST AM: GUARANTEE PERM FUND DIVIDEND**

SENATOR OGAN, prime sponsor of SJR 24, told members he decided to introduce this legislation because of his sincere belief that the voters will not allow any other use of the permanent fund until the permanent fund dividend program is protected in the Alaska Constitution. SJR 24 contains a provision that delays its effective date until the voters approve a constitutional amendment related to an appropriation limit. He explained:

I feel if - even with constitutionally protecting the permanent fund dividend that if it was protected, let's say tomorrow, that a lot of legislators would perceive that the rest of the money is available for appropriation and there would be a feeding frenzy. I have a personal belief that government generally grows in direct proportion to the amount of money available to spend and so I think we should protect the dividend, put a spending cap in place and then, and only then, discuss some of the excess earnings to be used for some of the critical needs that we have as a government.

As we all know, oil prices have been high but production will continue to decline in the near and far term and, even with the gas pipeline, we are not going to have adequate revenues to balance the budget in a few short years. I think this is an important first step.

He explained that SJR 24 essentially enshrines the permanent fund dividend program, as it exists in current statute.

SENATOR FRENCH asked if SJR 24 would put the entire earnings reserve account inside the permanent fund itself, instead of leaving it as a separate account.

SENATOR OGAN said it would.

SENATOR FRENCH asked if the distribution methodology for dividends would remain the same, that being 21 percent of the net income for the last five years.

SENATOR OGAN said it would and explained that Section 3 of SJR 24 enshrines the existing dividend formula. He said at the end of the day, if the percent of market value (POMV) plan is adopted, SJR 24 would have to be amended to use that approach. He said he does not believe the POMV is a bad thing on its face,

but if it is adopted he believes the dividend should still be protected.

SENATOR FRENCH asked how inflation proofing would work under SJR 24.

SENATOR OGAN deferred to Mr. Storer for an answer.

MR. ROBERT STORER, Executive Director of the Alaska Permanent Fund Corporation (APFC), told members as he reads SJR 24, inflation proofing would remain by statute. Currently, the dividend formula takes precedence over inflation proofing, although both are appropriated annually. He said if the existing statute were memorialized in the Constitution, the dividend would again take precedence over inflation proofing.

SENATOR FRENCH asked if SJR 24 requires that 50 percent of the income available for distribution be transferred from the earnings reserve account and used for the dividend program.

SENATOR OGAN said that is correct.

SENATOR FRENCH asked how that compares with the current dividend program.

MR. STORER said they are the same.

SENATOR OGAN explained that SJR 24 would put the existing statute in the Constitution, verbatim.

CHAIR SEEKINS announced that he would take testimony on all four resolutions before the committee simultaneously. He then asked for a motion to adopt version H [SJR 24] as the working document before the committee.

SENATOR OGAN so moved.

CHAIR SEEKINS announced the motion carried without objection; therefore Version H was before the committee. He then designated a proposed amendment distributed to members as Amendment 1.

SENATOR OGAN moved to adopt Amendment 1 [for the purpose of discussion], which reads as follows.

23-LS1543\H.1  
Cook  
8/19/04

A M E N D M E N T 1

OFFERED IN THE SENATE  
TO: SJR 24

Page 2, lines 14 - 15:  
Delete "a new section"  
Insert "new sections"

Page 2, following line 18:  
Insert

**"Section 31. Suspension and Repeal of amendments.** (a) Notwithstanding Section 1 of Article XIII, the 2004 amendments to Section 15 of Article IX are suspended on the date of an initial determination by the Internal Revenue Service that all or a portion of the permanent fund is subject to federal taxation. The suspension is terminated on the date the amendments are repealed under (b) of this section or one hundred eighty days after the date of a final, nonappealable judgment or order by a federal court deciding that no portion of the permanent fund would be subject to federal taxation as a result of the amendments. During the period of suspension under this subsection, Section 15 of Article IX shall apply as it read on January 1, 2003.

(b) Notwithstanding Section 1 of Article XIII, the 2004 amendments to Section 15 of Article IX are repealed one hundred eighty days after the date of a final, nonappealable judgment or order by a federal court deciding that all or a portion of the permanent fund is subject to federal taxation. Upon repeal of the 2004 amendments under this subsection, Section 15 of Article IX is amended to read as it read on January 1, 2003."

CHAIR SEEKINS noted without objection, Amendment 1 was before the committee.

SENATOR TOM WAGONER told members that he has had great concerns about enshrining the permanent fund dividend in the Constitution since before he took office because of the differing opinions on whether or not doing so would enable the IRS to tax the permanent fund. People knowledgeable about tax law say if the permanent fund dividend is enshrined in the Constitution, the IRS's ability to tax the permanent fund becomes tenuous because that money would no longer be available for government services. Amendment 1 contains a safety valve so that if the IRS attempts to tax the permanent fund, the dividend would revert to a

statutory mandate, not a constitutional mandate. He said he believes Amendment 1 should be attached to any permanent fund dividend bill because it gives the legislature final control.

SENATOR THERRIAULT felt adopting Amendment 1 would be prudent because the IRS will not guarantee that any interpretation of the tax code and case history is correct. He noted, however, that SJR 24 is structured so that the earnings reserve is still maintained and can be used for a public purpose, which probably mitigates the threat of taxation by the IRS.

SENATOR ELLIS raised a point of order and asked Chair Seekins to clarify whether the motion involving Amendment 1 was to introduce it for discussion.

CHAIR SEEKINS clarified it was to adopt Amendment 1 for the purpose of discussion and not to incorporate it into SJR 24.

SENATOR ELLIS noted it is atypical to ask if there is objection to introducing an amendment for discussion and wanted to affirm that the committee did not adopt the amendment. He then asked Senator Wagoner if he has read the legal opinion that Attorney General Renkes solicited on the taxation issue and, if so, asked him to comment on it. He maintained that the legislature has spent some money to get to the heart of the taxation issue because it has been a point of debate for years. Senator Green introduced a bill years ago to enshrine the permanent fund dividend but it received a lot of criticism that it would trigger unfavorable IRS action toward the State of Alaska. He asked if Senator Wagoner has read those materials but did not find those opinions definitive.

SENATOR WAGONER said he has read a couple of opinions that contradict each other or take different approaches toward what the IRS can and cannot do. He said Amendment 1 provides him with a higher comfort level than any of the opinions he has read.

CHAIR SEEKINS asked if the IRS has ever been constrained by the opinion of a state attorney general.

SENATOR WAGONER said the only entity that can restrain the IRS is Congress.

SENATOR ELLIS requested that Attorney General Renkes provide a position on the need for Amendment 1. He said the attorney general went through the time and expense of soliciting an

opinion from a Washington, D.C. law firm so he would appreciate hearing his opinion.

SENATOR WAGONER said he didn't think what the attorney general said would matter because Amendment 1 provides a comfort level that he wants anyway for himself and a lot of other people who distrust the IRS. He said he feels it would be a waste of Attorney General Renkes' time.

CHAIR SEEKINS asked if Attorney General Renkes' opinion was in writing.

SENATOR WAGONER said if it is, he would get a copy for committee members. He repeated that he feels Amendment 1 is a prudent safety valve.

SENATOR OGAN noted the only opinion that really counts is of "the guys that wear the robes in the U.S. Supreme Court so everybody else has got an opinion about it." He agreed that Amendment 1 is a circuit breaker if an adversarial opinion kicks in and removes the dividend program from the Constitution.

SENATOR THERRIALT pointed out that the language contained in Amendment 1 is identical to Section 3 of SJR 19 that Senator Ellis cosponsored.

SENATOR ELLIS told members he was not arguing against the inclusion of Amendment 1. He maintained, "I was asking about the attorney general - the time and expense we went to as a state and that might be a legitimate part of the committee record. I'd hate for Senator Therriault to mischaracterize my...."

CHAIR SEEKINS asked Senator Wagoner to get a copy of the written opinion to insert in the record.

SENATOR WAGONER offered to do so today.

SENATOR OGAN said one reason he introduced SJR 24 was because of a lengthy discussion he had with constituents in the Mat-Su Valley during the interim about the fact that the founding fathers of Alaska decided the state should retain the subsurface rights to land in Alaska. All residents collectively own the subsurface mineral estate, with the exception of the lands owned by Native corporations and lands patented before statehood. Additionally, the Alaska Constitution declares the subsurface rights as dominant so that a surface owner must allow access to the subsurface. That is also included in the Statehood Compact.

According to Section (6)(i) of that Compact, the U.S. attorney general is specifically instructed to litigate in the U.S. district court to procure those subsurface rights for the federal government if the state conveys the subsurface rights to anyone else. He feels very strongly that the dividend program needs to be protected because it represents the people's share of the collectively owned subsurface mineral rights.

CHAIR SEEKINS announced that with no further objection, Amendment 1 was adopted.

SENATOR FRENCH said he is curious about the language in the appropriation limit that is currently working its way through the legislature.

SENATOR OGAN said no one knows whether the legislature will have an appropriation limit at the end of the day, and how it will work, but SJR 24 will not take effect without one. He said he believes they should all be linked. He added:

And then we get into the discussion of whether or not it's a revision and I gotta put that on the record. I mean - and it's a little risky, and at the end of the day we might wish to just take that out and let it fly on its own. It could be viewed as a revision and we have to be honest with people that's a possibility. Of course they may view this as a revision because this effective date affects more than one section of the Constitution and I think the best case to address that and - so the committee needs to be cognizant of that. I don't want to try to hide it from anybody.

CHAIR SEEKINS pointed out, under Bess v. Ulmer, any section of the Constitution that affects too many other sections is no longer an amendment; it would be a revision.

SENATOR OGAN said he is unsure whether a constitutional amendment with an effective date contingent upon another [constitutional amendment] has ever been put before the voters so it is an untested section of law.

CHAIR SEEKINS noted that according to Bess v. Ulmer, an amendment to the Constitution is a clarification; a major change is a revision.

SENATOR ELLIS asked whether the governor has taken a position on SJR 24.

SENATOR OGAN said he has not had a discussion with the administration about it.

SENATOR ELLIS asked if he plans to do so.

SENATOR OGAN replied, "I don't think it's a function of the executive branch to - it's nice when they support your work but, frankly, the separation of powers, I think it's something we should - it'd be nice to have but isn't required to have to consider an amendment."

SENATOR ELLIS agreed but said the majority frequently solicits the governor's position, as it is important to the way the majority views various pieces of legislation.

CHAIR SEEKINS asked Senator Ellis to restrict his comments to his own conversations with the governor. He expressed concern that the term "you all" is inclusive and other people are not available to defend their positions.

SENATOR ELLIS asked the chair why he wanted to restrain his right to speak on the issue. He then clarified that he was referring to the Republican Majority when he said "you all."

CHAIR SEEKINS said the Republican Majority was not present and he did not want Senator Ogan to answer for him.

SENATOR ELLIS said he would ask the chair separately and was only interested in Senator Ogan's position.

SENATOR OGAN repeated that he has not discussed SJR 24 with anyone in the governor's office.

SENATOR THERRIAULT pointed out that SJR 24 prioritizes dividends over inflation proofing. He cautioned that the state could pay dividends during a down market and give the next generation a diminished asset. He views the permanent fund as a mechanism for taking a one-time asset and making it multi-generational so that possibility weighs heavy on his mind.

CHAIR SEEKINS noted that with no further discussion on SJR 24, he would set it aside until the end of the meeting.

**SJR 32- CONST AM: PERM FUND INCOME FOR DIVIDENDS**

SENATOR KIM ELTON, sponsor of SJR 32, described the measure as "if POMV, then SJR 32." The intent of SJR 32 is to codify one of the recommendations of the Conference of Alaskans: to constitutionally protect the permanent fund dividend. He said in response to Senator Therriault's concern about prioritizing inflation proofing over dividends, SJR 32 follows the POMV method, which does just that. SJR 32 also provides that 80 percent of the earnings from the POMV would be used for dividends. He stated:

It would probably be fair to point out that the sharpest minds at the [Alaska] Permanent Fund Corporation have, when they look out ahead and they compare this recipe to the existing recipe that's in statute, they would suggest that...a return that would probably most equal the existing statutory dividend would be in the neighborhood of about 60-40 - 60 percent for dividends, 40 percent for other purposes to be determined by the legislature. But, Mr. Chair, if you look back to 1990 and you take a retrospective look, the formula, if we had been operating under a POMV, the formula that most closely would replicate the existing statutory language would be in the neighborhood of about 76-24 so this errs just slightly to the benefit of the dividend program, 80-20 does.

SENATOR ELTON said he firmly believes the legislature has been able to protect the growing pool of the permanent fund because of the nexus between the permanent fund and the dividend program. He repeated that SJR 32 is written so that its enactment is contingent upon legislative and voter approval of the POMV methodology.

SENATOR OGAN moved to adopt Version H of SJR 32 as the working document before the committee.

CHAIR SEEKINS announced that without objection, the motion carried.

SENATOR FRENCH said his greatest concern is inflation proofing and that is protected fairly well under the POMV scheme. He said he tries to work backwards from the election in November to figure out a plan that will gain favor with the public to provide a dividend and allow some earnings to be used for essential government services. He

believes SJR 32 goes a long way toward doing that. He asked Senator Elton if he has received feedback about how the public will receive this resolution.

SENATOR ELTON said one reason he introduced SJR 32 was to make sure the legislature had all of the pieces necessary to accomplish the goals of the Conference of Alaskans. The one piece he found missing was a mechanism that provides a fairly simple and easily understood division of the earning stream for dividends and government services. He has had a considerable amount of discussion with people in his district and also with people at the conference. He noted one way to accomplish policy, especially when a revision of the Constitution is required, is to include a market component. The legislature must structure the constitutional amendment so that people can understand its benefits. He believes the POMV approach will be adopted if the citizens understand its effect on the permanent fund dividend.

CHAIR SEEKINS asked Senator Elton if he has any letters of support or e-mail messages showing support that could be inserted into the record.

SENATOR ELTON said that SJR 32 closely reflects the Conference of Alaskans' recommendations.

CHAIR SEEKINS asked Senator Elton to show a nexus. He said he read the Conference of Alaskans' report but the recommendations were not supported by enough of a majority that the legislature would have passed them as a proposed constitutional amendment.

SENATOR ELTON said it is unusual that a bill he introduces is heard within 10 days so he does not have letters of support.

CHAIR SEEKINS asked how many bills he has had referred to the Senate Judiciary Committee.

SENATOR ELTON said none. He then indicated the suggestions from the Conference of Alaskans were not supported unanimously but 37 of the 55 delegates suggested enshrining the dividend in the Constitution.

CHAIR SEEKINS said he is not aware of anything in the conference report that suggested an 80/20 split.

SENATOR ELTON said the Conference of Alaskans did not identify an appropriate split for earnings and dividends but SJR 32 comes closest to matching what the existing program has provided over the last 15 years. He repeated that despite the fact that this recommendation was not approved unanimously by the conferees, 37 out of 55 delegates did suggest the dividend be protected in the Constitution. He pointed out that kind of a margin in a legislative race would be considered as overwhelming.

CHAIR SEEKINS repeated [that margin] would not suffice for a constitutional amendment to come from the legislature.

SENATOR ELTON argued that would if the threshold is considered to be what it would take to pass on the general election ballot in November.

CHAIR SEEKINS asked if he believes the 55 conference delegates were representative of the people of the state.

SENATOR ELTON said he does not. The conferees were from a much higher socio-economic stratum than the average Alaskan. He added that two-thirds of the conferees indicated they earned over \$100,000 per year.

SENATOR FRENCH commented that the various proposals before the committee represent a struggle between the government and the people for the earnings of the permanent fund. The people have repeatedly expressed their will to get their share of the fund's earnings. SJR 32 embodies that will most closely.

CHAIR SEEKINS asked Senator Elton if he recalled what top two funding sources the conferees suggested the legislature look at.

SENATOR ELTON replied a unique voting system was applied at the Conference. When the conferees were able to vote anonymously, there was a weighted average. The conferees were asked to decide on their top three revenue enhancements. The weighted average showed an income tax was the preferred method, by a very slight margin, over the earnings of the permanent fund, which had a relatively small margin over natural resource taxes. He said he would characterize the top two as a virtual dead heat between the income tax and the permanent fund earnings.

CHAIR SEEKINS responded, "All of which are the people's money, correct?"

SENATOR ELTON agreed.

SENATOR THERRIAULT asked Senator Elton why he chose an 80/20 split rather than a ratio that is closer to the status quo.

SENATOR ELTON repeated that the sharpest minds at the Alaska Permanent Fund Corporation (APFC) did projections to the year 2010 and suggested that to best replicate the statutory dividend formula, 60 percent of the earnings stream would be necessary. Because many variables could occur in that timeframe, he personally took a retrospective look to 1990, had the POMV methodology been in place. The split of earnings would have been about 76 percent for dividends and 24 percent for government. He said he picked an 80/20 split in favor of the dividend.

SENATOR THERRIAULT said if the POMV methodology is established, the earnings reserve will no longer be in existence. He asked Senator Elton to elaborate on how the 20 percent would be used.

SENATOR ELTON said the 20 percent is unallocated and would be available for government spending, which would be codified by the legislature and the budget process.

SENATOR THERRIAULT noted that under POMV, 80 percent of up to 5 percent would be used for dividends. If the legislature uses 3 percent instead of 5, 80 percent of that amount will be used for dividends.

SENATOR ELTON explained that SJR 32 is based on a 5 percent return from POMV. If the return is less, the 80/20 ratio remains the same but a lower amount would be available for each.

SENATOR THERRIAULT asked Senator Elton:

Even though it doesn't say it here, the use of the other 20 percent, it's your intent that it be available for appropriation and, in fact, you say here at least 80 percent of the amount appropriated so that 20 percent has to be

appropriated for something. You have appropriated it from the earnings and whatever you have appropriated out, 80 percent shall go to a dividend but you have appropriated that other 20 percent too and you can't get to the dividend unless you appropriate that 20 percent.

SENATOR ELTON said he thinks all legislators would view this as a revenue source in the same way that an income tax or additional resource taxes would provide an income stream available for appropriation. This constitutional amendment provides that 80 percent of this revenue stream would be preserved for the dividend program. The other 20 percent would be available for government spending.

SENATOR ELTON said he appreciates the fact that SJR 32 is linked with the POMV. He believes there is a growing realization that the POMV truly is the best way to make the permanent fund permanent.

**TAPE 04-10, SIDE B**

SENATOR FRENCH maintained, regarding what split more accurately reflects the current system, there is no bright consensus. The APFC board has said a 60/40 split produces the current dividend. However, Sharman Haley, from the Institute of Social and Economic Research at UAA, recently wrote an article [in the Anchorage Daily News] in which she said the appropriate split is 70/30. He indicated that trying to replicate what is basically an earnings driven system under the current value driven system is like comparing apples to oranges. He commended Senator Elton for erring on the side of caution.

CHAIR SEEKINS indicated the discussion is not about whether the POMV system is a good one but about how much would be given to whom.

SENATOR ELTON agreed and pointed out that during his tenure in the legislature, the asset management of the fund was changed. He added:

All of those changes, what happens in the marketplace, all of these things make it very difficult to say with any kind of real authority it is 61.3 percent to most closely replicate - I mean you can't do that. We can trust the best

minds that we have down at the permanent fund, and I do trust them but it's kind of a rolling target that could change next year also.

SENATOR OGAN asked Senator Elton how much new money would be available to spend on government services with an 80/20 split.

SENATOR ELTON estimated about \$260 million, based on a 20 percent of the 5 percent return from the POMV, which would be \$1.3 billion this year.

SENATOR OGAN said he believes offering 80 percent for dividends is very generous, but his concern is that a new \$275 million funding source for government services will cause government to grow and the state will be in the same situation that it's in today in five years. He noted he wants to see a constitutional spending limit enacted first.

SENATOR ELTON commented that the legislature has acted in an extremely responsible way regarding the use of the permanent fund earnings. Regarding Senator Ogan's concern about new money being available for appropriation, he sees any new revenue stream as backfilling deficit spending that will allow the legislature to draw down the budget reserve at a slower rate.

CHAIR SEEKINS asked if all of the earnings of the permanent fund have been available to the legislature for spending since the beginning of the dividend program.

SENATOR ELTON said they have and because the program is statutory and not constitutional, it only requires a simple majority vote.

SENATOR OGAN expressed concern that SJR 32 means to him that the remaining budget gap will have to be filled with an income or sales tax to lock in the 80/20 split.

SENATOR ELTON agreed but noted that additional spending cuts are possible. He said the discussion is moving toward a philosophical one and his view is that SJR 32 is not a fiscal plan. It could be one component of a fiscal plan.

CHAIR SEEKINS asked Senator Elton if he believes in the need for an income tax before looking at spending the permanent fund earnings.

SENATOR ELTON said his position is most closely reflected by that of the fiscal policy caucus, a group made up of 28 members of the legislature. Its package included a cruise ship tax, alcohol tax, oil industry tax and a small income tax. He pointed out that none of the 28 members believed that plan was a perfect one, however they agreed it was as close as they could come to one. On an individual basis, they all preferred a different plan.

CHAIR SEEKINS announced a recess.

9:08 a.m.

**SJR 19-CONST. AM: PERMANENT FUND INCOME**

CHAIR SEEKINS called the meeting back to order and announced that SJR 19 was before the committee.

MR. MARK STOPHA, staff to Senator Lincoln, sponsor of SJR 19, said he was available to answer questions.

MR. MARK GNADT, staff to Representative Croft, sponsor of House companion legislation, offered to answer questions.

SENATOR THERRIAULT noted that Representative Croft stated at the last meeting that inflation proofing of the permanent fund was paramount, in his opinion. He said some of the other proposals before the committee have been drafted to do just that so that the permanent fund remains truly permanent and is not eroded by the effects of inflation. He pointed out that SJR 19 does not; it freezes the current statutes in place giving the dividend top priority. SJR 19 also provides a mechanism that allows spending on government services with the ratification of the people. Therefore, if dividends are given a preference and dollars are tight, he thinks the first thing that will fall off of the table is inflation proofing. He asked why Representative Croft signed on to a piece of legislation that does not make inflation proofing paramount.

MR. GNADT said he is correct in that inflation proofing falls second to dividends under SJR 19 but, to ensure that inflation proofing occurs, it requires ratification of 50 percent of the voters before spending for government services. Therefore, inflation proofing is prioritized above spending unless the people vote otherwise.

SENATOR THERRIAULT responded:

That still is a concern of mine because looking out for the next generation is I think what the permanent fund is all about and that allows current people to get a dividend in their pocket - the current people to vote to just use money for governmental services that they support, and I think the tendency is to do those things and not look out for the next generation. So, to me that's one of the whole beauties of the permanent fund.

He then said the current permanent fund dividend statutes, projected forward, result in a 60/40 split. He asked if Senator Lincoln and Representative Croft understand and support that.

MR. GNADT said he cannot speak to what percentage they support but they do support putting the existing dividend program into the Constitution.

SENATOR THERRIAULT repeated that means a 60/40 split going forward.

SENATOR FRENCH pointed out that several economists have tried to define the split necessary under a POMV plan to restate the current program, which is an earnings stream driven plan. He said no one has arrived at a "lock-tight" number.

CHAIR SEEKINS announced that with no further questions on SJR 19, the committee would take up SJR 18.

**SJR 18-CONST. AM: PF APPROPS/INFLATION-PROOFING**

CHAIR SEEKINS asked Mr. Storer if the percent of market value (POMV) system focuses the attention of the Board of Trustees primarily on making sure the permanent fund investments produce the highest amount of income possible for the citizens.

MR. ROBERT STORER, Executive Director of the Alaska Permanent Fund Corporation (APFC), said the POMV embodies two objectives. The first is to memorialize inflation proofing in the Constitution and the second is to establish

a management tool that gives the Board of Trustees direction in how to best manage the assets to eliminate ambiguity.

CHAIR SEEKINS asked Mr. Storer to provide the committee with the history of the 1996 anomaly in the realized gains of the permanent fund.

MR. STORER said he was not at the APFC at that time, but was close enough to describe what occurred. He noted the chart of realized income showed a lot of spikes up and down, with a big spike up in 1996. The distribution system is based on cash flow from dividends, interest, and the profit or loss from the sale of securities. In 1996, the [APFC board] discussed the fact that a substantial portion of the permanent fund's equity investment was in a passive portfolio during the bull market. Passive portfolios are designed to replicate the performance of an index. They are very low cost with virtually no turnover. The Board of Trustees was concerned about intergenerational equity so the board decided to liquidate some of the profits in that passive portfolio, which then became realized income and were distributed according to the statutes.

CHAIR SEEKINS asked if the Board of Trustees unilaterally decided to bring in a higher amount of realized earnings in order to distribute them through the dividend program.\

MR. STORER said that is correct; the board made the decision after discussions with the consultant and a lengthy discussion about intergenerational equity. He noted POMV is indifferent to that possibility because it captures the rising market in a measured way, i.e. the real income, and it harmonizes with current accounting practices and ignores the need for arbitrary or market decisions.

CHAIR SEEKINS asked if the APFC board is charged with accommodating intergenerational equity under its charter.

MR. STORER replied, "Mr. Chairman, I'd say embedded in all generations being treated equally or benefiting equally, that was, I assume, part of that evaluation."

CHAIR SEEKINS asked if the board is the body that determines how to equally treat all generations under the current system.

MR. STORER answered, "On that day, in that action."

CHAIR SEEKINS asked Mr. Storer if he had \$20+ billion and was to recommend how that fund should be managed for the benefit of current and future generations, how he would convince people to use the current system over the POMV system.

MR. STORER said that would be difficult. The hurdle would be to convince people to use a methodology that is inconsistent with current accounting methodology. A second hurdle would be to negate the fact that most endowment funds use some form of the POMV. He said the main criticism of the realized income basis, is that the realized income can be manipulated by making decisions independent of what the market is doing. He has given Chair Seekins' question a lot of thought but has failed to come up with a reasonable argument in support of the current methodology. He said it made a lot of sense in the 1970s when the permanent fund was created.

CHAIR SEEKINS asked Mr. Storer if he could reasonably defend the position that the current realized income system meets the fiscal responsibility of a trustee, in terms of the trustee's fiscal responsibility to the beneficiaries of a fund.

MR. STORER replied the POMV is consistent with the methodology of most funds. He explained:

Another way that you see out there is taking the less popular - you take the income stream - dividends, interest, and that's part of your payout and then you in effect inflation proof by not accounting for the appreciation in your assets, whether they're realized or not, they stay with the fund. So that's kind of a second tier so now you've created inflation proofing through appreciation and a distribution through the income stream.

So now we go to the third one, which memorializes the distribution of the profits that occur and creates an enormous amount of volatility. The statutes say that we as fiduciaries, this is how we manage the fund so the statutes have given us

the fiduciary responsibility [indisc.] to manage it and to be mindful with that.

CHAIR SEEKINS said he was speaking only to the responsibility to better meet the long-term needs of the beneficiaries under one's fiduciary role, not by statute.

MR. STORER said he believes he provided his opinion on the hierarchy of treating all generations equally. He said he has not heard any better method being discussed right now, which does not mean one won't be proposed in the future. The legislature has the ability to appropriate all of the realized income in the fund right now. The more insight a fiduciary has as to how to best manage a fund, the better job the fiduciary can do. The current methodology leaves a lot of room for ambiguity.

SENATOR OGAN commented that many citizens do not trust the legislature's or APFC Board of Trustees' motivations for wanting to adopt the POMV. They see it as allowing the legislature to get more money for government spending. He asked Mr. Storer if he believes the POMV method should be coupled with a spending limit to assure the people that it is not just a way for the legislature to get more money from the permanent fund to spend.

MR. STORER said he understands the citizens' distrust and thinks it is natural and healthy. He believes parallel issues are facing the legislature and voters right now - the proposed POMV, which addresses inflation proofing and is a management tool, and the state's fiscal problems. The APFC Board of Trustees would have proposed the POMV no matter what the state's fiscal situation was. The board and staff recognize that the [earnings] distribution is within the prerogative of the legislature.

SENATOR THERRIAULT noted that the previous question was phrased as public distrust of the APFC dividend trustees; however, no such body exists. The Board of Trustees is charged with making sure that this multigenerational asset is not diminished by inflation and that is the Board's motive behind proposing the POMV.

MR. STORER strongly agreed.

SENATOR OGAN thanked Senator Therriault for correcting his misstatement and pointed out the legislature has the

responsibility for paying the dividend. He maintained that the simultaneous discussion of the POMV proposal and the budget gap is making everyone very suspect of the motivations behind the POMV proposal.

MR. STORER said the Board of Trustees understands that completely and when it is given the opportunity to speak directly to individuals and answer questions, it has found, without exception, they understand the distinction. The difficulty is conveying that message.

SENATOR THERRIAULT noted that under SJR 19, there might not be enough revenue in a down market to pay a dividend and/or inflation proofing. SJR 19 freezes the existing statutes so that the dividend takes precedence. He asked Mr. Storer if that concerns him.

MR. STORER said the Board of Trustees strongly believes that how the funds are used is within the legislature's prerogative. He stated:

If you went back to June 30, and this is what we've been using, we're updating it and then in any given year under the existing formula, there's about a 10 percent chance that there would be no dividend - I'm not saying every year, I'm just saying within that continuum. So that is the risk with the existing formula.

Now, because the market has done so well, and once we visit our asset allocation we will remodel it and, at least for some foreseeable time, that 10 percent probability diminishes because we have a much larger cushion. But the 10 percent probability of a significantly smaller dividend would still exist under the existing formula, and then inflation proofing - I haven't really thought through the - if POMV passes and you have this existing formula, you have now put inflation proofing ahead of that formula.

CHAIR SEEKINS took public testimony.

MS. MARY GRISWOLD, representing herself, said she supports a combination of CSSJR 18(STA) and SJR 32. She told members:

POMV provides long-term protection for the buying power for the permanent fund by constitutionally inflation proofing the entire fund. Right now only the principal is inflation proofed, and that is done by an annual legislative appropriation subject to available funds. Equally important, POMV prevents erosion of the permanent fund's value by limiting the spending in times of plenty. This payout method complies with generally accepted accounting practices and is appropriate for diversified funds composed of stocks, bonds and real estate. Our current payout method is outdated because we are no longer invested only in income-producing bonds.

Implementing POMV must be kept simple and comparable to the existing dividend program to gain voter acceptance. So while I am not generally in favor of dedicating appropriations in the Constitution, this case warrants doing so. The political reality is that we are going to get nowhere resolving our growing difficulties without clearing the dividend issue from the table. I favor an 80-20 split of the payout because this is the most defensible math to preserve a comparable dividend formula. It is consistent with the performance model, which I trust better than short-term projections or look backs. The model stipulates 80 percent nominal returns, 3 percent inflation, and a 5 percent real return over time. Right now we are using half of the nominal returns for dividends. To equal this after POMV's implicit inflation proofing, we must use 80 percent of the 5 percent payout. This is straightforward and leaves 20 percent available for essential government services, which when combined with revenue from revised oil taxes and a 3 percent income tax based on federal adjusted gross income will [indisc.] bridge our fiscal gap.

SJR 19 and SJR 24 continue our outdated payout method, which threaten the value of the permanent fund by allowing overspending in years of high income. A combination of CSSJR 18 and SJR 32 is a good solution to protect the value of the permanent fund, preserve the dividend program

that Alaskans have learned to count on, and help us take a big step toward fiscal responsibility. Thank you.

MR. MARK NEWMAN, testifying on his own behalf from Big Lake, informed members that he was a delegate to the Conference of Alaskans. He has repeatedly heard the comment that it is necessary to get the POMV by the people. He said he has recently talked to many people who understand that with the current method, dividend checks will be higher when the stock market is up and lower when it is down. He noted the permanent fund began in 1976 with a deposit of \$728 million and it now amounts to \$28 billion, which shows that the current system is working very well. A commission report from 1990 showed the results of two questions put before Alaskans: what is the purpose of the permanent fund and what role will it play in Alaska's long-term future. The public clearly stated that it wants the permanent fund retained; the principal of the fund preserved; the current level of state spending lowered; and it does not want to use fund earnings to support state programs in the foreseeable future. Many people desperately need that dividend check. He expressed concern that the people are not being listened to by the politicians and government officials. He cautioned that to build public trust, the legislature must listen to and do what the people say. He invited members to call him.

MR. ROGER GAY, a resident of Big Lake, said he was tired of hearing about the issue of inflation proofing because the legislature cannot inflation proof anything by throwing more money into the permanent fund. He told members, "The only way to get the real value of or from a fluctuating and intrinsically worthless currency is to spend it now at today's value. Tomorrow your money is going to be worth less."

**TAPE 04-11, SIDE A**

MR. GAY said when inflation eats the value of the permanent fund down to zero that should be a lesson to the people who refuse to control their own currency. He added, "If it doesn't make sense to inflation proof the dividend, let's stop hearing about the oxymoron of inflation proofing...double digit inflation is going to be a bigger shock than the stock market crash and you can bet it's coming."

CHAIR SEEKINS announced that with no further witnesses wishing to testify, public testimony was closed.

SENATOR OGAN concurred with Mr. Newman's statement that a lot of people need the dividend check. He said he was glad Mr. Newman attended the Conference of Alaskans, as he represented the "average guy."

SENATOR THERRIAULT commented that the legislature always has to deal with reality versus perception and he believes there is the perception among the public that the management scheme of the permanent fund has never been changed. However, had the legislature never tinkered with that management structure, the permanent fund would not have increased in value as the result of the stock market rise. He explained that the permanent fund was originally set up as a bond fund and had the legislature chose to leave it that way, the stock market would have taken off and left the fund behind. That change resulted in a tremendous payout to the public, which people are now so dependent on.

[The following testimony by Chair Seekins is verbatim.]

CHAIR SEEKINS: I agree. Other comments? Discussion among the members? My intent here is to take a look at all four of these bills this morning and I think that the Judiciary Committee has discussed and discussed and discussed these bills. I think it's time for other members of the legislature to be able to discuss them as well. My intent here is to put an up and down vote as to whether we put all four of these bills forward or not. I don't have any problem with them going forward and being discussed in further committees of assignment. I think it's worthwhile to be able to do so.

On a personal level, I support some concepts and I don't support other concepts but I don't think that they've been fleshed out to the point where I would be on an up or down vote except on one thing, and that would be that I believe that the POMV system is superior to the system that we have now. I'm saying that both as a legislator, as a businessperson and as a former trustee. In 1991-1994, we had discussions as to whether or not the fund should be operated on a percent of market value way back then rather than the current system of realized gains. I think our

current system is antiquated. It's subject to market variability. It's subject to political manipulations and it's not the best system that we should have in place for my family currently, my children now, my grandchildren and their children to come. I do believe that we should intrinsically inflation proof the fund and I support that on that basis, and I think that that is an added benefit to the POMV system. I can't guarantee what inflation proofing is going to be next year but the way that SJR 18 is written, it gives the legislature the cap of 5 percent, not a mandate to spend 5 percent. I don't think people in general understand that.

As I've gone around the state and talked to people, I found out that once they understand that it's a management system and it's not a raid on the permanent fund, as some political opportunists would like to make it be, I think that they say well maybe that's not a bad system. The discussion though, would tend to be as to well how much and where would it go, as we heard in the committee this morning. I'm not at this point in favor of limiting the fiscal responsibility of the legislature, either now or in the future to be able to handle emergencies that may emerge and the flexibility that we would have to have.

On a personal basis, I don't have any problem with a spending limit - a constitutional spending limit, which is not part of what we're looking at this morning, where we would be able to override the provision in case of an emergency or collapse - some kind of a national disaster. My primary responsibility as a legislator fiscally is to make sure that we are meeting the essential needs of the government in the State of Alaska and I think that our Constitution was very strong in assigning that position to the legislature. I have not been in favor of endowing money for any purpose in my past, and I'm not at this point in time.

I don't have any problem - I believe, based on the track record of the legislature, we would continue to try our dead level best to be able to put a dividend into the hands of the people of the State of Alaska. It's a strong economic force. It's one of - I don't know where it would be but it's one of the top five economies in the state of Alaska. At one time I know it was second only to, I believe, fishing at that particular time. So, it's a strong economy. We would not choose, I don't think as a

legislative body, to cripple that economy, nor would we choose as a legislative body to cripple the State of Alaska when dire circumstances were necessary for us to be able to meet those essential needs of government.

So, I hope that as we look now - we're going to ask on an individual basis, I'm going to ask for recommendations from the committee on all four of these for the purposes of further discussion down the line in the rest of the body. We all know that we're coming up to a date when we [indisc.] by the Governor and we've agreed that we'd take a look at many different approaches to be able to look at how we would operate fiscally in the State of Alaska. And we have got recommendations from everywhere, including the 55 members of the Conference of Alaskans. So, I would ask first for the will of the committee as to SJR 24. Senator Therriault?

SENATOR THERRIAULT moved SJR 24 from committee with individual recommendations.

SENATOR ELLIS objected because he believes the committee has a superior work product before it that addresses the same issues.

The motion to move SJR 24 from committee with individual recommendations carried with Senators Ogan, Therriault, and Seekins in favor, and Senators Ellis and French opposed.

SENATOR THERRIAULT moved SJR 32 from committee with individual recommendations.

SENATOR OGAN moved a conceptual amendment to SJR 32, that being to incorporate Section 4 from SJR 24. That amendment reads:

**Sec. 4.** Article XV, Constitution of the State of Alaska, is amended by adding a new section to read:

**Section 30. Conditional Effect.** The 2004 amendments to the Alaska permanent fund (art. IX, sec. 15) take effect only if, in 2004, the voters approve an amendment relating to an appropriation limit (art. IX, sec. 16).

SENATOR ELTON asked for clarification of what the amendment does.

SENATOR OGAN explained that it would also require voter approval of a spending limit.

SENATOR ELTON said he would prefer to keep SJR 32 as simple as possible and expressed concern about predicating SJR 32 on another action. He suggested the Senate Finance Committee discuss that matter.

SENATOR ELLIS objected to the adoption of the amendment.

The motion to adopt the amendment carried with Senators Therriault, Ogan and Seekins in favor, and Senators Ellis and French opposed.

There being no further discussion on the motion to move SJR 32 as amended [CSSJR 32(JUD)] from committee, the roll was called. The motion carried with all Senators in favor.

SENATOR THERRIAULT moved CSSJR 18(STA) from committee with individual recommendations.

SENATOR ELLIS objected.

The motion to move CSSJR 18(STA) from committee carried with Senators French, Therriault and Seekins in favor, and Senators Ellis and Ogan opposed.

SENATOR ELLIS moved SJR 19 to the next committee of referral with individual recommendations.

SENATOR THERRIAULT objected and asked Senator Ellis, given the testimony that SJR 19 prioritizes the dividend over inflation proofing, whether he wished the committee to take action as an endorsement of the measure or just to keep it alive as a vehicle.

SENATOR ELLIS said individual recommendations by the members were inherent in his motion. He believes SJR 19 is a proposal that merits further consideration and each member can make a recommendation on the committee report.

SENATOR OGAN moved to adopt a conceptual amendment to SJR 19, that being to incorporate Section 4 from SJR 24. That amendment reads:

**Sec. 4.** Article XV, Constitution of the State of Alaska, is amended by adding a new section to read:

**Section 30. Conditional Effect.** The 2004 amendments to the Alaska permanent fund (art. IX, sec. 15) take effect only if, in 2004, the voters approve an amendment relating to an appropriation limit (art. IX, sec. 16).

SENATOR FRENCH said he is opposed to this amendment because he has a hard time endorsing a spending limit without any specifics in front of him at this time.

SENATOR OGAN said he understands that the committee would be voting on something that no one is able to describe at this time. However, the Senate could amend it on the floor.

SENATOR ELLIS told Senator Ogan that he might believe that adding the spending limit provision will enhance the chance of voter support but he encouraged members to think through the constitutionality of linking a constitutional spending limit with these other matters. He said it is unknown whether that goal will ultimately fail [in the courts]. He cautioned that the legislature would be asking for trouble down the road, past the voters. He agreed with Senator French that it is difficult to make a decision on this conceptual amendment in the timeframe provided by the chair.

The motion to amend SJR 19 carried with Senators Therriault, Ogan and Seekins in favor and Senators French and Ellis opposed.

The motion to move SJR 19 as amended [CSSJR 19(JUD)] from committee carried with all members in favor.