

**MINUTES**  
**SENATE FINANCE COMMITTEE**  
**April 12, 2006**  
**8:05 a.m.**

**CALL TO ORDER**

Co-Chair Lyda Green convened the meeting at approximately [8:05:10 AM](#).

**PRESENT**

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

**Also Attending:** DALE ANDERSON, citigroup/ Smith Barney; TIM RATTIGAN, Regional Banker for Northwest and Alaska, citigroup; JIM HADDON, Managing Director of Tobacco Securitization, citigroup; CHERYL FRASCA, Director, Office of Management and Budget, Office of the Governor; KEVIN BROOKS, Deputy Commissioner, Department of Administration; MIKE CALLAHAN, Director, Enterprise Technology Services, Department of Administration; NICO BUS, Acting Director, Division of Support Services, Department of Natural Resources;

**Attending via Teleconference:**

**SUMMARY INFORMATION**

SB 243-TOBACCO REV. FOR UNIV. & CORR. FACILITIES

The Committee heard a presentation by bond raters. The bill was held in Committee.

SB 231-BUDGET: CAPITAL & OTHER APPROPRIATIONS

The Committee heard presentations on the Alaska Land Mobile Radio project, statewide information technology requests, and

Governor Murkowski's priority project requests. The bill was held in Committee.

SB 235-SCHOOL PERFORMANCE BONUSES

The Committee considered and adopted an amendment. The bill was reported from Committee.

#SB243

[8:05:47 AM](#)

SENATE BILL NO. 243

"An Act relating to the financing of construction, major maintenance, and renovation of facilities for the University of Alaska; relating to the financing of construction of a correctional facility; authorizing the commissioner of revenue to sell the right to receive a portion of the anticipated revenue from a tobacco litigation settlement to the Northern Tobacco Securitization Corporation, with the proceeds of that sale to finance construction, major maintenance, and renovation of facilities for the University of Alaska and to finance the construction of a correctional facility; providing for the establishment of funds for deposit of those proceeds; authorizing the issuance of bonds by the Northern Tobacco Securitization Corporation for the purpose of acquiring the right to receive a portion of anticipated revenue from a tobacco litigation settlement; and providing for an effective date."

[8:05:51 AM](#)

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

Presentation by citigroup  
on  
Tobacco Bond Issuance

DALE ANDERSON, citigroup/ Smith Barney, introduced the presenters. Citigroup is the leader in tobacco settlement securitization and has been involved since 1999.

[8:07:53 AM](#)

TIM RATTIGAN, Regional Banker for Northwest and Alaska, citigroup, introduced Mr. Haddon.

[8:09:18 AM](#)

JIM HADDON, Managing Director of Tobacco Securitization, citigroup, gave a presentation utilizing a packet titled, "Presentation to: The State of Alaska, Tobacco Settlement Revenue Securitization Update, April 12, 2006" [copy on file]. References are not all made in sequential order.

[8:09:28 AM](#)

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Completed Tobacco Securitizations

71 completed issues totaling over \$34 billion in par amount since 1999.

[US map highlighting the dates, amounts and percentages of Securitizations Completed, Securitization Pending, and Legislation Introduced status of states, US territories, counties and cities.

Notations indicate that a percentage of the Tobacco Settlement Receipts (TSR) generated by the states of California and New York are allocated to counties and certain cities. Amounts or percentages of TSR are pledged for the states of Alabama, Arkansas and North Dakota. States not a party to the Master Settlement Agreement (MSA) are identified.]

Mr. Haddon outlined the information on this map.

[8:10:11 AM](#)

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Secondary Market Trading (2003 - 2006)

[Line graph showing Secondary Market Trading and Yield (%) of the 5.5 percent Northern Tobacco Securitization Corporation Series 2001 Maturing 2029, and the 30-Year MMD

"AAA", for selected months from March 2003 to March 2006. Pertaining legal actions are noted on the timeline, as well as the dates bond raters downgraded unenhanced tobacco securitization bonds. A notation reads, "Yields calculated as volume-weighted averages based on MSRB daily trading data."]

Mr. Haddon stated this graph is indicative of the status of the yield in the current market of the Alaskan bonds issued in 2001 and maturing in 2029.

Mr. Haddon pointed out the 200 basis point change in tobacco rate yield variations from 8.5 percent to 5.5 percent between March 2003 and March 2006. This is a "very event risk" market that is subject to media reports of consumption, significant "factor determination concerning nonparticipating manufacturer adjustment", and litigation against the industry. These occurrences cause the market to fluctuate as the market evaluates the security.

Mr. Haddon noted the 30-year AAA MMD provides a baseline market analysis. "Rates have drifted down in tobacco" and therefore now is an opportune time to consider a tobacco securitization.

[8:11:52 AM](#)

Senator Dyson requested the witness explain acronyms as they are used in the presentation.

[8:12:12 AM](#)

Mr. Haddon defined "triple A" as the highest credit rating possible, 30-year as the term of maturity, and MMD as Municipal Market Data. Secondary market trading reflects the buying and selling of the Alaska Northern Tobacco Securitization Corp bond issued in the year 2001.

[8:12:45 AM](#)

Mr. Rattigan furthered the amount the State pays for the securitization on the bonds is not impacted. That rate was set at the date of issuance in 2001. This information reflects activity in the secondary market as buyers and traders are selling and buying the bonds after the initial offering.

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#### 2005 Tobacco Market Overview

- In 2005, the market for tobacco securitization bonds continued to be shaped by three primary factors:
  - Large cash positions of high-yield / tobacco investors
  - Market supply of various types of high-yield bonds
  - Investor perception of tobacco industry creditworthiness, litigation risk, and consumption risk
- In early 2005 (after a year with no tobacco securitization issuance), large cash positions of tobacco investors (specifically, municipal high yield funds) and an improving litigation environment provided a favorable backdrop for new tobacco securitization issuance
- At the end of 2005, we witnessed a softening secondary market, with decreased tobacco trading volume occurring
  - Less hype over potential tobacco refundings
  - Investors somewhat more credit cautious given the developments in the Grand River case

Thirteen tobacco securitizations were completed in 2005 for a total of \$6.1 billion in par amount.

- \$4.5 billion refunding
- \$1.6 billion new money

And

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#### 2006 Tobacco Market Outlook

- New tobacco securitization issuance has continued in 2006, and there is a building forward calendar
- Cash positions in high yield funds remain robust, and we believe demand continues to exceed new supply. This was witnessed in the successful sale of \$1.75 billion

of tobacco securitization bonds during the week of January 30 alone, and an additional \$530 million brought to market year-to-date

- Institutions who have approved the tobacco credit continue to be buyers, and favorable yields and market outlook continue to attract new investors
- Despite recent developments regarding the Brattle Group's determination in the NPM Adjustment process, investors appear relatively comfortable in the current market environment, and market volatility has been minimal
- Tobacco market conditions and investor demand remain favorable

Over \$2.2 billion of unenhanced tobacco securitization bonds have been issued year-to-date.

- \$1.6 billion refunding
- \$600 million new money

Currently, litigation and NPM (Non-Participating Manufacturer) Adjustment risk are the most significant credit concerns in the tobacco securitization market.

Mr. Haddon stated that no tobacco securitizations were completed in 2004 due to significant litigation underway involving the State of Illinois and Phillip Morris, Inc. A \$13 million judgment was assessed against Phillip Morris in this case. As a result the company threatened to file bankruptcy proceedings, which caused volatility in the market. The market improved in 2005 and rates dropped. Several deals were made in 2005, as buyers became more interested in tobacco securitization bonds. The improvements continued in 2006.

[8:14:35 AM](#)

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Recent Secondary Market Trading (February - April 2006)

[Line graph showing Yield (%) of 5.5% Northern Tobacco Securitization Corporation Series 2001 Maturing 2029, Recent "BBB" Rated Tax-Exempt Capital Appreciation Bond Pricing, and 30-Year MMD "AAA", for various dates between February 1, 2006 and April 5, 2006. Pertinent events are

indicated. A notation reads, "Yields calculated as volume-weighted weekly averages based on MSRB daily trading data.]

Mr. Haddon noted the minimal volatility of the market in 2006 not withstanding issues involving a potential Non-Participating Manufacturers (NPM) Adjustment. He explained this pertains to whether the Master Settlement Agreement (MSA) was a significant factor in the market share loss of the Participating Manufacturers (PMs). The Brattle Group, an econometric firm, has been examining this matter and released a preliminary report on March 2 opining that the MSA was a significant factor. On March 27 the final report was issued. Despite this, the market conditions are favorable for issuers.

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#### NPM Adjustment: Overview

- The Non-Participating Manufacturer (NPM) Adjustment, measured by domestic sales of cigarettes by NPMs, operates to reduce the payments of the Participating Manufacturers ("PMs") under the Master Settlement Agreement ("MSA") in the event that the PMs incur losses in market share to NPMs during a calendar year as a result of the MSA
- Three conditions must be met in order to trigger an NPM Adjustment for one or more Settling States:
  - o (1) the aggregate market share of the PMs in any year must fall more than 2% below the aggregate market share held by those same PMs in 1997 (a condition that has existed for every year since 2000)
  - o (2) a nationally recognized firm of economic consultants must determine that the disadvantages experienced as a result of the previsions of the MSA were a significant factor contributing to the market share loss for the year in question, and
  - o (3) the Settling States in question must be proven to not have diligently enforced their Model Statutes
- The NPM Adjustment is applied to the subsequent year's Annual Payment and Strategic Contribution Payment and the decrease in total funds available as a result of

the NPM Adjustment is then allocated on a Pro Rata basis among those Settling States that have been found:

- o (i) to have not diligently enforced their Model Statutes, or
  - o (ii) to have enacted a Model Statute or Qualifying Statute that is declared invalid or unenforceable by a court of competent jurisdiction
- The MSA provides that the amount of an NPM Adjustment applied to any Settling State in any given year cannot exceed the amount of Annual and Strategic Contribution Payments to be received by such Settling State in such year.

The market for tobacco securitization bonds may be affected in upcoming months by recent developments relating to the "NPM Adjustment".

Mr. Haddon informed that the NPM Adjustment could potentially impact Alaska on two levels: the amount received in the payment due April 17, 2006, and the condition of the bonds already issued as well as the 20 percent of the settlement not securitized.

Mr. Haddon explained the NPM Adjustment. A tobacco manufacturer has two options: join the MSA, or be a NPM and submit an escrow payment to the State based on the amount of cigarettes sales made in the state. He outlined the conditions in which a NPM Adjustment could be made, which could decrease the amount of the payments the PMs must remit.

Mr. Haddon informed that the PMs have begun a procedure to achieve a NPM Adjustment. A greater than two percent market share loss since 1997 has occurred and subsequently, PMs could withhold a portion of their payments due in April or make the full payment and seek a NPM Adjustment for future payments.

Mr. Haddon also noted the determination must be made as to whether the State diligently enforced the MSA. A standard of diligent enforcement has yet to be established and would require either a court decision or binding arbitration. The PMs favor binding arbitration, while the Settling States prefer court involvement. Meanwhile, the manufacturers must decide whether to withhold partial payment.

Mr. Haddon reported that the market was "very concerned about this", although the market has not shown significant volatility as a consequence of these possible occurrences.

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NPM Adjustment: Recent Developments

- In May 2004, the Settling States and the PMs selected The Brattle Group as the firm of economic consultants responsible for making the "significant factor" determination regarding the Market Share Loss of the PMs for calendar year 2003
- On March 2, 2006, the Brattle Group issued its preliminary finding that the MSA was a significant factor contributing to the Market Share Loss of the PMs for calendar year 2003 (the preliminary determination was challenged by the Settling States and additional arguments/information were submitted to The Brattle Group for consideration in connection with its final decision)
- On March 27, 2006, The Brattle Group announced its final determination that the MSA was a significant factor contributing to the Market Share Loss of the PMs for calendar year 2003
- If the Original Participating Manufacturers ("OPMs") claim an NPM Adjustment for 2003 in April 2006, such OPMs may either make an appropriate deposit into the Disputed Payments Account or withhold payment reflecting the claimed NPM Adjustment, which could have a materially adverse impact on the available amount of tobacco settlement revenues ("TSRs") flowing to Settling States
- The Settling States have reserved the right to commence an enforcement action for compliance with the MSA. It has been reported that a majority of the Settling States have sent a notice to the PMs of their intent to commence such an action, including an action seeking a declaratory order that regardless of the "significant factor" determination, the PMs are not entitled to an NPM Adjustment because those

Settling States have been diligently enforcing their Qualifying Statutes

There can be no assurance as to the amount of any NPM Adjustment or the corresponding reduction in TSRs payable to the Settling States.

Mr. Haddon shared that Phillip Morris submitted its payment in advance of the April deadline. That manufacture occupies over 50 percent of the marketplace. RJR has submitted a partial payment and whether final payment would be withheld is unknown.

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NPM Adjustment: April 2006 Payment

- Assuming no NPM adjustment, the April 2006 payment due has been reported to be approximately \$6.5 billion
- The OPMs have requested the Independent Auditor for the MSA to reduce its calculation of the expected 2006 payment by \$1.14 billion plus interest (approximately \$1.2 billion total) to account for the NPM Adjustment for 2003
  - Assuming a \$1.2 billion NPM Adjustment, the impact to TSRs flowing to the State would be as follows:
    - Assumed NPM Adjustment: \$1.2 billion
    - State Allocation Percentage: 0.3414187%
    - Decrease in Total TSRs Flowing to the State:
      - 100.000%: \$4,097,024
    - Decrease in Amounts Available for Series 2000 Bonds: 40.000%: \$1,638,810
    - Decrease in Amounts Available for Series 2001 Bonds: 40.000%: \$1,638,810
    - Decrease in Non-Securitized TSRs:
      - 20.000%: \$819,405
- On March 31, Philip Morris reportedly made a full payment; RJR made a partial payment
  - Assuming Philip Morris' share was approximately 50%, this would suggest an NPM Adjustment of up to \$600 million; in this case, the impact to TSRs flowing to the State would be as follows:
    - Assumed NPM Adjustment: \$1.2 billion

State Allocation Percentage: 0.3414187%  
Decrease in Total TSRs Flowing to the State:  
100.000%: \$4,097,024  
Decrease in Amounts Available for Series  
2000 Bonds: 40.000%: \$1,638,810  
Decrease in Amounts Available for Series  
2001 Bonds: 40.000%: \$1,638,810  
Decrease in Non-Securitized TSRs:  
20.000%: \$819,405

There can be no assurance as to the amount of any NPM Adjustment or the corresponding reduction in TSRs payable to the Settling States.

Mr. Haddon indicated the information on this page explains the potential impact of a NPM Adjustment.

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#### Preliminary Financing Results

- Scenarios 1 and 3 of the following page assume a full refunding of State's Series 2000 and Series 2001 Tobacco Settlement Asset-Backed Bonds, respectively
  - Scenario 1 allows State to achieve \$114.5 million in upfront new money net proceeds
  - Scenario 3 allows State to achieve \$106.5 million in upfront new money net proceeds
- Scenarios 2 and 4 assume the Series 2000 and 2001 Bonds remain outstanding. The Series 2006 Bonds are structured on a subordinate basis to the Series 2000 and 2001 Bonds, respectively. In the respective scenarios, no revenues will be available for debt service on the Series 2006 Bonds until the currently outstanding bonds are fully repaid
  - Scenario 2 allows State to achieve \$90 million in upfront net proceeds
  - Scenario 4 allows State to achieve \$87.8 million in upfront net proceeds
- Though the bonds in each scenario have a stated maturity of 2060, with their turbo amortization structure they are projected to be fully repaid by

2041 in Scenarios 1 and 3, and 2040 in Scenarios 2 and 4

- o Shortening the final planned amortization date of the refunding scenarios to that of the Series 2000 and 2001 Bonds (2015) allows the State to achieve approximately \$20 million from a refunding of the Series 2000 Bonds, and approximately \$12 million from a refunding of the Series 2001 Bonds

Mr. Haddon noted this explains the opportunities for the State to generate additional revenue in 2006.

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#### Preliminary Financing Results

State of Alaska Tobacco Settlement Asset-Backed Bonds, Series 2006, Scenario Summary as of 4/10/2006  
[Spreadsheet listing Delivery Date and % of TSRs Pledged; then calculating Initial Par, less (OID)/Premium, equaling Gross Proceeds; less COI and Underwriter's Discount, Debt Service Reserve, Capitalized Interest, Escrow Cost net of Debt Service Fund, and Operating Expenses, plus Release from Series 2000 and 2001 SDR, totaling Net Proceeds to the State; Final Maturity and Final Planned Amortization dates are listed, as well as Cost of Capital and Yield on Final Maturity percentages for Scenario 1: New Money and Refunding of Series 2000 Bonds; Scenario 2: New Money Only: CABs Subordinate to Series 2000; Scenario 3: New Money and Refunding of Series 2001 Bonds; and Scenario 4: New Money Only: CABs Subordinate to Series 2001.]

Mr. Haddon outlined the four scenarios. The first would generate the most money possible, over \$14 million. Scenario 3 employs the same structure.

[8:22:04 AM](#)

Mr. Haddon clarified he considered Scenarios 1 and 3 to involve restructuring rather than refunding, because the bonds would not be refunded "purely for economical savings" but would instead extend debt.

Mr. Haddon hypothesized leaving the Series 2000 and 2001 bonds outstanding and "only try to wrap new money around" those bonds, saying the new bonds must be "subordinate" to the existing bonds. A zero coupon structure would be required because no revenues would be received until the payment of the Series 2000 and 2001 bonds were fully paid off. No interest payments would be made during that period.

Mr. Haddon stated that if a zero coupon structure were used, the State could generate \$90 million subordinate to the Series 2000 bonds, and \$87 million subordinate to the Series 2001 bonds, to total approximately \$180 million. These would be "leveraged out to the maximum amount" the bonds could be sold in the marketplace.

[8:23:39 AM](#)

Senator Bunde asked the earnings of the Series 2000 bonds without the "wrapping of new money".

[8:24:16 AM](#)

Mr. Haddon replied that the State has already issued the bonds and received payment so the State would generate no additional funds. The projected payoff of those bonds is 2015.

[8:24:38 AM](#)

Senator Bunde surmised the proposal is to refinance these bonds. He asked if the same bonds could be sold twice.

[8:24:50 AM](#)

Mr. Haddon clarified that a new set of bonds would be issued with a portion of the proceeds deposited into an escrow account to service the debt of the Series 2000 bonds. Technically, the first bonds would no longer have claim to the TSRs and the TSR funds would then be "freed up" and available for debt service on the new bonds.

Mr. Haddon pointed out the spreadsheet details that the Escrow Cost net of Debt Service Fund would be deducted from the gross proceeds.

[8:26:12 AM](#)

Senator Bunde commented that each time Citigroup becomes involved in the sale or refinance of these bonds, the State incurs a cost. He therefore questioned how the State would generate additional income from the scenarios posed.

[8:26:41 AM](#)

Mr. Haddon responded that rates are lower, and the time is opportune to participate in the marketplace. The State would generate \$114 million net of all fees on the refunding of Series 2000 bonds. This is a market opportunity and is not required. Currently, the State would resume retention of TSR funds when the current bonds mature.

[8:27:38 AM](#)

Co-Chair Green understood the current timing is optimal due to activity in the market.

[8:27:48 AM](#)

Mr. Haddon affirmed. He informed that this market has volatility, evidenced in 2004 when the market "shut down". The market is "open now". He could not guarantee whether the market would close again in the future, whether significant litigation would be decided against the tobacco industry or against the Settling States of the MSA. The State "did the right thing" in selling off the TSR risk in 2000 and 2001. If the State were to decide to repeat the action, this would be an ideal time.

[8:28:44 AM](#)

Senator Bunde estimated the cost of undertaking the action posed in Scenarios 1 or 3 would be approximately \$100,000,000. He based this on the Gross Proceeds amount of almost \$212 million, less the multiple deductions, totaling approximately \$114.5 million Net Proceeds to the State.

[8:29:08 AM](#)

Mr. Haddon clarified that \$90 million of the Gross Proceeds must be provided as escrow for the original bond issuances. A debt service reserve must also be provided. These are not costs to

the State, but rather necessary to refund the 2000 and 2001 Series bonds.

Mr. Rattigan pointed out that once the Series 2000 and 2001 bonds were refunded, the TSR would no longer need to be dedicated to their repayment and would be "freed" to pay the debt service on the new bonds.

[8:29:57 AM](#)

Mr. Haddon when refund 00 bonds, not longer using tobacco revenues.

[8:30:12 AM](#)

Senator Bunde asked the cost to the State of Scenario 1.

[8:30:24 AM](#)

Mr. Haddon listed transactions costs of approximately \$2 million [actual amount shown on spreadsheet is \$2,800,831].

[8:30:56 AM](#)

Senator Hoffman understood the Series 2000 bonds are currently scheduled to be paid off in 2015 and if no changes were made, the State would have the ability to appropriate the TSR funds after that date.

[8:31:13 AM](#)

Mr. Haddon responded that 2015 is a target date but is not certain. The target date would be achieved if tobacco revenues "come in" as projected. At the full amortization of the Series 2000 bonds, the 40 percent of TSR pledged to the repayment of those bonds would revert to the State.

[8:31:38 AM](#)

Senator Hoffman asked the amount anticipated annually and the total amount over time.

[8:32:04 AM](#)

Mr. Haddon indicated he would calculate the amounts. He noted the State would resume retention of the TSR funds.

[8:32:24 AM](#)

Senator Hoffman ascertained the issue as deciding whether the State needs revenues from the TSR immediately with no further TSR revenues until 2060; or to receive no revenue until 2015, but resume collection of TSR at that time. The question is whether receipt of \$114 million this year would be more advantageous.

[8:33:03 AM](#)

Mr. Haddon affirmed Senator Hoffman's assessment.

Mr. Haddon informed that bonds secured with TSRs have an expected payment date and a stated payment date. The Series 2000 bonds are targeted to pay off in 2015 with a stated maturity of 2031. The proposed bonds of Scenario 1 have stated payment date of 2060 and an expected payment date of 2041. He would therefore compare the 2015 payoff date of the Series 2000 bonds with the proposed expected payoff date of 2041 of Scenario 1 bonds. He agreed that the refunding of the original bonds and issuance of new bonds would extend the debt a number of years.

Mr. Haddon explained that by issuing new bonds, the State would receive a present value payment of future TSRs. If no changes were made and the original bonds paid out in 2015, the State would begin collecting revenue from the TSR although not in a "lump sum". If the Series 2000 bonds do not pay out in 2015, the State would not receive TSR revenue until the bonds were fully paid.

Mr. Haddon identified the policy question as whether to receive the funding "up front" based on projections that could be sold in the current marketplace; or to accept annual payments in the amount based on annual consumption once the original bonds are repaid. That amount could be significantly lower than current projections.

[8:34:59 AM](#)

Senator Hoffman countered that the amount could also be considerably higher.

[8:35:01 AM](#)

Mr. Haddon agreed this was possible. If so and new bonds were issued, those bonds would be paid off sooner.

[8:35:23 AM](#)

Senator Stedman commented to the question of whether the State should capitalize on the TSR at a time of surplus, or wait until oil prices are down and revenue is needed. A proposal that is "attractive today" could also be worth consideration several years in the future. This, plus how the revenues would be expended, are the policy discussions.

[8:36:30 AM](#)

Senator Bunde identified a third topic for policy discussion as the worth of the "price of doing business". The State would "give up a lot" by having use of the revenues immediately rather than allowing the settlement to "play out".

[8:37:00 AM](#)

Co-Chair Green asked the benefits of refunding and reissuing stocks at this time, and the benefits of making no changes.

[8:37:08 AM](#)

Mr. Haddon gave the favorable market as the reason for undertaking this now. Interest rates are relatively low compared to previous years and the market is "willing to accept" these bonds, meaning the bonds would be saleable. In 2004, the market was not favorable and similar bonds could not be sold. The question is whether the market would be favorable in the future for later bond issuances. Tobacco settlement-secured bonds represent a small portion of the bond market.

Mr. Haddon continued that the State could make no changes at this time if officials predicted that tobacco consumption would continue at the current level, the funds were not needed at this time, and receipt of future annual payments in unknown amounts was deemed acceptable.

[8:39:05 AM](#)

Senator Hoffman asked the amount the Series 2000 and 2001 bonds were sold.

[8:39:16 AM](#)

Mr. Haddon replied that he would provide this information, surmising the amount of the proposed sales would not be substantially different. Current rates are less than one percent or 100 basis points lower than they had been at the time of the original offerings. Refunding the existing bonds would not result in a significant savings. Therefore, he considered the proposals to be more of a restructuring.

[8:40:25 AM](#)

Senator Hoffman calculated that the State would generate \$114 million on the Series 2000 bonds by extending the potential earnings from 2015 to 2060.

[8:40:48 AM](#)

Mr. Haddon affirmed; clarifying the target payoff date of the Scenario 1 bonds is 2041.

[8:41:02 AM](#)

Senator Hoffman asked if the returns would not be a result of previous interest rates of 8.5 percent compared to the current rate of 5.5 percent as reflected on the graph on Page 5.

[8:41:13 AM](#)

Mr. Haddon noted the Series 2000 bonds were not sold at a rate of 8.5 percent. The graph instead demonstrated the rates in which the secondary bond market, i.e. tobacco settlement-secured bonds, has traded over time.

Mr. Haddon stated that if the maturity of the Series 2000 bonds was held at the 2015 target date and new bonds were sold "doing a straight refunding", the State would net \$20 million after escrow costs to restore the original bonds were paid. This amount is significantly less than the amount projected for Scenario 1 and demonstrates that approximately \$80 million of

the \$114 million would be generated as a result of extending the debt.

Mr. Haddon qualified that if the situation involved general obligation bonds rather than TSR secured bonds, and the State could save \$20 million, or ten-percent, through a refunding process, the State would likely undertake the process. Receiving an upfront payment of debt service cost of ten percent is "above the normal threshold that states look to do refundings for."

[8:43:14 AM](#)

Mr. Rattigan addressed refunding versus "new money". "Freeing up" the tobacco revenues currently dedicated to the Series 2000 and 2001 bonds would allow for issuance of bonds that would be "more desirable by the market." These are current interest bonds that "pay regular interest" and "come at a much lower interest rate" than the zero coupon bond structure that would be required if the refunding was not done.

Mr. Rattigan suggested that if a "new money target project list of a certain dollar amount" was agreed upon, the refunding of the existing bonds could allow for the issuance of new bonds at a lower interest rate. Significantly less zero coupon bonds, which are more expensive and generate lower proceeds, would be necessary.

AT EASE [8:44:14 AM](#) / [8:44:33 AM](#)

Senator Hoffman understood that \$20 million would be derived from the release of the Series 2000 and 2001 bonds if the State restructured the bonds.

[8:45:00 AM](#)

Mr. Haddon corrected that the State would receive \$20 million under a straight refunding scenario with a targeted maturity of 2015. The existing bonds have an \$11 million debt service reserve account and the new bond scenario would require a \$14 million debt service reserve. The \$3 million difference would be utilized to pay off the bonds at their maturity.

[8:45:42 AM](#)

Mr. Rattigan noted that the handout referenced for this presentation does not include a straight refunding scenario. This presentation is based on the assumption that the State would intend to generate more than \$20 million.

[8:46:24 AM](#)

Senator Stedman referenced conversations about the benefits of shifting risks given the uncertainty of future TSR payments and the potential that tobacco manufacturing corporations could dissolve. He requested financial information on these corporations, including international activities, Standard and Poor ratings and the bond and stock ratings of other firms, to help determine possible insolvency.

[8:47:37 AM](#)

Mr. Haddon replied that rating agencies carry ratings on all the major tobacco companies. However, those companies do not comprise the full component of the TSR. Small tobacco manufacturers also contribute. Philip Morris, Inc. represents approximately 50 percent of the marketplace and has been awarded a weak BBB rating by Standard and Poor.

Mr. Haddon also pointed out that the payments per the Master Settlement Agreement are based on domestically shipped cigarettes and do not involve the international markets. In evaluating the security of Philip Morris, only the domestic subsidiary of the company could be considered. RJR, Inc., formally Reynolds Tobacco, is rated below investment grade by the major rating services. The third largest tobacco company, Loews, is a larger conglomerate involving more than tobacco manufacturing. It is therefore difficult to isolate the rating of just its tobacco operations.

Mr. Haddon stated that the highest rating TSR secured bonds could receive is BBB. By considering the solvency of all participating manufacturers, the rating agencies consider the revenue stream for these bonds slightly stronger than the individual companies.

[8:49:52 AM](#)

Senator Stedman surmised that the market place already factors the current financial scenario of the settlement agreements.

Therefore, an imminent demise of the corporations would be reflected in current ratings.

[8:50:24 AM](#)

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#### Tobacco Securitization Credit Risks

[Flow Chart showing the interrelationship between Tobacco Securitization Credit and Non-Participating Manufacturer (NPM) Adjustment Risk; Decreased Market Share of Participating Manufacturers; Litigation Against Participating Manufacturers; Legal Risks to Master Settlement Agreement; Bankruptcy of Participating Manufacturers; and Uncertainty of Future Consumption.]

Mr. Haddon directed attention to this page to demonstrate the risks.

[8:51:00 AM](#)

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#### Market Share of PMs and NPMs

[Spreadsheet listing Historical Market Shares as follows:

##### OPMs

1998	-	96.5%
1999	-	92.3%
2000	-	91.4%
2001	-	89.4%
2002	-	86.1%
2003	-	84.5%
2004	-	83.75%

##### SPMs

1998	-	3%
1999	-	3.9%
2000	-	5.2%
2001	-	6.2%
2002	-	7.2%
2003	-	7.4%
2004	-	7.5%

##### NPMs

1998	-	0.5%
------	---	------

1999 - 3.7%  
2000 - 3.5%  
2001 - 4.4%  
2002 - 6.7%  
2003 - 8.2%  
2004 - 8.75%

Source: "Opinion And Order Partially Denying Preliminary Injunction" in 02 Civ. 2939 (AKH), September 14, 2004, Alvin K. Hellerstein, U.S. District Judge, United States District Court for the Southern District of New York.]

- NPMs pay into an escrow and do not contribute to the payments flowing to Settling States
- Increasing NPM market share means less money flowing to Settling States

Mr. Haddon stated this page demonstrates how market shares have changed with an increasing market share going to the nonparticipating manufacturers. An increase in NPM decreases the amount of revenue generated from the MSA because NPM do not make payments into the MSA. This is a risk of holding the TSR.

[8:51:40 AM](#)

Mr. Haddon returned to the flow chart on Page 18 to speak to the significant litigation against tobacco manufactures. Individual suits are filed, with occasional large judgments made against the manufacturers. Class action suits have also resulted in large judgments against the industry. Such continued losses could result in financial duress to manufacturers.

Mr. Haddon furthered that the Master Settlement Agreement itself is being challenged on "two major fronts." Small manufactures are challenging the MSA arguing it is an anti-trust agreement resulting in restraint of trade. If one of these challenges prevailed, the MSA could be "disrupted" and the requirement that the PMs make payments could be "decoupled".

Mr. Haddon explained the other challenge is "consumption risk going forward."

[8:53:22 AM](#)

Senator Stedman remarked that these bonds are not insured against default for the purchaser. The purchaser would have at least as much information about the MSA as the State does. Therefore, he surmised the purchaser would adjust the purchase price to reflect the perceived risk levels.

[8:53:57 AM](#)

Mr. Haddon affirmed, replying this is the reason the interest rates are higher yielding than general obligation bonds. There is no insurance on tobacco bonds and the purchaser requires higher payment for assuming the risk.

[8:54:20 AM](#)

Mr. Rattigan added that volatility of the secondary market trading is not only interest rate movement, but also includes "tobacco event occurrence" that caused the risk to be perceived as higher. The market evaluates events that could affect the securitization stream and adjusts accordingly either in the secondary market or in the primary market, which issued no tobacco securitization bonds in 2004 because the risk was deemed too high to be compensated by higher interest rates.

[8:55:05 AM](#)

Senator Stedman understood that the higher the risk level, the larger the discount the State must concede to attract purchasers. The larger discount would result in less income to the State in the future. He concluded, "It's not a zero sum gain."

[8:55:45 AM](#)

Mr. Haddon agreed.

[8:55:50 AM](#)

Mr. Haddon referenced the line graph on Page 5 to point out that the variance between the "general municipal market" and the secondary tobacco securitization market is currently minimal, indicating the market is favorable for selling new TSR bonds. The interest rate is determinative of the discount paid "to present value these payment streams". The higher the interest

rate, the bigger the discount factor, but would impact the amount of revenue received "up front" for the State.

Mr. Haddon characterized this as a situation in which the State could make no changes and receive the TSR funds once the existing bonds have matured in an amount higher or lower than current payments. The State could instead, refinance the bonds and receive the funds immediately.

Mr. Haddon concluded that if new bonds were sold and the State received the revenue "up front" and if the long-term TSR revenues were lower than projected, the State would have "got a good deal". If the TSR revenues were higher than projected, the bonds would be paid off sooner and the State would resume collecting the revenues earlier, albeit later than the repayment date of the existing bonds.

[8:58:16 AM](#)

Mr. Rattigan commented that in securitizing the TSRs and receiving money up front, the bondholder is assuming the risk.

[8:59:49 AM](#)

Senator Olson asked the impact on the State's bond rating in the event of a "catastrophic event" involving the MSA.

[9:00:05 AM](#)

Mr. Rattigan replied that such an event should have not affect on Alaska's credit ratings. Bond raters recognize the TSR bonds are no reflection of the State's solvency.

[9:00:33 AM](#)

Senator Olson asked what actions other states were taking in this regard.

[9:00:44 AM](#)

Mr. Haddon referred back to Page 4 and the US map listing the completed and pending tobacco securitizations of all states and some counties and cities. Other states are considering restructuring existing bonds and issuing new bonds.

[9:01:52 AM](#)

Mr. Rattigan noted that approximately three-quarters of the "deals" done in 2005 and 2006 have been refundings of earlier offerings.

[9:02:40 AM](#)

Mr. Haddon asserted that the market is favorable for such activities. Alaska would not be required to do refunding of its existing bond offerings. New bonds could be sold, although this would require additional legal restructuring. These are policy issues the legislature must decide to determine the length of extension.

Mr. Haddon stated he would provide additional information to address questions raised during this presentation.

[9:03:30 AM](#)

Senator Dyson asked the amount that citigroup would earn if the State undertook the refinancing of existing bonds and issuance of new bonds. He also asked the net return that the holders of the existing bonds would realize.

[9:04:12 AM](#)

Mr. Haddon responded that if the Series 2000 bonds were restructured, the bondholders would receive payment from the escrow account. The "security character" of those bonds would be changed, as the TSR revenues would no longer be the guarantee. These bonds would have higher value.

Mr. Haddon continued that the bondholders would have the option to redeploy "that money" into the new bonds. As an underwriter, citigroup would attempt to have the Series 2000 bondholders to purchase the new bonds at a higher interest rate. However, the bondholders would not be required to do so.

[9:05:38 AM](#)

Senator Dyson again asked the rates and the net return the bondholders would receive.

[9:05:53 AM](#)

Mr. Haddon stated that citigroup could sell new bonds at lower rates, with the bondholders obtaining bonds with a lower yield. The escrow guarantee on the existing bonds would provide incentive to purchase the new bonds.

[9:06:35 AM](#)

Mr. Rattigan furthered that the holder of Series 2000 bonds, if purchased at the initial offering would receive a return rate of approximately six percent. If the initial bonds were sold at present in the current market, a higher gain of "a few percentage points" would be realized based on the value of the bonds at the time of sale. The bondholders would not be required to sell the bonds.

Mr. Rattigan continued that the return on the new bonds would not be set until they were sold and would be determined by the market. The new bonds would likely have a lower rate of return than the existing bonds. A regular market exists for tobacco bonds, those issued by all participating states and local governments. The return on the original Alaska bonds that had been traded would be dictated by the market rate at the time they were traded.

[9:08:47 AM](#)

Senator Dyson expressed that the witnesses did not answer any of his questions. He again asked how much the company would earn from these transactions.

[9:09:06 AM](#)

Mr. Haddon told of an underwriting discount, spread, or fee paid on tobacco bonds. The underwriting fee on bonds sold for \$216 million would be approximately \$1.2 million. If citigroup were the lead underwriter, it would expect to receive fifty percent of the fee, or \$600,000.

[9:09:49 AM](#)

Senator Dyson reposed his second question asking the amount the bondholders could potentially realize if the State were to refund existing bonds and issue new bonds. He asked if the amount would be \$5 million, \$10 million or another amount.

[9:10:14 AM](#)

Mr. Haddon responded that the value of the bonds is determined by interest rates. The value of the Series 2000 bonds at the time of initial purchase was low because the interest rates were high. As interest rates decreased, the value of the bonds increased. The increased value of the bonds would only be realized if the bonds were sold when the interest rates were lower.

Mr. Haddon continued that Series 2000 bonds would actually trade at an amount higher than 100 cents on the dollar if the State restructured because the original bonds would have a higher security. However, the bonds would generate a lower interest rate and those bondholders could chose to redeploy their investment into the new bonds, which would pay a higher interest rate.

[9:12:16 AM](#)

Senator Stedman stated that the \$2.8 million "COI and Underwriter's Discount" deduction from "Gross Proceeds" in Scenario 1 shown on Page 16 is "the cost of doing the deal". He asked how the amount designated for the escrow account is determined, and whether the amount is an estimate or a firm figure.

[9:13:22 AM](#)

Mr. Haddon answered that the escrow amount is not an estimate. It is calculated, for Scenario 1, from the debt service owed on the Series 2000 bond deal for the "call date". The call date is the date when the bonds could be retired. The escrow account is established to make the interest payments to the call date and provide principle to retire the bonds. The original terms of the Series 2000 bonds provided that the bonds could be "called in" on "certain terms" and therefore the call date would be defined by those requirements as well as the debt service requirements on those bonds. An independent accountant does this calculation to ensure accuracy. This is a legal requirement and the amount must be calculated to the "penny".

[9:14:34 AM](#)

Senator Stedman asked if no reinvestment risk would be incurred.

[9:14:42 AM](#)

Mr. Rattigan responded that no reinvestment risk would exist for the escrow, due to the requirement that the account have sufficient funds. Tobacco securitization contains many "nuance and complications". The escrow and refunding components are no different than any refundings the State has done in the past. He gave airport bonds as an example in which older bonds were refunded to achieve a savings. Those older airport bonds are now guaranteed by an escrow account and no longer have any claim to airport revenues. At the time of pricing, a deposit is required in an amount verified by an independent accounting firm to be sufficient.

[9:15:46 AM](#)

Senator Stedman asked if escrow funds would be set aside and would collect interest.

Mr. Haddon affirmed.

Senator Stedman asked how all interest rate exposure would be removed. The escrow account would be held for years if not decades.

[9:16:17 AM](#)

Mr. Haddon replied that the escrow funds would be utilized to purchase federal government securities guaranteed by the U.S. Treasury Department or other federal agencies. The interest rate of those securities would be fixed and the income generated would be calculated to determine the amount of securities necessary to pay the principle and interest payments on the original bonds. The escrow account is required before the TSRs could be pledged for new bonds.

[9:17:33 AM](#)

Senator Stedman understood the issue of buying zero coupons or government backed bonds. He asked about the imbedded costs of establishing and administering the escrow account.

[9:18:05 AM](#)

Mr. Haddon answered that the escrow account would have no embedded cost. The securities "will cost what they cost based on the current market". The \$88 million cited for Scenario 1 could change with interest rates over next couple weeks. This is the risk of delaying the transaction.

[9:18:39 AM](#)

Mr. Rattigan told of the requirement that the securities purchased to fund the escrow "are bid out to the market" to ensure that the State has achieved the "best possible price." Bond council would also provide a "defeasance opinion" avowing that the Series 2000 bonds were officially defeased and no longer have the right to receive TSR payments they were originally secured by.

[9:19:23 AM](#)

Co-Chair Green suggested the witnesses meet with interested Committee members individually to address concerns and respond to questions.

[9:19:39 AM](#)

The bill was HELD in Committee.

#SB231

[9:20:11 AM](#)

SENATE BILL NO. 231

"An Act making appropriations, including capital appropriations and appropriations to capitalize funds; and providing for an effective date."

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

[9:20:27 AM](#)

CHERYL FRASCA, Director, Office of Management and Budget, Office of the Governor, gave a presentation utilizing a handout titled, "Governor's Capital Budget Proposals, Senate Finance Committee,

Cheryl Frasca, Director, Office of Management and Budget" [copy on file].

[9:21:10 AM](#)

Page 2

Capital Budgets by Fund Source FY 98 - FY 07  
[Bar graph showing amount in million of dollars of federal funds, general funds and other funds for each of the fiscal years indicated.]

Ms. Frasca pointed out the proposed FY 07 capital budget would appropriate approximately \$125 million more general funds than the previous year. The graph shows the funding sources in context over time.

[9:21:57 AM](#)

Page 3

FY 07 Capital Budget by Program Category  
General Funds & Other Funds

[Pie chart demonstrating the following:

Transportation	55%
Development	6%
Natural Resources	2%
Education	5%
University	15%
General Government	<1%
Health & Human Services	8%
Housing/Social Services	5%
Public Protection	3%
Law & Justice	1%]

Ms. Frasca explained this chart does not delineate by department, but rather program category, and includes both general fund and other fund sources. Capital budgets of the 1970s and 1980s were categorized in this manner. She pointed out that Law and Justice activities involve more agencies than the Department of Corrections and the Department of Public Safety. It also encompasses the Office of Public Advocacy, the Public Defenders Agency, the Alaska Court System and other State agencies.

Ms. Frasca stated that approximately \$350 million was proposed for the Transportation category and \$98 million for the University of Alaska. The funding source for the University projects would be proceeds from tobacco securitization bonds. Health and Human Services projects would receive \$52 million and Housing and Social Services would receive \$32 million.

[9:24:11 AM](#)

Page 4

FY 07 Capital Budget by Fund Source

[Pie chart demonstrating the following:

Federal Funds	\$1,268.8m	66%
General Funds	465.2m	24%
Tobacco Refinance	89,2m	5%
Other Funds	65.9m	3%
AHFC Dividend	31.2m	2%]

Ms. Frasca overviewed this page.

[9:24:46 AM](#)

Page 5

Investment of FY 06 Additional Revenue

December 15, 2005 Proposal

[Pie chart demonstrating the following:

Advance Fund K-12 Education	\$565 million
Deferred Maintenance	43 million
Save for Gas Pipeline Ownership	400 million
Road Projects	86 million]

Ms. Frasca informed that Governor Frank Murkowski proposed to invest a portion of the surplus revenue generated in FY 06 into capital projects. This is a notable event, although not much different than the legislator's decision to appropriate excess earnings of FY 05 for FY 06 capital projects.

Ms. Frasca listed examples of the intended transportation, including \$86 million for repaving the Richardson Highway, \$12 million for improvements to the Palmer/Wasilla Highway, and \$30 million for projects to alleviate congestion in Anchorage.

Ms. Frasca also told of \$700 million in identified deferred maintenance needs, of which the University submitted requests for approximately \$428 million. The Office of Management and Budget selected projects totaling \$43 million to be addressed in FY 07. Almost \$9 million of the amended amount would be appropriated for transportation projects, \$10 million for the University, and \$1.6 million for parks.

[9:27:09 AM](#)

Page 6

Investment Priority: K-12 Education

- Alternatives to help more Alaskans succeed
  - Galena, Nenana boarding schools
  - Military Youth Academy expansion
  - Mt. Edgecumbe maintenance, repairs
- School maintenance, construction
  - 78% FY 06 grants unexpended to date
  - School debt reimbursement
    - \$134 million (19%) from 2002 approved by voters but unsold
    - \$185 million (97%) from 2005 not yet approved by voters

Ms. Frasca acknowledged that increased funding is requested in the FY 07 operating budget for K-12 education; however, capital investments are necessary for some alternative education programs. The Mt. Edgecumbe facility was constructed during the 1940s.

Ms. Frasca explained the reason that a significant percentage of grants approved for FY 06 had not yet been expended because the funds became available in July 2006 after the onset of the construction season. Most of these funds would be expended in the upcoming 2007 summer construction season.

Ms. Frasca stated that some projects identified for the grants approved by the legislature in 2002 had yet to be presented for voter approval, thus explaining the unexpended balance of that appropriation.

[9:30:05 AM](#)

Senator Dyson requested affirmation that all the projects outstanding for which grants were approved in 2002 had not yet been subject to voter approval.

[9:30:25 AM](#)

Ms. Frasca corrected that some of the projects had been placed on the ballot but were rejected by voters.

[9:30:37 AM](#)

Page 7

Investment Priority: University of Alaska

- Maintain existing facilities, equipment
  - \$35 million of \$98 million requested
- New facilities, other projects
  - \$55 million of \$152 million requested
    - Funds first priority: Integrated Science Building

Ms. Frasca noted the board of Regents requested \$98 million for deferred maintenance projects. The Integrated Science Building is located on the University of Alaska, Anchorage campus.

[9:31:27 AM](#)

Page 8

Investment Priority: Job Training

- Preparing Alaskans for the future's opportunities
  - Fairbanks Pipeline Training Center
  - AVTEC
    - Distance training videoconferencing
    - Dormitory remodel
    - Facility replacement

Ms. Frasca spoke to the job training needs, especially in preparation of a natural gas pipeline. The Governor proposes a \$3 million grant to fund the Fairbanks Pipeline Training Center. The Committee supported this effort the previous legislative session.

Ms. Frasca informed of the intent to provide distance-training programs through the Alaska Vocational Technical Center (AVTEC)

to rural areas. Additionally, the dormitories at the campus are 30 years old, pose life safety issues and must be upgraded to comply with safety codes. An appropriation of \$2 million is requested to replace a facility on the campus. The current facility was constructed ten years ago with the intent it would be temporary.

[9:32:55 AM](#)

Page 9

Investment Priority: Resource Development

- Oil and gas development
  - Unified Permitting Process
  - Frontier Basis Geologic Assessment
  - Bristol Bay Energy Development
  - Geologic Data for new North Slope Exploration
  - Pipeline Corridor Geologic Hazards
  - Shallow Coring Program

Ms. Frasca stated the funding requested for the Unified Permitting Process would be utilized for the third phase of a multi-year project to modernize the system. The Frontier Basis Geologic Assessment would allow for oil and gas development. The Bristol Bay Energy Development project pertains to a new lease and would provide an understanding of resources. The Geological Data project would provide the State with information to obtain maximum investment with private industry. The proposed natural gas pipeline could go through Delta Junction to the Canadian border, so the geologic hazards of that area must be studied. The Shallow Coring Program would generate data on potential resources around the state.

[9:34:51 AM](#)

Page 10

Investment Priority: Public Safety

- Tools to respond effectively
  - APSIN re-design
  - Online fire, life safety plan review system
  - Crime lab design
- Emergency preparedness
  - ALMR, satellite phones
  - Alert warning system

- Correctional system upkeep

Ms. Frasca told of the Alaska Public Safety Information Network (ASPIN) that would enable data sharing with all law enforcement agencies operating in the state. The FY 07 proposed capital budget includes \$3 million State funds and \$1 million federal funds for this project.

Ms. Frasca stated that the on-line fire, life safety plan review system would make the processes more efficient.

Ms. Frasca requested \$4.8 million to design a new crime laboratory. Yesterday a connection was made in the DNA evidence of a murder that occurred in 1991. The existing laboratory is undersized.

Ms. Frasca deferred to the Department of Administration and the Department of Natural Resources to detail the Alaska Land Mobile Radio (ALMAR) project.

Ms. Frasca informed that funding is necessary to make the Alert Warning System compliant with federal standards.

Ms. Frasca described the planned correctional system upkeep projects as typical maintenance and repair items and completion of the installation of a closed circuit monitoring system.

[9:37:17 AM](#)

Page 11

Investment Priority: Public's Health

- Safe water, sewer
  - VSW and community projects
- Immunization, Disease Registry
- Safe community housing
  - Bring the Kids Home
  - Pioneer Homes code compliance
  - AHFC programs

Ms. Frasca noted the request of approximately \$29 million general funds to match \$74 million federal funds for the Village Safe Water (VSW) program. Other community projects include one located in Sawmill Cove at Sitka, the landfill at Unalaska, and the water line at Ketchikan.

Ms. Frasca told of the requested immunization and disease registry tracking system and database for the Department of Health and Social Services that would provide "real time" information. The current system is not as updated as those in other states and is necessary to address certain events such as Hurricane Katrina.

Ms. Frasca stated that planning, design and construction of facilities is necessary to implement the Bring the Kids Home plan. Planned Alaska Housing Finance Corporation (AHFC) projects include creating housing for teachers and public safety officials. Eighteen communities have applied for grants to fund these projects, which has assisted villages with teacher retention.

[9:39:52 AM](#)

Page 12

Investment Priority: Transportation

- \$481 million of overall capital budget
- State match of \$90 million for \$405 million
  - Aviation \$16 million
  - Highways: \$74 million
- State harbors, docks, AMHS - \$41 million
- Community priorities
  - Pt. Mackenzie Road
  - Port of Anchorage
  - Seward Dock
  - Whittier boat harbor

Ms. Frasca informed that transportation projects comprise the largest amount of general fund and other State funding appropriations in the FY 07 proposed capital budget. Eight projects at State-owned harbors have been identified for upgrades and eventual transfer to local government ownership. The Governor is requesting \$14 million for the Point Mackenzie Road project. The Port of Anchorage serves statewide purposes and the Seward Dock has been identified as a local priority. The Whittier boat harbor project would expand the existing facilities and allow for additional waterfront development.

[9:42:01 AM](#)

Governor's Transportation Initiative:

- Prepare Alaska's infrastructure for tomorrow's opportunities
  - o Alaska Railroad extension
  - o Juneau Access
  - o Roads to Resources
  - o Parks Highway
  - o Dalton Highway

Ms. Frasca noted that funding for these projects would be entirely State general funds.

Ms. Frasca spoke to the extension of the Alaska Railroad to the Canadian border. A feasibility study was underway in cooperation with the Yukon Territory and British Columbia and Canadian First Nations to determine potential routes and the economic benefit to Alaska. If the study, to be completed in July 2006, finds the plan feasible, the \$50 million of this request would be utilized for the next step of the project. If the study determines the plan to not be feasible, the funding would not be expended and would lapse to the general fund available for legislative appropriation the next session.

Ms. Frasca noted the \$45 million requested for the Juneau Access project would be expended to include the road, terminals and ferries related to the project.

Ms. Frasca explained the Roads to Resources program relates to industrial roads and that the funding would be utilized to further projects including access to Point Thompson, a Foothills West road, Lucky Shot line and timber access roads in Southeast. The program is intended to address opportunities as they arise.

Ms. Frasca informed that funds were needed to address load capacity on the Parks Highway. Currently load limits must be imposed for approximately six months each year. This results in higher costs, as goods must be transported in smaller loads.

Ms. Frasca stressed the importance of maintaining the Dalton Highway, which serves as a link to oil and gas development sites on the North Slope. The requested funding would allow for continued maintenance. Co-Chair Wilken wrote a letter in support of such activities.

[9:46:30 AM](#)

Page 14

Investment Priority: Economic Development

- Tourism destination promotion, development
  - Morris Thompson Cultural, Visitor Center
  - Tongass Coast Aquarium
  - Anchorage Museum
  - Alaska Native Heritage Center
- Maintain parks, campgrounds

Ms. Frasca emphasized the need to make Alaska more attractive to tourists. Funding from other sources has been secured for each of the aforementioned projects; the requested general funds would provide the State's contribution. The Alaska Tourism Association provides marketing for businesses located along the road system aimed at independent and international travelers.

Ms. Frasca expressed appreciation for the Committee's appropriation for State park operations. Additional capital funds are requested to ensure the parks are well maintained.

[9:48:09 AM](#)

Senator Stedman pointed out that the proposed Gravina Island bridge project in Ketchikan was not included in the community transportation priorities listed on page 12.

[9:48:37 AM](#)

Ms. Frasca responded that this listing did not focus on federal projects. The Governor's proposed budget contains an appropriation to provide State matching funds for the project.

[9:49:24 AM](#)

Senator Stedman, referencing page 2, questioned the comparisons to budgets of previous years.

[9:50:10 AM](#)

Ms. Frasca explained that the graph is intended to demonstrate a pattern over a period of time. She admitted some appropriations

made in one year were not expended until the following year. She would provide detailed information.

[9:51:23 AM](#)

Senator Stedman asked how receipt authority for funds never actually received is reflected in this presentation.

[9:51:42 AM](#)

Ms. Frasca acknowledged that "budgeting versus spending" is not delineated. She gave FY 05 as an example as including federal receipt authority for the Gravina Island and Knik Arm Crossing projects, although the funds were not received in that year.

[9:52:30 AM](#)

Senator Stedman commented that at times, authority is granted but the funds are not received.

[9:52:43 AM](#)

Co-Chair Wilken appreciated the emphasis on the Dalton Highway. He traveled this road during the 1980s and again last year. The road condition was worse on his second trip and he was surprised at the amount of traffic activity. Some areas were dangerous. Upgrades are needed given the increased natural resource exploration occurring on the North Slope.

[9:53:56 AM](#)

Co-Chair Wilken understood that discussions had occurred with the Governor's staff regarding funding a science facility at the University of Alaska, Fairbanks campus utilizing tobacco settlement receipts. However, the project is not included in this Governor's proposed budget, although funding for the integrated science facility at the Anchorage campus is included. He requested to be kept better apprised of these discussions and decisions.

[9:54:25 AM](#)

Senator Olson asked about improvements to the Dalton Highway.

[9:54:58 AM](#)

Ms. Frasca responded that the Department of Transportation and Public Facilities has a five-year proposal for upgrading and improving the Dalton Highway.

[9:55:40 AM](#)

Senator Dyson asked if the project to extend lighting along the Glenn Highway between Anchorage and the Parks Highway is included in the Governor's request.

Ms. Frasca would provide information on this.

[9:56:20 AM](#)

Senator Dyson understood that a certain percentage of spending be allocated for capital projects. He asked the specifics of this guideline.

[9:56:50 AM](#)

Ms. Frasca surmised that Senator Dyson was speaking to the constitutional spending limit instituted under the governorship of Jay Hammond, which directed that one-third of spending be allocated for capital improvements. This provision has never been implemented because revenues were inadequate to "support the level of spending" allowed under that limit. Otherwise, she was unaware of no requirements for distribution of appropriations for capital projects.

[9:58:12 AM](#)

Presentation by Department of Administration  
on the  
Alaska Land Mobile Radio Project

AT EASE [9:58:18 AM](#)

[10:01:18 AM](#)

KEVIN BROOKS, Deputy Commissioner, Department of Administration, introduced Mr. Callahan who recently transferred to the Department from the Department of Military and Veterans Affairs

where he was head of the Alaska Land Mobile Radio Project (ALMR).

MIKE CALLAHAN, Director, Enterprise Technology Services, Department of Administration, gave a presentation titled, "Alaska Land Mobile Radio Project, ALMAR, Presented by: The Department of Administration" [copy on file].

[10:01:57 AM](#)

Page 2

What is the ALMR project?

- The first step in statewide interoperable communications for the State of Alaska
  - Ability to communicate on demand in real time
- First responders first
- ALMR was created in 1995 as a broad governmental partnership
- Executive Council representatives
  - Department of Defense
  - State of Alaska
  - Alaska Municipal League
  - Federal (Non-DoD) agencies

Mr. Callahan outlined this information. He gave examples of first responders as those who would fight fires and respond to crimes.

[10:03:27 AM](#)

Page 3

LMR Now A National Issue

Compatible radio systems would cost billions  
By Paul Davidson, USA TODAY

As chaos engulfed New Orleans after Hurricane Katrina struck, emergency responders traded urgent information in a way that was hardly a model of 21st century high technology.

With the floodwaters surging, they scurried on foot to ferry messages among city police, state troopers and the National Guard.

It's not that the agencies' radio systems didn't work. They just didn't work with each other.

The breakdown in New Orleans was the latest proof of a troubling quandary: Many of the USA's 50,000 public-safety agencies still can't talk to each other in a crisis. The problem has plagued emergency responders in every big disaster in recent memory - from the Oklahoma City bombing to 9/11 to Katrina.

The main culprit? Incompatible radio equipment.

"We didn't learn our lesson after the '93 World Trade Center bombing; we didn't learn our lesson after Sept. 11," Senate Commerce Committee hearing on Katrina. "We don't need anymore failures."

H. Darr Beiser, USA TODAY

Mr. Callahan pointed out the issue is not unique to Alaska and would not "go away" unaddressed. In this state, events such as the Millers Reach wildfire, emergency calls to 911 and others raised questions as to why emergency workers were unable to communicate with each other.

[10:03:52 AM](#)

Page 4

Project objectives:

- Replace aging LMR infrastructure
- Enhance personnel safety and operational capabilities
- Phased implementation
  - o Highway system
  - o Southeast Alaska and Kodiak
  - o Rural areas where cost effective
- Cost share infrastructure cost among the federal, state and local governments

Mr. Callahan informed that both systems currently in operation have reached the end of their period of usability and that replacement parts could no longer be obtained. Rather than just purchasing new radios, the system would be upgraded and replaced.

Mr. Callahan reported that the highway system portion of the project was completed the previous year and includes the road systems from Valdez to Fairbanks to Anchorage and Kenai. System

replacement for Southeast Alaska would be undertaken in the upcoming year.

Mr. Callahan stated that because this project involves the US Department of Defense, a significant amount of federal funding is appropriated.

[10:05:19 AM](#)

Page 5

Current Phase Build out

[Map depicting Alaska, with the exception of the northernmost area, with multiple sites marked as ALMAR locations.]

Mr. Callahan stressed the importance of the site located on St. Paul Island.

[10:05:43 AM](#)

Page 6

End of 2004 Status

[Map depicting and area spanning from the Canadian Border to the east, the Kenai Peninsula to the south, Mount Susitna to the north and Money Knob (north of Fairbanks) to the north. Areas including Valdez, Anchorage, the Alaska Highway between Ester and Delta and an area east of Fairbanks are highlighted.]

Mr. Callahan compared the progress of this year to that of the following year.

[10:05:51 AM](#)

Page 7

[Map depicting and area spanning from the Canadian Border to the east, the Kenai Peninsula to the south, Mount Susitna to the north and Money Knob (north of Fairbanks) to the north. Most areas along the major road systems between Valdez and Fairbanks, Delta and Tok, Ester and Whittier and Seward, and Glennallen and Anchorage are highlighted.]

Mr. Callahan spoke to the "immense amount of work" accomplished during this period. Although not officially completed, the system is operational in the highlighted areas.

[10:06:17 AM](#)

Co-Chair Wilken asked when the sites of Gerstle River, Byers Creek, and Honolulu would be addressed. These areas on the Alaska Highway and the Parks Highway are not highlighted as completed on the aforementioned map.

[10:06:31 AM](#)

Mr. Callahan replied that these sites are scheduled for completion in the current year. These areas present unique challenges. Permit issues in the Honolulu locations had to be resolved. Other sites require significant expense to deliver power to the facilities.

[10:07:26 AM](#)

Co-Chair Wilken clarified that power delivery is the reason the three sites were not completed with the majority of the project in this region.

[10:07:33 AM](#)

Mr. Callahan affirmed, noting that the problem is likely solved for two of those sites.

[10:07:43 AM](#)

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How does this benefit Alaska?

- 1st responders can now communicate with each other on a single radio platform.
- ALMR will serve 87 sites along the highway and railbelt from Anchorage to Fairbanks and down to Kodiak, at the completion of this phase of the buildout.
- Sites connected via SOA microwave system (SATS)

- o Fully meets congressional mandates for a "private, government owned and operated LMR network for first responders"
- o Enhanced survivability compared to fiber optics
- Establishes infrastructure for future mobile data projects and remote data reporting

Mr. Callahan defined the "private, government owned and operated LMR network" as being limited to first response use. This would avoid an incident in which a first responder was unable to access the network due to a high volume of other users, such as what occurs in Anchorage during rush hour commutes.

[10:08:27 AM](#)

Senator Hoffman asked if first responders include health care workers.

[10:08:31 AM](#)

Mr. Callahan affirmed, adding that security personnel for the TransAlaska Pipeline System would also be connected to the system.

Mr. Callahan cited the most significant danger to the existing system would be earthquake damage to fiber optic cables.

Mr. Callahan listed future uses of the ALMAR system. The Department of Transportation and Public Facilities is considering installing cameras at weather stations to provide information on road conditions. Also, "wire connection" could be established for "road workers".

[10:10:37 AM](#)

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#### 2005 Key Accomplishments:

- Implemented 41 sites, covering the bulk of the road system between Anchorage and Fairbanks
- The Users Council is operational
- Completed St. Paul Island technology demonstration
- Two Transportable Sites
  - o Quickly add coverage

- o Augment existing coverage

[Photograph of a facility titled, "R1 North" including a two-story building, radio towers and satellite disks.]

Mr. Callahan noted that as of 1995, the system could not work over satellite. Vendors changed technology and tests of the new systems were successful. The system could be utilized in rural areas.

Mr. Callahan explained the advantages of the transportable sites in the event of a large disaster in which the basic system were overloaded.

[10:12:28 AM](#)

Page 10

Direct Benefits:

- December 2005 - for the first time ever, DOT snow removal crews can communicate with each other via 2-way radio in Thompson Pass.
- Alaska Shield/Northern Edge '05 Homeland Security Exercise
  - o One of three "national level of interest" exercises for the year
  - o ALMR was the successful technology demonstration project for the exercise

Mr. Callahan stressed the importance of communication between snow removal crews, as they routinely plow in white-out conditions. If a vehicle went off the road, assistance could be given immediately thus reducing life-threatening situations.

Mr. Callahan reported that the security exercises determined the ALMR technology to be sufficient.

[10:13:57 AM](#)

Page 11

Financial Status Report

[Spreadsheet showing the following:

Funded to Date	
Department of Defense	\$65,300,000
State of Alaska	17,977,000
Federal Grants	13,827,442
Project Total	\$97,104,442
Funding to Finish	
State of Alaska	2,500,000
Federal Grants	7,500,000

\*Note: \$5 million additional SATS infrastructure money included in FY 07 request.]

Mr. Callahan qualified that the Governor's proposed FY 07 budget includes additional funding requests. Half of the requests relate to the ALMR project with the remaining relating to other maintenance requirements.

[10:15:15 AM](#)

Page 12

How we service these sites:

[Three photographs showing sites in remote locations with helicopters flying overhead, towing a large container and landed.]

Mr. Callahan commented to the difficult accessibility to some locations, noting one site was "blown off the top of the mountain."

[10:15:36 AM](#)

Page 13

Winter Challenges

[Two photographs of the Mt. Bede site in winter conditions with blown snowpack covering the building and tower. A person wearing a survival suit is shown at the site.]

Mr. Callahan told the Committee that crews used chainsaws to penetrate the snow pack.

[10:15:55 AM](#)

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Pillsbury Mountain Site

[Two photographs of a worker at this location showing the small building, transmission tower, a solar panel and other equipment on a clear day with a few inches of snow-covering.]

Page 15

Saddle Mountain (Juneau) site

[Photograph of building, towers, solar panel and miscellaneous gear on the snow-free mountaintop site next to an alpine lake overlooking Gastineau Channel.]

Mr. Callahan noted that some maintenance work is conducted during summer months.

[10:16:17 AM](#)

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Frequently Asked Questions

Mr. Callahan indicated the following pages address these questions.

[10:16:24 AM](#)

Page 17

Is the existing ALMR system compatible with the planned Municipality of Anchorage system?

- Yes. The Muni system will use 700 MHz frequencies instead of VHF, but the three system controllers will interconnect the users
- If Muni assets/subscribers travel outside the Anchorage bowl they will use their deployable VHF radios, with they are buying with the system

Mr. Callahan outlined this information.

[10:17:11 AM](#)

Page 18

Is ALMR Outdated Technology?

- No
- The ALMR System fully meets congressional mandates for a "private, government owned and operated LMR network for first responders"

Mr. Callahan informed that one additional upgrade would be installed in the fall, after which, no mandatory upgrades would be required for 14 years.

[10:18:09 AM](#)

Page 19

How many Radios are on the system?

- Current: 9,894
- Projected by end of CY 2007: 14,900

Mr. Callahan reiterated that the system is operational despite not being officially completed.

[10:18:21 AM](#)

Page 20

Are all costs included in these budget numbers?

- All infrastructure costs are covered.
- Subscriber units are the responsibility of the individual agencies. Almost all non-state agencies buy their subscriber units using federal grant funds.

Mr. Callahan explained that participating municipalities are applying for federal funds for their portions of this program.

[10:18:45 AM](#)

Page 21

What is the Cost per unit for radios?

[Spreadsheet listing the following:

Portable (Handheld)		
Motorola	\$4771	
EF Johnson	2324	
Mobile (Installed in Vehicle)		
Motorola	\$5514	
EF Johnson	3442]	

Mr. Callahan noted that some first responder participants would be unable to secure total funding for the purchase of these units and that the State is "trying to help them". He exemplified that the Ester Volunteer Fire Department could not hold enough pancake breakfasts necessary to raise enough funding to buy the five radios it needs.

[10:19:06 AM](#)

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Projected FY 08 Budget impacts/requirements

- Capital funds: Motobridge Interconnect Requirements \$2.764M
  - Originally Department of Defense funded - lost funds
  - Intent to fund through federal grant/s
  - Uncertainty due to changes in earmark capabilities
- O&M funds: Chargebacks & options
  - Model not defined and agreed
  - Proposals range from "you play, you pay - by radio" to State of Alaska and Department of Defense split the cost

Mr. Callahan informed that the State "lost" federal funds to competing grants.

Mr. Callahan cautioned that "earmark" rule changes could affect the amount of federal funding received. However, he was "highly confident" the State would receive the full amount of these funds because the ALMR project matches the federal government's plan for homeland security.

Mr. Callahan stated that information regarding the operation and maintenance funds would be available by August 2006.

[10:20:38 AM](#)

Senator Olson, referencing the locations of ALMR sites on a map of Alaska, noted the "line of sight" between most locations. He asked why a facility was constructed on St. Paul Island, which does not appear to be in the line of sight of the other locations.

[10:21:02 AM](#)

Mr. Callahan told of the test project conducted in conjunction with the US Institute of Justice to demonstrate the system could operate over satellite link. Such a link was not technologically supportable until a year ago.

[10:21:30 AM](#)

Senator Olson asked the plan for distribution of the ALMR to the remainder of the state.

[10:21:38 AM](#)

Mr. Callahan responded that a plan had yet to be determined. With satellite capacity, more areas could be addressed. Sites in regional hubs would likely be chosen rather locating the system in every village. A more cost effective method would need to be identified.

[10:22:16 AM](#)

Senator Hoffman asked the cost of the Pribilof site.

[10:22:25 AM](#)

Mr. Callahan replied the cost was "slightly" over \$300,000. Infrastructure was already available on St. Paul Island, including a power supply and radio tower.

[10:22:55 AM](#)

Senator Hoffman asked if existing infrastructure in other rural sites, such as Dillingham and Bethel, was sufficient to accommodate an ALMR site.

[10:23:12 AM](#)

Mr. Callahan answered that generally these communities did not have the necessary infrastructure. Although a mixed frequency repeater exists in Bethel, it would require significant upgrades to integrate with the ALMR system.

[10:23:40 AM](#)

Co-Chair Wilken asked the amount of power required to operate sites such as the Pillsbury Mountain site.

[10:23:58 AM](#)

Mr. Callahan responded that the amount of power necessary to operate a site varies on the number of channels utilized. Peak power is 18.5 kilowatts.

[10:24:26 AM](#)

Senator Olson acknowledged this is a significant amount of power.

[10:24:31 AM](#)

Mr. Callahan stated this explains the problems encountered when a site could not be linked to an existing power grid.

[10:24:53 AM](#)

KEVIN BROOKS, Deputy Commissioner, Department of Administration, furthered Ms. Frasca comments on proposed capital information technology projects utilizing a spreadsheet titled, "Capital IT Projects" [copy on file]. The spreadsheets list over 35 projects totaling \$64 million of which approximately \$13 million is general funds. These projects involve 11 State departments.

Mr. Brooks outlined the process undertaken to identify and review these projects and select only those that are technologically supportable, meet the business needs of the affected department, and would provide a service to the public.

[10:26:47 AM](#)

Mr. Brooks informed that during the summer of 2003 the state began a process to develop a statewide information technology plan. Before then, State agencies were "working hard doing some really great things with computers" to implement permitting processes and providing public access. However, this was done without an enterprise approach. Instead, each agency addressed only their own business needs and not attention was given to the interaction of State agencies. As a result, some redundancies occurred. Three years ago, department representatives agreed to the need to "work better and smarter".

Mr. Brooks stated the plan adopted in 2003 has been updated annually, with the third revision completed in preparation for the FY 07 Capital budget.

Mr. Brooks told of the establishment of the five-member Enterprise Investment Board that meets twice a year to ensure the overall policy direction and investment level was appropriate as it relates to the remainder of the budget. The commissioner of the Department of Administration, the director of the Office of Management and Budget, the chief of staff to the governor, a director of a State Division of Administrative Services, and the director of the Enterprise Technology Services, comprise the membership.

[10:29:16 AM](#)

Mr. Brooks explained the precluding level of review consists of the directors of administrative services divisions of all 15 State departments. This IT workgroup meets regularly to address matters of common concern.

[10:29:44 AM](#)

Mr. Brooks informed that each department now employs an Information Technology (IT) Manager. Previously, many departments did not have a centralized "voice" to address information technology. Six of these managers serve on a Technology Management Council. This council establishes standards and guidelines to ensure that agencies are working in collaboration.

Mr. Brooks noted that the IT managers of the Department of Health and Social Services and the Department of Transportation and Public Facilities each hold a seat on the Council. The Department of Environmental Conservation, the Department of Fish and Game and the Department of Natural Resources has one aggregate "voice" on the council to represent natural resources interests. The IT managers of these three departments collaborate on certain functions, such as mapping.

Many methods exist to accomplish a function, the council attempts to establish a standard method.

10:31:10 AM

Mr. Brooks explained the intent to group collaborators at appropriate levels. Subject matter experts are also included to advise on e-mail, etc.

10:31:43 AM

Mr. Brooks reported this system has worked well. Projects agreed upon through this process could then be included in preparation of the budget.

10:32:06 AM

Mr. Brooks explained that the agencies submit proposed projects for review by the three aforementioned entities. Proposed projects are reviewed for technical merit, then to ensure they would meet the State's business needs. A policy decision is then made as to whether the State should undertake a project. Those proposed projects that successfully complete this review process are forwarded for possible inclusion in the governor's capital budget request. The spreadsheet contains projects that completed the review process and have been deemed to be the most critical and time sensitive. Some of the projects are necessary to meet deadlines imposed by the federal government.

Mr. Brooks told of the more than 80 standards adopted, including types of computers and software to be utilized by the agencies. Certain aspects of the information technology infrastructure should be centralized. However, other functions should be overseen within agencies because they are the experts in identifying their customers and understanding how to deliver

their services. Specialized functions would still comply with certain standards.

Mr. Brooks remarked that standardization would reduce the need for training State employees who transfer between agencies.

[10:35:20 AM](#)

Mr. Brooks furthered that working as a single enterprise the State could achieve significant savings on purchases. Under consideration, is a conversion of all systems to a single Microsoft application. Currently five different e-mail systems are utilized and although they interact without difficulty, the State could incur savings through licensing costs, training and maintenance if one system were in place.

[10:36:30 AM](#)

Senator Stedman directed attention to the Statewide Digital Mapping project on the spreadsheet. The Department of Natural Resources already has a "powerful" system. He asked if the proposed project would enhance the existing system and allow public access to digital mapping.

[10:37:19 AM](#)

Mr. Brooks deferred to Department of Natural Resources staff.

[10:37:42 AM](#)

Senator Stedman remarked on the benefits of providing access to detailed mapping information of Alaska.

[10:37:54 AM](#)

Mr. Brooks reported that efforts had been made so mapping activities of the Department of Natural Resources, the Department of Fish and Game and other agencies would be interactive.

[10:38:12 AM](#)

Co-Chair Wilken understood that the mapping project would include enhancement of aviation navigation to allow real time navigation of certain mountain passes.

[10:38:37 AM](#)

NICO BUS, Acting Director, Division of Support Services, Department of Natural Resources, testified to the intent to obtain additional elevation mapping. A Memorandum of Understanding has been signed with the Department, the Department of Military and Veterans Affairs and the University of Alaska to ensure all data would be available to the public. The investment must provide the broadest application for the public, private entities and the State.

[10:39:49 AM](#)

Senator Olson asked if the mapping activities were undertaken by the private sector.

[10:40:14 AM](#)

Mr. Bus stated this project would be funded with over \$8 million in federal funds and \$2 million in general funds and would be utilized to purchase information from the private sector.

[10:40:52 AM](#)

Senator Olson surmised that the affected industries approve of this project.

[10:41:00 AM](#)

This bill was HELD in Committee.

#SB235

[10:41:22 AM](#)

SENATE BILL NO. 235

"An Act relating to a public school performance incentive program; and providing for an effective date."

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

Co-Chair Green noted interest expressed by the Committee to discuss certain aspects of this legislation.

[10:41:58 AM](#)

Amendment #1: This amendment inserts language to Sec. 14.03.123. Public school performance incentive program., added by Section 2 of the bill on page 3, following line 3 to read as follows.

(d) Notwithstanding (a) of this section, the department may not distribute a school performance incentive payment to more than 850 certified employees annually. The limitation of this subsection does not affect the number of noncertified employees and central office personnel to whom the department distributes a school performance incentive payment under (a) and (b) of this section. The department's regulations adopted under this section shall implement the requirements of this subsection.

(e) The public school performance incentive program described in this section expires June 30, 2009. The program may be continued or reestablished by the legislature. The Legislative Budget and Audit Committee shall review the program not later than December 31, 2008, and may submit its recommendations to the respective houses of the legislature in the form of a bill that, if enacted into law, would continue or reestablish the program on or before July 1, 2009.

Senator Bunde moved for adoption.

Senator Bunde explained he supported the basic concept of the legislation. Co-Chair Wilken had made a compelling argument on the benefits of providing incentives to reward good performance of employees in private enterprises.

Senator Bunde, however, had concerns about the considerable expense of the proposed program. He therefore suggested establishing it as a pilot program, and one that school districts could choose to participate in rather than providing another State mandate. These changes would reduce the fiscal note cost from \$15 million to \$5.8 million.

[10:43:49 AM](#)

Senator Bunde detailed that the pilot program would operate through the year 2008, at which time the Legislative Budget and Audit Committee would submit a recommendation to the legislature to expand or eliminate the program. This would provide an acceptable compromise.

Senator Bunde commented that the argument could be made that the funding for this proposed program should instead be appropriated to the education foundation funding formula. However, improvements in education are necessary and this program is a method that could assist in achieving improvements.

[10:44:51 AM](#)

Senator Hoffman asked how the participating schools would be selected.

[10:45:14 AM](#)

Senator Bunde responded that the program would be available on a "first come first served" basis in which schools would be accepted in the order their applications were received.

[10:45:25 AM](#)

There was no objection and the amendment was ADOPTED.

[10:45:32 AM](#)

Senator Bunde offered a motion to report the bill, as amended, from Committee with individual recommendations and new fiscal note.

Without objection, CS SB 235(FIN) was MOVED from Committee with a new fiscal note dated 2/23/06 from the Department of Education and Early Development in the amount of \$5,800,000.

[10:46:00 AM](#)

Co-Chair Green noted the representatives from citigroup would be available to meet with Members individually to provide additional information on the proposal to reissue tobacco settlement revenue bonds.

#

**ADJOURNMENT**

Co-Chair Lyda Green adjourned the meeting at [10:46:21 AM](#)