

ALASKA STATE LEGISLATURE
SENATE STATE AFFAIRS STANDING COMMITTEE

May 3, 2005

3:44 p.m.

MEMBERS PRESENT

Senator Gene Therriault, Chair
Senator Thomas Wagoner, Vice Chair
Senator Charlie Huggins
Senator Kim Elton

MEMBERS ABSENT

Senator Bettye Davis

COMMITTEE CALENDAR

CS FOR HOUSE BILL NO. 215(FIN)

"An Act relating to the investment responsibilities of the Alaska Permanent Fund Corporation; relating to regulations proposed and adopted by the Board of Trustees of the Alaska Permanent Fund Corporation and providing procedures for the adoption of regulations by the board; and providing for an effective date."

MOVED CSHB 215(FIN) OUT OF COMMITTEE

PREVIOUS COMMITTEE ACTION

BILL: HB 215

SHORT TITLE: PERM FUND CORP. INVESTMENTS/REGULATIONS

SPONSOR(S): REPRESENTATIVE(S) ROKEBERG BY REQUEST

03/09/05	(H)	READ THE FIRST TIME - REFERRALS
03/09/05	(H)	STA, FIN
04/12/05	(H)	STA AT 8:00 AM CAPITOL 106
04/12/05	(H)	Moved Out of Committee
04/12/05	(H)	MINUTE(STA)
04/13/05	(H)	STA RPT 5DP 1NR
04/13/05	(H)	DP: GARDNER, LYNN, ELKINS, RAMRAS, SEATON;
04/13/05	(H)	NR: GATTO
04/14/05	(H)	FIN AT 1:30 PM HOUSE FINANCE 519
04/14/05	(H)	Moved CSHB 215(FIN) Out of Committee
04/14/05	(H)	MINUTE(FIN)
04/15/05	(H)	FIN RPT CS(FIN) 4DP 5NR

04/15/05 (H) DP: HAWKER, FOSTER, MEYER, CHENAULT;
04/15/05 (H) NR: CROFT, MOSES, HOLM, STOLTZE, KELLY
04/19/05 (H) BEFORE THE HOUSE
04/19/05 (H) WEYHRAUCH NOTICE OF RECONSIDERATION
WITHDRAWN
04/20/05 (H) TRANSMITTED TO (S)
04/20/05 (H) VERSION: CSHB 215(FIN)
04/21/05 (S) READ THE FIRST TIME - REFERRALS
04/21/05 (S) STA, FIN
04/26/05 (S) STA AT 3:30 PM BELTZ 211
04/26/05 (S) Heard & Held
04/26/05 (S) MINUTE(STA)

WITNESS REGISTER

Jim Baldwin
Department of Law
PO Box 110300
Juneau, AK 99811-0300

POSITION STATEMENT: Answered questions on HB 215

Mike Burns, CEO
Alaska Permanent Fund Corporation
Department of Revenue
PO Box 110400
Juneau, AK 99811-0400

POSITION STATEMENT: Answered questions related to the HB 215

ACTION NARRATIVE

CHAIR GENE THERRIault called the Senate State Affairs Standing Committee meeting to order at [3:44:52 PM](#). Present were Senators Elton, Wagoner, Huggins and Chair Therriault.

CSHB(FIN) 215-PERM FUND CORP. INVESTMENTS/REGULATIONS

CHAIR GENE THERRIault announced HB 215 to be up for consideration. He asked for an explanation of the regulatory process that would be used in setting up this new system.

JIM BALDWIN, Department of Law, explained that the new abbreviated regulatory process is very similar to the process used in the Alaska Industrial Development and Export Authority (AIDEA) and the Alaska Housing Finance Corporation (AHFC). Those processes were enacted in law when the corporations argued that they needed to be more nimble than the regular line agency to have the ability to adapt to market conditions. AIEDA needed an

abbreviated adoption process since it was in the housing and secondary mortgage market.

He noted the comparison between the AS 44.62 regulation adoption process and the proposed process in CSHB 215(FIN). The basic differences are in the amounts of time for public notice and the amount of time it takes a regulation to become effective once it's filed. Another significant difference is that there is no Department of Law review and approval by the regulations attorney. They are effective upon filing with the Lieutenant Governor's Office.

DOL is closely involved with the Permanent Fund Corporation and he suggested DOL would be involved in drafting the regulation so the Permanent Fund Corporation would not escape DOL review or involvement.

[3:48:01 PM](#)

CHAIR THERRIault asked Mr. Burns to explain the types of additional investment opportunities and to review the handout titled "Alaska Permanent Fund Corporation Reducing Risk, Increasing Return."

MICHAEL BURNS, CEO, Alaska Permanent Fund Corporation, directed members to the graph on page 4 labeled "Efficient Frontier." The horizontal line indicates risk according to annualized standard deviation, and the vertical line indicates annualized return.

The chart shows potential risk and return for various portfolios under the Fund's current investment restrictions (blue line), and under the Prudent Investor Rule alone (red line).

The chart demonstrates that under the Prudent Investor Rule, the Fund could potentially earn the same return as the current portfolio (March 2004 target) with more than 3 percent less risk (Expected Return = 8.83). Or, for the same risk the Fund could earn almost 1 percent more return (Standard Deviation = 10.29).

[3:50:39 PM](#)

As previously mentioned, all but six states have adopted the Prudent Investor Rule rather than maintaining statutory investment lists.

CHAIR THERRIAULT asked how availing yourself of riskier investment options, would lower the risk.

MR. BURNS initiated the explanation by saying that the corporation just released one small cap manager and hired nine small cap managers. Small cap investment is capacity constrained. The investment firms tend to be small and although they may do a good job of managing \$300 million, the staff and systems are probably insufficient to manage \$500 million. In addition, the math shows that in the small cap area of investment management, it's better to have more managers to come up with more ideas. Of course, that's not the case in all asset classes.

Accordingly, the corporation released the one small cap manager that was paid \$550 million per annum and hired nine managers at just over \$60 million apiece. Interestingly, of those nine managers, between one third and one half wouldn't have been hired on their own. Together the corporation liked the way they fit into the breadth approach of the small cap market place.

He went on to explain that the investment key is to try to get investments that don't correlate. The effort is to achieve balance and have assets moving in different directions because higher risk investments that are uncorrelated can give a portfolio that is less risky. Finally, he made the point that portfolios today are managed as portfolios and not as an asset class or an individual ownership.

CHAIR THERRIAULT summarized it's the blend of risks.

MR. BURNS said yes.

SENATOR CHARLIE HUGGINS asked if hedging is employed as an investment strategy.

MR. BURNS replied an absolute return strategy might be used to lock in a percentage and those are basically hedged assets. He suggested the types of assets wouldn't be dramatically different; there would be combinations of long and short strategies of hedged positions.

[3:55:09 PM](#)

SENATOR HUGGINS asked if hedging would be a greater part of the strategy than it is currently.

MR. BURNS said it would depend on how the market reacts to the different conditions. What's most important about the statutory list is its lack of responsiveness to changing market conditions.

[3:56:01 PM](#)

SENATOR HUGGINS asked if the Prudent Investor Rule requires more or less financial agility.

MR. BURNS replied the corporation uses the term "prudent investor" because it's widely known and is the standard that's used across the country. He read page 1, lines 11 through page 2, line 1 and pointed out it refers to an institutional investor rather than a prudent investor.

[3:57:32 PM](#)

SENATOR KIM ELTON questioned whether the prudent investor rule works differently for real estate investments than for equity investments.

MR. BURNS replied the equity investment process is different than the real estate investment process, which tends to be more yield-driven.

SENATOR ELTON asked if the provisions in HB 215 would apply equally to the real estate investment portfolio and to the equities portfolio.

MR. BURNS said yes.

CHAIR THERRIault noted the bill had a zero fiscal note. He asked Mr. Burns to be aware that some Senate members have questions on the bill and they would look to Senator Stedman and Senator Seekins for a final opinion before it moves to the floor.

[4:01:26 PM](#)

SENATOR WAGONER motioned to report CSHB 215(FIN) and attached fiscal notes from committee with individual recommendations. There being no objection, it was so ordered.

There being no further business to come before the committee, Chair Therriault adjourned the meeting at [4:01:43 PM](#).