

**ALASKA STATE LEGISLATURE
LEGISLATIVE BUDGET AND AUDIT COMMITTEE**

September 28, 2009

1:34 p.m.

MEMBERS PRESENT

Senator Kevin Meyer, Chair
Representative Nancy Dahlstrom, Vice Chair
Senator Lyman Hoffman
Senator Charlie Huggins (via teleconference)
Senator Linda Menard
Senator Bert Stedman
Representative Mike Hawker
Representative Mark Neuman
Representative Mike Doogan
Senator Donald Olson (Alternate)
Representative Bill Stoltze (Alternate) (via teleconference)
Representative Chris Tuck (Alternate) (via teleconference)

MEMBERS ABSENT

Representative Bill Thomas

COMMITTEE CALENDAR

APPROVAL OF MINUTES
REVISED PROGRAM - LEGISLATIVE (RPLs)
EXECUTIVE SESSION
AUDIT REQUESTS
OTHER COMMITTEE BUSINESS
PRESENTATIONS

PREVIOUS COMMITTEE ACTION

No previous action to record

WITNESS REGISTER

DAVID TEAL, Legislative Fiscal Analyst
Legislative Finance Division
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Provided information to the Joint Committee on Legislative Budget and Audit regarding the RPLS before it.

BRIAN BUTCHER, Public Affairs Director

Alaska Housing Finance Corporation (AHFC)
Department of Revenue
Anchorage, Alaska

POSITION STATEMENT: Answered questions on RPL 04-0-1021, AHFC State Energy Efficient Appliance Rebate Program.

DAN FAUSKE, CEO
Alaska Housing Finance Corporation (AHFC)
Department of Revenue
Anchorage, Alaska

POSITION STATEMENT: Answered questions on RPL 04-0-1021, AHFC State Energy Efficient Appliance Rebate Program.

JOHN ANDERSON, Program Officer
Weatherization
Alaska Housing Finance Corporation (AHFC)
Department of Revenue
Anchorage, Alaska

POSITION STATEMENT: Answered questions regarding RPL 04-0-1021, AHFC Energy Efficient Appliance Rebate Program.

ALISON ELGEE, Assistant Commissioner
Office of the Commissioner
Department of Health and Social Services (DHSS)
Juneau, Alaska

POSITION STATEMENT: Answered questions regarding RPL 06-0-0133, H1N1 disaster preparedness funds.

BOB PICKETT, Commissioner/Chair
Regulatory Commission of Alaska
Department of Commerce, Community, & Economic Development
(DCCED)
Anchorage, Alaska

POSITION STATEMENT: Discussed RPL 08-0-0067.

JAMES KING, Director
Division of Parks and Outdoor Recreation
Department of Natural Resources (DNR)
Anchorage, Alaska

POSITION STATEMENT: Answered questions regarding RPL 10-0-5006 related to the Alaska Trails Initiative Program.

PAT DAVIDSON
Legislative Auditor
Division of Legislative Audit
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Provided information on the audit requests.

DAN DICKINSON, Certified Public Accountant (CPA), Consultant
Legislative Budget and Audit Committee
Anchorage, Alaska

POSITION STATEMENT: Provided an interim report of a fiscal model.

DAVID WOOD, Consultant
Legislative Budget and Audit Committee
United Kingdom

POSITION STATEMENT: Reviewed the fiscal model being presented to the committee.

STEVE FRANK, Chair
Board of Trustees
Alaska Permanent Fund Corporation (APFC)
Juneau, Alaska

POSITION STATEMENT: Offered comments and answered questions during the presentation by the Alaska Permanent Fund Corporation.

MICHAEL BURNS, Executive Director
Alaska Permanent Fund Corporation (APFC)
Juneau, Alaska

POSITION STATEMENT: Answered questions regarding the Alaska permanent fund.

JEFF SCOTT, Chief Investment Officer
Alaska Permanent Fund Corporation (APFC)
Juneau, Alaska

POSITION STATEMENT: Answered questions regarding the Alaska permanent fund.

MICHAEL O'LEARY, JR., Executive Vice President/Manager
Fund Sponsor Consulting
Callan Associates
Denver, Colorado

POSITION STATEMENT: Provided information and comments on the new allocation framework.

ACTION NARRATIVE

[1:34:47 PM](#)

CHAIR KEVIN MEYER called the Legislative Budget and Audit Committee meeting to order at 1:34 p.m. Senators Stedman, Hoffman, Menard, Olson (Alternate), and Meyer and Representatives Hawker, Neuman, Doogan, Stoltze (Alternate) (via teleconference), and Dahlstrom were present at the call to order. Senator Huggins (via teleconference) and Representative Tuck (Alternate) (via teleconference) arrived as the meeting was in progress. Also in attendance was Representative Johansen.

APPROVAL OF MINUTES

[1:34:59 PM](#)

REPRESENTATIVE DAHLSTROM made a motion to approve the minutes of August 14, 2009, and September 8, 2009, meetings. There being no objection, the minutes from the aforementioned meeting dates were approved.

REVISED PROGRAM - LEGISLATIVE (RPLs)

[1:35:11 PM](#)

CHAIR MEYER announced that the next order of business would be consideration of the RPLs before the committee. He asked Mr. Teal to describe each RPL and if there were questions, the RPL would be set aside for further discussion.

[1:36:37 PM](#)

DAVID TEAL, Legislative Fiscal Analyst, Legislative Finance Division, Alaska State Legislature, began with the Alaska Housing Finance Corporation (AHFC) RPL 04-0-1021 for \$658,000 of federal stimulus funding for the energy efficient appliance rebate program, a capital project. At this time there are no details as to how the program will work. Mr. Teal said that he didn't see any technical problems with the RPL.

CHAIR MEYER objected.

[1:37:42 PM](#)

MR. TEAL then moved on to RPL 05-0-0124 in which the Department of Education and Early Development requested \$703,654 in federal funds. These aren't stimulus funds. The funds are being requested to fund a roof repair and fire alarm system at Mt. Edgecumbe High School.

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REPRESENTATIVE STOLTZE, speaking on behalf of Representative Thomas, related support for RPL 05-0-0124.

There being no objection, RPL 05-0-0124 was approved.

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MR. TEAL continued with RPL 06-0-0133, which is a request for federal receipt authority in the amount of \$7,550,000 for H1N1 disaster preparedness. The RPL specifies some line item detail. Although he expressed concern that there isn't much detail as to the benefits to Alaskans or the impact to the Department of Health and Social Services' work flow or budget, there were no technical issues with the RPL.

[1:39:39 PM](#)

REPRESENTATIVE HAWKER objected, and thus RPL 06-0-0133 was held.

[1:39:52 PM](#)

MR. TEAL turned to RPL 08-0-0067, which is a request for capital funds for the Regulatory Commission of Alaska (RCA) for capitol funds, stimulus funds in the amount of \$767,493. If the committee wants to approve the RPL, he recommended that the amount be reduced to about \$96,000 and [the funding source] be changed to operating.

REPRESENTATIVE HAWKER objected, thus RPL 08-0-0067 was held.

[1:41:11 PM](#)

MR. TEAL moved on to RPL 45-0-1134 for \$5 million for the University of Alaska. This RPL will fund capital projects with stimulus funds. The original request, he noted, was for \$2.8 million but has increased to \$5 million plus. Since there are more grants to come some, the committee probably needs to address how to deal with the continuing flow of these grants, particularly once session starts.

[1:42:30 PM](#)

MR. TEAL, in response to Representative Hawker, confirmed that since the September 18th list of university grants, three more

grants have been received and aren't included in the \$5 million plus of receipt authority being requested.

[1:43:28 PM](#)

REPRESENTATIVE DOOGAN surmised then that the motion is to accept the \$5.4 million in receipt authority for the University of Alaska.

MR. TEAL replied yes.

[1:43:43 PM](#)

There being no objection, RPL 45-0-1134 was approved.

[1:43:58 PM](#)

MR. TEAL turned the committee's attention to [RPL 10-0-5006, a Department of Natural Resources (DNR) request for \$2,087,200 of federal funds for] the Alaska Trails Initiative Program, for which the committee requested a list of projects and impacts on the areas. He noted he had no technical issues with the RPL.

[1:44:27 PM](#)

REPRESENTATIVE NEUMAN related that he had questions about how the monies and the trails were selected as well as the public process. He said that although he had a fairly good discussion with the director of the Division of Parks and Outdoor Recreation, he opined that maintenance on some existing trails was left out. He identified the existing trails as the Rex Trail and Chitna Access. He asked if there are more opportunities for other trails to obtain funds. He also asked if there is the opportunity for public participation, particularly in regard to the purchase of equipment and supplies. He mentioned the notion of having volunteer organizations participate, and questioned whether such organizations had the opportunity to apply for these funds. Representative Neuman related his understanding that there is a limited timeframe with regard to these funds, and therefore original applicants were the only people contacted about applying.

[1:46:01 PM](#)

CHAIR MEYER surmised then that there was an objection to RPL 10-0-5006, and thus it was held for further discussion. He then

related his understanding that the following RPLs were held: RPL 04-0-1021 regarding the AHFC State Energy Efficient Appliance Rebate Program, RPL 08-0-0067 for the RCA, RPL 06-0-0133 for H1N1 disaster preparedness, and RPL 10-0-5006 for the Alaska Trails Initiative. He suggested that the committee return its attention to RPL 04-0-1021.

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CHAIR MEYER inquired as to when AHFC anticipates the program will be available.

[1:47:54 PM](#)

BRIAN BUTCHER, Public Affairs Director, Alaska Housing Finance Corporation (AHFC), Department of Revenue, answered that AHFC anticipates that the program will be running in December. He related that AHFC has a deadline of October 15th to submit a draft [of the program] to the U.S. Department of Energy, which then must be approved. As with all federal funds, there are some steps that will occur prior to the administration of the program.

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SENATOR HOFFMAN asked if there will be allocations. He pointed out that often rural areas don't get up to speed on programs such as this and often funds are exhausted prior to their involvement. He also inquired as to how the program will be administered. For those in rural Alaska, obtaining an energy efficient appliance can cost two to three times the cost elsewhere in the state due to transportation costs to the rural location. He opined that it would be fair for transportation costs in rural areas to be part of the program.

DAN FAUSKE, CEO, Alaska Housing Finance Corporation (AHFC), Department of Revenue, said that AHFC is trying to determine the best way to administer the program. He then pointed out that it's a small amount of funds in terms of spreading it from Barrow to Ketchikan. Mr. Fauske told the committee that AHFC is prepared to donate the administrative time to this program versus trying to add staff to allocate funds. He indicated the need to keep in mind allocating the funds without the program being cumbersome to operate. He acknowledged the rural versus urban situation. In terms of developing a program, this RPL just isn't a lot of money to spread throughout the state, he opined.

[1:51:16 PM](#)

SENATOR HOFFMAN related his expectation that this will be a popular program. He asked if AHFC is considering supplementing this request with state funds as well.

MR. FAUSKE replied, no, not at this point. There has been discussion about including it in the existing weatherization program, for which there would have to be guidelines to equally distribute the funds throughout the state.

SENATOR HOFFMAN offered that he has some ideas.

[1:52:07 PM](#)

MR. BUTCHER, in response to Representative Neuman, said that he wasn't aware of any time period in which people would have to purchase these energy efficient appliances. In terms of time, the only requirement is that the funds have to be expended in three years. Although the requirements of the rebate allow AHFC to take up to 10 percent of the funds for administrative costs, AHFC doesn't want to do that. The hope is to give 100 percent of the funds in rebates, and thus AHFC is trying to keep the administration of the program as simple as possible. In further response, Mr. Butcher said that it's difficult to specify a date when folks can begin to apply because he doesn't know how long it will take the federal government to respond to Alaska's application.

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MR. FAUSKE related that AHFC has considered ways in which to achieve the best bang for the buck, especially since other federal funds are being distributed and the amount of this fund is fairly small. At one point, there was discussion of distributing the funds to specific groups, such as disabled Alaskans or returning veterans, in an effort to avoid a huge expectation with a limited resource. He noted that the rural situation will be considered.

MR. BUTCHER interjected that AHFC hasn't met with the governor's office yet regarding what it desires. However, once the dates and details of the program are known legislators will be notified.

[1:56:06 PM](#)

REPRESENTATIVE STOLTZE asked if the funds could be spent on large state-directed projects.

MR. BUTCHER related his understanding that the funds need to be distributed as a rebate.

REPRESENTATIVE STOLTZE opined that this rebate program seems difficult in terms of distributing it to the citizenry. Therefore, he indicated that perhaps the funds could be used to address needs such as boiler replacements at schools or senior centers. Furthermore, a criteria specifying a return on investment would likely result in the funds going to rural Alaska.

MR. BUTCHER said that AHFC reviewed such a distribution method initially, but the federal legislation specified that the funds had to be disbursed as rebates to individuals and fall into 10 general appliance categories.

MR. FAUSKE reviewed the suggested appliance list from which the state should choose. Mr. Fauske remarked that with the American Recovery and Reinvestment Act of 2009 (ARRA) funds, there isn't much detail, which creates some confusion while providing some leeway.

[1:59:35 PM](#)

REPRESENTATIVE STOLTZE asked then if the option of distributing the funds to projects on a needs list, as mentioned earlier, could be broached with the federal government.

JOHN ANDERSON, Program Officer, Weatherization, Alaska Housing Finance Corporation (AHFC), Department of Revenue, responded that AHFC can ask for a clarification of the definition of "consumer," but the language specifies that the funds have to be rebated to consumers.

[2:00:34 PM](#)

REPRESENTATIVE DOOGAN asked if there will be a restriction on those who can apply. For instance, can consumers who purchased appliances a year ago apply for this rebate, he asked. He predicted a fairly short and intense stampede in which the first approximately 600-700 people seeking the rebate will actually receive it.

MR. FAUSKE related his understanding that [purchase] dates will be specified once U.S. DOE approval is obtained. He related his assumption that once the program is approved, there will be a plan [to disburse funds] going forward. In further response to Representative Doogan, Mr. Fauske said that AHFC received complaints from people who just missed rebates with the original weatherization rebate program. He suggested that because the funds are limited, it makes AHFC more diligent in determining the rush that will occur. If this federal program is successful and there is desire to continue, its continuation could be considered under the existing \$360 million. Mr. Fauske related that personally he's more inclined to find a group of people or project to which to provide these funds.

[2:04:51 PM](#)

SENATOR OLSON predicted that in rural Alaska, residents are more apt to purchase refrigerators and deep freezers as rural residents would tend to have even more inefficient models than might be expected. He inquired as to the amount of money necessary from the state to supplement replacement of major energy inefficient appliances.

MR. FAUSKE answered that it would amount to a lot of money. He related that AHFC has discussed internally the requirement that the appliance must be purchased from a certified energy star supplier. The aforementioned is problematic for those areas without a certified energy star supplier. Although residents could purchase such appliances through Sears or other supplier, it would come with added costs. Mr. Fauske reiterated that if an energy efficient appliance rebate program were added to the existing weatherization program, the cost would be substantial.

[2:07:21 PM](#)

SENATOR MENARD asked if AHFC has addressed a regional lottery program, which she opined would be fair across the board.

MR. FAUSKE replied yes, adding that AHFC will try to list as many reasonable options as possible to the governor, including a regional lottery.

[2:08:24 PM](#)

SENATOR STEDMAN returned to the earlier mentioned allocation issue in which some areas don't have access to stores from which to purchase energy efficient items. He then suggested

incentivizing heat pumps, which utilize one-half to one-third less electrical energy, because they would take some of the pressure off the electrical systems.

[2:09:53 PM](#)

REPRESENTATIVE HAWKER expressed the need to recognize the diversity of needs and opinions of all Alaskans. He explained that although there has been much discussion regarding the challenges faced in rural Alaska, there is also concern with regard to the most populous areas of the state that don't qualify for those programs that specifically target rural areas.

[2:10:36 PM](#)

REPRESENTATIVE STOLTZE asked if AHFC has considered the disposal of old appliances in its program as disposal costs are expensive and sometimes cause individuals to leave their old appliances on the side of the road.

MR. FAUSKE answered that the legislation recommends a disposal or recycle phase for the appliances.

CHAIR MEYER asked if this energy efficient appliance rebate is similar to cash for clunkers.

MR. ANDERSON responded that a new energy star appliance doesn't mean just another appliance plugged into another room. The aforementioned will be the result of the scope of work in the individual's plan.

REPRESENTATIVE STOLTZE remarked that he isn't excited about more government subsidization of individuals.

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CHAIR MEYER removed his objection to RPL 04-0-1021.

[2:12:52 PM](#)

REPRESENTATIVE STOLTZE objected.

CHAIR MEYER related that his thought had been that the money would be accepted and that AHFC would come before the committee once the program is in place. At that point, the program could be modified or accepted.

2:13:42 PM

A roll call vote was taken. Representatives Hawker, Neuman, Doogan, Tuck (Alternate), and Dahlstrom and Senators Stedman, Hoffman, Huggins, Menard, Olson, and Meyer voted in favor of RPL 04-0-1021. Representative Stoltze (Alternate) voted against it. Therefore, RPL 04-0-1021 was approved by a vote of 11-1.

2:15:01 PM

CHAIR MEYER requested that AHFC present the program to the committee once it's structured.

MR. FAUSKE agreed to do so.

2:15:34 PM

CHAIR MEYER then returned the committee's attention to RPL 06-0-0133 for H1N1 disaster preparedness.

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REPRESENTATIVE HAWKER maintained his objection. He related that he had requested that the department be prepared to provide information regarding how this request fits into the existing operating budget. He asked if any program managers were present. Representative Hawker also asked how this request for a significant amount of funds fits into existing immunization programs in terms of manpower allocations and other aspects of the Division of Public Health's existing budget.

2:18:13 PM

ALISON ELGEE, Assistant Commissioner, Office of the Commissioner, Department of Health and Social Services (DHSS), specified that she is the only DHSS representative present at this time. In further response to Representative Hawker, she explained that the department anticipates using a portion of these funds to support existing staff for the vaccination program. Because the magnitude of this effort is going to be so significant, it was determined best to bring the entire grant proposal forward for review by the committee rather than trying to determine how much federal authority the department has and piece meal it. She related the department's expectation that a good portion of the funding will be used to support all efforts within the Division of Public Health that are currently being supported by federal funds.

2:19:03 PM

REPRESENTATIVE HAWKER surmised then that this request may involve a duplication of existing federal authority, but the department isn't sure where the overlap will occur.

MS. ELGEE replied yes.

REPRESENTATIVE HAWKER asked if DHSS stands behind the line item breakdown on page 2 of the RPL.

MS. ELGEE said that it's the best information available at this time. Until the distribution of the vaccine begins and there is knowledge as to how prevalent the H1N1 virus response will be in the state, no better information is available.

2:19:59 PM

REPRESENTATIVE HAWKER asked if the line item for personal service funds is for new or existing positions.

MS. ELGEE specified that the department is proposing seven short-term non-permanent positions with the remainder of the funding to help existing Division of Public Health staff that may be transferred to the H1N1 effort.

REPRESENTATIVE HAWKER surmised that the seven short-term non-permanent positions are new staff.

MS. ELGEE replied yes.

REPRESENTATIVE HAWKER related that when he last talked with the department it seemed to be addressing this issue competently with existing staff. Therefore, he questioned whether public information officers are necessary.

MS. ELGEE explained that last spring when the H1N1 virus was initially identified, the need for an individual to be stationed full-time at the Incident Command Center operated by the Department of Military & Veterans' Affairs (DMVA) was discovered. The department doesn't have sufficient staff to do so if it becomes an ongoing effort, she stated.

2:21:46 PM

REPRESENTATIVE HAWKER moved on to the contractual line item in the amount of \$4.167 million for laboratory testing, disease surveillance, and shipping and delivery of vaccines. He asked if the aforementioned amount of funds spent is contingent upon the degree of the outbreak. He recalled when the department came to him regarding the avian flu and the potential for a pandemic, which never materialized.

MS. ELGEE answered that Representative Hawker is correct that the amount of funds expended will fluctuate depending upon the incidence of the disease. She then explained that the department is using the planning effort for incidence response and command structure for pandemic that was done for the potential avian pandemic. From a preparedness standpoint, the department is in a much better position than had the avian flu planning effort not been undertaken.

[2:23:08 PM](#)

REPRESENTATIVE HAWKER inquired as to how much of the \$7.5 million request the department intends on spending in the fiscal year (FY) 2010 budget cycle.

MS. ELGEE clarified that how much is spent is dependent upon the prevalence of the disease. The Center for Disease Control and Prevention predicts that additional funding will be available in future years should this be an ongoing need. The department is trying to obtain additional information in order to determine what should be reflected in the FY 2011 budget.

[2:24:05 PM](#)

REPRESENTATIVE HAWKER inquired as to the accountability and limitations on these funds. For instance, should the entire \$7.5 million not be needed to address the H1N1 vaccination program, could the remaining funds be used for other purposes that fall under the public health function, he asked.

MS. ELGEE responded that she didn't believe any of the funds could be used for other public health functions. She related her understanding that this grant award is specifically for the purpose of the [possible H1N1 pandemic].

[2:24:58 PM](#)

REPRESENTATIVE HAWKER remarked that addressing pandemic threats is very important. He asked if because funds are available, a

threat is being created or is there a threat for which these funds are absolutely necessary.

MS. ELGEE said that she didn't think there is an answer to that yet. The state will receive the vaccine in October. The public expects that the vaccine will be made available, and thus the funding being provided is for that end.

[2:25:50 PM](#)

REPRESENTATIVE HAWKER related that he has heard that this vaccine, which has come to the market quickly, might be a carcinogen. He questioned whether the department is absolutely comfortable with the medical merits of the vaccination.

MS. ELGEE responded that she is not capable of answering that question.

[2:26:28 PM](#)

SENATOR HOFFMAN said that he was originally concerned about the amount of the funds, but the H1N1 virus has become more real since his niece's daughter has tested positive. He reminded the committee that this virus is most detrimental to the young and the elderly. Senator Hoffman said he would err on the side of caution and would support the appropriation if it saves lives. He related his strong support for the appropriation.

[2:29:45 PM](#)

REPRESENTATIVE NEUMAN said that H1N1 isn't a new issue, and therefore he asked if the department has received funds in prior legislative budgets for H1N1.

MS. ELGEE clarified that H1N1 is a new flu strain and is the first pandemic declared by the World Health Organization (WHO) in over 40 years. Therefore, this is something different than the normal annual flu. In further response to Representative Neuman, Ms. Elgee relayed that if the funds are accepted, there are no mandatory requirements.

[2:31:01 PM](#)

REPRESENTATIVE DAHLSTROM related her support of this appropriation going to DHSS for dispersing shots and education. However, she questioned whether another public information officer is necessary. If a pandemic were to occur, there is

already a chain of command regarding public announcements. Those announcements wouldn't come from DHSS, but rather would come from the emergency management [agencies]. Therefore, she expressed interest in utilizing the funds for staff that vaccinate and educate the public. Representative Dahlstrom said that with the information she has she can't support another public information officer.

MS. ELGEE reiterated that last year when the H1N1 virus became well known, the department had to station a full-time public information officer at the Incident Command Center that DMVA operates. The aforementioned is part of the public preparedness plan in which DHSS and DMVA work together, although DHSS supplies staff to support that effort. Since there isn't sufficient staff to utilize an existing public information officer on a full-time basis, it's necessary to hire a public information officer.

REPRESENTATIVE DAHLSTROM expressed her surprise with the answer because the incident command rooms are set up with space and computers for only so many individuals. She stated that she has serious concern about the public information officer position.

[2:33:49 PM](#)

SENATOR OLSON inquired as to the views of the new department's chief medical officer regarding the \$7.5 million request.

MS. ELGEE answered that she hasn't had a conversation with him regarding this RPL, and therefore can't respond.

SENATOR OLSON said he is in favor of this RPL.

[2:34:53 PM](#)

REPRESENTATIVE STOLTZE said that although he will support this RPL as well, he is concerned with the department's response to Representative Hawker's questions.

[2:35:59 PM](#)

REPRESENTATIVE DAHLSTROM asked if Ms. Elgee can assure the committee that DHSS won't come to the legislature to request funding for this public information officer position to become a full-time permanent position.

MS. ELGEE answered that the department views the position as a temporary need, and thus at this time doesn't intend to request converting this public information officer position to an ongoing full-time position.

[2:36:49 PM](#)

REPRESENTATIVE HAWKER withdrew his objection, but stated that he would've felt more comfortable if Division of Public Health staff had been present to answer his questions.

[2:37:17 PM](#)

There being no objection, RPL 06-0-0133 was approved.

[2:37:27 PM](#)

CHAIR MEYER moved on to RPL 08-0-0067, in the amount of \$767,493 to the RCA. He recalled that Representative Hawker had objected to this RPL.

[2:38:05 PM](#)

BOB PICKETT, Commissioner/Chair, Regulatory Commission of Alaska, Department of Commerce, Community, & Economic Development (DCCED), stated that he is present to request approval of ARRA stimulus funding in the amount of \$767,493. He explained that over the past couple of years, the RCA has been inundated with a variety of federal initiatives that have opened up rather expensive proceedings that have consumed a lot of staff time that has been diverted from other areas. When this possible funding source became available, the RCA was asked to make assurance and certification to the U.S. Department of Energy regarding stimulus funding and energy initiatives. The RCA did so and indicated to the U.S. Department of Energy that the RCA would take appropriate action in rate-case proceedings and other proceedings to address some of the fundamentals of these certifications. This staffing [funded by this RPL] will help the RCA better do the aforementioned. Mr. Pickett pointed out that the RCA receives no general funds and has a number of state unfunded programs, such as power cost equalization (PCE). He further pointed out that the RCA faces great challenges; staff has been stretched and there has been much turnover. Therefore, the RCA views this RPL as an opportunity to fill in some of the voids.

[2:40:23 PM](#)

REPRESENTATIVE HAWKER acknowledged the situation of RCA, particularly the burdens the state has placed on the organization. However, he expressed concern that the RCA has been utilizing what had been built up as operating reserves. Recalling that the RCA's deficit has been about \$800,000-almost \$1 million per annum, he inquired as to how long before the RCA's reserves are depleted.

MR. PICKETT clarified that the RCA has had approved budgets in the amount of about \$8 million per year, but due to the inability to fill positions and turnover the RCA in FY 09 will have expended less than \$7 million. He specified that in the 18 months he has been with the RCA, there has been turnover in approximately 30 positions out of 57, with some positions having vacancies more than once.

[2:42:18 PM](#)

REPRESENTATIVE HAWKER indicated his dismay with "the old state trick" of balancing the budget by using the vacancy factor. If the RCA can attribute almost \$1 million dollars of the budget to unfilled positions and turnover, he questioned who would fill the two positions being targeted and keep them on staff for four years.

MR. PICKETT noted that there is a classification study underway that will impact one of those positions. As of the last five to six months, the RCA has been able to fill some of its positions, which he attributed partly to the current economy. Mr. Pickett emphasized that the RCA can't control the rate cases that come before it or the timing of various special contracts, both of which are very time-consuming and highly technical. The need for these people is present, and therefore the RCA will do what it can to fill the positions, he said.

[2:43:17 PM](#)

REPRESENTATIVE HAWKER remarked that he would like to continue this dialogue next legislative session when the budget is crafted.

[2:43:31 PM](#)

REPRESENTATIVE DOOGAN inquired as to why funds for personnel are included in the capital budget.

MR. PICKETT explained that these are grant funds and he was drawing from his experience working with AHFC when grant funds were always placed in the capital budget. Part of the reasoning with placing the funds in the capital budget is that there is less administrative overhead. By placing the grant funds in the operating budget, the agency will have to return to the legislature a number of times. He acknowledged that a large portion of the funds are for personnel, which he specified are temporary non-permanent positions tied to the period of the grant - four years in this case.

[2:44:39 PM](#)

REPRESENTATIVE HAWKER noted that the legislature has gone through a reclassification of items in the capital budget such that items in the capital budget have been returned to the operating budget. He opined that the funds being requested under RPL 08-0-0067 are truly for operating activities that are continuing multi-year operations. He then questioned whether the committee should approve enough funds for the FY 10 increment and have the other two years be brought forward in a broader discussion regarding the operating requirements in the coming years.

MR. PICKETT said the RCA will do what it can to work with committee, although what Representative Hawker suggests poses more of an administrative challenge.

[2:46:02 PM](#)

REPRESENTATIVE HAWKER moved to redesignate the funding source for RPL 08-0-0067 from capital to operating.

There being no objection, it was so ordered.

[2:46:35 PM](#)

REPRESENTATIVE HAWKER inquired as to the Senate Finance Committee co-chairs' thoughts regarding his suggestion to approve the FY 10 increment and placing the remainder of the funds on the table during the legislature's budget process.

SENATOR STEDMAN said the aforementioned sounds reasonable.

SENATOR HOFFMAN related his understanding that if the committee approves the receipt of the stimulus energy funds, the administration can expend the funds anyway.

[2:47:41 PM](#)

MR. TEAL explained that if the committee approves a certain amount for FY 10, then the RCA will simply have to come before the legislature in 2011 and place the remaining request in the 2011 or 2012 operating budget. However, the purpose of the request is to offset the cost of the operating workload associated with the stimulus project. Mr. Teal related that he, too, is concerned because the approved budget is larger than the expenditures, which are at the statutory cap. Therefore, this may come before the budget committees anyway. Furthermore, the RCA's testimony indicates that because of vacancies in other areas, the RCA has low expenditures while the revenue generation has been larger than expected expenditures. The funds from the RPL are simply supplemental operating money that can be used as ARRA funds, but it isn't limited to that. Mr. Teal opined that at this point, he isn't sure of the need for the 2010 RPL.

[2:49:29 PM](#)

MR. PICKETT, referring to the carry forward/reserves, explained that technically these are regulatory cost charges (RCC) charged only to regulated entities. In the event the RCA is overcollecting, the RCA may need to revisit the situation in the fall, revisit the RCCs, and perhaps lower them until positions are filled. Mr. Pickett said that the RCA is trying to comply with the intent of the statute. He mentioned that there is some flexibility that's based on how the legislature interprets it. Mr. Pickett highlighted the difficulty in hiring an engineer or financial analyst for a four-year timeframe, but not being able to give them specific assurance that the position will be reauthorized. The desire is to provide a bit more assurance to the potential employee, he remarked.

[2:50:58 PM](#)

REPRESENTATIVE HAWKER noted that this federal receipt authority is only a portion of the compensation per the RPL. Some \$90,000 would still be taken out of the RCA's RCCs. He recommended that the monies be available January 1, 2010, through December 31, 2013.

REPRESENTATIVE HAWKER moved that RPL 08-0-0067 be reduced to an amount that's the ratable portion effective for the FY 10 budget.

SENATOR HOFFMAN estimated that to amount to \$96,000.

[2:52:09 PM](#)

There being no objection, it was so ordered.

[2:52:36 PM](#)

MR. PICKETT asked if this approval allows the RCA to enter into a grant agreement with the U.S. Department of Energy for the full amount.

REPRESENTATIVE HAWKER pointed out that the committee is authorizing receipt authority. At this point, the committee is only offering the first incremental expenditure. He didn't view the aforementioned as prohibiting the RCA from entering into an agreement.

[2:53:38 PM](#)

MR. PICKETT related his understanding that at this time the RCA has zero receipt authority to accept federal funds.

[2:53:52 PM](#)

MR. TEAL stated his agreement with Representative Hawker that anything the RCA does for 2010 is spending authority for 2010. The RCA can still sign the grant agreement with the federal government; it's a continuing operating grant from that time forward. Whether it's capital versus operating is irrelevant to the federal government.

[2:54:24 PM](#)

SENATOR HOFFMAN related his understanding that if the committee approves the RPL, the RCA can extend the anticipated expenditure of \$96,000 between January 1, 2010, and June 30, 2010. However, the RCA will have to come to the legislature for the approval of the remainder of the funds during the legislature's budgetary process.

REPRESENTATIVE HAWKER noted his agreement.

[2:55:00 PM](#)

CHAIR MEYER returned the committee's attention to [RPL 10-0-5006, a Department of Natural Resources (DNR) request for

\$2,087,200 of federal funds for] the Alaska Trails Initiative Program.

2:56:25 PM

REPRESENTATIVE NEUMAN asked if the funds specified for the trails listed on the document entitled "Alaska Trails Initiative Project Selections - 2009/10" are locked in or is there the possibility of funding other trails.

JAMES KING, Director, Division of Parks and Outdoor Recreation, Department of Natural Resources (DNR), explained that when the division was first notified of this funding, it reviewed the timeline. The division determined it would take two years to get funds on the ground due to the time it takes to do the following: advertise for a new set of grant applications, receive and review applications, obtain approval from the Federal Highway Administration (FHWA) - a process that has slowed considerably due to stimulus package projects, and notify applicants. Furthermore, groups weren't particularly interested in applying for funds that wouldn't be available for two years. Therefore, the division reviewed other options such as reviewing existing projects that had been funded twice before. Of those almost 40 projects, the division asked if they were complete. The list before the committee specifies the projects that aren't complete. Mr. King related that the division determined it to be the best approach to complete these projects as they are shovel ready in that the projects have already went through the permitting, environmental, and public processes. This list is the division's initial take with information from the projects. If the list is approved, the division will seek further detail and have the Outdoor Recreation Trail Advisory Board (ORTAB) review the proposals for approval. In response to Representative Neuman, Mr. King acknowledged that there is the opportunity to open the funds up to other projects, but reiterated that the lengthiness of the timeline makes it unreasonable. Moreover, there is also another grant program, the Recreation Trails Program that has an application deadline of November 1st. If the aforementioned program proceeds as in the past, the division has been able to fund the reasonable projects that apply. "So, we did not feel that there was a big demand to open this back up again; that it was more important to finish what we had already started," he opined.

3:00:25 PM

REPRESENTATIVE NEUMAN opined that there are a lot of projects, other than those that have already received funding, supported by groups who could provide matching funds, free labor, and already have supplies for the trails. Two such trails are the Rex Trail and access to Chitna River, which is a subsistence fishery. These are trails which are problematic and which he believes the state has known about for some time. Representative Neuman further opined that other groups should be given an opportunity to apply no matter if the funds are received two years from now. There are worthwhile projects that, if allowed to apply for these funds, could address subsistence and RS 2477 access. He asked if all the funds have to be spent on these projects now and suggested that perhaps half of the funds could be spent on the projects listed and the other half made available to other organizations.

MR. KING acknowledged that there are many deserving trails. He explained that the Alaska Trails Initiative Project was established to empower nonprofits, cities, municipalities, and user groups to fix the trails they use. The challenge is that no group has ever applied for the Rex Trail or access to the Chitna River. The aforementioned is a challenge because it takes a lot of energy and skill to write the grants, administer the grants, find qualified people to design the trail and perform the work. The division works closely with Alaska Trails, a nonprofit umbrella organization that works with groups interested in working on trails by helping them through the process described above. At this point, the division feels it is keeping up with that demand through the Recreation Trails Program. Mr. King clarified that it's a situation in which the infrastructure of groups aren't in place.

[3:04:31 PM](#)

REPRESENTATIVE NEUMAN pointed out that the Recreational Trails Program fund is just under \$2 million and it has historically been whittled down to \$400,000. He reiterated that there are many organized groups, such as the Friends of Palmer Hay Flats, that would like to have the opportunity to access these funds. He said he would like for that to occur.

[3:05:09 PM](#)

REPRESENTATIVE STOLTZE said that he has heard large demand to open the aforementioned trails and hears a lot different priority than that related by Mr. King. Representative Stoltze related his understanding that the state has lost more trail

access over the last three years, which is appalling. He then inquired as to the percentage of trails on the proposed list that are used by multiple users.

MR. KING answered that there are three projects on the proposed list that relate to motorized use. He emphasized that these funds aren't the state reaching out and addressing the trails that are most needed in the state. This is a grant program by which organizations apply for the funds. Mr. King agreed that there is more need and demand than the division can meet. He reiterated that the division isn't receiving applications for the projects mentioned today, which the division realizes is a challenge. Therefore, the division is working to reach out to those groups, to empower them so that they can participate in this grant process.

3:07:13 PM

REPRESENTATIVE STOLTZE pointed out that the proposed project list includes U.S. Forest Service projects. He said that he knows the director of the Division of Land and Water Management and others have heard concerns regarding the earlier mentioned trails. Therefore, he related shock that divisions within DNR aren't talking to each other in an attempt to obtain resources toward these trails with intense needs. Representative Stoltze remarked that he understands the division's philosophies, which are clearly reflected in the proposed project list. He then informed everyone that he intends to vote against this RPL because he wants the division to work harder and talk within DNR. "I see some really serious problems in this approach and I think just even within the Department of Natural Resources if you guys were talking to each other and addressing some of the most pressing access needs, I think ... there might be a few other projects on there," he said. Although there are many good projects on the list, only a minor portion of the projects have multiple uses, which he characterized as troubling. Furthermore, he attributed the lack of a big demand to open this up to other projects to a lack of outreach, even within the department.

3:09:31 PM

SENATOR STEDMAN related his belief that the process the department followed was reasonable, particularly in terms of focusing on projects that are underway and presenting the list to the committee and ORTAB. Although there are clearly other

trail needs, Senator Stedman opined that it would be beneficial to move this RPL forward so that it can move to the next phase.

3:11:03 PM

REPRESENTATIVE HAWKER turned attention to the Iditarod Easement Adjudication in the amount of \$360,000. He asked if this trail involves any takings of any kind. He also asked where the adjudication will occur.

MR. KING highlighted that the challenge with the Iditarod is that there is no knowledge as to the actual location of the trail; it's merely a line on a map. The map used to designate the beginning of the trail in Anchorage, but as development has occurred and easements weren't acquired the beginning of the trail has moved to Willow. The funds for this trail aren't going to be used to take land from anyone but rather to define the line between Willow and Nome and obtain a legal easement so that corridor remains open and is preserved. Mr. King reiterated that the Iditarod Easement Adjudication doesn't involve the taking of any private land. In further response to Representative Hawker, Mr. King confirmed that this project is specific to the Iditarod Trail from Willow to Nome.

3:13:14 PM

MR. KING, in response to Representative Stoltze, said that the division has tried to be fair in this process, which is a public process that was advertised and sought public participation. Furthermore, the other divisions within DNR know about this program. The other divisions don't have staff to administer a grant, put together trail specifications, obtain permits, and build trails. Mr. King said that the division would be happy to do the aforementioned if it had the money to do so. The priority of the division is to represent all Alaskans, he emphasized. To that end, he encouraged Representative Stoltze to work with him.

3:14:45 PM

SENATOR HUGGINS referred to the notion of unity of effort. He then suggested that perhaps this granting process overseen by ORTAB needs to be reviewed. Senator Huggins pointed out that trails such as Rex Trail aren't under Mr. King's purview, although it's under the purview of DNR. Senator Huggins then opined that he doesn't believe the process with trails is open enough to address all Alaskans. He then inquired as to when

reaching out to all Alaskans with a process with which everyone can identify will occur.

MR. KING related that although the process may need review, the process has been reviewed quite often. The challenge with grant programs, he reiterated, is that it requires a lot of energy. Someone has to complete the application, review it, proceed through the public process, proceed through an environmental review process, obtain permits, find someone to design the trail, and individuals to perform the work. The reality, however, is that many people don't have the expertise or energy to do the aforementioned, which is why it's often said that the division isn't representing all Alaskans. The division tries to reach people and work with groups, such as Alaska Trails, who can help communities or user groups that don't have the aforementioned abilities or expertise. In the past, when there was less of a process, more people expressed interest in obtaining funds for a trail or project. However, two to three years later the funds would be returned because they didn't have the ability to move through the process. Therefore, the grant process was established to allow people to move through the process and complete projects. Mr. King offered that he is open to any thoughts or suggestions regarding ways in which to change the grant process or have the division keep the funds and do the work.

[3:18:49 PM](#)

SENATOR HUGGINS suggested that as a starting point, DNR would have a top 10 list of the trails that have to be fixed. If the grant process doesn't work for projects in the top 10 list, there should be a default that causes those projects to be addressed. He encouraged pursuit of the aforementioned because trails and access are a high priority for Alaskans that needs to be addressed. In conclusion, Senator Huggins said that he stands ready to work with Mr. King.

[3:20:28 PM](#)

REPRESENTATIVE NEUMAN maintained his objection.

[3:20:40 PM](#)

REPRESENTATIVE DOOGAN inquired as to the funding source of this RPL and inquired as to what happens if these funds aren't approved.

MR. KING explained that this program was started in 2005 by U.S. Senator Stevens with approximately \$4 million placed in the Alaska Trails Initiative with a list of 12 specific trails that could apply for the funding. The second round of funding in 2007 was about \$2 million and at that point, the funds were opened up to everyone. This third installment, he surmised, will likely be the last of the Alaska Trails Initiative. Mr. King pointed out that one of the reasons the division is trying to commit these funds now is because currently the federal government is performing rescissions. The fear is that the funds will be taken away, particularly since they're not part of a specific program. Furthermore, pass through funds are attached to this initiative for Sitka Trail Works.

[3:22:48 PM](#)

SENATOR HOFFMAN commented that those who applied for these grants did so in good faith, and thus it would be a breach of the committee's responsibilities if these funds weren't approved. Therefore, Senator Hoffman said that he would vote in support of the RPL.

[3:23:18 PM](#)

REPRESENTATIVE STOLTZE announced that he will vote in opposition to the approval of this RPL because he views it as a breach of the expectations of his constituents if this RPL goes "quietly."

[3:23:37 PM](#)

REPRESENTATIVE NEUMAN restated that he maintains his objection, which he attributed to the lack of public process. He emphasized that 40 organizations had already applied for and received funds and those were the only organizations who knew about these funds. He opined that the aforementioned isn't appropriate as it's not a fair public process.

[3:24:38 PM](#)

A roll call vote was taken. Representatives Hawker, Doogan, Dahlstrom and Senators Stedman, Hoffman, Huggins, Menard, and Meyer voted in favor of approving [RPL 10-0-5006, a Department of Natural Resources' (DNR) request for \$2,087,200 of federal funds for] the Alaska Trails Initiative Program. Representatives Neuman and Stoltze voted against it. Therefore, [RPL 10-0-5006, a Department of Natural Resources' (DNR) request

for \$2,087,200 of federal funds for] the Alaska Trails Initiative Program was approved by a vote of 8-2.

EXECUTIVE SESSION

[3:26:30 PM](#)

REPRESENTATIVE DAHLSTROM made a motion to move to executive session for the purpose of discussing confidential audit reports under AS 24.20.301. There being no objection, the committee went into executive session at 3:26 p.m.

RELEASE OF AUDITS

[4:57:33 PM](#)

REPRESENTATIVE DAHLSTROM made a motion for the following final audits to be released to the public for response: University of Alaska, Unit Cost Analysis and Other Selected Issues, Part 3, Distance Education (45-30033C-09); Department of Public Safety, Alcoholic Beverage Control Board, Sunset Review (12-20063-09) with a one-year extension and attached letter from the committee.

[4:58:09 PM](#)

PAT DAVIDSON, Legislative Auditor, Division of Legislative Audit, Alaska State Legislature, clarified that the committee, through the aforementioned letter, is suggesting a one-year extension.

[4:58:22 PM](#)

There being no objection, the aforementioned final audits were released to the public.

[4:58:32 PM](#)

REPRESENTATIVE DAHLSTROM made a motion for the following preliminary audits to be released to the appropriate agency for response: Special Report on the Department of Administration, Alaska Data Services Reporting know as ALDR; Special Report on the Department of Corrections selected health and safety issues to be issued also to the Corrections' Officers Association with the protocol to be developed by Chair Meyer and Ms. Davidson; Special Report on Department of Transportation & Public

Facilities Anchorage International Airport Capital Projects.
There being no objection, it was so ordered.

AUDIT REQUESTS

[4:59:34 PM](#)

CHAIR MEYER noted that Representative Neuman has requested an audit of the Alaska Natural Gas Development Authority (ANGDA).

[4:59:56 PM](#)

REPRESENTATIVE NEUMAN pointed out that several organizations are working on the deliverability of energy. He expressed the desire to obtain the best information possible without duplication of efforts with the gas pipeline project.

[5:01:29 PM](#)

CHAIR MEYER inquired as to when the auditors could address this request.

MS. DAVIDSON projected that the Legislative Audit Division will likely complete the 2009 statewide audit in March. At that point, a couple of staff will be available to work on this project. As Representative Neuman indicated there are a lot of players involved and if the goal is to seek out duplication of effort, a strong understanding of ANGDA and all the involved players has to be obtained. Although Ms. Davidson opined that this isn't a simple request, she characterized it as a very informative one for the legislature.

[5:02:35 PM](#)

REPRESENTATIVE HAWKER expressed the need for the scope of work to be sufficiently comprehensive to include a presentation of all state funds appropriated to ANGDA and where those funds have been spent. Such a report already exists and has been distributed amongst legislators.

[5:03:48 PM](#)

REPRESENTATIVE DAHLSTROM made a motion to approve Representative Neuman's request for an audit of ANGDA. There being no objection, the audit request was approved.

OTHER COMMITTEE BUSINESS

5:04:12 PM

CHAIR MEYER announced that the committee would next hear a status update from individuals with whom the committee contracts.

5:04:51 PM

DAN DICKINSON, Certified Public Accountant (CPA), Consultant, Legislative Budget and Audit Committee, reminded the committee that he is working on an eight-month project, which should be completed in November or December. Today, he said he would provide an interim report regarding what has been produced thus far. As many members are aware, last year Dr. Wood did a report on fiscal design of future discoveries of 10 yet-to-be discovered fields. At that time, Dr. Wood was directed not to engage in the current issues about a gas pipeline. However, the work Mr. Dickinson and Dr. Wood have been charged with now does engage in the current issues of a gas pipeline while maintaining a multi-year focus. He then turned the committee's attention to slide 3 and discussed the five dimensions of the model. The first dimension is the upstream in which an individual field, such as Prudhoe Bay, can be reviewed. Furthermore, review of the entire North Slope or yet-to-find fields or a cross-cut can occur. The second dimension is the downstream in which there are 10 components that are mixed and matched such that one of the three major projects is created. Mr. Dickinson opined that the three ways in which gas will become important in the Alaska fiscal system is if there's a gas-to-liquids (GTL) plant, liquefied natural gas (LNG) that is supported, or a gas pipeline that goes into Canada. The third dimension is review of the various economic cases. Many of the models included spikes, which provide information regarding how progressivity produces lots of tax dollars that move from producers to the state. The fourth dimension is that this model can be analyzed in terms of various fiscal regimes. Dr. Wood had 10 fiscal mechanisms based on international studies and what is found worldwide. Those mechanisms are built-in as are the other oil and gas producing states, such as how Prudhoe Bay would be taxed if it was located in another state. The fifth dimension is sensitivities. He explained that any model includes assumptions, and the question is what happens if the assumptions are changed.

MR. DICKINSON then clarified that this fiscal model is not an economic model about jobs and it won't answer the question as to what is the best approach. Furthermore, the model won't answer

the question of how much investment will occur. The model can specify the fiscal effects of a given set of assumptions, what fiscal impacts will be, and how will that drive taxes and oil. He then pointed out that slide 4 in an Excel document with spreadsheets within it that allow one to change the high level variables, the inputs and the outputs, and view the resulting effects of any changes.

[5:11:34 PM](#)

DAVID WOOD, Consultant, Legislative Budget and Audit Committee, explained that he would review slides that illustrate how the model will work in the aforementioned five dimensions. Dr. Wood said that from the dashboard of the model quite a lot of analysis in several of the dimensions can be performed. He pointed out that the dashboard can be used to change factors such as oil price, fiscal terms, and various field cases - all of which can provide information rather quickly. He reviewed the series of inputs on the left and the outputs on the right, the built-in price scenarios, and production tax rates all of which can be changed to receive the immediate impact. The aforementioned model, he said, is interactive and provides the user with meaningful information.

[5:15:42 PM](#)

DR. WOOD emphasized that this model is a multi-year model that includes up to 50 years of analysis. The model, he reminded the committee, allows one to vary the production profile, downstream capacity, and review the impact on the fiscal take. In addition to the North Slope fields, 10 hypothetical fields are included in the model. The fields range from small to large gas fields and small to large oil fields that can be used to test certain fiscal designs. Although this is referred to as a gas model, oil and gas needs to be reviewed together. The model is doing so in that it's reviewing oil and gas from a production perspective as well as price perspective. Moreover, the fields built into the model allow one to quickly combine fields and fractions of those fields. For example, most of the gas in the North Slope is under the control of three major companies and most of the proved reserves of that gas are located in three fields. The model allows the fraction of holdings of each of the companies in each field and that can be combined to view the impacts to the holdings of one of the companies. From a fiscal perspective, it's interesting to review the corporate position.

[5:18:51 PM](#)

DR. WOOD then moved to the downstream and mid stream dimension. The model has the ability to put together 10 downstream components in order to establish a single supply chain or the components can be put together in combinations. He noted that the more complex scenarios require a bit more input into the model to establish the appropriate capacities. For each component, the model can calculate the tariff four different ways on a levelized basis and a rolled-in basis with expansion. He remarked that there's a systematic and rigorous rate calculation for tariffs for each component. The aforementioned provides debt:equity variations, different scheduling of capital expenditures, and a range of inputs to establish tariffs with different combinations. This ability will be very useful in terms of the take from the fiscal perspective.

5:20:52 PM

DR. WOOD continued with the downstream component and reviewed the case of a gas pipeline with a NGL component. He illustrated the ease with which changes could be made in the model, but noted that one must check that the capacities are appropriate. The model is designed to be dynamic in that numbers can be changed and the impact of those changes can be seen as well as view the economic and fiscal impacts on the model.

5:23:09 PM

DR. WOOD, returning to the presentation, pointed out that a number of cases can be reviewed, such as price scenarios. For example, the model can handle four cases with different price scenarios. He opined that being able to switch between scenarios allows much interaction and results very quickly. This is important because there is a lot of fluctuation in oil and gas fields. On a true energy basis, the ratio of oil price to gas price should be 6:1. Although most of the time that ratio stays below 13 or so, in recent months it has fluctuated dramatically. In fact, in August 2009 the ratio of gas price to oil price was over 20. From a fiscal perspective, this is significant because some of the fiscal elements in the Alaska fiscal design respond very differently to different ratios of price. Therefore, running the scenarios with different price ratios, the impacts can be highlighted. He then showed a slide with seven price scenarios in which it's apparent that there's a difference in all cases when the current progressivity setup is used versus when it's separated out for oil and gas. There's a large gap in the case in which there's a low gas price and a

high price. Under the current progressivity mechanism, a low gas price tends to dilute the fiscal effects of a high oil price. The aforementioned can be quantified by using this model, he pointed out. The model further allows review of the following cases: Field 11 (indisc.) for Prudhoe Bay, a pipeline, LNG, and GTL under different price scenarios. For five of those cases, the pipeline provides the highest fiscal return. However, in the case in which the oil price is high and the gas price is low, the GTL option is more attractive in terms of fiscal return. In the situation in which there's a high oil price and a high gas price sustained over many years, the LNG option rises to the top. He reminded the committee that there are many assumptions and the model can allow quick analysis of the various scenarios.

DR. WOOD informed the committee that different options are built into the model for progressivity for gas so that restructure of the fiscal elements could be analyzed in order to determine how the fiscal take might behave under various scenarios. He noted that he has drawn on his international gas contract experience in structuring the model and various fiscal mechanisms to test how the progressivity would work with the drivers seen in other countries in the world. The model also includes the fiscal mechanisms of the main oil and gas producing U.S. states, which illustrates that in most cases the Alaska fiscal take is higher than most other states. The model also allows the ability to review the impact of the gas being sold in-state versus out-of-state. He noted that the price of the transport tariff is relatively low in the Lower 48 but high in the Alaska field development. The model, he pointed out, also includes a netback sheet that calculates the netback along the supply chains that are structured. He then showed a graph that illustrates the large difference in netback between the pipeline route versus the GTL route. Again, the model is structured such that the aforementioned analysis can be performed rather quickly as well as allow price scenarios and fiscal designs. He reminded the committee that this is a multi-year model that focuses on the fiscal design and returns. Furthermore, the resulting graphs can be broken down in terms of the main contributors for fiscal take and any changes in price scenario and downstream configuration.

[5:32:01 PM](#)

DR. WOOD pointed out that there's a series of different graphics can provide a visual representation of the particular inputs. One other dimension is the sensitivity dimension which is

allowed by macros, he explained. By varying variables one at a time the impacts are very apparent on the graphs. Dr. Wood suggested that this multi-dimensional structure allows much detailed analysis. He opined that the model is flexible, interactive, and provides enough detail for future scenarios whether the view desired is high level or complex.

[5:33:38 PM](#)

MR. DICKINSON, referring to the last two slides, related that the model is created with different users in mind, such that various levels of detail can be provided. Mr. Dickinson told the committee that the project is about two-thirds complete, and he and Dr. Wood will continue to run cases, sensitivities, develop results, and illustrate some of the conclusions that can be reached. There is a three-part report that goes with the model for which the model description that includes the cases and sensitivities that is currently in draft form. He said that the desire is to come to certain conclusions and recommendations. Mr. Dickinson highlighted that as one continues to run the model, it will create situations that will be cause for pause.

[5:37:33 PM](#)

CHAIR MEYER reminded the committee that this is an update and the final product will be presented in December. He opined that the model will be very useful.

[5:37:59 PM](#)

REPRESENTATIVE NEUMAN inquired as to whether the creators of the model will provide access to it so that members can use it to understand it better.

MR. DICKINSON clarified that first he and Dr. Wood would like to finish the model. He also said he and Dr. Wood are available to review the model with members individually.

[5:38:47 PM](#)

SENATOR STEDMAN related his understanding that the completed model will be available well before Christmas in order to allow members time to digest the information and then have the consultants come before the legislature in February for formal presentations. He suggested that the consultants consider the marginal economic view because he recalled hearing concern

within the industry that under the current tax regime, the incentive to the industry doesn't differ no matter the price. Therefore, the industry feels that it isn't incentivized enough. He then expressed the need to address the impact of heavy oil. With regard to the gas tax and the British thermal unit (Btu) equivalency, he said that it's problematic to tax something on a heating unit (Btu) basis versus a monetary unit, which is what it's valued at in the market place. The aforementioned creates complications because the legislature has ignored the gas component and concentrated on oil, which has been capped at about \$60 per barrel. Clearly, that's not the existing environment and means that the legislature has some analytical work to do to create a [fiscal] structure that remains functional.

[5:43:07 PM](#)

DR. WOOD related his hope that the model could address all of those points, such that the model can relate the impact in Prudhoe Bay as well as small fields while factoring in high cost heavy oil developments.

SENATOR STEDMAN also expressed the need to address not just the new entrants but also BP, Exxon, and Conoco in regard to how to encourage them to develop the fields in Alaska. He then noted that he met with Dr. Wood in London, and thus has had a few more discussions than most members.

[5:44:48 PM](#)

REPRESENTATIVE DOOGAN asked if the model will take into account situations in which there is more oil flowing through the pipeline that isn't taxed by the state. Or, will oil production from the Outer Continental Shelf (OCS) be able to be taken out to determine any fiscal impact to the state, he asked.

DR. WOOD replied yes, the model is such that for each field case a fiscal design can be structured within limits. For example, on federal lands certain fiscal components can be eliminated. Furthermore, private royalties or fractions of royalties can be introduced to fit a particular field case.

[5:46:04 PM](#)

REPRESENTATIVE STOLTZE asked if cost of production and production use can be factored into the model, noting that a federal policy could be passed that changes the economics.

MR. DICKINSON opined that the difficulty is that many of the federal issues are stopping or hindering development. In the model those are represented by moving fields out for some years; there isn't a switch for aggressive or nonaggressive federal action. He suggested that it may be useful that the Gulf of Mexico has been modeled. The Gulf of Mexico is an extraordinary regime because a federal royalty and a federal income tax is all that's being paid. Although some of that royalty is being shared by the states, there's no direct state take. Therefore, it illustrates what can happen with federal development when "they're pushing it." Mr. Dickinson specified that it's not a switch in the model.

REPRESENTATIVE STOLTZE inquired as to utilizing a cap and trade window.

MR. DICKINSON opined that such would get into the pricing scenario being used. He indicated that perhaps one would review what costs would be increased if admissions are. He noted that some of those are numbers that are being guessed at and have been characterized as a complication, although it may help directionally. Unfortunately, many of the scenarios built into the model are based on experiences that have already happened.

PRESENTATIONS

[5:49:16 PM](#)

CHAIR MEYER announced that the next order of business would be presentations from the Alaska Permanent Fund Corporation and the Alaska Energy Authority.

[5:50:28 PM](#)

STEVE FRANK, Chair, Board of Trustees, Alaska Permanent Fund Corporation (APFC), said that he and other APFC staff are present to answer the committee's questions. He reiterated that the APFC is not really changing its asset allocation other than to add cash and Treasury Inflation Protection Securities (TIPS).

[5:51:01 PM](#)

MICHAEL BURNS, Executive Director, Alaska Permanent Fund Corporation (APFC), in response to a question from Representative Doogan at the last hearing, clarified that mineral royalties don't impact performance as they are

subtracted out. He explained that mineral royalties don't add to performance in the same manner in which the dividend doesn't detract from performance. The aforementioned is carefully tracked, he noted.

[5:51:44 PM](#)

JEFF SCOTT, Chief Investment Officer, Alaska Permanent Fund Corporation (APFC), reminded the committee of Senator Stedman's request to review the upside and downside scenarios and the difference in the new asset allocation causes versus the old asset allocation. The committee packet, he pointed out, should include a slide entitled "Scenario Analysis." He explained that the asset allocation has been changed such that 2 percent in cash has been added for the liabilities, the dividend. The asset allocation has also added 3 percent as an inflation hedge to TIPS. Scenarios have run both positive and negative stress tests as well as historical scenarios. The table on the slide illustrated that the returns look roughly the same on both the downside and the upside, which is expected given that the asset allocation hasn't been changed very much. Mr. Scott informed the committee that the APFC's risk system can run up to 100 different scenarios and stress tests and do so in a (indisc.) weighted fashion.

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REPRESENTATIVE DOOGAN recalled that the first managers of the fund were reminded that the primary purpose of the fund is to maintain the value of the fund and only secondarily to increase the value of the fund through investment. As one watches the value of the permanent fund rise and fall, it would seem to suggest that the fund is no longer trying to achieve those goals in that order. Therefore, he questioned the confidence he should have that the APFC has a management system that's primarily concerned with maintaining the value of the fund and only secondarily with trying to beat the market.

[5:55:04 PM](#)

MR. FRANK assured the committee that APFC is not trying to beat the market but rather is trying to maintain purchasing power and have a modern portfolio that's consistent with other institutional investors, pension funds, and endowments. The permanent fund is well diversified in order to avoid the risk of investing too heavily in a specific asset class, particularly since the corporation doesn't know which asset class will

perform the best in the future. The desire, he explained, is to avoid having too much risk in any one area. The permanent fund, he said, has slowly evolved over the years to a more modern portfolio that has equity elements in order to maintain purchasing power. Usually the fixed income elements within the asset allocation have been depended upon as protection against a down market. However, APFC found recently that some of the fund's fixed income acted more like equity, which is why the fund's risk is being viewed slightly different. Mr. Frank then related that he is confident that the Alaska permanent fund has a well-diversified portfolio that will allow APFC to maintain purchasing power of the fund over time while earning a good risk-adjusted return to provide for a payout. He opined that no matter the structure there are risks. This new asset allocation, he further opined, is a reasonable approach and is consistent with the trustee's approach over the long history of the permanent fund.

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MR. BURNS interjected that if there is a change it's to focus more on maintaining value for multiple generations. Today, it's clear that the fund is for multiple generations whereas originally it was more of a goal or aspiration when it was created.

[5:59:16 PM](#)

REPRESENTATIVE DOOGAN expressed concern that the asset allocation is being changed now to be sure that the cash to pay the dividend is available, which initially was never part of the decision making mix. Therefore, he related that he wants to do what he can to ensure "the tail isn't wagging the dog." Representative Doogan said that he doesn't want to see the fund go too far in satisfying some resident's aspirations for [high dividends] or to get too state of the art with investments that may be on the leading edge of a decline.

[6:01:12 PM](#)

REPRESENTATIVE HAWKER questioned why the legislature should be confident with this new asset allocation.

MR. FRANK opined that APFC's asset allocation has been fairly consistent over the last several years, save discussion of viewing the risk a bit differently. He related that the APFC is trying to learn as it moves through the process. "That's all

we're doing, is looking at it [risk] a little differently. We are not changing anything," he opined. Mr. Frank said that the reason this discussion is occurring is because the APFC failed to appreciate that it should've talked with the legislature about the asset allocation, which has only been changed in terms of becoming more conservative with cash on hand such that it didn't require selling [stocks] when the dividend is paid out. The other change is to add TIPS as an inflation (indisc.). Mr. Frank commented that he uses the term confident in order to assure legislators that APFC isn't doing anything strange or anything that would cause legislators to lose confidence in APFC's or its staff's ability to manage the fund.

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REPRESENTATIVE HAWKER clarified that this isn't a blame game, but the fund is likely the most highly valued asset of the working populous. He explained that at the last meeting he read the permanent fund statutes because he wasn't sure the APFC's new staff understood the legislature's role in this matter. Furthermore, Representative Hawker found it inconsistent for APFC to say that nothing has really changed after the financial media reports, after this asset allocation approach was already in place, that it was a leading edge approach.

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MR. SCOTT clarified that what has changed is the cash for liabilities and the purchase of TIPS to protect for inflation. The other 95 percent hasn't changed. What has changed that is profound and on the leading edge is the way in which risk is viewed. The allocation of capital to what is invested in is not leading edge. He noted that APFC has hired Callan Associates, one of the best consultants in the business. He informed the committee that during the last board meeting, Callan Associates performed an 83-year history of the fund's asset allocation to provide some level of confidence with the fund's objectives.

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REPRESENTATIVE HAWKER surmised then that the change in the allocation of the capital was not leading edge, although there were changes with the addition of TIPS and farming out of \$2 billion to other benchmark investors.

MR. SCOTT clarified that the aforementioned program hasn't been implemented yet, but APFC is looking to hire external managers

to perform the same thing APFC does in multi-asset classes, not new asset classes or private securities but rather in fixed income, equities, TIPS, and cash. The APFC will review these external managers in an attempt to learn from them while extending staff's ability to answer some tough questions of the APFC board.

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REPRESENTATIVE HAWKER inquired as to how the new regime will be benchmarked against the status quo/historic situation to provide some comfort with the alternative approaches.

MR. SCOTT answered that performance will be shown relative to the fund's return objective, which is a 5 percent real return. There will also be review of a traditional peer representation such that the fund's portfolio will be compared to the average pension, which is about 60 percent equity, 30 percent fixed income, and 10 percent real estate. If the APFC board requests such, it can be shown what the fund would be if the 3 percent in TIPS and 2 percent in cash weren't owned.

[6:10:20 PM](#)

REPRESENTATIVE HAWKER asked if prior to the new regime that is a change in the aggregate.

MR. SCOTT replied no.

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REPRESENTATIVE HAWKER related his understanding that the desire is to more aggressively manage risk while lowering the risk assumed by the state and maintaining the same return.

MR. SCOTT replied, "That would be a goal." He specified that the objective is to clearly delineate why every asset in the fund's portfolio is owned.

MR. BURNS, in regard to why the committee should be confident, explained that a number of years ago the APFC went through an exercise to [become aware of the environment] of a different size fund. The exercise determined that any size change is well out in the future and that the existing size of the fund can attract the best talent in the world. Mr. Burns characterized [APFC] as a preferred customer and "the best people" want to be

the fund's vendors. The challenge is to pick the appropriate one, he said.

REPRESENTATIVE HAWKER questioned whether Enron was also in a market position to hire the best.

MR. SCOTT said that he didn't know.

[6:12:50 PM](#)

REPRESENTATIVE NEUMAN related his understanding that there has been much testimony from APFC staff regarding trying to reduce risk.

MR. BURNS acknowledged that the first step is to understand the risk, which is why Mr. Scott expressed the need to know exactly why certain assets are owned and categorize those together.

REPRESENTATIVE NEUMAN recalled that several years ago, legislation was passed that allowed the APFC Board to invest in riskier investments. He noted that Mr. Burns was a major part of the discussion, and therefore he asked if the fund was [hurt] by some of those [riskier] investments.

MR. BURNS said that he didn't have the numbers in front of him. However, he related his confidence that the majority of the losses were from assets prior to the change in law that Representative Neuman mentioned. He recalled that of the 218 years that have been tracked, calendar year 2008 was one of the five worst years for the U.S. Stock Market. In 2008, the fund held roughly 60-some percent in stocks. He acknowledged that the new asset classes didn't do very well, although they didn't perform as poorly as some of the old asset classes.

REPRESENTATIVE NEUMAN requested information on the impact to the fund's portfolio after the [2008] legislation was passed.

MR. FRANK opined that one has to take risk to obtain a good return. Furthermore, no matter the asset allocation used, risk will be taken. "It's not that we're all of a sudden afraid of risk, ... it's a little different perspective, a little more knowledge," he remarked. Mr. Frank further opined that it's unfortunate that the situation has been mischaracterized by the press.

[6:17:40 PM](#)

REPRESENTATIVE DOOGAN directed attention to slides [15 and 16 entitled "How does this change look? Historical Framework" and "How does this change look? New Framework," respectively]. He related his understanding that under the historical framework "we've moved around about 18 percent of the value of the fund" between the historical allocation and the new allocation. Whereas under the new framework, that difference between the old allocation and the new allocation is 44 percent. He characterized either of the aforementioned changes as a substantial change in the asset allocation for the fund. He inquired as to what he's missing.

MR. SCOTT related his belief that Representative Doogan is referring to slide 16. He pointed out that the graph has a category entitled "Opportunities," which specifies that the historical allocation was 6 percent and the new allocation is 21 percent. The aforementioned reflects a large change that hasn't yet happened; such a change would only happen through the APFC Board. If any special opportunities were identified, those would be pulled out of the company exposure, where the largest return is generated, and place it in the special opportunities, he explained. The fund's portfolio had a 3 percent commercial-backed mortgage when the new observation was started. Therefore, those commercial-backed mortgages weren't purchased but rather were identified as fixed income but not fixed income that would protect [the fund] for deflation in a crisis event. Furthermore, those wouldn't be held long term. The aforementioned returns to the notion of knowing the fund's holdings and why it has those holdings, he said.

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MR. BURNS remarked that slide [16] can be confusing. He clarified that what is new is getting rid of mortgage-backed securities and purchasing TIPS and cash.

MR. SCOTT clarified that since the May APFC Board meeting, 4 percent of mortgage-backed securities have been sold, and 3 percent in TIPS and 1 percent in cash has been purchased, and the Alaska CD program has been moved to the cash bucket. Therefore, the opportunities bars on the chart on [slide 16] that illustrates a large difference may never happen. He reiterated that if there is a special opportunity, it would be pulled out of the company's exposure and placed in the special opportunity category. Such a change would cause there to be a press release noting that.

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REPRESENTATIVE DOOGAN, referring to slide 15, inquired as to how the change in equities, a 9 percent change, under the historical framework is not a significant change.

MR. SCOTT informed the committee that at the May APFC Board meeting, the portfolio held 2 percent in high yield securities, which had a higher risk adjusted return than equities; 1 percent in distress debt; slight overweight in commercial mortgage-backed securities of another couple of percent; and 13-14 percent in private real estate. Therefore, the actual securities held didn't change that much.

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REPRESENTATIVE DOOGAN indicated that he didn't understand. He then related his understanding that the slides are snapshots of changes. If all the changes are exactly as represented on the slides, then he questioned how the fund only moved about 5 percent of value.

MR. SCOTT clarified that the portfolio didn't look exactly like the policy allocation on the day he came to the APFC due to the tremendous volatility in the equity markets. He reminded everyone that after Lehman Brothers failed in September, the equity markets fell dramatically. The allocation wasn't changed with the charts.

[6:25:57 PM](#)

MICHAEL O'LEARY, JR., Executive Vice President/Manager, Fund Sponsor Consulting, Callan Associates, referring to the graph on slide 16, clarified that the new allocation to opportunities actually was funded from the company area. However, that hasn't been implemented yet. The company area includes corporate bonds and equities.

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REPRESENTATIVE DOOGAN surmised then that the charts aren't necessarily "done deals." Therefore, the differences projected in the asset allocation areas aren't necessarily accomplished.

MR. O'LEARY replied yes. For example, the opportunities under the historical view were dominated by absolute return strategies, such as hedge funds. The APFC staff and board

recognized that there was a small distressed investment that had been previously grouped in the broad fixed income portfolio as well as high yield bonds that had been previously grouped in the fixed income portfolio. The distressed investment was moved, in terms of place holding, into opportunities while the high yield bonds were moved to company exposure.

REPRESENTATIVE DOOGAN then asked if this means that at some point, these changes will be made.

MR. SCOTT answered, not necessarily, adding that there could be a situation in which no special opportunities are identified. However, the commercial mortgage-backed securities situation could be solved in a timely fashion and the fund's holdings in that space may be reduced.

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REPRESENTATIVE HAWKER expressed concern with the relatively simultaneous co-occurring activities of the extreme market volatility, the change of framework, and the significant change in asset allocation. The aforementioned changes occurring at the same time was unfortunate. Still, he questioned whether it was imprudent to have made the changes at the time. He then directed attention to slide 15, which reviews the old and new allocation in terms of the historical framework. The rebalancing of the old allocation in the context of the new allocation resulted in a significant liquidation of equity holdings. He then pointed out that the legislature has before it a huge amount of realized losses in which positions have been liquidated and losses on the investment have occurred. On the short horizon today, he inquired as to where the fund would stand had it been rebalanced to the old allocation rather than the new allocation. He related his understanding that had such happened, there wouldn't have been such significant realized losses. He then asked whether, during this triple change, other funds entered into significant liquidations or hold for the market bounce.

MR. BURNS informed the committee that APFC terminated some managers and liquidated their holdings because of their performance and other things happening in the firm. However, those funds went into equity. He clarified that realized losses were experienced when the managers were terminated, which he characterized as prudent since those managers weren't performing. In further response, Mr. Scott couldn't specify whether the permanent fund would've been farther ahead or

farther behind. He did explain that funds were taken from large cap managers and placed in a large cap passive fund, and therefore he surmised that it should be about a "push."

MR. SCOTT, with regard to the liquidation of equity managers during winter months, clarified that the fund moved from active management to passive management of a similar style or asset class in order to protect the permanent fund. The money wasn't used to buy cash or TIPS. He acknowledged that rebalancing occurred in December when over 1 percent in equities was added to the portfolio. On March 9th there was a decision to work toward rebalancing during which another couple of percent in equity was added as the fund moved toward the strategic asset allocation set by the APFC Board. He pointed out that the rebalancing occurred in the second and third fiscal quarters. In fact, the rebalancing occurred in the [first] fiscal quarter because the equity markets increased to the point that they needed to sell.

[6:36:49 PM](#)

REPRESENTATIVE HAWKER remarked that it's not so much what APFC did but when it did it.

MR. SCOTT said that when he came on board it was very important to him for everyone to be on the same page and understand in what securities the fund is invested. When he reviewed the fixed income portfolio, he could see high yield securities, commercial mortgage-backed securities, and distress debt, he wanted to be clear that those fixed income securities won't protect the fund if the market continues downward. One must recognize, he explained, that these are securities that will produce long-term returns. As the chief investment officer, Mr. Scott said he doesn't believe in guessing which way the market will go. Furthermore, the time horizon is long-term, as in a decade or longer, and thus decisions won't be made on a weekly or monthly basis. At the time, Mr. Scott felt it was prudent to change and have the APFC Board and staff to move together to the strategic asset allocation it desires while reflecting the risk in the portfolio.

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REPRESENTATIVE HAWKER opined that it sounds like a fairly profound decision process.

MR. O'LEARY, responding to the earlier question regarding what others were doing, related that all major funds became under allocated relative to their targets or equities, given the magnitude of the equity market decline. Others were also impacted by the lag in private market assets. The aforementioned created a challenge in determining how far from the target they were. Therefore, he opined that the process of rebalancing in the industry all the way to the target was slow, and the high fear level likely contributed. The permanent fund did begin to rebalance. He acknowledged that in hindsight, it would've been beneficial to have rebalanced more rapidly. However, he said he felt [APFC] rebalanced as quickly as the typical fund, which is in part reflected in the fiscal year performance in which the total year fund return was better than the median major public fund. The aforementioned wouldn't have been attainable had the fund not participated in a meaningful way in the March-June risk asset recovery. He pointed out that it wasn't just stocks, but also included high yield bonds and other sensitive issues.

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REPRESENTATIVE STOLTZE recalled this past legislative session when the APFC Board communicated an investment policy [divesture of investments in Sudan] that integrated social policy goals with investment goals. He asked if the APFC Board is considering revisiting that issue.

MR. FRANK said that it's not on the agenda at this time. He acknowledged that there is a difference in opinion on APFC's change in position, such that some legislators are disappointed. The desire, he explained, was to try to find a solution that would be collaborative. However, APFC missed the mark in terms of degree of collaboration and failed to recognize the level of concern within the legislature. He opined that the APFC was trying to reach something that would work and the approach was thought to be reasonable.

MR. BURNS offered to forward an article in which the Obama Administration has said that the situation has dropped below the previous definition of genocide; the situation is believed to be resolving itself.

[6:44:59 PM](#)

REPRESENTATIVE STOLTZE opined that it's not about the policy but rather about the APFC Board getting involved in social policies.

He suggested that although the APFC Board seemed to be dragged into the issue, it still colored how the legislature takes the APFC Board's position in terms of whether they are sound financial positions.

[6:48:20 PM](#)

ADJOURNMENT

There being no further business before the committee, the Legislative Budget and Audit Committee meeting was adjourned at 6:48 p.m.