

HOUSE FINANCE COMMITTEE
February 5, 2013
1:32 p.m.

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CALL TO ORDER

Co-Chair Austerman called the House Finance Committee meeting to order at 1:32 p.m.

MEMBERS PRESENT

Representative Alan Austerman, Co-Chair
Representative Bill Stoltze, Co-Chair
Representative Mark Neuman, Vice-Chair
Representative Bryce Edgmon
Representative Les Gara
Representative Lindsey Holmes
Representative Scott Kawasaki, Alternate
Representative Cathy Munoz
Representative Steve Thompson
Representative Tammie Wilson

MEMBERS ABSENT

Representative David Guttenberg
Representative Mia Costello

ALSO PRESENT

Mike Burns, Executive Director, Alaska Permanent Fund Corporation, Department of Revenue; Laura Achee, Director of Communications and Administration, Alaska Permanent Fund Corporation, Department of Revenue.

SUMMARY

^OVERVIEW: ALASKA PERMANENT FUND CORPORATION

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MIKE BURNS, EXECUTIVE DIRECTOR, ALASKA PERMANENT FUND CORPORATION (APFC), DEPARTMENT OF REVENUE, provided a PowerPoint presentation titled "Alaska Permanent Fund Corporation Designed for Sustainability" (copy on file). He

pointed to slide 2 titled "Renewable Resource." He discussed that the corporation's accounting was confusing, which was exacerbated by new government accounting standards. He referred to the information on slide 2 as "checkbook" accounting. He communicated that \$16.5 billion had been deposited to the Alaska Permanent Fund (APF) to date, \$19.8 billion in dividends had been paid, and the fund's current value was \$45 billion. He believed the fund had been incredibly successful and felt that Alaskans should be proud of the accomplishment. He moved to slide 3 that showed fiscal year to date (FYTD) returns for FY 13; the total FYTD return was 7.3 percent, the benchmark return was 7.4 percent, the ending balance was \$43.7 billion and the change from FY 12 was \$3.4 billion. He shared that the return through the end of January 2013 was 10.4 percent and the fund balance was \$44.9 billion. He stressed that the fund investment strategy focused on the long-term, but some individual months were very successful (e.g. January 2013).

Mr. Burns moved to slide 4 related to FY 12 performance. The total return had been -0.01 percent with a benchmark of -0.2 percent. The fund's FY 12 ending balance had been \$40.3 billion. He addressed the fund's performance over the past 28.5 years on slide 5. He noted that the fund had existed beyond 28.5 years, but the records from the performance consultant only went back that far. The fund's performance during the 28.5 year period was 8.8 percent. He highlighted that 2008 and 2009 had been devastating on returns as seen in the 5-year performance of 1.2 percent compared to the 3-year return of 10.4 percent. He shared that the 2008 calendar year was one of the 3 worst years in the 200-year history of available stock market records. He relayed that the other worst returns had occurred prior to the war of 1812 when the U.S. had cut off trade with France and England.

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Mr. Burns directed attention to the fund's asset allocation on slide 6. Categories included real assets, company exposure, opportunity pool, cash, and interest rates. He noted that assets within each of the categories were grouped by risk. Real assets accounted for 19 percent of the fund and worked to protect against inflation; the category included real estate, Treasury Inflation Protected Securities (TIPS), infrastructure, and other. The company exposure category included all public, private, domestic,

international equity and corporate debt. The grouping allowed fund investors to move in the capital structure of companies and industries (e.g. money could be moved from credit to equity) and enabled the fund to take advantage of growth and prosperity cycles. The interest rates category included U.S. treasuries and sovereign debt of developed countries, which worked to protect the fund against deflation. The other opportunity pool accounted for 18 percent of the fund's allocation and included market anomalies and special opportunities discovered over time. He explained that while the other asset allocations represented targets, the opportunity pool was limited to 18 percent given that special opportunities did not exist all of the time. He noted that any money that did not have a "special opportunity home" went into the company exposure allocation. He communicated his intent to further explain the slide later in the presentation.

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Mr. Burns pointed to a handout titled "Total Fund Value" as of February 1, 2013 (copy on file). The chart included rows for each asset allocation and columns showed traditional asset classes [e.g. equities, fixed income, and other]. Slide 7 included a pie chart of the fund's target asset allocation: stocks 36 percent, real estate 12 percent, absolute return 6 percent, private equity 6 percent, infrastructure 4 percent, cash 2 percent, bonds 20 percent, and other 12 percent (a small blue unlabeled segment represented public/private credit including mezzanine debt, high yield, and other).

Mr. Burns turned to slide 8 titled "The Effect of Diversification." The yellow line on the chart showed the total fund's performance from 2007 to 2012; individual asset classes were represented in blue. The slide's purpose was to demonstrate the importance of diversification and how the success of each asset class fluctuated with time. He relayed that APFC looked forward and not back; it did not operate as a market timer. He detailed that targets for each asset class also included bands; there was "risk dashboard" on 20 items that was looked at each day. The dashboard included red, green, and yellow zones. He elaborated that the chief investment officer and staff had the authority to trade within the green zone; approval by the executive director was required to operate in the yellow zone; and the board was notified when investments

moved into the red zone. The board could request a special meeting, members could request individual explanations, or the board could accept the staffs' written explanation. He elaborated that moving into the yellow and red zones triggered a discussion about investments. He noted that there could be a reason for moving into the areas and that the goal may be to be light in specific investments. He furthered that the board was apprised of the yellow zones at its regular meetings. He relayed that sometimes markets were unfavorable and it was not possible to adjust asset classes such as real estate and infrastructure; however, liquid asset classes could be adjusted.

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Mr. Burns stated that one of the fund's biggest strengths was that it was multi-generational; it had the ability to take a very long-term view and could handle illiquidity better than most funds. He detailed that historically illiquid assets provided a better return because they did not require a liquidity premium. The long-term view was taken as much as possible (sometimes in illiquid assets and private markets). He relayed more money was being invested in illiquid assets over time. He pointed to slide 27 titled "Risk Dashboard: Dollar Allocation Limits." He reiterated his earlier testimony that the dashboard was generated on a daily basis; risk measures included country, liquidity, and other. The corporation was proud of the dashboard that had been developed internally. He added that the overall zone parameters were reviewed on an annual basis.

Mr. Burns addressed slide 9 titled "2012 Performance by Asset Class." He relayed that the fund had performed close to and slightly better than benchmark in most asset classes, with the exception of real estate and absolute return. He communicated that it was difficult to match the NCREIF index [National Council of Real Estate Investment Fiduciaries]. He explained that the index used higher leverage than APFC; in difficult markets the APF would outperform the index. He shared that leverage was generally used in partnerships in the real estate portfolio. For example, the fund owned 50 percent of two large shopping centers with a public retail REIT [Real Estate Investment Trust]. The fund returns had also fallen well below the absolute return benchmark. He detailed that APFC had created the absolute return benchmark in 2004; it had never met the benchmark and it was clearly not the correct

target. He believed APFC had held out for managers to earn LIBOR [London Interbank Offering Rate] plus 400 basis points; however, the asset class did not generate income at that level. The corporation was in the process of looking at the HFR Index [Hedge Fund Research]; APFC managers had consistently beaten the HFR Index.

LAURA ACHEE, DIRECTOR OF COMMUNICATIONS AND ADMINISTRATION, ALASKA PERMANENT FUND CORPORATION, DEPARTMENT OF REVENUE, used the poor absolute return performance on slide 9 to point out the importance of portfolio diversification spread across a multitude of asset classes.

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Mr. Burns turned to slide 10 titled "Stock Portfolio." The inner ring of a circular chart included the active, passive, and quasi-passive methods of management for accessing equity; active management represented slightly over 50 percent of the management options. He detailed that passive management followed indices, which was momentum driven. As a stock became increasingly successful it made up a larger portion of the index; he used Apple as an example. He added that under passive management the purchase price was typically high because it followed the success of a stock. Quasi-passive compared and ranked the fundamentals (sales growth, earnings growth, and other) of various companies. Active management was the most expensive and passive was the cheapest. Quasi-passive was more value driven. The next ring represented APFC's three portfolios: U.S., non-U.S., and global. He explained that global managers could invest in U.S. and non-U.S. investments. He listed major global exposure including Japan, U.S., U.K., Asia, Europe, and other.

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Mr. Burns directed attention to slide 11, which included the fund's top 5 holdings as of 12/31/2012. Top stocks included Apple, Samsung, Google, Microsoft, and Exxon Mobil.

Ms. Achee added that the chart showed the top 5 holdings out of the 6,000 individual securities owned by the fund.

Mr. Burns remarked that some of the 6,000 securities were owned by multiple APFC investment managers on behalf of the

fund. He added that Exxon Mobil may be the fund's top stock currently. Slide 12 illustrated the fund's bond portfolio, which included corporate, treasuries, non-U.S. government, mortgage-backed, commercial mortgage backed securities, non-U.S. corporate. He noted that non-U.S. bonds accounted for 7 percent of the portfolio. He continued to discuss the bond portfolio on slide 13. The slide included two circular charts, which showed that the portfolio's percentage of non-U.S. bonds had decreased in the last six months of 2012. He explained that the legislature had approved funds for two additional fixed income staff the prior year in order to allow APFC to begin managing international fixed income internally; he noted that the savings were dramatic. During the time APFC was preparing to make the transition from external managers to in-house management Europe began to have substantial financial problems; therefore, APFC had elected to hold off on making the change. He relayed that initially the fund had approximately \$950 million to \$1 billion in non-U.S. bonds (primarily in developed nations); however, it had reduced its exposure to approximately \$300 million. He noted that APFC was getting close to reversing the decision and filling the positions.

Ms. Achee added that the APFC managed portion shown in red (slide 13) would be larger in the following year.

Mr. Burns agreed. He remarked that internal management in any area was dramatically less expensive compared to external management. He continued to discuss internal management and noted that there were some items that could not be managed in-house. He added that APFC did not spend GF money; it was funded by receipt authority.

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Mr. Burns directed attention to real estate on slide 14. He believed the allocation was managed economically; management was conducted both internally and externally. The fund used five direct equity managers and one REIT manager. He discussed real estate's illiquid nature. He stated that the closest proxy to owning real estate was to own REITs. The portfolio consisted of 33 percent office, 30 percent retail, 25 percent multifamily, 7 percent REITs, and 5 percent industrial. He communicated that the barriers to entry in industrial real estate were not high, which made it difficult for long-term investors to find attractive properties. He observed that it was possible to

have the best warehouse one year only to see other identical warehouses built in the area the following year.

Mr. Burns looked at the portfolio's Tysons Corner Center real estate investment on slide 15. He shared that the fund had owned the property for many years, which was beginning an expansion phase. He detailed that the property had 2 million square feet of developed space; he equated it to a small city. He elaborated that the Washington, D.C. train system was planned to extend to Dulles and currently went two stops past the center. He elaborated on the train system. The building shown on the right had 440 apartments, the middle building was a 500,050 square foot office building, and the third building would be a Hyatt hotel; the buildings were all currently under construction.

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Mr. Burns continued to discuss Tyson's Corner Center on slide 15. The office building was 65 percent pre-leased; the lead tenant was Intelsat. He believed leasing the remaining 35 percent would not be difficult. He opined that the apartments would be attractive and would fill a need in the area; 20 of the units would be marketed at a lower price. He discussed the expense of new parking, which would be below ground; the spaces would be shared by the hotel and retail customers. He believed that sharing the spaces had saved \$50,000 per parking space. He added that the project used approximately 40 percent leverage.

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Mr. Burns looked at the real estate investment 299 Park Avenue on slide 16. The office building was 42 stories and was located next to the Waldorf Astoria hotel. The fund's investment partner was Fisher Brothers, who owned five major skyscrapers in New York. He shared that the Fisher family had built approximately 60 Fisher Houses across the country that were aimed at accommodating family of injured soldiers. He pointed to the building value [\$1.2 billion] and added that the building was approximately 50 percent leveraged. He remarked that investments in Manhattan were typically liquid assets.

Mr. Burns directed attention to the CityCenter II, III, and IV properties on slide 17 (CityCenter III was shown on the slide). The properties were office and retail, which were

located next to hotels and two interstates in Houston, Texas. He detailed that CityCenter II was fully leased, CityCenter III was close to or completely leased, and CityCenter IV was under construction. He remarked that the property did not carry a Manhattan price tag [\$50 million property value]. He moved to the residential Parc Huron property located in Chicago (slide 18). The property had been marketed as condominiums, which had not sold. He believed converting the units from apartments to condominiums could bring a high payout; however, APFC currently had no plans to make the conversion. Slide 19 pertained to the Simpson Housing LLLP based in Denver, Colorado. The corporation and the State of Michigan each owned 47 percent; the balance was owned by management. The real estate operating company had 16,000 units nationwide. He explained that the partnership was in the third year of a five-year plan to expand and update the properties; older product would be sold and replaced. He relayed that apartments were the "hottest asset class," which made it difficult to purchase properties that penciled out.

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Mr. Burns discussed private assets on slide 20, which included private equity, infrastructure, American Homes 4 Rent, and private credit. He detailed that private credit included mezzanine debt, bank loans, syndicated bank loans, and other. He moved to slide 23 related to American homes 4 rent; APFC owned 80 percent and the operator owned the remaining 20 percent. The head of operations had started Public Storage, which was larger than all other public storage companies combined. The homes were single family and had been purchased at foreclosure sales. He shared that in the past there had been no asset class for institutional ownership of single family homes; however, that had changed. He discussed that the partner had done a great job operating the venture, which included approximately 4,700 houses in various states. The corporation had committed \$600 million to date; the partner had invested \$150 million. He shared that two of the states APFC had liked the most were Texas and Georgia; every foreclosure sale occurred on the first Tuesday of each month, which made logistics challenging. He noted that Atlanta was the focus in Georgia, but the market was large and challenging. He listed Texas property locations including Dallas, Houston, San Antonio, and Austin.

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Mr. Burns continued to speak to slide 23 and relayed that competition for the homes was tight. He stated that individuals were walking around with stacks of cashier's checks. He continued to discuss the home purchase process. He communicated that American Homes 4 Rent had expanded to over 300 contract employees in the past year. He talked about the condition of the homes. The partnership may choose to sell the houses when they appreciated or may sell them to a REIT or to another aggregator. He relayed that the investment was expected to bring in a 6 percent to 7 percent yield; there was no leverage used.

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Mr. Burns explained that private equity consisted of purchasing companies that were not publicly traded. Private equity could include the sale of a family company for estate planning purposes, the sale of a subsidiary of a major corporation that no longer fit with the company's long-term goals, or other. The asset class used a significant amount of leverage; however, APFC believed returns were better than those on public equity. The asset class was limited to 6 percent in the APFC portfolio; however, it had not reached that amount. Money from earlier investments was paying out, while the corporation continued to make new investments. He shared that APFC consultant Callan Associates had to put a limitation on private equity when making investment recommendations.

Mr. Burns addressed infrastructure investments on slides 21 and 22. He relayed that infrastructure assets were traditionally government owned or regulated. Examples included toll roads, pipelines, electrical transmission lines, ports, airports, and other. The corporation was invested in three partnerships with properties in the U.S. the United Kingdom, India, Argentina, and Canada. He elaborated that holdings included a propane distribution system in India, the airport in Vancouver, British Columbia, and the Gatwick and City airports in London. The legislature had approved a new co-investment infrastructure position in FY 13. He detailed that when APFC negotiated contracts with partnerships it was specified that the corporation would never invest more than a set amount into a project; if a project was over the set amount, another investor was required. He expounded that APFC bargained for

co-investment rights and the co-investment staff and outside consultant could make an independent decision on projects. He relayed that private investment had expensive fees; whereas co-investment had no fees. He stated that the staff could save the corporation millions or nothing, given that staff may decide not to invest in many projects. The corporation believed the position was a good investment.

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Mr. Burns looked at slide 24 titled "Multi-asset strategies." He discussed the corporation's affinity for emerging markets. Significant emerging markets included the BRIC countries (Brazil, Russia, India, and China), which were sometimes altered and referred to as BRIM (Brazil, Russia, India, and Mexico). The corporation believed the markets would grow more significantly than developed markets. He referred to emerging market debt and equity managers (two had been found in the same company). Cap Guardian and PIMCO managed APFC's emerging markets investments across three asset classes (equity, bonds, and currency). The investment managers had the ability to move money back and forth between the three asset classes. He relayed that APFC was happy with the results thus far.

Mr. Burns explained that absolute return was hedge fund investing and was the least risky asset class. He shared that it was necessary to take more risk than APFC managers currently took. He elaborated that the three managers had consistently outperformed the hedge fund indices; the index had not surpassed LIBOR plus 400 basis points. The corporation planned to examine its current policies related to absolute return. There were 157 underlying investments, 6 were owned by more than one manager. The risk had been spread, which was expensive, but diversification protection was necessary in order to limit potential financial impact if one of the investments failed.

Ms. Achee noted that the corporation's risk exposure was approximately \$10 million to \$15 million; if an investment did fail the company would not lose more than this amount. She noted the figures were significant, but not disastrous.

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Mr. Burns addressed the APFC external CIO program on slide 26. The program was in its second year and five managers

had been hired out of a larger pool. The corporation was interested to know how the managers would invest if they were "unshackled"; he noted APFC had not completely unshackled them. The managers had been instructed to invest money in any way they believed would be the most successful with the exception of real estate and provided that the money would be available in two years. Slide 26 showed pie charts for two of the managers including PIMCO and GMO. The investment strategies were very different; GMO invested more heavily in equities (shown in green). He added that other managers had very little invested in equities. The goal was broad style diversification; the corporation was pleased with the outcomes. He continued that one of the managers had outperformed expectations; GMO had underperformed; however, the company's style was to wait it out until valuations came its way. He remarked that the company had lost half of its business when it had refused to invest in the dot-com era because it did not believe the valuations made sense. The company's strategy was to invest at the bottom. He relayed that one of the external CIO managers was invited to speak at each of the APFC board meetings.

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Mr. Burns detailed slide 28: "Financial Networks." The slide illustrated all APFC systems and how they interrelated. He remarked on the system's complexity. The system required substantial security to protect it from hackers in various nations. He relayed that the systems shown on slide 28 were needed to run the \$45 billion in funds.

Ms. Achee discussed the APFC systems that were created by independent software companies specializing in the particular area. She explained that the information technology staff was tasked with working to ensure that the various systems were compatible and could communicate effectively. She mentioned the difficulty of incorporating the different technologies. She stressed that the technologies were instrumental in enabling the corporation to compete with global investors. She relayed that the corporation would be requesting funds in years to come for new systems and consulting on existing systems.

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Mr. Burns addressed dividend calculation on slide 29. He explained that statutory net income was the corporation's cash flow; it included dividends, interest, and rent received and realized capital gains. The Alaska Permanent Fund Dividend (PFD) calculation used five fiscal years. Each year the income from the earliest of the five fiscal years dropped off as the most current fiscal year was added. He pointed to the \$2.9 billion figure in FY 08 and commented that it was unlikely a number that large would replace it. The corporation anticipated that the PFD would decrease again in the current year. He detailed that when the negative \$2.5 billion figure from FY 09 dropped off the formula would change dramatically. He believed that in the next five years statutory net income would continue to be a small number despite fund growth. He elaborated that the largest component had historically been from fixed income, but with the 10-year treasury at 2 percent to 2.4 percent, it would not bring significant earnings; low interest rates would hold the statutory net income down for some time.

Ms. Achee noted that there was no direct correlation between mineral royalties (oil included) and the dividend calculation (slide 31). She explained that incoming royalties boosted the PFD's total principal value over time, which did increase statutory net income. She elaborated that the royalties did add to the dividend in a subtle way over time.

Mr. Burns discussed peer recognition on slide 32. He relayed that APFC had won an aiCIO industry innovation award two years earlier. He shared that APFC met with the Singapore Government Investment Corporation on several occasions; Singapore had two of the largest sovereign wealth funds in the world. Other public and private fund managers APFC had met with included the Norway Government Pension Fund, Mitsubishi UFJ Trust and Banking, Massachusetts PRIM, California State Teachers Retirement System, and the University of California. He added that the representatives with the major Japanese government investment fund would be visiting APFC in the near future. He stated the APFC was essentially a sovereign wealth fund. He pointed to an international group that included all sovereign wealth funds; the two U.S. representatives were the U.S. treasury and APFC. He believed the corporation had a good reputation.

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Representative Wilson wondered why APFC was not investing in infrastructure in Alaska. She believed the message implied that Alaska projects were not worth investing in. She asked if a project or two could fit into the portfolio in the future.

Mr. Burns replied that APFC was required to obtain a specific return. There had not been many projects available in Alaska. He detailed that the corporation invested in infrastructure projects via [pooled] funds with other investors. He remarked that he would inform other investors if an appropriate project emerged in Alaska. He discussed that APFC was potentially interested in more Alaska real estate; however, it would be possible for APFC to overheat the market very quickly. He elaborated that the institutional size the corporation would need to invest in was substantial; there were not institutional-sized deals. He continued that the real estate market in Alaska was pretty well balanced. He reiterated that APFC could upset that market fairly quickly. He added that one of its real estate managers was tasked with looking for deals in Alaska.

Representative Wilson clarified her interest in an infrastructure project such as the pipeline or a Liquid to Natural Gas (LNG) plant on the North Slope. She understood that Alaska did not have very large real estate investment opportunities, but she believed there were mega infrastructure projects that APFC could invest in.

Mr. Burns responded that APFC had been directed by the legislature in statute to not act as a lender or investor of last resort. He explained that APFC would prefer to invest in Alaska if the numbers worked. The corporation did not want to go into deals that required it to locate \$200 million (or other) in low-cost capital.

Vice-Chair Neuman asked whether APFC had any investments in Alaska. Mr. Burns replied it had two investments in Alaska including the Goldbelt Building in Juneau and an old mortgage of approximately \$60,000. He elaborated that the mortgage was the remainder of an old program.

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Ms. Achee added that APFC was not averse to investing in Alaska; statutes outlined that if it was presented with two equal investments (one in Alaska and another outside of Alaska) it was directed to choose the Alaska investment. Ultimately the corporation's direction was to make money. She elaborated that if a mega project presented itself in Alaska and the numbers worked out, there would be no reason why APFC would not be interested in being in a pool of investors. She added that diversification was important and the corporation would not invest as a sole financial supporter in a project.

Representative Gara asked APFC to keep its eye on the development of shale oil on the North Slope. He surmised that the development may present a potential partnership investment opportunity. He asked what kind of cost savings could be achieved if some of the more expensive private contracts could be replaced with in-house staff.

Mr. Burns answered that the next step would be a co-investment position for private equity that would include the same type of follow-on rights used in infrastructure investments, which saved on fees. There were two positions for international fixed income that had not been filled because APFC had veered away from the asset class; the corporation was looking to increasing investments in the area and planned to fill the positions. He communicated that approximately half of the savings from the international fixed income manager had been realized due to APFC's divestment in the asset class. The corporation had contemplated a mathematically driven internal stock fund that would require a specific market cap, dividend yield, and price/earnings ratio. The fund would be quasi-passive. He could not quantify the number. The corporation's operating budget request was approximately \$12 million, but its manager budget was at least 10 times larger. He communicated that there were currently some investments that the corporation would not consider. Things that seemed out of reach currently may be reachable if interim steps were taken over time. He remarked on the number of APFC positions.

Ms. Achee clarified that there were currently 38 positions. Mr. Burns added that two of the positions were currently vacant.

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Representative Gara asked whether APFC would be coming forward with a plan regarding bringing positions in-house for cost savings. Mr. Burns replied that APFC was planning a board meeting that would focus on refreshing the corporation's strategic plan later in the spring. The entity only provided one service, which was to manage money for returns. He believed it may be possible to provide the legislature with a multi-year plan the following legislative session.

Ms. Achee elaborated that the board had been thinking about the ideas; the three positions received for FY 13 were phase 1 of a plan devised by the board in the past two years. She stated that growth had been taken in a managed approach. She relayed that the corporation would present additional phases in future years until it reached the point where management could not be internalized any further. She communicated that it was challenging to attract talented staff from out of state that would enable the corporation to internalize some of the management.

Mr. Burns noted that it may be advantageous for the corporation to have an office out of state if it planned to invest heavily in private equity and co-investments. He detailed that it was necessary to be with the other investors on a daily basis. He was uncertain where the employees would be located (e.g. New York, San Francisco, or other). He discussed the importance of interaction with gatekeepers and those running underlying funds. He clarified that the corporation was not moving out of Alaska.

Ms. Achee agreed that the corporation did not intend to leave Alaska.

Co-Chair Stoltze suggested looking to the Alaska Railroad for advice on how not to develop the urban transfer center property at Tyson's Corner. He observed a shale oil investment seemed like a good deal; however, it would be moving money from one state pocket into the PFD given the way tax credits worked. He surmised the public would be unhappy if tax credits were taken from the General Fund for deposit into the PFD.

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Mr. Burns answered that he was uncertain about how the shale credits would work. He reminded the committee that APFC had no use for tax credits. He surmised that the investment may be good for a tax paying entity.

Co-Chair Stoltze made a remark about tax credits and politics. Mr. Burns noted that APFC was not a tax payer. Co-Chair Stoltze understood and noted that his comment may have been editorial.

Representative Kawasaki asked about external managers and brokers and wondered how frequently contracts were reviewed and turned over. He discussed the history of APFC. The permanent fund of other states such as Wyoming, Montana, New Mexico, and others did not come close to the Alaska fund. He understood that making money was the corporation's primary goal; however, he lamented that the goal could not include Alaskan investments.

Mr. Burns answered that it varied slightly by asset class. He informed the committee that its equity staff had been hired to oversee the managers on a daily basis to ensure that APFC's directives were followed. He communicated that real estate worked more with external managers; fixed income staff monitored the few external fixed income managers. He discussed that monitoring managers performance across the asset classes was a primary duty of the APFC staff. He addressed manager turnover and relayed that APFC had let managers go due to poor performance; however, managers were terminated due to other reasons as well. He stated that if a manager had bad year it was the worst time to get rid of them. He compared the job to that of a fireman running towards the fire. He relayed that additional causes for termination included a change in ownership, the replacement of a managerial team, a change in finances, an ethical lapse occurred, or other.

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Representative Kawasaki was curious about the management of APFC. He mentioned the number of employees and contractors worldwide. Ms. Achee answered that APFC had 38 full-time employees; the two fixed income positions were vacant, which APFC hoped to fill by the end of the current fiscal year. There were roughly 60 external contractors across all of the corporation's asset classes (listed on the APFC website). The internal operating budget was approximately

\$11.5 million for FY 14 and slightly over \$100 million for external managers. She pointed to expertise and specialty provided by external managers and noted that some of the firms were small (APFC sized) whereas others were much larger global firms.

Mr. Burns added that APFC was large enough to access the best talent in the world. He pointed to the external management cost of approximately \$114 million for FY 14 only represented external manager fees that were billed to APFC. Certain asset classes (e.g. real estate) retained fees; they were taken as a reduction in income.

Ms. Achee invited legislators to visit the APFC office anytime.

Representative Kawasaki asked if APFC was subject to state procurement codes when it hired for contracts. He asked whether fees were reviewed frequently. Mr. Burns replied that generally the state did follow procurement codes; however, there was an exception for any fiduciary services.

Ms. Achee elaborated that for non-fiduciary contracts APFC followed the state procurement code. A similar process was used for fiduciary contracts; proposals were scored and compared. The corporation was not required to make a change to its general consultant Callan Associates, but it did choose to do a contract renewal on occasion; Callan Associates had twice beaten other companies in a request for proposal process. She noted that the state pension fund used the same process. She highlighted that the corporation did not fall under the state salary structure; statutes directed the APFC board to set the fund's salary management program.

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Co-Chair Austerman discussed that the committee would not meet the following day.

ADJOURNMENT

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The meeting was adjourned at 3:02 p.m.