

HOUSE FINANCE COMMITTEE
March 1, 2019
1:32 p.m.

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CALL TO ORDER

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

MEMBERS PRESENT

Representative Neal Foster, Co-Chair
Representative Tammie Wilson, Co-Chair
Representative Jennifer Johnston, Vice-Chair
Representative Dan Ortiz, Vice-Chair
Representative Ben Carpenter
Representative Andy Josephson
Representative Gary Knopp (via teleconference)
Representative Bart LeBon
Representative Kelly Merrick (via teleconference)
Representative Colleen Sullivan-Leonard
Representative Cathy Tilton

MEMBERS ABSENT

None

ALSO PRESENT

Lacey Sanders, Budget Director, Office of Management and Budget; Paloma Harbour, Administrative Services Director, Department of Labor and Workforce Development, Office of Management and Budget; Brad Ewing, Administrative Services Director, Department of Revenue, Office of Management and Budget; Bruce Tangeman, Commissioner, Department of Revenue; Michelle Prebula, State Investment Officer, Treasury Division, Department of Revenue; Bob Mitchell, Chief Investment Officer, Treasury Division, Department of Revenue.

SUMMARY

HB 39 APPROP: OPERATING BUDGET/LOANS/FUNDS

HB 39 was HEARD and HELD in committee for further consideration.

HB 40 APPROP: MENTAL HEALTH BUDGET

HB 40 was HEARD and HELD in committee for further consideration.

FY 20 BUDGET OVERVIEWS: DEPARTMENT OF REVENUE
 DEPARTMENT OF LABOR

PRESENTATION: INVESTMENT FUNDS UPDATE and CASH FLOW
DEFICIENCY PLAN PRESENTATION

Co-Chair Foster reviewed the meeting agenda.

#hb39

#hb40

HOUSE BILL NO. 39

"An Act making appropriations for the operating and loan program expenses of state government and for certain programs; capitalizing funds; amending appropriations; making appropriations under art. IX, sec. 17(c), Constitution of the State of Alaska, from the constitutional budget reserve fund; and providing for an effective date."

HOUSE BILL NO. 40

"An Act making appropriations for the operating and capital expenses of the state's integrated comprehensive mental health program, including supplemental appropriations; and providing for an effective date."

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^FY 20 BUDGET OVERVIEW: DEPARTMENT OF LABOR and WORKFORCE DEVELOPMENT

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LACEY SANDERS, BUDGET DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET, introduced herself and relayed intent to address a presentation.

PALOMA HARBOUR, ADMINISTRATIVE SERVICES DIRECTOR, DEPARTMENT OF LABOR AND WORKFORCE DEVELOPMENT, OFFICE OF MANAGEMENT AND BUDGET, provided a PowerPoint presentation titled "'FY2020 Governor's Amended Budget" dated March 1, 2019 (copy on file).

Co-Chair Foster acknowledged Representative Merrick online.

Ms. Harbour began on slide 6 of the presentation. She reported on the department's budget. The overall position count would go from 734 to 725 - the majority of the change was due to statewide consolidation initiatives.

Co-Chair Wilson noted the shift in positions.

Ms. Harbour replied there were two full time positions that would be deleted. She shared that the changes were mental health agreement and one as a result of a bill that passed the previous session (HB 79).

Co-Chair Wilson noted that there was \$294,000 in UGF, which was not included, but was offset by \$269,000 in DGF. She wondered whether those two items were in the same area.

Ms. Harbour replied that the information was on the upcoming slide.

Ms. Harbour moved to slide 7 and addressed the proposed changes to the budget:

- Discontinued Alaska Mental Health Trust Agreement (- \$125.5 GF and -1 FT)
- Decrease UGF to Offset Technical Vocational Educational Program (TVEP) funding for the Alaska Vocational Technical Center (+/--\$261.7 Net Zero Change)
- Statewide Support - Executive Branch 50 percent Travel Reduction (-\$146.7 GF)

Co-Chair Wilson asked if it was a one-time or ongoing cost related to TVEP.

Ms. Harbour replied that the figure changed annually. She stated that the amount distributed was the available projection. She noted that in FY 20, the overall amount was

\$1.5 million higher than FY 19. She anticipated that the balance moving forward would be at least that amount, based on the current revenue projections and healthy level of state wages.

Co-Chair Wilson asked for verification that the item would not impact other.

Ms. Harbour replied that all of the members were receiving an increase, and offset by a UGF decrease of the same amount.

Co-Chair Wilson wanted to ensure that the intent was clear, and that the schools were doing a good job training the youth.

Co-Chair Foster requested an allocation list.

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Vice-Chair Ortiz asked about the reduction to statewide travel. He asked what would not occur due to the reduction.

Ms. Harbour replied that the department would do more with telecommunications. She remarked on the ability to set the travel budget to accomplish the mission, it would still be allowable but would have to make reductions in other areas.

^FY 20 BUDGET OVERVIEW: DEPARTMENT OF REVENUE

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BRAD EWING, ADMINISTRATIVE SERVICES DIRECTOR, DEPARTMENT OF REVENUE, OFFICE OF MANAGEMENT AND BUDGET, continued with the PowerPoint presentation titled "FY2020 Governor's Amended Budget" dated March 1, 2019 (copy on file). He began on slide 3 of the presentation and addressed the department's budget.

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Mr. Ewing continued with the chart on slide 3.

Vice-Chair Ortiz asked about the increase from \$291 million to \$619 million. He thought much of the change had to do with a change in accounting and that previously the fees

had been taken out of investment totals. He asked for the accuracy of his statement.

Mr. Ewing agreed with the statements.

Vice-Chair Ortiz surmised that earnings figures would be up, wondered whether they would be a part of the earnings total.

Mr. Ewing would follow up.

Vice-Chair Ortiz thought it would mean the earnings total would be greater; therefore, when a PFD calculation or draw was made, it would be from a larger total.

Ms. Sanders clarified the point of the increment reflected in the chart was to show the actual cost for managing the funds.

Vice-Chair Ortiz asked for Ms. Sanders to repeat her last sentence.

Ms. Sanders answered it was not changing the amount being earned, it was changing the management fees.

Vice-Chair Ortiz replied that was his understanding. He pointed out that it would increase by that calculation, and wondered whether it would now be part of the earnings total.

Ms. Sanders would follow up on the question.

Co-Chair Wilson stated they were trying to find out how the \$291 million was used, and whether it was true that revenue was eating cost.

Ms. Sanders replied that the amount in the reports did not include the amount for management fees.

Co-Chair Wilson asked for verification that they had been charging the right amount, but it was not reflected in the budget.

Ms. Sanders agreed.

Co-Chair Wilson surmised that change and value of the funds, because it was being paid, was not shown in the represented fashion of the presentation.

Ms. Sanders replied in the affirmative and stated it was her understanding.

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Representative Josephson recalled a meeting with Angela Rodell, Executive Director, Alaska Permanent Fund Corporation, discussing the fees associated with the investments. He wanted to ensure that the statutory definition of what constitutes "earnings" did not somehow get impacted by a declaration by the legislature that the money was considered "earnings." He stressed that he only wanted clarification.

Ms. Sanders agreed.

Co-Chair Foster noted other individuals were available online.

Mr. Ewing continued to address the chart on slide 3.

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Mr. Ewing moved to slide 4:

- Align Management Fees with Actuals:
 - Alaska Permanent Fund Corporation (+\$269,501.3 Other)
 - Alaska Retirement Management Board (+\$60,000.0 Other)
 - Treasury Division (+\$117.2 GF and +\$70.4 Other)
 - Deregulate Small Charitable Gaming (-\$212.2 Other and -2 PFT)
 - Statewide Support - Executive Branch 50 percent Travel Reduction (-\$53.3 GF)

Co-Chair Wilson queried the deregulation of small charitable gaming, and its intent.

Mr. Ewing replied that there were two associated proposed bills addressed reducing the regulations. There were also two positions that would be impacted in the gaming section of the tax division. The proposal was that a permit or

annual fee would no longer be required, if gross receipts for that organization or municipality were less than \$20,000 per year.

^PRESENTATION: INVESTMENT FUNDS UPDATE and CASH FLOW DEFICIENCY PLAN PRESENTATION

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BRUCE TANGEMAN, COMMISSIONER, DEPARTMENT OF REVENUE, introduced a PowerPoint presentation titled "Discussion of State Cash Flows" dated March 1, 2019 (copy on file).

MICHELLE PREBULA, STATE INVESTMENT OFFICER, TREASURY DIVISION, DEPARTMENT OF REVENUE, relayed she had been the cash manager until the previous July. She provided information about her career background. She began on slide 2, "Treasury Division":

The Treasury provides cash management, investment and portfolio management, debt management, unclaimed property management and accounting services for the state's general fund, constitutional budget reserve fund, retirement funds, and numerous other funds and trusts. The Division provides staff to the Alaska Retirement Management Board and Alaska Municipal Bond Bank Authority and oversees the Alaska ABLE plan.

Ms. Prebula looked at slide 3, "Treasury Facts and Figures":

- 45 current Treasury Division staff.
- At 12/31/18, managed \$38.8B in assets in 45 separate accounts in a pooled environment:
 - 14 defined benefit funds under the direction of ARMB (\$24.8B).
 - 4 participant directed funds under the direction of ARMB (\$6B).
 - 25 funds under the direction of the Commissioner of Revenue (\$7.7B).
 - 2 funds under the direction of other state fiduciaries (\$225M).

➤ Debt Management issues state debt and lease/purchase financings for the State.

➤ Cash Management collects all revenues, pays all expenditures and determines the amount of cash available for investment daily. Cash flows are forecasted to determine future cash needs.

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Ms. Prebula continued to discuss slide 4, "Treasury Facts and Figures":

➤ Annually, or as needed, the Chief Investment Officer and staff perform research and analysis to develop asset allocations recommendations for discussion with the fiduciary of each fund.

➤ Consideration is given to the type and use of the fund, how long the fund is expected to be invested and what type of risk the fund can take.

➤ Callan and Associates provides 10 year Capital Market Assumptions that are used to build models to determine potential assets allocations that are discussed.

Ms. Prebula looked at slide 6, "GeFONSI I and II":

➤ GeFONSI includes the General Fund and Other Non-segregated funds invested in a pooled environment (GF proper= \$400 million).

➤ Department of Administration separately accounts for each fund within State Accounting system.

➤ Department of Revenue is responsible for investing the GeFONSI and calculating and allocating daily investment earnings to each fund.

➤ 180 funds, assigned as Types 1, 2, or 3. Type 1 funds receive their earnings, the others do not.

➤ GeFONSI II was created in 2018 to target a higher risk return profile and includes funds that are type 2 or 3.

Ms. Prebula advanced to a chart showing a daily projection model for the General Fund on slide 6. The slide showed 6 months at a time. She briefly looked at slide 7.

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Ms. Prebula moved to slide 8 and addressed takeaways. She noted that cash flow forecasting was an estimate. She remarked that estimates were wrong. The actual cash flows would be different, and the magnitude of the difference was unknown. She remarked that, even with a balanced budget, borrowing for cash flow deficits may occur. She remarked that, even in balanced budget years, there was often a requirement of a source for funding for cash purposes.

Commissioner Tangeman noted that the slide represented the expectation of the balance in the CBR. He remarked that aggregating the slide would show that a \$1.4 billion would be minimum amount. He felt that that the current balance of \$1.7 billion was a comfortable balance. He felt that

Vice-Chair Ortiz asked wondered whether the CBR was currently at \$1.7 billion.

Commissioner Tangeman answered in the affirmative.

Vice-Chair Ortiz recalled that the last figure he recalled was \$2.1 billion. He wondered whether the reduction was a result of one of the recent borrowings.

Commissioner Tangeman replied that the first draw on July 9 was the entire \$700 million in the CBR that was estimated based on the passed budget. He explained that the reason the CBR was drawn first was because it earned less. He stated that there was a desire to leave the Earnings Reserve untouched for as long as possible. The first Earnings Reserve draw was on September 11 for the Permanent Fund Dividend. He stressed that the first SB 26 draw for the government purpose was October 1.

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Vice-Chair Ortiz stated that the \$2.1 billion he thought was in the CBR was now \$1.7 billion.

Commissioner Tangeman answered it was due to the first \$700 million draw. A \$200 million draw had been taken on February 14 as well. He explained that it was more like a \$250 million deficit, and the difference would remain in the GF.

Representative Josephson asked if the difference would be swept back around the 30th of June.

Ms. Prebula replied that the Division of Finance would provide that information.

Commissioner Tangeman added it would be drawn down initially on the two dates into GF.

Representative Josephson stated that if they drew more from the CBR than was needed, the CBR would be restored to the required extent.

Commissioner Tangeman answered that the sweep would take place.

Representative Josephson asked about the time prior to 1990 and what had been done for cashflow. He noted that there was a smaller government at the time.

Ms. Prebula replied that she had begun as cash flow manager in 1998, so she had limited knowledge before then. She assumed that he was referring to 1999 when oil revenues were approximately \$9 per barrel.

Representative Josephson agreed.

Ms. Prebula responded that GF sufficiency at that time reached \$43 million. The legislature had passed a cap on the CBR, and how much could be borrowed. She noted that the budget was balanced at that time, at \$700 million. She explained that once that legislature adjourned, oil prices reduced to roughly \$9 per barrel. She noted that the \$700 was used rapidly, and the legislature reconvened in order to increase the cap. She stated that the minimum was currently \$400 million, and at that former time it was \$100 million.

Representative LeBon asked for verification that the working cash position was the CBR.

Ms. Prebula replied that the working cash was in the General Fund and the CBR and/or the ERA was the savings account.

Representative LeBon asked for verification that daily use of money from the CBR did not take place.

Ms. Prebula replied in the affirmative.

Representative LeBon asked if the CBR was available if needed.

Ms. Prebula answered in the affirmative.

Representative LeBon asked for verification that moving money from Alaska Industrial Development and Export Authority (AIDEA) and the SBR did not impact the working capital position of the state in any way.

Ms. Prebula responded in the negative.

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Representative Merrick asked about slide 2 and wondered the procedure for clearing the cash receipts in suspense, and whether there were departments that could clear money more quickly to have cash on hand.

Ms. Prebula replied that the procedure varied by department. She elaborated that in 1999 when there was only \$43 million in GF, many people were contacted to clear the receipts. She stressed that agencies were monitored for their clearing. There was an aging schedule, and agencies were notified of anything older than thirty days.

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Representative Josephson asked about the minimum amount to keep a healthy cash cushion. He referenced the amounts provided by Ms. Prebula, which was \$100 million 20 years prior and was currently \$400 million. He noted that there was a belief that it was the "minimum", but there was a healthier more responsible minimum of \$1.4 billion or higher.

Ms. Prebula agreed. She stated that \$400 million was the bare bones minimum for daily working capital. The number was composed of two days of expenditures. She shared that she had recently found that 10 days in the recent 3 years, there were out flows of over \$200 million. She shared that the \$1.4 billion was considered help keep the \$400 million above water throughout the entire year.

Commissioner Tangeman elaborated that it got to the heart of what was considered a "balanced budget." He remarked that a balanced budget did not necessarily mean there were no cash flow issues.

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Representative Josephson thought of the draw on the CBR like a straw connecting the GF to the CBR to provide capital in the event of fires or state emergencies. He asked if there were requests in the current budget.

Commissioner Tangeman deferred to OMB.

Vice-Chair Ortiz asked about the minimum balance that should be maintained in the CBR.

Commissioner Tangeman answered that the amount was about \$1.4 billion, and he thought it was about \$1.7 or \$1.8 billion - \$2 billion would be a more comfortable minimum for the CBR.

Vice-Chair Ortiz was looking for the department's recommendation. He clarified that he was not an advocate of taking more from the CBR, but some may be.

Commissioner Tangeman answered in the affirmative, and felt that they were currently at the comfortable minimum.

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Representative LeBon stated that when he had worked in banking there would be an analysis of a business's efficiency by days accounts receivable and days accounts payable. He wondered whether Alaska had a good reputation in being timely payers of its obligations.

Ms. Prebula replied that the Treasury Division was not responsible for paying all of the bills of the state, but it's using its working capital to the best of its ability.

[2:24:13 PM](#)

BOB MITCHELL, CHIEF INVESTMENT OFFICER, TREASURY DIVISION, DEPARTMENT OF REVENUE, provided information on his education and career. He introduced a PowerPoint presentation titled "Performance Comparison," dated March 1, 2019 (copy on file). He moved to slide 2 and spoke to investment performance. He pointed to another document in members' files for information only.

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Mr. Mitchell noted that the information was his personal assessment of the portfolio. He stressed that the information had not been endorsed by the Permanent Fund Corporation, but they may have a different perspective. He noted that there was an equity target of the various portfolios. He shared that considering the riskiness of a portfolio was a proportion of that portfolio that was held in equities. He stated that in some cases, on the state side, there were portfolios whose equity allocation had changed over the previous five years. He provided an example. He shared that in FY 14 the allocation to equities in that portfolio was 42 percent, then increased to 50 percent, then to 55 percent. It stayed at 55 percent for a few years until the asset allocation was changed in November 2018. It was currently in the high 60 percentage range.

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Representative Sullivan-Leonard asked about the investment performance for the past couple of years in the format on slide 2.

Mr. Mitchell agreed to provide that information.

Representative Sullivan-Leonard wanted the information to appear like slide 2.

Mr. Mitchell replied in the affirmative.

Co-Chair Wilson asked for clarification about the benefit of moving the PCE endowment.

Mr. Mitchell replied that the CBR asset allocation was more conservative than the Power Cost Equalization (PCE).

Co-Chair Wilson asked if Mr. Mitchell would recommend moving the PCE into the CBR.

Mr. Mitchell answered it depended on the use of the fund. He stated it was a policy call.

Co-Chair Wilson countered that she believed it was a numbers call. She thought they would be hurting themselves by moving the money that was making more than it would be if moved.

Commissioner Tangeman answered that it was a policy call. He stated it was a liquidity issue - if the purpose was to make funds more liquid, since seeing greatly reduced available revenues.

Co-Chair Wilson understood the policy call about what the money would be used for, and she thought it may be a question for the governor. She thought they were long overdue if they were waiting for oil to save the state. She thought it was important to save the money.

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Commissioner Tangeman felt that was an accurate statement, because the discussion was regarding a very finite amount of revenue.

Vice-Chair Johnston referenced asset allocations for ARMB and APFC. She asked how the asset allocation was determined.

Mr. Mitchell replied there was a board of trustees for APFC and ARMB responsible for determining an asset allocation. For other state managed funds the CIO worked with the DOR commissioner to determine the allocations.

Vice-Chair Johnston asked whether the department did a stress analysis to determine the allocation.

Mr. Mitchell characterized the process of revisiting the funds, addressing needed changes, and set a portfolio to maximize income. He noted the need to build a portfolio that sought to deliver the objective with the least amount of risk.

Vice-Chair Johnston asked if they had some flexibility.

Mr. Mitchell replied that once an allocation had been established, they worked to adhere to the allocation.

Representative LeBon asked about the first two funds listed under DOR Funds on slide 2 and asked for detail.

Mr. Mitchell answered that General Fund and Other Non-Segregated Investments (GeFONSI) funds were in one pool managed from the investment perspective. He explained that there were approximately 180 funds total, and the motivation for doing so was to take a subset of the funds.

Representative LeBon asked about the Public School Trust fund and how the earnings were utilized.

Mr. Mitchell answered that the fund was managed like an endowment and was paid out based on 5 percent of the past five year average. He stated that it was a moving average based on market values, which was a fairly aggressive target. He noted that there were a number of factors that were taken into consideration when thinking about an appropriate asset allocation. He explained that it had a risk profile with equities that were almost 70 percent.

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Co-Chair Wilson asked about the CBR prior to taking money out of it. She asked if he remembered how much the money they had made on the investment.

Mr. Mitchell did not recall the specifics. He would follow up.

Co-Chair Wilson thought it would be helpful to Alaskans to know that was an effort not only trying to keep \$2 billion but to allow the account to begin growing again. She noted it had only been making 1 percent, which was too low.

Mr. Mitchell noted Co-Chair Wilson's point. He elaborated that the intent of the legislature at the time had been to create a vehicle for DOR to earn a higher rate of return.

Mr. Mitchell moved to slide 3 and provided an investment fund snapshot.

Co-Chair Wilson appreciated the list of funds, but understood that many could not be touched. She used the airport fund as an example. She asked the department to provide a list.

Co-Chair Foster thanked the presenters for their presentation.

Co-Chair Wilson noted that the committee was still waiting for the priority list from OMB. She asked commissioners to provide a priority. She wanted to understand how the budget had been compiled. She noted they had been waiting.

HB 39 was HEARD and HELD in committee for further consideration.

HB 40 was HEARD and HELD in committee for further consideration.

Co-Chair Foster addressed the schedule for the following week.

ADJOURNMENT
2:55:27 PM

The meeting was adjourned at 2:55 p.m.