

HOUSE FINANCE COMMITTEE
January 23, 2024
1:36 p.m.

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CALL TO ORDER

Co-Chair Johnson called the House Finance Committee meeting to order at 1:36 p.m.

MEMBERS PRESENT

Representative Bryce Edgmon, Co-Chair
Representative Neal Foster, Co-Chair
Representative DeLena Johnson, Co-Chair
Representative Julie Coulombe
Representative Mike Cronk
Representative Alyse Galvin
Representative Sara Hannan
Representative Andy Josephson
Representative Dan Ortiz
Representative Will Stapp
Representative Frank Tomaszewski

MEMBERS ABSENT

None

ALSO PRESENT

Pam Leary, Director, Treasury Division, Department of Revenue; Zach Hanna, Chief Investment Officer, Treasury Division, Department of Revenue.

PRESENT VIA TELECONFERENCE

Adam Crum, Commissioner, Department of Revenue.

SUMMARY

PRESENTATION: SAVINGS, RESERVES, & INVESTMENT FUNDS

Co-Chair Johnson gave an overview of the agenda for the day. She indicated that testifiers were online and in the room to present.

^PRESENTATION: SAVINGS, RESERVES, & INVESTMENT FUNDS

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PAM LEARY, DIRECTOR, TREASURY DIVISION, introduced herself and her staff.

ADAM CRUM, COMMISSIONER, DEPARTMENT OF REVENUE, ANCHORAGE (via teleconference), appreciated the committee's time. He apologized for not being at the meeting in person due to weather issues.

Ms. Leary introduced the PowerPoint Presentation "Update on the State's Investment Funds and Cash Flows" dated January 18, 2024 (copy on file). She reviewed the agenda for the presentation on slide 2. She advanced to slide 4 and offered an overview of the Treasury Division's role under the Department of Revenue (DOR). The slide showed four of the sections in the division: the Cash Management Section was in the bottom right corner of the slide and the remaining three sections related to the investments. The division had 40 experienced staff members, many of whom held professional designations such as CFAs, CPAs, CTPs, and other advanced degrees and designations. Managing numerous funds and cash flows was a complex task and required an understanding of investment management and banking systems which were highly integrated into the state accounting system.

Ms. Leary directed attention to the Portfolio Management Section on the slide. She relayed that the section was referred to as the "front office" of the treasury and invested assets for state fiduciaries using the Alaska Retirement Management Board (ARMB). In FY 23, there were 57,000 trades made on behalf of hundreds of state accounts that rolled into 48 investment funds and utilized 32 investment pools. The pools were supported by 150 external and internal investment managers and 600 private equity funds.

Ms. Leary continued to the accounting and operations portion of the treasury, which ensured that all trades and costs were directed and accounted for in the correct accounts and funds. The next section of the division was the compliance office, or "middle" office, which performed 160 compliance tests on trades every day and calculated

daily performance for 30 state funds internally. Cash management processed roughly 100,000 transactions annually for departments to realize revenue and expenditures in the accounting system. Cash inflows and cash outflows totaled over \$15 billion annually. The cash management team coordinated with the investment team to maximize the state's investment assets.

Ms. Leary advanced to slide 5 and gave an overview of the complex funds that were managed by the treasury. The treasury managed \$50 billion in assets for 48 funds across the risk spectrum from lower risk cash-equivalent investments through higher risk endowment and retirement funds. Retirement funds had the highest risk tolerance and included 18 different funds totaling \$41 billion. The remaining funds on the slide were state funds and were listed by risk tolerance. Over half the assets managed by the treasury were directed or traded internally by treasury staff. The treasury met with ARMB and state fiduciaries quarterly to review investment performance and set investment policy and asset allocations. There was also a three-person investment advisory committee that provided independent viewpoints based on the members' respective investment backgrounds. The treasury team had provided excess returns, cost savings, and error prevention.

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Co-Chair Johnson asked what the chart on the right side of the slide was referring to. She asked for more information on the Illinois Creek Mine.

Ms. Leary responded that the Illinois Creek Mine fund contained money that was given out upon bankruptcy of a mine managed by the state. The monies would be used for mine reclamation for the Illinois Creek Mine.

Co-Chair Johnson asked where the mine was located.

Ms. Leary responded that she did not know but she would follow up.

Representative Josephson responded that he thought the mine was in the Yukon-Kuskokwim Delta.

Ms. Leary remarked that the mine had a long history and money changed hands multiple times in order to acquire the

funds for the mine reclamation. She would follow up with more detail.

Co-Chair Johnson asked if the mine was already on deposit for reclamation of the site. She asked if the mine itself transferred hands.

Ms. Leary responded that the management company transferred hands. The responsible company experienced bankruptcy and the money was received by the state as payment for the bankruptcy. She understood that there was a schedule for using the money.

Co-Chair Johnson wanted to ensure that the proper reclamation efforts had occurred.

Representative Hannan asked what the assumed end date would be for the reclamation plan. She wondered if the state still needed \$1 million from reclamation or if it needed closer to \$1 billion.

Co-Chair Johnson asked Ms. Leary to follow up with some general information about the mine.

Ms. Leary would follow up with the requested information.

Representative Tomaszewski noted that there were two school funds listed on the slide: the Public School Trust Fund (PSTF) with \$799 million in assets and the Education Endowment with \$1.3 million. He asked for more information about the funds.

Commissioner Crum replied that he would be covering PSTF in more detail later in the presentation. The Education Endowment fund was essentially a raffle, and it was growing in size.

Representative Tomaszewski replied that he would be happy to wait for the information further on in the presentation.

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ZACH HANNA, CHIEF INVESTMENT OFFICER, TREASURY DIVISION, DEPARTMENT OF REVENUE, continued the presentation on slide 6. Overall, 2023 was a strong year for the funds managed by the treasury. Returns exceeded peer-performance and benchmarks which meant that state assets had seen an influx

of revenue. The treasury team focused on low-cost internal investment management which made the state's costs lower than its peers.

Mr. Hanna advanced to slide 8 which detailed an update on the capital market performance. The prior few years had been volatile and capital markets had been focused on the interplay of inflation, interest rates, and economic growth. The Federal Reserve responded strongly to inflation by increasing short-term interest rates to 5.25 percent, which decreased annualized inflation from 9.1 percent in June of 2022 to 3.4 percent in December of 2023. The chart on the right side of the slide ranked benchmark returns by asset class from 2018 through 2023 and performance in 2023 was positive across all measured asset classes. There was also a 26 percent increase in broad U.S. equities and roughly 5 percent in returns for core U.S. fixed income and cash equivalents.

Mr. Hanna continued to slide 9, which included a chart on the treasury asset class performance that the treasury managed for non-retirement state portfolios. The investment pools were all comingled and used to construct highly lucrative portfolios for the state that were efficient and low cost. The majority of the assets were managed internally and focused on delivering market returns with significant upsides and limited downsides.

Mr. Hanna explained that the top section of the chart showed the total performance by asset class, the middle section showed benchmark performance, and the bottom section showed performance relative to the benchmark. All of the numbers were relevant through December of 2023. Returns were strong in the top section and cash and bonds ranged from 4 percent to 8 percent and equities ranged from 10 percent to 26 percent. The returns added over \$300 million in income gains during 2023.

Mr. Hanna relayed that the bottom section also showed strong overall returns. More than 80 percent of the assets in the state portfolio were in the first three categories: cash, short-term fixed income, and core fixed income. The categories were all internally managed and produced consistently excellent returns. Total excess returns in 2023 for internally managed accounts across ARMB and state assets added \$90 million in value over benchmark returns.

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Representative Stapp referred to the Real Estate Investment Trust (REIT) asset class listed on the slide. He noted that REITs typically paid high dividends. He asked if the high dividend payouts were included in the figures or if the figures represented the base of the investment itself.

Mr. Hanna responded that REIT performance figures represented the total return between the appreciation and the income component. The REITs returns were the lowest returns listed on the chart due to the challenging real estate market.

Representative Stapp assumed that the treasury was responding accordingly to the market.

Mr. Hanna responded that REITs were a small part of the state portfolio and were only used in the larger endowment-style funds. He relayed that REITs were the smallest allocation of the funds and made up about 1.5 of total assets. The REITs were used primarily for diversification of funds and the division was comfortable maintaining the current allocation given the strong performance.

Co-Chair Edgmon remarked that the PCE Endowment was moved over to the Alaska Permanent Fund Corporation (APFC) through a bill that had been passed in the prior session. He asked whether the transition had been completed.

Mr. Hanna responded that there were upcoming slides that would cover the topic in detail. The transition occurred at the end of the prior fiscal year and was successful.

Co-Chair Johnson asked about the relationship between Callan and Associates and the state agencies.

Mr. Hanna responded that Callan was the consultant for ARMB but it was not a consultant for the treasury's assets. He explained that ARMB went through a periodic request for proposal (RFP) process to hire investment consultants and Callan had been a successful recipient of the RFP for a long period of time. The RFP process was set to occur in the present year. He added that Callan was also APFC's consultant. From the division's perspective, Callan was an ARMB consultant and not a state retirement consultant.

Callan had often reported to the legislature due to the meaningful relationships it had with ARMB and APFC.

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Ms. Leary continued to slide 10 and detailed the savings reserve funds. She relayed that the blue part of the chart on the slide discussed the fiscal year-end balance of the main fund of the Constitutional Budget Reserve Fund (CBRF). The fund was created in 1990 when Alaska voters approved an amendment to the constitution. All money received by the state after July 1, 1990, through resolution of disputes about the amount of certain mineral-related income was required to be deposited into the CBRF.

Ms. Leary explained that the yellow area of the chart showed the amounts of the subaccount of the CBRF which the legislature created in 2000. In accordance with AS 37.10.430, money invested in the subaccount would be invested to earn higher returns than in the main fund. Utilizing the subaccount was limited based on the assumption that the funds would not be needed for at least five years. In 2008, \$4.1 billion was deposited into the subaccount and was managed to achieve a higher return than the main fund. In April of 2015, the balance was returned to the main fund when it was determined that the fund would be needed within five years. The legislature may appropriate funds from the CBRF under certain circumstances to fund the operations of state government with a simple majority vote when the amount for appropriation was less than the prior year, in which case a three-quarters vote would be required.

Ms. Leary indicated that the green area represented the statutory budget reserve (SBR) fund which was created in 1986 and was part of the General Fund and Other Non-Segregated Investments (GeFONSI) before and after being managed as a separate fund from 2013 through 2015. On June 30, 2023, the balance of the CBRF was \$2.6 billion and the SBR contained \$404 million.

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Mr. Hanna continued on slide 11. The treasury had a formal state investment review with the commissioner and an independent investment advisory committee. Capital markets and performance were reviewed for each fund quarterly and

reviewed capital market assumptions and select asset classes for investment at least once per year. The treasury went through each fund and set the appropriate policy and asset allocation in a transparent manner. He relayed that the CBRF had a low-risk tolerance and could be used as an emergency reserve during times of cash flow uncertainty. The fund had a potentially short time horizon and needed high principal protection. The CBRF was invested in 100 percent cash equivalents and 2023 was a good year for short-term investments such as the CBRF. The one-year performance was 5.39 percent, which beat the benchmark by 41 basis points. He clarified that one basis point represented one one-hundredth of a percent; therefore, 41 basis points was 0.41 percent.

Co-Chair Edgmon commented that it seemed like there was a lot going on and that the treasury had a substantial amount of in-flow and out-flow. He asked if the CBRF was a buffer and if it was considered the working capital reserve. He appreciated all of the work done by the treasury.

Mr. Hanna replied that he appreciated the acknowledgment. Both the general fund and the CBRF were subject to a potentially high volume of cash transactions.

Representative Josephson asked Mr. Hanna to explain the growth in the CBRF over the previous year. He understood that the legislature did not draw from the CBRF in the prior year and that there would be surplus funds coming in, but the funds had not been seen yet. He was surprised by the growth of the fund.

Ms. Leary responded that the sweep occurred in the prior two years but there was not a reverse sweep. The surplus of about \$1.5 million had been moved to the CBRF permanently. She did not have all of the details but the Department of Administration (DOA) would have the information.

Representative Josephson understood that when the previous \$400 million balance of the higher education fund was swept, it would account for \$400 million of the \$2.7 billion.

Ms. Leary responded that Representative Josephson offered an accurate example, but the higher education fund was refinanced. There were smaller funds that were also swept and the monies were not put back into the smaller funds.

Representative Hannan asked if the treasury had an opinion or formula as to how much money should be kept in the CBRF.

Ms. Leary responded that there were various types of metrics that cities, states, and other organizations utilized to determine the amount of money that should be kept in a fund. A variety of amounts had been cited as the ideal number for a variety of reasons, from about \$500 million to \$2 billion and above. The treasury thought that \$2 billion was a reasonable marker.

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Commissioner Crum added that DOR would continue to address the amount of money kept in the CBRF. A previous slide showed the subaccount structure, and he explained that the subaccounts were at the discretion of the commissioner of DOR as to how much to invest. The topic was brought up before the Senate Finance Committee and there were internal discussions on the topic within DOR. The department continued to discuss how to determine when it was appropriate to put dollars forward from the CBRF to the subaccount to invest for the long term.

Ms. Leary continued on slide 12 and the historical balances of the two GeFONSI accounts. The general fund itself was part of the GeFONSI and all cash flows that came into the state and went out of the state flowed through the general fund. A minimum of \$400 million was kept in the general fund to ensure that there were enough funds for the state to make its required payments. There were about 180 other accounts and funds that had assets within the GeFONSI and the accounts were managed together but accounted for separately. The first GeFONSI was created in 1992 as a way to pool accounts for investments and the second GeFONSI was created in 2018 to target a slightly higher risk tolerance for a subset of the funds. As on June 30, 2023, there was \$3.27 billion in the GeFONSI funds combined and \$1.2 billion of the total represented the general fund.

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Representative Josephson asked why money was left in the general fund during the years of high oil prices from around 2007 through 2012.

Ms. Leary responded that the legislature decided to maintain the money in the general fund and not put it into the CBRF.

Representative Galvin asked if there was an opinion as to what the balance of the CBRF would need to be to allow the subaccount to be funded.

Ms. Leary replied that there was a five-year usage requirement for any funds that went into the subaccount. Unless there was money that would not be touched or needed for five years, the money would remain in the main account. Both the subaccount and the main account had independent asset allocations, which was also a matter of discussion.

Representative Stapp understood that the CBRF was being utilized in five years depending upon revenue factors. He asked if there was a ballpark number for the amount of money that needed to be kept in the CBRF.

Ms. Leary responded that the total amount incoming to the CBRF was known, but the amount coming to the general fund was not known. There was a significant amount of uncertainty about whether money would be available to the general fund.

Ms. Leary mentioned that the appendix and the end of the presentation listed the top 30 funds in both GeFONSI accounts. She thought members might be interested in reading through the list.

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Mr. Hanna continued on slide 13. The risk factors for GeFONSI I and GeFONSI II were on the moderate high end of the scale. Both funds had a short-term investment horizon and principal protection needed to be high. He indicated that GeFONSI I was 85 percent cash equivalents and 15 percent short-term bonds and GeFONSI II was 61 percent cash equivalents, 33 percent short-term bonds, and 6 percent equity. Performance was good for both funds in 2023 with a 5.34 percent return for GeFONSI I and a 6.22 percent return for GeFONSI II. Both accounts performed well in excess of benchmarks.

Ms. Leary continued to slide 14 and detailed the Alaska Higher Education and Investment Fund (AHEIF). The slide

showed the historical balances of AHEIF. The fund was capitalized with a \$400 million balance from receipts of the Alaska Housing Capital Corporation (AHCC) and was used for paying Alaska Performance Scholarship Awards (APSA) and the AlaskAdvantage Education Grants (AEG). She relayed that at least 7 percent could be appropriated for scholarships, two-thirds of which was allocated to the APSA and one-third was allocated to AEG. In FY 22, HB 322 established AHEIF as a separate fund and deemed it as a fund that could not be swept to the CBRF.

Representative Josephson acknowledged that using the word "separate" when referring to AHEIF was "magical." He consulted the appendix and noted that there were large sums in other accounts. He asked how vulnerable the other accounts were to the failure to reverse sweep on June 30, 2023. He wondered if the accounts would all be essentially spent by the operating budget.

Ms. Leary replied that she was unsure which components of the funds were sweepable, but she understood that it was a fairly small number. Some funds were used over time and other funds were replenished at the start of the year and were used for a particular year.

Mr. Hanna continued on slide 15 and explained that AHEIF had a high-risk profile to work to achieve the fund's spending objective, which was capped at 7 percent. The risk profile for the fund was set at the risk equivalent of 70 percent equities and 30 percent bonds. The full asset allocation for 2022 was 39 percent U.S. equities, 29 percent international equities, 5 percents REITs, 30 percent core U.S. fixed income, and 1 percent cash. The performance over the past year was strong at 16.45 percent, which was 55 basis points in excess of the benchmark. The ten-year performance was strong at 6.74 percent through a volatile period.

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Ms. Leary continued on slide 16 and detailed the historical invested assets in PSTF. She shared that the ending value of the fund in 2023 was \$761 billion. The fund was stood up in 1978 and was funded by one half of one percent of state receipts from the management of state lands. The fund was used to provide an offset for the kindergarten through twelfth grade formula funding. For FY 24, the fund

contributed \$32 million to the public education fund and was expected to contribute approximately \$35 million in FY 25.

Mr. Hanna continued on slide 17 and explained that the PSTF had a long time horizon. The fund had the same high risk profile as the higher education fund and its performance over the last year was similar and strong at 16.43 percent, which was 53 points in excess of the benchmark. The ten-year performance of the fund was 6.46 percent.

Representative Coulombe understood that there was a five percent draw from the PSTF which contributed to funding the formula; however, there were boundaries around the use of the fund. She asked if there was any avenue to access the account apart from the five percent draw.

Ms. Leary responded that she was not aware of any other avenue.

Representative Coulombe recalled that AHEIF was capped at 7 percent. She asked if all of the funds from the 7 percent appropriation were being used for the scholarship grants. She asked if the money was only pulled out as it was needed.

Ms. Leary responded that AHEIF had been used for awards and grants and less than 7 percent had been taken out. The rest of the monies still remained in the fund. She indicated that the fund was used in the past for other purposes and was not exclusively for PSTF. She understood that there was a bill that would potentially increase the amount of the scholarships and the grants.

Ms. Leary continued on slide 18 and the Power Cost Equalization (PCE) fund. The slide showed the asset balances through June 30, 2023, which totaled \$946 million. The management duties of the fund were transferred to APFC through the passage of SB 98 and would go into effect on July 1, 2023.

Mr. Hanna continued on slide 19 and noted that PCE was fully liquidated to cash for transfer at the end of the fiscal year [FY 23]. Performance was tracked through June 30, 2023, and the fund performed well with a one-year performance of 9.59 percent. The team made sure that the fund was fully invested for as long as possible, and it

managed to capture the majority of the market rebound that occurred during the first part of the fiscal year. The fund was at 100 percent cash on the last day of the fiscal year.

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Ms. Leary advanced to slide 20 and noted the assets for two of the funds for which ARMB was the fiduciary: Public Employees' Retirement System (PERS) and Teacher's Retirement System (TRS). The funds totaled \$29.8 billion. She explained that the defined benefits plans were closed funds and experienced withdrawals. The board was comprised of nine trustees: two for PERS, two for TRS, two commissioners, two public representatives, and one finance officer. The investment returns were just over 7 percent in 2023 and the 39-year average for PERS and TRS was 8.95 percent, which compared favorably with the current assumed actuarial rate of 7.25 percent.

Representative Stapp understood that the treasury had to liquidate all of the assets of the PCE fund in order to transfer the assets. He asked why the assets could not simply be transferred from the fund without being liquidated.

Mr. Hanna clarified that when assets were sold, new securities needed to be purchased by APFC. He explained that APFC had a different asset allocation than the incoming PCE assets; therefore, many of the assets needed to be sold anyway in order to buy into the pools managed by APFC. There were also many operational and legal complexities in transferring securities between entities. The judgement of the treasury in consultation with APFC was that the operational challenges and potential implications of the challenges outweighed the potential benefits of transferring assets without first liquidating the assets.

Mr. Hanna continued on slide 21 and noted that PERS and TRS made up about 80 percent of assets managed by the treasury. The systems had a more complex asset allocation because the accounts did not have the same liquidity requirements as direct state assets. The current asset allocation was 43 percent public equities, 21 percent fixed income, and 36 percent alternative investments. Returns had been strong and the treasury typically focused on longer-term returns for the retirement systems to increase stability. The ten-

year return had been 7.4 percent, which was 91 basis points over the benchmark return.

Mr. Hanna relayed that the treasury had received a suggestion from one of the state's independent investment advisors to quantify the benefit in dollars because the basis points system was sometimes confusing. The analytics team used ten years of daily cash flow data to calculate how much additional value the excess returns provided in assets. On average, the total excess returns were well over \$2 billion when the retirements systems were roughly valued at \$20 billion. The returns were in the top quartile when compared with other public pension systems. Part of the excess return could be attributed to the low-cost approach employed by the treasury, which led to costs that were roughly 30 percent lower than the systems' median peers and equated to a consistent annual savings of between 30 million and 50 million. Overall, strong returns from ARMB had provided meaningful contributions to retirement assets and reduced the needs for higher state contributions.

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Co-Chair Johnson commented that the returns were impressive. She asked if the treasury's unique strategy was the reason that the retirement systems had higher returns than the Permanent Fund.

Mr. Hanna replied that the returns from the Permanent Fund and from the retirement systems had been fairly similar over the long term. The retirement systems had differing asset allocations from the Permanent Fund and a different purpose. The retirement systems were mature and were becoming more mature over time and the liquidity requirements would increase as time went on while the ability to hold alternative investment would decrease over time. Returns would differ on an annual basis and in some years, the retirement systems had higher returns while in other years the Permanent Fund had higher returns. He thought that all of the funds were well-managed investments for the state.

Representative Stapp commented that Alaska State Senate was debating a bill regarding retirement systems that assumed a rate of return that was above the five-year average of the existing retirement funds. The board revised the rate of return down from 7.38 percent to 7.25 percent. He was

concerned that the rate of return from the board itself would be revised down again and cause problems with the benefits system. He asked if the treasury had seen anything that would suggest that the projected rates of return would be revised down in the near future.

Mr. Hanna replied that ARMB went through a process every four years that involved setting accrual assumptions inclusive of the rates of return. In 2022, the long-standing expected return of 7.3 percent had been revised downward to 7.25 percent. The numbers tended to be influenced by a backward look at performance and there had been a long period of extremely low rates that cumulated in zero interest rates in 2021. Rates influenced the expected returns and performance for a long period of time, which had culminated in most public pensions reducing the rates of return, including ARMB. A few years prior, the interest rates were at 0 percent but in the present day, interest rates were over 5 percent, which provided a significant uplift for most portfolios. The retirement systems' portfolio had a 21 percent exposed fixed income and the expected returns were now in excess of 5 percent. The expected returns influenced other asset classes.

Mr. Hanna remarked that he had seen the capital market assumptions released by Callan in the prior week and the treasury utilized the assumptions for ARMB as well as other longer-term state assets. The treasury assumed that ARMB and other 70/30 endowments like PSTF would experience an increase of 25 basis points to 40 basis points over a ten-year investment horizon. The next time ARMB set actuarial assumptions, it would review capital market assumptions and all of the economic information and set the best expectation possible. A decrease in expected returns was no longer expected and it was more likely that the returns would "bottom out" or potentially experience an uplift.

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Representative Galvin asked for a description of the treasury's low cost methods.

Mr. Hanna responded there were dedicated direct investment teams within the treasury. His team had a group that had managed direct fixed-income investments for the state for decades and managed long-standing direct investments of cash portfolios and fixed income. There was a dedicated

equity group that managed direct investments on the equity side that focused mainly on retirement systems, which was a source of savings. The treasury was able to manage investments and assets which made the process better and cheaper than outsourcing the tasks. The treasury had moved away from "active" management on the equity side towards more index oriented management which was much less costly. Returns were not always higher, but the returns in the recent years had been higher.

Representative Tomaszewski understood that there was \$29.8 billion in PERS and TRS. He directed attention to slide 5 which indicated that there was \$41.5 billion in assets in ARMB. He asked where the discrepancy was.

Mr. Hanna responded that there were fourteen retirement systems and he was only discussing four of the systems. The defined contributions systems were close to \$10 billion in assets, which made up most of the discrepancy. The other \$1.1 billion was a collection of other retirement and defined benefit systems or defined benefit components of the defined contribution plans.

Representative Tomaszewski asked if there was a slide on the topic.

Mr. Hanna responded that he would be happy to follow up with the information.

Representative Josephson asked for clarification that the \$10 billion in defined contributions was the employer share of assets. He asked if the employee contributions were segregated from the total.

Mr. Hanna responded in the affirmative. As of December 31, 2023, participant directed investments totaled \$9.4 billion. The figure represented the asset value in participant directed accounts in total and included both the employee and employer contributions that occurred through the end of the calendar year.

Representative Stapp asked if the consumer-directed accounts were performing better than other types of accounts.

Mr. Hanna replied that he did not have the information. The default option for participant-directed assets were age-

appropriate target-date funds and the funds had a strong performance overall.

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Ms. Leary continued on slide 22 and indicated that the next portion of the presentation would focus on state cash flows. She advanced to slide 23 which was a depiction of the general fund and the cash inflows and cash outflows of the fund. Examples of cash inflows included tax revenue, the earnings reserve funds, federal dollars, and agency receipts. Examples of cash outflows included school education payments, Medicaid payments, payroll and pension payments, and debt service payments. All of the money coming in and out of the state went through the general fund.

Ms. Leary continued to slide 24 to discuss the cash inflows and outflows in greater detail. One of the biggest components of cash inflows was commodity or petroleum revenues, which were projected to be 37 percent for FY 24. There was some uncertainty surrounding petroleum revenue due to volatility and production. There would always be uncertainty because oil was based on in-year forecasted revenues. The other large component of cash inflows was investment revenues, which accounted for about 56 percent of general funds in FY 24. There was certainty surrounding incoming investment revenues in the present year and in the following year due to a lagging percent of market value (POMV) from APFC. The certainty allowed for more consistency in knowing which funds were coming into the general fund to make payments.

Ms. Leary moved to slide 25 and discussed the impact of expenditures. There was often a need for cash outflows before there were sufficient cash inflows, such as for federal programs like Medicaid that required that the state spend money before it could be reimbursed. There were also appropriations at the beginning of each year which needed to be allocated to various funds in order to be utilized by various agencies. The appropriations would not match incoming revenue at the beginning of the year. There were also seasonal cash flow needs that impacted the amount of money that was needed to flow out of the general fund each year; for example, summer was the peak season for construction projects and seasonal workers.

Co-Chair Johnson noted that a concern she had heard from state contractors was that the contractors were "carrying the state at a level they had never carried the state before." Many contractors were not getting invoices paid on time. One contractor in particular told her that they were owed \$18 million. She did not think it was an isolated incident and it seemed to be a pattern. She asked if Ms. Leary had any thoughts as to what was causing the situation.

Ms. Leary responded that the treasury's cash management group oversaw net cash inflows and outflows. The group could see which agency the cash was flowing through but not necessarily the details of which bills were being paid. The only situation in which the treasury would get involved was if agencies were not requesting federal funds in a timely manner. She did not have a detailed response and thought it was an agency issue.

Co-Chair Johnson wanted to clarify that the problem was not systemic across all state payments, but it seemed to her that it was systemic. She wanted to make sure payments were being made and would continue to look into the issue.

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Representative Josephson commented that for the second year in a row, the Foraker Group had expressed frustration that non-profits were not receiving payments from grants. He understood that non-profit groups could legally charge interest and penalty to the state if the groups were not paid on time. He assumed the treasury was not the correct agency to consult about the issue.

Ms. Leary responded that the treasury was purely "agnostic" in terms of cash inflows and outflows. The role of the treasury was to ensure that the money was flowing to the correct destination. The treasury was not independently able to stop payments unless it was informed that payments going out needed to be halted. There was often a lack of direction or description on where general fund inflows belonged, in which case the cash inflows would be put into a suspense account until the treasury could determine where the money belonged.

Representative Coulombe asked for more information on the Federal Emergency Management Agency (FEMA) payment process, particularly in relation to wildfire mitigation.

Ms. Leary responded that the money that came in from FEMA was put into a fund with a direct purpose and would be under the purview of the agency overseeing the FEMA amounts. She was not overly familiar with the process.

Representative Coulombe understood that DOR would spend the money, then the FEMA money would be set aside for a direct purpose and the funds would return to the department.

Ms. Leary responded in the affirmative.

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Ms. Leary continued on slide 26 and detailed cash flow deficiencies, which referred to situations in which there were expenditures that were greater than the sum of the incoming revenue. The general fund was used in the past for a wider variety of reasons, while there were more specified funds in the present day that captured funds like the ones detailed in the appendix of the presentation. The general fund was somewhat constricted by the amount of money contained in the fund for the purpose of paying the state's bills. There would be cash flow deficiencies throughout the year which were managed by adjusting the timing of the ERA transfer to the general fund and managing timing of expenditures. About ten years prior, all of the money went into the education funds for payment all at once, but the money was not being used immediately. The treasury worked out a payment structure to implement more consistency by transferring money into the education fund on a quarterly basis. She relayed that the treasury would employ the same strategy with other expenditures.

Ms. Leary advanced to slide 27 and explained that revenue shortfalls were different than cash flow timing deficiencies. Revenue shortfalls occurred when revenue was insufficient to cover general fund appropriations in any given fiscal year. There was language in the operating budget that appropriated budget reserve funds for revenue shortfalls. The treasury had relied on the appropriation to authorize use of budget reserve funds to address both revenue shortfalls and cash flow timing mismatches. The CBRF had been used to cover revenue shortfalls

historically. She clarified that revenue shortfalls did not necessarily occur every year.

Representative Galvin understood that there had been issues paying contractors in a timely manner. She asked if the funds were available for the check writers. She wondered if the problem was that the funds had not been transferred early enough for the check writers to have access to the funds when writing the checks.

Ms. Leary responded that one of the main functions of the cash management groups was to ensure that there was enough money to pay the state's bills on time. The treasury had a \$400 million minimum cash threshold for the general fund and it acted as a safeguard to ensure that the state could pay its bills even if the bills were all due at once, which was unlikely. The treasury maintained the threshold and any time there was a risk of the total decreasing below the threshold, it would utilize funds from an available source to compensate for the lower total. There was \$3.5 billion scheduled in ERA transfers in the current year, and from January 1, 2024, through the present day, the treasury had called about \$2.1 billion of the ERA transfers. The treasury worked with APFC to change the schedule when it was necessary. The schedule was set at the beginning of the year and it was based on forecasted incoming revenue. Specific expenses were also a known value and the treasury aimed to monitor the expenses at all times. The treasury intended to always have enough money to pay the bills.

Representative Galvin commented that important transactions should always continue. She hoped that the state could get to the bottom of the problem.

[2:50:03 PM](#)

Ms. Leary advanced to slide 28, which was a discussion on the cash deficiency memorandum of understanding developed in 1994 between DOR, DOA, the Office of Management and Budget (OMB), and the Department of Law (DOL). The minimum cash threshold had changed over the years to become the current \$400 million threshold. The memorandum outlined procedures on how to address cash flow timing mismatches. The procedures included developing monthly cash projections, monitoring daily general fund cash balances, executing appropriated transfers, and performing temporary fund borrowing to be repaid by the fiscal year end. In the

event of a forecasted revenue shortfall, the treasury would seek legislative action through the governor's office to access additional funds through appropriation from other reserve funds. If all strategies failed, the treasury would begin to prioritize disbursements.

Representative Tomaszewski asked about the details of borrowing money and whether it would involve inter-fund borrowing or if there was a line of credit.

Ms. Leary replied that the treasury did not have a line of credit. She explained that there was a past legislative bill that allowed borrowing to be an alternative to accessing any funds. The treasury was presently limited to the ERA and CBRF and borrowing from the sweepable sub funds. She emphasized that the treasury had never restricted cash payments out the door.

Representative Hannan asked if there was an update on the management of cash from cannabis sales. She acknowledged that the question was slightly off-topic.

Co-Chair Johnson suggested that Ms. Leary finish the presentation prior to answering Representative Hannan's question.

Ms. Leary summarized slide 29 and indicated that cash flow forecasting changed due to the amount and timing of revenues and expenditures. Even with balanced budgets, cash flow timing mismatches would still occur. She explained that revenue shortfalls could occur if the forecasted assumptions were wrong. She concluded her presentation.

Representative Hannan restated her question about cannabis cash management. She knew there were some issues regarding the cash used to pay taxes on cannabis. She understood that there was a plan to address the problem and she was looking for an update.

Ms. Leary responded that she did not have an update. There was a plan to deposit cash into a safe, but she did not know the status of the plan. She relayed that the issue was mainly under the purview of the Tax Division although the treasury would receive the money.

Representative Hannan asked for clarification that Ms. Leary's understanding was that there was still only one

depository with an inflow of cash and all of the taxes across the state had to transfer the cash to Anchorage.

Ms. Leary responded in the affirmative.

[2:55:17 PM](#)

Representative Stapp asked about the GeFONSI Permanent Fund Dividend (PFD) Trust account listed in the appendix of the presentation. He asked for confirmation that the account contained the "hold harmless" funds.

Ms. Leary responded that the fund contained the money that was transferred to APFC to pay dividends. She clarified that the account held the funds that were used to pay out the PFD checks.

Representative Stapp noted that there was a budgetary provision that took PFD revenue and paid the hold harmless funds to the Social Security Administration. When the money was allocated for the dividend, the actual spending for the program was around \$6 million below what was appropriated in the budget. He asked what happened to the excess funds.

Ms. Leary responded that the money remained in the account and was used in the calculations going forward for the following year.

[2:56:53 PM](#)

Co-Chair Johnson reviewed the agenda for the following day's meeting.

#

ADJOURNMENT

[2:57:25 PM](#)

The meeting was adjourned at 2:57 p.m.