

SCOMM

#18:25



530 Start

Gardner chairman

Tifton meeting, Terge sitting in.

Discussion of amendments - 4 pages

540 Cotton wires and ind. 2.

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1150 520 and adopted after discussion to

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Coffee meeting?

clean copy for Monday. - 1:00.

& conference will look over committee
report & have suggestions.

1329 end of mtg.

3/30 PF FCC

1330 start

run thru final draft.

1435 Ray objects to \$400 figure. motion to change to \$250. 3-3 fails (Ray, Haugen, Tillier)

1485 technical error p. 10 line 24. 25 should read 15. Ray moves Q5.

1585 Jim Rhode explains reason for 15. 3-3 motion fails.

1725 p. 13

p. 14 transition & eff. date

committee report - TG asks for comments

1780 Sackett moves adoption of bill 5-1 (Ray)

1820 adjourn

SENATE AND HOUSE JOINT
JOURNAL SUPPLEMENT

4/2/80

Wednesday

No. 7

Alaska State Legislature

FCCS
SB
161

FREE CONFERENCE COMMITTEE REPORT

FCCS FOR SB 161

In making their decision on the Alaska Permanent Fund, the Free Conference Committee has focused on a single question --- the management of the Fund's principal.

It is to be an inviolate trust which, in the words of this bill, conserves "...a portion of the state's revenues from mineral resources to benefit all generations of Alaskans..." (page 4).

It is to be an independent trust, yet made accountable in various ways to "...maintain safety of principal while maximizing total return..." (page 4).

The contribution rate has been set at 50% of mineral lease bonuses (except from the Beaufort Sea, which has been left at 25%) and 50% of mineral lease royalties and net profits from the Beaufort Sea and other future sales. The rate for Prudhoe Bay remains at 25% plus any other money appropriated annually by the Legislature.

Three major concerns --- safety of principal, accountability, and legislative oversight --- are addressed by the legislation.

Safety of Principal

The Free Conference Committee Permanent Fund bill provides a framework for fiscally conservative and responsible management of the Fund's principal. It assures and emphasizes the safety of the assets while providing the responsible managers with sufficient investment latitude to achieve superior results. Under the terms of this bill, the Alaska Permanent Fund would consist of a wide variety of quality, high-grade investments.

The Fund is designed to be a trust which focuses on the safety of principal first and the maximization of earnings second (page 4). It is a trust held to a more restricted list of investments than most other fiduciary trusts including the Alaska State Pension Funds and it confirms in law the

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161

current state practice of evaluating performance according to nationally recognized and accepted standards. The investment managers are required to maintain investment diversification and are allowed to determine the investment mix of short, intermediate, and long-term investments. The flexibility allowed enables the managers to achieve a sound rate of return on investments.

The bill provides the investment managers with the authority to place funds in direct obligations of the United States Treasury, federal agency securities, certificates of deposit, high-grade corporate bonds, quality short-term investments, and federally guaranteed loans (pages 8-9). The fund is directed to give preference to Alaska investments as long as they meet the standards of quality set out in the bill. Specifically, deposits can be made in Alaska banks, mutual savings banks, savings and loan associations, and credit unions. Residential real estate (owner-occupied single family dwellings, duplexes, and condominiums) may also be purchased if the mortgage is privately insured by a company doing business in Alaska (page 9). The order in which the investments are listed is not meant to express a priority for one type of investment over another.

Importantly, the bill has a minimum of investment restrictions yet provides a very definite and certain framework. It does not authorize investments in stock or bullion, restricts the purchase of corporate bonds to 25% of the Fund's total investments, and limits the purchase of loans and mortgages to 25% of the total. Purchases of residential mortgages may be a further 15% of total assets. The bill allows the Fund to use the futures market to protect investments from the severe declines in value that are being suffered today. These futures contracts, however, may be used only to hedge and not to speculate. The bill also prohibits the Fund from either borrowing or guaranteeing the obligations of others (page 8).

The bill also provides for the handling of gains and losses and income (page 11). Any losses not offset by gains on the sale of securities shall be deducted from income and added to the Fund principal; this protects the Fund principal from erosion. Losses from sales of securities are spread over a period of time equal to the remaining life; this encourages the managers to get rid of bad investments. Capital gains are added to the Fund principal, helping to offset the effects of inflation. The Fund income is defined as the interest received on the investments, and the amount of income available for disbursement will be determined on an averaging basis; this insures a relatively steady income flow.

Accountability

It was the aim of the Committee to establish a management system for the Alaska Permanent Fund which would be protected from political influences but, at the same time, responsive to changes in state policy and accountable to the people through their elected officials. In short, the aim was insulation without isolation. It was agreed that the best way of achieving these ends was not to place the management within the Department of Revenue, but to create a public corporation distinct from state government. Although the Department of Revenue currently manages the pension funds as well as the general fund, it was agreed that the Permanent Fund, with its fundamentally different goals and large size, should not be in the hands of the same people whose primary duty is managing money for day-to-day use by the state. The Corporation is placed within the Department of Revenue for administrative matters such as payroll, but has a legal existence independent of and separate from the state.

The proposed Permanent Fund Corporation, therefore, has its own board of trustees which is made accountable in several ways (page 5). The six members of the board will be appointed by the Governor and consist of the Commissioner of Revenue, two other commissioners, and three public members. They will be confirmed by the Legislature, except for the Commissioner of Revenue who serves by right of his office; the other commissioners are to submit to a separate confirmation for their duties as trustees. Terms are three years; staggered, and members may be reappointed subject to confirmation. Members may be removed from the board by the Governor and the Legislature may override this decision in a Joint Session. The public members of the board may not hold any other state or federal office or employment and must have recognized competence and wide experience in finance, investments, or other business management-related fields. They are subject to the conflict of interest law and must disclose any interest in entities in which corporate assets are invested. They will be paid honorariums competitive with the largest private corporations in the state. It is intended that every two years the Governor shall make recommendations on adjusting the level of the honorarium. The board will employ an executive director who is also subject to the conflict of interest law and responsible for hiring additional staff with the board's approval.

The corporation's operating budget is from the general fund and is subject to the Executive Budget Act (page 10). This provision offers another check on the management and will prevent such things as the hiring of excessive numbers of employees or uncontrolled expense accounts.

Among the board's responsibilities is the publishing of a yearly report (page 11) including a financial statement reviewed by independent auditors, a statement of earnings from each investment, a market-value appraisal of the investments, and a performance evaluation with recommendations for needed changes. These reports, which must be written in easily understandable language, will be available to the Governor, the Legislature, and the public. The income statement and balance sheet will be published yearly in newspapers and every two years in the election pamphlet.

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The bill thus insures that the board of trustees of the Alaska Permanent Fund Corporation will be the best investment managers available in the state, will be accountable to both the executive and legislative branches through appointment and budget processes and oversight by the Legislative Budget and Audit Committee, and will keep the public informed about the Fund's investment performance.

Legislative Oversight

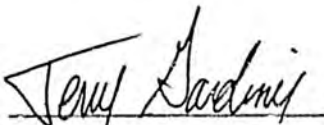
The Free Conference Committee found a need for coordinated, continuing oversight of all the state's investment efforts. Accordingly, the review will extend beyond the Alaska Permanent Fund to include the Alaska Renewable Resources Fund, loan programs, the several authorities, and the general fund. As well as building up a body of legislators with detailed knowledge of investments, this new approach will give the Legislature and the broad public better information on the policies and efficiency of the various investment agencies, on the extent to which these agencies conform to statutory intent, and on the extent to which the economic and social goals of the various programs are being achieved.

The House Finance Committee had considered providing in the Permanent Fund bill for a new interim committee to handle this oversight function but decided, in the interest of efficiency, to simply expand the powers and duties of the present Legislative Budget and Audit Committee (pages 1-3). As proposed, the Legislative Budget and Audit Committee will review the plans and reports of all state agencies involved in lending or investing, report to the Legislature its findings and recommendations, and provide for audits and performance evaluations of the Alaska Permanent Fund Corporation's investment program.

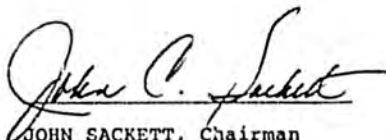
It is the Committee's intent, however, that these new duties be assigned to the Legislative Budget and Audit Committee on a trial basis and that the committee report back to the Legislature within two years, recommending how best the oversight duty could be carried out and including consideration of the option of delegating the responsibilities to a separate committee.

The Future

As stated earlier, this bill addresses only the question of Fund management and leaves the separate question of how to use the Fund earnings to separate legislation. It merely assures that there will be income and does not preclude any options for its use. Unless another determination is made, the Permanent Fund earnings will be deposited in the general fund. No matter what use(s) are decided for the income, the very establishment of a secure trust will be a sign to the national financial community that Alaska is following a responsible fiscal policy.



TERRY GARDINER, Chairman
Conference Committee



JOHN SACKETT, Chairman
Conference Committee

Original sponsors: Kelly, Hohman,
Colletta and Sackett

1 IN THE SENATE

BY THE FREE CONFERENCE COMMITTEE

2 FREE CONFERENCE CS FOR SENATE BILL NO. 161

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 ELEVENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act relating to the Alaska permanent fund; to
7 nonrenewable resource revenues; to legislative over-
8 sight; and providing for an effective date."

9 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. FINDINGS. The legislature finds that there is a substantial
11 need for oversight of the performance of those agencies of the state which
12 perform lending or investment functions since those functions do not receive
13 the detailed review to which other expenditures of public money are subject,
14 and therefore the knowledge necessary for sound legislation in this area is
15 not readily available. There is a need for legislative oversight which will
16 provide information on the policy and performance of these agencies, the
17 extent to which the agencies conform to statutory intent, and the impact of
18 their performance on the economy and the state treasury.

19 * Sec. 2. AS 24.20 is amended by adding new sections to read:

20 Sec. 24.20.156. PURPOSES. The purposes of the Legislative Budget
21 and Audit Committee include

22 (1) monitoring and reporting

23 (A) the performance of the agencies of the state which
24 perform lending or investment functions,

25 (B) the extent to which the performance of these agen-
26 cies has contributed to the fiscal, financial, economic and social
27 improvement of the state and its citizens,

28 (C) the extent to which these agencies and the executive
29 have prepared and coordinated short and long term economic, fiscal,

1 investment and financial planning;

2 (2) holding these agencies accountable to statutory intent in
3 their performance by recommending, where appropriate, changes in policy
4 to the agencies or changes in legislation to the legislature;

5 (3) annually reviewing the extent of capitalization of the
6 investment funds of the state and alternative investment policy for the
7 general fund surplus and recommending needed legislation.

8 Sec 24.20.206. DUTIES. The Legislative Budget and Audit Commit-
9 tee shall

10 (1) report to the legislature its recommendations relating to
11 the confirmation of appointees to the Board of Trustees of the Alaska
12 Permanent Fund Corporation and the Board of Trustees of the Alaska
13 Renewable Resources Corporation;

14 (2) annually review the long-range operating plans of all
15 agencies of the state which perform lending or investment functions;

16 (3) review periodic reports from all agencies of the state
17 which perform lending or investment functions;

18 (4) present a complete report of investment programs, plans,
19 performance, and policies of all agencies of the state which perform
20 lending or investment functions to the legislature within 30 days after
21 the convening of each regular session;

22 (5) present to the legislature within 30 days after the con-
23 vening of each regular session a review of the report of the governor
24 under AS 37.07.020(d) with recommendations for needed legislation;

25 (6) in conjunction with the finance committee of each house
26 recommend annually to the legislature the investment policy for the
27 general fund surplus and for the income from the permanent fund;

28 (7) provide for an annual post audit and annual operational
29 and performance evaluation of the Alaska Permanent Fund Corporation in-

1 vestments and investment programs.

2 Sec. 24.20.209. RECORDS. The Legislative Budget and Audit Commit-
3 tee shall keep a complete file of all reports presented to it and all
4 reports presented by it to the legislature or to a legislative commit-
5 tee.

6 * Sec. 3. AS 24.20.201(a) is amended by adding new paragraphs to read:

7 (9) hold public hearings on the confirmation of the members
8 of the Board of Trustees of the Alaska Permanent Fund Corporation, and
9 the members of the Board of Trustees of the Alaska Renewable Resources
10 Corporation;

11 (10) make recommendations to the legislature and to agencies
12 of the state which perform lending or investment functions concerning
13 the structure and operating practices of the agencies;

14 (11) enter into and enforce all contracts necessary or desira-
15 ble for the functions of the committee.

16 * Sec. 4. AS 37.07.020 is amended by adding a new subsection to read:

17 (d) The governor shall annually, before the convening of the
18 legislature, report to the legislature through the Legislative Budget
19 and Audit Committee the long-range fiscal and economic consequences of

20 (1) alternate levels of capitalization of the investment
21 funds of the state; and

22 (2) alternative investment policy for the general fund sur-
23 plus.

24 * Sec. 5. AS 37 is amended by adding a new chapter to read:

25 CHAPTER 13. ALASKA PERMANENT FUND.

26 Sec. 37.13.010. ALASKA PERMANENT FUND. (a) Under art IX, sec. 15
27 of the state constitution, there is established as a separate fund the
28 Alaska permanent fund. The Alaska permanent fund consists of

29 (1) 25 percent of all mineral lease rentals, royalties,

1 royalty sale proceeds, net profit shares under AS 38.05.180(f) and (g)
2 and federal mineral revenue sharing payments received by the state from
3 mineral leases issued on or before December 1, 1979, and 25 percent of
4 all bonuses received by the state from mineral leases issued on or
5 before February 15, 1980;

6 (2) 50 percent of all mineral lease rentals, royalties,
7 royalty sale proceeds, net profit shares under AS 38.05.180(f) and (g)
8 and federal mineral revenue sharing payments received by the state from
9 mineral leases issued after December 1, 1979, and 50 percent of all
10 bonuses received by the state from mineral leases issued after
11 February 15, 1980;

12 (3) any other money appropriated to or otherwise allocated by
13 law to the Alaska permanent fund.

14 (b) Payments due the Alaska permanent fund under (a) of this
15 section shall be made to the fund once each month.

16 (c) The Alaska permanent fund shall be managed by the Alaska
17 Permanent Fund Corporation established in this chapter.

18 Sec. 37.13.020. FINDINGS. The people of the state, by constitu-
19 tional amendment, have required the placement of at least 25 percent of
20 all mineral lease rentals, royalties, royalty sale proceeds, and federal
21 mineral revenue sharing payments and bonuses received by the state into
22 a permanent fund. The legislature finds with respect to the Alaska
23 Permanent Fund Corporation that

24 (1) the corporation should provide a means of conserving a
25 portion of the state's revenues from mineral resources to benefit all
26 generations of Alaskans;

27 (2) the corporation's goal should be to maintain safety of
28 principal while maximizing total return;

29 (3) the corporation should be used as a savings device

1 managed to allow the maximum use of disposable income from the corpora-
2 tion for purposes designated by law.

3 Sec. 37.13.030. PURPOSE. It is the purpose of this chapter to
4 provide a mechanism for the management and investment of those permanent
5 fund assets allocated to the Alaska Permanent Fund Corporation in a
6 manner consistent with the findings in AS 37.13.020.

7 Sec. 37.13.040. ALASKA PERMANENT FUND CORPORATION. There is
8 established the Alaska Permanent Fund Corporation. The corporation is a
9 public corporation and government instrumentality in the Department of
10 Revenue managed by a board of trustees. The purpose of the board is to
11 manage and invest the assets of the corporation in accordance with this
12 chapter.

13 Sec. 37.13.050. COMPOSITION AND QUALIFICATIONS OF BOARD OF TRUS-
14 TEES. (a) The Board of Trustees of the Alaska Permanent Fund Corpora-
15 tion consists of six members appointed by the governor. Three of the
16 members shall be heads of principal departments of state government; one
17 of whom shall be the commissioner of revenue. Three members shall be
18 appointed by the governor from the public and may not hold any other
19 state or federal office, position or employment, either elective or
20 appointive, except as a member of the armed forces of either the United
21 States or of this state. Members other than the commissioner of revenue
22 shall be separately confirmed by a majority of the members of the legis-
23 lature in joint session.

24 (b) The three public members of the board shall have recognized
25 competence and wide experience in finance, investments, or other busi-
26 ness management-related fields.

27 (c) The board shall annually elect a chairman from among its
28 members.

29 Sec. 37.13.060. TERM OF OFFICE. The members of the board shall be

1 appointed for terms of three years, and they may be reappointed subject
2 to confirmation by a majority of the members of the legislature in joint
3 session. Terms shall be staggered. Initial terms for members other
4 than the commissioner of revenue shall be two members serving for one
5 year, two members serving for two years, and one member serving for
6 three years.

7 Sec. 37.13.070. REMOVAL AND VACANCIES. (a) The governor may
8 remove a member of the board from office. However, the removal of a
9 member of the board is subject to disapproval by a vote of a majority of
10 the members of the legislature at the first joint session held 10 or
11 more days after the legislature receives notice of the removal from the
12 governor. A removal by the governor shall be in writing and shall state
13 the reason for the removal. A member who is removed by the governor may
14 not participate in board business and may not be counted for purposes of
15 establishing a quorum between the time he receives written notice of his
16 removal from the governor and the time that the legislature's power to
17 disapprove the removal under this subsection expires. If the legisla-
18 ture disapproves the removal of a board member, the board member shall
19 be reinstated.

20 (b) A vacancy on the board shall be promptly filled by appointment
21 by the governor and confirmation by a majority of the members of the
22 legislature in joint session. An appointee to a vacancy shall hold
23 office for the balance of the term for which his predecessor on the
24 board was appointed. If a vacancy arises on the board while the legis-
25 lature is not in session, the governor may appoint an interim board
26 member who shall exercise the powers of a board member until the legis-
27 lature fails to confirm the appointment of the interim board member.

28 (c) A vacancy on the board does not impair the authority of a
29 quorum of the board to exercise all the powers and perform all the

1 duties of the board.

2 Sec. 37.13.080. QUORUM. Four members of the board constitute a
3 quorum for the transaction of business and the exercise of the powers
4 and duties of the board.

5 Sec. 37.13.090. COMPENSATION OF BOARD MEMBERS. Public members of
6 the board receive an honorarium of \$400 for each meeting day if they
7 attend the meeting. All members of the board are entitled to per diem
8 and travel allowances as provided by law for members of state boards and
9 commissions.

10 Sec. 37.13.100. CORPORATION STAFF. The board may employ and
11 determine the salary of an executive director. The executive director
12 may, with the approval of the board, select and employ additional staff
13 as necessary. No employee of the corporation, including the executive
14 director, may be a member of the board. The executive director and the
15 other employees of the board are in the exempt service under AS 39.25.

16 Sec. 37.13.110. CONFLICTS OF INTEREST. (a) Members of the board
17 and the executive director are subject to the provisions of AS 39.50.

18 (b) If a member of the board or an employee of the corporation
19 acquires, owns or controls an interest, direct or indirect, in an entity
20 or project in which corporation assets are invested, he shall im-
21 mediately disclose the interest to the board. The disclosure is a
22 matter of public record and shall be included in the minutes of the
23 board meeting next following the disclosure.

24 Sec. 37.13.120. INVESTMENT RESPONSIBILITIES OF THE BOARD. (a)
25 The prudent-man rule shall be applied by the board in the management and
26 investment of Alaska permanent fund assets. The prudent-man rule as
27 applied to investments of the corporation means that in making invest-
28 ments the board shall exercise the judgment and care under the circum-
29 stances then prevailing which an institutional investor of ordinary

1 prudence, discretion, and intelligence exercises in the management of
2 large investments entrusted to it not in regard to speculation but in
3 regard to the permanent disposition of funds, considering probable
4 safety of capital as well as probable income.

5 (b) The corporation assets shall only be used for income-producing
6 investments.

7 (c) The board shall maintain a reasonable diversification among
8 investments unless under the circumstances it is clearly prudent not to
9 do so.

10 (d) The board shall submit long-range and quarterly investment
11 reports to the Legislative Budget and Audit Committee.

12 (e) The corporation may not borrow funds or guarantee from princi-
13 pal of the Alaska permanent fund the obligations of others.

14 (f) The board may enter into and enforce all contracts necessary,
15 convenient or desirable for purposes of the corporation.

16 (g) Subject to the limitations in (h) and (i) of this section, the
17 board may invest corporation assets in

18 (1) obligations of, or obligations insured by or guaranteed
19 by, the United States or agencies or instrumentalities of the United
20 States;

21 (2) obligations secured by reserves paid in by the United
22 States or agencies or instrumentalities of the United States or obliga-
23 tions of corporations in which the United States is a shareholder or
24 member;

25 (3) certificates of deposit issued by United States domestic
26 banks which are members of the Federal Deposit Insurance Corporation for
27 which a generally recognized secondary market exists or which are fully
28 secured at all times as to payment of principal and interest by invest-
29 ments described in (1) - (2), (8) or (12) - (16) of this subsection; the

1 security pledged under this paragraph shall be at least equal to the
2 face value of the deposit and the board may require substitution of
3 collateral;

4 (4) shares of federally chartered savings and loans associa-
5 tions in Alaska which are fully secured at all times as to payments of
6 principal and interest by investments described in (1) - (2) of this
7 subsection;

8 (5) savings certificates issued by state chartered savings
9 and loan associations in Alaska which are fully secured at all times as
10 to payments of principal and interest by investments described in (1) -
11 (2) of this subsection;

12 (6) deposits with mutual savings banks in Alaska which are
13 fully secured at all times as to payments of principal and interest by
14 investments described in (1) - (2) of this subsection;

15 (7) fixed-term certificates of indebtedness of federally
16 insured credit unions which are fully secured at all times as to payments
17 of principal and interest by investments described in (1) - (2) of this
18 subsection;

19 (8) corporate debt securities which are rated AA or better by
20 a nationally recognized rating service;

21 (9) short-term corporate promissory notes of the highest
22 ratings assigned by a nationally recognized rating service;

23 (10) bankers' acceptances drawn on and accepted by United
24 States banks each of which have a combined capital and surplus aggregat-
25 ing at least \$200,000,000;

26 (11) repurchase agreements, the securities underlying the
27 agreements being any of the items in (1) - (3) and (8) - (10) of this
28 subsection;

29 (12) the guaranteed portion of Federal Small Business Adminis-

1 tration loans;

2 (13) the portion of first lien real estate mortgages guaran-
3 teed by the Federal Veterans Association;

4 (14) the portions of business and industrial loans made under
5 the Rural Development Act of 1972 which are guaranteed by the Farmer's
6 Home Administration;

7 (15) the guaranteed portion of Farmer's Home Administration
8 loans;

9 (16) notes secured by mortgages of residential real estate if
10 the mortgages are insured by a private mortgage insurance corporation
11 which is authorized to do business in Alaska and has combined capital,
12 surplus and reserves aggregating at least \$20,000,000; the minimum
13 coverage shall be 10 percent for loans having a loan-to-value ratio of
14 less than 90 percent, and the minimum coverage shall be 20 percent for
15 loans having a loan-to-value ratio of 90 percent or more.

16 (h) The board may enter into futuro contracts for the sale of
17 investments purchased under (g) of this section only for the purpose of
18 hedging an existing equivalent ownership position in these securities.

19 (i) Investments under (g)(8) of this section may not exceed 25
20 percent of the total investments of the Alaska permanent fund. Invest-
21 ments under (g)(16) of this section may not exceed in the aggregate ¹⁵~~25~~
22 percent of the total investments of the Alaska permanent fund.

23 (j) The assets of the Alaska permanent fund may not be used for
24 the purchase of bonds of a corporation, upon which any regular interest
25 payment has been defaulted within five years before purchase, except
26 bonds never in default but which have been outstanding for less than
27 five years.

28 (k) The board shall establish and from time to time as necessary
29 modify guidelines for the investment of the assets of the corporation.

1 Before adoption of any guidelines the guidelines shall be reported to
2 the Legislative Budget and Audit Committee for review and comment.

3 (1) The board shall invest the assets of the corporation in in-
4 state investments to the extent in-state investments are available if
5 the in-state investments

6 (1) have a risk level and expected yield comparable to alter-
7 nate investment opportunities; and

8 (2) are included in the list of permissible investments in
9 (g) of this section.

10 Sec. 37.13.130. GAINS AND LOSSES. At the end of each fiscal year,
11 the total amount of losses on the sales of securities, not offset by
12 gains on the sales of securities during that year, shall be computed,
13 with a portion of these losses to be deducted each fiscal year from the
14 income and the resulting amount of income added to the principal of the
15 Alaska permanent fund. Losses taken on the sales of securities shall be
16 accumulated over a period equal to the average remaining life of the
17 securities sold, unless these losses are offset by gains on future sales
18 of securities. In any fiscal year in which the gains on the sales of
19 securities exceed the losses on the sales of securities, the excess
20 shall be added to the principal of the Alaska permanent fund.

21 Sec. 37.13.140. INCOME. The interest received in a year is the
22 income of the corporation for that year. The income available for
23 disbursement shall be determined on an averaging basis. For the first
24 five years, income will be the simple averaging of the annual current
25 return at cost. Subsequently, there will be a moving average current
26 return, in which the latest fiscal year will replace the oldest year.
27 The income available for disbursement will be the lesser of the latest
28 fiscal year's income, or the average annual current income for the past
29 five fiscal years of the Alaska permanent fund at cost, and after

1 adjustment for capital losses charged to that fiscal year.

2 Sec. 37.13.150. BOARD BUDGET. The operating budget of the board
3 is from the general fund and is subject to the Executive Budget Act
4 (AS 37.07).

5 Sec. 37.13.160. AUDITS. The Legislative Budget and Audit Commit-
6 tee shall provide for an annual post audit and annual operational and
7 performance evaluations of the corporation's investments and investment
8 programs.

9 Sec. 37.13.170. REPORTS AND PUBLICATIONS. By September 30 of each
10 year, the board shall publish a report of the corporation for distribu-
11 tion to the governor, legislature, and the public. The report shall be
12 written in easily understandable language. The report must include
13 financial statements audited by independent outside auditors, a state-
14 ment of the amount of money received by the Alaska permanent fund from
15 each investment during the period covered, a statement of investments of
16 the corporation including an appraisal at market value, a description of
17 corporation investment activity during the period covered by the report,
18 a comparison of the corporation performance with the intended goals
19 contained in AS 37.13.020, an examination of the impact of the invest-
20 ment criteria of this chapter on the corporation portfolio with recom-
21 mendations of any needed changes and any other information the board
22 believes would be of interest to the governor, the legislature, and the
23 public. The annual income statement and balance sheet of the corpora-
24 tion shall be published in at least one newspaper in each judicial
25 district. The income statement and balance sheet for the two fiscal
26 years preceding the publication of the election pamphlet under AS 15.57
27 shall be included in that pamphlet.

28 Sec. 37.13.180. TAX EXEMPTION. The corporation is exempt from all
29 taxes and assessments in the state. All security instruments issued by

1 the corporation, their transfer, and their income are exempt from all
2 taxes and assessments in the state.

3 Sec. 37.13.190. POLITICAL ACTIVITIES. The resources of the cor-
4 poration may not be used to finance or influence political activities.

5 Sec. 37.13.200. PUBLIC ACCESS TO INFORMATION. Information in the
6 possession of the corporation is a public record, except that infor-
7 mation which discloses the particulars of the business or affairs of a
8 private enterprise or investor is confidential and is not a public
9 record. Confidential information may be disclosed only for the purposes
10 of an official law enforcement investigation or when its production is
11 required in a court proceeding. These restrictions do not prohibit the
12 publication of statistics presented in a manner that prevents the iden-
13 tification of particular reports, items, persons, or enterprises.

14 Sec. 37.13.210. DEFINITIONS. In this chapter,

15 (1) "board" means the Board of Trustees of the Alaska Per-
16 manent Fund Corporation;

17 (2) "corporation" means the Alaska Permanent Fund Corpora-
18 tion.

19 * Sec. 6. AS 38.05.180(g) is amended to read:

20 (g) The share of the net profit derived from a lease reserved to
21 the state under (f) of this section is royalty sale proceeds for the
22 purposes of the Alaska permanent fund under AS 37.13.010 [AS 37.10.065]
23 and the Alaska renewable resources development fund under AS 37.11.020.

24 * Sec. 7. AS 39.25.110 is amended by adding a new paragraph to read:

25 (22) members of the board of trustees, the executive director,
26 and staff of the Alaska Permanent Fund Corporation.

27 * Sec. 8. AS 39.50.200(9) is amended by adding a new subparagraph to
28 read:

29 (SS) Board of Trustees and executive director of the

1 Alaska Permanent Fund Corporation.

2 * Sec. 9. TRANSITION. The commissioner of revenue shall transfer the
3 Alaska permanent fund to the Alaska Permanent Fund Corporation established by
4 this Act after request for transfer is made by the board of trustees of the
5 corporation. Notwithstanding AS 37.10.065(a), the commissioner of revenue
6 may invest the money in the Alaska permanent fund in the investments de-
7 scribed in AS 37.13.120(g) subject to the limitations of AS 37.13.120(h) and
8 (i).

9 * Sec. 10. AS 37.10.065 is repealed.

10 * Sec. 11. Section 10 of this Act takes effect upon transfer of the
11 Alaska permanent fund to the Alaska Permanent Fund Corporation as provided in
12 sec. 9 of this Act. The remainder of this Act takes effect immediately in
13 accordance with AS 01.10.070(c).



Alaska State Legislature

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JUNEAU, ALASKA 99811
OFFICIAL BUSINESS

FREE CONFERENCE COMMITTEE REPORT

FCCS for HCS for SB 161

In making their decision on the Alaska Permanent Fund, the Free Conference Committee has focused on a single question --- the management of the Fund's principal.

It is to be an inviolate trust which, in the words of this bill, conserves "...a portion of the state's revenues from mineral resources to benefit all generations of Alaskans..." (page 4).

It is to be an independent trust, yet made accountable in various ways to "...maintain safety of principal while maximizing total return..." (page 4).

The contribution rate has been set at 50% of mineral lease bonuses (except from the Beaufort Sea, which has been left at 25%) and 50% of mineral lease royalties and net profits from the Beaufort Sea and other future sales. The rate for Prudhoe Bay remains at 25% plus any other money appropriated annually by the Legislature.

Three major concerns --- safety of principal, accountability, and legislative oversight --- are addressed by the legislation.

Safety of Principal

The Free Conference Committee Permanent Fund bill provides a framework for fiscally conservative and responsible management of the Fund's principal. It assures and emphasizes the safety of the assets while providing the responsible managers with sufficient investment latitude to achieve superior results. Under the terms of this bill, the Alaska Permanent Fund would consist of a wide variety of quality, high-grade investments.

The Fund is designed to be a trust which focuses on the safety of principal first and the maximization of earnings second (page 4). It is a trust held to a more restricted list of investments than most other fiduciary trusts including the Alaska State Pension Funds and it confirms in law the

current state practice of evaluating performance according to nationally recognized and accepted standards. The investment managers are required to maintain investment diversification and are allowed to determine the investment mix of short, intermediate, and long-term investments. The flexibility allowed enables the managers to achieve a sound rate of return on investments.

The bill provides the investment managers with the authority to place funds in direct obligations of the United States Treasury, federal agency securities, certificates of deposit, high-grade corporate bonds, quality short-term investments, and federally guaranteed loans (pages 8-9). The fund is directed to give preference to Alaska investments as long as they meet the standards of quality set out in the bill. Specifically, deposits can be made in Alaska banks, mutual savings banks, savings and loan associations, and credit unions. Residential real estate (owner-occupied single family dwellings, duplexes, and condominiums) may also be purchased if the mortgage is privately insured by a company doing business in Alaska (page 9). The order in which the investments are listed is not meant to express a priority for one type of investment over another.

Importantly, the bill has a minimum of investment restrictions yet provides a very definite and certain framework. It does not authorize investments in stock or bullion, restricts the purchase of corporate bonds to 25% of the Fund's total investments, and limits the purchase of loans and mortgages to 25% of the total. Purchases of residential mortgages may be a further 15% of total assets. The bill allows the Fund to use the futures market to protect investments from the severe declines in value that are being suffered today. These futures contracts, however, may be used only to hedge and not to speculate. The bill also prohibits the Fund from either borrowing or guaranteeing the obligations of others (page 8).

The bill also provides for the handling of gains and losses and income (page 11). Any losses not offset by gains on the sale of securities shall be deducted from income and added to the Fund principal; this protects the Fund principal from erosion. Losses from sales of securities are spread over a period of time equal to the remaining life; this encourages the managers to get rid of bad investments. Capital gains are added to the Fund principal, helping to offset the effects of inflation. The Fund income is defined as the interest received on the investments, and the amount of income available for disbursement will be determined on an averaging basis; this insures a relatively steady income flow.

Accountability

It was the aim of the Committee to establish a management system for the Alaska Permanent Fund which would be protected from political influences but, at the same time, responsive to changes in state policy and accountable to the people through their elected officials. In short, the aim was insulation without isolation. It was agreed that the best way of achieving these ends was not to place the management within the Department of Revenue, but to create a public corporation distinct from state government. Although the Department of Revenue currently manages the pension funds as well as the general fund, it was agreed that the Permanent Fund, with its fundamentally different goals and large size, should not be in the hands of the same people whose primary duty is managing money for day-to-day use by the state. The Corporation is placed within the Department of Revenue for administrative matters such as payroll, but has a legal existence independent of and separate from the state.

The proposed Permanent Fund Corporation, therefore, has its own board of trustees which is made accountable in several ways (page 5). The six members of the board will be appointed by the Governor and consist of the Commissioner of Revenue, two other commissioners, and three public members. They will be confirmed by the Legislature, except for the Commissioner of Revenue who serves by right of his office; the other commissioners are to submit to a separate confirmation for their duties as trustees. Terms are three years; staggered, and members may be reappointed subject to confirmation. Members may be removed from the board by the Governor and the Legislature may override this decision in a Joint Session. The public members of the board may not hold any other state or federal office or employment and must have recognized competence and wide experience in finance, investments, or other business management-related fields. They are subject to the conflict of interest law and must disclose any interest in entities in which corporate assets are invested. They will be paid honorariums competitive with the largest private corporations in the state. It is intended that every two years the Governor shall make recommendations on adjusting the level of the honorarium. The board will employ an executive director who is also subject to the conflict of interest law and responsible for hiring additional staff with the board's approval.

The corporation's operating budget is from the general fund and is subject to the Executive Budget Act (page 10). This provision offers another check on the management and will prevent such things as the hiring of excessive numbers of employees or uncontrolled expense accounts.

Among the board's responsibilities is the publishing of a yearly report (page 11) including a financial statement reviewed by independent auditors, a statement of earnings from each investment, a market-value appraisal of the investments, and a performance evaluation with recommendations for needed changes. These reports, which must be written in easily understandable language, will be available to the Governor, the Legislature, and the public. The income statement and balance sheet will be published yearly in newspapers and every two years in the election pamphlet.

The bill thus insures that the board of trustees of the Alaska Permanent Fund Corporation will be the best investment managers available in the state, will be accountable to both the executive and legislative branches through appointment and budget processes and oversight by the Legislative Budget and Audit Committee, and will keep the public informed about the Fund's investment performance.

Legislative Oversight

The Free Conference Committee found a need for coordinated, continuing oversight of all the state's investment efforts. Accordingly, the review will extend beyond the Alaska Permanent Fund to include the Alaska Renewable Resources Fund, loan programs, the several authorities, and the general fund. As well as building up a body of legislators with detailed knowledge of investments, this new approach will give the Legislature and the broad public better information on the policies and efficiency of the various investment agencies, on the extent to which these agencies conform to statutory intent, and on the extent to which the economic and social goals of the various programs are being achieved.

The House Finance Committee had considered providing in the Permanent Fund bill for a new interim committee to handle this oversight function but decided, in the interest of efficiency, to simply expand the powers and duties of the present Legislative Budget and Audit Committee (pages 1-3). As proposed, the Legislative Budget and Audit Committee will review the plans and reports of all state agencies involved in lending or investing, report to the Legislature its findings and recommendations, and provide for audits and performance evaluations of the Alaska Permanent Fund Corporation's investment program.

It is the Committee's intent, however, that these new duties be assigned to the Legislative Budget and Audit Committee on a trial basis and that the committee report back to the Legislature within two years, recommending how best the oversight duty could be carried out and including

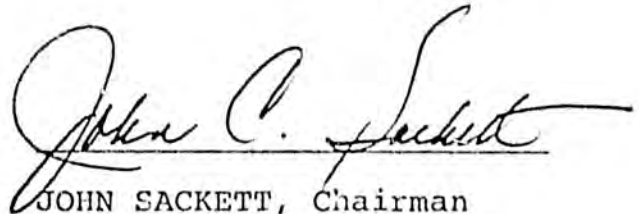
consideration of the option of delegating the responsibilities to a separate committee.

The Future

As stated earlier, this bill addresses only the question of Fund management and leaves the separate question of how to use the Fund earnings to separate legislation. It merely assures that there will be income and does not preclude any options for its use. Unless another determination is made, the Permanent Fund earnings will be deposited in the general fund. No matter what use(s) are decided for the income, the very establishment of a secure trust will be a sign to the national financial community that Alaska is following a responsible fiscal policy.



TERRY GARDINER, Chairman
Conference Committee



JOHN SACKETT, Chairman
Conference Committee

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In making their decision on the Alaska Permanent Fund, the Free Conference Committee has focused on a single question --- the management of the Fund's principal.

It is to be, as the Governor has urged, "...an inviolate trust..." which, in the words of this bill, conserves "...a portion of the state's revenues from mineral resources to benefit all generations of Alaskans..." (page 4).

It is to be an independent trust, yet made accountable in various ways to "...maintain safety of principal while maximizing total return..." (page 4).

The contribution rate has been set at 25% of mineral lease bonuses (after deducting payments under the Alaska Native Claims Settlement Act and for the Alaska Renewable Resources Fund), 25% of the mineral lease royalties plus any other money appropriated by the Legislature.

Three major concerns --- safety of principal, accountability, and legislative oversight --- are addressed by the legislation.

Safety of Principal

The Free Conference Committee Permanent Fund bill provides a framework for fiscally conservative and responsible management of the Fund's principal. It assures and emphasizes the safety of the assets while providing the responsible managers with sufficient investment latitude to achieve superior results. Under the terms of this bill, the Alaska Permanent Fund would consist of a wide variety of quality, high-grade investments.

The Fund is designed to be a trust which focuses on the safety of principal first and the maximization of earnings second (page 4). It is a trust held to a more restricted list of investments than most other fiduciary trusts including the Alaska State Pension Funds and it confirms in law the current state practice of evaluating performance according to nationally recognized and accepted standards. The investment managers are required to maintain investment diversification and are allowed to determine the investment mix of short, intermediate, and long-term investments. The flexibility allowed enables the managers to achieve a sound rate of return on investments.

The bill provides the investment managers with the authority to place funds in direct obligations of the United States Treasury, federal agency securities, certificates of deposit, high-grade corporate bonds, quality short-term investments, and federally guaranteed loans (pages 8-9). The fund is directed to give preference to Alaska investments as long as they meet the standards of quality set out in the bill. Specifically, deposits can be made in Alaska banks, mutual savings banks, savings and loan associations, and credit unions. Residential real estate (owner-occupied single family dwellings, duplexes, and condominiums) may also be purchased if the mortgage is privately insured by a company doing business in Alaska (page 9). The order in which the investments are listed is not meant to express a priority for one type of investment over another. Importantly, the bill has a minimum of investment restrictions yet provides a very definite and certain framework. It does not authorize investments in stock or bullion, restricts the purchase of corporate bonds to 25% of the Fund's total investments, and limits the purchase of loans and mortgages to 25% of the total. Purchases of residential mortgages may be a further 15% of total assets. The bill allows the Fund to use the futures market to protect investments from the severe declines in value that are being suffered today. These futures contracts, however, may be used only to hedge and

not to speculate. The bill also prohibits the Fund from either borrowing or guaranteeing the obligations of others (page 8).

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Accountability

It was the aim of the Committee to establish a management system for the Alaska Permanent Fund which would be protected from political influences but, at the same time, responsive to changes in state policy and accountable to the people through their elected officials. As former House Permanent Fund Committee Chairman Clark Gruening had said, "We want insulation without isolation." It was agreed that the best way of achieving these ends was not to place the management within the Department of Revenue, but to create a public corporation distinct from state government. Although the Department of Revenue currently manages the pension funds as well as the general fund, it was agreed that the Permanent Fund, with its fundamentally different goals and large size, should not be in the hands of the same people whose primary duty is managing money for day-to-day use by the state.

The proposed Permanent Fund Corporation, therefore, has its own board of trustees which is made accountable in several ways

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