

HOUSE
COMMITTEE REPORT

2/21

Date referred: 1/13/86

FURTHER REFERRALS: FINANCE

DATE: 2/19/86

The STATE AFFAIRS Committee has considered HB 465

"An Act relating to fiscal matters involving the state and persons doing business in the Republic of South Africa; and providing for an effective date."

and recommends: individual Recommendation

- do pass
- do not pass
- do pass with attached amendment(s)
- no recommendation
- replace with _____ same title
 new title

and recommends _____

further referral to the _____ Committee

- and attaches:
- letter of intent
 - first fiscal note
 - new fiscal notes
 - zero fiscal note w/analysis
- } Sup # 89
} Sup # 89

SIGNING DO PASS:

SIGNING OTHER RECOMMENDATIONS:

Katie Hurley
Mr. Miller

Roger Jordan No Rec
Betty Cato No Rec

Katie Hurley
Chairman

Cook
1364

Cook

Introduced: 1/13/86
Referred: State Affairs and
Finance

1 IN THE HOUSE

BY CLOCKSIN AND KOPONEN

2 HOUSE BILL NO. 465

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FOURTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act relating to fiscal matters involving the
7 state and persons doing business in the Republic of
8 South Africa; and providing for an effective date."

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

10 * Section 1. AS 37 is amended by adding a new chapter to read:

11 CHAPTER 24. FISCAL MATTERS RELATING TO SOUTH AFRICA.

12 Sec. 37.24.010. PROHIBITED INVESTMENTS AND DEPOSITS. (a) An
13 agency may not

14 (1) deposit an asset in a bank or financial institution
15 that directly or through a subsidiary has outstanding loans to the
16 Republic of South Africa or an instrumentality of the Republic of
17 South Africa; or

18 (2) invest an asset in the stocks, bonds, securities or
19 other obligations of a company engaged directly or through a
20 subsidiary in manufacturing, assembling, warehousing, or other
21 substantial business operations within the Republic of South Africa.

22 (b) For purposes of this section "asset" means any asset of the
23 state including money in the general fund, the permanent fund, or
24 other fund of the state or an agency.

25 Sec. 37.24.020. DIVESTMENT OR WITHDRAWAL OF DEPOSITS. An agency
26 with an investment or deposit that is prohibited under AS 37.24.010
27 shall sell, redeem, divest or withdraw the investment or deposit as
28 soon as possible consistent with sound investment policy and, in any
29 case, no later than December 31, 1988.

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2 investment that is prohibited under AS 37.24.010 shall exercise share-
3 holder voting rights and take other action as feasible to encourage
4 the company to curtail its business involvement in the Republic of
5 South Africa.

6 Sec. 37.24.040. ANNUAL REPORTS. (a) An agency with investments
7 or deposits prohibited under AS 37.24.010 shall by January 15 of each
8 year file a report with the legislature

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25 that the person engages in substantial business within the Republic of
26 South Africa.

27 Sec. 37.24.060. CONFLICTING LAWS INAPPLICABLE. To the extent
28 that the provisions of this chapter conflict with the provisions of
29 other state law, the provisions of this chapter prevail.

1 Sec. 37.24.100. DEFINITION. In this chapter "agency" means a
2 state agency or public corporation of the state, other than a munic-
3 ipality, and includes the University of Alaska.

4 * Sec. 2. This Act takes effect immediately in accordance with AS 01.-
5 10.070(c).

2/21/86
SOP 8/9

STATE OF ALASKA 1986 LEGISLATIVE SESSION
FISCAL NOTE

Page 1 of 2

Revision Date: _____

REQUEST

Bill/Resolution No: HB 465 No. 1
Title: State and Persons Doing Business in the Republic of South Africa

FISCAL DETAIL

Agency Affected: _____
BRU: _____
Components: _____

Sponsor: Clocks in
Requestor: House State Affairs
Date of Request: February 11, 1986

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 86	FY 87	FY 88	FY 89	FY 90	FY 91
OPERATING						
PERSONAL SERVICES	-	-	-	-	-	-
TRAVEL	-	-	-	-	-	-
CONTRACTUAL	-	-	-	-	-	-
SUPPLIES	-	-	-	-	-	-
EQUIPMENT	-	-	-	-	-	-
LANDS & STRUCTURES	-	-	-	-	-	-
GRANTS, CLAIMS	-	-	-	-	-	-
MISCELLANEOUS	-	-	-	-	-	-
TOTAL OPERATING	-	-	-	-	-	-
CAPITAL	-	-	-	-	-	-
REVENUE	-	(1,000)	(1,000)	(1,000)	(1,000)	(1,000)

FUNDING: (Thousands of Dollars)

GENERAL FUND	-	(1,000)	(1,000)	(1,000)	(1,000)	(1,000)
FEDERAL FUNDS	-	-	-	-	-	-
OTHER	-	-	-	-	-	-
TOTAL	-	(1,000)	(1,000)	(1,000)	(1,000)	(1,000)

POSITIONS:

FULL-TIME	-	-	-	-	-	-
PART-TIME	-	-	-	-	-	-
TEMPORARY	-	-	-	-	-	-

ANALYSIS: See attached analysis.

Prepared By: Milt Barker MB
Division: Treasury

Phone: 465-2350
Date: February 12, 1986

Approved by Commissioner: Max G. Stankovic
Agency: Department of Revenue

Date: 2/12/86

Distribution (by Agency preparing fiscal note):

- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
- Impacted Agency(ies)

HB 465 No. 1 Page 2 of 2
Fiscal Note Analysis

HB 465 is also estimated to reduce retirement fund earnings as described in the attached memo. The effect on the General Fund and municipalities' finances from the higher required employer contributions would require actuarial evaluation.

The estimated effects of HB 465 on retirement fund earnings stem in large part from certain inherent restrictions on the flexibility of the funds to be restructured in line with divestment requirements. Even if South Africa-free securities were to offer higher returns in the future than those of firms doing business in South Africa, the requirements of fiduciary duty, fund size, and Alaska statutes would so affect the restructuring of the investment portfolios that there would still be reductions in overall earnings.

More specifically, the five year earnings loss for the retirement funds, estimated in the attached memo to be \$178 million, would still be a loss of approximately \$107 million if one assumed that South Africa-free stocks earned the same rate of return as South Africa-related stocks.

South Africa-free stocks would have to earn approximately 19.3 percent under the divestment scenario shown in the table attached to the memo to eliminate any loss. Such a rate on South Africa-free stocks would imply a 10.1 percent return on South Africa-related stocks to produce the average 15.0 percent return assumed in the no-divestment scenario. A spread of 9.2 percent for South Africa-free stocks over South Africa-related stocks would be highly improbable over any sustained period of time.

The restructuring of the portfolio, as described in the memo, would be done to avoid increasing the risk of the portfolio, which otherwise would result from replacing blue chip common stocks with stocks of smaller, less diversified corporations. This avoidance of excessive risk would be required by the prudent investor rule as well as specific statutory restraints such as the prohibition on purchase of stocks which have not paid dividends for the last three years. The restructuring also would be necessary because it would be difficult to invest funds of this size in a smaller group of stocks with much smaller market values without affecting the prices at which they are purchased.

STATE OF ALASKA
DEPARTMENT OF REVENUE

HB 465-701

MEMORANDUM

Page 1
TO: Milt Barker *MB*
Deputy Commissioner

FROM: James R. Wilson
State Investment Officer

DATE: September 9, 1985

RE: South African Divestment Effects

The proposed divestment of investments in companies doing business in South Africa would have the effect of removing

62% of the 50 largest U.S. companies,
57% of the Fortune 100 companies,
47% of the S & P 500 companies, and
35% of the Wilshire 5000 companies

and would constitute avoiding, to name a few,

91% of international oil companies,
90% of office equipment companies,
89% of drug companies,
88% of chemical companies, and
87% of automobile manufacturers.

The common stock portfolios would have to avoid most of the large, heavily capitalized, successful, and relatively secure U.S. companies and would have to concentrate on utility, transportation, and retail stocks. Because the smaller companies in which investments would have to be made are inherently riskier on a credit basis, they also have more volatile stock prices and hold a greater chance of losing money on the investments. The non-South African S & P 265 (what is left of the 500) has been shown to be 1.84 times more volatile on the upside but 2.27 times more volatile on the downside. This translates to a drop of 18.9% in the probable rate of return over long periods of time. For large funds like the Alaska Retirement Systems, common stock holdings would have to be excessively diversified into too many small holdings. It has been demonstrated that common stock portfolios approaching 100 or more stocks have virtually no chance of surpassing the general stock market's average performance -- ergo, a lower

Milt Barker
September 9, 1985
Page 2

HB 465 #1

Page 2

return than we currently enjoy. Consequently, we would find it necessary to reduce our potential risk by reducing what otherwise would be the size of our common stock portfolios.

The divestment would also affect our bond and money market portfolios by removing much of our potential investment universe; i.e.,

77% of commercial paper issuers,
87% of bank issued paper, and
60% of industrial corporate bonds.

The loss of money opportunities would reduce our yield by .25% in those areas, but the loss of most of the best credits in the corporate bond area would have more pronounced effects. Because the remaining industrial bonds would be substantially more risky, we would have to maintain a smaller, relative position -- although it would cost us 1.1% in yield. Prudence would also demand a smaller utility bond position as well so we would not be overly weighted in that riskier and less call protected area.

Divestment would have similar but somewhat reduced effects on the State's General Fund and on the Public School and University of Alaska Funds. These endowment funds would lose their only equity investments (convertibles) and more than half of their high yielding corporate bonds. The General Fund would be practically trapped into only U.S. Treasury issues for a give-up of about \$1 million a year.

In order to quantify the effects on the Retirement Systems' investments, I have calculated their probable average positions and rates of return for each of the next five fiscal years. Then, after allowing for the divestment effects on the portfolio's positions and yields -- as previously noted in this memorandum -- I have recalculated the rates of return for the same five fiscal years. The results of these calculations are shown in the attached table. The divestment portfolios have smaller common stock and corporate bond positions and larger U.S. Treasury positions, and yields on common stocks are lower. The net result for the sum of the five years is a reduction in returns on investments totalling \$177,890,000.

JRW/gb

Attachment

HB 465, Vol 1

Combined Retirement Systems Investments
Average Assets & Yields During Fiscal Years
(\$ Millions)

Page 3

	1986		1987		1988		1989		1990		Sum of 5 years
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	
Common Stocks	\$ 517.9	15.00%	\$ 716.6	15.00%	\$ 913.2	15.00%	\$1,127.1	15.00%	\$1,252.6	15.00%	\$2,027.58
Industrial Bonds	97.8	12.00	162.2	12.00	251.9	12.00	345.4	12.00	416.2	12.00	
Utility Bonds	69.1	12.25	162.2	12.25	251.9	12.25	345.4	12.25	416.2	12.25	
Treasury Bonds	658.4	10.90	727.4	10.90	691.2	10.90	667.2	10.90	715.9	10.90	
Money Market	262.4	9.20	162.2	9.20	188.9	9.20	218.1	9.20	249.7	9.20	
R. E. Equities	168.0	14.00	202.8	14.00	242.5	14.00	287.2	14.00	333.0	14.00	
Mortgages	529.5	12.50	570.5	12.50	609.3	12.50	645.4	12.50	678.4	12.50	
Total	\$2,303.1	12.31%	\$2,703.9	12.60%	\$3,148.9	12.73%	\$3,635.8	12.83%	\$4,162.0	12.88%	
Return	\$283.51		\$340.69		\$400.85		\$466.47		\$536.06		

Divestment Effects (Less 47% stocks, 60% industrial bonds, 87% of CD's, BA's, & 77% of com. paper)

Common Stock	\$ 274.6	12.15%	\$ 379.8	12.15%	\$ 484.0	12.15%	\$ 597.4	12.15%	\$ 717.1	12.15%	\$1,849.69
Industrial Bonds	39.2	12.00	64.9	12.00	100.8	12.00	138.2	12.00	166.5	12.00	
Utility Bonds	34.5	12.25	64.9	12.25	100.8	12.25	138.2	12.25	166.5	12.25	
Treasury Bonds	994.9	10.90	1,258.8	10.90	1,422.6	10.90	1,611.3	10.90	1,850.8	10.90	
Money Market	262.4	9.10	162.2	9.10	188.9	9.10	218.1	9.10	249.7	9.10	
R. E. Equities	168.0	14.00	202.8	14.00	242.5	14.00	287.2	14.00	333.0	14.00	
Mortgages	529.5	12.50	570.5	12.50	609.3	12.50	645.4	12.50	678.4	12.50	
Total	\$2,303.1	11.48%	\$2,703.9	11.60%	\$3,148.9	11.61%	\$3,635.8	11.62%	\$4,162.0	11.61%	
Return	\$264.40		\$313.64		\$365.59		\$422.48		\$481.58		
Divestment Loss	- \$19.11		- \$27.05		- \$35.26		- \$43.99		- \$52.48		

STATE OF ALASKA 1986 LEGISLATIVE SESSION
FISCAL NOTE

Revision Date: _____

REQUEST Page 1 of 2 FISCAL DETAIL

Bill/Resolution No.: HB 465 No. 2 Agency Affected: A11

Title: An act relating to fiscal matters BRU: _____

involving the State and persons doing

business in the Republic of South Africa..

Sponsor: Clocks in and Koponen Components: A11

Requestor: House State Affairs

Date of Request: February 12, 1986

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 86	FY 87	FY 88	FY 89	FY 90	FY 91
OPERATING						
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	0	0	0	0	0	0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LAND & STRUCTURES	0	0	0	0	0	0
GRANTS, CLAIMS	0	0	0	0	0	0
MISCELLANEOUS	0	0	0	0	0	0
TOTAL OPERATING	0	0	0	0	0	0
CAPITAL	0	0	0	0	0	0
REVENUE	0	0	0	0	0	0

FUNDING: (Thousands of Dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS	0	0	0	0	0	0
OTHER	0	0	0	0	0	0
TOTAL	0	0	0	0	0	0

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

ANALYSIS: Attach a separate page if necessary See Attached

Prepared By: Kenneth E. Bischoff Phone: 465-2200

Division: Finance Date: _____

Approved by Commissioner: Eleanor Andrews Date: 3-12-86

Agency: Department of Administration

Distribution (by Agency preparing fiscal note):

- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
- Impacted Agency(ies)

CONTINUATION of FISCAL NOTE ANALYSIS

For Bill/Resolution No. HB 465 No. 2

Page 2 of 2

SUBJECT OF PROPOSED BILL:

An act relating to fiscal matters involving the State and persons doing business in the Republic of South Africa

SUMMARY/EXPLANATION OF INTENT:

The Department of Administration (DOA) is only directly impacted by one section of this bill, Section 37.24.050 as it relates to DOA's general oversight responsibility for statewide purchasing and contracting defined elsewhere in AS 37.

It is difficult to measure the fiscal impact, if any, that this bill may produce on State contracting and procurement activities. We do not feel that the potential impact will be significant if this bill is passed.

A schedule is attached showing FY 86 payments made by the State of Alaska to businesses who have been identified as having business interests within the Republic of South Africa.

ESTIMATED FISCAL IMPACT:

Capital:

Operating:

ALASKA STATE LEGISLATURE

.14th.. Legislature SECOND... Session

HOUSE ..BILL..... NO. .465..

By .CLOCKSIN .AND. KOPONEN.....

"An Act relating to fiscal matters involving the state and persons doing business in the Republic of South Africa; and providing for an effective date."

South Africa business.

Introduced in the House .1/13...., 19. 86

HISTORY IN THE HOUSE

1986		Read first time and referred to Committee on
Jan	13	STATE AFFAIRS AND FINANCE Reported back with recommendation that
		Read second time and
		Read third time and
		PASS Effective Date
		Yeas Yeas
		Nays Nays
		Absent Absent
		Excused Excused
		Reconsideration
		PASS Effective Date
		Yeas Yeas
		Nays Nays
		Absent Absent
		Excused Excused
		Reported correctly engrossed
		Signed by Speaker
		Sent to Senate
CHIEF CLERK OF THE HOUSE		

HISTORY IN THE SENATE

19		Read first time and referred to Committee on
		Reported back with recommendation that
		Read second time and
		Read third time and
		PASS Effective Date
		Yeas Yeas
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		Reported correctly engrossed
		Signed by President
		Returned to House
SECRETARY OF THE SENATE		

HISTORY IN THE HOUSE

19		Received from Senate
		Concurred in Senate amendment thus adopting: VOTE
		Failed to concur in Senate amendment; asked Senate to recede VOTE
		Senate receded from amendment VOTE
		Senate failed to recede from amendment VOTE
		CC appointed by House
		CC appointed by Senate
		CC adopted by House VOTE
		CC adopted by Senate VOTE
		To enrolling Reported correctly enrolled Sent to Governor by Governor
		Filed with Lt. Governor
		Chapter No.

Introduced: 1/13/86
Referred: State Affairs and
Finance

1 IN THE HOUSE

BY CLOCKSIN AND KOPONEN

2

HOUSE BILL NO. 465

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

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FOURTEENTH LEGISLATURE - SECOND SESSION

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