

**HB**

**422**

**HFIN**

**FILE**



CS FOR HOUSE BILL NO. 422(STA)

IN THE LEGISLATURE OF THE STATE OF ALASKA  
TWENTY-THIRD LEGISLATURE - SECOND SESSION

BY THE HOUSE STATE AFFAIRS COMMITTEE

Offered: 3/8/04  
Referred: Finance

Sponsor(s): HOUSE FINANCE COMMITTEE

A BILL

FOR AN ACT ENTITLED

1 "An Act repealing the special subaccount established in the constitutional budget  
2 reserve fund; and providing for an effective date."

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

4 \* Section 1. AS 37.10.430(c) is repealed.

5 \* Sec. 2. The uncodified law of the State of Alaska is amended by adding a new section to  
6 read:

7 TRANSITION. The special subaccount investments established under  
8 AS 37.10.430(c), repealed by sec. 1 of this Act, merge with other assets of the budget reserve  
9 fund (art. IX, sec. 17, Constitution of the State of Alaska) into a single account.

10 \* Sec. 3. This Act takes effect immediately under AS 01.10.070(c).

# FISCAL NOTE

STATE OF ALASKA  
2004 LEGISLATIVE SESSION

Fiscal Note Number: 1  
Bill Version: HB422  
( ) Publish Date: \_\_\_\_\_

Revision Date/Time (Note if correction): \_\_\_\_\_ Dept. Affected: Revenue  
Title Budget Reserve Fund Investment BRU Revenue Programs & Services  
Component Treasury Management  
Sponsor House Finance  
Requester House State Affairs Component No. 121

**Expenditures/Revenues** (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
Personal Services						
Travel						
Contractual	<125.0>	<125.0>	<125.0>	<125.0>	<125.0>	<125.0>
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
<b>TOTAL OPERATING</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES ( )						
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**FUND SOURCE** (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Constitutional Budget Reserve Fund)	<125.0>	<125.0>	<125.0>	<125.0>	<125.0>	<125.0>
<b>TOTAL</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>	<b>&lt;125.0&gt;</b>

Estimate of any current year (FY2004) cost: 0.0  
Mark this box (X) if funding for this bill is included in the Governor's FY 2005 budget proposal:

**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)

This legislation would eliminate the requirement to invest the CBRF subaccount in equity securities. Investing in equities requires contracting with investment managers. The current cost of the investment contracts is \$125.0 per year. These fees would no longer be required if this legislation passes.

The legislation would also require the CBRF to invest only in investment grade fixed income securities. Less diversification may result in lower investment returns if there is a substantial increase in equity prices. However, the decline in the CBRF fund balance creates a compelling need for a more conservative asset allocation to preserve the fund.

Prepared by: Gary Bader Phone 465-4399  
Division: Treasury Date/Time: 2/9/04 9:45 AM  
Approved by: Tom Boutin Date: 2/9/2004  
Agency: Department of Revenue

## Constitutional Budget Reserve Subaccount

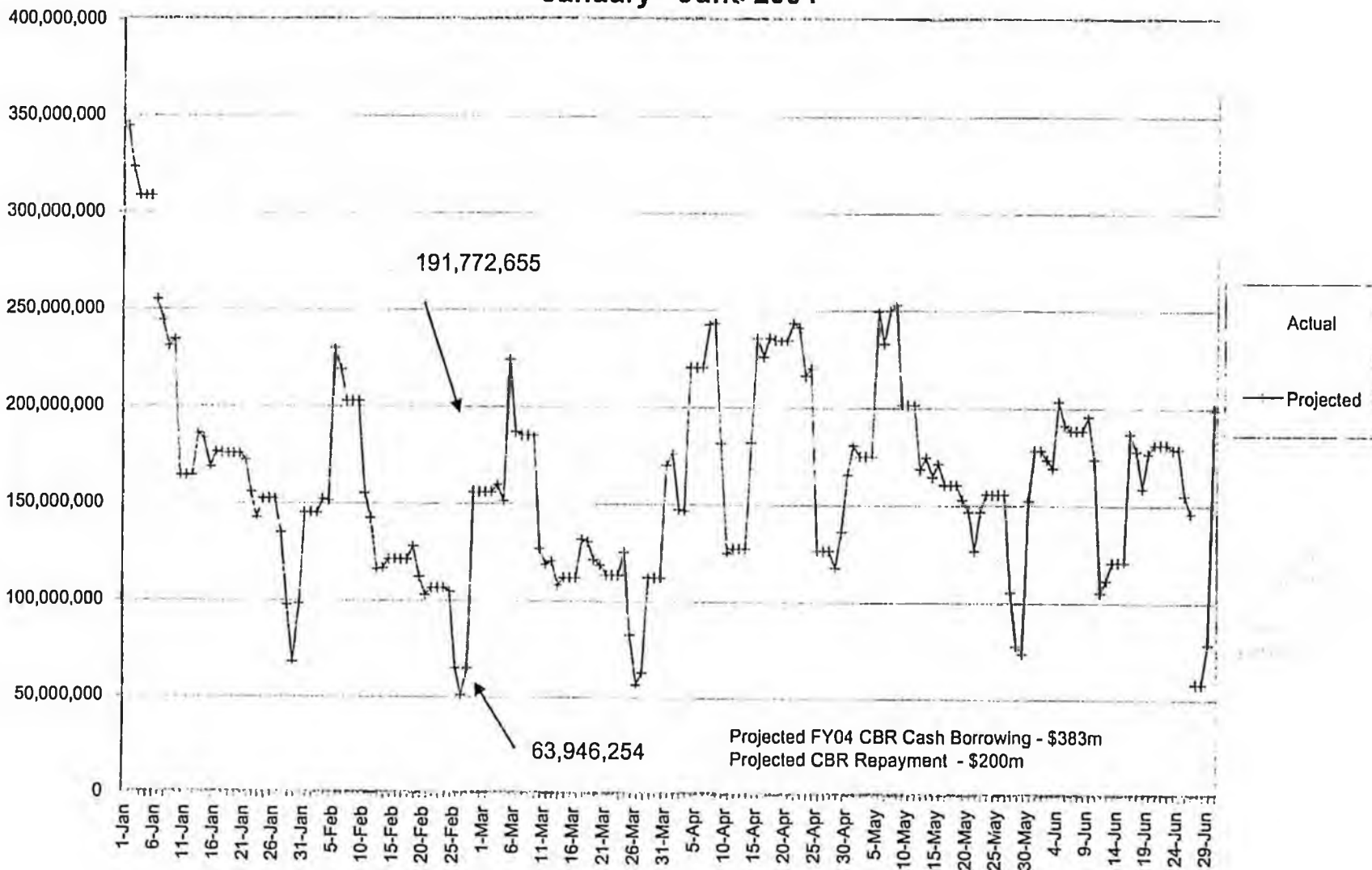
AY10 CBRF Subaccount As of 12/31/03	Actual Allocation	Target Allocation	3 Months	YTD	1 Year	3 Year	5 Year
Broad Market Fxd Income	39.76%	44%					
Russell 3000 Index	42.79%	39%					
Short Term Pool	0.00%	0%					
SOA International Equity	17.45%	17%					
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>7.81</b>	<b>19.17</b>	<b>19.17</b>	<b>1.79</b>	
Benchmark			7.77	20.09	20.09	1.73	
Market Value As of 12/31/03	\$409,785,494						

## Constitutional Budget Reserve

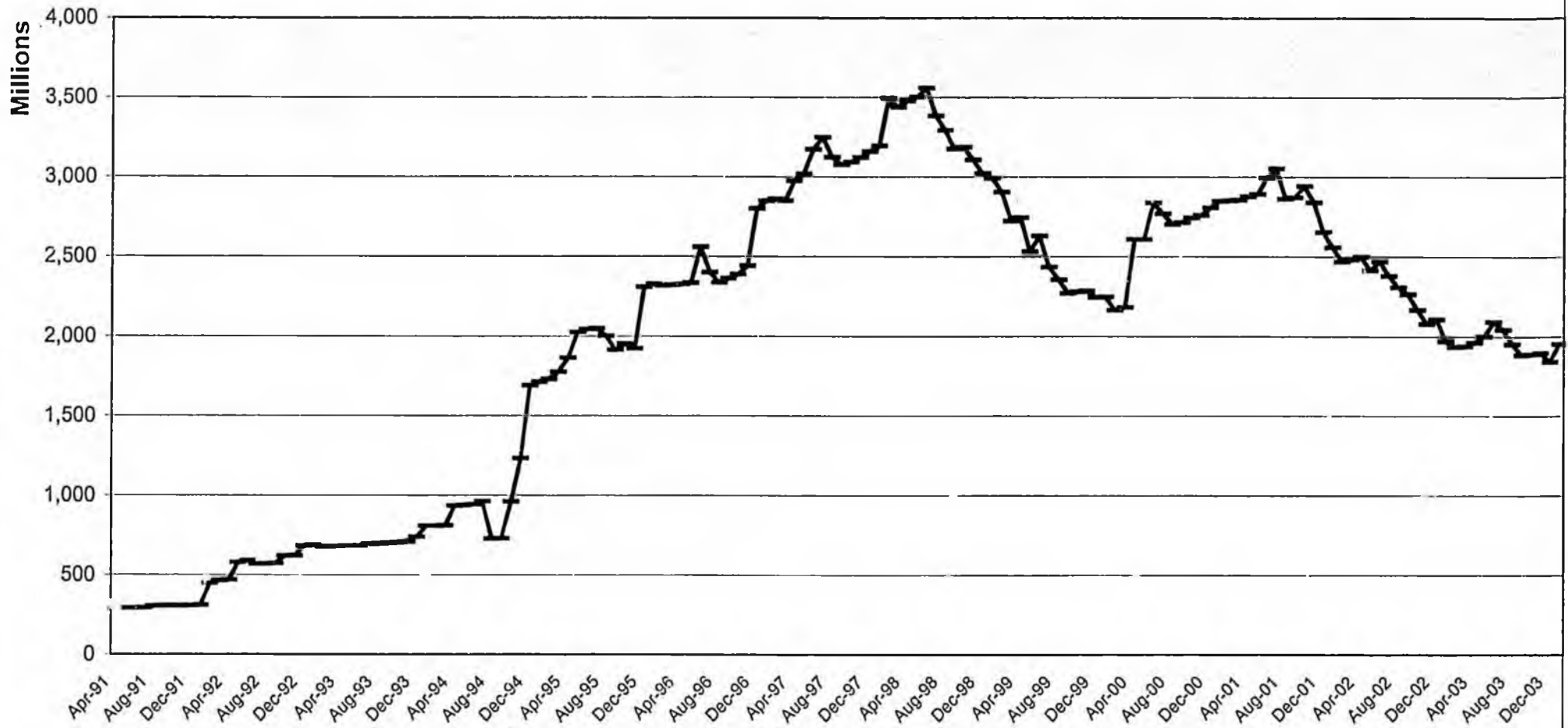
AY19 Constitutional Budget Reserve Fund As of 12/31/03	Actual Allocation	Target Allocation	3 Months	YTD	1 Year	3 Year	5 Year
Broad Market Fxd Income	20.00%	20%					
Short Term Pool	20.12%	20%					
Intermediate Term Fxd Income	59.88%	60%					
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>0.30</b>	<b>3.50</b>	<b>3.50</b>	<b>5.93</b>	<b>5.62</b>
Benchmark			0.13	2.57	2.57	6.07	5.67
Market Value As of 12/31/03	\$1,430,965,670						

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**FY04(B)**  
**General Fund Sufficiency Balance Projection**  
**January - June 2004**

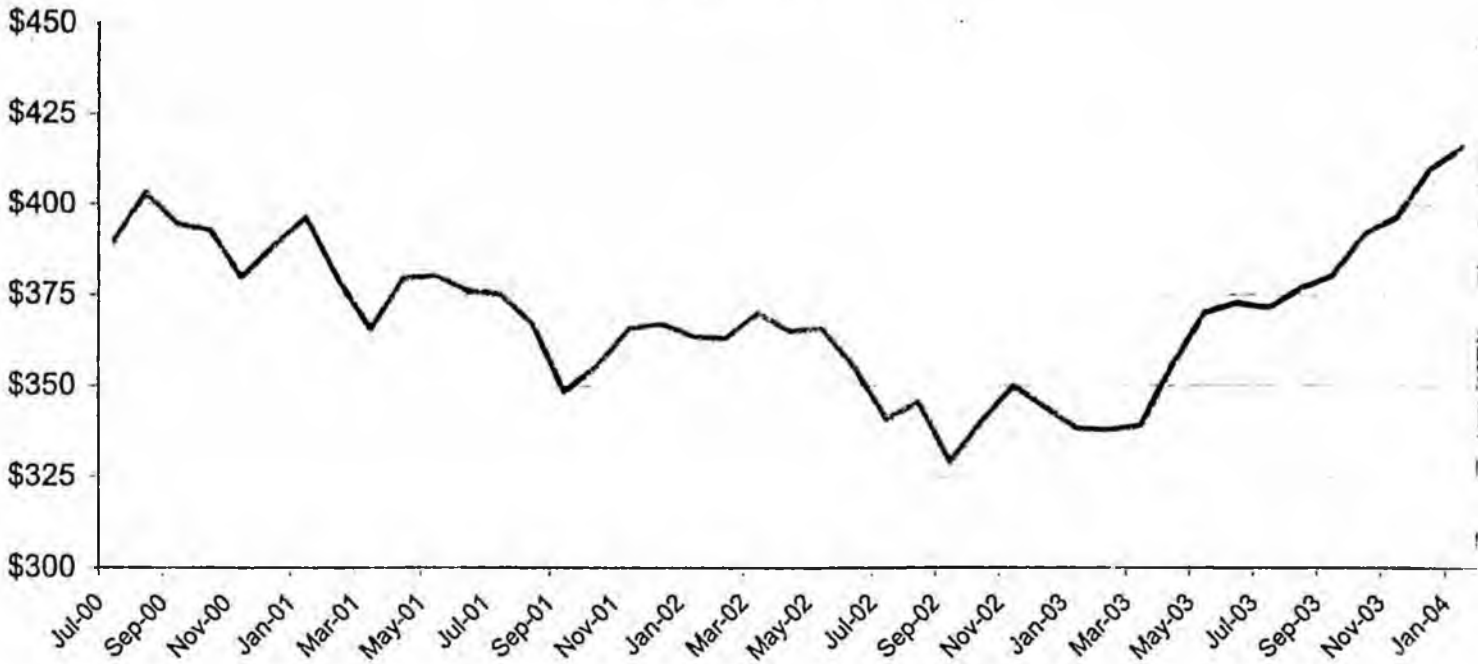


**Constitutional Budget Reserve Fund Monthly Ending Balance  
April/1991 to January/2004**

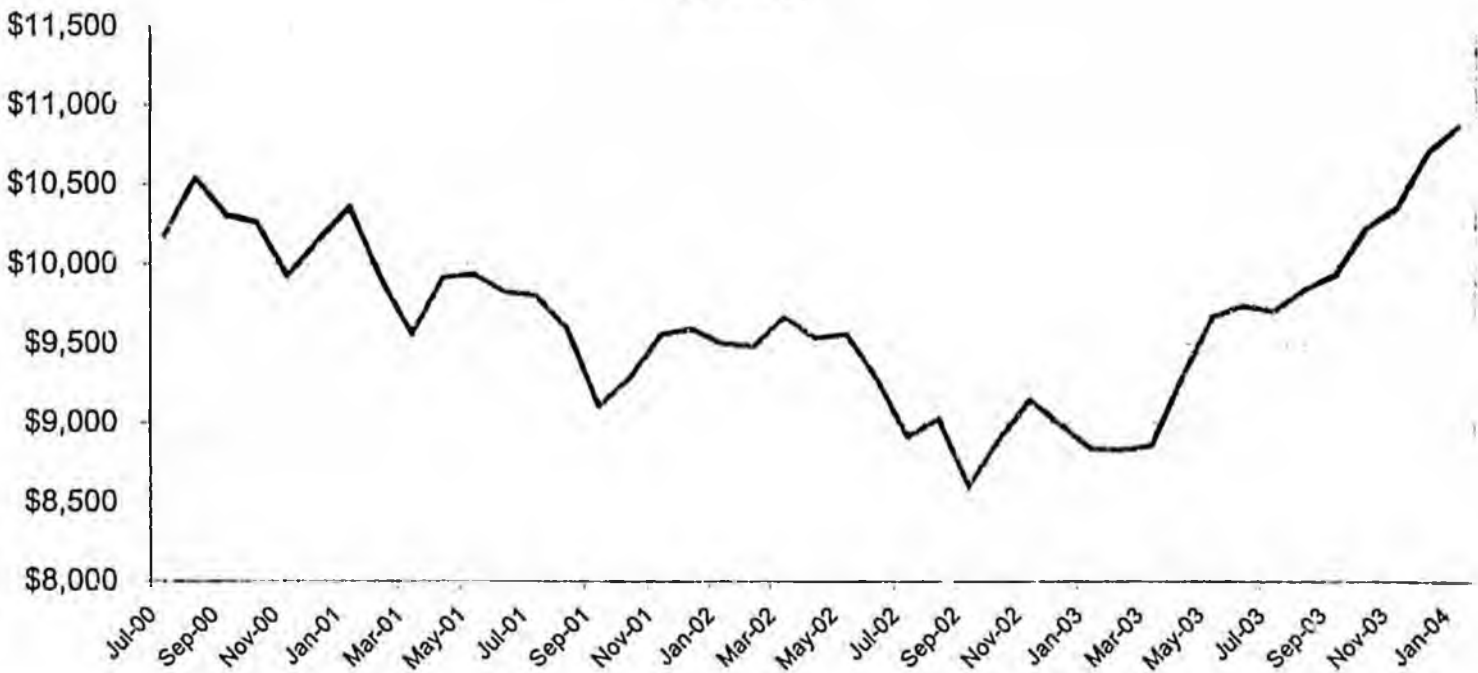


**Notes:** CBRF Subaccount starts July/2000.  
 Withdrawals from the CBRF occur when the General Fund sufficiency balance slips below \$100 million.  
 Deposits to the CBRF occur when settlement money is received or when the General Fund sufficiency balance exceeds \$200 million.

**CBR Subaccount Monthly Ending Balance**  
 July/2000 to January/2004  
 (in Millions)



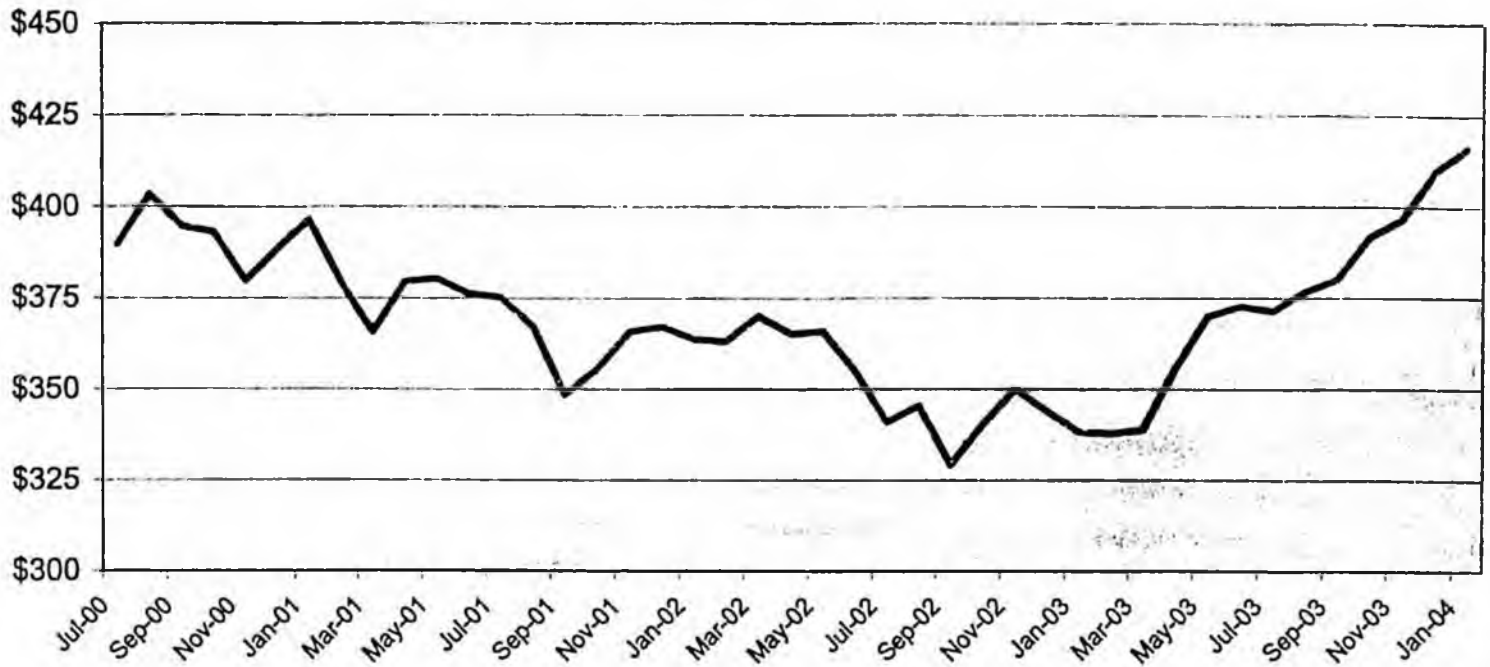
**CBR Subaccount Estimated Monthly Fees Paid**  
 July/2000 to January/2004  
 (actual \$)



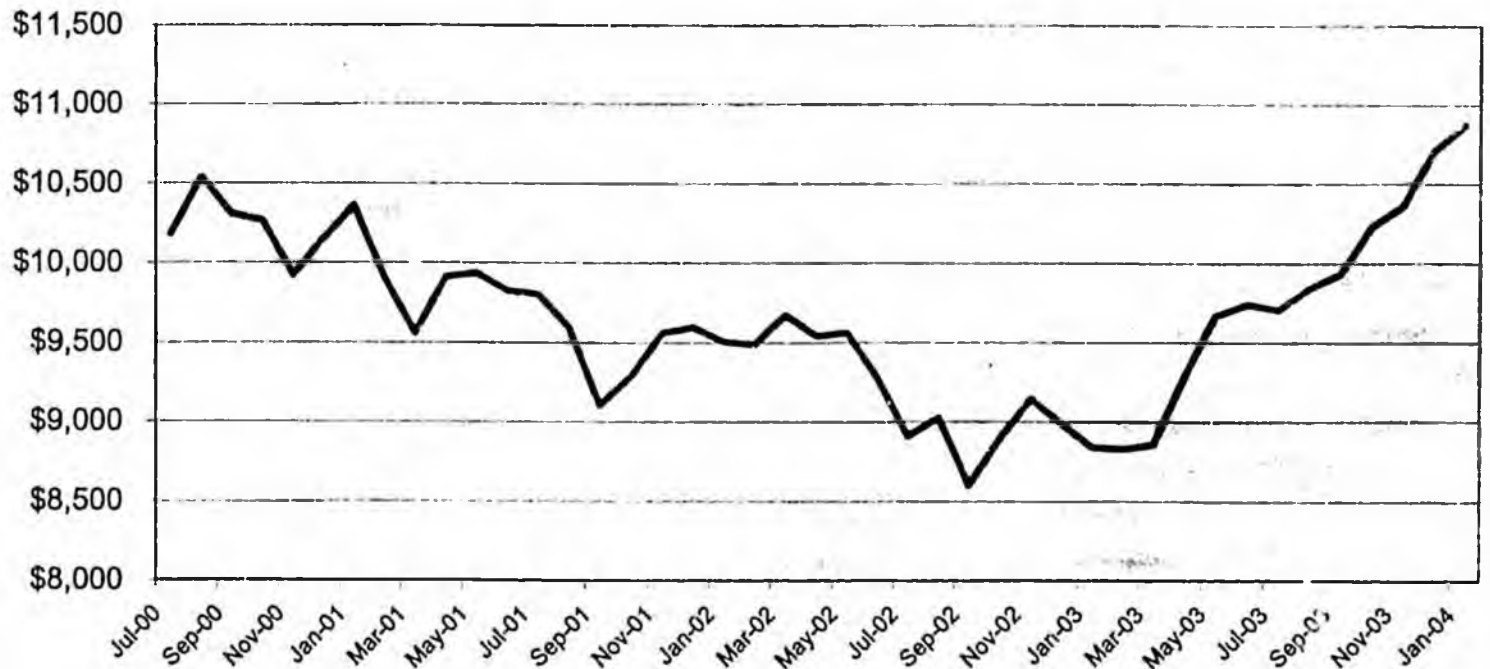
<b>Annual Returns</b>	<b>CBRF</b>	<b>Subaccount</b>
2000*	9.2%	-1.5%
2001	7.6%	-5.5%
2002	6.7%	-6.3%
2003	3.5%	19.2%
2003 - 3 Year Annualized	5.9%	1.8%

\*Note: Only 3 months in 2000 for CBRF Subaccount

**CBR Subaccount Monthly Ending Balance**  
 July/2000 to January/2004  
 (in Millions)



**CBR Subaccount Estimated Monthly Fees Paid**  
 July/2000 to January/2004  
 (actual \$)



Alaska State Legislature  
House Finance Committee

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Sponsor Statement for  
House Bill 422

An Act relating to the existence and management  
of the sub account in the Constitutional Budget Reserve Fund

House Bill 422 would repeal the Constitutional Budget Reserve (CBR) sub account and allow the entire CBR balance to be invested in fixed income securities along with the general fund and other non-segregated money.

In 2000, the legislature passed Senate Bill 312 that transferred \$400 million from the CBR into a separate sub account in an effort to obtain a higher yield by investing the funds with a long-term outlook. The legislation also directed the Commissioner of Revenue to assume that sub account funds will not be needed for at least five years.

However, current budget projections show the CBR being continually drawn down rather than being periodically increased to historically higher balances. While the CBR may extend beyond five years, a CBR balance of at least \$1 billion is needed to meet cash flow needs and prudent financial management given the state's dependence upon oil prices. HB 422 also repeals the five-year provision enacted by SB 312.

The almost certain continual decline in the CBR balance creates a compelling need for a more conservative asset allocation.

Additionally, HB 422 is a cost savings measure as the state would not incur the annual \$125,000 in sub account management fees.

**Government Finance Associates, Inc.**

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March 1, 2004

**TO: TOM BOUTIN  
DEPUTY COMMISSIONER OF REVENUE**

**FROM: GOVERNMENT FINANCE ASSOCIATES, INC.**

**SUBJECT: CHANGE IN INVESTMENT POLICY FOR CBRF**

As you know, Government Finance Associates, Inc., (GFA), has been the financial advisor to the Alaska State Bond Committee since 1983. As such, we have worked with the State over many economic cycles and have aggressively sought to maintain the State's bond rating at high quality levels. We are in constant communication with the nationally recognized rating agencies, on behalf of the State of Alaska as well as on behalf of our other state clients. Furthermore, as you know, both principals of the firm, who are the day-to-day advisors to the State, began their respective careers at Moody's Investors Service with one of the team members having spent 21 years at Moody's, twelve of which as head of the Public Finance Department. GFA prides itself on its unique credit rating agency knowledge and proven track record with Alaska. For example, during all of 1991 through the first half of 1992, Alaska was the only state that had its investment grade rating increased by either of the nationally recognized rating agencies.

You have asked our opinion of a change in the investment policy for the Alaska Constitutional Budget Reserve Fund (CBRF). It is our opinion that an adjustment in the investment guidelines for the State will not pose a credit concern for the rating agencies. Shifting the CBRF's investments from a mix of equities and fixed income securities to all fixed income securities will be viewed as a conservative investment approach which diminishes risk. Since the State has, in recent years, been utilizing the corpus of the CBRF for budget balancing purposes, the purpose of the CBRF has changed from that of a financial cushion to needed operating cash. Therefore, a more conservative investment approach for the CBRF will, actually, create a more dependable reserve, taking into account the extreme volatility that has existed in the equities market over the last several years. More limited reserves require a more conservative investment approach to provide a guarantee of funds for future budgets. Until such time as the State can match recurring expenditures against recurring revenues and not utilize the CBRF for budget balancing purposes, the reserves will be tapped and a conservative investment approach is a prudent one.