

**HJR**

**26**

**SFIN**

**FILE**

# SENATE FINANCE COMMITTEE REPORT

REPORTED OUT  
MAY 06 2004  
SENATE FINANCE  
COMMITTEE

DATE: 5/1/04

FURTHER:

DATE TURNED  
IN TO OFFICE: 05/06/04

Finance Committee considered CS FOR HOUSE JOINT RESOLUTION NO. 26(FIN)

HJR 26 CONST. AM: PF APPROPS/INFLATION-PROOFING

Proposing amendments to the Constitution of the State of Alaska relating to and limiting appropriations from the Alaska permanent fund based on an averaged percent of the fund market value.

and recommends:

- be replaced with \_\_\_\_\_ CS \_\_\_\_\_ (\_\_\_\_\_)
- adopt previous \_\_\_\_\_ CS \_\_\_\_\_ (\_\_\_\_\_)
- attached amendment(s)
- adopt Letter of Intent by \_\_\_\_\_ Committee
- further referral to \_\_\_\_\_ Committee

**Senate Bill:**  
 Same Title  
 New Title

**House Bill:**  
 Same Title  
 Technical Title Change  
 New Title w/ SCR # \_\_\_\_\_

**NEW FISCAL NOTE(S):**

Department	Date	Fiscal	Indet.	Zero.	FN#
Revenue	4/13/04			✓	4

**PREVIOUS FISCAL NOTE(S):**

Department	Date	Fiscal	Indet.	Zero	FN#
Elections	1/16/04	1.5			3

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	DO PASS	DO NOT PASS	NO REC	AMEND
<i>[Signature]</i>			✓	
<i>[Signature]</i>			✓	
<i>[Signature]</i>			✓	
<i>[Signature]</i>	✓			
<i>[Signature]</i>			X	
COCHAIR: <i>[Signature]</i>			✓	
COCHAIR: <i>[Signature]</i>			✓	

1/16/04 2004

# FISCAL NOTE

STATE OF ALASKA  
2004 LEGISLATIVE SESSION

Fiscal Note Number: 3 SENATE FINANCE  
Bill Version: CSHJR-26(FIN) COMMITTEE  
(H) Publish Date: 4/7/04

Revision Date/Time (Note if correction): \_\_\_\_\_ Dept. Affected: GOV  
Title Constitutional amendment relating to and RDU Elections  
limiting appropriations from and inflation-proofing APF Component Elections  
Sponsor Rules  
Requester House Finance Component No. 21

**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	1.5					
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
<b>TOTAL OPERATING</b>	<b>1.5</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

<b>CAPITAL EXPENDITURES</b>						
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<b>CHANGE IN REVENUES ( )</b>						
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**FUND SOURCE** (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF	1.5					
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
<b>TOTAL</b>	<b>1.5</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</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						
Part-time						
Temporary						

**ANALYSIS:** (Attach a separate page if necessary)

This figure includes the cost of providing information about this issue in the Official Election Pamphlet, as required by AS 15.58. If this measure requires the printing of an 8-1/2 by 18 inch ballot, the cost will increase by \$22.0.

Prepared by: Leonard G. Jones  
Division: Division of Elections  
Approved by: Laura A. Glaiser, Director  
Agency: Office of the Lt. Governor, Division of Elections

Phone 465-3051  
Date/Time 1/16/04 9:06 AM  
Date 1/16/2004

REPORTED OUT

MAY 06 2004

SENATE FINANCE  
4 COMMITTEE

# FISCAL NOTE

STATE OF ALASKA  
2004 LEGISLATIVE SESSION

Fiscal Note Number: \_\_\_\_\_  
Bill Version: CSHJR 26(FIN)  
( ) Publish Date: 5/6/04

Revision Date/Time (Note if correction): \_\_\_\_\_ Dept. Affected: Revenue  
Title Const. Am:PF Approps/Inflation-Proof RDU AK Permanent Fund Corporation  
Component AK Permanent Fund Corporation  
Sponsor House Rules Committee  
Requester House Rules Committee Component No. 109

**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						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
<b>TOTAL OPERATING</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</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 1105 PF Receipts						
<b>TOTAL</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</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						
Part-time						
Temporary						

**ANALYSIS:** (Attach a separate page if necessary)

HJR 26 will not effect the budgeted costs to manage and invest the Permanent Fund.

HJR 26 will not change the amount of income earned by Permanent Fund investments.

See the attached schedule for financial projections of the Fund comparing the "Status Quo" to a 5% POMV spending limit.

Prepared by: Robert D. Storer Phone 465-2047  
Division Alaska Permanent Fund Corporation Date/Time 4/13/04 12:00 AM  
Approved by: William Corbus, Commissioner Date 4/13/2004  
Agency Department of Revenue



**Alaska Permanent Fund Corporation**  
**HJR 26 - Financial projection comparison of the Alaska Permanent**  
**Fund under status quo versus POMV spending limit beginning in**  
*\$ millions*

Status Quo	-----projected-----											
	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15
Total Return	15.25%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%
Contributions & appropriations (after payouts)	23,300	24,179	25,042	25,922	26,824	27,748	28,688	29,652	30,628	31,623	32,668	33,725
Unrealized appreciation/depreciation on Invested assets	3,451	3,898	4,284	4,634	4,958	5,262	5,546	5,524	5,865	6,191	6,125	6,498
Realized earnings account (after payouts)	850	1,341	1,943	2,516	3,041	3,591	4,180	5,069	5,640	6,270	7,294	7,942
Total market value end of year (after payouts)	<u>27,601</u>	<u>29,417</u>	<u>31,268</u>	<u>33,072</u>	<u>34,823</u>	<u>36,600</u>	<u>38,414</u>	<u>40,245</u>	<u>42,133</u>	<u>44,084</u>	<u>46,087</u>	<u>48,165</u>
Annual realized income	1,311	1,602	1,796	1,969	2,129	2,280	2,430	2,866	2,643	2,799	3,329	3,044
Dividend (lump sum) - status quo	561	499	560	739	925	1,027	1,113	1,226	1,297	1,367	1,477	1,542
Transfer status quo Inflation-proofing (ER to principal)	0	613	635	657	680	703	727	751	776	801	828	855

POMV - 5% (beginning in FY05)	-----projected 5% POMV beginning in FY05-----											
	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15
Total Return		7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%
Total Market Value End of Year (after payouts)	<u>27,601</u>	<u>28,605</u>	<u>29,621</u>	<u>30,654</u>	<u>31,686</u>	<u>32,710</u>	<u>33,739</u>	<u>34,782</u>	<u>35,840</u>	<u>36,912</u>	<u>38,025</u>	<u>39,153</u>
5 year average market value lagged one year		26,224	26,669	27,674	29,191	30,843	32,061	33,146	34,243	35,346	36,453	37,572
POMV Payout available for appropriation in lump sum		1,311	1,333	1,384	1,460	1,542	1,603	1,657	1,712	1,767	1,823	1,879

**Assumptions:**

- Both scenarios show payouts net of inflation.
- POMV payout assumes calculation methodology is 5% of the ending market value (pre payout) for the first five of the last six fiscal years.
- Callan Associates 2003 Capital Market Assumptions, APFC 2003 asset allocation, Fall 2003 revenue forecast, financial statements through 12/31/03. All payouts are assumed to happen at fiscal year end, all dollar values in millions.
- Per SB 100, currently there is no FY04 Inflation-proofing appropriation, and \$354 million of FY04's projected Inflation-proofing of \$523 was pre-funded in FY03.

SENATE FINANCE COMMITTEE  
5/10/2004 COMMITTEE ACTION

Bill Number	HJR 26		
Amendment			
Motion	to Report		
<u>Motion by</u>	Bunde		
<u>Objection by</u>	" No Objection		
<u>Removed</u>			
<u>Second Objection by</u>			
<u>Committee Member</u>	<u>Y</u>	<u>Vote</u>	<u>N</u>
Senator Hoffman			
Senator Olson			
Senator Stevens			
Senator Bunde			
Senator Dyson			
Co-Chair Green			
Co-Chair Wilken			
<u>Tally</u>			
Yea			
Nay			
Absent			
<u>MOTION</u>	PASSED		



Alaska Permanent Fund Corporation  
Analysis of House Joint Resolution (HJR) 26  
April, 2004

House Joint Resolution 26 proposes changing Alaska's Constitution to require inflation proofing of the entire Permanent Fund and to limit the payouts from the fund. This resolution was introduced at the request of the Permanent Fund Corporation's Board of Trustees.

Many large endowments and public funds use a system known as "percent of market value" payouts, or POMV, to provide payouts while still protecting both the principal and earnings of a fund. POMV limits payouts to a set percentage of the fund's market value, often 5 percent. This has shown to be the maximum sustainable payout rate that will still maintain a fund's real value over time.

However, under current law only the principal of the Permanent Fund is protected and inflation-proofed. The earnings reserve account is not considered part of the principal, is not inflation-proofed and is open to appropriation. In addition, payouts are computed as a portion of the Fund's earnings. This means that if the Fund were to have little or no earnings in a single year, a payout for dividends or other State spending would not be allowed.

Moving to a POMV system and adding the earnings reserve to the Fund would not only provide inflation proofing of the entire fund, but would provide a more reliable and predictable payout each year, regardless of the Fund's performance in an individual year. This would make it more likely that the State could continue the Permanent Fund Dividend program in the future, an outcome that is heartily supported by many Alaskans.

Making these changes in the Constitution, rather than in Alaska Statutes adds an additional layer of protection to the fund because the Constitution can only be changed with a vote of the people.

If passed, HJR 26 would place an initiative on the next statewide election ballot that would propose the following three changes to Alaska's Constitution:

- Remove the provision that "all income be deposited in the general fund unless otherwise provided by law"
- Add a provision that would not allow appropriations from the Fund to exceed 5 percent of the average market value of the Fund over five years
- Add a provision that would consider the money in the earnings reserve account to be part of the Permanent Fund



**Alaska Permanent Fund Corporation  
Percent of Market Value talking points  
April, 2004**

**Realized income** is the cash income from assets (rent, interest payments, stock dividends) and the net profits from the sale of assets.

**Unrealized gains** are the increases in the value of held assets.

**Principal** is comprised of the contributions to the Fund from mineral royalties and legislative appropriations. Unrealized gains are accounted for as principal until they are realized.

**How is the current method broken?**

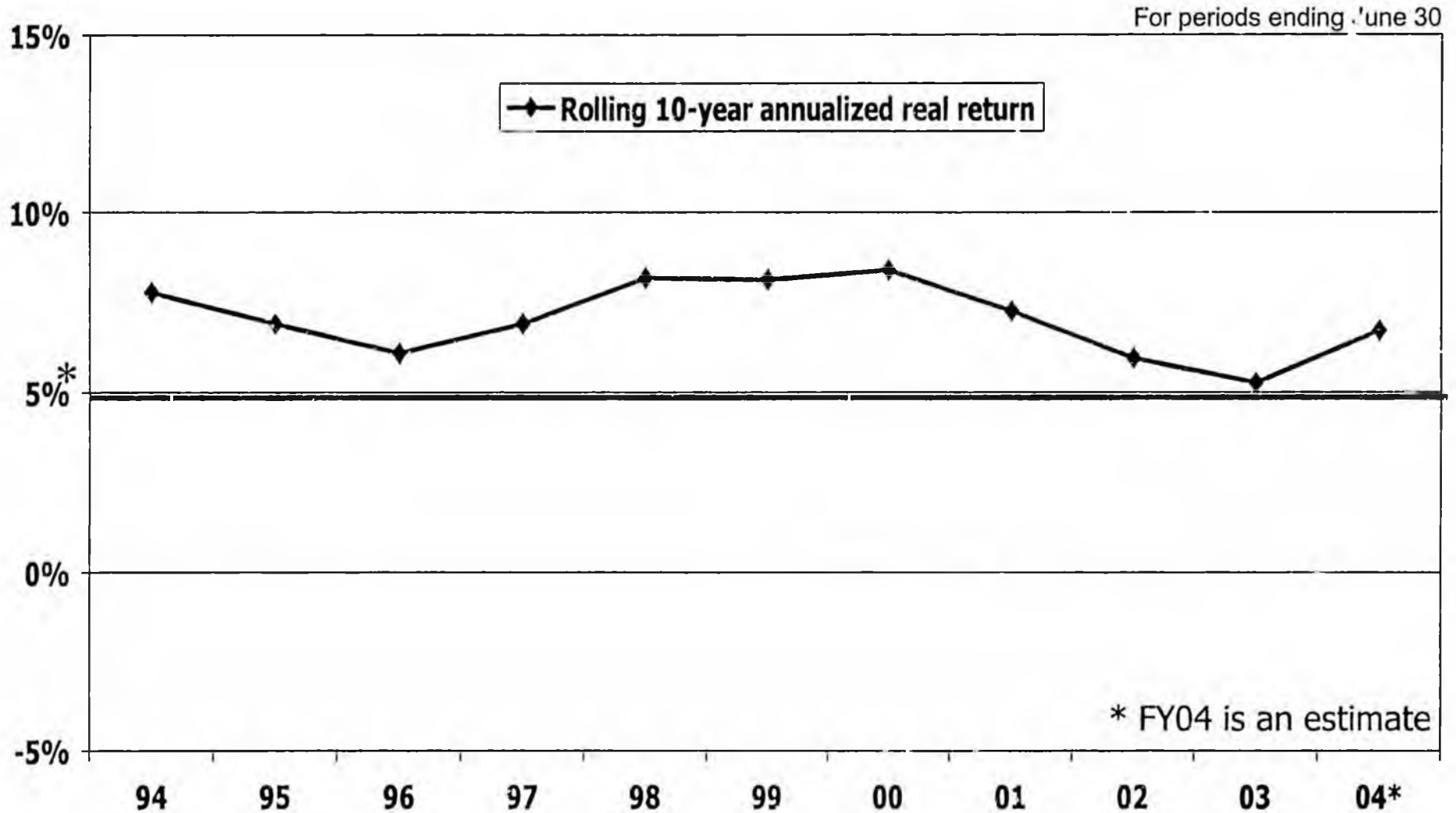
- It allows over-spending in good years (in some years up to 20% of the Fund has been available for appropriation).
- Only part of the principal is protected from spending.
  - Unrealized gains become realized income when an asset is sold, and move from principal to earnings.
- It creates the possibility of reduced or zero payouts for dividends or other purposes in bad years.
- Inflation proofing is optional, requiring an annual legislative appropriation.
- Payouts are now based on realized income and are incompatible with the Fund's current investments.
  - When the Fund was created it was invested entirely in bonds, and a payout method based on realized income made sense.
  - Now the Fund is invested in stocks and real estate in addition to bonds, assets that increase in value as well as providing some cash income, and that would be compatible with a POMV payout method.

**How does POMV provide the solution?**

- An annual spending limit of no more than 5% of the total value of the Fund will protect the entire Fund from overspending.
- A POMV payout method would provide more stable and predictable payout amounts from year to year, even in down market years.
- Inflation proofing is inherent and no longer requires an appropriation.
  - The Fund is invested for a 5% real rate of return after inflation. If 5% is withdrawn, the increase in value due to inflation will remain in the Fund.
- A POMV payout method based on the total Fund value is compatible with Fund's current investments.



# Rolling 10-year real return – Fiscal year



ACCOUNTABILITY

FOR ALASKANS, FOR ALASKANS

Provided by PFC 5/6/04



*Alaska Permanent Fund Corporation*

Financial projection of the Alaska Permanent Fund under a POMV spending limit and payouts designated in House Bill 298, beginning in FY05.

\$ millions (except per person dividend)

	<u>FY05</u>	<u>FY06</u>	<u>FY07</u>	<u>FY08</u>	<u>FY09</u>	<u>FY10</u>	<u>FY11</u>	<u>FY12</u>	<u>FY13</u>	<u>FY14</u>	<u>FY15</u>
<b>POMV - 5% (beginning in FY05)</b>											
Contributions & appropriations (principal)	23,844	24,135	24,370	24,595	24,819	25,042	25,263	25,475	25,683	25,878	26,066
Unrealized appreciation/depreciation on assets	3,467	3,515	3,437	3,595	3,590	3,801	3,814	4,057	4,072	4,333	4,567
Realized earnings account (after payouts)	1,864	2,677	3,641	4,371	5,254	5,941	6,846	7,550	8,504	9,242	10,034
<b>Total market value end of year (after payouts)</b>	<b>29,175</b>	<b>30,327</b>	<b>31,447</b>	<b>32,561</b>	<b>33,633</b>	<b>34,784</b>	<b>35,923</b>	<b>37,082</b>	<b>38,258</b>	<b>39,452</b>	<b>40,666</b>
5 year average market value lagged one	26,323	26,875	28,015	29,684	31,507	32,814	33,999	35,188	36,385	37,590	38,807
Total available for appropriation	1,316	1,344	1,401	1,484	1,575	1,641	1,700	1,759	1,819	1,879	1,940
APFC management costs	43	44	45	47	48	50	51	53	54	56	57
<b>Payout after APFC costs:</b>											
payout 50% lump sum dividend	637	650	678	719	764	796	824	853	883	912	941
payout 45% for public education	573	585	610	647	688	716	742	768	795	821	847
payout 5% for municipal dividend	64	65	68	72	76	80	82	85	88	91	94
<b>Per person dividend</b>	<b>\$ 1,010</b>	<b>\$ 1,030</b>	<b>\$ 1,070</b>	<b>\$ 1,130</b>	<b>\$ 1,200</b>	<b>\$ 1,240</b>	<b>\$ 1,280</b>	<b>\$ 1,320</b>	<b>\$ 1,360</b>	<b>\$ 1,400</b>	<b>\$ 1,440</b>

SENATE FINANCE COMMITTEE

SIGN-IN

**HJR 26-CONST. AM: PF APPROPS/INFLATION-PROOFING**

✓ NAME: Bob Bartholomew Subject/Bill No: HJR 26  
Co./Dept./Title: Permanent Fund Corp. Phone: 465-3663  
Address: \_\_\_\_\_ Zip: \_\_\_\_\_

Do you wish to testify?  Yes  No  Respond To Questions

NAME: \_\_\_\_\_ Subject/Bill No: \_\_\_\_\_  
Co./Dept./Title: \_\_\_\_\_ Phone: \_\_\_\_\_  
Address: \_\_\_\_\_ Zip: \_\_\_\_\_

Do you wish to testify?  Yes  No  Respond To Questions

NAME: \_\_\_\_\_ Subject/Bill No: \_\_\_\_\_  
Co./Dept./Title: \_\_\_\_\_ Phone: \_\_\_\_\_  
Address: \_\_\_\_\_ Zip: \_\_\_\_\_

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Co./Dept./Title: \_\_\_\_\_ Phone: \_\_\_\_\_  
Address: \_\_\_\_\_ Zip: \_\_\_\_\_

Do you wish to testify?  Yes  No  Respond To Questions