

SB

326

SFIN

FILE

SENATE FINANCE COMMITTEE REPORT

DATE: 3/5/04

MAR 29 2004
SENATE FINANCE
COMMITTEE

FURTHER:

DATE TURNED IN TO OFFICE: 29 March 2004

Finance Committee considered

SENATE BILL NO. 326

SB 326 PERMANENT FUND INVESTMENTS

"An Act relating to investments of Alaska permanent fund assets; and providing for an effective date."

and recommends:

- be replaced with _____ CS _____ (_____)
- adopt previous _____ CS SB 326 (STF)
- attached amendment(s)
- adopt Letter of Intent by _____ Committee
- further referral to _____ Committee

Senate Bill:	
<input checked="" type="checkbox"/>	Same Title
<input type="checkbox"/>	New Title
House Bill:	
<input type="checkbox"/>	Same Title
<input type="checkbox"/>	Technical Title Change
<input type="checkbox"/>	New Title w/ SCR # _____

NEW FISCAL NOTE(S):

Department	Date	Fiscal	Indet.	Zero.	FN#

PREVIOUS FISCAL NOTE(S):

Department	Date	Fiscal	Indet.	Zero	FN#
Revenue	9/01/04			✓	#1

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>			✓	
COCHAIR: <i>[Signature]</i>	✓			
COCHAIR: <i>[Signature]</i>	✓			

CS FOR SENATE BILL NO. 326(STA)
IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-THIRD LEGISLATURE - SECOND SESSION

BY THE SENATE STATE AFFAIRS COMMITTEE

Offered: 3/5/04
Referred: Finance

Sponsor(s): SENATE RULES COMMITTEE BY REQUEST OF THE LEGISLATIVE BUDGET AND
AUDIT COMMITTEE

A BILL
FOR AN ACT ENTITLED

1 "An Act relating to investments of Alaska permanent fund assets; and providing for an
2 effective date."

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

4 * Section 1. AS 37.13.120(e) is amended to read:

5 (e) The corporation may not borrow money or guarantee from principal of the
6 fund the obligations of others except as provided in this subsection. With respect to
7 [REAL PROPERTY] investments of the fund, the corporation may, through an entity
8 in which the investment is made, borrow money if the borrowing is without recourse
9 to the corporation and the fund.

10 * Sec. 2. AS 37.13.120(k) is amended to read:

11 (k) The board shall establish and from time to time as necessary modify
12 guidelines for the investment of the assets of the fund. Before adoption of any
13 guidelines, the guidelines shall be reported to the Legislative Budget and Audit
14 Committee for review and comment. Notwithstanding (g), (h), and (j) of this section

1 or the percentage investment limitations under (i) of this section and so long as doing
2 so satisfies the prudent-investor rule under (a) of this section, the board may invest up
3 to 10 [FIVE] percent of the total assets of the fund in either or a combination of the
4 following:

5 (1) other types of investments not specifically listed in (g) of this
6 section;

7 (2) categories of investment subject to the percentage investment
8 limitations established in (i) of this section, even though investing additional assets in
9 a category will cause the aggregate investment in the category to exceed the applicable
10 percentage limitation.

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

REPORTED OUT
MAR 29 2004
SENATE FINANCE
COMMITTEE

FISCAL NOTE

STATE OF ALASKA
2004 LEGISLATIVE SESSION

Fiscal Note Number: 1
Bill Version: CSSB 326(STA)
(S) Publish Date: 3/5/04

Revision Date/Time (Note if correction): _____ Dept. Affected: Revenue
Title Permanent Fund Investments RDU AK Permanent Fund Corporation
Component AK Permanent Fund Corporation
Sponsor Rules by request of LBA
Requester Senate State Affairs 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						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

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 (Specify Type--Do not abbreviate)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

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)

The existing manager fee budget of \$40 million is sufficient to cover any changes in investments under this legislation.

Prepared by: Robert D. Storer, Executive Director Phone 465-2047
Division Alaska Permanent Fund Corporation Date/Time 2/24/04 9:37 AM
Approved by: Steve Porter, Deputy Commissioner Date 2/6/2004
Agency Department of Revenue



Alaska Permanent Fund Corporation
801 West 10th Street, Suite 302 Juneau, AK 99801
Tel: (907) 465-2047 Fax: (907) 586-2057

Sponsor statement for SB 326

Background

Alaska Statute 37.13.120 provides a list of investment guidelines for the Alaska Permanent Fund, and the Fund's Trustees make investment decisions within these guidelines. Sometimes it is necessary to update the Fund's statutes as investment practices evolve. Periodically the Trustees bring these proposed changes to the Legislature.

In 1999 the Legislature passed HB 156, a bill that made a number of necessary changes to the statutes. One change was the creation of a "basket clause" in AS 37.13.120(k). This clause allows the Trustees to invest up to 5% of the Fund in investments not included in the allowed statutory list, but that are appropriate under the prudent investor rule. The basket clause may also be used for allowed investments in which the Fund has reached its statutory limitation.

However the alternative investments allowed under the basket clause may conflict with the investments not allowed under the statutory list. AS 37.13.120(e) prevents the Fund from borrowing money against assets other than real estate to leverage an investment. AS 37.13.120(h) restricts the situations in which Fund assets may be invested in futures contracts. AS 37.13.120(j) bars investing in any debt instrument on which an interest payment has been defaulted in the preceding five years.

Many alternative investments, such as hedge funds, use one or more of the methods restricted in (e), (h) and (j) as part of their overall investment strategy. The Permanent Fund could not make these investments under current statutes, despite the fact that they might represent sound investment opportunities.

Senate Bill 326

SB 326 achieves two objectives. The first is to provide clean-up language for AS 37.13.120(e) and (k), in part by explicitly stating that the investments restricted under AS 37.13.120(h) and (j) are allowed under the basket clause. According to transcripts of committee hearings, the Legislature was aware when it created the basket clause, that it would be used for these types of alternative investments. The change in this bill would clean up the discrepancy in language between the sections while still maintaining the original legislative intent.

The second would expand the basket clause from 5% to 10%. This is necessary because the 5% limit is too small to allow the Trustees enough flexibility to keep up with changes in investment practices. For example, the Trustees are planning on placing up to 3% of the Fund in private equity investments. If these are successful investments, the value will grow to 4% or more of the Fund, leaving less than 2% of the basket clause for other investments.



Alaska Permanent Fund

Senate Finance Committee

Senate Bill 326

Investment Flexibility

ACCOUNTABILITY

TO ALASKANS FOR ALASKANS



Summary of Fund's statute changes

1980 – SB 161, Sponsored by Sen. Tim Kelly, Sen. George Hohman, Sen. Mike Colletta, and Sen. John Sacket

SB 161 created the Alaska Permanent Fund Corporation to manage the Permanent Fund and started the existing statutory list of allowed investments. This list extended beyond the Fund's initial investment limitation of Treasury bonds to include corporate bonds, certificate of deposits and bankers acceptances. The list initially allowed the Permanent Fund to invest in shares of savings and loan associations, but this provision has since been removed.

1982 – SB 684, sponsored by Gov. Jay Hammond

SB 684 allowed the Permanent Fund to invest in common stocks, partial ownership of real estate properties (not to exceed 40%), loans for commercial real estate and deposits of US dollars held overseas.

1989- HB 69, sponsored by Gov. Steve Cowper

HB 69 gave the APFC authority to invest in non-domestic (International) stocks and bonds.

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3/29/04



Summary of statute changes (cont.)

1992 – SB 39, sponsored by the Senate Finance Committee

SB 39 gave the APFC authority to invest in A rated corporate bonds to a maximum of 5%. Prior to this change, the Fund could only be invested in bonds rated AA or higher.

1994 – HB 373, sponsored by the Legislative Budget and Audit Committee

HB 373 allowed the Fund to own up to 100% in real estate properties worth less than \$150 million, and up to 67% in properties worth greater than \$150 million.

1996 – HB 525, sponsored by the House Finance Committee

HB 525 gave the APFC authority to invest in corporate bonds rated BBB or higher.

1999 – HB 156, sponsored by the Legislative Budget and Audit Committee

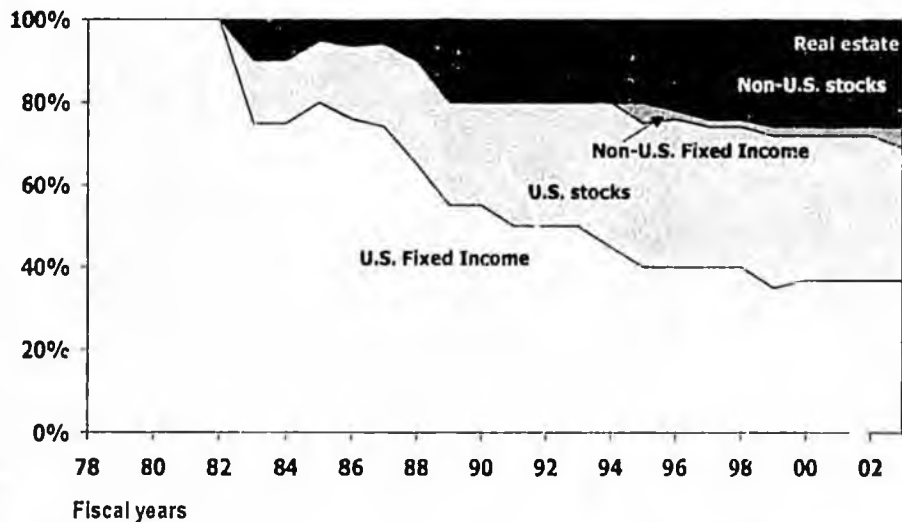
HB 156 allowed the Fund to leverage real estate investments and increased asset allocation limit for stocks to 55% of the total market value of the Fund. HB 156 also created the "basket clause" that allows up to 5% of the Fund to be invested in alternative investments or to be applied to existing asset allocations to expand their limits. In addition, HB 156 allowed the Permanent Fund to be the sole owner of any real estate property, regardless of value.

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Fund's historical asset allocation



ACCOUNTABILITY ⁴

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Benefits of proposed changes

- Investment flexibility
- Increased returns
- Increased diversification

ACCOUNTABILITY 5

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Potential questions

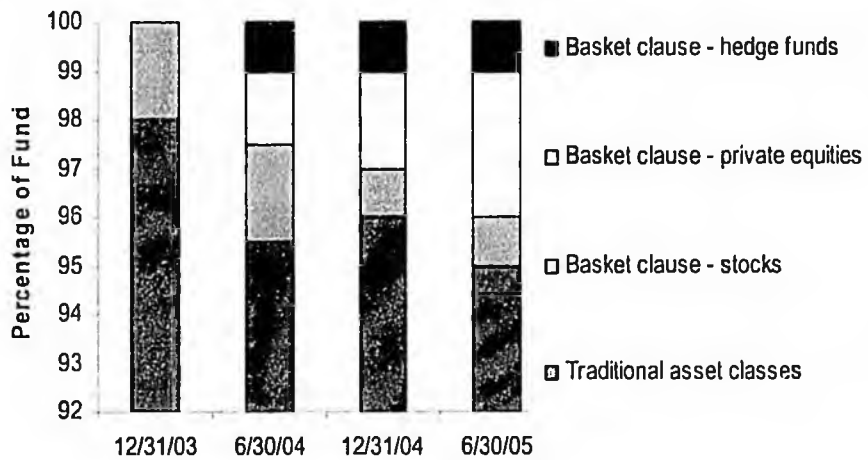
- Too much risk?
- How will the Board of Trustees use this flexibility?
- Derivatives?

ACCOUNTABILITY 6

TO ALASKANS FOR ALASKANS



Permanent Fund asset allocation



ACCOUNTABILITY 7

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SENATE COMMITTEE REPORT
First Committee of Referral

DATE: 2/13/04

FURTHER: Finance

Date of 5-Day Notice: 2/19/04
 (in accordance with Uniform Rule 23)

DATE TURNED
 IN TO OFFICE: 3/5/04

State Affairs Committee considered SENATE BILL NO. 326

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<input type="checkbox"/>	New Title w/ SCR # _____

NEW FISCAL NOTE(S):

Department	Date	Fiscal	Indet.	Zero	FN#
<u>REV</u>	<u>2/24/04</u>			<input checked="" type="checkbox"/>	<u>1</u>

PREVIOUS FISCAL NOTE(S):

Department	Date	Fiscal	Indet.	Zero	FN#

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	Do PASS	Do NOT PASS	No REC	AMEND
<i>Cowdery</i> <u>John J. Cowdery</u>	<input checked="" type="checkbox"/>			
<u>Bertie R. Steinhilber</u>			<input checked="" type="checkbox"/>	
<i>G. Stevens</i> CHAIR: <u>[Signature]</u>			<input checked="" type="checkbox"/>	

SENATE FINANCE COMMITTEE

SIGN-IN

SB 326-PERMANENT FUND INVESTMENTS

NAME: Bob STORER Subject/Bill No: SB 326
Co./Dept./Title: APFC Phone: _____
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: _____

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