

SJR

18

SENATE COMMITTEE REPORT

First Committee of Referral

DATE: 4/17/03

FURTHER: Judiciary
Finance

Date of 5-Day Notice: 4/24/03
(in accordance with Uniform Rule 23)

DATE TURNED
IN TO OFFICE: 5/7/03

State Affairs Committee considered SENATE JOINT RESOLUTION NO. 18

SJR 18 CONST. AM: PF APPROPS/INFLATION-PROOFING

Proposing amendments to the Constitution of the State of Alaska relating to limiting appropriations from and inflation-proofing the Alaska permanent fund by establishing a percent of market value spending limit.

and recommends:

- be replaced with _____ CS SJR 18 (STA)
- 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
- new: SCR # _____

NEW FISCAL NOTE(S):

Department	Date	Fiscal	Zero	FN#
<u>COG</u>	<u>4/24/03</u>	<input checked="" type="checkbox"/>		<u>1</u>
<u>DOR</u>	<u>4/29/03</u>		<input checked="" type="checkbox"/>	<u>2</u>

PREVIOUS FISCAL NOTE(S):

Department	Date	Fiscal	Zero	FN#

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	DO PASS	DO NOT PASS	NO REC	AMEND
<u>[Signature]</u>			<input checked="" type="checkbox"/>	
<u>[Signature]</u>			<input checked="" type="checkbox"/>	
<u>[Signature]</u>	<input checked="" type="checkbox"/>			
CHAIR: <u>[Signature]</u>			<input checked="" type="checkbox"/>	

23-LS1007D
Cook
5/6/03

CS FOR SENATE JOINT RESOLUTION NO. 18()
IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY

Offered:
Referred:

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

A RESOLUTION

1 Proposing amendments to the Constitution of the State of Alaska relating to and limiting
2 appropriations from the Alaska permanent fund based on an averaged percent of the
3 fund market value to protect the fund from inflation and assure that the real value of
4 the fund will be preserved over the long term.

5 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

6 * Section 1. Article IX, sec. 15, Constitution of the State of Alaska, is amended to read:

7 Section 15. Alaska Permanent Fund. (a) At least twenty-five per cent of all
8 mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing
9 payments and bonuses received by the State shall be placed in a permanent fund,
10 Except as appropriated under (b) of this section, money in the permanent fund [,
11 THE PRINCIPAL OF WHICH] shall be used only for those income-producing
12 investments specifically designated by law as eligible for permanent fund investments.
13 [ALL INCOME FROM THE PERMANENT FUND SHALL BE DEPOSITED IN
14 THE GENERAL FUND UNLESS OTHERWISE PROVIDED BY LAW.]

15 * Sec. 2. Article IX, sec. 15, Constitution of the State of Alaska, is amended by adding a

1 new subsection to read:

2 (b) To protect the permanent fund from the effects of inflation and thereby
3 assure that the real value of the permanent fund will be preserved over the long term,
4 appropriations from the permanent fund for a fiscal year may not exceed five percent
5 of the average of the market values of the fund on June 30 for the first five of the six
6 fiscal years immediately preceding that fiscal year.

7 * Sec. 3. Article XV, Constitution of the State of Alaska, is amended by adding a new
8 section to read:

9 Section 30. Transition. On the effective date of the 2004 amendment relating
10 to the Alaska Permanent Fund (art. IX, sec. 15), the unencumbered, unappropriated
11 balance of the earnings reserve account established under AS 37.13.145(a) is added to
12 the balance in the Alaska Permanent Fund.

13 * Sec. 4. The amendments proposed by this resolution shall be placed before the voters of
14 the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the
15 State of Alaska, and the election laws of the state.

I am an enthusiastic supporter of a 5 POMV payout because it constitutionally inflation-proofs the entire permanent fund. Right now, only the principal is inflation-proofed, and that is done by statute, and after the dividend program is funded.

The second reason I support 5 POMV is that it sets a spending limit. Under the current distribution methodology, the legislature may appropriate the entire earnings reserve account. 5 POMV forces us to resist the temptation to appropriate too much money when the fund is flush, yet makes distributions available in lean years.

Third, an annual payout based on market value is compatible with the fund's diversified portfolio that is managed, in conformance to industry standards, for long-term value over short-term gain. The current distribution method, based on income, was appropriate 20 years ago when the fund was invested primarily in bonds. A 5% payout is generally recognized by large fund managers as the highest sustainable payout, beyond which the real value of the fund would diminish over time. This approach protects the value of the fund and provides a limited, predictable, and sustainable revenue stream.

The permanent fund trustees combined the fund's principal and income in one pot of money to make 5 POMV work effectively. Segregating the principal interferes with value-management goals by exerting pressure to produce short-term income for dividends or other distributions during periods of poor performance. Segregating the principal also tempts the legislature to provide for a greater than 5% payout when the earnings reserve account is flush, as in HJR 1. This is just what POMV is designed to avoid.

How the legislature chooses to divide the payout is an important question. 5 POMV is a management tool, not a distribution plan. However, the two are intrinsically linked. The use of the payout should not be set in the constitution because this is an appropriation issue better left to the legislative process. Alaska Statutes 37.13.140 and 37.13.145 relating to permanent fund income and income distribution must be amended to conform to 5 POMV because they will no longer apply as written. I urge you to establish a comparable dividend formula when you change

these statutes. 5 POMV is too valuable an asset to risk voter rejection by threatening their dividend checks.

For modeling purposes, we assume an 8% total return, 3% inflation, and a 5% real return. Under the existing statutes, 50% of the income available for distribution, or 4%, goes to the dividend program. Inflation-proofing then takes 3% of the total return, leaving 1% for other legislative appropriation, which has never been touched. For this distribution to work under POMV, 80% of the 5% payout must be allocated to the dividend program to provide a comparable amount of money. Inflation-proofing of 3% has already been accounted for by establishing a 5% payout limit, leaving 20% of the payout for other legislative appropriation, which is the same as the 1% under the existing distribution statutes. 50% of the money available for distribution after inflation-proofing cannot provide the same amount for dividends as 50% of the money available for distribution before inflation-proofing. 50% of 8 translates to 80% of 5.

It is time to move forward on a fiscal plan. This constitutional amendment combined with a change to the statutes securing 80% of the annual payout for dividends is a critical step. It is a three-way win. The permanent fund gets a better management framework, the legislature gets a predictable revenue stream, and the people keep their dividend formula.

Thank you.

Mary Griswold

Homer

Methods to determine funds available for appropriation:

Five key differences between the Status quo and the proposed Percent of Market Value (P.O.M.V.)

A presentation by the Alaska Permanent Fund Corporation
to the House Ways and Means Committee

April 21, 2003

Note: This presentation supports the changes proposed in SJA 18.



Five key differences between the status quo and POMV

1. POMV offers constitutional inflation-proofing protection of the entire Fund. The status quo statutorily inflation-proofs Fund principal.
2. POMV is a spending limit. It limits funds available for appropriations to real income over time. Under the status quo, the entire earnings reserve may be appropriated.
3. During volatile markets, POMV offers greatly improved stability in year-to-year amounts available for appropriation as compared to the status quo.



Differences between the status quo and POMV

4. POMV is compatible with the Fund's diversified, long-term investment strategy of achieving a 5% real rate of return over time. The status quo was designed a quarter century ago for a Fund invested 100% in bonds.
5. Predictable annual appropriations are provided under POMV. Under the status quo, it is not known whether funds will be available for appropriation in any given year.





Alaska Permanent Fund Corporation
 HJR 26 - Financial projection comparison of the Alaska Permanent Fund
 under status quo versus POMV spending limit, beginning in FY05.

\$ millions

Status Quo	-----projected-----										
	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13
Total Return	-3.42%	7.38%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%
Principal - end of year (after payouts)	22,348	23,268	24,149	25,057	25,988	26,937	27,910	28,899	29,899	30,918	31,956
Realized earnings reserve (after payouts)	633	398	648	1,102	1,581	2,028	2,446	2,886	3,358	3,865	4,487
Unrealized earnings reserve	(632)	118	610	960	1,232	1,468	1,708	1,929	2,135	2,332	2,434
Total earnings reserve - end of year (after payouts)	0	516	1,258	2,062	2,813	3,496	4,154	4,816	5,493	6,197	6,921
Total Market Value End of Year (after payouts)	<u>22,348</u>	<u>23,784</u>	<u>25,407</u>	<u>27,118</u>	<u>28,801</u>	<u>30,433</u>	<u>32,065</u>	<u>33,715</u>	<u>35,392</u>	<u>37,115</u>	<u>38,876</u>
Annual net income	(851)	1,620	1,775	1,897	2,026	2,152	2,275	2,397	2,521	2,647	2,776
Dividend (lump sum) - Status Quo	686	510	409	442	597	766	887	979	1,059	1,131	1,209
Transfer status quo Inflation-proofing (ER to principal)	102	590	612	635	659	683	707	732	758	783	810

POMV - 5% (beginning in FY05)	-----projected 5% POMV beginning in FY05-----										
	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13
Total Return			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>23,784</u>	<u>24,581</u>	<u>25,429</u>	<u>26,307</u>	<u>27,186</u>	<u>28,078</u>	<u>28,978</u>	<u>29,881</u>	<u>30,795</u>	<u>31,717</u>
Annual net income			1,775	1,834	1,898	1,963	2,028	2,094	2,161	2,228	2,295
POMV Payout available for appropriation in lump sum			1,235	1,243	1,274	1,329	1,380	1,426	1,473	1,520	1,568
5 year average market value			24,706	24,854	25,480	26,576	27,608	28,526	29,463	30,409	31,363

Assumptions: Callan Associates 2003 Capital Market Assumptions, APFC 2003 asset allocation, Spring 2003 revenue forecast, financial statements through 3/31/03. All payouts are assumed to happen at fiscal year end, all dollar values in millions.



Alaska Permanent Fund Corporation

Calculation of annual effective rates of 5% POMV spending limit
\$ millions

	<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>
Payout based on 5 year moving average	1,235	1,243	1,274	1,329	1,380	1,426	1,473	1,520	1,568
Ending market value (after payout)	24,581	25,429	26,307	27,186	28,078	28,978	29,881	30,795	31,717
Ending market value (pre payout)	25,816	26,672	27,581	28,515	29,458	30,404	31,354	32,315	33,285
Effective payout rate *	4.78%	4.66%	4.62%	4.66%	4.69%	4.69%	4.70%	4.71%	4.71%
	<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>
Payout based on 5 year moving average	1,235	1,243	1,274	1,329	1,380	1,426	1,473	1,520	1,568
less APFC costs to manage the Fund	38	39	41	42	43	44	46	47	49
5% available for spending after deducting APFC costs	1,197	1,203	1,233	1,287	1,337	1,382	1,427	1,473	1,520
Effective rate after deducting APFC costs *	4.64%	4.51%	4.47%	4.51%	4.54%	4.55%	4.55%	4.56%	4.57%
APFC costs to manage the Fund in %	0.16%	0.16%	0.16%	0.16%	0.16%	0.16%	0.16%	0.16%	0.16%

* Note: The effective rate is defined as the payout over the ending market value of the Fund (pre-payout) expressed as a percentage.

23-LS1006Y
Cook
4/29/03

CS FOR HOUSE JOINT RESOLUTION NO. 26()
IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY

Offered:
Referred:

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

A RESOLUTION

1 **Proposing amendments to the Constitution of the State of Alaska relating to and limiting**
2 **appropriations from the Alaska permanent fund based on an averaged percent of the**
3 **fund market value to protect the fund from inflation and ensure that the real value of**
4 **the fund is preserved.**

5 **BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

6 *** Section 1.** Article IX, sec. 15, Constitution of the State of Alaska, is amended to read:

7 **Section 15. Alaska Permanent Fund.** (a) At least twenty-five per cent of all
8 mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing
9 payments and bonuses received by the State shall be placed in a permanent fund.
10 Except as appropriated under in (b) of this section, money in the permanent fund
11 [, THE PRINCIPAL OF WHICH] shall be used only for those income-producing
12 investments specifically designated by law as eligible for permanent fund investments.
13 [ALL INCOME FROM THE PERMANENT FUND SHALL BE DEPOSITED IN
14 THE GENERAL FUND UNLESS OTHERWISE PROVIDED BY LAW.]

15 *** Sec. 2.** Article IX, sec. 15, Constitution of the State of Alaska, is amended by adding a

1 new subsection to read:

2 (b) To protect the permanent fund from the effects of inflation and thereby
3 assure that the real value of the permanent fund will be preserved, appropriations from
4 the permanent fund for a fiscal year may not exceed five percent of the average of the
5 market values of the fund on June 30 for the first five of the six fiscal years
6 immediately preceding that fiscal year.

7 * **Sec. 3.** Article XV, Constitution of the State of Alaska, is amended by adding a new
8 section to read:

9 **Section 30. Transition.** On the effective date of the 2004 amendment relating
10 to the Alaska Permanent Fund (art. IX, sec. 15), the unencumbered, unappropriated
11 balance of the earnings reserve account established under AS 37.13.145(a) is added to
12 the balance in the Alaska Permanent Fund.

13 * **Sec. 4.** The amendments proposed by this resolution shall be placed before the voters of
14 the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the
15 State of Alaska, and the election laws of the state.

LEGISLATIVE BUDGET & AUDIT COMMITTEE

REPRESENTATIVE RALPH SAMUELS, CHAIR

Sponsor Statement for SJR 18

Senate 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, SJR 18 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

Email: Representative_Ralph_Samuels@legis.state.ak.us

Session: Alaska State Capitol, Juneau, Alaska 99801-1182 • Phone: (907) 465-2095 Fax: (907) 465-3810
Interim: 716 W. 4th Ave., Anchorage, Alaska 99501-2133 • Phone: (907) 269-0240 Fax: (907) 269-0242

ALASKA PERMANENT FUND CORPORATION

RESOLUTION OF THE BOARD OF TRUSTEES OF THE
ALASKA PERMANENT FUND CORPORATION RELATING TO A
CONSTITUTIONAL AMENDMENT LIMITING APPROPRIATIONS FROM
AND INFLATION-PROOFING THE ALASKA PERMANENT FUND
BY ESTABLISHING A PERCENT OF MARKET VALUE SPENDING LIMIT

RESOLUTION 03-05

Preserving the real value of the money deposited into the Alaska Permanent Fund ("Fund") over the long term has been a public policy priority of the Board of Trustees ("Board") since the original Board was appointed over 20 years ago. In response to the Board's concerns in 1982 about the effects of inflation on the value of the Fund, the legislature adopted statutory inflation-proofing that same year. That change has successfully protected (by statute) the principal of the Fund for the past 20 years. After several years of review, the Board believes it is now time for the People of Alaska to make another decision that would: 1) constitutionally protect the current purchasing power of the whole Fund (both principal and income) against inflation; and 2) improve the rules governing distributions from the Fund.

To accomplish these goals, the Board has examined the use by various large endowment and public funds of a formula approach to establish appropriate limits on the size of payouts from those funds. This formula approach, generally referred to as a "percent of market value" ("POMV") spending limit, is applied by those funds in a manner that assures that, on average, only *real* income of a fund (i.e. income *net of inflation*) can be spent, thereby assuring that the real value of the contributions paid into the fund will not be touched. Because a POMV spending limit would provide for distributions from the Fund that are

predictable and limited, the Board believes that its use is in the best interest of the Fund and of the people of the State of Alaska.

The Board further believes that the best way to implement a POMV spending limit methodology for determining a level of distributions from the Fund that is predictable and limited is to amend the constitutional provision that established the Fund (Article IX, section 15 of the Alaska Constitution). Providing for a POMV spending limit in this manner would assure all Alaskans that the real value of the contributions to the Fund will be preserved for all time.

At the Board's request, APFC staff has presented a draft constitutional amendment for further discussion by the Board which, if adopted by the people of the State of Alaska, would provide for the following:

1. an annual limit on appropriations from the Fund of up to five percent of the total market value of the Fund, averaged over a period of five years;
2. using a five year period that allows the legislature and the governor to know before a fiscal year begins the exact amount that will be available for distribution from the Fund;
3. Fund income is part of the Fund, rather than being subject to appropriation by the legislature, as currently provided;
4. assures that the current statutory earnings reserve account established by AS 37.13.145 becomes part of the Fund when the constitutional amendment takes effect; and
5. the current references to "principal" and "income" are removed, as POMV ensures protection of the principal over the long-term through a constitutional spending limit.

The Board believes that this approach effectively balances the goal of providing for an annual distribution from the Fund that is predictable and limited with the long-term goal of protecting the real value of contributions to the Fund.

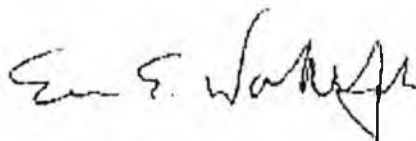
In addition, the Board believes strongly that implementing a POMV spending limit approach by constitutional amendment is such an important public policy goal that proposals for incorporating any other amendments to Article IX, section 15 which might in any way either lessen the chances of approval of such an amendment by the voters or undermine the legal status of the Fund should be rejected by the legislature.

Finally, the Board recognizes that implementation of a POMV spending limit methodology by constitutional amendment may necessitate changes to existing statutes that deal with the formula for determining and distributing the amount of the Fund that may be spent each year, including, but not necessarily limited to, payment of Permanent Fund Dividends and inflation-proofing the Fund. In anticipation of voter approval of a constitutional amendment providing for a POMV spending limit, the Board is hopeful that the legislature and the governor will work together to develop appropriate legislation to harmonize existing statutory provisions with the operation of the amendment and/or to adopt such new statutes as they may consider desirable. In this regard, the Board and APFC staff stand ready to provide any information or other assistance that may be helpful.

NOW, THEREFORE, BE IT RESOLVED by the Board of Trustees that the legislature of the State of Alaska, in consultation with the governor and the Board, are urged to consider and approve the proposal (dated 4/14/03) for a constitutional amendment that would implement a POMV spending limit mechanism that would provide an annual distribution from the Fund that is predictable and limited.

BE IT FURTHER RESOLVED by the Board of Trustees that the proposal for such an amendment be limited solely to implementation of the foregoing goal.

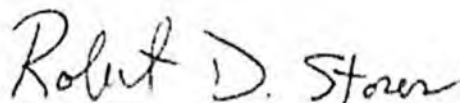
PASSED AND APPROVED by the Board of Trustees of the Alaska Permanent Fund Corporation this 14th day of April 2003.



Eric E. Wohlforth

Chair, Board of Trustees

ATTEST:



Robert D. Storer, Corporate Secretary

**Testimony before the
House Special Committee on Ways & Means
Clark S. Gruening
April 22, 2003**

Note: This testimony was for HJR 26, which is the companion bill for SJR 18.

Mr. Chairman and members of the House Special Committee on Ways & Means, thank you for the opportunity to discuss with you HJR 26, a proposed constitutional amendment for inflation-proofing the Alaska Permanent Fund.

Before speaking to how this proposal changes the way the Permanent Fund is inflation-proofed, I'd like to make some brief comments about how the Board came to recommend this change.

For 23 of the Fund's 27 years of existence, the APFC has been governed by a six-member Board of Trustees. Protecting the Fund against inflation has been the highest public policy goal of the Trustees since the original Board was appointed in 1980. The first Board testified to the legislature that the greatest threat to the permanence of the Fund is inflation. In response, the legislature adopted statutory inflation-proofing in 1982.

In more recent years, the Board has examined the use by various large endowments and public funds of a formula approach to determine the method and size of payouts from these funds. This approach is generally referred to as "percentage of market value" payouts or "POMV" for short.

The purpose of placing this formula in the state constitution is to protect the long-term real value of the Fund and to provide consistent and predictable distributions for the long-term. After considerable review and discussion, the Board recommended in February of 2001, a constitutional change in the form of

HJR 15 and SJR 13 which received committee hearings but did not come to the floor for a vote.

As in the prior proposal, the language in HJR 26 provides a spending limit on what can be currently spent or, in legislative parlance, appropriated. The existing constitutional language establishing the Alaska Permanent Fund only prohibits the appropriation of principal. In other words, anything but "principal" is income and can be spent.

Since the first Board of Trustees, 23 years ago, the Permanent Fund corporation has calculated principal as a notational number that simply equals the sum of the constitutionally mandated 25 percent of mineral deposits and the non-mandated (or voluntary) deposits the legislature has chosen to make. Principal does not vary or move up or down with the market.

Unlike the present statutory provision for inflation-proofing, HJR 26 provides for inflation-proofing of the entire Fund. But clearly, one of the most important reasons to support the proposal is that it would maximize distributions over the long term by establishing a percent of market value spending limit. By eliminating the distinction between principal and income, this proposal would also avoid the situation where market volatility on the down side prevents any distribution from the fund for any purpose, whether for dividends or anything else.

This is significant because since 1982, Alaska's fiscal picture has changed dramatically. The Alaska Permanent Fund can be reasonably expected to produce more future state revenue than any single Alaska resource -- more than oil or natural gas, more than fishing or any other natural resource.

Whatever future decisions are made by the legislature or the voters regarding the use of Fund earnings, the five percent payout of market value limit will assure complete and protected inflation-proofing while providing predictable and sustainable distributions over the long term.

In managing Alaska's fishery stocks, the only sensible choice is to avoid taking too much of any fish stock so that, over the long term, the harvest is maximized. Of course, over-harvesting can reap short-term rewards of more fish, but the inevitable result is, at best, fewer fish, and at worst, permanent impairment or destruction of a fisheries stock. The same is true for managing distributions from a large investment fund like the Alaska Permanent Fund.

I want to close by emphasizing two key points regarding the Board's proposed constitutional amendment. The first point is that if Alaska is going to have a Fund that is truly permanent, we must take those steps necessary to ensure permanence. This means investing for future generations as well as current generations. This will require commitment to basic principles of long-term investing.

But the critical flip side of a sound long-term investment strategy is a sound, sustainable, and predictable distribution plan – a plan that will sustain and provide benefits to each generation of Alaskans.

The second and last point I want to leave you with is that if the Permanent Fund is going to continue to serve each generation of Alaskans it has to be able to make distributions so that current generations receive some benefit while not

"over harvesting" the fund so that there is little or nothing left for future generations.

We all want to avoid, at all costs, defaulting to the position where the Constitutional Budget Reserve (or "CBR") is today. Within the next three to four years, the CBR is destined for extinction. As the investment horizon of the CBR steadily shortens, it will be necessary to keep the assets of the CBR in very short-term and less-profitable investments.

I believe that as the day of the CBR's demise grows near, the Trustees and staff of the Fund may have to seriously consider a shorter investment horizon for a significant portion of the Fund.

So, whether we liken the Alaska Permanent Fund to a resource industry like Alaska's fisheries, one thing is clear: the Alaska Permanent Fund can continue to import significant new money into our state year after year.

Properly invested and protected, the Alaska Permanent Fund will successfully convert the non-renewable petroleum wealth of our State into a permanent and substantial stream of revenue for generations after the last barrel of oil has been pumped.

Legislative passage and voter approval of the Board's proposed amendment would protect the ability of the Fund to be managed for the long-term and to continue to pour money into the Alaska economy over the long-term.

The proposed constitutional change before you in the form of HJR 26 is more compatible with the Fund's diversified, long-term investment strategy of achieving a five percent real rate of return over time. The present constitutional

language was designed over a quarter century ago for a Fund that was invested 100 percent in bonds.

I believe that succeeding generations will rightly view this proposed amendment with the same degree of appreciation and admiration as the original one Alaskans overwhelmingly approved 27 years ago. The Trustees believe that this proposal for complete and protected inflation-proofing makes ultimate good sense for Alaska's Permanent Fund and for Alaska's future.

FISCAL NOTE

STATE OF ALASKA
2003 LEGISLATIVE SESSION

Fiscal Note Number: _____
 Bill Version: SJR18
 () Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: Revenue
 Title Constitutional Amendment: BRU Permanent Fund Corp
Permanent Fund Appropriations Component Permanent Fund Corp
 Sponsor Senate Rules
 Requester Senate State Affairs Component No. 109

Expenditures/Revenues (Thousands of Dollars)

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

OPERATING EXPENDITURES	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
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 (FY2003) cost: 0.0
 Check this box (X) if funding for this bill is included in the Governor's FY 2004 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

SJR 18 would ask voters in the next general election whether to approve a constitutional amendment that would limit annual appropriations to no more than 5% of the average year-end market value of the Fund for the preceding five years.

SJR 18 would not affect the budgeted costs to manage and invest the Permanent Fund, nor would it 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, Executive Director Phone (907)465-2047
 Division Alaska Permanent Fund Corporation Date/Time 4/25/03 5:00 PM
 Approved by: William Corbus, Commissioner Date 4/29/2003
 Agency Department of Revenue



Alaska Permanent Fund Corporation
 SJR 18 - Financial projection comparison of the Alaska Permanent Fund
 under status quo versus POMV spending limit, beginning in FY05.

\$ millions

Status Quo	-----projected-----										
	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13
Total Return	-3.42%	7.38%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%	7.60%
Principal - end of year (after payouts)	22,348	23,268	24,149	25,057	25,988	26,937	27,910	28,899	29,899	30,918	31,956
Realized earnings reserve (after payouts)	633	398	648	1,102	1,581	2,028	2,446	2,886	3,358	3,865	4,487
Unrealized earnings reserve	(632)	118	610	960	1,232	1,468	1,708	1,929	2,135	2,332	2,434
Total earnings reserve - end of year (after payouts)	0	516	1,258	2,062	2,813	3,496	4,154	4,816	5,493	6,197	6,921
Total Market Value End of Year (after payouts)	<u>22,349</u>	<u>23,784</u>	<u>25,407</u>	<u>27,118</u>	<u>28,801</u>	<u>30,433</u>	<u>32,065</u>	<u>33,715</u>	<u>35,392</u>	<u>37,115</u>	<u>38,876</u>
Annual net income	(851)	1,620	1,775	1,897	2,026	2,152	2,275	2,397	2,521	2,647	2,776
Dividend (lump sum) - Status Quo	686 *	510	409	442	597	766	887	979	1,059	1,131	1,209
Transfer status quo inflation-proofing (ER to principal)	102	590	612	635	659	683	707	732	758	783	810

* The APFC FY03 projected dividend, paid to Alaska citizens in October, 2003 is subject to available earnings reserve. The volatility in the stock market has taken earnings reserve to zero or below several times this fiscal year. If the earnings reserve balance is zero or negative on 6/30/03, no dividend distribution will be paid to the Department of Revenue.

POMV - 5% (beginning in FY05)	-----projected 5% POMV beginning in FY05-----										
	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13
Total Return			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>23,784</u>	<u>24,581</u>	<u>25,429</u>	<u>26,307</u>	<u>27,186</u>	<u>28,078</u>	<u>28,978</u>	<u>29,881</u>	<u>30,795</u>	<u>31,717</u>
Annual net income			1,775	1,834	1,898	1,963	2,028	2,094	2,161	2,228	2,295
POMV Payout available for appropriation in lump sum			1,235	1,243	1,274	1,329	1,380	1,426	1,473	1,520	1,568
5 year average market value			24,706	24,854	25,480	26,576	27,608	28,526	29,463	30,409	31,363

Assumptions: Callan Associates 2003 Capital Market Assumptions, APFC 2003 asset allocation, Spring 2003 revenue forecast, financial statements through 3/31/03. All payouts are assumed to happen at fiscal year end, all dollar values in millions.