

ALASKA LEGISLATURE COMMITTEE FILES 2001-2002 00/2

10299 HOUSE JUDICIARY



Alaska Permanent Fund Corporation  
P.O. Box 25500 Juneau, Alaska 99802-5500  
(907) 465-2047

**MEMORANDUM**

APR 11 2001

**DATE:** April 11, 2001

**TO:** Representative Norm Rokeberg, Chair  
House Judiciary Committee

**FROM:** Robert D. Storer, (RS)  
Executive Director

**SUBJECT:** House Joint Resolution 15 - Permanent Fund  
Constitutional Inflation-Proofing Amendment

This is to request a hearing at your earliest convenience on House Joint Resolution 15, "Proposing amendments to the Constitution of the State of Alaska relating to inflation-proofing the permanent fund."

HJR 15 accomplishes inflation-proofing by constitutionally limiting the annual payout of Fund income to no more than 5 percent of the Fund's five-year average market value. This amount comprises all of the Fund's expected "real," i.e., inflation-adjusted, income. For example, the Board's current asset allocation is designed to earn 8.25 percent annually and inflation is expected to average 3.25 percent. By retaining that difference between what is earned and what is paid out, the purchasing power of the Permanent Fund is fully protected against inflation.

The Board is unanimous in its support for this proposal. They believe its benefits are compelling:

1. Provides constitutional protection against inflation for the total Permanent Fund, thereby more effectively safeguarding the Fund and increasing the amount protected.

2. Establishes a limit on annual distributions which helps ensure that the Fund will continue to grow in perpetuity in both nominal and real, inflation-adjusted dollars.
3. Maximizes the total amount of Fund income which can be paid out in the future, at least as compared to higher payout rates, and provides for intergenerational equity by striking a fine balance between short-term and long-term distributions.
4. Beginning in 2003, makes available \$175-\$300 million per year, depending on the Fund's market value, for purposes other than inflation-proofing and dividends. This amount will grow over time as the Fund grows.
5. Uses the percent of market value (POMV) payout methodology which smoothes volatility, treats realized and unrealized income equally as investment return, and is consistent with generally accepted accounting principles and modern endowment practice.
6. Lets lawmakers know in advance, within a relatively narrow range, how much Fund income will be available for appropriation each year.

In short, the Trustees believe HJR 15 serves the best interests of the Fund and the people of Alaska, and we request an opportunity this session to begin discussing with the members of your Committee the very important issues addressed in this resolution.

Thank you for your consideration.



**Alaska Permanent Fund Corporation**  
P.O. Box 25500 Juneau, Alaska 99802-5500  
(907) 465-2047

RECEIVED  
MAY 23 2001

May 10, 2001

Honorable Norman Rokeberg  
Chairman, House Judiciary  
State Capitol, Room 118  
Juneau, Alaska 99801-1182

Re: HJR 15 -- Constitutional amendment for inflation-proofing the Alaska Permanent Fund

Dear Representative Rokeberg:

This is to provide some information and make a request regarding HJR 15, the Board's proposed constitutional amendment for inflation-proofing the Alaska Permanent Fund.

Late in the session, we had a hearing on SJR 13 (the companion bill to HJR 15) in the Senate State Affairs Committee. At that hearing we were presented with a copy of a February 12, 2001 memo prepared by Tamara Cook, the director of Legal Services, raising certain legal issues. Subsequently, we asked Ron Lorensen, outside counsel for the Alaska Permanent Fund Corporation (APFC), to review and comment on Ms. Cook's memo discussing the above-referenced bill. A copy of Ms. Cook's memo and Mr. Lorensen's memo, dated May 9, 2001, are enclosed for your information.

The APFC Board of Trustees held one of its regular meetings here in Juneau on April 30 - May 1. During the Board's work session on May 1, the Board, staff and Mr. Lorensen spent over an hour discussing several of Ms. Cook's comments and concerns. After those discussions, the clear consensus on the Board continues to be strong support for maintaining the existing distinction between principal and income contained in the Constitution and for continuing the Constitution's present protection of principal from appropriation by the Legislature.

In this regard, the Board considered alternative approaches both to the operation of the amendment and to the language of the amendment. At the conclusion of those discussions, the members of the Board reaffirmed their view that the proposed amendment as presently drafted provides the best approach to implementing the Board's policy goals for protecting the Fund for the benefit of both present and future Alaskans.

Honorable Norman Rokeberg  
May 10, 2001  
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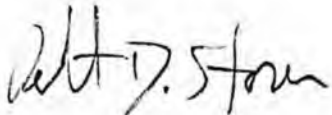
While it is likely that interpretational issues will arise, the Board believes it is important to keep the proposed amendment as short and uncomplicated as possible. The Trustees further believe that they can, in the course of presenting written and oral testimony which helps create the legislative record, make it quite clear that the proposal is definitely intended to continue to keep the principal inviolate.

Now that the first session of this legislature has drawn to a close, the Board asked that I express its hope that your committee and the remaining committees of referral in both houses will continue to move ahead with deliberations on the proposed amendment over the interim and into the second session. In particular, we urge that further hearings on the bills be scheduled so that, if they continue to receive favorable support from the committees, they can be taken up by each house relatively early in that session.

By approving the amendment early next year and avoiding pulling it into the last-minute flurry of negotiations and compromises over funding mechanisms and sources that can arise in the closing days of a legislative session, the Legislature would likely be seen by the public as making a strong statement of its support for providing additional protection to the Fund. Also, the earlier the amendment is passed by the Legislature, the sooner the public discussion and debate over the merits of the proposal can begin in advance of the 2002 general election.

Thank you for your continued interest in the Permanent Fund and attention to this issue.

Sincerely,



Robert D. Storer  
Executive Director

Enclosures

c: Board of Trustees

LAW OFFICES OF  
SIMPSON, TILLINGHAST, SORENSEN & LONGENBAUGH, P.C.

ONE SEALASKA PLAZA, SUITE 300 • JUNEAU, ALASKA 99801

TELEPHONE: 907-586-1400 • FAX: 907-586-3065

To: Jim Kelly, APFC

From: Ronald W. Lorensen, STS&L

Date: May 9, 2001

Re: SJR 13/HJR 15--Constitutional amendment for inflation-proofing the Alaska  
Permanent Fund  
Our File No.: 846.14

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You have asked for my comments on the February 12, 2001 memo from Tamara Brandt Cook, director of the Legislature's Division of Legal and Research Services, to Senator Gene Therriault discussing the Board of Trustee's proposed constitutional amendment for inflation-proofing the fund. I address her concerns in the order they are discussed in that memo:

1. Title of bill. I think Ms. Cook's observation that the title of the proposed resolution does not reflect its contents is probably the result of an insufficient understanding of the use of percent of market value (POMV) payout rules. On its face, the POMV rule expressed by the resolution appears to be intended simply as a limit on the Legislature's ability to appropriate Fund income (which is not expressed by the title). However, as the Board and those of us who have been studying endowment models and the use of POMV payout rules have come to understand, the real purpose of such a rule is to assure the long-term viability of a fund by allowing, over the long term, only the real portion of the income earned by that fund to be spent. With a POMV spending rule, a fund retains that portion of its income attributable to inflation, with the expectation that the fund will grow (again, over the long term) at the same rate as inflation--thereby "inflation-proofing" the fund.

2. Distinction between principal and income. Ms. Cook does not explain why she believes that retaining the distinction between principal and income of the Fund makes little sense. In any event, it is my understanding that continuing this distinction and assuring that Fund principal remains "inviolable" is an important policy goal for the Board in proposing this constitutional amendment (see my further discussion of this point at Paragraph 3, below). I think Ms. Cook is correct that, by retaining the distinction, the constitution's current requirement that Fund principal be used only for those income-producing investments specifically authorized by law would not apply directly to the Fund's income.

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E. BUDD SIMPSON • JON K. TILLINGHAST • STEPHEN F. SORENSEN • LESLIE LONGENBAUGH

L. MERRILL LOWDEN • RONALD W. LORENSEN (OF COUNSEL)

However, the Legislature has already addressed that issue in AS 37.13.145(a) by requiring that money in the earnings reserve account be invested in investments authorized for the investment of Fund principal under AS 37.13.120 ("the legal list").

3. Continued protection of Fund principal. It appears from Ms. Cook's discussion in the third paragraph of her memo that she does not interpret the proposed constitutional amendment to continue to protect Fund principal from appropriation and expenditure by the Legislature (i.e., if the earnings reserve account in a particular year was smaller than the permissible payout for that year, the difference could be satisfied out of principal). As indicated above, that interpretation runs counter to the Board's policy goal of keeping Fund principal "inviolable."

In our (the Board's and staff's) efforts to keep the proposed amendment as short and uncomplicated as possible, we have recognized that this interpretational issue may arise. However, because (i) the amendment retains the distinction between principal and income and (ii) does not in any way alter the existing constitutional language that provides the basis for treating Fund principal as "inviolable",<sup>1/</sup> I believe that the better interpretation of the amendment is that principal must continue to be inviolable and that the Legislature cannot "dip into" principal in order to make a payout otherwise permitted under new subsection (b). As we have discussed with the Board, one way to strengthen the analytical basis for this latter interpretation is for the Board and staff to create a written and testimonial record that makes it clear that the intended effect and interpretation of the amendment is to continue the special protection that Fund principal currently enjoys. This has, in fact, been done consistently since the Board first formally proposed the amendment at its December, 2000 meeting in Anchorage.

4. Effective date of the amendment. Under Section 1, Article XIII of our constitution, a proposed amendment to the constitution must be presented to the voters at the next general election after it is passed by the Legislature. Under that same provision, if the amendment is approved by the voters, it takes effect 30 days after the election results are certified by the lieutenant governor, unless a different date is provided for in the amendment. The amendment as presently proposed does not specify an effective date. Given the timing of the next general

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<sup>1/</sup> The first sentence of the provision creating the Alaska Permanent Fund (Section 15, Article IX) provides the basis for keeping Fund principal "inviolable." It reads as follows:

At least twenty-five per cent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses received by the State shall be placed in a permanent fund, *the principal of which shall be used only* for those income-producing investments specifically designated by law as eligible for permanent fund investments. (emphasis added)

The proposed amendment does not change this language.

election (November 5, 2002)--and assuming there is no unusual, protracted election contest as recently occurred in the 2000 Presidential election in Florida--the amendment, if approved by the voters, would almost certainly take effect before the beginning of the 23<sup>rd</sup> Alaska Legislature on January 21, 2003 (the third Tuesday in January following a gubernatorial election--AS 24.05.090).

In her memorandum, Ms. Cook suggests that having the amendment take effect in the middle of a fiscal year would be awkward, as it would allow the Legislature to appropriate any amount of the Fund's income in the earnings reserve account during the first part of the 2003 fiscal year, while restricting the amount available to the Legislature during the latter part of that fiscal year, after the amendment takes effect. Why or how this situation might be awkward is not readily apparent to me, however, considering that, unless the 22<sup>nd</sup> Alaska Legislature convenes itself in special session after its regular adjournment in May, 2002 for the express purpose of appropriating money from the Permanent Fund, its first opportunity in FY 2003 to appropriate funds from the Fund will not arise until after the amendment takes effect.

In any event, the timing of the effective date of the proposed amendment raises a policy question for the Legislature, rather than a legal one. In terms of policy considerations, one could actually argue that providing for a July 1, 2003 effective date as suggested by Ms. Cook could actually undermine the chances for passage of the amendment. This is because the delayed effective date might be seen by those who are exceptionally distrustful of the Legislature and the political process as providing an after-the-fact opportunity for the Legislature to "raid" the Fund before the amendment, although passed by the voters, actually goes into effect.

5. Status of earnings reserve account when amendment takes effect. At the end of her memo, Ms. Cook indicates uncertainty about the status of the earnings reserve account when the amendment takes effect and then states her assumption that the entire balance of that account would be available for appropriation under the constitutional provision as it read before the amendment. I do not believe this assumption is correct--once the amendment takes effect, for any fiscal year, the POMV payout rule expressed in new subsection (b) will operate to limit the Legislature's ability to appropriate from the earnings reserve account to the amount calculated under that rule. Subsection (b) expressly applies to "appropriations from the permanent fund," and, under existing AS 37.13.145(a), the earnings reserve account is already a part of the Fund.<sup>2/</sup> Unless the Legislature changes current law before the amendment takes effect, that account will continue to be a part of the Fund on the effective date of the amendment and, thus, subject to the limitation of subsection (b) on appropriations from the Fund.

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<sup>2/</sup> AS 37.13.145(a) provides in pertinent part: "The earnings reserve account is established as a separate account in the fund. Income from the fund shall be deposited by the corporation into the account as soon as it is received

Jim Kelly, APFC

May 9, 2001

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If you have any questions about these comments or would like to discuss them further, please do not hesitate to contact me.

cc: Jim Baldwin, Assistant Attorney General, Department of Law

# LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES  
LEGISLATIVE AFFAIRS AGENCY  
STATE OF ALASKA

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FAX (907) 465-2029  
Mail Stop 3101

JK  
State Capitol  
Juneau, Alaska 99801-1182  
Deliveries to: 129 6th St., Rm. 329

## MEMORANDUM

February 12, 2001

**SUBJECT:** Alaska Permanent Fund (Work Order No. 22-LS0534\C)

**TO:** Senator Gene Therriault, Chair  
Legislative Budget and Audit Committee  
Attn: Heather Brakes

**FROM:** Tamara Brandt Cook  
Director *TBC*

You ask for my observations on this draft resolution proposing an amendment to the state constitution dealing with the permanent fund. The title does not reflect the contents of the resolution and, because a joint resolution is supposed to be treated like a bill under the Uniform Rules, normally the title is drafted to reflect the contents. However, because Art. II, sec. 13 only applies to bills, the title defect in this situation is only a procedural and not a constitutional problem. Likewise, a new subsection is normally added as a new bill section and the material is not underlined. The way subsection (b) has been added does not conform to the Legislative Drafting Manual, but will not be fatal to the validity of the resolution if it is adopted by the legislature and approved by the voters.

Substantively, I observe that it makes little sense to retain the distinction between principal and income in subsection (a), since appropriations allowed under subsection (b) are based on averaged market value of the fund and no longer on income generated by the fund. Furthermore, by retaining the distinction between principal and interest, the provision that addresses permanent fund investments applies only to investments of principal. There is no constitutional requirement that interest retained in the fund also "be used only for those income-producing investments specifically designated by law as eligible for permanent fund investments." This seems a bit puzzling, but the legislature can address the investment of interest by law, so the approach probably does not create any great problem.

Subsection (b) is not as clear as might be desirable, but I think it can be applied. However, from my conversation with Mr. Jim Kelly, I gather that it is expected that only income of the fund will be available for appropriation. If this is the intended result, it has not been achieved. That is to say, if fund income is low for a period of years, it will be mathematically possible for an appropriation to be made based on the average of the market values formula that includes some fund principal. Perhaps, this possibility is so remote as not to be a serious problem.

Senator Gene Therriault, Chair

February 12, 2001

Page 2

I think it will be awkward for the constitutional amendment to spring into effect in the middle of a fiscal year and suggest that a July 1, 2003 effective date be added. Otherwise, for part of the year the legislature will be able to appropriate fund income, while at the end of the same year it will have access to an amount based on market value of the fund. Also, I am not sure about the status of the balance in the earnings reserve account on the day the amendment takes effect. I assume the entire balance on that day is available for appropriation under the constitutional language as it read prior to the amendment.

TBC:lmb

01-044.lmb

*Investing for Generations*



Alaska  
Permanent Fund  
Corporation

Annual Report 2001

# Legacy of the past, hope for the future

The Permanent Fund means different things to each generation of Alaskans.

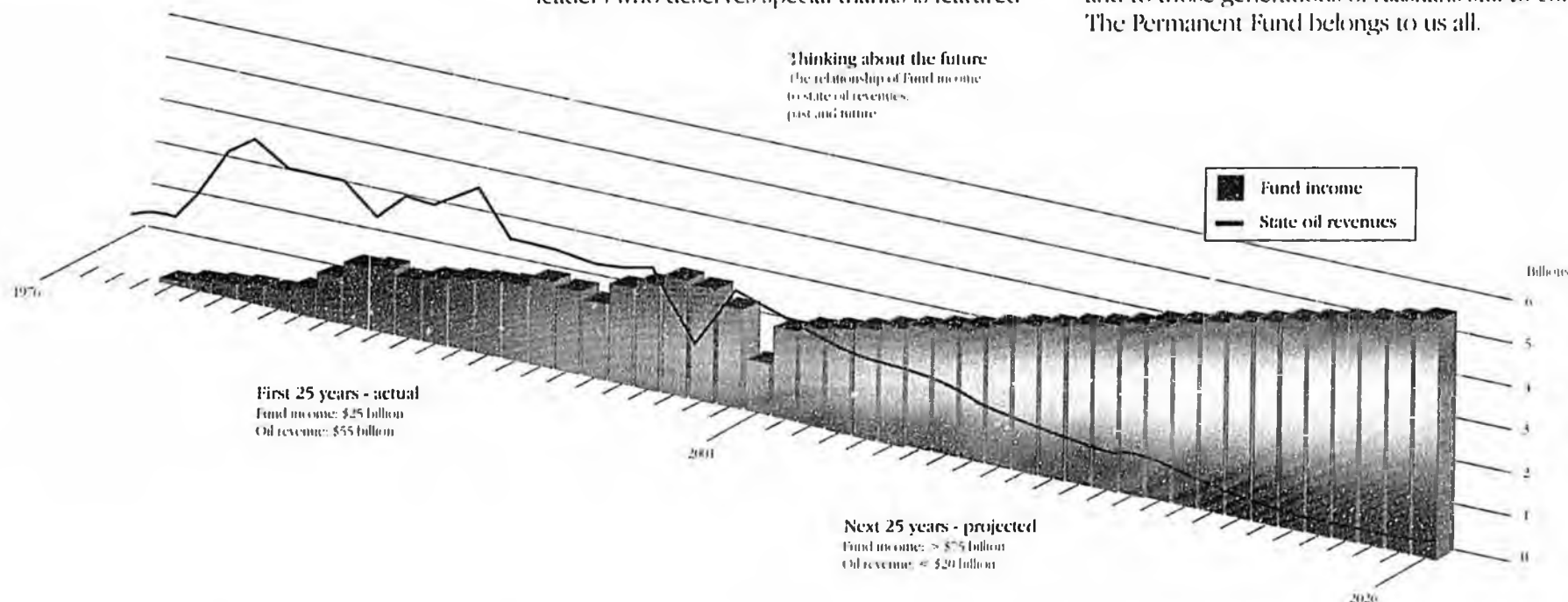
Children born in this year of the 25th anniversary of Alaska's Permanent Fund do not yet know what an important role the state's savings account will play in their lives. Their parents do, and so do pioneer Alaskans who, over the last quarter century, have watched the Fund grow beyond their most hopeful expectations.

Alaskans who are 25 years old have never known a time when the Permanent Fund was not a part of this state's public policy. They don't remember a fall season since 1982 when they didn't receive their own personal share of Alaska's oil wealth. The Permanent Fund, this great experiment in saving and sharing public wealth, is an integral part of their lives.

It took wisdom and leadership, courage and tenacity 25 years ago to create something of such enduring and abiding value. One of Alaska's past leaders who deserves special thanks is featured

on the cover of this report. Hugh Malone, who passed away this year, made such a lasting contribution that the Trustees this year named the Alaska Permanent Fund Corporation's board room in his honor.

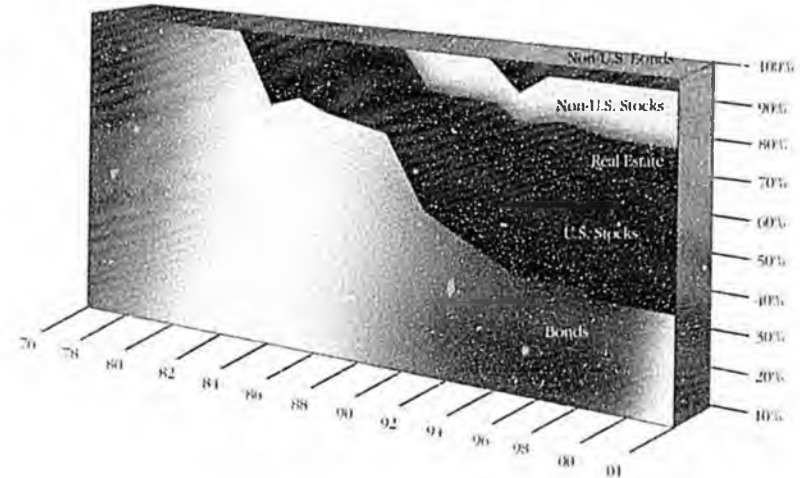
This annual report, which marks the 25th anniversary of the creation of the Permanent Fund, will tell you what happened to the Fund in fiscal 2001. But, it will also highlight the Fund's history and demonstrate why we Alaskans today owe so much to those generations who have come before ... and to those generations of Alaskans still to come. The Permanent Fund belongs to us all.



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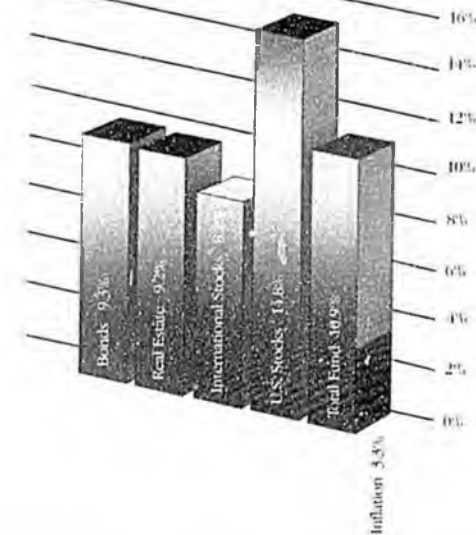
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## Managing risk and return by diversifying Fund's asset allocation 1970-2001



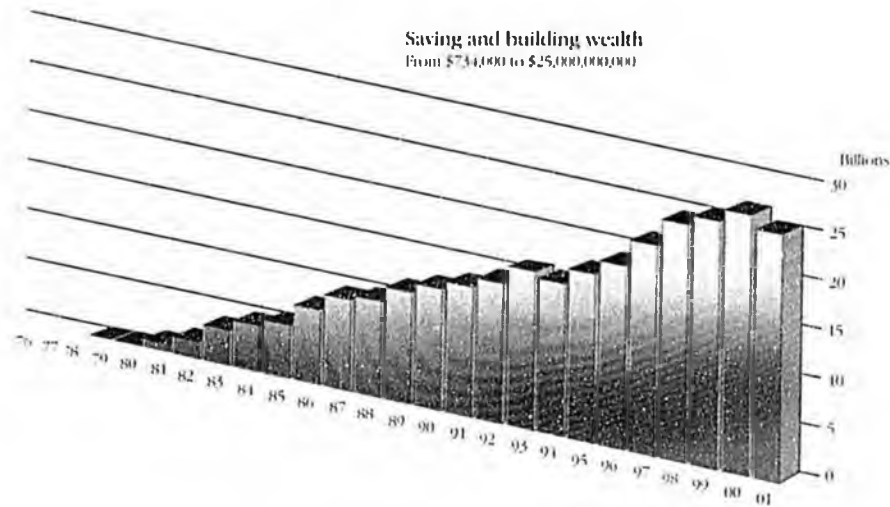
## Investing to beat inflation

Long-term returns: 17.5 years ended June 30, 2001  
except international stocks is 10 years



## Saving and building wealth

From \$74,000 to \$25,000,000,000



# Letter from the Chair: "Investing for generations"

## Dear Alaskan:

In November 1976, voters of Alaska, by a two-to-one margin, approved an amendment to the state's constitution and thereby created the Permanent Fund. This was, arguably, the most significant public policy action in state history. Shortly thereafter, in February 1977, the Fund received its first deposit of dedicated oil revenues: \$734,000. Now, 25 years later, Fund assets exceed \$25 billion.

That remarkable growth is due primarily to two factors: positive financial markets and prudent fiscal management. The chart on the preceding page shows the impact of the positive financial markets. For the prudent fiscal management, we have to thank those who have worked together over many years to maintain and grow the Fund,

diversify it, inflation-proof it for future generations and ensure its safety of principal. Those responsible include 37 distinguished Alaskans who have served as members of the APFC Board of Trustees, and all the Alaska legislatures, governors and APFC employees and investment managers who have worked with the Trustees to enable this unique Fund to invest so successfully.


There have been many significant milestones in the Fund's 25-year history and you can view them in the four-page fold-out timeline that begins on page 19.

Certainly the Fund would not be the magnificent legacy it is today if the residents of Alaska had not voted 25 years ago to save a portion of our one-time oil wealth. Nor would the Fund be as large as it is if the people's elected representatives had not

voted to add approximately \$14 billion of non-constitutionally required money to the Fund's principal by special appropriation and inflation-proofing.

The Fund would not be the empowering source of hope for the future that it is today if not for the Trustees who have consistently argued for, developed and implemented sound investment policies which have proven their value in the crucible of time.

All of the key benchmarks of Alaska's oil-fired public savings account have been achieved by steadfastness, vision, dedication — and a shared common mission — to keep the Permanent Fund permanent.



As one who was privileged to be around when the Fund was being created and now, 25 years later, to have served as the chair of the Board of Trustees, I am humbled by what we have, collectively, been able to accomplish. But, I get truly excited when I think about the future.

The Fund has a proven record of success. That success can and should continue, but we cannot and should not take the future for granted. Just as 25 years ago Alaskans took action to build a bright future by constitutionally creating the Permanent Fund, it is time to take action again, this time to keep the Permanent Fund permanent. That is why the Board of Trustees is urging the legislature and Alaskans to support our proposal to provide complete and protected inflation-proofing.

The proposal calls for constitutionally limiting the annual payout of Fund income to no more than 5 percent of the Fund's five-year average market value. (Note: 5 percent is more than is currently being paid out.) You can read more about it on page 16, but it can only come to pass if it is supported by the legislature and the majority of Alaska's voters, just as the original Permanent Fund constitutional amendment was 25 years ago.

In a world in which the future is uncertain, this proposal represents the Board's best judgment about how best to protect the Fund's purchasing power, ensure that the Fund will continue to grow, and provide the maximum amount of sustainable income to benefit current and future generations.

The proposal has been introduced in the legislature as Senate Joint Resolution 13 and House Joint Resolution 15 and is pending action.

As you reflect on the past 25 years of the Fund's history, I encourage you to try to envision the next 25 years. Think about how you want this unique public trust to move forward. In our view, the future can be quite bright if we Alaskans continue to take a disciplined, long-term, generational approach in both our investment and our public policies.



Clark Gruening  
Chair, Board of Trustees

# Executive Director's letter: "Focusing on the

*Dear Alaskan:*

In fiscal 2001, the Alaska Permanent Fund recorded its first-ever fiscal year loss, - 3.3 percent. In a very difficult year for equity markets around the globe, the APFC minimized Fund losses by adhering to a disciplined investment approach which emphasized asset diversification, risk management and "staying the course."

Despite the negative return, it was actually a pretty good year for the Fund:

- Each Permanent Fund portfolio – stocks, bonds and real estate – beat its respective benchmark. For example, the Fund's combined U.S. stocks outperformed the Russell 3000 stock index.
- The Alaska Permanent Fund's performance was better than that of the average public pension fund – largely due to the fact that most other funds had higher allocations to stocks than the Fund.
- Constitutionally protected principal grew by \$1 billion; \$686 million was transferred from the earnings reserve for inflation-proofing and \$339 million was added from new oil and other mineral revenues.
- A total of \$1.13 billion, down \$60 million from last year's all-time record, will be transferred this fall for payment of the 2001 PFDs.
- Long-term asset allocation, designed to balance the risks of negative returns in the short term against the rewards of higher positive returns in the longer term, stayed on course.

## **Policy actions**

One focus of activity during the year was increased internal monitoring. This began with reviewing and rewriting all investment policies to ensure consistency and to emphasize secure internal controls and increased reporting. In the fixed-income area, there was direction provided to increase scenario and compliance analysis. In the area of stocks, more quantitative tools were added to better analyze and monitor the Fund's equity holdings.

The turbulence in the financial markets this year challenged the Board of Trustees to adhere to its disciplined, long-term strategy. At the beginning of the fiscal year, investments in U.S. and non-U.S. stocks totaled 53.5 percent of the Fund, slightly above the asset allocation target of 53 percent. At the end of February 2001, declining markets brought the market value of total stocks below the lower policy boundary of 48 percent. It might have been tempting to allow the Fund's exposure to stocks to continue to decline – but in mid-March the Board instead authorized the purchase of \$750 million of additional stocks to bring the Fund's holdings back within the control bands of the asset allocation policy. This was not an attempt to "time" the market. Rather, it was an affirmation of the belief that a long-term investor will eventually do well by rebalancing; that is, taking profits in the investments that have done well and reinvesting the proceeds in those investments whose prices have fallen below normal levels.

During the year the Board allocated funds to a new Enhanced S&P 500 Index portfolio and selected Deutsche Asset Management to manage it. This portfolio is designed to add incremental return above the index return from security selection, but within much tighter risk constraint and with lower fees than an actively managed portfolio.

The Board of Trustees also made watchful judgments as to the two equity managers who had been placed under heightened scrutiny in the previous year. The Board determined that one of the managers had coped with the changes and uncertainties of new ownership and reorganizations well enough to warrant their retention. The manager went on to post the best

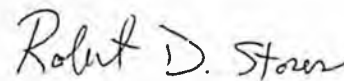
returns for the year of all the active stock managers in both U.S. and international portfolios. The other manager was terminated.

One other challenge facing the Board was how best to use the increased investment flexibility authorized by the 2000 legislature. That flexibility included a 5 percent “basket clause” which allows the Trustees to invest up to 5 percent of the Fund in any investment which meets prudent investor standards. As part of their due diligence looking into alternative investments, the Trustees completed an in-depth study of private equity (i.e., companies which have not yet gone public), and although they decided not to proceed immediately, the issue is certain to come up again in fiscal 2002.

#### **Administrative changes**

New directors were hired for two key departments. Joining the APFC this year were Allan Moore who replaced retiring Chief Investment Officer Terry Brown, and Marshal Kendziorek who became the new Director of Information Technology. On the Board, Attorney General Bruce Botelho replaced retiring Trustee John Shively.

The Corporation has been fortunate indeed in the caliber of the professionals who have worked here over the years, and I would like to thank all those who have been with the organization in the past as well as those who continue on with us as we celebrate the Permanent Fund's 25th anniversary.



Robert D. Storer

Robert D. Storer  
Executive Director

Fiscal Year 2001 will be remembered as a time when a number of trends ended and reversed. The decade-long economic expansion finally ended, the seemingly inexorable growth in capital expenditures for technology finally abated, and U.S. and international stocks plummeted. Real estate and fixed-income investments produced stronger-than-average returns, but their good performance was insufficient to offset the magnitude of the fall in stocks, and the Alaska Permanent Fund recorded its first-ever fiscal year loss.

More trend reversals are evident by comparing this year's conditions to those reported in last year's 2000 Annual Report. In 2000, the Federal Reserve tried to slow an overheating economy by raising interest rates in steps totaling 1.75 percent; in 2001 the Federal Reserve tried to stimulate a faltering economy by fast steps that lowered rates by 2.75 percent. In 2000, the Fund's international stocks were the best-performing asset class, up 23.3 percent; in 2001 they were the worst-performing asset, down 22.9 percent. In 2000, growth stocks continued several years of superior performance even with a very weak final quarter; in 2001 value stocks bested growth by never-before-seen margins.

## Changing benchmarks

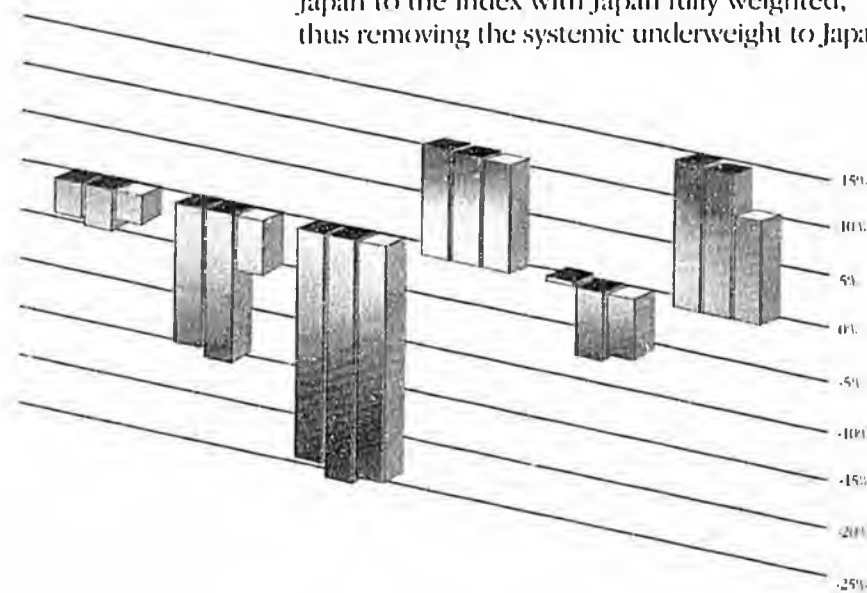
Defining a benchmark for a portfolio is how the Fund establishes objectives and measures results. This year, the Board changed benchmarks for select portfolios investing in both stocks and bonds to better reflect the breadth and depth of the investable markets.

The Board changed the benchmark for the internally managed fixed-income portfolio to the Lehman U. S. Aggregate from the Lehman U.S. Government/Credit index. This "simple" change which adds mortgage-backed securities to the APFC's investment universe, necessitated the turnover of some \$3 billion of fixed-income securities, but it will allow the portfolio to garner equivalent returns with less risk.

The Fund changed the benchmark for two global portfolios, one managed by Brinson Partners and one by Lazard Asset Management. Previously, the benchmark had been a combination of 60 percent S&P 500 — representing U.S. stocks and 40 percent MSCI (Morgan Stanley Capital International) EAFE (Europe, Australia and Far East) index—representing international stocks of developed countries. The new benchmark is the MSCI World Index, which better reflects the Fund's objective to obtain a return like that of all the global developed markets. It also challenges the investment managers to add value by actively managing the ratio of U.S. versus international stocks.

Lastly, the benchmark for the Schrodgers' Pacific Basin portfolio was changed from the Pacific Basin index with a fifty percent weighting for Japan to the index with Japan fully weighted, thus removing the systemic underweight to Japan.

Fund 2001 performance  
Permanent Fund compared to benchmarks,  
other funds and inflation



| Fund 2001 performance |            |             |                      |                   |                            |             |
|-----------------------|------------|-------------|----------------------|-------------------|----------------------------|-------------|
|                       | Total Fund | U.S. Stocks | International Stocks | U.S. Fixed Income | International Fixed Income | Real Estate |
| Inflation             | 3.4%       |             |                      |                   |                            |             |
| APFC                  | -3.3%      | -13.1%      | -22.9%               | 11.4%             | 0.8%                       | 14.8%       |
| Benchmark             | -1.5%      | -14.5%      | -23.8%               | 11.2%             | -7.4%                      | 14.1%       |
| Median fund           | -3.6%      | -5.3%       | -23.4%               | 11.0%             | -6.5%                      | 10.2%       |

## Alaska Permanent Fund Asset Allocation

Dollars in millions, as of June 30, 2001 (including cash held by managers)

|  | Market Value  | % of Total Fund |  | Market Value  | % of Total Fund |
|--|---------------|-----------------|--|---------------|-----------------|
| <b>Actively Managed Stocks</b>             |               |                 | <b>Fixed Income</b>                      |               |                 |
| <b>U.S. Managers</b>                       |               |                 | <b>APFC - Internal Fixed Income</b>      |               |                 |
| Alliance Capital Management                | 151           | 0.58%           | Alaska Permanent Capital Management      | 238           | 0.91%           |
| Brinson Partners                           | 550           | 2.11%           | Alliance Bernstein                       | 342           | 1.31%           |
| Dresdner RCM - Large Cap                   | 1,225         | 4.70%           | Brinson Partners                         | 300           | 1.15%           |
| Invesco Capital Management                 | 503           | 1.93%           | Julius Baer                              | 271           | 1.04%           |
| Lazard Freres                              | 521           | 2.00%           | Rogge Global Partners                    | 325           | 1.25%           |
| McKinley Capital Management                | 174           | 0.67%           | Alaska CD Program                        | 149           | 0.57%           |
| Putnam Investments                         | 601           | 2.31%           |  |               |                 |
| Capital Guardian - Small Cap               | 693           | 2.66%           | <b>Total - all fixed-income managers</b> | <b>10,554</b> | <b>40.48%</b>   |
| Dresdner RCM - Small Cap                   | 355           | 1.36%           |  |               |                 |
| <b>Total - U.S. managers</b>               | <b>4,773</b>  | <b>18.31%</b>   | <b>Real Estate</b>                       |               |                 |
| <b>International Managers</b>              |               |                 | <b>Direct Investments</b>                |               |                 |
| Capital Guardian                           | 501           | 1.92%           | AEW Capital Management                   | 188           | 0.72%           |
| Clay Finlay - Europe                       | 606           | 2.33%           | CB Richard Ellis                         | 368           | 1.41%           |
| Schroders Pacific Rim                      | 194           | 0.74%           | Heitman Property                         | 46            | 0.18%           |
| Brinson Partners                           | 590           | 2.26%           | Henderson Investors                      | 74            | 0.28%           |
| Lazard Freres                              | 532           | 2.04%           | Kennedy Property                         | 225           | 0.86%           |
| Dresdner RCM                               | 157           | 0.60%           | L&B Property                             | 340           | 1.30%           |
| Schroders Capital Mgmt. - Emerging Markets | 193           | 0.74%           | LaSalle Property                         | 307           | 1.18%           |
| Capital Guardian - Emerging Markets        | 263           | 1.01%           | Sentinel I & II                          | 193           | 0.74%           |
| <b>Total - international managers</b>      | <b>3,037</b>  | <b>11.65%</b>   | <b>Total real estate - direct</b>        | <b>1,742</b>  | <b>6.68%</b>    |
| <b>Total active equity</b>                 | <b>7,810</b>  | <b>29.95%</b>   | <b>Other</b>                             |               |                 |
| <b>Passively Managed Stocks</b>            |               |                 | Commingled Funds                         | 9             | 0.03%           |
| Deutsche Asset Mgmt. - S&P 500             | 2,591         | 9.94%           | REITs (Real estate investment trusts)    | 679           | 2.60%           |
| Deutsche Asset Mgmt. - S&P 500 Enhanced    | 830           | 3.18%           | Mortgages / CMBS                         | 306           | 1.17%           |
| Deutsche Asset Mgmt. - S&P 1000            | 546           | 2.09%           | <b>Total real estate - other</b>         | <b>994</b>    | <b>3.81%</b>    |
| Deutsche Asset Mgmt. - EAFE                | 1,006         | 3.86%           | <b>Total - all real estate managers</b>  | <b>2,736</b>  | <b>10.49%</b>   |
| <b>Total passive equity</b>                | <b>4,974</b>  | <b>19.08%</b>   |  |               |                 |
| <b>Total - all equities managers</b>       | <b>12,784</b> | <b>49.03%</b>   |  |               |                 |

Market events over the past twelve months reminded investors that patience, humility and moderation are virtues, that beauty is subjective, and that financial markets can be very fickle indeed. Above all, the past year underscored the importance of diversification, both within and between asset classes.

The Fund's equity performance for the past year has been consistent with market trends. Overall, the U.S. stock portfolio returned -13.1 percent. Style and size were the major determinants of performance, as value and small-cap stocks returned to favor. Brinson Partners led all Fund

U.S. equity managers with an 11.7 percent return, and outperformed its benchmark, the Russell 1000, by 26.7 percent.

The Fund's passive S&P 1000 portfolio (consisting of the S&P MidCap 400 Index and the S&P SmallCap 600 Index) returned 9.8 percent, reflecting benchmark returns for smaller-cap equities. However, the remainder of the Fund's domestic equity portfolios posted negative returns for the fiscal year, ranging from -0.5 percent for Lazard Asset Management's portfolio to -29.3 percent for Dresdner RCM Global Investors' small-cap growth product.

The Board concluded its search for an enhanced S&P 500 index product in September by hiring Deutsche Asset Management. Deutsche also manages the Fund's other passive equity portfolios. In December, the Board terminated a large-cap value manager, due to poor long-term performance. To avoid a potential style imbalance in comparison to the broad market (i.e., growth stocks versus value stocks, large capitalization versus small capitalization), in April the Board of Trustees subsequently authorized searches for two value style managers, one large-cap and one small-cap.



*"Indeed the strength and impact of the Alaska Permanent Fund is felt in ways we cannot measure or quantify."*

Byron I. Mallott,  
former trustee and executive director

## U.S. equities managers' performance

FOR PERIODS ENDED JUNE 30, 2001

| U.S. EQUITY LARGE CAP                     | 1-Year<br>Return | 3-Year<br>Returns | 5-Year<br>Returns | 10-Year<br>Returns | 17 1/2-Year<br>Returns |
|---|------------------|-------------------|-------------------|--------------------|------------------------|
| <b>Passive Managers</b>                   |                  |                   |                   |                    |                        |
| Deutsche Asset Mgmt. - S&P 500            | -14.7%           | -4.0%             | 14.5%             | 15.1%              | 15.3%                  |
| Deutsche Asset Mgmt. - S&P 500 Enhanced   | -                | -                 | -                 | -                  | -                      |
| <i>S&amp;P 500 Index</i>                  | -14.8%           | -3.9%             | 14.5%             | 15.1%              | 15.3%                  |
| <b>Large-Cap Value Managers</b>           |                  |                   |                   |                    |                        |
| Brinson Partners                          | 11.7%            | 2.6%              | 10.6%             | -                  | -                      |
| Invesco Capital Management                | -1.2%            | 0.3%              | 9.7%              | 13.0%              | -                      |
| Lazard Freres                             | -0.5%            | 2.4%              | 11.0%             | -                  | -                      |
| <i>Russell 1000 Index</i>                 | -15.0%           | 4.3%              | 14.3%             | 15.2%              | 15.1%                  |
| <i>Russell 1000 Value</i>                 | 10.3%            | 5.4%              | 15.0%             | 15.8%              | 15.3%                  |
| <b>Large-Cap Growth Managers</b>          |                  |                   |                   |                    |                        |
| Alliance Capital Management               | -28.2%           | -                 | -                 | -                  | -                      |
| Dresdner RCM                              | -18.2%           | 16.2%             | 22.2%             | 18.6%              | 18.1%                  |
| McKinley Capital Management               | -26.3%           | -                 | -                 | -                  | -                      |
| Putnam Investments                        | -27.8%           | 0.8%              | -                 | -                  | -                      |
| <i>Russell 1000 Index</i>                 | -15.0%           | 4.3%              | 14.3%             | 15.2%              | 15.1%                  |
| <i>Russell 1000 Growth</i>                | -36.2%           | 0.7%              | 12.0%             | 13.8%              | 14.2%                  |
| <b>U.S. EQUITY SMALL CAP</b>              |                  |                   |                   |                    |                        |
| <b>Passive Managers</b>                   |                  |                   |                   |                    |                        |
| Deutsche Asset Mgmt. - S&P 1000           | 9.8%             | 12.8%             | -                 | -                  | -                      |
| <i>S&amp;P 1000 Index</i>                 | 9.5%             | 12.5%             | -                 | -                  | -                      |
| <b>Small-Cap Value Managers</b>           |                  |                   |                   |                    |                        |
| Capital Guardian                          | -22.4%           | -                 | -                 | -                  | -                      |
| <i>Russell 2000 Index</i>                 | 0.6%             | 5.3%              | 9.6%              | 13.5%              | 11.0%                  |
| <i>Russell 2000 Value Index</i>           | 30.8%            | 6.9%              | 13.4%             | 16.0%              | 13.2%                  |
| <b>Small-Cap Growth Managers</b>          |                  |                   |                   |                    |                        |
| Dresdner RCM                              | -29.3%           | -                 | -                 | -                  | -                      |
| <i>Russell 2000 Index</i>                 | 0.6%             | 5.3%              | 9.6%              | 13.5%              | 11.0%                  |
| <i>Russell 2000 Growth Index</i>          | -23.3%           | 2.2%              | 4.8%              | 10.2%              | 8.4%                   |
| <b>Combined Fund U.S. equities return</b> |                  |                   |                   |                    |                        |
| <i>Russell 3000 Index</i>                 | -13.1%           | 4.1%              | 13.0%             | 14.5%              | 14.8%                  |
|   | -13.9%           | 4.2%              | 13.8%             | 15.0%              | 14.7%                  |

## Permanent Fund's target asset allocation

|                          |            |              |
|--------------------------|------------|--------------|
| U.S. Equities            | 37%        | +/-7%        |
| International Equities   | 16%        | +/-5%        |
| <b>Total Equities</b>    | <b>53%</b> | <b>+/-5%</b> |
| U.S. Bonds               | 35%        | +/-7%        |
| Non-Dollar Bonds         | 2%         | +/-2%        |
| <b>Total Bonds</b>       | <b>37%</b> | <b>+/-5%</b> |
| <b>Total Real Estate</b> | <b>10%</b> | <b>+/-2%</b> |

Increasing correlations between the world's equity markets and the growing interdependence of global economies contributed to poor returns for the Fund's international stock portfolios.

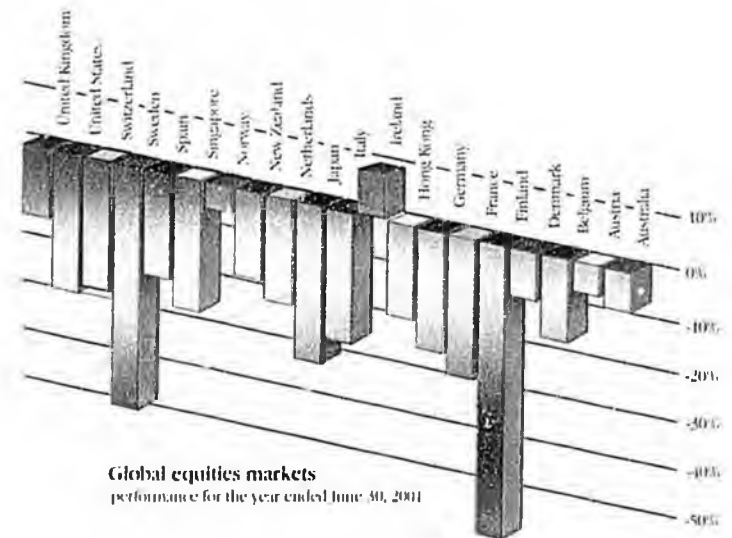
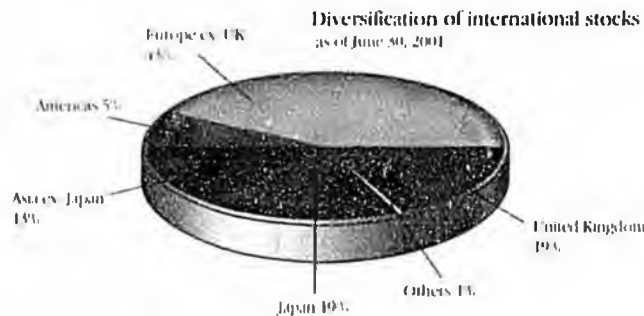
Developed and emerging markets both suffered as growth in U.S. GDP slowed, particularly in capital goods spending.

*"I was proud growing up in Alaska to be taught about the Fund and how our leaders took the initiative to establish something that can live on for many generations."*

Aдриanna Coonrod, 25-year-old Alaskan.

The best absolute and relative performing non-U.S. Fund manager was Brinson Partners. Although Brinson's MSCI EAFE (Morgan Stanley Capital International Europe, Australia and Far East stock index) portfolio lost 12.8 percent during the fiscal year, the firm outperformed its benchmark by 11.0 percent. Dresdner RCM Global Investors, because of its strong growth-style orientation, went from being one of last year's top performing non-U.S. EAFE managers to the APFC's worst this fiscal year, down 30.0 percent. The passively managed EAFE index portfolio returned -23.3 percent.

In the emerging markets, increasing investors' risk aversion contributed significantly to a 25.9 percent decline in the MSCI Emerging Markets Free Index. The Fund's emerging markets managers Schroder Investment Management and Capital Guardian Trust, who are benchmarked against the MSCI Emerging Markets Free Index, returned a disappointing -31.2 percent and -31.8 percent, respectively for the fiscal year, lagging the benchmark return of -25.9 percent.



## International equities managers' performance

FOR PERIODS ENDED JUNE 30, 2001

|  | 1-Year<br>Return | 3-Year<br>Returns | 5-Year<br>Returns | 10-Year<br>Returns |
|--|------------------|-------------------|-------------------|--------------------|
| <b>EAFE Passive Manager</b>                        |                  |                   |                   |                    |
| Deutsche Asset Mgmt. - EAFE                        | -23.3%           | -1.0%             | 4.0%              | -                  |
| Morgan Stanley Capital International (MSCI) EAFE   | -23.8%           | -1.3%             | 2.8%              | 6.4%               |
| <b>EAFE Active Managers</b>                        |                  |                   |                   |                    |
| Brinson Partners                                   | -12.8%           | 2.3%              | 6.7%              | -                  |
| Lazard Freres                                      | -19.0%           | -0.7%             | 7.0%              | -                  |
| Dresdner RCM                                       | -30.0%           | -                 | -                 | -                  |
| Capital Guardian                                   | -27.4%           | 7.6%              | 11.5%             | 13.4%              |
| MSCI EAFE (Europe, Australia and Far East)         | -23.8%           | -1.3%             | 2.8%              | 6.4%               |
| <b>Europe Manager</b>                              |                  |                   |                   |                    |
| Clay Finlay  | -18.8%           | 1.5%              | 13.8%             | 14.6%              |
| MSCI Europe Index                                  | -22.1%           | -3.8%             | 9.6%              | 11.6%              |
| <b>Pacific Manager</b>                             |                  |                   |                   |                    |
| Schroders Capital Management - Pacific Rim         | -17.8%           | 15.3%             | -4.8%             | 5.5%               |
| Custom Pacific Basin target                        | -21.6%           | 12.7%             | -7.7%             | 3.6%               |
| <b>Emerging Markets Managers</b>                   |                  |                   |                   |                    |
| Capital Guardian                                   | -31.8%           | -                 | -                 | -                  |
| MSCI Emerging Markets Free Index                   | -25.9%           | -                 | -                 | -                  |
| Schroders Capital Management                       | -31.2%           | -                 | -                 | -                  |
| MSCI Emerging Markets Free Custom Index            | -26.3%           | -                 | -                 | -                  |
| <b>Combined Fund international equities return</b> | <b>-22.9%</b>    | <b>1.3%</b>       | <b>6.0%</b>       | <b>8.2%</b>        |



As real estate in general experienced stronger-than-average returns in fiscal 2001, the Fund's real estate portfolio posted an overall return of 14.3 percent net of fees, compared to its blended benchmark of 14.1 percent.

It was the Fund's best performing asset class for the year and for the trailing three years.

These positive results in real estate reflect the value of asset diversification in a year marked by a significant downturn in the stock market. The portfolio was fully invested at 10.5 percent at fiscal year-end, marking the first time it has ever been above its asset allocation target of 10 percent of the total Fund.

Approximately two-thirds of the real estate portfolio consists of direct holdings of individual properties. The Fund's direct investments returned 11.4 percent net of fees, just short of the NCREIF Classic Index of 11.5 percent gross of fees.

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*"This accomplishment is something all Alaskans can take great pride in. It is also exciting to think about how large the Fund can grow in the future if we continue the prudent policies of the past."*

Oral Freeman, former trustee.

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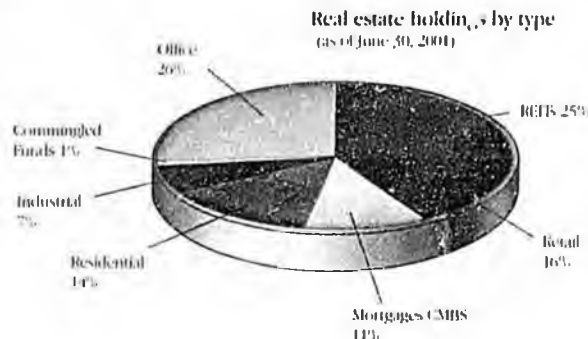
Another 25 percent of the Fund's real estate portfolio was invested in Real Estate Investment Trusts (REITs). The APFC's two REIT portfolios managed by AEW Capital Management continued to post above-average returns, with 23.8 and 24.2 percent. The returns from the equity securities component of the portfolio exceeded

the benchmark Morgan Stanley REIT Index return of 23.5 percent.

The remaining 11 percent of the Fund's real estate portfolio was invested in mortgages. Managed by Lend Lease, this is a fully invested, diversified portfolio of investment-grade commercial mortgage-backed securities (CMBS) and whole loans. Lend Lease returned 13.3 percent for the year compared to the Lehman Brothers Corporate Series A Index of 12.5 percent.

During the year, two direct investments – 919 North Michigan and Arboretum Lakes – and three commingled funds were sold, there were no new acquisitions, and partner's interests were purchased in two apartment properties, making those properties, the Island Club located on Brickel Key in downtown Miami and Treetops located in suburban Philadelphia, 100 percent wholly owned by the Alaska Permanent Fund.

The total portfolio closed the year with a market value of \$2.8 billion which included \$293 million in unrealized gains



## Real estate managers' performance

PERIODS ENDED JUNE 30, 2001

|                              | 1-Year<br>Return | 3-Year<br>Return | 5-Year<br>Return | 8 1/2-Year<br>Return |
|------------------------------|------------------|------------------|------------------|----------------------|
| <b>Direct Investments</b>    | <b>11.4%</b>     | <b>11.7%</b>     | <b>12.1%</b>     | <b>9.5%</b>          |
| AEW Capital Mgmt             | 10.6%            | 15.8%            | 20.9%            | -                    |
| CB Richard Ellis             | 9.7%             | 9.3%             | 11.7%            | -                    |
| Heitman Property Agg         | 33.0%            | 19.5%            | 16.8%            | 9.5%                 |
| Henderson Investors          | 12.2%            | 12.4%            | 12.5%            | -                    |
| Kennedy Property Agg         | 8.7%             | 9.8%             | 10.1%            | 8.8%                 |
| L&B Property Agg             | 8.3%             | 9.8%             | 9.3%             | 6.9%                 |
| LaSalle Property Agg         | 17.3%            | 14.2%            | 11.7%            | 10.0%                |
| Sentinel I & III*            | 8.5%             | 10.6%            | 11.0%            | 11.7%                |
| <b>REITs</b>                 | <b>23.8%</b>     | <b>11.9%</b>     | <b>10.0%</b>     | <b>7.6%</b>          |
| AEW Capital - Focus          | 23.8%            | -                | -                | -                    |
| AEW Capital                  | 24.2%            | 10.6%            | -                | -                    |
| Simon Property Group         | 21.7%            | 12.0%            | 10.4%            | 7.9%                 |
| <b>Real Estate Mortgages</b> | <b>13.3%</b>     | <b>-</b>         | <b>-</b>         | <b>-</b>             |
| Lend Lease                   | 13.3%            | -                | -                | -                    |
| Commingled                   | 4.8%             | 7.6%             | 10.2%            | 8.7%                 |

### Combined Fund Real Estate

|              |       |       |       |      |
|--------------|-------|-------|-------|------|
| Net of Fee   | 14.3% | 11.6% | 11.9% | 9.3% |
| Gross of Fee | 14.8% | 12.1% | 12.4% | 9.9% |

### Benchmarks

|                      |       |       |       |       |
|----------------------|-------|-------|-------|-------|
| NCREIF Classic Index | 11.5% | 12.6% | 13.5% | 10.4% |
| Morgan Stanley REIT  | 23.5% | 5.4%  | 11.0% | -     |
| LB Credit A          | 12.5% | 5.6%  | 7.3%  | 7.3%  |
| APFC Target          | 14.1% | 10.4% | 11.6% | 9.3%  |



Fixed-income performance was quite good last year. The Fund's total domestic fixed income returned 11.4 percent versus 11.2 percent for its benchmark. That small increment of added value may seem modest, but on a base of \$10 billion in assets it's \$20 million of profit. Likewise, the Fund's international non-dollar assets return of 0.8 exceeded the benchmark's return of 0.4 percent.

Among the domestic bond managers, the portfolio managed by APFC staff provided the best returns, while Julius Baer topped the non-dollar manager rankings. Please refer to the accompanying table showing performance data for more details.

### Diversification makes sense

The difference in performance between bonds and stocks was so large last year that the Trustees were forced to rebalance in late March in order to stay within the Fund's asset allocation control bands. So, the Fund sold \$750 million of bonds, on which the Fund had earned a large profit, to buy stocks, which had fallen in price. If one never buys stocks when they are down in price, one never owns cheap stocks. And if one never sells bonds when prices are high, one always owns expensive bonds.

### Benchmark and procedural changes

There were a number of procedural changes made during the last year to better assure that the APFC staff is taking all reasonable steps to invest and monitor the Fund's investments in fixed income. The Board changed the benchmark for the internal domestic portfolio to the Lehman U.S. Aggregate from the Lehman U. S. Government/Credit index. This change adds mortgage-backed securities issued by major government-sponsored agencies such as Federal National Mortgage Association to our investment universe. Mortgage-

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*"The most important thing for my future is that the Fund is protected so it can continue to grow."*

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Scott Bell, 15-year-old Alaskan.

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backed securities are a high quality bond sector, and so this change reduces some of the credit risk inherent in the previous benchmark.

The Board's guidelines for fixed-income investing were rewritten to reflect the new benchmark. At the same time, the Board decided to apply the same guidelines to our external domestic managers that we apply to the internally managed portfolio, to consolidate all fixed-income

resolutions into one simpler document. All of the changes were designed to expand and streamline oversight of internal and external managers.

### How the economy affected bonds

Last year was truly a tale of two economies. The first half of the fiscal year saw real economic growth in excess of a 4 percent annual rate, with growing capacity constraints, particularly in skilled labor.

As the year began, the Federal Reserve had just finished raising its target for the federal funds rate for the sixth time. They raised the rate a total of 1.75 percent in six steps beginning in mid-1999 to reach 6.50 percent. By the end of the fiscal year, it was the complete opposite. The Federal Reserve had just finished its sixth reduction in rates, having dropped them a full 2.50 percent in six steps beginning at the end of December.

By fiscal year-end, the economy had slowed dramatically, capital investment had dropped precipitously and profits were collapsing. All of these things were supportive of lower interest rates and higher bond prices, but also indicated a deterioration in credit quality of corporate bonds.

### Market highlights

There were several noteworthy bond market developments last year. The first is that virtually the entire decline in interest rates occurred in the bonds with shortest maturities. Thirty-year interest rates fell only one-eighth of one percent while one-year rates for treasury notes fell over two percentage points.

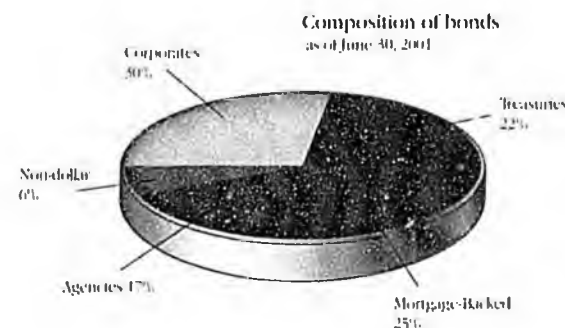
The second is that during the year 2000 and the first half of 2001, the publicly traded securities portion of the U. S. treasury market shrank in size. This helped treasuries to post excellent results during the period. Normally, this less-risky asset also provides a less robust return. The rapidly disappearing federal budget surplus may cause a reversal of this trend soon.

The third event of note concerns the significant transformation of the corporate bond sector. On the one hand, there has been remarkably strong foreign investor demand for U. S. corporate bonds. This has raised prices in the corporate bond market so far this calendar year. On the other hand, the sharp decline in profits and a reduced appetite for risk have reduced the prices for any corporate bonds perceived as likely to be down-graded by a major rating agency. The market prices of such bonds can decline precipitously. The only antidotes are strong research and widespread diversification of holdings.

### Fixed-income managers' performance

FOR PERIODS ENDED JUNE 30, 2001

| U.S. FIXED INCOME                                 | 1-Year Return | 3-Year Returns | 5-Year Returns | 10-Year Returns | 17 1/2-Year Returns |
|---|---------------|----------------|----------------|-----------------|---------------------|
| APFC in-house                                     | 11.5%         | 5.5%           | 7.1%           | 7.7%            | 9.3%                |
| Alaska Permanent Capital Mgmt.                    | 9.3%          | 5.4%           | -              | -               | -                   |
| Brinson Partners                                  | 10.5%         | 5.9%           | -              | -               | -                   |
| Alliance Bernstein                                | 10.9%         | 6.5%           | -              | -               | -                   |
| APFC in-house target                              | 11.2%         | 6.0%           | 7.4%           | 7.9%            | 9.5%                |
| Lehman Aggregate Index                            | 11.2%         | 6.3%           | 7.5%           | 7.9%            | 9.6%                |
| <b>Combined Fund U.S. fixed-income return</b>     | <b>11.4%</b>  | <b>5.5%</b>    | <b>7.1%</b>    | <b>7.7%</b>     | <b>9.3%</b>         |
| NON-U.S. FIXED INCOME                             | 1-Year Return | 3-Year Returns |                |                 |                     |
| Julius Baer                                       | 1.7%          | 2.6%           |                |                 |                     |
| Rogge Global Partners                             | 0.0%          | 2.4%           |                |                 |                     |
| Salomon Non-US World Gov Bond Index (50% Hedged)  | 0.4%          | 3.1%           |                |                 |                     |
| <b>Combined Fund non-U.S. fixed-income return</b> | <b>0.8%</b>   | <b>2.5%</b>    |                |                 |                     |



*"I'm sure that it's obvious to everyone who is sitting ... around this table that one of the big problems with the Permanent Fund is that there's no protection against inflation ..."*

*— Trustee Tom Williams, Minutes of the Board of Trustees' first meeting, September 12, 1980*

The Board of Trustees this year put forth a proposal to solve that problem once and for all. The proposal, introduced in the legislature as Senate Joint Resolution 13 and House Joint Resolution 15, calls for constitutionally limiting the annual payout of Fund income to no more than 5 percent of the Fund's five-year average market value.

The proposed constitutional amendment is designed to

- preserve the Fund's purchasing power;
- maximize distributions of Fund income over the long-term; and
- limit spending to "real," i.e., after inflation-proofing, Fund income.

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*"Trustees should always have a due regard for the contract with the public and the foundation of trust upon which this institution is built."*

*The late Hugh Malone, former trustee.*

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The proposal would add a new constitutional limit on Permanent Fund spending. Principal would continue to be off-limits for spending, and appropriations from the earnings reserve would be limited to no more than 5 percent of the Fund's average market value for the past five years.

### ***Why limit the payout to 5 percent?***

- 5 percent real rate of return is at the high end of what is actually achievable for the Permanent Fund;
- 5 percent is the maximum sustainable payout rate that still maintains the Fund's real value;
- 5 percent allows greater distributions over time than a higher payout; and
- 5 percent is what the majority of endowments pay out.

The proposal does not impact the existing dividend program because the 5 percent limit is set higher than what is needed to accommodate the annual distribution which, under current law, pays out the equivalent of approximately 4 percent of the Fund's average market value. All income not used in excess of the 5 percent payout limit would be retained in the Fund to offset inflation.

In the words of Board Chair Clark Gruening, "It's been 25 years since we've asked the people of Alaska to make a constitutional change to the Fund, and it may be another 25 years or longer before another change is recommended. This proposal is of the utmost importance as we look at the long-term. It will keep Alaska's Permanent Fund permanent."

### **How SJR 13/HJR 15 works**

|               |  |
|---------------|--|
| 8.25%         | Fund's projected average annual return   |
| <u>-5.00%</u> | Maximum sustainable payout from Fund   |
| 3.25%         | Equals projected average annual inflation/ remains in the Fund as inflation-proofing |

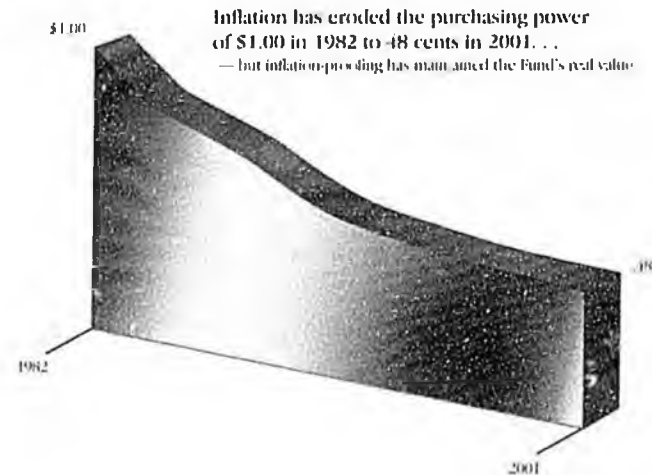
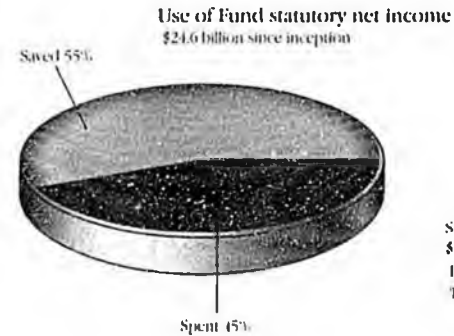
**Trustees' proposed constitutional amendment for complete and protected inflation-proofing**

Section 15. Alaska Permanent Fund. (a) At least twenty-five percent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses received by the State shall be placed in a permanent fund, the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for permanent fund investments. All income from the permanent fund shall be deposited in the permanent (GENERAL) fund [UNLESS OTHERWISE PROHIBITED BY LAW].

(b) For any fiscal year, appropriations from the permanent fund shall be limited to five percent of the average of the year-end market values of the permanent fund for the last five fiscal years, including the fiscal year just ended. No other appropriations from the permanent may be made.

NOTE: New language to be added is underlined; language removed is [CAPS IN BRACKETS].

|   |                      |
|---|----------------------|
| Saved for future generations                  | \$14.4 billion (55%) |
| Added to principal by inflation-proofing:     | \$ 0                 |
| Added to principal by special appropriations: | \$ 1                 |
| Retained in Fund as undistributed income:     | \$ 1                 |

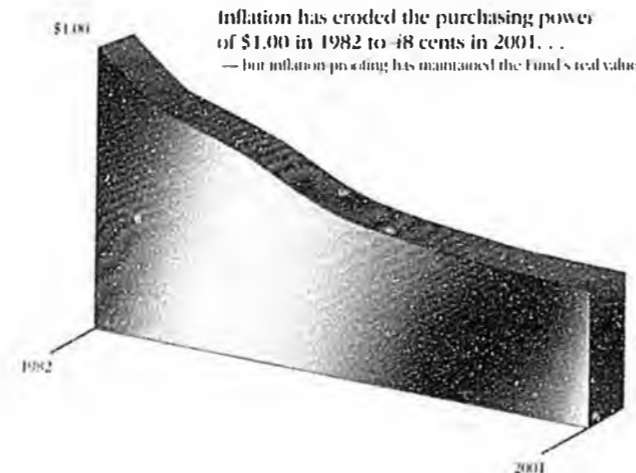
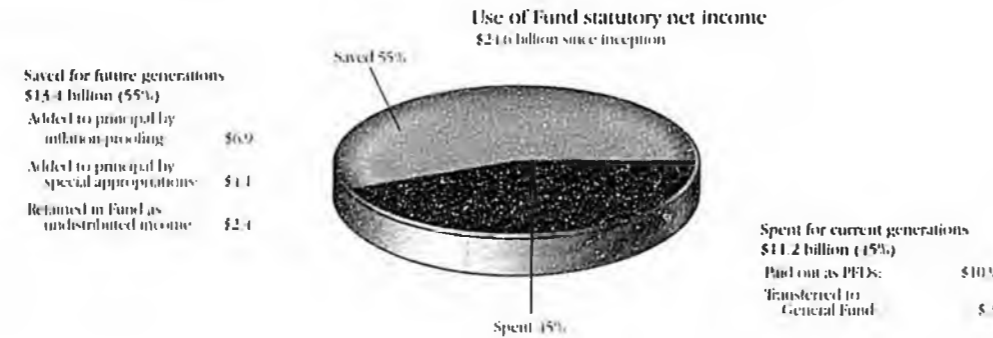


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NOTE: New language to be added is underlined; language removed is [CAPS IN BRACKETS].



Since the APFC was established by statute in 1980, 37 Alaskans have been members of the Board of Trustees. The Board is comprised of six members, of whom four are public members appointed by the governor, and two, including the Commissioner of Revenue, are Cabinet members. The board members serve staggered four-year terms.

*"My wish for the Permanent Fund on its 25th birthday is that it will grow even larger and stronger by its 50th birthday."*

Austin Sture, 9-year-old Alaskan.

This year, the 25th anniversary of the Fund, the Board consists of Chair Clark Gruening, who was a key participant in legislation establishing the Fund, Vice Chair Melphine Evans, Trustee Wilson Condon, who served on the original 1980 Board, and Trustees Jim Sampson, Bruce Botelho and Eric Wohlforth.

The APFC Board of Trustees sets policy for the Corporation and establishes the Fund's asset allocation.

The APFC staff is led by Executive Director Robert D. Storer, who oversees the management and daily operations of the Fund. Allan Moore assumed the position of Chief Investment Officer in November, 2001. He is responsible for all investment functions and a staff of ten. Bob

Bartholomew is the Fund's Chief Operating Officer. He is responsible for the APFC's annual management plan and directs the activities of all support departments (Administration, Finance, Information Technology and Communications).

The APFC's Finance Director is Chris Phillips, who oversees the financial reporting, accounting and supervision of the Finance Department. Marshal Kendziorek is Director of Information Technology, having joined the organization in March, 2001. Communications Director Jim Kelly leads the public information program, overseeing communication with the public, media and legislature, as well as all external print and electronic publications.



From left to right: Chair Clark S. Gruening, Vice Chair Melphine Evans, Trustee Wilson L. Condon, Trustee Jim Sampson, Trustee Eric E. Wohlforth, Trustee Bruce M. Botelho and Executive Director Robert D. Storer.



## 1976

In the General Election on November 2, Alaska voters approve a constitutional amendment establishing the Permanent Fund by a margin of 75,588 to 38,518.

## 1977

On February 28, the Permanent Fund receives its first deposit of dedicated oil revenues totaling \$734,000.

## 1978-79

Continuing debate concerning whether the Permanent Fund should be invested and managed as a public trust or as an economic development bank.

## 1980

The Alaska Legislature creates the Alaska Permanent Fund Corporation, adds \$900 million in surplus oil revenues to the Permanent Fund by special appropriation, and approves the first Permanent Fund Dividend program, which later was ruled unconstitutional by the Supreme Court.

## 1981

The Alaska Legislature approves a second special appropriation of surplus oil revenues to the Permanent Fund for \$1.8 billion.

## 1982

The Alaska Legislature, at the request of the Board of Trustees, enacts inflation-proofing to protect the Fund's purchasing power. The first Permanent Fund dividend check of \$1,000 is distributed. (Note: The legislature paid this first dividend, not with Permanent Fund income, but with surplus oil revenues.)

## 1983

The Permanent Fund makes its first investment in the stock market, and later that year, in equity real estate.

## 1984

Permanent Fund assets reach \$5 billion.

## 1985

The Permanent Fund initiates the "Learning is Permanent" education program.

## 1986

The Alaska Legislature approves the Fund's third special appropriation. This \$1.26 billion addition to Fund principal is transferred from undistributed Fund income.

## 1987

In its first decade, the Alaska Permanent Fund has grown larger than any endowment or private Foundation in the U.S.

## 1988

The Permanent Fund, with an above-national-average allocation to bonds, ranks in the top 9 percent of all public funds in the United States as the stock market crashes in the preceding October.



## 1989

Permanent Fund assets reach \$10 billion.

## 1990

The Permanent Fund begins to invest in stock and bond markets outside the United States.

## 1991

The Permanent Fund's dedicated share of state oil revenues reaches \$435 million, the largest single-year amount in its history.

## 1992

The Permanent Fund dividend distributed to Alaskans totals \$488 million, or \$915.84 per person.

## 1993

Permanent Fund assets reach \$15 billion.

## 1994

Dedicated oil revenues received by the Fund since inception reach \$5 billion.

## 1995

The Permanent Fund's investments in stocks reach \$7 billion.

## 1996

Fund assets reach \$24 billion.

## 1997

The Fund combined all its custody and safekeeping services under one global contractor, Bank of New York, the nation's oldest bank.

## 1998

For the first time, Fund earnings exceed state oil revenues as the Fund earns a record \$2.6 billion and reaches \$25 billion in assets.

## 1999

The Alaska Legislature grants increased investment flexibility to the Board of Trustees, including, for the first time, authorization to invest up to 5 percent of the Fund in accordance solely with the Prudent Investor Rule rather than the statutory list of investments.

## 2000

With markets returning to higher, more traditional levels of volatility, Trustees further diversify the Fund's investment portfolio and increase the equity allocation to 53 percent.

## 2001

At the request of the Board of Trustees, the Alaska Legislature introduces House Joint Resolution 15 and Senate Joint Resolution 13, which would place before Alaska voters a constitutional amendment to provide complete and permanently protected inflation-proofing to the Fund.

The Alaska Permanent Fund owes much of its success to the efforts of many dedicated Alaskans. This group includes all the Trustees, past and present who have worked diligently as fiduciaries in maintaining the safety of principal and maximizing income within prudent risk parameters. To those who have committed their time, expertise and energy to this challenge, we pay tribute.

*"The Permanent Fund is not a private business. It is not a pension fund. There is no other fund like it on the face of the earth ... Public confidence is the very backbone and lifeblood of the Permanent Fund Corporation."*

March, 1991, Trustee Oral Freeman.

*"Twenty-five percent of the mineral bounty has been, in one form or another, parked in the Permanent Fund. That's a huge commitment by the people of Alaska to the future."*

August, 1990, Trustee Hugh Malone.

On the 25th anniversary of the Fund, we'd like to provide a special acknowledgement of those Trustees who served the Fund and have passed away. These include Hugh Malone, a former legislator and House Speaker from the Kenai Peninsula, who, more than anyone, can properly be called the father of the Permanent Fund. Also included are long-time Alaska bankers Elmer Rasmuson and Arnold Espe, former Commissioner of Transportation and Public Facilities Robert Ward, Anchorage CPA and business leader Clyde Sherwood and former Fairbanks lawmaker Charlie Parr.

These Trustees are each in their own way responsible for part of the foundation upon which the Fund was firmly constructed. Their hard work and dedication, their foresight and commitment will not be forgotten.

*"I think we might well preserve the essential objective, which is safety ... and offset the ravages of inflation, which I just think is prudent for anybody managing money to consider."*

January, 1981, Trustee Elmer Rasmuson.



From left to right: Arnold Espe, Hugh Malone, Charlie Parr, Elmer Rasmuson, Clyde Sherwood and Robert Ward

Providing benefits to the people of Alaska has always been a critical part of the APFC's mission. Maintaining safety of principal and producing a competitive rate of return are the primary ways the mission is accomplished, but there are other means as well. One is the APFC's Alaska college student internship program.

The intern program, which began in 1988 as a way for the Fund to help young Alaskans gain entry into the field of finance and investing, is a cooperative effort between the APFC and its various investment managers. Students are accepted to intern either directly with the APFC or with one of the managers. In fiscal 2001, there were 18 participating firms and 14 Alaska students were hired.

Designed to serve as a career springboard for Alaska college students, the program has a high success rate of permanent placement. One of the APFC's managers, Kennedy Associates of Seattle, has permanently hired a total of seven Permanent Fund interns.

In addition to investing in our young Alaskans, the APFC provides opportunities for established Alaska money managers. There are currently two such Alaska businesses serving as Permanent Fund investment managers.

Another means by which the Fund contributes to the Alaska economy is the Alaska brokerage program, through which nine Alaska businesses are able to share in the commissions that result from the Fund's stock trades.

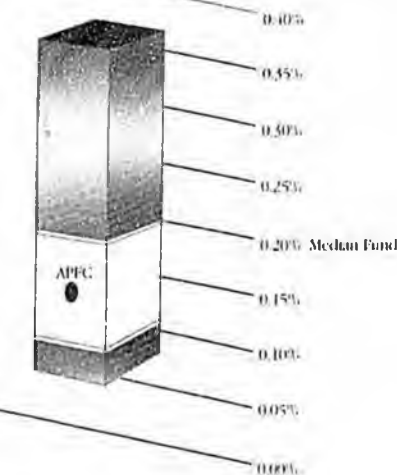
Lastly, the APFC manages three other funds besides the Permanent Fund. See the financial statements footnote 17 for details.

APFC FY01 total operating expenses were \$39.5 million, or .15% of the Fund's average market value. That equates to 15 cents for every \$100 of Fund value — compared to 20 cents for the median large (10 billion plus) institutional fund. Source: APFC and Cullin Associates, Inc.

Management costs for each APFC portfolio are well below median

| Operating expenses by asset class |             |                 |            |                |
|-----------------------------------|-------------|-----------------|------------|----------------|
|                                   | U.S. Stocks | Non-U.S. Stocks | U.S. Bonds | Non-U.S. Bonds |
| APFC                              | .19%        | .27%            | .03%       | .22%           |

APFC operating expenses  
Compare favorably to other large institutional funds



Olivia Mendoza of UAS, an intern this summer with Kennedy Associates in Seattle.

The Board of Trustees  
Alaska Permanent Fund Corporation  
(A Component Unit of the State of Alaska):

We have audited the accompanying statements of assets, liabilities, principal and earnings reserve of the Alaska Permanent Fund as of June 30, 2001 and 2000, and the related statements of revenues and expenses, changes in principal and earnings reserve, and cash flows for the years then ended. These financial statements are the responsibility of the Alaska Permanent Fund Corporation's (a Component Unit of the State of Alaska) management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Alaska Permanent Fund as of June 30, 2001 and 2000, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

**KPMG LLP**

Anchorage, Alaska  
August 10, 2001

*Statements of assets, liabilities, principal and earnings reserve*

| June 30,   | 2001                            | 2000                         |
|--|---------------------------------|------------------------------|
| <b>Assets</b>  |                                 |                              |
| Cash and temporary investments                           | \$ 544,014,000                  | 747,739,000                  |
| Receivables, prepaid expenses and other assets           | 365,158,000                     | 496,173,000                  |
| Investments  |                                 |                              |
| Marketable debt securities                               | 10,005,722,000                  | 9,723,751,000                |
| Preferred and common stock                               | 12,617,711,000                  | 14,663,750,000               |
| Real estate  | 2,504,466,000                   | 2,326,403,000                |
| Alaska certificates of deposit                           | 147,423,000                     | 152,318,000                  |
| Total investments  | <u>25,275,322,000</u>           | <u>26,866,248,000</u>        |
| <b>Total assets</b>                                      | <b><u>\$ 26,184,494,000</u></b> | <b><u>28,110,160,000</u></b> |
| <b>Liabilities</b>                                       |                                 |                              |
| Accounts payable   | \$ 253,160,000                  | 419,018,000                  |
| Income distributable to the State of Alaska              | 1,116,444,000                   | 1,175,231,000                |
| <b>Total liabilities</b>                                 | <b><u>1,369,604,000</u></b>     | <b><u>1,594,249,000</u></b>  |
| <b>Principal and earnings reserve</b>                    |                                 |                              |
| Principal  | 21,047,579,000                  | 20,014,648,000               |
| Earnings reserve   |                                 |                              |
| Unrealized earnings reserve                              | 1,383,576,000                   | 3,528,801,000                |
| Remaining earnings reserve                               | 2,383,735,000                   | 2,972,459,000                |
| Total earnings reserve                                   | <u>3,767,311,000</u>            | <u>6,501,263,000</u>         |
| <b>Total principal and earnings reserve</b>              | <b><u>24,814,890,000</u></b>    | <b><u>26,515,911,000</u></b> |
| <b>Total liabilities, principal and earnings reserve</b> | <b><u>\$ 26,184,494,000</u></b> | <b><u>28,110,160,000</u></b> |

Years ended June 30,

2001

2000

**Revenues**

Investment income —

|                              |                      |                      |
|------------------------------|----------------------|----------------------|
| Interest                     | \$ 710,312,000       | 687,158,000          |
| Dividends                    | 155,551,000          | 166,816,000          |
| Real estate and other income | 225,215,000          | 195,570,000          |
| Total investment income      | <u>1,091,078,000</u> | <u>1,049,544,000</u> |

Net increase (decrease) in the fair value of investments —

|                            |                        |                      |
|----------------------------|------------------------|----------------------|
| Marketable debt securities | 359,608,000            | (334,289,000)        |
| Preferred and common stock | (2,486,857,000)        | 1,547,321,000        |
| Real estate                | 119,877,000            | 29,186,000           |
| Foreign exchange contracts | 37,172,000             | 2,296,000            |
| Currency                   | (5,280,000)            | (3,825,000)          |
| Total gains (losses)       | <u>(1,975,480,000)</u> | <u>1,240,689,000</u> |
| <b>Total revenues</b>      | <b>(884,402,000)</b>   | <b>2,290,233,000</b> |

**Expenses**

|                          |                                |                             |
|--------------------------|--------------------------------|-----------------------------|
| Operating expenses       | <u>(39,490,000)</u>            | <u>(41,457,000)</u>         |
| <b>Net income (loss)</b> | <b>\$ <u>(923,892,000)</u></b> | <b><u>2,248,776,000</u></b> |

Adjustments to bring net income (loss) to statutory net income — settlement earnings and unrealized (gains) losses

|  |                      |                     |
|--|----------------------|---------------------|
|  | <u>2,122,997,000</u> | <u>(26,613,000)</u> |
|--|----------------------|---------------------|

|                             |                                |                             |
|-----------------------------|--------------------------------|-----------------------------|
| <b>Statutory net income</b> | <b>\$ <u>1,199,105,000</u></b> | <b><u>2,222,163,000</u></b> |
|-----------------------------|--------------------------------|-----------------------------|

# Statements of changes in principal and earnings reserve

Years ended June 30,

**2001**

**2000**

## Principal

|                                      |                          |                       |
|--------------------------------------|--------------------------|-----------------------|
| Balance, beginning of year           | \$ 20,014,648,000        | 19,000,909,000        |
| Dedicated state revenues             | 339,315,000              | 310,488,000           |
| State transfer from earnings reserve | —                        | 250,000,000           |
| Inflation-proofing                   | 685,929,000              | 422,920,000           |
| Settlement earnings                  | 7,687,000                | 30,331,000            |
| <b>Balance, end of year</b>          | <b>\$ 21,047,579,000</b> | <b>20,014,648,000</b> |

## Earnings reserve

|                                       |                         |                      |
|---------------------------------------|-------------------------|----------------------|
| Balance, beginning of year            | \$ 6,501,263,000        | 6,131,203,000        |
| Appropriation to other state agencies | (3,843,000)             | (3,014,000)          |
| State transfer from earnings reserve  | —                       | (250,000,000)        |
| Inflation-proofing                    | (685,929,000)           | (422,920,000)        |
| Settlement earnings                   | (7,687,000)             | (30,331,000)         |
| Dividends                             | (1,112,601,000)         | (1,172,451,000)      |
| Net income (loss)                     | (923,892,000)           | 2,248,776,000        |
| <b>Balance, end of year</b>           | <b>\$ 3,767,311,000</b> | <b>6,501,263,000</b> |

## Total

|                                       |                          |                       |
|---------------------------------------|--------------------------|-----------------------|
| Balance, beginning of year            | \$ 26,515,911,000        | 25,132,112,000        |
| Dedicated state revenues              | 339,315,000              | 310,488,000           |
| Appropriation to other state agencies | (3,843,000)              | (3,014,000)           |
| Dividends                             | (1,112,601,000)          | (1,172,451,000)       |
| Net income (loss)                     | (923,892,000)            | 2,248,776,000         |
| <b>Balance, end of year</b>           | <b>\$ 24,814,890,000</b> | <b>26,515,911,000</b> |

## Earnings reserve components

|                               |                         |                      |
|-------------------------------|-------------------------|----------------------|
| Unrealized earnings reserve   | \$ 1,383,576,000        | 3,528,804,000        |
| Remaining earnings reserve    | 2,383,735,000           | 2,972,459,000        |
| <b>Total earnings reserve</b> | <b>\$ 3,767,311,000</b> | <b>6,501,263,000</b> |

| Years ended June 30,  | 2001                   | 2000                 |
|---|------------------------|----------------------|
| <b>Cash flows from investments</b>  |                        |                      |
| Net (purchases), sales and maturities of investments —                      |                        |                      |
| Marketable debt securities  | \$ 23,805,000          | 675,380,000          |
| Preferred and common stock  | (506,180,000)          | (1,505,015,000)      |
| Real estate   | (54,310,000)           | (283,401,000)        |
| Alaska certificates of deposit  | 4,896,000              | (9,903,000)          |
| Net change in unsettled trades  | (53,186,000)           | 38,051,000           |
| Total net (purchases), sales and maturities                                 | (584,975,000)          | (1,084,888,000)      |
| Investment income received  | 1,288,180,000          | 2,302,054,000        |
| Undistributed real estate income  | (34,697,000)           | (25,679,000)         |
| <b>Net cash provided by investments</b>                                     | <b>668,508,000</b>     | <b>1,191,487,000</b> |
| <b>Cash flows from non-capital financing</b>                                |                        |                      |
| Contributions from the state  | 345,382,000            | 282,385,000          |
| Income distributions  | (1,175,231,000)        | (1,048,225,000)      |
| <b>Net cash used by non-capital financing</b>                               | <b>(829,849,000)</b>   | <b>(765,840,000)</b> |
| <b>Cash flows from operations</b>   |                        |                      |
| Net increase (decrease) in cash and temporary investments                   | (42,384,000)           | (39,089,000)         |
| Cash and temporary investments at beginning of year                         | (203,725,000)          | 386,558,000          |
| <b>Cash and temporary investments at end of year</b>                        | <b>747,739,000</b>     | <b>361,181,000</b>   |
| <b>Reconciliation of net income to net cash used by operations</b>          |                        |                      |
| Net income (loss)   | \$ (923,892,000)       | 2,248,776,000        |
| Adjustments to reconcile net income (loss) to net cash used by operations — |                        |                      |
| Investment (earnings) loss  | 884,402,000            | (2,290,233,000)      |
| Net change in prepaid expenses and accrued liabilities                      | (2,894,000)            | 2,368,000            |
| <b>Net cash used by operations</b>  | <b>\$ (42,384,000)</b> | <b>(39,089,000)</b>  |

June 30, 2001 and 2000

### **1. Entity**

The Constitution of the State of Alaska (the "State") was amended by public referendum in 1976 to dedicate a portion of certain natural resource revenues to the Alaska Permanent Fund (the "Fund"). The principal of the Fund is to be invested in perpetuity. The Alaska State Legislature (the "Legislature") created the Alaska Permanent Fund Corporation (the "Corporation"), a component unit of the State that is administered by a board of trustees (the "Trustees"), to manage the investments of the Fund. By statute, (i) a portion of annual earnings is transferred to the State's dividend fund, and (ii) a portion of the earnings reserve account sufficient to offset the impact of inflation is transferred to the principal of the Fund. The balance of the Fund's earnings is held in the earnings reserve account and is subject to appropriation by the Legislature.

The accounting and reporting policies of the Fund conform to generally accepted accounting principles. The Fund follows the accrual method of accounting. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the balance sheet and revenue and expenses for the period. Actual results could differ from those estimates. The more significant accounting and reporting policies applied in the preparation of the accompanying financial statements are discussed in note 2.

### **2. Significant Accounting Policies**

As allowed by the Governmental Accounting Standards Board Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Corporation has elected not to apply Statements and Interpretations issued by the Financial Accounting Standards Board after November 30, 1989.

#### **Contributions**

Contributions from dedicated State revenues are recorded when certain revenues defined by statute are received or reported by the Alaska Department of Natural Resources. Contributions from appropriations and other sources are recorded when received.

#### **Dividend Appropriations**

Current statutes require that one-half of twenty-one percent of the Fund's net income for the last five fiscal years, excluding earnings from contributions made in the North Slope royalty case (*State v. Amerada Hess, et al.*) settlements and unrealized gains and losses, be made available for the payment of dividends and other appropriations each year.

### Forward Exchange Contracts

The Fund is party to a variety of forward contracts in its trading activities and in the management of its foreign exchange rate exposure. These contracts are speculative in nature and the contract amounts do not appear on the balance sheet. Realized and unrealized gains and losses are currently included in net income, and are determined on the maturity date of the contracts. Unrealized gains and losses are calculated using foreign currency forward rates at the balance sheet date.

### Inflation Impact

The impact of inflation is measured by the change in the prior calendar year average of the United States consumer price index for all urban consumers, applied against the balance of contributed equity at the end of the fiscal year. The inflation rates were 3.37% and 2.19% and applied to the years ended June 30, 2001 and 2000, respectively.

### Interest Income

Interest income is accrued monthly as earned.

### Income Taxes

As integral parts of the State, the Fund and the Corporation are not subject to Federal or State income taxes. In addition, the Internal Revenue Code provides that gross income for tax purposes does not include income accruing to a state or any subdivision thereof, which is derived from the exercise of any essential governmental function. The Fund and the Corporation perform an essential governmental function and are therefore exempt from Federal income taxes under that provision, as well.

### Investments

The Fund's marketable securities, excluding direct real estate investments, are reported at fair value in the financial statements. Unrealized gains and losses are reported as components of net income. Fair values are obtained from independent sources for marketable debt and equity securities and real estate investment trusts.

Real estate commingled funds, direct real estate investments and direct commercial mortgages are carried at historical cost plus the Fund's share of undistributed earnings. If, in the opinion of management, a permanent impairment of value has occurred, the investment is written down to fair market value by a charge to operations.

### Securities Transactions

Securities transactions are recorded on the trade date that securities are purchased or sold.

### Statement of Cash Flows

The Fund considers all highly liquid short-term investments purchased with an original maturity of one year or less to be cash equivalents for purposes of the statement of cash flows.

**3. Cash and Temporary Investments**

All cash and temporary investments bear interest at competitive rates, and are summarized as follows at June 30:

|   | 2001                  | 2000               |
|---|-----------------------|--------------------|
| Cash <sup>(a)</sup>                             | \$ 111,649,000        | 99,981,000         |
| U.S. agencies <sup>(b)</sup>                    | 60,839,000            | 212,719,000        |
| Commercial paper <sup>(c)</sup>                 | 271,526,000           | 435,039,000        |
| <b>Total Cash and<br/>Temporary Investments</b> | <b>\$ 544,014,000</b> | <b>747,739,000</b> |

a) Share ownership in a money market fund, payable on demand.

Collateralized by underlying securities held by the fund in the name of the custodian.

b) Debt obligation guaranteed by the U.S. government.

c) Commercial paper rated investment grade.

**4. Receivables, Prepaid Expenses and Other Assets**

Receivables, prepaid expenses and other assets at June 30 are as follows:

|   | 2001                  | 2000               |
|---|-----------------------|--------------------|
| Interest receivable   | \$ 144,902,000        | 173,928,000        |
| Dividends receivable  | 13,973,000            | 13,761,000         |
| Sales receivable  | 154,712,000           | 255,660,000        |
| Foreign exchange contracts                                      | 8,152,000             | 3,337,000          |
| Contributions receivable  | 43,419,000            | 49,487,000         |
| <b>Total Receivables, Prepaid<br/>Expenses and Other Assets</b> | <b>\$ 365,158,000</b> | <b>496,173,000</b> |

### 5. Marketable Debt Securities

The Corporation is authorized by statute to invest Fund assets in (i) corporate bonds rated investment grade; (ii) obligations of the United States Treasury, its agencies and instrumentalities; and (iii) foreign obligations of comparable quality. All marketable debt securities are held by custodian banks in the name of the Corporation on behalf of the Fund.

Marketable debt securities at June 30 are summarized as follows:

|   | Cost                     | Market                | Unrealized<br>Gains/(Losses) |
|---|--------------------------|-----------------------|------------------------------|
| <b>2001</b>                                 |                          |                       |                              |
| Treasury notes/bonds                        | \$ 2,266,045,000         | 2,214,159,000         | (51,886,000)                 |
| Mortgage-backed securities                  | 2,516,102,000            | 2,521,856,000         | 5,754,000                    |
| Other federal agencies                      | 1,657,298,000            | 1,708,042,000         | 50,744,000                   |
| Corporate bonds                             | 2,954,476,000            | 3,005,088,000         | 50,612,000                   |
| Non-domestic bonds                          | 587,719,000              | 556,577,000           | (31,142,000)                 |
| <b>Total Marketable<br/>Debt Securities</b> | <b>\$ 9,981,640,000</b>  | <b>10,005,722,000</b> | <b>24,082,000</b>            |
| <b>2000</b>                                 |                          |                       |                              |
| Treasury notes/bonds                        | \$ 3,234,534,000         | 3,191,033,000         | (43,501,000)                 |
| Mortgage-backed securities                  | 811,435,000              | 786,199,000           | (25,236,000)                 |
| Other federal agencies                      | 1,675,307,000            | 1,650,972,000         | (24,335,000)                 |
| Corporate bonds                             | 3,751,391,000            | 3,587,763,000         | (163,628,000)                |
| Non-domestic bonds                          | 532,778,000              | 507,784,000           | (24,994,000)                 |
| <b>Total Marketable<br/>Debt Securities</b> | <b>\$ 10,005,445,000</b> | <b>9,723,751,000</b>  | <b>(281,694,000)</b>         |

### 6. Preferred and Common Stock

The Corporation is authorized by statute to invest Fund assets in the preferred and common stock of United States and non-domestic corporations. All preferred and common stock investments are held by custodian banks in the name of the Corporation on behalf of the Fund.

The Corporation may invest Fund assets in (i) equity securities up to 55% of total Fund investments, and (ii) other investments, which meet the test of prudence, including those currently authorized by law, up to 5% of total Fund investments.

Preferred and common stocks at June 30 are summarized as follows:

|   | Cost                     | Market                | Unrealized<br>Gains/(Losses) |
|---|--------------------------|-----------------------|------------------------------|
| <b>2001</b>                                 |                          |                       |                              |
| Domestic                                    | \$ 7,608,189,000         | 8,924,945,000         | 1,316,756,000                |
| Non-domestic                                | 3,752,908,000            | 3,692,766,000         | (60,142,000)                 |
| <b>Total Preferred<br/>and Common Stock</b> | <b>\$ 11,361,097,000</b> | <b>12,617,711,000</b> | <b>1,256,614,000</b>         |
| <b>2000</b>                                 |                          |                       |                              |
| Domestic                                    | \$ 7,469,847,000         | 10,297,594,000        | 2,827,747,000                |
| Non-domestic                                | 3,385,069,000            | 4,366,182,000         | 981,113,000                  |
| <b>Total Preferred<br/>and Common Stock</b> | <b>\$ 10,854,916,000</b> | <b>14,663,776,000</b> | <b>3,808,860,000</b>         |

### **7. Real Estate**

The Corporation is authorized by statute to invest Fund assets in real estate improved by substantially rented buildings located in the United States. Real estate investments may take the form of direct equity interests, real estate title-holding entities, real estate investment trusts, real estate operating companies or other entities whose assets consist primarily of real property, debt obligations secured by real property or similar entities. All real estate investments are held by the Corporation in its own name on behalf of the Fund, and are managed by professional real estate management firms. Real estate investment trusts and commercial mortgage backed securities are held by custodian banks in the name of the Corporation on behalf of the Fund.

The carrying value of real estate at June 30 was \$2,504,466,000 in 2001 and \$2,326,403,000 in 2000. Carrying value consists of the equity value of direct real estate investments, commingled funds and commercial mortgages and the market value of real estate investment trusts and commercial mortgage backed securities.

In the ordinary course of business, the Corporation has made commitments related to real estate investments. In the opinion of management, meeting these commitments will not have a material adverse effect on the Corporation's financial position, results of operation or liquidity.

Real estate investments at June 30 are summarized as follows:

|  | Book<br>Value           | Market               | Unrealized<br>Gains/(Losses) |
|--|-------------------------|----------------------|------------------------------|
| <b>2001</b>                              |                         |                      |                              |
| Commingled funds                         | \$ 4,783,000            | 8,984,000            | 4,201,000                    |
| Real estate investment trusts            | 559,071,000             | 651,590,000          | 92,519,000                   |
| Commerical mortgage<br>backed securities | 221,026,000             | 223,773,000          | 2,747,000                    |
| Commercial mortgages                     | 72,035,000              | 72,035,000           | —                            |
| Alaska residential mortgages             | 117,000                 | 117,000              | —                            |
| Direct investments -                     |                         |                      |                              |
| Retail                                   | 398,817,000             | 430,200,000          | 31,383,000                   |
| Office                                   | 625,644,000             | 725,416,000          | 99,772,000                   |
| Industrial                               | 184,223,000             | 197,485,000          | 13,262,000                   |
| Residential                              | 343,484,000             | 388,148,000          | 44,664,000                   |
| <b>Total Real Estate</b>                 | <b>\$2,409,200,000</b>  | <b>2,697,748,000</b> | <b>288,548,000</b>           |
| <b>2000</b>                              |                         |                      |                              |
| Commingled funds                         | \$ 12,338,000           | 18,236,000           | 5,898,000                    |
| Real estate investment trusts            | 510,621,000             | 520,799,000          | 10,178,000                   |
| Commerical mortgage<br>backed securities | 225,937,000             | 221,971,000          | (3,966,000)                  |
| Commerical mortgages                     | 65,644,000              | 64,278,000           | (1,366,000)                  |
| Alaska residential mortgages             | 198,000                 | 198,000              | —                            |
| Direct investments -                     |                         |                      |                              |
| Retail                                   | 385,377,000             | 385,166,000          | (211,000)                    |
| Office                                   | 636,194,000             | 753,364,000          | 117,170,000                  |
| Industrial                               | 172,459,000             | 177,166,000          | 4,707,000                    |
| Residential                              | 311,423,000             | 329,820,000          | 18,397,000                   |
| <b>Total Real Estate</b>                 | <b>\$ 2,320,191,000</b> | <b>2,470,993,000</b> | <b>150,807,000</b>           |

### **8. Alaska Certificates of Deposit**

The Corporation is authorized by statute to invest Fund assets in certificates of deposit or the equivalent instruments of banks, savings and loan associations, mutual savings banks, and credit unions doing business in Alaska. Letters of credit from the Federal Home Loan Bank secure these investments. The market value of these certificates approximates cost.

### **9. Accounts Payable**

Accounts payable at June 30 are summarized as follows:

|                               | <u>2001</u>           | <u>2000</u>        |
|-------------------------------|-----------------------|--------------------|
| Accrued liabilities           | \$ 9,505,000          | 12,398,000         |
| Service fees payable          | 1,754,000             | 3,275,000          |
| Foreign exchange contracts    | 740,000               | 8,051,000          |
| Securities purchased          | 241,161,000           | 395,294,000        |
| <b>Total Accounts Payable</b> | <b>\$ 253,160,000</b> | <b>419,018,000</b> |

**10. Income Distributable to The State of Alaska**

The Legislature appropriated a portion of the Fund's statutory net income for various purposes, including the payment of dividends to qualified residents of the State of Alaska. In addition, the Legislature appropriated a portion of the Fund's earnings reserves to fund various other agency activities. Income distributable to the State at June 30 is summarized as follows:

|                                       | <u>2001</u>                    | <u>2000</u>                 |
|---------------------------------------|--------------------------------|-----------------------------|
| Dividends                             | \$ 1,082,300,000               | 1,142,148,000               |
| Appropriation to the Departments of - |                                |                             |
| Corrections                           | 3,615,000                      | 2,929,000                   |
| Health and Social Services            | 16,147,000                     | 17,518,000                  |
| Revenue                               | 5,099,000                      | 4,985,000                   |
| Public Safety                         | 5,376,000                      | 4,871,000                   |
| Legislature                           | 64,000                         | —                           |
| Total to Dividend Fund                | <u>1,112,601,000</u>           | <u>1,172,451,000</u>        |
| Other agencies                        | <u>3,843,000</u>               | <u>2,780,000</u>            |
| <b>Total Income Distributable</b>     | <b><u>\$ 1,116,444,000</u></b> | <b><u>1,175,231,000</u></b> |

**11. Principal**

The principal balance of the Fund at June 30 is shown as follows:

|                               | <u>2001</u>                     | <u>2000</u>                  |
|-------------------------------|---------------------------------|------------------------------|
| Dedicated State revenues      | \$ 7,070,741,000                | 6,731,426,000                |
| Appropriations from the State | 6,885,906,000                   | 6,885,906,000                |
| Inflation-proofing            | 6,929,350,000                   | 6,243,421,000                |
| Settlement earnings           | <u>161,582,000</u>              | <u>153,895,000</u>           |
| <b>Total Principal</b>        | <b><u>\$ 21,047,579,000</u></b> | <b><u>20,014,648,000</u></b> |

On June 30, 2000, a \$250,000,000 transfer was made from earnings reserve to the principal of the Fund. The transfer was authorized by the Legislature through House Bill 18, "An Act making a special appropriation in an amount not to exceed \$250,000,000 from the earnings reserve account to the principal of the permanent fund; and providing for an effective date."

The Fund received dedicated State revenues from North Slope royalty case (*State v. Amerada Hess, et al.*) settlements. By statute, realized earnings from these settlements are to be treated in the same manner as other Fund income, except that these earnings on settlements are excluded from the dividend calculation. Total realized earnings on settlement principal were \$22,230,000 in 2001 and \$38,638,000 in 2000. Of these amounts, \$14,543,000 and \$8,307,000 during 2001 and 2000 respectively, were added to inflation-proofing. The remaining earnings of \$7,687,000 and \$30,331,000 during 2001 and 2000 respectively, have been added to Fund principal in accordance with law. Accumulated settlement related activity, which is included in the principal balance of the Fund at June 30, is shown as follows:

|                                   | 2001                  | 2000               |
|-----------------------------------|-----------------------|--------------------|
| Settlement -                      |                       |                    |
| Principal                         | \$ 229,242,000        | 215,655,000        |
| Earnings                          | 161,582,000           | 153,895,000        |
| Inflation-proofing                | 62,948,000            | 48,405,000         |
| <b>Total Settlement Principal</b> | <b>\$ 453,772,000</b> | <b>417,955,000</b> |

**12. Investment Income by Source**

Investment income during the years ended June 30 is summarized as follows:

|   | <u>2001</u>          | <u>2000</u>        |
|---|----------------------|--------------------|
| <b>Interest</b>                               |                      |                    |
| Marketable debt securities                    | \$ 656,442,000       | 672,348,000        |
| Alaska certificates of deposit                | 7,633,000            | 8,189,000          |
| Cash and other interest                       | 46,237,000           | 6,621,000          |
| <b>Total Interest</b>                         | <b>\$710,312,000</b> | <b>687,158,000</b> |
| <b>Dividends</b>                              |                      |                    |
| Domestic preferred<br>and common stock        | \$ 89,212,000        | 100,122,000        |
| Non-domestic preferred<br>and common stock    | 66,339,000           | 66,694,000         |
| <b>Total Dividends</b>                        | <b>\$155,551,000</b> | <b>166,816,000</b> |
| <b>Real Estate and Other Income</b>           |                      |                    |
| Real estate interest                          | \$ 22,297,000        | 21,568,000         |
| Real estate dividends                         | 39,130,000           | 34,086,000         |
| Other real estate income                      | 150,226,000          | 129,963,000        |
| Loaned security and other income              | 13,562,000           | 9,953,000          |
| <b>Total Real Estate<br/>and Other Income</b> | <b>\$225,215,000</b> | <b>195,570,000</b> |

Under Statute 37.13.120(f), the Corporation is authorized to enter into securities lending transactions. The Corporation, through an agreement with the Bank of New York (the "Bank"), lends marketable debt and equity securities. These loans are fully collateralized at not less than one hundred two percent (102%) of the market value of the loaned securities for U.S. securities and one hundred five percent (105%) of market value for non-U.S. securities. The Corporation is fully indemnified by the Bank against any loss resulting from a default on a loaned security. The Corporation is able to sell any securities out on loan. The Bank may sell collateral upon borrower default. The Bank receives a fee based on earnings from securities lending. At June 30, 2001, there was \$3,670,925,000 in loaned securities outstanding. During the years ended June 30, 2001 and 2000, there were no losses incurred as a result of securities lending transactions.

### ***13. Net Realized Losses On Currency***

Net realized losses on foreign currency inventory were \$5,280,000 and \$3,825,000 for the years ended June 30, 2001 and 2000, respectively. Currency gains and losses resulting from the purchase and sale of securities are included as part of the net increase or decrease in the fair value of the traded securities.

### ***14. Foreign Exchange Contracts and Off-Balance Sheet Risk***

The Corporation entered into foreign currency forward exchange contracts to buy and sell specified amounts of foreign currencies at specified rates on specified future dates for the purpose of hedging existing cash positions in these currencies. The maturity periods for these contracts ranged from one to five months. At June 30, 2001, the Corporation had net unrealized gains with respect to such contracts.

The counterparties to the foreign currency forward contracts consisted of a diversified group of financial institutions. The Corporation is exposed to credit risk to the extent of non-performance by these counterparties; however, the Corporation considers the risk of default to be remote. The Corporation's market risk is limited to the difference between contractual rates and forward rates at the end of the fiscal year.

The Corporation had net sale contracts outstanding totaling \$8,053,000 and \$263,447,000 for the years ended June 30, 2001 and 2000, respectively. The market value of these contracts, using the forward rate at June 30, 2001 and 2000, was \$506,000 and \$268,228,000, respectively. This resulted in net unrealized gains of \$12,328,000 for the year ended June 30, 2001 and net unrealized losses of \$11,690,000 for the year ended June 30, 2000, including prior year reversals in each year. The Fund had realized gains amounting to \$24,844,000 and \$13,986,000 for the years ended June 30, 2001 and 2000, respectively.

**15. Operating Expenses**

Operating expenses of the Corporation for the years ended June 30 are summarized as follows:

|                                      | <u>2001</u>                 | <u>2000</u>              |
|--------------------------------------|-----------------------------|--------------------------|
| Salaries and benefits                | \$ 2,687,000                | 2,810,000                |
| Travel                               | 235,000                     | 245,000                  |
| Communications                       | 978,000                     | 864,000                  |
| Custody and safekeeping fees         | 1,701,000                   | 2,047,000                |
| Consulting fees                      | 369,000                     | 595,000                  |
| Investment management fees           | 32,135,000                  | 32,784,000               |
| Legal and audit fees                 | 278,000                     | 433,000                  |
| Public information and subscriptions | 245,000                     | 231,000                  |
| Rent                                 | 154,000                     | 308,000                  |
| Property and equipment               | 203,000                     | 340,000                  |
| Other expenses                       | 505,000                     | 800,000                  |
| <b>Total Operating Expenses</b>      | <b><u>\$ 39,490,000</u></b> | <b><u>41,457,000</u></b> |

**16. Pension Plan**

All full-time employees of the Corporation participate in the State of Alaska Public Employees Retirement System (PERS), a multiple employer public employee retirement system. Total salaries and benefits for employees covered by PERS for the years ended June 30, 2001 and 2000 amounted to \$2,687,000 and \$2,810,000, respectively.

Corporation employees are required to contribute 6.13% of their annual salaries to PERS. The Corporation contributes the remaining amounts necessary to pay benefits when due. These contributions represented 8.09% and 8.13% of covered salary expenses in the years ended June 30, 2001 and 2000, respectively.

**17. Investments Managed on Behalf of Other Entities**

By statute, the Alaska Science and Technology Endowment Fund, the Alaska Mental Health Trust Fund and the International Trade and Business Endowment Fund (other funds) are invested by the Corporation under the same investment authority as the Fund is managed. The assets of the other funds are commingled with the assets of the Fund for investment purposes. Earnings are separately allocated to the other funds on the basis of unit and fractional unit shares, which have undivided beneficial interests in the commingled assets equal to the proportion that such shares bear to the total units outstanding. Unit shares are credited to the other funds on the basis of amounts contributed to the investment pool. The following represents the other funds' shares of the commingled net assets, which are not reflected in the accompanying financial statements:

|  | <u>2001</u>                  | <u>2000</u>               |
|--|------------------------------|---------------------------|
| Alaska Science and<br>Technology Endowment Fund    | \$ 106,680,000               | 117,715,000               |
| Alaska Mental<br>Health Trust Fund                 | 306,406,000                  | 327,301,000               |
| International Trade and<br>Business Endowment Fund | <u>5,647,000</u>             | <u>5,917,000</u>          |
| <b>Total Other Funds</b>                           | <b><u>\$ 418,733,000</u></b> | <b><u>450,933,000</u></b> |



***Executive Director  
& Corporate Secretary/Treasurer***

ROBERT D. STORER

Sandra Firestack, Executive Assistant

***Investments***

ALLAN MOORE, CHIEF INVESTMENT OFFICER

Joyce Andrews, Executive Secretary

Rosemarie Santana, Investment Associate

***Fixed Income***

Richard Shafer, Manager of Fixed Income Investments

Jim Parise, Senior Investment Officer/Fixed Income

Steven Eason, Investment Officer/Fixed Income

***Equities***

Michael Bell, Manager of Equities Investments

Christy Leer, Investment Associate

***Real Estate***

Peter Naoroz, Manager of Real Estate Investments

Andrew Donovan, Investment Officer/Real Estate

Christi Grussendorf, Investment Officer/Real Estate

***Chief Operating Officer***

ROBERT N. BARTHOLOMEW

***Administration***

Shawn Lew, Executive Secretary

Freda Westman, Administrative Officer

Kathy Thatcher, Administrative Specialist

Ted Fosket, Procurement Specialist

Lisa Flores, Receptionist/Secretary

***Finance***

CHRIS PHILLIPS, DIRECTOR OF FINANCE

Dawn Vetter, Executive Secretary

Valerie Mertz, Controller

Tobie Putman, Portfolio Accountant

Ruth Danner, Portfolio Accountant

Karen Emberton, Accountant

Jeffrey Holzinger, Accounting Technician

***Information Technology***

MARSHAL KENDZIOREK,

DIRECTOR OF INFORMATION TECHNOLOGY

Rob McKnight, Senior Information Technology Specialist

Andrew Loney, Information Technology Specialist

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JIM KELLY, DIRECTOR OF COMMUNICATIONS

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HJR

17



# FISCAL NOTE

**STATE OF ALASKA**  
**2001 LEGISLATIVE SESSION**

Fiscal Note Number: \_\_\_\_\_  
 Bill Version: HJR 17  
 (H) Publish Date: \_\_\_\_\_

Revision Date/Time (Note if correction): \_\_\_\_\_ Dept. Affected: All Departments  
 Title: Destroy Brady Bill Records BRU: \_\_\_\_\_  
 Sponsor: Rep. Hayes Component: \_\_\_\_\_  
 Requester: House Judiciary Committee Component Number: \_\_\_\_\_

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

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

| OPERATING EXPENDITURES | FY 2002    | FY 2003    | FY 2004    | FY 2005    | FY 2006    | FY 2007    |
|------------------------|------------|------------|------------|------------|------------|------------|
| 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> |

|                             |  |  |  |  |  |  |
|-----------------------------|--|--|--|--|--|--|
| <b>CAPITAL EXPENDITURES</b> |  |  |  |  |  |  |
|-----------------------------|--|--|--|--|--|--|

|                               |  |  |  |  |  |  |
|-------------------------------|--|--|--|--|--|--|
| <b>CHANGE IN REVENUES ( )</b> |  |  |  |  |  |  |
|-------------------------------|--|--|--|--|--|--|

**FUND SOURCE** (Thousands of Dollars)

|                          |            |            |            |            |            |            |
|--------------------------|------------|------------|------------|------------|------------|------------|
| 1002 Federal Receipts    |            |            |            |            |            |            |
| 1003 GF Match            |            |            |            |            |            |            |
| 1004 GF                  |            |            |            |            |            |            |
| 1005 GF/Program Receipts |            |            |            |            |            |            |
| 1037 GF/Mental Health    |            |            |            |            |            |            |
| Other (Specify Type)     |            |            |            |            |            |            |
| <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 (FY2001) cost: 0.0

**POSITIONS**

|           |  |  |  |  |  |  |
|-----------|--|--|--|--|--|--|
| Full-time |  |  |  |  |  |  |
| Part-time |  |  |  |  |  |  |
| Temporary |  |  |  |  |  |  |

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

This bill is not expected to have any fiscal impact.

Prepared by: Heather Nobrega

Phone 465-4990

Representative Norman Rokeberg, House Judiciary Committee  
 Committee Chair

Date 4/27/01

## House Committees

Labor & Commerce  
Military & Veterans Affairs  
State Affairs  
Regulation Review

# Alaska State Legislature Representative Joe Hayes

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*While in Juneau*  
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## Representative Joe Hayes Sponsor Statement

### HJR 17- Destroy Brady Bill Records

When the United States Congress passed the Brady Bill in 1993 to establish a system to keep firearms out of the hands of criminals, it was clear that this system was not to be used by government as a way to monitor legitimate firearm ownership by law-abiding Americans.

The Brady Bill established the "national instant criminal background check system" to check criminal backgrounds during firearm purchases. In order to ensure that non-criminal records were not retained, language was included that directly addressed this fundamental issue. Under the section referring to lawful firearm purchases, the code clearly states the intent to "destroy all records of the system with respect to the call (other than the identifying number and the date the number was assigned) and all records of the system relating to the person or the transfer."<sup>1</sup>

The problem arose when the Administration gave this clear statutory language a novel interpretation. Final regulations purporting to implement the Brady Bill state that all information regarding legitimate firearm purchases would be retained for "audit" purposes and "will be destroyed after not more than six months after the transfer is allowed."<sup>2</sup>

By extending the holding of non-criminal records for up to one hundred and eighty days, the Administration has violated both the spirit and letter of the original Brady Bill.

HJR 17 urges the President of the United States and the Congress to prevent federal agencies from using the Brady Bill Act as a vehicle to unlawfully collect data about legitimate firearm owners. HJR 17 also requests that necessary statutory changes be implemented to ensure this does not occur again in the future.

I respectfully ask you to join me in seeing that this message is clearly heard at our nation's capitol.

<sup>1</sup> 18 USC Sec. 922 (t)(2)(c)

<sup>2</sup> 28 CFR Sec. 25.9 (a) (1)

# **Alaska Civil Liberties Union**

*An Affiliate of the American Civil Liberties Union*

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Phone: (907) 258-0044 Fax: (907) 258-0288 Email: akclu@alaska.net

February 28, 2001

## **ALASKA CIVIL LIBERTIES UNION STATEMENT IN SUPPORT OF HOUSE JOINT RESOLUTION NO. 17**

The Alaska Civil Liberties Union (AkCLU) strongly supports the passage of House Joint Resolution Number Seventeen. The AkCLU believes that the privacy of an individual is directly affected by the collection, maintenance, use and dissemination of personal information by government agencies and the private sector. The increasing use of computers and sophisticated information technology has substantially magnified the harm to individual privacy that can occur from any collection, use, maintenance or dissemination of personal information. The AkCLU supports HJR 17 because it urges the government to destroy lawfully collected information once that information is no longer necessary to carry out the government's purpose.

Government agencies and the private sector possess billions of records containing personal information, and there is often no provision or plan for disposal of that information in such a way that the privacy of the individual is protected. The collection and use of such enormous quantities of personal information raise a number of privacy and civil liberties concerns. Presently, many government agencies have nearly unrestrained access to each other's computerized record systems containing personal, sensitive information. Although much of the information is initially given voluntarily by individuals to government agencies, those agencies then match and verify separate record systems for purposes unrelated to their initial collection.

There is a danger in the aggregation and linking of multiple agency databases. Databases maintained for purposes of the Brady Bill in the Department of Justice and the Federal Bureau of Investigation may become or already are linked to other agency databases such as those maintained by the Internal Revenue Service, the Immigration and Naturalization Services, Health and Human Services or other agencies. The government, including state government, is increasingly moving towards the instant linkage of separate databases in order to verify information. Information collected for purposes of the Brady Bill should be destroyed consistent with the intent of the law. It should not be maintained nor spread to other databases.

It is nearly impossible for individuals to control information about themselves once it is in the hands of the government. Computer-driven techniques such as data matching and front-end verification make it possible for information to be stored in decentralized databases but then matched, merged or verified with information in one or more separate databases. A centralized national data bank is no longer necessary given the new technologies.

HJR 17 position paper -- AkCLU  
Page 2 of 2

The Alaska Civil Liberties Union supports efforts on the part of government entities and the private sector to properly dispose of information collected provided that such information is originally gathered for a necessary and legitimate purpose. The fact that an agency may have been justified in collecting such information does not justify maintaining the information if it is not necessary for a lawful government purpose. The AkCLU urges the members of the legislature to pass HJR 17.

Please feel free to contact me if you have any questions or civil liberties concerns. Thank you very much for your consideration of this matter.

Very truly yours,

Jennifer Rudinger  
Executive Director



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CFR s 25.9  
28 C.F.R. § 25.9

**CODE OF FEDERAL REGULATIONS  
TITLE 28--JUDICIAL  
ADMINISTRATION  
CHAPTER I--DEPARTMENT OF  
JUSTICE  
PART 25--DEPARTMENT OF JUSTICE  
INFORMATION SYSTEMS  
SUBPART A--THE NATIONAL  
INSTANT CRIMINAL BACKGROUND  
CHECK SYSTEM**

Current through January 1, 1999; 63 FR  
72352

§ 25.9 Retention and destruction of records in  
the system.

(a) The NICS will retain NICS Index records that indicate that receipt of a firearm by the individuals to whom the records pertain would violate Federal or state law. The NICS will retain such records indefinitely, unless they are canceled by the originating agency. In cases where a firearms disability is not permanent, e.g., a disqualifying restraining order, the NICS will automatically purge the pertinent record when it is no longer disqualifying. Unless otherwise removed, records contained in the NCIC and III files that are accessed during a background check will remain in those files in accordance with established policy.

(b) The FBI will maintain an automated NICS Audit Log of all incoming and outgoing transactions that pass through the system.

(1) The Audit Log will record the following information: type of transaction (inquiry or response), line number, time, date of inquiry, header, message key, ORI, and inquiry/response data (including the name and other identifying information about the prospective transferee and the NTN). In cases of allowed transfers, all information in the

Audit Log related to the person or the transfer, other than the NTN assigned to the transfer and the date the number was assigned, will be destroyed after not more than six months after the transfer is allowed. Audit Log records relating to denials will be retained for 10 years, after which time they will be transferred to a Federal Records Center for storage. The NICS will not be used to establish any system for the registration of firearms, firearm owners, or firearm transactions or dispositions, except with respect to persons prohibited from receiving a firearm by 18 U.S.C. 922(g) or (n) or by state law.

(2) The Audit Log will be used to analyze system performance, assist users in resolving operational problems, support the appeals process, or support audits of the use of the system. Searches may be conducted on the Audit Log by time frame, i.e., by day or month, or by a particular state or agency. Information in the Audit Log pertaining to allowed transfers may only be used by the FBI for the purpose of conducting audits of the use and performance of the NICS. Such information, however, may be retained and used as long as needed to pursue cases of identified misuse of the system. The NICS, including the NICS Audit Log, may not be used by any department, agency, officer, or employee of the United States to establish any system for the registration of firearms, firearm owners, or firearm transactions or dispositions. The Audit Log will be monitored and reviewed on a regular basis to detect any possible misuse of the NICS data.

(c) The following records in the FBI-operated terminals of the NICS will be subject to the Brady Act's requirements for destruction:

(1) All inquiry and response messages

(regardless of media) relating to a background check that results in an allowed transfer; and

(2) All information (regardless of media) contained in the NICS Audit Log relating to a background check that results in an allowed transfer.

(d) The following records of state and local law enforcement units serving as POCs will be subject to the Brady Act's requirements for destruction:

(1) All inquiry and response messages (regardless of media) relating to the initiation and result of a check of the NICS that allows a transfer that are not part of a record system created and maintained pursuant to independent state law regarding firearms transactions; and

(2) All other records relating to the person or the transfer created as a result of a NICS check that are not part of a record system created and maintained pursuant to independent state law regarding firearms transactions.

<General Materials (GM) - References, Annotations, or Tables>

28 C. F. R. § 25.9

28 CFR § 25.9

END OF DOCUMENT

**§ 4.24 General disclosures required.**

(v) \* \* \*

(3) Must be placed as follows, unless otherwise specified by Commission rules, provided that where a two-part document is used pursuant to rules promulgated by a registered futures association pursuant to Section 17(j) of the Act, all supplemental information must be provided in the second part of the two-part document:

3. Section 4.25 is amended by revising paragraph (c)(5) introductory text to read as follows:

**§ 4.25 Performance disclosures.**

(c) \* \* \*

(5) With respect to commodity trading advisors and investor pools for which performance is not required to be disclosed pursuant to § 4.25(c)(3) and (4), the pool operator must provide a summary description of the performance history of each of such advisors and pools including the following information, provided that where the pool operator uses a two-part document pursuant to the rules promulgated by a registered futures association pursuant to Section 17(j) of the Act, such summary description may be provided in the second part of the two-part document:

Dated: October 26, 1998.

By the Commission.

Jean A. Webb,

Secretary of the Commission.

[FR Doc. 98-29102 Filed 10-29-98; 8:45 am]

BILLING CODE 6351-01-P

**DEPARTMENT OF JUSTICE****28 CFR Part 25**

[AG Order No. 2186-98]

RIN 1105-AA51

**National Instant Criminal Background Check System Regulation**

**AGENCY:** Federal Bureau of Investigation, Department of Justice.

**ACTION:** Final rule.

**SUMMARY:** The United States Department of Justice (DOJ) is publishing a final rule implementing the National Instant Criminal Background Check System (NICS) pursuant to the Brady Handgun Violence Prevention Act ("Brady Act"), to provide notice of the establishment of the NICS, to establish policies and procedures for ensuring the privacy and security of this system, and to

implement a NICS appeals policy for persons denied acquisition of a firearm based on information in the NICS that they believe to be erroneous or incomplete.

**EFFECTIVE DATE:** November 30, 1998.

**FOR FURTHER INFORMATION CONTACT:** Emmet A. Rathbun, Unit Chief, Federal Bureau of Investigation, Module C-3, 1000 Custer Hollow Road, Clarksburg, West Virginia 26306-0147, telephone number (304) 625-2000.

**SUPPLEMENTARY INFORMATION:** This rule finalizes two notices of proposed rulemaking: the National Instant Criminal Background Check System Regulation published in the Federal Register on June 4, 1998 (63 FR 30430), and the National Instant Criminal Background Check System User Fee Regulation, published in the Federal Register on August 17, 1998 (63 FR 43893). The FBI accepted comments on the proposed rules from interested parties until September 16, 1998, and approximately 2,000 comments were received.

In publishing this final rule, the Department also is giving notice, pursuant to section 103(d) of the Brady Act, Public Law 103-159, 107 Stat. 1536, to Federal Firearm Licensees (FFLs) and the chief law enforcement officer of each state that the NICS is established as of October 31, 1998. With limited exceptions, FFLs are required by the Brady Act to begin contacting the system beginning on November 30, 1998, thirty days after the establishment of the system, before they may transfer a firearm to a non-licensee. FFLs shall contact the NICS by contacting either the FBI NICS Operations Center or a state point of contact (POC) for the NICS, as specified by the Bureau of Alcohol, Tobacco, and Firearms (ATF), United States Department of the Treasury. The ATF will notify each FFL of the method by which FFLs must contact the NICS in their state.

**Significant Comments or Changes****The NICS User Fee**

The largest number of comments pertained to the FBI's proposed user fee to be charged FFLs that contact the FBI NICS Operations Center directly for a NICS background check. All of those who commented on the proposed user fee opposed the fee. This issue was the subject of Congressional action since the time of the initial publication of the proposed NICS rule. The Omnibus Appropriations Act for fiscal year 1999 provided additional monies to the FBI to fund the operation of the NICS and prohibited the FBI from charging a fee for NICS checks. Accordingly, the FBI

will not be charging the user fee set forth in the proposed NICS user fee regulation. This does not preclude state or local agencies acting as POCs for the NICS from charging such fees as may be appropriate under state or local law.

**The NICS Audit Log**

A significant number of comments were received opposing the retention by the NICS of a temporary log of background check transactions that allow a firearm transfer to proceed. Most of these comments expressed an opinion that such a log would constitute a national firearms registry, the establishment of which is prohibited by the Brady Act.

The FBI will not establish a federal firearms registry. The FBI is expressly barred from doing so by section 103(i) of the Brady Act. In order to meet her responsibility to maintain the integrity of Department systems, however, the Attorney General must establish an adequate system of oversight and review. Consequently, the FBI has proposed to retain records of approved transactions in an audit log for a limited period of time solely for the purpose of satisfying the statutory requirement of ensuring the privacy and security of the NICS and the proper operation of the system. Although the Brady Act mandates the destruction of all personally identified information in the NICS associated with approved firearms transactions (other than the identifying number and the date the number was assigned), the statute does not specify a period of time within which records of approvals must be destroyed. The Department attempted to balance various interests involved and comply with both statutory requirements by retaining such records in the NICS Audit Log for a limited, but sufficient, period of time to conduct audits of the NICS.

The NICS Audit Log will contain information relating to each NICS background check requested by FFLs and will allow the FBI to audit use of the system by FFLs and POCs. By auditing the system, the FBI can identify instances in which the NICS is used for unauthorized purposes, such as running checks of people other than actual gun transferees, and protect against the invasions of privacy that would result from such misuse. Audits can also determine whether potential handgun purchasers or FFLs have stolen the identity of innocent and unsuspecting individuals or otherwise submitted false identification information, in order to thwart the name check system. The Audit Log will also allow the FBI to perform quality control checks on the

system's operation by reviewing the accuracy of the responses given by the NICS record examiners to gun dealers.

Under the proposed rule, personally identified information in the NICS Audit Log associated with allowed transfers would be destroyed after eighteen months. Because of the numerous comments objecting to this retention period as too long, the Department reexamined the time period needed to perform audits of the NICS. In light of the statutory requirement that records for allowed transfers be destroyed, and the countervailing statutory requirement to provide for system privacy and security, the Department determined that the general retention period for records of allowed transfers in the NICS Audit Log should be the minimum reasonable period for performing audits on the system, but in no event more than six months. Section 25.9(b) in the final rule was revised to reflect this and to provide that such information may be retained for a longer period if necessary to pursue identified cases of misuse of the system. The Department further determined that the FBI shall work toward reducing the retention period to the shortest practicable period of time less than six months that will allow basic security audits of the NICS. By February 28, 1999, the Department will issue a notice of a proposed revision of the regulation setting forth a further reduced period of retention that will be observed by the system.

Various comments expressed concern that the Audit Log would allow POCs and law enforcement agencies access to records of approved transfers. This is not a well-founded concern because only the FBI will be able to access information in the transaction log. Section 25.9(b)(1) of the final rule was revised to provide explicitly that such information is available only to the FBI, and only for the purposes of conducting audits of the use and performance of the NICS or pursuing cases of misuse of the system.

There were also suggestions in the comments that more specific language be added to the final rule setting forth requirements for the FBI to ensure that transaction logs of the separate National Crime Information Center (NCIC) record system also be destroyed to the extent they reflect allowed firearm transfers. The NCIC information system is separate from the NICS. Nonetheless, the FBI has taken steps to preclude transaction logging of personally identified information in either NCIC or the Interstate Identification Index (III) that would pertain to allowed firearm transactions. Thus, the only logging of

this information by the FBI is in the NICS Audit Log. Similar steps will be taken to prevent such logging in the future FBI information systems NCIC 2000 and the Integrated Automated Fingerprint Identification System (IAFIS) as soon as practicable, but in no event more than one year after those systems come on-line in July 1999. For NICS disaster recovery, a tape of each weekly, full system backup will be maintained in an off-site location for up to six months. Full system backup tapes will also be stored locally to recycle the off-site storage. The FBI keeps no systematic paper copies of transactions.

Finally, comments were received from state and local law enforcement agencies that will serve as POCs seeking clarification that none of the information about NICS checks in state record systems that they maintain pursuant to state law will be subject to the record destruction requirement. The proposed rule provided: (1) that POC records of inquiry and response messages relating to the initiation and result of a NICS check that allows a transfer must be destroyed; and (2) that POC records of NICS checks that the POC processes that are part of a state record system created and maintained in accordance with state law are not subject to the Brady Act record destruction requirement. Sections 25.9(d)(1) and (2) of the final rule were revised to make it clear that the referenced state records of allowed transfers would not be subject to the Brady Act record destruction requirement if they are part of a record system created and maintained pursuant to independent state law regarding firearms transfers. The reason for this clarification is to avoid interfering with state regulation of firearms. If a state is performing a gun eligibility check under state law, and state law requires or allows the retention of the records of those checks, the state's retention of records of the concurrent performance of a NICS check would not add any more information about gun ownership than the state already retains under its own law.

#### *NICS Checks on Pawnshop Redemptions and Gunsmith Transactions*

A significant number of comments on this rule pertained to conducting background checks on firearms redeemed from pawnshops and firearms that were the subject of repair or modification by a gunsmith. Although the Brady Act requires the Attorney General to establish a national instant criminal background check system, it is the Secretary of Treasury through the

ATF who defines what constitutes a firearms transfer, how long a background check is valid, which firearm permits constitute a substitute or alternative to a background check, and the recordkeeping requirements for FFLs. The ATF has issued proposed regulations dealing with these issues. (63 FR 8379). Questions and comments about these matters should be directed to the ATF.

A number of comments from the pawnbrokers' industry addressed the circumstances that will develop when a person redeems a firearm from pawn but the firearm cannot be transferred back to the individual because of a disqualifying word found by the NICS check. The U.S. Department of Treasury Fiscal Year 1999 appropriations legislation includes a provision to allow pawnbrokers the option of requesting a NICS background check at the time a person offers the firearm for pawn. An additional check would still be necessary at the time of redemption. NICS will be made available to pawnbrokers for this purpose. No change in the rule is necessary to address this.

#### *Use of State Points of Contact*

Some comments questioned the legality of using state POCs to process NICS checks in light of the Supreme Court's decision in *Printz v. United States*, (17 S. Ct. 2365 (1997)), which held that Congress could not compel the states to perform Brady checks. In response to these comments we note that the states that will act as POCs for the NICS are not being required to do so by Federal law or regulation, but will do so voluntarily pursuant to their own state authority. The final rule's definition of a POC acknowledges that a state or local agency serving that function will be doing so by express or implied authority pursuant to state statute or executive order.

Some commenters objected to the use of state or local law enforcement agencies as NICS POCs even if such agencies do so voluntarily. The FBI considers the use of POCs (serving as intermediaries between FFLs and the system) to be an appropriate means to implement the Brady Act. Fostering state and local participation in the NICS is entirely consistent with both our federal form of government and with practices under the Brady Act's interim provision. Moreover, state and local authorities are likely to have readier access to more detailed information than a single centralized processor, such as the FBI, thus resulting in fewer system misses of disqualified persons and enhancing system responsiveness

(i) 5 business days (meaning days on which State offices are open) have elapsed from the date the transferor furnished notice of the contents of the statement to the chief law enforcement officer, during which period the transferor has not received information from the chief law enforcement officer that receipt or possession of the handgun by the transferee would be in violation of Federal, State, or local law; or

(ii) the transferor has received notice from the chief law enforcement officer that the officer has no information indicating that receipt or possession of the handgun by the transferee would violate Federal, State, or local law;

(B) the transferee has presented to the transferor a written statement, issued by the chief law enforcement officer of the place of residence of the transferee during the 10-day period ending on the date of the most recent proposal of such transfer by the transferee, stating that the transferee requires access to a handgun because of a threat to the life of the transferee or of any member of the household of the transferee;

(C)(i) the transferee has presented to the transferor a permit that—

(i) allows the transferee to possess or acquire a handgun; and

(ii) was issued not more than 5 years earlier by the State in which the transfer is to take place; and

(iii) the law of the State provides that such a permit is to be issued only after an authorized government official has verified that the information available to such official does not indicate that possession of a handgun by the transferee would be in violation of the law;

(D) the law of the State requires that, before any licensed importer, licensed manufacturer, or licensed dealer completes the transfer of a handgun to an individual who is not licensed under section 923, an authorized government official verify that the information available to such official does not indicate that possession of a handgun by the transferee would be in violation of law;

(E) the Secretary has approved the transfer under section 5812 of the Internal Revenue Code of 1986; or

(F) on application of the transferor, the Secretary has certified that compliance with subparagraph (A)(iii) is impracticable because—

(i) the ratio of the number of law enforcement officers of the State in which the transfer is to occur to the number of square miles of land area of the State does not exceed 0.0025;

(ii) the business premises of the transferor at which the transfer is to occur are extremely remote in relation to the chief law enforcement officer; and

(iii) there is an absence of telecommunications facilities in the geographical area in which the business premises are located.

(2) A chief law enforcement officer to whom a transferor has provided notice pursuant to paragraph (1)(A)(iii) shall make a reasonable effort to ascertain within 5 business days whether receipt or possession would be in violation of the law, including research in whatever State and local record-keeping systems are available and in a national system designated by the Attorney General.

(3) The statement referred to in paragraph (1)(A)(i) shall contain only—

(A) the name, address, and date of birth appearing on a valid identification document (as defined in section 102B(d)(1)) of the transferee containing a photograph of the transferee and a description of the identification used;

(B) a statement that the transferee—

(i) is not under indictment for, and has not been convicted in any court of, a crime punishable by imprisonment for a term exceeding 1 year;

(ii) is not a fugitive from justice;

(iii) is not an unlawful user of or addicted to any controlled substance (as defined in section 102 of the Controlled Substances Act);

(iv) has not been adjudicated as a mental defective or been committed to a mental institution;

(v) is not an alien who is illegally or unlawfully in the United States;

(vi) has not been discharged from the Armed Forces under dishonorable conditions; and

(vii) is not a person who, having been a citizen of the United States, has renounced such citizenship;

(C) the date the statement is made; and

(D) notice that the transferee intends to obtain a handgun from the transferor.

(4) Any transferor of a handgun who, after such transfer, receives a report from a chief law enforcement officer containing information that receipt or possession of the handgun by the transferee violates Federal, State, or local law shall, within 1 business day after receipt of such request, communicate any information related to the transfer that the transferor has about the transfer and the transferee to—

(A) the chief law enforcement officer of the place of business of the transferor; and

(B) the chief law enforcement officer of the place of residence of the transferee.

(5) Any transferor who receives information, not otherwise available to the public, in a report under this subsection shall not disclose such information except to the transferee, to law enforcement authorities, or pursuant to the direction of a court of law.

(B)(A) Any transferor who sells, delivers, or otherwise transfers a handgun to a transferee shall retain the copy of the statement of the transferee with respect to the handgun transaction, and shall retain evidence that the transferor has complied with subclauses (iii)

and (iv) of paragraph (1)(A)(i) with respect to the statement.

(B) Unless the chief law enforcement officer to whom a statement is transmitted under paragraph (1)(A)(iv) determines that a transaction would violate Federal, State, or local law—

(i) the officer shall, within 20 business days after the date the transferee made the statement on the basis of which the notice was provided, destroy the statement, any record containing information derived from the statement, and any record created as a result of the notice required by paragraph (1)(A)(iii);

(ii) the information contained in the statement shall not be conveyed to any person except a person who has a need to know in order to carry out this subsection; and

(iii) the information contained in the statement shall not be used for any purpose other than to carry out this subsection.

(C) If a chief law enforcement officer determines that an individual is ineligible to receive a handgun and the individual requests the officer to provide the reason for such determination, the officer shall provide such reasons to the individual in writing within 20 business days after receipt of the request.

(7) A chief law enforcement officer or other person responsible for providing criminal history background information pursuant to this subsection shall not be liable in an action at law for damages—

(A) for failure to prevent the sale or transfer of a handgun to a person whose receipt or possession of the handgun is unlawful under this section; or

(B) for preventing such a sale or transfer to a person who may lawfully receive or possess a handgun.

(8) For purposes of this subsection, the term "chief law enforcement officer" means the chief of police, the sheriff, or an equivalent officer or the designee of any such individual.

(9) The Secretary shall take necessary actions to ensure that the provisions of this subsection are published and disseminated to licensed dealers, law enforcement officials, and the public.

(1)(1) Beginning on the date that is 30 days after the Attorney General notifies licensees under section 103(d) of the Brady Handgun Violence Prevention Act that the national instant criminal background check system is established, a licensed importer, licensed manufacturer, or licensed dealer shall not transfer a firearm to any other person who is not licensed under this chapter, unless—

(A) before the completion of the transfer, the licensee contacts the national instant criminal background check system established under section 103 of that Act;

(B)(i) the system provides the licensee with a unique identification number; or

NICS PROVISIONS OF BRADY

(l) 3 business days (meaning a day, on which State offices are open) have elapsed since the licensee contacted the system, and the system has not notified the licensee that the receipt of a firearm by such other person would violate subsection (g) or (n) of this section; and

(C) the transferor has verified the identity of the transferee by examining a valid identification document (as defined in section 102B(d)(1) of this title) of the transferee containing a photograph of the transferee.

(2) If receipt of a firearm would not violate section 922(g) or (n) or State law, the system shall—

(A) assign a unique identification number to the transfer;

(B) provide the licensee with the number; and

(C) destroy all records of the system with respect to the call (other than the identifying number and the date the number was assigned) and all records of the system relating to the person or the transfer.

(3) Paragraph (1) shall not apply to a firearm transfer between a licensee and another person if—

(A)(i) such other person has presented to the licensee a permit that—

(i) allows such other person to possess or acquire a firearm; and

(ii) was issued not more than 5 years earlier by the State in which the transfer is to take place; and

(ii) the law of the State provides that such a permit is to be issued only after an authorized government official has verified that the information available to such official does not indicate that possession of a firearm by such other person would be in violation of law;

(B) the Secretary has approved the transfer under section 5812 of the Internal Revenue Code of 1986; or

(C) on application of the transferor, the Secretary has certified that compliance with paragraph (1)(A) is impracticable because—

(i) the ratio of the number of law enforcement officers of the State in which the transfer is to occur to the number of square miles of land area of the State does not exceed 0.0025;

(ii) the business premises of the licensee at which the transfer is to occur are extremely remote in relation to the chief law enforcement officer as defined in subsection (s)(B); and

(iii) there is an absence of telecommunications facilities in the geographical area in which the business premises are located.

(4) If the national instant criminal background check system notifies the licensee that the information available to the system does not demonstrate that the receipt of a firearm by such other person would violate subsection

(g) or (n) or State law, and the licensee transfers a firearm to such other person, the licensee shall include in the record of the transfer the unique identification number provided by the system with respect to the transfer.

(5) If the licensee knowingly transfers a firearm to such other person and knowingly fails to comply with paragraph (1) of this subsection with respect to the transfer and, at the time such other person most recently proposed the transfer, the national instant criminal background check system was operating and information was available to the system demonstrating that receipt of a firearm by such other person would violate subsection (g) or (n) of this section or State law, the Secretary may, after notice and opportunity for a hearing, suspend for not more than 6 months or revoke any license issued to the licensee under section 923, and may impose on the licensee a civil fine of not more than \$5,000.

(6) Neither a local government nor an employee of the Federal Government or of any State or local government, responsible for providing information to the national instant criminal background check system, shall be liable in an action at law for damages—

(A) for failure to prevent the sale or transfer of a firearm to a person whose receipt or possession of the firearm is unlawful under this section; or

(B) for preventing such a sale or transfer to a person who may lawfully receive or possess a firearm.

(u) It shall be unlawful for a person to steal or unlawfully take or carry away from the person or the premises of a person who is licensed to engage in the business of importing, manufacturing, or dealing in firearms, any firearm in the licensee's business inventory that has been shipped or transported in interstate or foreign commerce.

(v)(1) It shall be unlawful for a person to manufacture, transfer, or possess a semiautomatic assault weapon.

(2) Paragraph (1) shall not apply to the possession or transfer of any semiautomatic assault weapon otherwise lawfully possessed under Federal law on the date of the enactment of this subsection.

(3) Paragraph (1) shall not apply to—

(A) any of the firearms, or replicas or duplicates of the firearms, specified in Appendix A to this section, as such firearms were manufactured on October 1, 1993;

(B) any firearm that—

(i) is manually operated by bolt, pump, lever, or slide action;

(ii) has been rendered permanently inoperable; or

(iii) is an antique firearm;

(C) any semiautomatic rifle that cannot accept a detachable magazine that holds more than 5 rounds of ammunition; or

(D) any semiautomatic shotgun that cannot hold more than 5 rounds of ammunition in a fixed or detachable magazine.

The fact that a firearm is not listed in Appendix A shall not be construed to mean that paragraph (1) applies to such firearm. No firearm exempted by this subsection may be deleted from Appendix A so long as this subsection is in effect.

(4) Paragraph (1) shall not apply to—

(A) the manufacture for, transfer to, or possession by the United States or a department or agency of the United States or a State or a department, agency, or political subdivision of a State, or a transfer to or possession by a law enforcement officer employed by such an entity for purposes of law enforcement (whether on or off duty);

(B) the transfer to a licensee under title I of the Atomic Energy Act of 1954 for purposes of establishing and maintaining an on-site physical protection system and security organization required by Federal law, or possession by an employee or contractor of such licensee on-site for such purposes or off-site for purposes of licensee-authorized training or transportation of nuclear materials;

(C) the possession, by an individual who is retired from service with a law enforcement agency and is not otherwise prohibited from receiving a firearm, of a semiautomatic assault weapon transferred to the individual by the agency upon such retirement; or

(D) the manufacture, transfer, or possession of a semiautomatic assault weapon by a licensed manufacturer or licensed importer for use purposes of testing or experimentation authorized by the Secretary.

(w)(1) Except as provided in paragraph (2), it shall be unlawful for a person to transfer or possess a large capacity ammunition feeding device.

(2) Paragraph (1) shall not apply to the possession or transfer of any large capacity ammunition feeding device otherwise lawfully possessed on or before the date of the enactment of this subsection.

(3) This subsection shall not apply to—

(A) the manufacture for, transfer to, or possession by the United States or a department or agency of the United States or a State or a department, agency, or political subdivision of a State, or a transfer to or possession by a law enforcement officer employed by such an entity for purposes of law enforcement (whether on or off duty);

(B) the transfer to a licensee under title I of the Atomic Energy Act of 1954 for purposes of establishing and maintaining an on-site physical protection system and security organization required by Federal law, or possession by an employee or contractor of such licensee on-site for such purposes or off-site for purposes of licensee-authorized training or transportation of nuclear materials;

(C) the possession, by an individual who is retired from service with a law enforcement agency and is not otherwise

# AMENDMENTS TO THE CONSTITUTION.

## ARTICLE I.

**Freedom of religion, of speech, and of the press.** Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the government for a redress of grievances.<sup>9</sup>

## ARTICLE II.

**Right to keep and bear arms.** A well regulated militia, being necessary to the security of a free state, the right of the people to keep and bear arms, shall not be infringed.<sup>10</sup>

## ARTICLE III.

**Quartering of soldiers.** No soldier shall, in time of peace be quartered in any house, without the consent of the owner, nor in time of war, but in a manner to be prescribed by law.<sup>11</sup>

## ARTICLE IV.

**Searches and seizures.** The right of the people to be secure in their persons, houses, papers, and effects, against unreasonable searches and seizures, shall not be violated, and no warrants shall issue, but upon probable cause, supported by oath or affirmation, and particularly describing the place to be searched, and the persons or things to be seized.<sup>12</sup>

## ARTICLE V.

**Rights of accused in criminal proceedings; due process; eminent domain.** No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall he be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.<sup>13</sup>

## ARTICLE VI.

**Right to speedy trial, witnesses, etc.** In all criminal prosecutions, the accused shall enjoy the right to a speedy and public trial, by an impartial jury of the state and district wherein the crime shall have been committed, which district shall have been previously ascertained by law, and to be informed of the nature and cause of the accusations; to be

9. Proposed by Congress on September 25, 1789, and declared ratified on December 15, 1791.

10. Proposed by Congress on September 25, 1789, and declared ratified on December 15, 1791.

11. Proposed by Congress on September 25, 1789, and declared ratified on December 15, 1791.

12. Proposed by Congress on September 25, 1789, and declared ratified on December 15, 1791.

13. Proposed by Congress on September 25, 1789, and declared ratified on December 15, 1791.

age v. Scavenius, 539 P.2d 1169 (Alaska 1975).

**Denial of new trial.** — The trial court did not commit an abuse of discretion in denying the state's motion for new trial, where the jury's determination of just compensation was within the range of the testimony. State v. 45,621 Square Feet of Land, 475 P.2d 1161 (Alaska 1970).

**Jury's award of \$0.00 as just compensation to a property owner for the taking of an easement was not patently inadequate or violative of constitutional provisions pertaining to eminent domain.** Scavenius v. City of Anchorage, 539 P.2d 1161 (Alaska 1975).

The taking of an easement does constitute an appropriation of the owner's property regardless of its minuscule effect. But where the property owner failed to object to instructions expressly permitting the entry of an award of no compensation and the difference between an award of \$0.00 compensation and a

nominal sum to which the property owner would have been entitled is de minimus, the failure to award compensation per se did not require reversal. Scavenius v. City of Anchorage, 539 P.2d 1161 (Alaska 1975).

**Inconsistent verdict.** — State was entitled to a new trial on the amount of just compensation required for the taking of an abutting landowner's right of access to a controlled access highway, where the jury's answers to special interrogatories were internally inconsistent and inconsistent with the general verdict and the jury's conclusion that the remaining property was worth more after the taking than the entire parcel was worth before the taking was irreconcilable with its conclusion that the remainder received no special benefit from the highway project. State v. Lewis, 785 P.2d 24 (Alaska 1990).

**Collateral references.** — 26 Am.Jur.2d, Eminent Domain, §§ 7, 13 to 24.

29A C.J.S., Eminent Domain, §§ 4, 21 to 26.

Use or improvement of highway as establishing grade necessary to entitle abutting owner to compensation on subsequent change. 2 ALR3d 985.

Restrictive covenant or right to enforcement thereof as compensable property right. 4 ALR3d 1137.

Zoning as a factor in determination of damages in eminent domain. 9 ALR3d 291.

Deduction of benefits in determining compensation or damages in proceedings involving opening, widening or otherwise altering highway. 13 ALR3d 1149.

Restrictive covenant, existence of, as element in fixing value of property condemned. 22 ALR3d 961.

Eminent domain: right to enter land for preliminary survey or examination. 29 ALR3d 1104.

Attaching or planning in anticipation of improvement taking or damaging of property affected. 37 ALR3d 77.

Cost of substitute facilities as measure of compensation paid to state or municipality for condemnations of public property. 40 ALR3d 143.

Measure of damages for condemnation of cemetery lands. 42 ALR3d 1314.

Traffic noise and vibration from highway as element of damages in eminent domain. 51 ALR3d 860.

Condemned property's location in relation to proposed site of building complex or similar improvement as factor fixing compensation. 51 ALR3d 1050.

Goodwill or "going concern" value as element of lessee's compensation for taking leasehold in eminent domain. 58 ALR3d 566.

Loss of liquor license as compensable in condemnation proceeding. 58 ALR3d 581.

Compensation for diminution in value of remainder of property resulting from taking or use of adjoining

land of others for the same undertaking. 59 ALR3d 488.

Consideration of fact that landowner's remaining land will be subject to special assessment in fixing severance damages. 59 ALR3d 534.

Determination of just compensation for condemnation of billboards or other advertising signs. 73 ALR3d 1122.

Right to condemn property owned or used by private educational, charitable or religious organization. 80 ALR3d 833.

Goodwill as element of damages for condemnation of property on which private business is conducted. 81 ALR3d 198.

Recovery of value of improvements made with knowledge of impending condemnation. 98 ALR3d 504.

Zoning regulations limiting use of property near airport as taking of property. 18 ALR4th 542.

Local use zoning of wetlands or flood plain as taking without compensation. 19 ALR4th 756.

Airport operations or flight of aircraft as constituting taking or damaging of property. 22 ALR4th 863.

Eminent domain: compensability of loss of view from owner's property — state cases. 25 ALR4th 671.

Seizure of property as evidence in criminal prosecution or investigation as compensable taking. 44 ALR4th 360.

Validity, construction, and application of state relocation assistance laws. 49 ALR4th 491.

Inverse condemnation state court class actions. 49 ALR4th 618.

Court appointment of attorney to represent, without compensation, indigent in civil action. 52 ALR4th 1063.

Eminent domain: industrial park or similar development as public use justifying condemnation of private property. 62 ALR4th 1183.

**Section 19. Right to Keep and Bear Arms.** A well-regulated militia being necessary to the security of a free state, the right of the people to keep and bear arms shall not be infringed. The individual right to keep and bear arms shall not be denied or infringed by the State or a political subdivision of the State.

**Effect of amendments.** — The amendment, effective December 30, 1994 (18th Legislature's Legislative Resolve No. 45), added the second sentence.

NOTES TO DECISIONS

**Section 20. Quartering Soldiers.** No member of the armed forces shall in time of peace be quartered in any house without the consent of the owner or occupant, or in time of war except as prescribed by law. The military shall be in strict subordination to the civil power.

**Collateral references.** — 54 Am.Jur.2d, Military and Civil Defense, § 280.

**Section 21. Construction.** The enumeration of rights in this constitution shall not impair or deny others retained by the people.

NOTES TO DECISIONS

**Right of self-representation has been so retained by the people.** — See *McCracken v. State*, 518 P.2d 85 (Alaska 1974).

A prisoner has a right to represent himself in post-conviction relief proceedings. *McCracken v. State*, 518 P.2d 85 (Alaska 1974).

The right to counsel should not be used to bar self-representation. *McCracken v. State*, 518 P.2d 85 (Alaska 1974).

The right to self-representation is not absolute. *McCracken v. State*, 518 P.2d 85 (Alaska 1974).

**Collateral references.** — 16 Am.Jur.2d, Constitutional Law, §§ 7, 280.

**Section 22. Right of Privacy.** The right of the people to privacy is recognized and shall not be infringed. The legislature shall implement this section. [Approved August 22, 1972]

**Cross references.** — For the unprivileged nature of communications to physicians or other licensed practitioners in an effort to unlawfully procure controlled substances, see AS 11.71.360.

**Statute prohibiting felon from residing in dwelling containing firearm.** — Application of AS 11.61.200(a)(10), prohibiting a felon from residing in a dwelling knowing there is a firearm in the dwelling, does not infringe on the constitutional right to keep and bear arms. *Morgan v. State*, 943 P.2d 1208 (Alaska Ct. App. 1997).

acquiring, having, carrying, or using firearms or weapons. 39 ALR4th 967.

Sufficiency of prior conviction to support prosecution under state statute prohibiting persons under indictment for, or convicted of, crime from acquiring, having, carrying, or using firearms or weapons. 39 ALR4th 983.

Validity of state statute proscribing possession or carrying of knife. 47 ALR4th 651.

Validity of state gun control legislation under state constitutional provisions securing the right to bear arms. 86 ALR4th 931.

Federal constitutional right to bear arms. 37 ALR Fed. 696.

6 C.J.S., Armed Services, § 7.

**Qualifications on right of self-representation in post-conviction proceedings.** — See *McCracken v. State*, 518 P.2d 85 (Alaska 1974).

**Criminal R. 39(b) construed in light of this section.** — See *McCracken v. State*, 518 P.2d 85 (Alaska 1974).

Applied in *James v. State*, 739 P.2d 1314 (Alaska Ct. App. 1987); *Garrison v. State*, 762 P.2d 465 (Alaska Ct. App. 1988).

Quoted in *Falke v. Fairbanks N. Star Borough*, 648 P.2d 597 (Alaska 1982).

16 C.J.S., Constitutional Law, §§ 53, 58; 16A C.J.S., Constitutional Law, § 445.

**Effective dates.** — This section took effect October 14, 1972 (7th Legislature's HCS SJR 68 (1972).)

**Opinions of attorney general.** — A legislative auditor may not examine confidential records on file

for state income tax returns and submitted by employees and employees of Labor in connection with of the State Employment Security persons receiving assistance from Health and Social Services under Assistance and Aid to families children were eligible. Such data is protection intended to be afforded under this section of the state constitution. Att'y Gen. No. 8.

- I. General Consideration.
- II. Application.
  - A. Illegal Substances.
  - B. Children.
  - C. Sexual Conduct.
  - D. Professional — Client Relationship.
  - E. State Authority.
  - F. Documents.
  - G. Right of Privacy in Speech.
- III. Practice and Procedure.

I. GENERAL CONSIDERATION

**History of right to privacy.** 525 P.2d 524 (Alaska 1974).

The effect of this section among the specifically enumerated constitution. *Ravin v. State*, 1975; *Woods & Rohde, Inc. v. State*, 565 P.2d 138 (Alaska 1977).

Scope to be afforded right of privacy. The fact that privacy is among the rights in the Alaska Constitution itself, yield answers concerning accorded to this right of privacy. P.2d 494 (Alaska 1975).

The contours of Alaska's right to privacy are not yet firmly established. of necessity must vary dependent text and the often competing the individual. *State v. Glas*, 1978).

The test for what interests Alaska's constitutional right person has exhibited an action of privacy and, second, one that society is prepared to protect. *Hilbers v. Municipality of Anchorage*, 31 (Alaska 1980).

Alaska's constitution, under the right to privacy, contains an explicit right to privacy. *Woods & Rohde, Inc. v. State*, P.2d 138 (Alaska 1977).

While the federal right to privacy is broad, the federal right to privacy is broad reading of the due process amendment or from "emanating from" constitutional provisions, the right guaranteed by an explicit i.e., this section. *Falcon v. State*, Comm'n, 570 P.2d 469 (Alaska 1977).

Thus, state right is broad. — It is clear from both decisional law that the right of privacy of Alaskan citizens is broader than the federal constitutional right. *State v. State*, Dep't of Labor