

# ALASKA PERMANENT FUND PROTECTION ACT

---

Randall Hoffbeck, *Commissioner of Revenue*

Craig W. Richards, *Attorney General*



Centennial Hall  
April 20, 2016

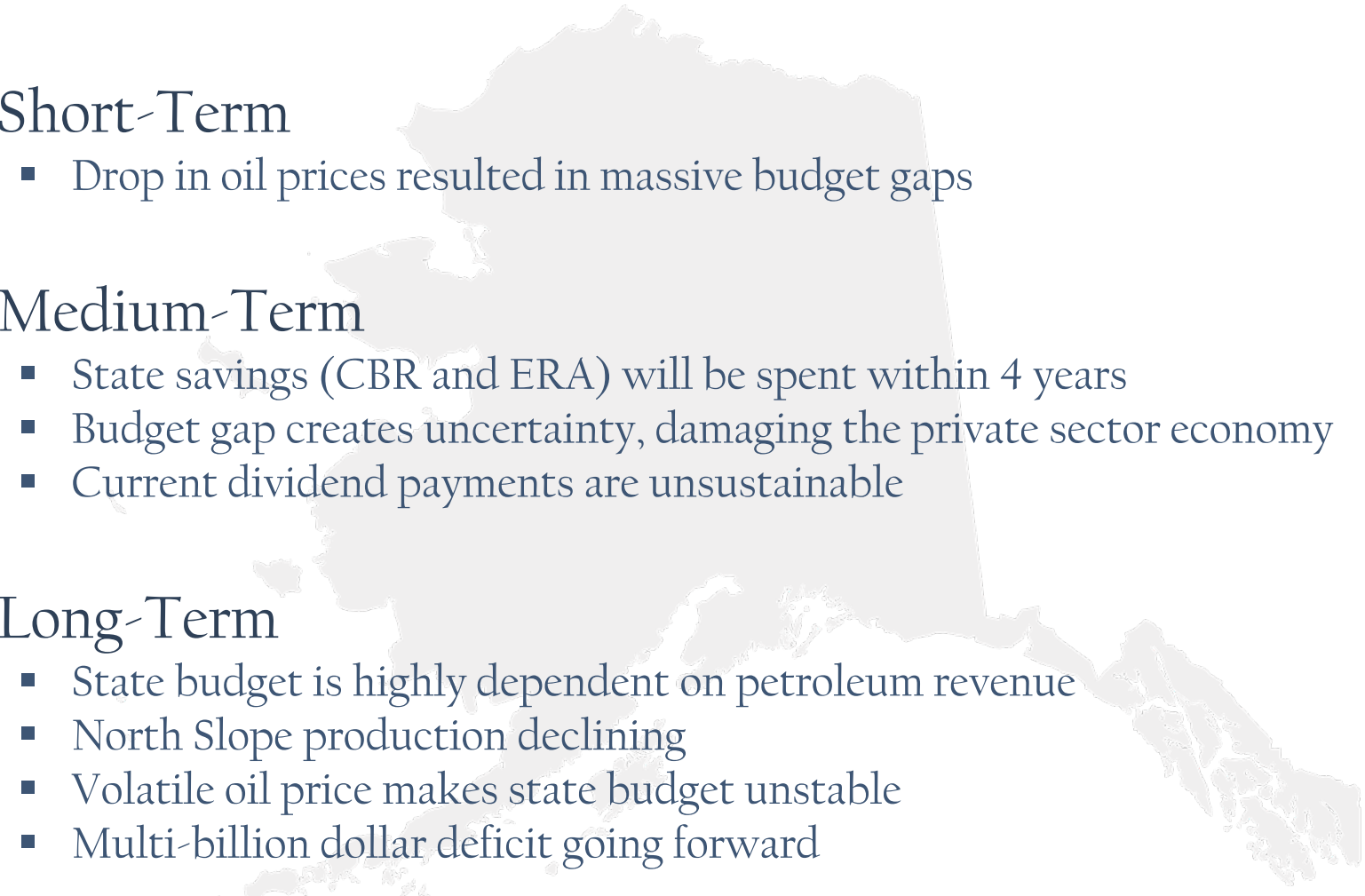


The Fiscal Challenge

---

# DEFINING THE PROBLEM

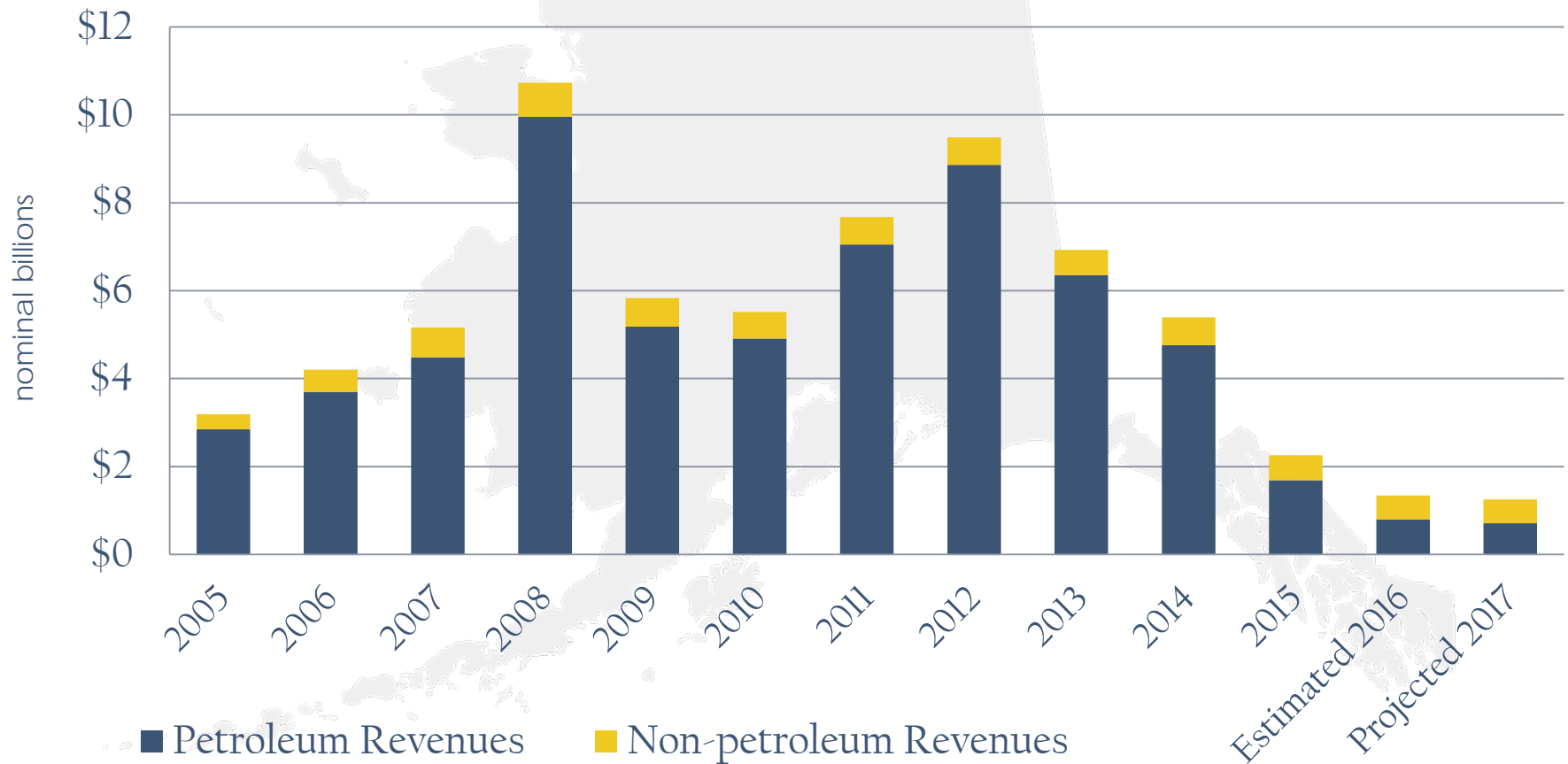
# DEFINING THE PROBLEM

- 
- Short-Term
    - Drop in oil prices resulted in massive budget gaps
  - Medium-Term
    - State savings (CBR and ERA) will be spent within 4 years
    - Budget gap creates uncertainty, damaging the private sector economy
    - Current dividend payments are unsustainable
  - Long-Term
    - State budget is highly dependent on petroleum revenue
    - North Slope production declining
    - Volatile oil price makes state budget unstable
    - Multi-billion dollar deficit going forward

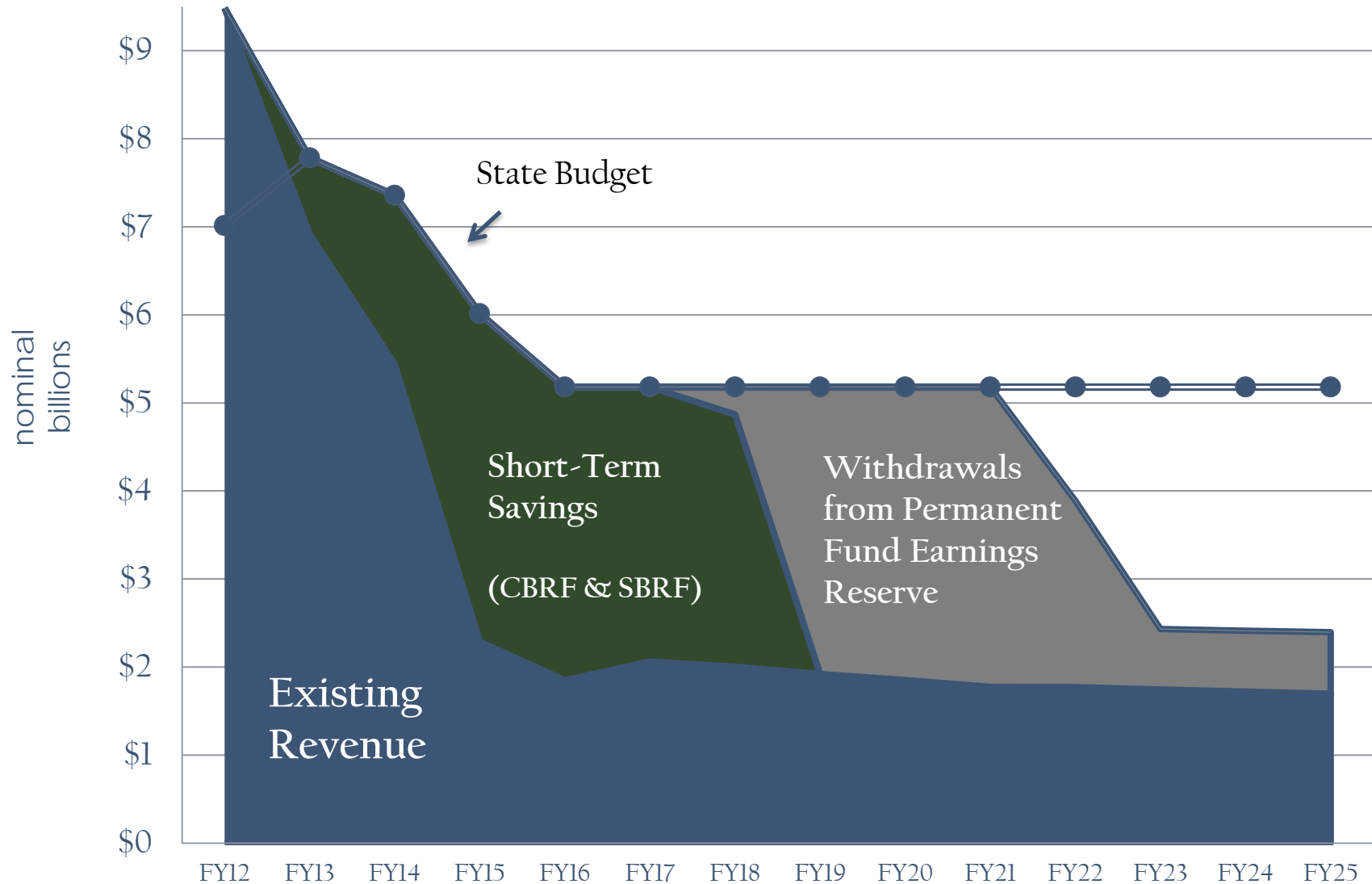


# SHORT-TERM PROBLEM

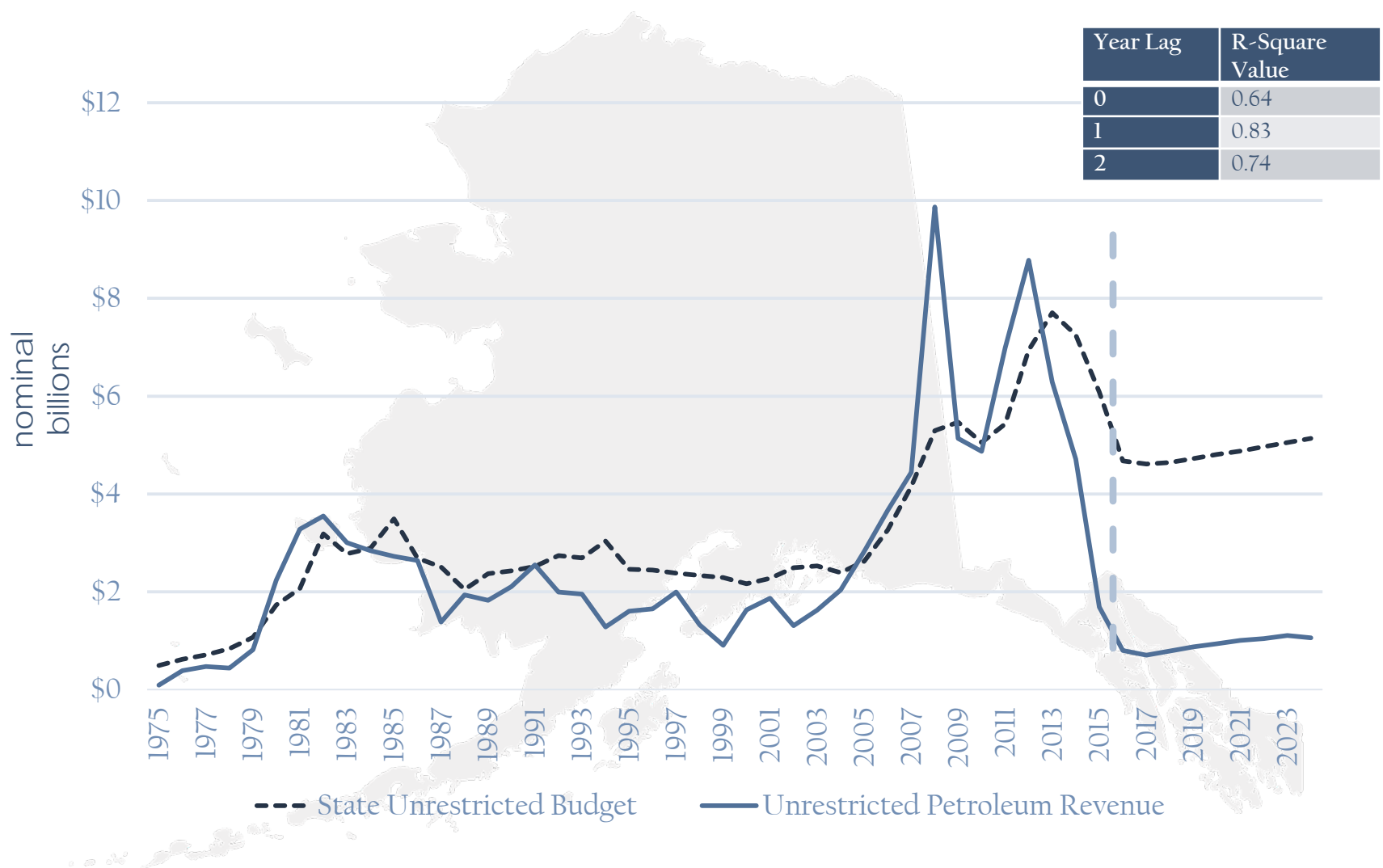
Alaska's Unrestricted General Fund Revenue



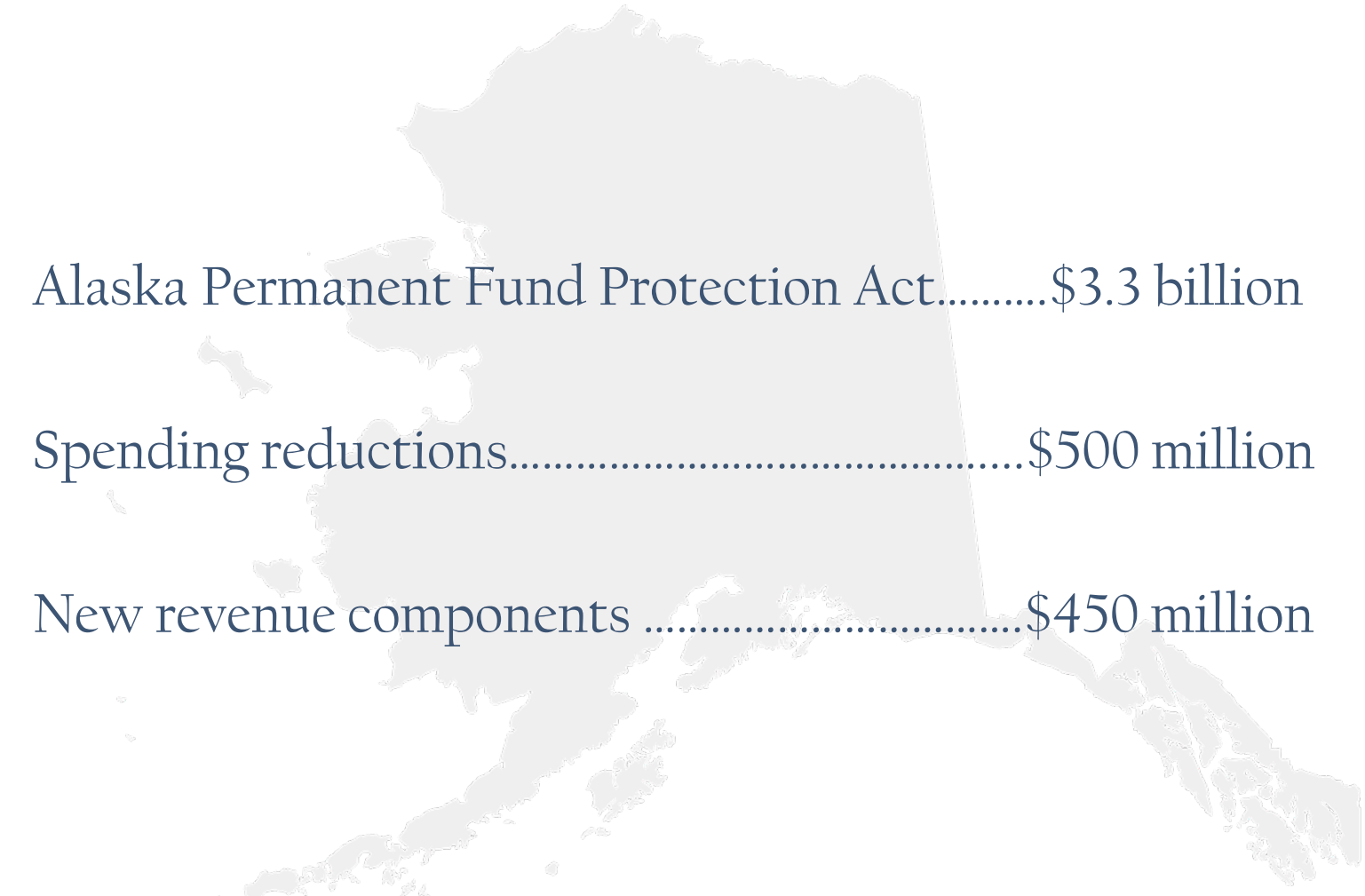
# MEDIUM-TERM PROBLEM



# LONG-TERM PROBLEM



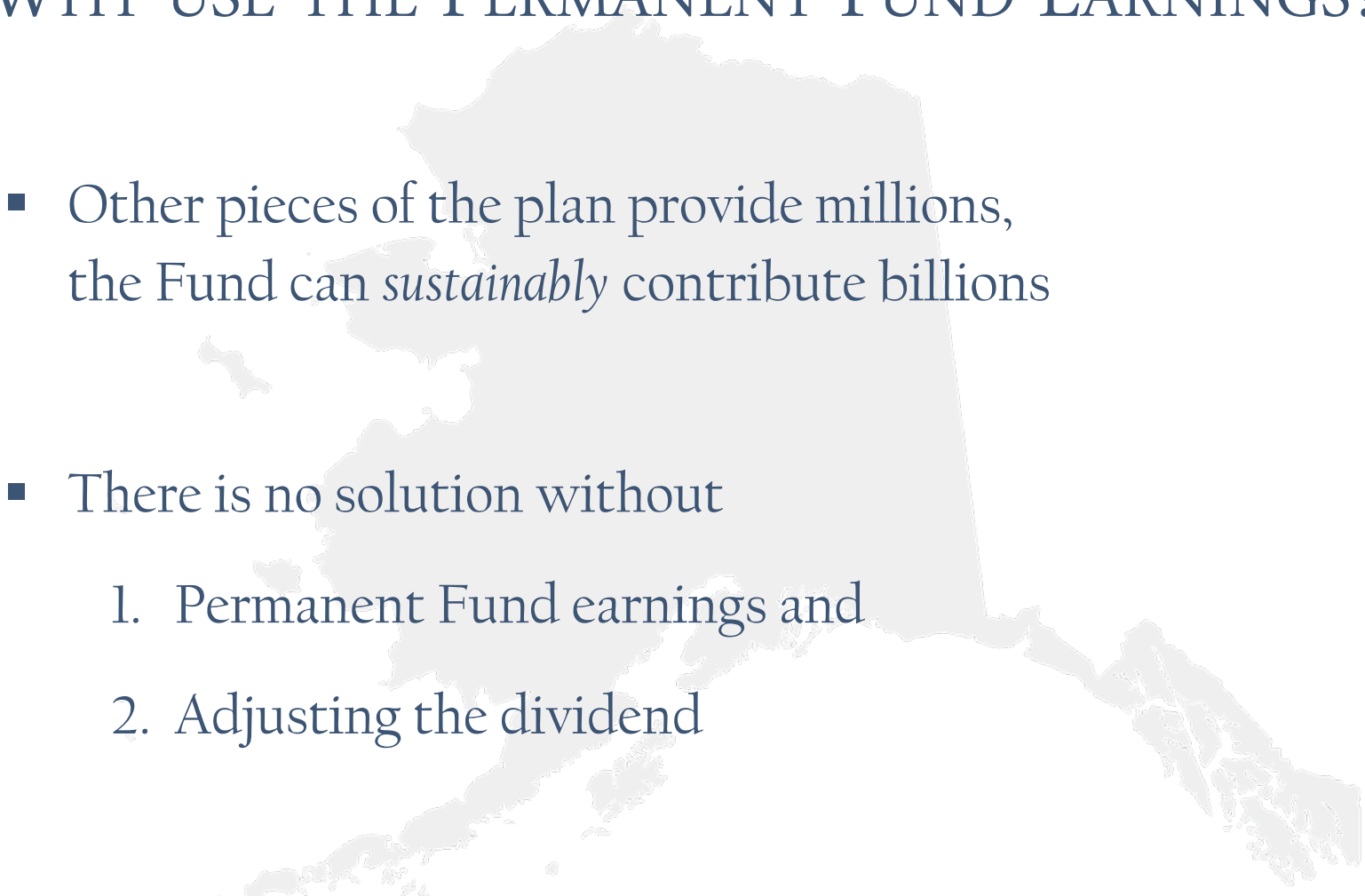
# THE NEW SUSTAINABLE ALASKA PLAN



Alaska Permanent Fund Protection Act.....	\$3.3 billion
Spending reductions.....	\$500 million
New revenue components .....	\$450 million



# WHY USE THE PERMANENT FUND EARNINGS?

- 
- Other pieces of the plan provide millions, the Fund can *sustainably* contribute billions
  - There is no solution without
    1. Permanent Fund earnings and
    2. Adjusting the dividend







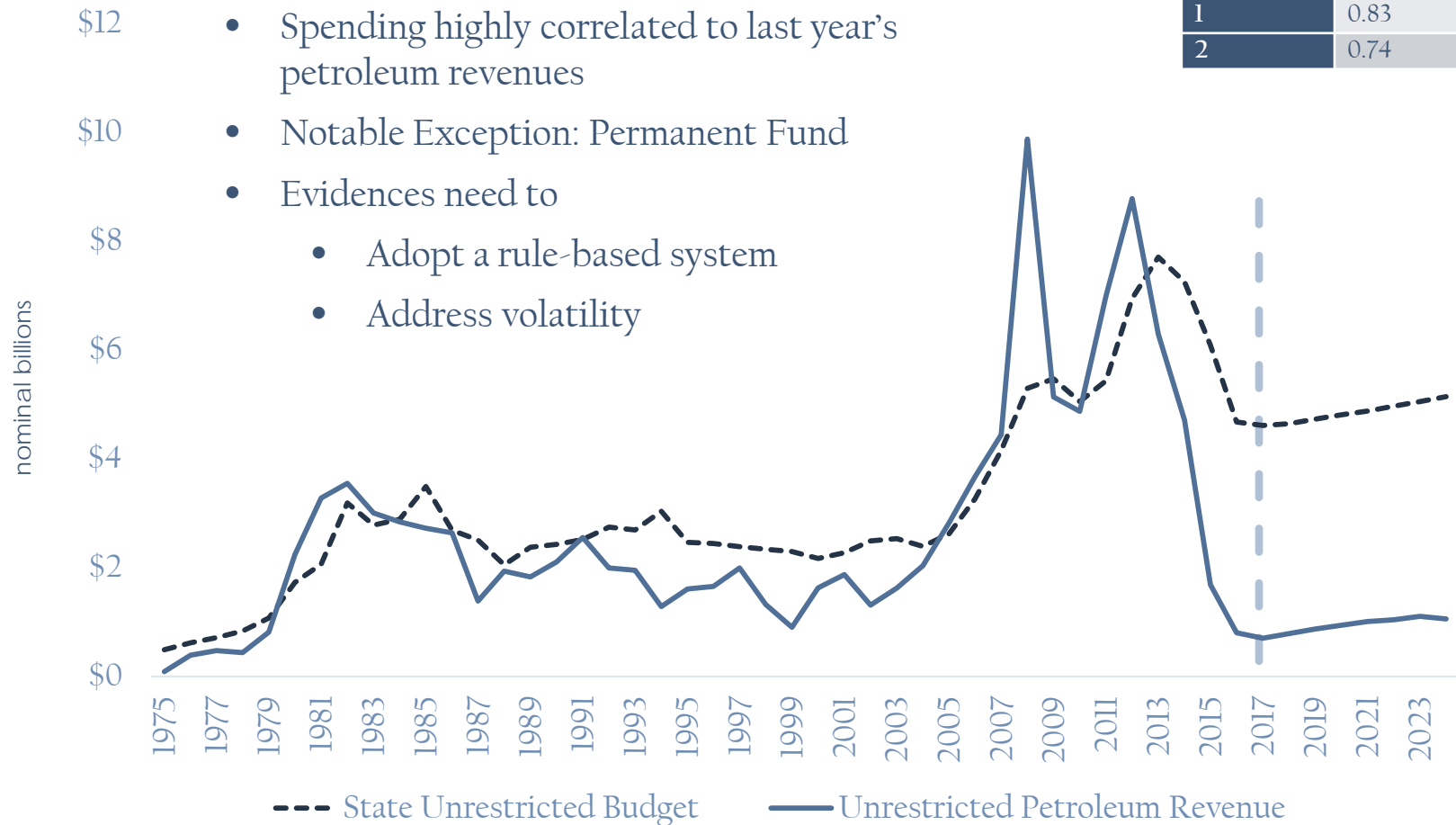
Fiscal Policy for Alaska

---

# ALASKA PERMANENT FUND PROTECTION ACT

# RULE-BASED FRAMEWORK

Year Lag	R-Square Value
0	0.64
1	0.83
2	0.74



# APFPA

Committee Substitute

## 1. 5.25% POMV

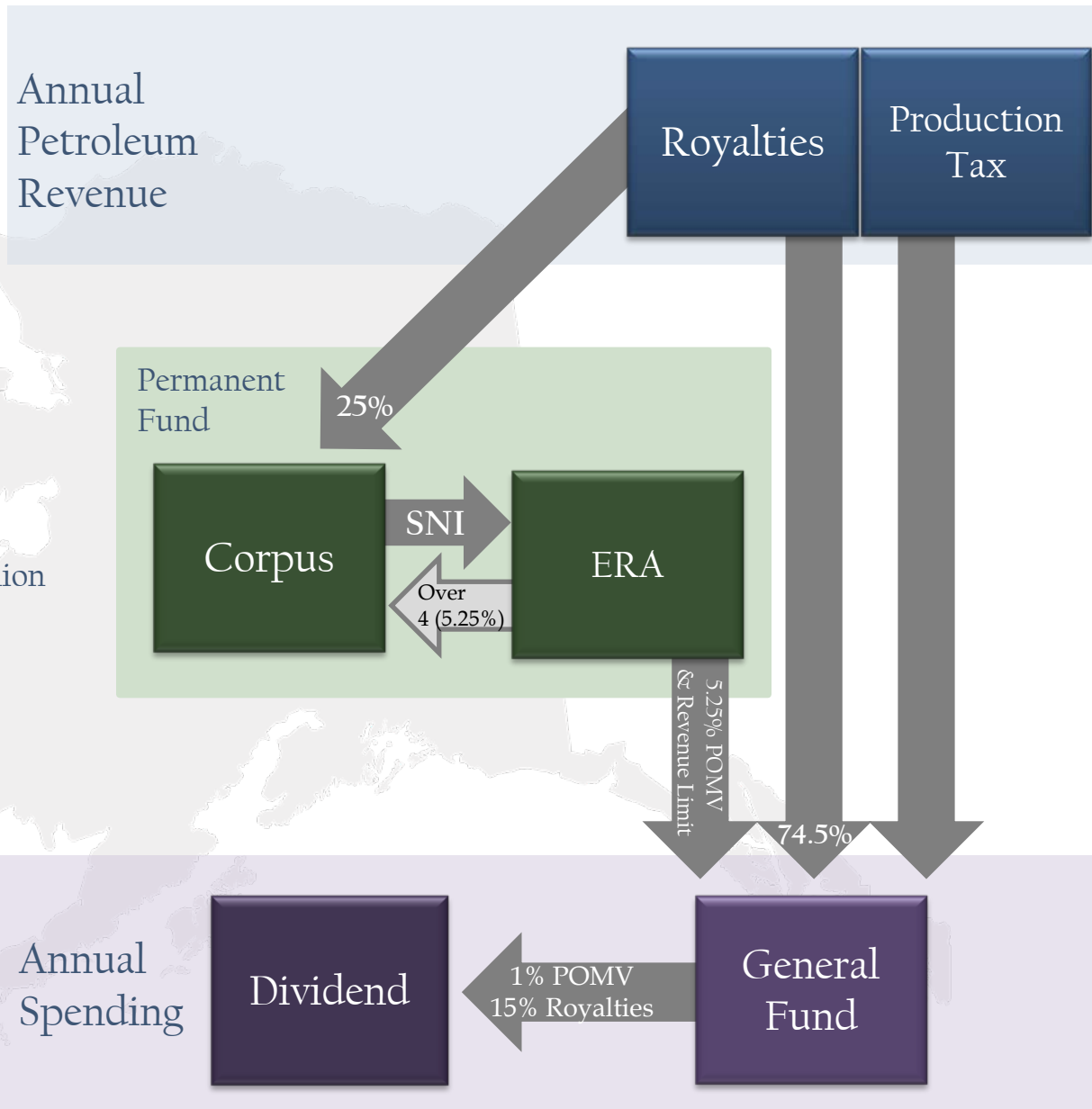
draw to the General Fund

## 2. Revenue Limit

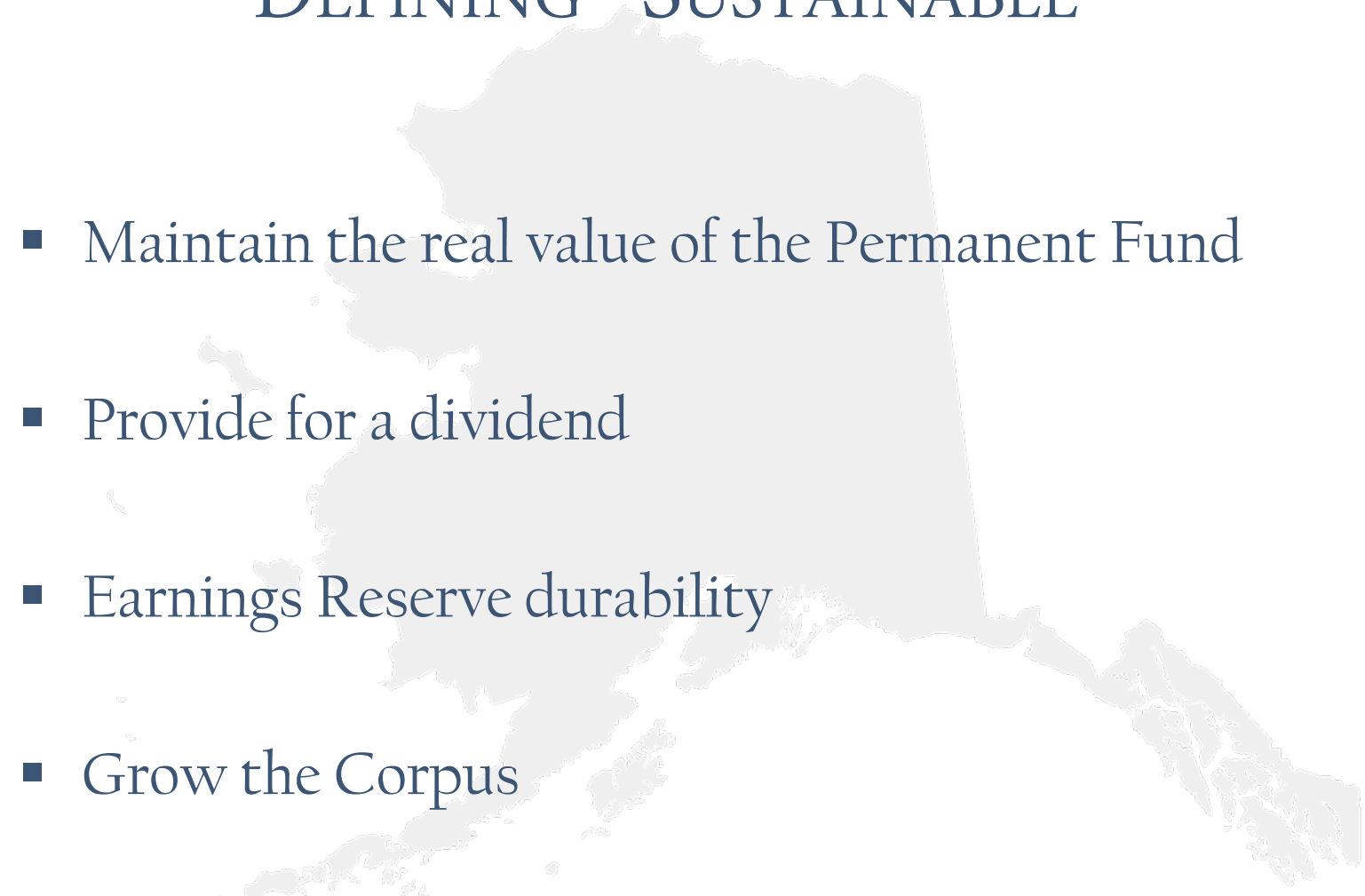
reduces draw when royalties & production taxes exceed \$1.2 billion

## 3. Sustainable Dividend

- 20% of UGF royalties
- 20% of ERA POMV draw



# DEFINING “SUSTAINABLE”

- 
- Maintain the real value of the Permanent Fund
  - Provide for a dividend
  - Earnings Reserve durability
  - Grow the Corpus



# DETERMINING THE ANNUAL DRAW

## Section 9

- 5.25% of the average value of the fund in the first 5 of the last 6 years
- Example: draw calculation for fiscal year 2017

FY	Fund Value* (millions\$)	First 5 of the Last 6 Years
2011	\$40,140	Average = \$45,868
2012	\$40,333	
2013	\$44,853	
2014	\$51,214	
2015	\$52,800	
2016	\$52,081	
2017	---	

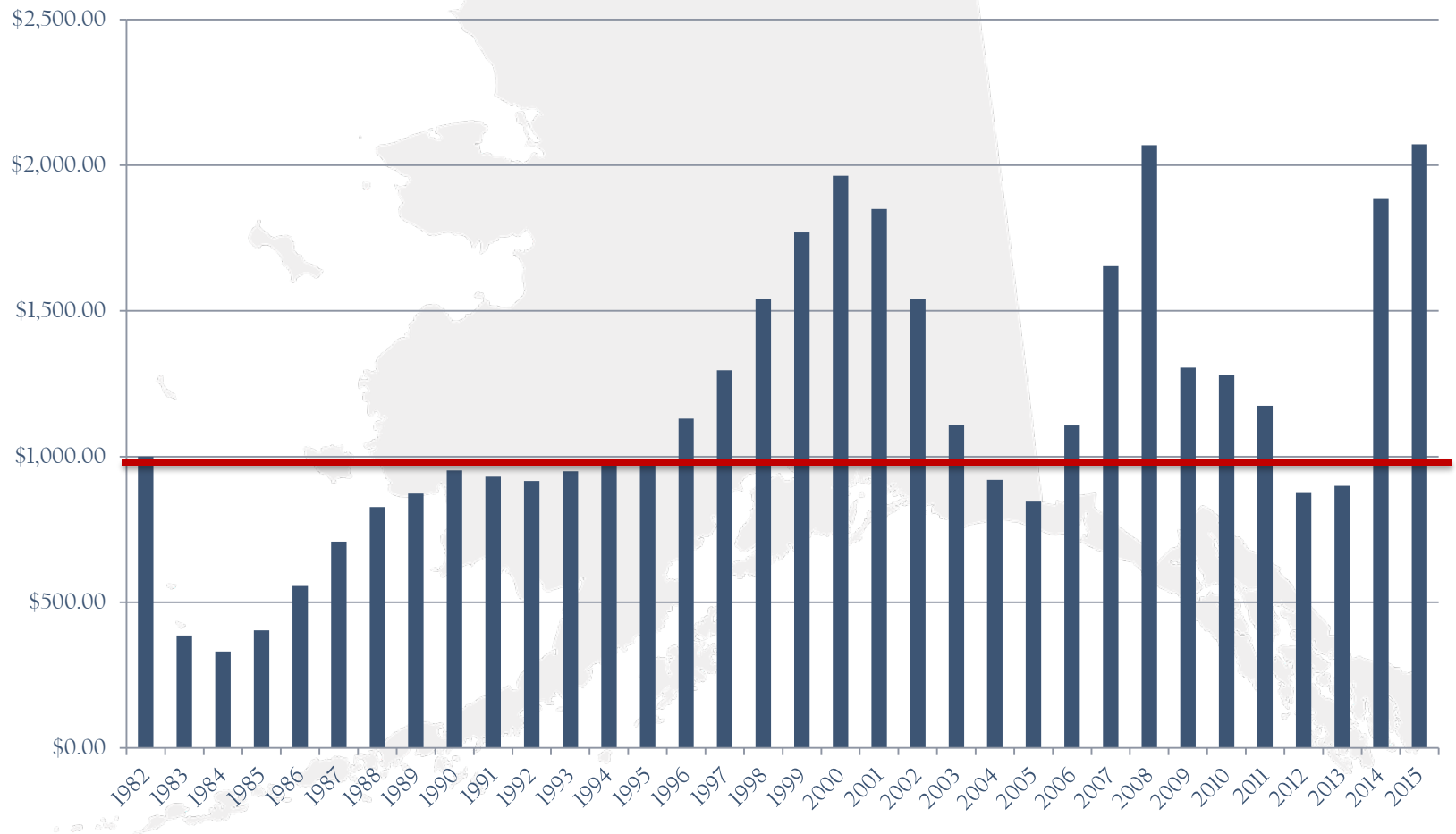
- Average fund value in the first 5 of the last 6 years  
= \$45,868
- 5.25% of \$45,868  
= \$2,408
- Effective POMV: \$2,408  
= 4.62% of 2016 value

- Aggressive, but sustainable



# HISTORIC DIVIDEND

50% of Statutory Net Income



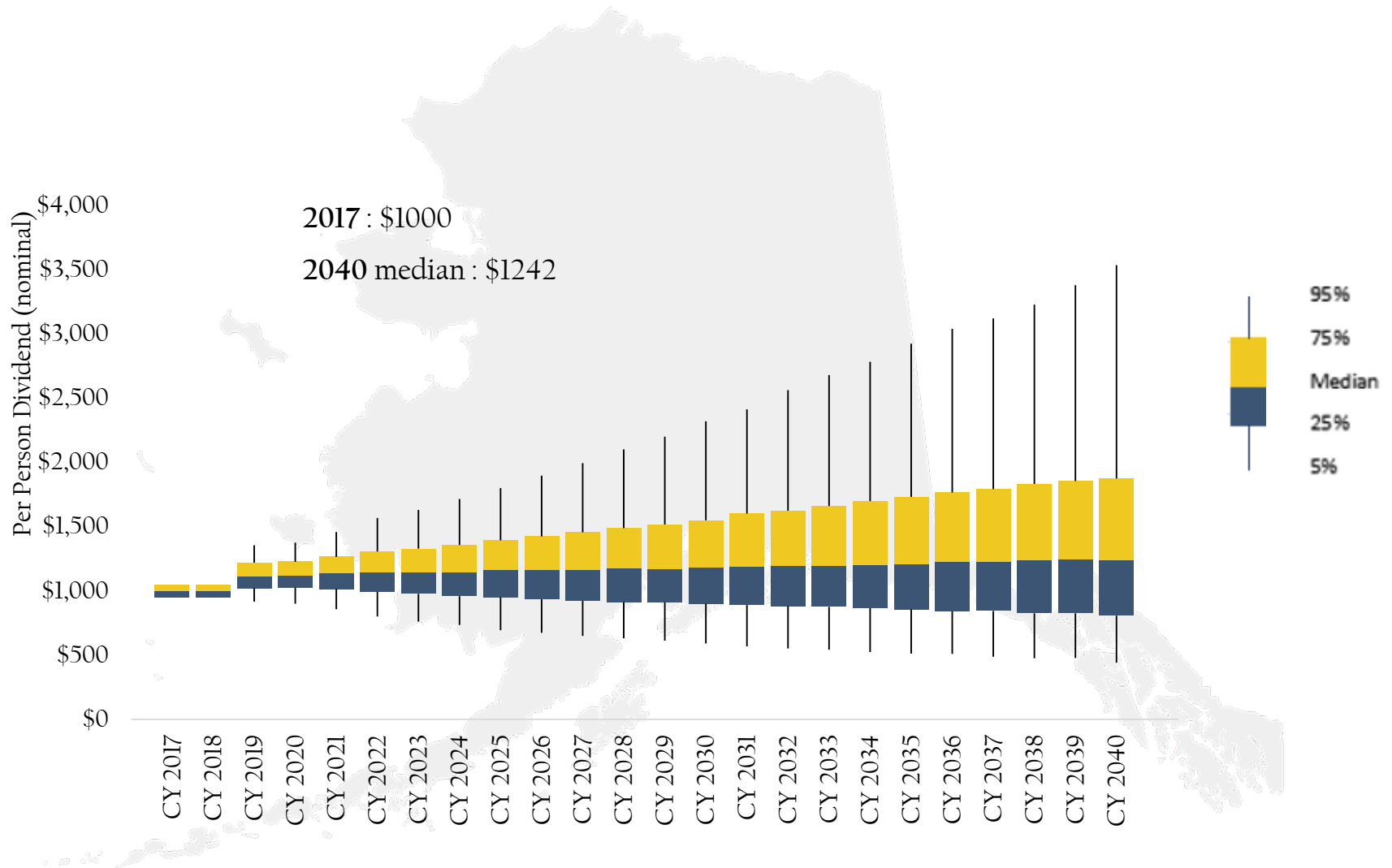
# NEW DIVIDEND FORMULA

## Section 11

- \$1,000 per person for first 3 years
- Annual mineral royalties
  - 20% of UGF royalties (15% of all royalties)
  - Ties Alaskans to economic health of the state
  - Creates upside in dividend
- Value of the permanent fund
  - 20% of the 5.25% POMV draw (about 1% POMV)
  - Protects the permanent fund by
    - Encouraging actions to grow the fund and
    - Ensuring public attention to future proposals to change the fund



# DIVIDEND FORECAST





# INFLATION PROOFING TRANSFERS

## Section 10

- AS 37.13.145(c) currently provides for annual inflation proofing transfers from the ERA to Corpus
- The ERA needs a sufficient balance to be able to meet draw each year
- CS provides that the ERA balance over 4 times the draw (after current year draw) is transferred to Corpus



# POMV DRAW LIMIT

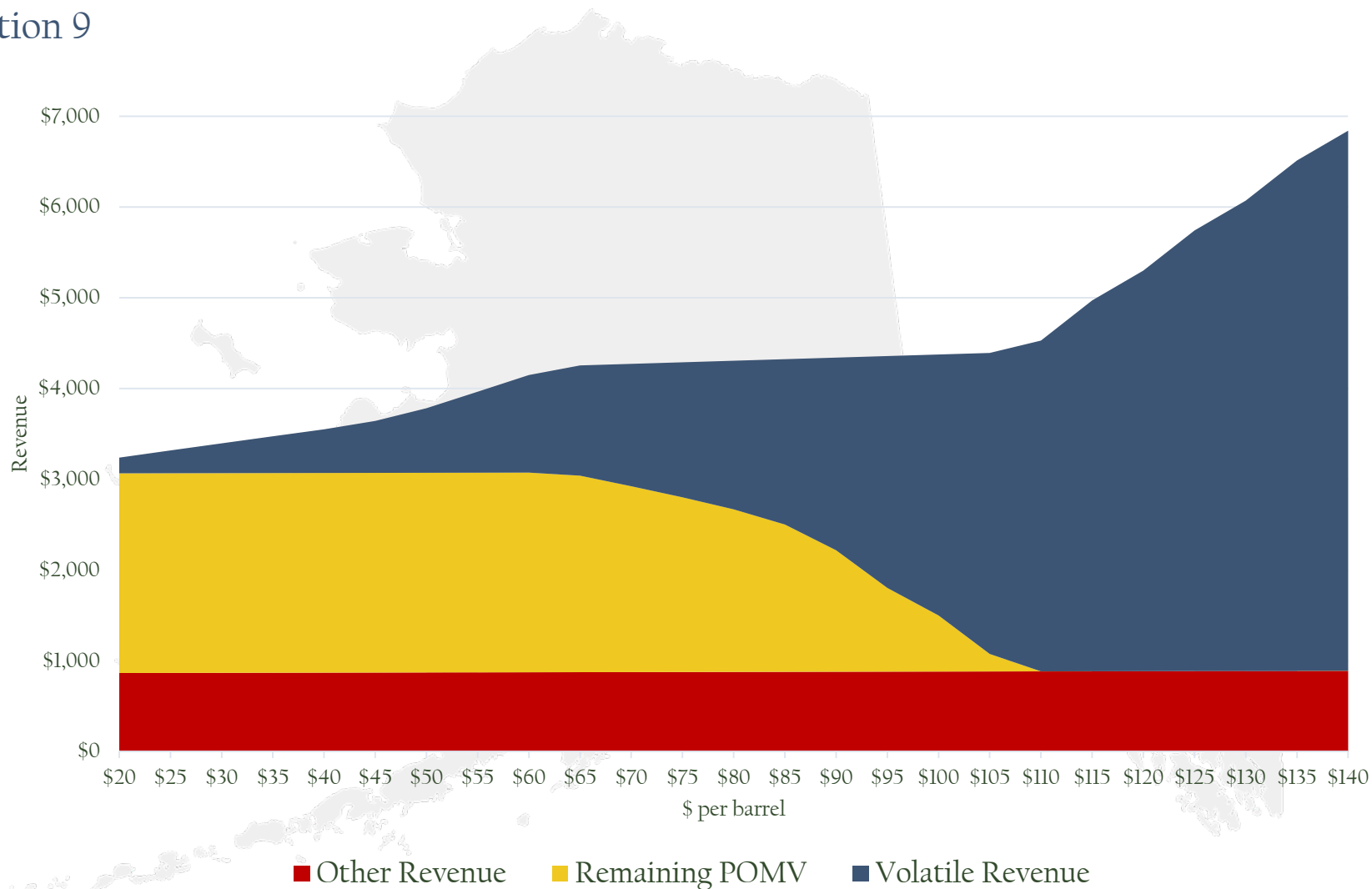
## Section 9

- The POMV draw is reduced by a dollar for every dollar that UGF production taxes and royalties exceed \$1.0 or \$1.2 billion
- Does not apply to funds for the dividend




# POMV DRAW LIMIT

## Section 9



# POMV DRAW LIMIT

## Section 9

- 
- Manages revenue volatility
  - Avoids spending Fund earnings when oil price is high
  - Allows for more growth in the Fund





The Fiscal Challenge

---

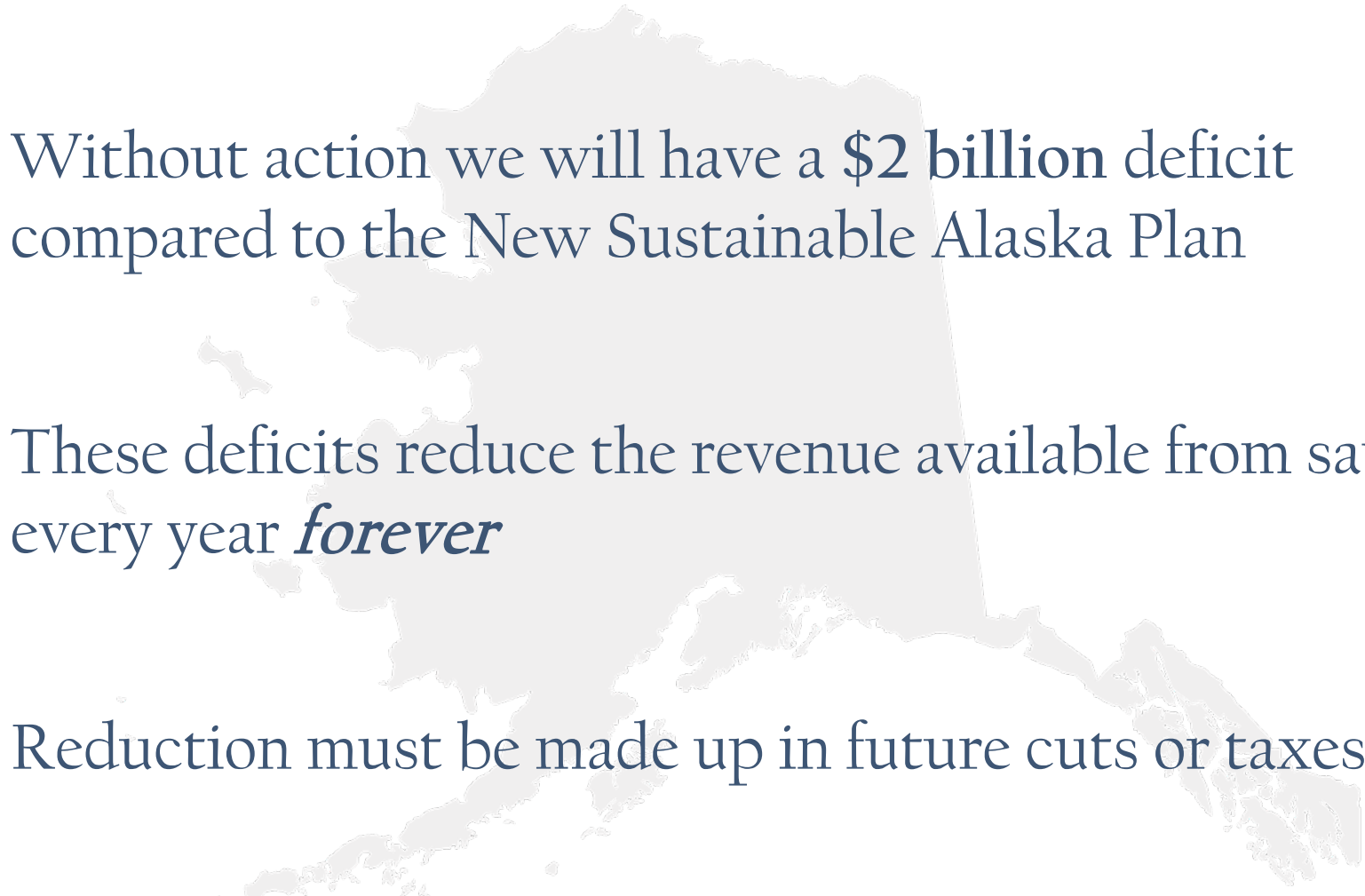
# THE COST OF DELAY

# DELAY WILL . . .

- Reduce our savings
- Risk further downgrade of Alaska's credit rating
- Damage the economy



# REDUCE SAVINGS

- 
- Without action we will have a **\$2 billion** deficit compared to the New Sustainable Alaska Plan
  - These deficits reduce the revenue available from savings every year *forever*
  - Reduction must be made up in future cuts or taxes



# COST OF A DOWNGRADE

“The state sold \$135 million of general obligation bonds yesterday [03/09/16], its first sale in almost a year. Tax-exempt securities maturing in August of 2035 sold at a top yield of 2.9 percent, about 0.35 percentage point higher than the benchmark securities due in 20 years. That gap is four times wider than what the state paid when it last sold debt in March of 2015.”

*Bloomberg News*



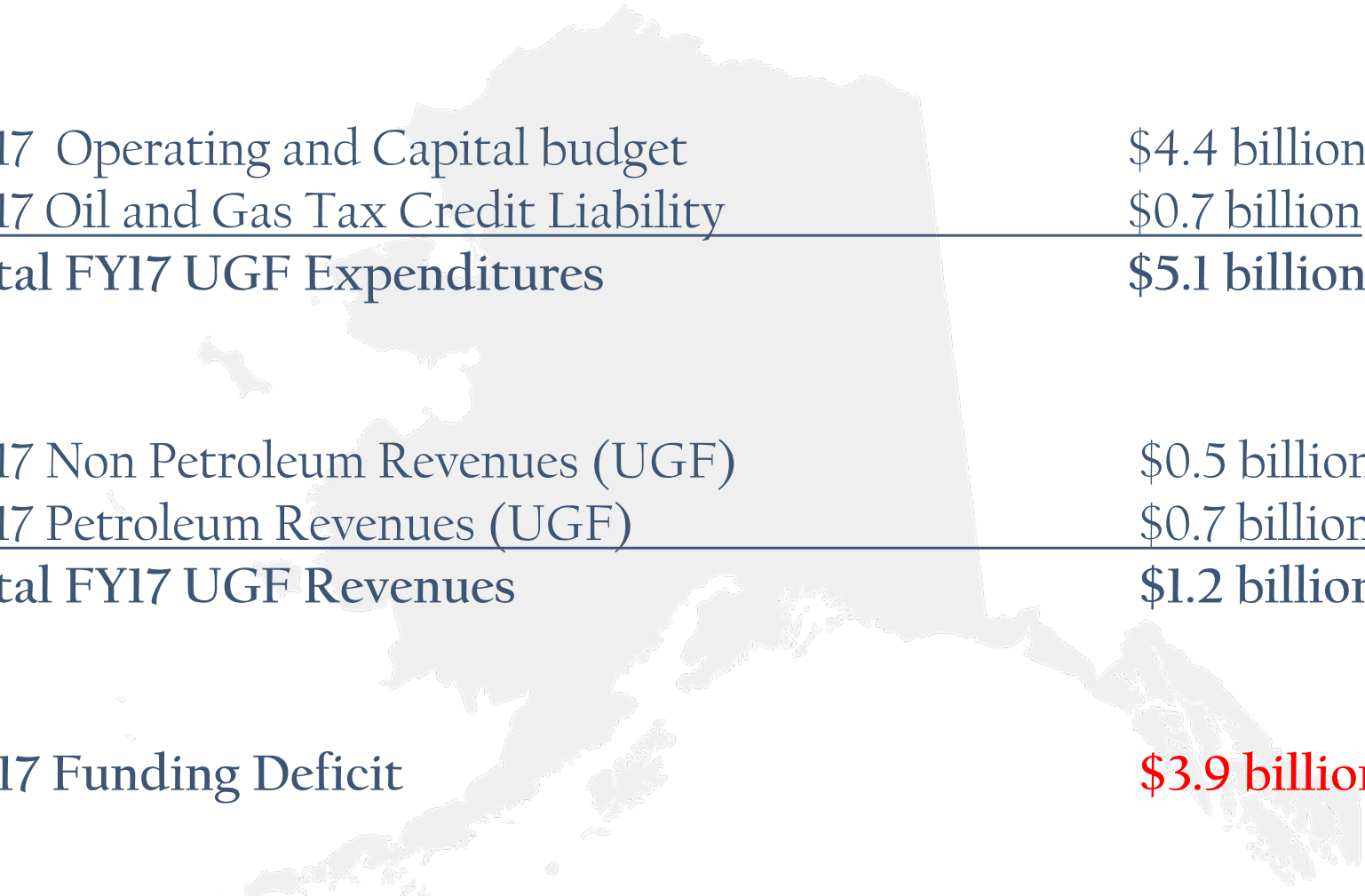


# DAMAGE TO ALASKA'S ECONOMY

- Lower sustainable draw from financial assets requires
  - More taxes
  - Less government spending (services and jobs)
- Degraded confidence and less private sector investment
- Direct impacts on Alaskans
  - Job Market
  - Home Values



# WHERE WE ARE NOW



FY17 Operating and Capital budget	\$4.4 billion
<u>FY17 Oil and Gas Tax Credit Liability</u>	<u>\$0.7 billion</u>
Total FY17 UGF Expenditures	\$5.1 billion
FY17 Non Petroleum Revenues (UGF)	\$0.5 billion
<u>FY17 Petroleum Revenues (UGF)</u>	<u>\$0.7 billion</u>
Total FY17 UGF Revenues	\$1.2 billion
FY17 Funding Deficit	<b>\$3.9 billion</b>



# WHERE WE ARE NOW

Projected CBR at year end FY16 \$6.5 billion

Deficit FY17 as of now \$3.9 billion

Projected CBR at year end FY17 **\$2.6 billion**



# THE NEW SUSTAINABLE ALASKA PLAN

