ALASKA PERMANENT FUND PROTECTION ACT

SECTIONAL ANALYSIS
SB 128

FOR THE SENATE STATE AFFAIRS COMMITTEE

Section 1 - Revenues to the Corpus

Section 1 amends AS 37.13.010(a) to increase the petroleum revenues directed to the corpus of the permanent fund, subject to a redirection mechanism that ensures the earnings reserve account is not degraded.

- Production Taxes: 100% of production taxes are directed to the corpus
    - Currently, these funds go to the general fund
    - Requires an appropriation

- Mineral Royalties: 49.5% of all mineral royalties are directed to the corpus
    - Constitutionally mandated 25% (no change)
    - An additional 24.5% (an increase from 5%)

- Redirection Mechanism: if needed to maintain the target balance (*see* Sections 2 and 6), some petroleum revenue may be redirected to the earnings reserve account

- Removes distinction between old and new leases

Section 2 - Target Balance of the Earnings Reserve Account

Section 2 adds subsection (d) to AS 37.13.010, which cross-references AS 37.13.145(l) (*see* Section 6), setting the target balance at equal to four times the prior year's sustainable draw.

Section 3 – Conforming Amendment

Section 3 is a conforming amendment to AS 37.13.140 that removes the calculation of "income available for distribution" because (1) the term relates to the current dividend formula, which would change (see Section 4), and (2) other revenues, including production taxes and royalties, may also be available in the earnings reserve account.

Section 4 – Transfers from the Earnings Reserve Account to the Dividend Fund

Section 4 amends AS 37.13.145(b) to change the calculation of the annual dividend.

- Changes the amount transferred from earnings reserve account to the dividend fund to 50% of the prior year royalties instead of approximately 50% of realized investment earnings

- Changes timing of the transfer from the end of the fiscal year to the beginning

Section 5 – Transfers from the Earnings Reserve Account to the Corpus

Section 5 amends AS 37.13.145(c) to change the timing and amount of transfers from the earnings reserve account to the corpus.

- Changes amount transferred to the corpus from the amount necessary to inflation proof the corpus to funds in earnings reserve account exceeding the "target balance"

- Changes timing of the transfer from every year to when excess funds are available

- Flexible inflation proofing and a presumption of savings
  - Over time, these transfers inflation proof the corpus
  - Transferred funds may exceed the amount needed for inflation proofing
  - The flexibility in timing improves the durability of the earnings reserve account and protects the corpus

Section 6 – Revenues to the Earnings Reserve Account and the Sustainable Draw to the General Fund

Section 6 adds subsections (e) to (l) to AS 37.13.145 to direct some petroleum revenues to the earnings reserve account and establish the endowment transfer to the general fund.

- **Redirection Mechanism:** Subsections (e) and (f) mirror the redirection provisions in Section 1. Specifically, if needed to maintain the target balance, up to 100% of production taxes and 24.5% of royalties that are otherwise deposited in the corpus may be redirected to the earnings reserve account.
  - Durability of the earnings reserve account: making these petroleum revenues available to the earnings reserve account helps ensure it is not depleted if there are several consecutive years of low petroleum revenue and low investment income

  - Protects the corpus: depleting the earnings reserve account would put the corpus at risk as the state searches for additional funds to pay for government
  - Savings: establishes a presumption of saving excess revenue in the corpus when possible

- **Dividend Royalties**: Subsection (g) provides that funds for the dividend (50% of royalties) gather in the earnings reserve account until they are transferred to the dividend fund under Section 4.
  - Retains the connection between the dividend and the permanent fund.
  - Helps with cash flow, particularly in first few years.
  - Establishes the cash flow pathways in the first year and minimizes departures from the permanent framework.

- **Sustainable Draw**: Subsections (h) and (i) provide for the annual endowment transfer from the earnings reserve account to the general fund.

  - $3.3 billion fixed-draw
    - Maximum amount
    - Adjusted for inflation beginning in FY 2020
    - Flexible transfer timing allows the Treasury and the Alaska Permanent Fund Corporation to work out a practical and efficient system based on cash flow needs and investment practices

  - Appropriation
    - Framework relies on legislature partnering with the executive
    - The Alaska legislature has a long history of following a rule-based policy for the earnings reserve account

- **Periodic Review**: Subsections (j) and (k) provide for a periodic sufficiency of assets review and adjustments to the draw amount.

  - The Commissioner of Revenue, in consultation with the Alaska Permanent Fund Corporation, conducts a review of the state's financial assets and forecasts and may recommend adjusting the draw amount

  - Scheduled: 2017, 2020, then every 4 years

  - Formulaic: the periodic review uses the same approach and variables used to calculate the initial draw

  - Protects the permanent fund: the periodic review ensures that, in light of experience, Alaska remains on a sustainable fiscal course

  - Collaborative: the review is provided to the legislature
  - Transparent: all supporting material – data, modeling, etc. – must be made available to the public in its native file format (except for confidential taxpayer information which may be provided in aggregated form)

- Subsection (l) defines “sustainable draw amount” and “target balance.”

Section 7 – Conforming Amendment

Section 7 is a conforming amendment to AS 37.13.300(c) isolating income of the mental health trust fund from net income available for transfer to the general fund.

Section 8 – Conforming Amendment

Section 8 is a conforming amendment to AS 43.55.080 directing production taxes to the permanent fund.

Section 9 – $1,000 Dividends in 2016

Section 9 amends uncodified law to specify that 2016 dividend checks will be $1,000 per person. This provision eases the transition to the new dividend formula.

Section 10 – July 1, 2016 effective date