



THE STATE
of **ALASKA**
GOVERNOR BILL WALKER

Department of Revenue

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February 21, 2017

The Honorable Neal Foster and the Honorable Paul Seaton
Alaska State Representatives
Co-chairs, House Finance Committee
State Capitol Rooms 410 and 505
Juneau, AK 99801

Dear Co-Chairs Foster and Seaton:

The purpose of this letter is to provide you with responses to the questions asked of the Department of Revenue (DOR) during our presentations to the House Finance Committee on February 2 and 3, 2017, regarding the Alaska Permanent Fund Protection Act (APFPA). Please see questions in italics and our responses immediately below the questions.

1. *What are the projected future dividends under each of the Permanent Fund proposals on slide 25? Include the spreadsheets that back up the graphs.*

Please see the attached zipped folder "Question 1 – Slide 25 proposals." DOR modeled the following proposals:

- Original APFPA, Senate Bill 128 (2016), with a fixed draw
- House Bill 224 (2016)
- Senate Bill 114 / House Bill 303 (2016)
- Senate Bill 21 (2017)
- House Bill 115 (2017)
- 2017 proposal for a 50-50 split of statutory net income between government and dividends
- The status quo forecast for comparison

For each proposal, DOR modeled a scenario with a full fiscal plan—i.e., the budget gap is filled through new revenues or budget cuts—as well as a scenario with no full fiscal plan, where the continued budget deficits create unplanned draws on the Permanent Fund. Each file in the zipped folder contains graphs and spreadsheets for the following variables:

- Earnings reserve failure rate
- Dividend per person
- Total unrestricted general fund revenue
- Permanent Fund size

2. *Provide a spreadsheet that shows how the POMV calculations work in the model for the current version of the APFPA.*

Response previously provided in the letter dated February 10, 2017.

3. *Which oil and gas tax credits does the APFPA model account for?*

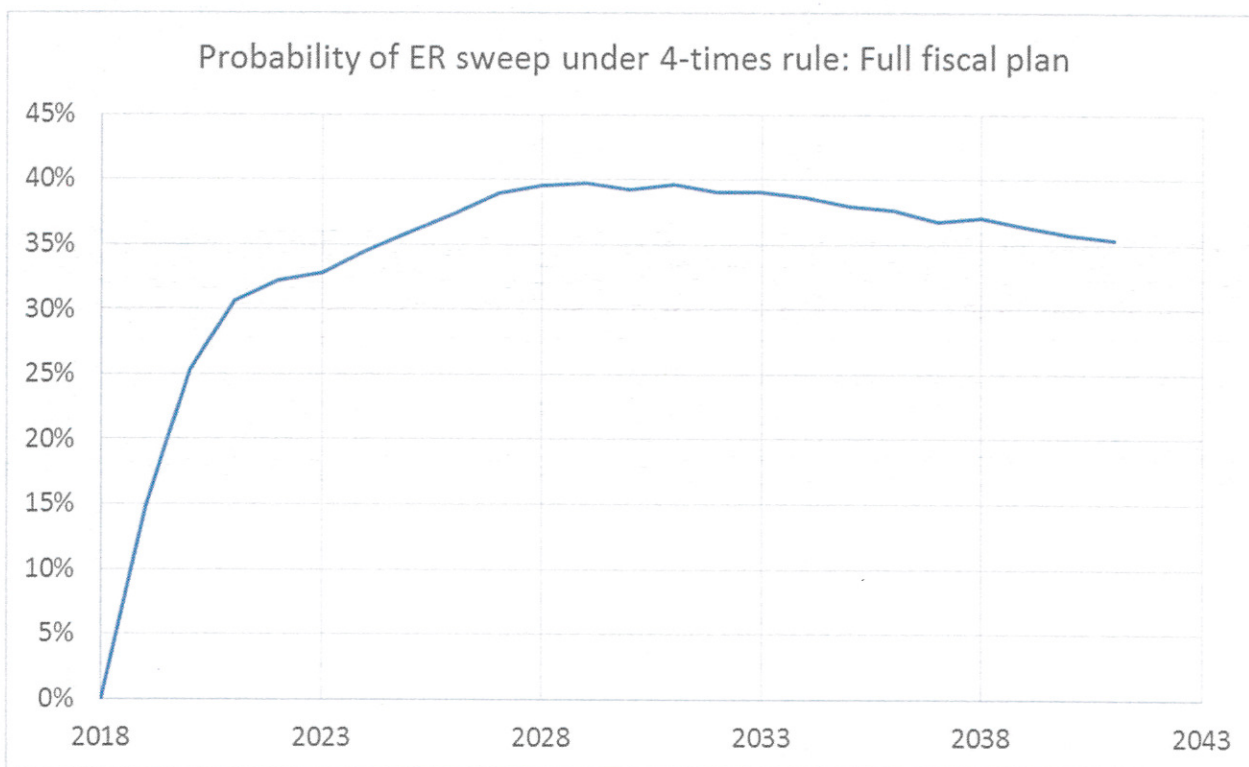
Response previously provided in the letter dated February 10, 2017.

4. *How long will it take to reach a scenario an inflation-proofing sweep from the earnings reserve into the principal occurs? Will this be an ongoing situation?*

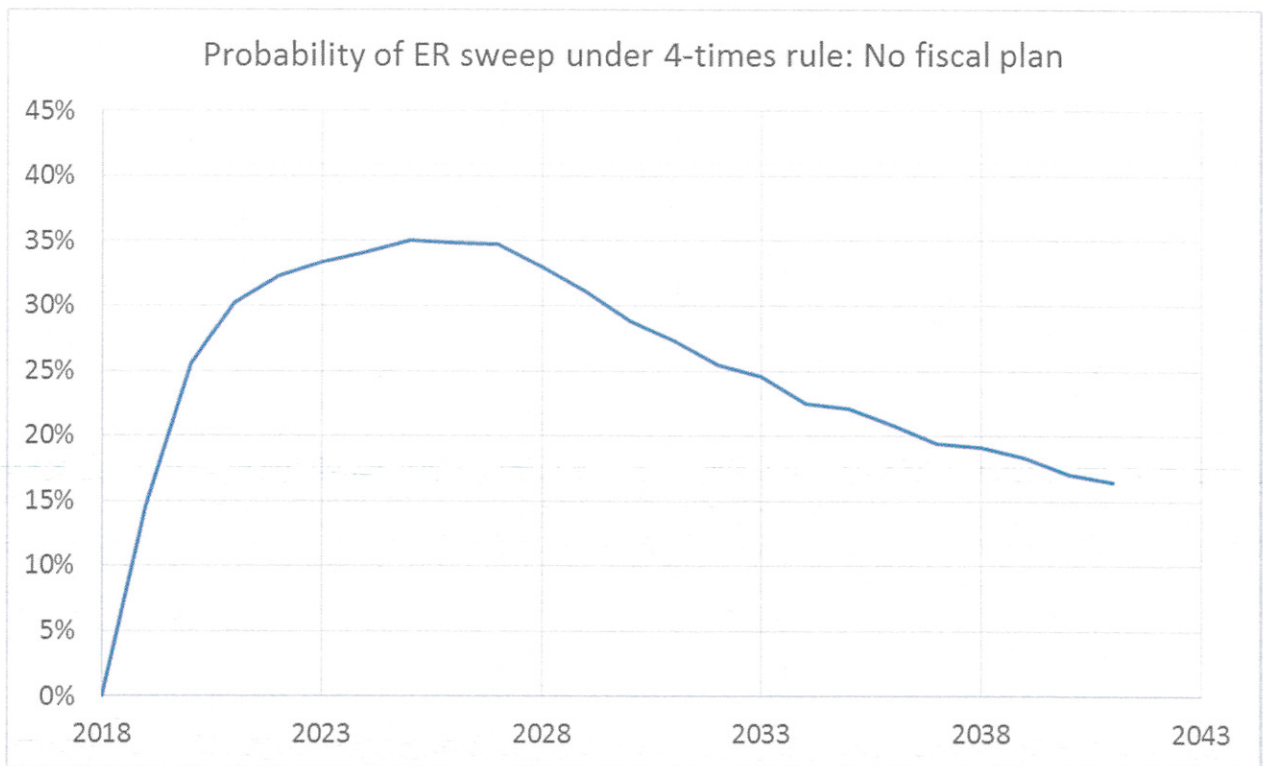
Updated response below:

The APFPA stipulates that there will be a sweep if the earnings reserve balance at the beginning of a fiscal year, minus the draw calculated for that fiscal year (which may be reduced according to the \$1.2 billion petroleum revenue threshold), exceeds four times the originally calculated draw (before reductions).

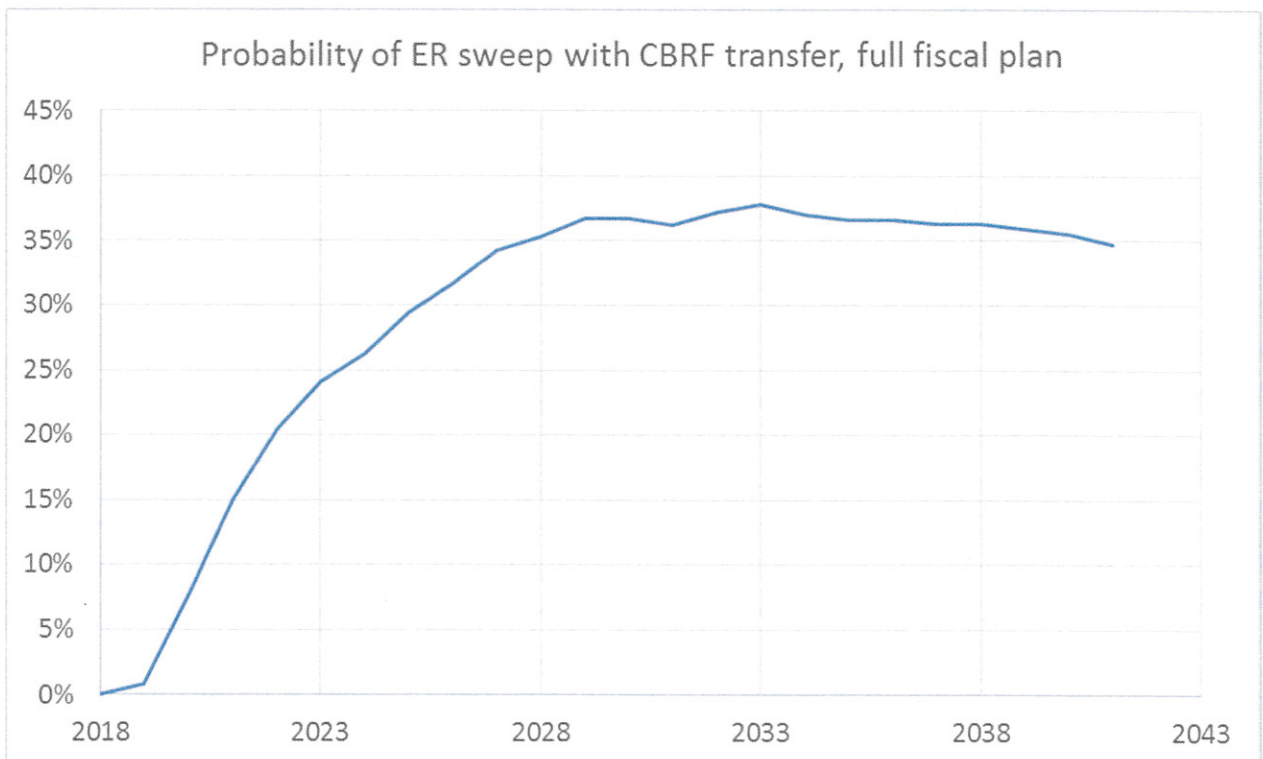
In the deterministic case according to the APFPA model, assuming a full fiscal plan, the sweep will occur every fiscal year starting in FY 2028. Of course, there is a wide variety of possible outcomes. The following graph shows the probability of an earnings reserve sweep in each fiscal year assuming a full fiscal plan.



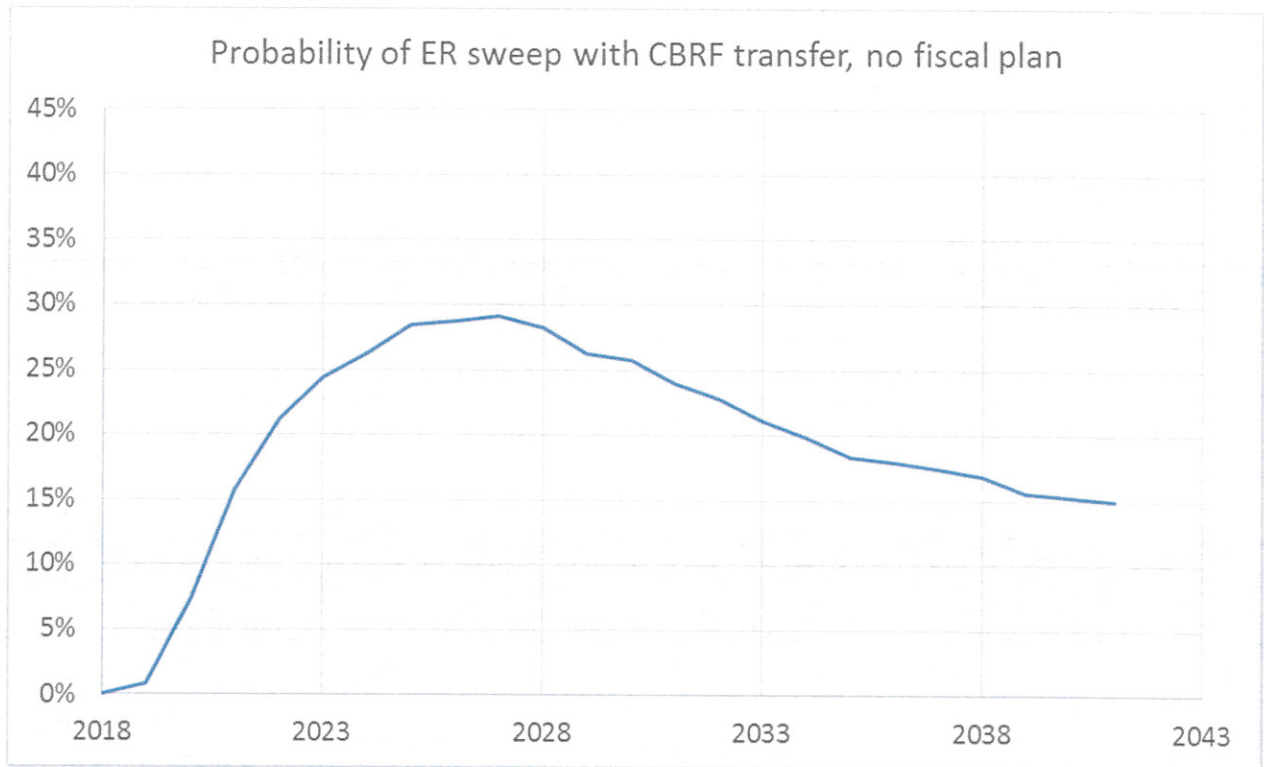
In the deterministic case according to the APFPA model, assuming no full fiscal plan and the extended OMB 10-year plan (discussed in question 7), the sweep will occur only in FY 2028 through FY 2029. Again there is a wide range of possible outcomes, but the chance of an earnings reserve sweep in later years is considerably reduced with no full fiscal plan, since earnings reserve funds will be needed to cover continued budget deficits. The following graph shows the probability of an earnings reserve sweep in each fiscal year assuming no full fiscal plan.



DOR also modeled these two cases with a \$2.4 billion transfer from the Permanent Fund to the Constitutional Budget Reserve Fund (CBRF) in 2017. With a full fiscal plan and the CBRF transfer, the deterministic case of the model shows the earnings reserve exceeding four times the annual draw every year starting in FY 2034. The following graph shows the probability of an earnings reserve sweep in each fiscal year assuming a full fiscal plan and a CBRF transfer.



With no full fiscal plan and the \$2.4 billion CBRF transfer, the deterministic case of the model shows no earnings reserve sweep within the 24-year modeling period. The following graph shows the probability of an earnings reserve sweep in each fiscal year assuming no full fiscal plan and a CBRF transfer.



This analysis takes into account the fact that unrealized gains are allocated between the principal and the earnings reserve according to the ratio between the realized portions of the two accounts. When an earnings reserve sweep occurs, that alters the unrealized gains allocation ratio. Therefore, DOR modeled the sweep such that the total amount swept from the earnings reserve to the principal—realized and unrealized portions—adds up to the correct amount of the sweep.

5. *The APFPA includes a limit of \$1.2 billion on production tax and royalties, above which the POMV draw would be reduced dollar-for-dollar. Provide modeling of alternate values of this limit, e.g., \$1.5 or \$1.7 billion, including the spreadsheets that back up the graphs.*

DOR modeled four different draw limit thresholds: \$1.0, \$1.2, \$1.5, and \$1.7 billion. Please see the attached zipped folder “Question 5 – different draw limit thresholds” which contains graphs and spreadsheets for the following variables:

- Earnings reserve failure rate
- Dividend per person
- Total unrestricted general fund revenue
- Permanent Fund size

6. *Provide a matrix of projected per-person dividend amounts under different oil price and production scenarios.*

Response previously provided in the letter dated February 10, 2017.

7. *What are the exact budget forecasts used in the "extended OMB 10-year plan" budget assumptions in the APFPA model?*

Response previously provided in the letter dated February 10, 2017.

8. *Why is the Constitutional Budget Reserve (CBR) balance of \$4.4 billion in the APFPA model different than the number in the OMB 10-year plan?*

Response previously provided in the letter dated February 10, 2017.

9. *Provide dollar amounts to accompany the graphs on slide 29 (pure POMV) and slide 31 (POMV with draw limit) that show projected amount of revenue in relation to oil price.*

Updated response below:

DOR has updated the relevant graphs, included the backup spreadsheets, and they are attached in the file "Revenue vs oil price graph for House Finance with/without reduction of POMV."

I hope you find this information to be useful. Please do not hesitate to contact me if you have further questions.

Sincerely,



Randall Hoffbeck
Commissioner

Attachments:

- Question 1 – slide 25 scenarios
- Question 5 – different draw limit thresholds
- Revenue vs oil price graph for House Finance with reduction of POMV
- Revenue vs oil price graph for House Finance without reduction of POMV