Bicameral Permanent Fund Working Group Report

January 20, 2020

Bicameral Permanent Fund Working Group Report

January 20, 2020

Table of Contents

1. Executive Summary

The goal of the 31st Alaska State Legislature's Bicameral Permanent Fund Working Group was to review key historical and legal facts about the Alaska Permanent Fund, its earnings, and permanent fund dividends; review fiscal models on the permanent fund, dividend, and the state budget; and, provide policy recommendations to the legislature on the future use of the earnings of the Alaska Permanent Fund.

Members first met on June 12, 2019. At their second meeting the next day, they formed three teams to study the pros and cons of paying out three different sizes of permanent fund dividends: one based on the current statutory formula; another that reflected the $1,600 checks Alaskans received in 2018; and, one that resulted from surplus funds left over after balancing the state budget with traditional revenues and an amount of permanent fund earnings limited by the Senate Bill 26 percent of market value law approved by legislators in 2018.

As the three teams worked on their assignments, members were addressed by Governor Mike Dunleavy and heard a history on June 19 of permanent fund and dividend laws. On June 28, the executive director of the Alaska Permanent Fund Corporation detailed the mission and history of the fund as well as the roles and responsibilities of the trustees who manage it. That afternoon, the working group reviewed fiscal models presented by the director of the Alaska Division of Legislative Finance and commissioner of the Alaska Department of Revenue.

On July 8, about two weeks after being tasked with researching and analyzing fiscal impacts of three different sizes of dividends, teams presented their work to the full working group.

The sixth and final meeting of 2019 took place on October 7. A legislative fiscal analyst presented permanent fund, dividend, and budget models based on requests from working group members. Also unveiled at the meeting were the working group's website, www.pfalaska.org, and a permanent fund dividend interactive model based on the Fiscal Year 2020 budget to allow members of the public to see how figures they choose for oil prices and dividends affect the state budget and the size of the deficit. All these models and other documents presented at working group meetings may be found at the website above.

The working group recommends that legislators and members of the public review this body of work – especially the reports by the three teams and the fiscal scenarios provided by budget officials. While agreement on the size of a dividend still may be difficult to attain, members agree that the permanent fund must be protected from inflation so that future generations of Alaskans may benefit from it. A majority of members agree that use of permanent fund earnings for state services and dividends must stay within draw limits established by a structure like the percent of market value law enacted in 2018.

2. Creation of the Working Group

The 31st Alaska State Legislature created the Bicameral Permanent Fund Working Group on June 10, 2019, near the end of the year's first of two special sessions, with the passage of House Concurrent Resolution 101.

The measure called on eight legislators – four from the Senate, four from the House – to review the use of Alaska Permanent Fund earnings and make recommendations on how to use these funds in the future.

The eight-member group is made up of lawmakers from across the state, from both major parties, and includes members from House and Senate majorities and minorities. They are:

- Senator Click Bishop, R-Fairbanks, Co-Chair
- Representative Jennifer Johnston, R-Anchorage, Co-Chair
- Senator Shelley Hughes, R-Palmer
- Senator Donny Olson, D-Golovin
- Senator Bert Stedman, R-Sitka
- Representative Jonathan Kreiss-Tomkins, D-Sitka
- Representative Kelly Merrick, R-Eagle River
- Representative Adam Wool, D-Fairbanks

Creation of the working group came while the legislature was still working on the Fiscal Year 2020 budget.

The June 10 passage of HCR 101, to create the working group, occurred on the same day that the first Fiscal Year 2020 operating budget measure, House Bill 39, got final approval in the Senate, after passing the House the day before. That legislation did not provide funding for Permanent Fund Dividends. The first capital budget measure, Senate Bill 19, also did not include PFD funding when it won final passage a few days later on June 13.

Funding for dividends as well as final legislative action in 2019 on the operating budget, capital budget, and authorization to use the constitutional budget reserve came the following month, during a second special session, on July 29, with passage of HB 2001 and SB 2002.

3. A Brief History of the Alaska Permanent Fund and Dividend

Alaska Statehood and Mineral Rights

When Alaska achieved statehood in 1959, it was with the understanding that we would be able to operate much of our state government using natural resource revenues. There was considerable skepticism in Washington, D.C. that Alaska, with a small population and economic base, could support itself without ongoing federal funding provided to the Territory. This, in large part, is why Alaska was granted an historically unique land selection of more than 100 million federal acres at statehood. Notably, mineral rights to this land were to be retained by the state. This provision was not controversial at the time and was based in part on federal minerals leasing reform from 1920. However, combined with the relatively small amount of land in private hands, it provides context to the belief held by some Alaskans that revenue from resources on state land is an individual right. This is seen as compensating residents for the loss of comparable land rights held by those in other states such as Texas ranchers. The tension between the belief that funds derived from mineral rights are a source of revenue for government and the view that state land rights are a commonly held asset of Alaskans underpins much of the current debate over the dividend and other potential uses of fund earnings.

Prudhoe Bay and the Bonus Boom

Because the state directly owns more than 100 million acres of land, it means the state itself is the leasing entity for minerals development, and the state itself collects the landowners' royalty from that development. The 1968 Prudhoe Bay discovery on a portion of the central North Slope that had been "selected" by the state at statehood set the stage for the revenue boom that has defined the last 50 years of Alaska's history.

Soon after this discovery, a major state lease sale made the nearby acreage available. Famously, the state received more than $900 million in "bonus bids" in a single day, September 10, 1969. In contrast, the unrestricted revenue received during the rest of Fiscal Year 1970 was less than $165 million, with the largest items being $36 million in Cook Inlet royalties and production taxes, $38 million in personal and corporate income taxes, and $10 million in motor fuel taxes.

At the time, Alaska was substantially undeveloped with unmet needs throughout the state. The state budget roughly doubled in the early 1970s, and the $900 million was more or less depleted by about 1975.[1] A substantial portion of the budget increase was for municipal revenue sharing that reduced local tax burdens but did not produce much in the way of tangible new construction. That led many, as described by Governor Hammond, to feel that this initial windfall had been "blown."

[1] Because of delays in permitting the Trans Alaska Pipeline system, first production from the North Slope was not until mid-1977. To fund ongoing state operations during the 1975-1977 period, the state passed a temporary "reserves tax" on undeveloped oil resources in the ground, which was then refunded to producers as a credit against oil and gas production taxes once production began.

Creating the Alaska Permanent Fund

Memories of spending most of the $900 million oil windfall were still fresh during the 1976 legislative debate on creation of the Alaska Permanent Fund, and the desire was strong to save for the future. The final language, with 25 percent of royalties and related landowner interests going into the fund corpus, was a compromise. Governor Hammond initially proposed depositing 50 percent of both royalties and production taxes.

Although the initial purpose of the fund was not specified, it was clear that the broad intent was to turn finite and short-term resource wealth into infinite financial wealth. As Governor Hammond described it, he wanted to turn oil wells pumping for a limited period into money wells pumping for eternity. The growing pot of money would be equivalent to a retirement plan for the state that continued to generate revenue for the general fund long after the oil fields were exhausted.

The language proposed by the legislature and approved by voters in 1976 was a new provision added to the Alaska Constitution that became Article IX, Section 15:

> *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 general fund unless otherwise provided by law.*

Notably, neither the constitution nor the explanatory summary provided to voters contained any mention of a dividend, only that the earnings would be used by the state. One initial hope for the dividend program, when it was introduced several years later, was to make Alaskans feel vested in the management of the fund and thereby protect it from unnecessary and premature withdrawal.

The fund began receiving deposits in 1977 based on the constitutional formula. Several additional deposits were made by the legislature in the early years as funds were available. Interestingly, one of the first extra deposits to the fund, in 1981, was $900 million to symbolically replace the 1969 bonus bid payment.

The “otherwise provided by law” phrase in the 1976 constitutional amendment required subsequent legislative action to clarify how fund earnings could be used. Initially, they were annually deposited into the general fund as described in the constitution. Later, legislation established the dividend program – roughly half of earnings went to dividends, the corpus received an annual transfer for inflation-proofing, and the earnings reserve account was created to hold the remaining amount. Before Fiscal Year 2019, the permanent fund was not used for general government outside of limited expenses specifically related to collecting, distributing, and litigating fund earnings.

Struggle to Create the Alaska Permanent Fund Dividend

As part of his initial proposal, Governor Hammond proposed a formula in which half the earnings would be distributed to Alaskans, not as a cash dividend but as shares of a commonly owned investment fund, "Alaska, Inc.," that would pay dividends. Had Governor Hammond's plan passed, it would have provided for far smaller initial payments to individuals. For example, if the initial "share" earned by a person was $500, that would have been received as a share in the "Alaska, Inc." fund. The individual's cash dividend would be based on the earnings of that $500 – or about $25 per year, assuming typical real returns. This would have grown over time as the individual shares accumulated from year to year.

Instead, the legislature in 1980 authorized the initial dividend program and created the Alaska Permanent Fund Corporation to manage the fund's assets. This was also based on "shares," with each resident earning a share for each year they had been in Alaska since statehood. This was the plan that was successfully challenged in *Zobel v. Williams,* based on the idea that longer-term residents would benefit unequally from the oil wealth. In response to that court case, the legislature in 1982 passed a new formula in which Alaskans received an equal share, based on the previous five years of fund earnings. This statutory formula has remained largely unchanged since then. [2]

The initial 1982 dividend distribution was exactly $1,000, representing roughly what would have been the three years of dividends that would have been received in 1980-1982 but had been delayed by the *Zobel* lawsuit. The 1983 dividend, based on the statutory formula, was $386, and the amount did not exceed $1,000 again until 1996.

Statutory Dividend Formula

The current dividend formula is intended to distribute half of the permanent fund's earnings via the annual dividend. More precisely, the dividend calculation is based on statutory net income, which equals actual (accounting) net income less unrealized gains and less earnings on the "*Amerada Hess*" portion of the permanent fund that cannot be spent on dividends.

Statutory net income is reported by the Alaska Permanent Fund Corporation. The statutory dividend formula for Fiscal Year 2020 is based on 21 percent of the total fund earnings for fiscal years 2015 through 2019 which was $17.9 billion. This number multiplied by 21 percent is $3.77 billion, and half of this amount is $1.885 billion. This figure is the basis for the so-called "full statutory dividend." Based on the final number of eligible recipients for 2019, this would result in a dividend of about $2,911.

Proposals to Use Permanent Fund Earnings

There have been various proposals to use permanent fund earnings for state services. During the 1985-1988 crash in oil prices, there was little ability to do so. The fund was worth less than

[2] More precisely, the "21% of the past five year's net income" structure did not take effect until 1986 with the passage of SB346 (ch 28, SLA 86). The original 1982 PFD formula called for the "average of the past five year's net income", which is actually about 5% less (20/21) than the current formula.

$10 billion in those years, and it would have been impossible to use a substantial portion of it to pay for the state budget without depleting the fund's value.

Continuing deficits driven by low oil prices throughout the 1990s and early 2000s were routinely filled using the Constitutional Budget Reserve Fund, with support from a three-quarters' vote of both the House and the Senate. As spending depleted this fund and money was projected to run out, various legislators floated proposals to use earnings to support state operations. Famously, the first advisory vote on one of them, in 1999, received only 17 percent of votes cast.

The first Percent of Market Value (POMV) plan was a constitutional amendment, House Joint Resolution 15, proposed by the Legislative Budget and Audit Committee in 2001 by request of the Alaska Permanent Fund Corporation. It would have allowed no more than 5 percent of the five-year-average fund value to be appropriated and was silent on the issue of the dividend.[3] In support of their proposal, the corporation published a 2002 trustee paper detailing the concept. Governor Frank Murkowski in 2004 called the Conference of Alaskans, at which he hoped to build support for a similar POMV structure. The conference was inconclusive, and no statutory or constitutional changes were passed.

Eventually, oil prices recovered and then boomed. State petroleum revenue hit record levels in the 2008-2013 period, eliminating budget fears and enabling the legislature to repay the $5.5 billion that had been cumulatively borrowed from the constitutional budget reserve. Armed with those and additional savings, the debate was forestalled for another decade or more.

Oil Price Crash and Reduced Dividends, 2016-2018

Starting in late 2014, oil prices rapidly declined from about $100 per barrel to a low of $26 in early 2016. Unrestricted oil revenue declined by 90 percent between Fiscal Years 2012 and 2017. The state went from an era of multibillion-dollar budget surpluses to even larger deficits that persisted even after significant budget reductions. These deficits were initially filled by drawing down reserves from accounts including the Statutory Budget Reserve, the previously forward-funded Public Education Fund, and the Constitutional Budget Reserve Fund which was reduced to about $2.1 billion by the end of Fiscal Year 2019.

Governor Walker proposed several revisions to permanent fund formulas that would have allowed for use of earnings, as well as a variety of new revenue measures. After the 2016 session, when none of these had passed and the state was facing continuing large deficits, he vetoed roughly half of the PFD appropriation in the FY 2017 budget. This was historic, the first time since 1982 that the dividend formula had not been followed. His stated intent at the time was to draw attention to the seriousness of Alaska's fiscal crisis. Subsequently, the legislature followed this precedent and appropriated less than the statutory formula during the 2017 and 2018 sessions.

[3] Structurally, the 2001 language was nearly identical to HJR 18, proposed by the House State Affairs committee in 2019.

The initial 2016 veto was challenged in court, based upon the statutory language that said the corporation "shall" transfer the 50 percent of earnings calculation to the dividend fund (AS 37.13.145(b)). The Alaska Supreme Court, in *Wielechowski v. State*, concluded that this statutory language did not supersede the legislature's requirement to pass an annual budget and legislators' freedom to set the amount of various appropriations. The basis of this decision was the Alaska Constitution, which has a strong prohibition against dedicated funds. The constitutional requirement to deposit at least 25 percent of mineral royalties into the permanent fund is a specific exception to this. Essentially, the supreme court said that any exception to the dedicated funds clause must be interpreted as narrowly as possible.

Passage of Senate Bill 26 in 2018

After three years of debate, the legislature passed Senate Bill 26 in 2018 that enacted a POMV formula based on the average fund value over the first five of the six preceding fiscal years. The theory behind this sustainable draw is that the expected average annual fund earnings, less expected inflation, could be drawn from the permanent fund indefinitely without reducing its real (inflation-adjusted) value. In recent years, fund managers have assumed annual average earnings would be roughly 6.5 percent to 7 percent and inflation would be about 2 percent.

Because of the expectation that the fund will increase in value in most years, the 5.25 percent draw figure (5 percent beginning in FY 2022) will typically result in a smaller percentage of the current year's actual value being drawn – something closer to 4.5 percent. Additionally, using the "previous five of six" method allows the legislature to predict, with relative precision, what the expected draw amount will be each legislative session during their annual budgeting process. The annual draw for FY 2020 is $2.933 billion, and the draw for FY 2021 will be very close to $3.090 billion.

SB 26 conformed with the idea that any plan to use fund earnings must be rules-based and sustainable. However, the version of SB 26 that ultimately passed into law was missing several additional components (rules) that had been in earlier versions of the bill. These items had passed both the House and Senate but were removed from the final version by the conference committee. The most important of these were:

1) A defined split of the annual draw between the part funding government services and the portion funding permanent fund dividends. The House proposed 33 percent of the draw amount go to dividends, the Senate proposed 25 percent, and the actual FY 2019 budget passed with a $1,600 dividend that represented about 37 percent of the draw. These changes would have replaced the current dividend formula.
2) Provisions by which the annual draw would be reduced if that year's oil and gas revenues surpassed a target amount. This would have served two purposes. First, it would have prevented inflating the state budget to unsustainable spending levels during a temporary period of high oil prices. Second, in years when oil prices are high, the annual draw would be less than the full statutory percentage. This "averaging" would allow for a slightly higher sustainable draw percentage during other years.

3) A mechanism by which surplus funds would be swept into the permanent fund principal when more than four years' worth of expected annual draws are in the earnings reserve account.

Importantly, the undistributed portions of the 2016 and 2017 dividends were not spent on state services. Those funds, totaling about $1.5 billion, remain in the earnings reserve account and have continued to earn returns. This contrasts with the 2018 dividend that was paid in the context of the POMV draw that passed that year. The legislature divided the $2.7 billion appropriation, with $1.0 billion paying the $1,600 individual dividend and the remaining $1.7 billion going to the general fund. In 2019, the legislature divided up the $2.9 billion draw, with nearly $1.1 billion for $1,606 individual dividends and more than $1.8 billion for state services.

Earnings vs. Market Value

There is a potential conflict between two statutes. The historic dividend is based on the "income available for distribution" in AS 37.13.140(a), equaling 21 percent of the five-year earnings lookback. This contrasts with the statutory "amount available for appropriation" added by SB 26 in AS 37.13.140(b), which is the 5.25 percent of the five-year market value lookback (reduced to 5 percent for FY 2022). The historic dividend formula is 50 percent of the "income available for distribution," per AS 37.13.145(b). The versions of SB 26 that passed the House and Senate included language, later removed in conference committee, that would have overwritten the old formula with a new one based on a percentage of the POMV. Because these sections did not survive in the final version, the two different language versions remain in statute.

Part of the current debate derives from the mathematical tension between the historic dividend formula, which is based on relatively volatile fund earnings, and the POMV appropriation, which is based on the much more stable fund value. Today, following multiple years of strong market performance, the dividend calculation would absorb roughly two-thirds of the entire POMV draw: the difference between the $2.933 billion POMV draw and the $1.885 billion statutory dividend leaves $1.048 billion for government services.

However, the statutory dividend calculation is highly vulnerable to a major market correction. Although the statutory formula dividend calculation has been trending upwards, this is the result of a historically unusual 10-year bull market. Notably, the 2013 PFD of $900 more than doubled to $1,884 in 2014. This is entirely the result of the late-2008 stock market crash falling off the five-year lookback "tail." That same market event led to the 2008 dividend of $2,069 declining to $1,305 in 2009.

Now that the POMV has become law, this volatility adds a new concern for the state. An essential purpose of switching to a value-based POMV draw is to limit the draws on the fund to protect its value for future generations and provide a predictable revenue stream for state government. So long as the volatile earnings-based dividend remains in place, the general fund portion of the draw is equally volatile based on "whatever is left" after subtracting the dividend calculation.

The state's official forecasts show a relatively flat, consistent level of fund earnings of about $4 billion per year. However, a change in earnings has a much more dramatic impact on the dividend calculation than it does on the POMV draw calculation. It is important to look at results at different levels of fund performance.

For example, it is useful to contemplate what happens if fund earnings fail to meet the forecast. Consider this scenario: what happens if instead of earning $4 billion, the fund merely breaks even in FY 2020? In this scenario, all subsequent years' performance is unchanged.

This $4 billion lost from the future value of the fund shows up as a small decrease to the POMV: about $40 million in FY 2022 and $200 million in FY 2026 and beyond. However, that same $4 billion loss would have a much more immediate and dramatic impact on the dividend formula: $425 million per year, reducing the next five individual dividends by more than $600 each. Additionally, since the POMV impact is smaller than the dividend impact, the general fund portion of the annual draw would increase by more than $300 million per year for several years. In other words, in current law, funds available for budgeting each year are greater when the permanent fund performs poorly.

Because of the tension between two statutes, a dividend based on fund earnings introduces volatility that could reduce the effectiveness of the POMV, as it makes it much harder to project the funds available for a given budget cycle. Regardless of one's feelings on the appropriate size of the dividend, this is an issue that should be discussed and resolved.

4. Working Group Meeting Synopses

What follows are synopses of the six meetings in 2019 of the Bicameral Permanent Fund Working Group. See the appendix for minutes of each hearing.

Meeting One – June 12, 2019

Topic: Organizational meeting.
Presenters: None. Members discuss tasks and organizational structure.
Presentations: None. House Concurrent Resolution 101 provided as backup document.

The first meeting of the Bicameral Permanent Fund Working Group began at 9:30 a.m. on June 12, 2019, in the Senate Finance Committee Room of the Alaska State Capitol. All members were present. The purpose of the meeting was to introduce staff assigned to the working group, outline the organizational structure, and describe tasks the working group had been authorized to perform. Upon completion of this business by the co-chairs, individual members were given the opportunity to make any opening statements. Representative Wool, Senator Stedman, Senator Hughes, and Representative Kreiss-Tomkins gave brief remarks about their personal perspectives on the permanent fund dividend. Following the opening statements, Co-Chair Bishop adjourned the meeting at 9:50 a.m.

Meeting Two – June 13, 2019

Topic: Creation of three teams to analyze three PFD scenarios.
Presenters: None. Members discuss perspective on permanent fund and dividend.
Presentations: None. Documents on 1999 permanent fund advisory vote provided as background information.

The second meeting of the Bicameral Permanent Fund Working Group began at 9:30 a.m. on June 13, 2019, in the Senate Finance Committee Room of the Alaska State Capitol. All members were present. Co-Chair Johnston began the meeting by discussing protocol and establishing some ground rules for meetings. The purpose of this meeting was to give each member an opportunity to outline their expectations and deliverables for the working group. Each member described in greater detail their personal perspective on the permanent fund and the dividend program and how that perspective could be relevant to potential deliverables for the working group. Following that dialog, Co-Chair Johnston announced the intention of the co-chairs to appoint three separate teams of two members each to research and analyze different permanent fund dividend scenarios and report back to the full working group with their conclusions. Senator Hughes and Representative Kreiss-Tomkins were assigned a $3,000 dividend; Senator Olson and Representative Wool were assigned a $1,600 dividend; and Senator Stedman and Representative Merrick were assigned a “surplus” dividend, meaning whatever remains after the current budget is balanced using whatever draw necessary from the Permanent Fund Earnings Reserve Account. Specifically, the teams were asked to research and

analyze the economic and social impacts, the fund sources, and the opportunity costs or gains for each dividend scenario. Finally, Co-Chair Johnston announced the intention of the co-chairs to begin working on a thorough review of the history of the Permanent Fund and the dividend program to be presented at the next meeting. Co-Chair Johnston adjourned the meeting at 10:08 a.m.

Meeting Three – June 19, 2019

Topic: History of permanent fund and dividend laws.
Presenters: Governor Mike Dunleavy; Cori Mills & Bill Milks, Alaska Department of Law; Anne Weske, Alaska Permanent Fund Dividend Division; Emily Nauman & Linda Bruce, Alaska Legislative Legal Services.
Presentations: History of the Permanent Fund and the Payment of Dividends; Permanent Fund Law.

The third meeting of the Bicameral Permanent Fund Working Group began at 10:00 a.m. on June 19, 2019, in the Anchorage Legislative Building. All members were present. Co-Chair Bishop opened the meeting by introducing Governor Dunleavy and inviting him to address the group. Governor Dunleavy stressed the importance of the permanent fund dividend program to the residents of Alaska and wished the group luck in its work. He reiterated his position that the state should continue to follow the law as it pertains to the statutory calculation for the distribution of dividends even though it's contradicted by the POMV statute passed by the 30th Legislature. He encouraged the group to review the history of the permanent fund dividend program and consult notable Alaskans who were involved it its creation. Finally, he urged the Legislature to engage Alaskans through a public vote to reach finality on the question of the permanent fund dividend.

Following the governor's opening comments, Co-Chair Bishop continued the order of business by announcing the presentation documents that have been distributed and then invited representatives from the Department of Law to begin the first presentation on the history of the permanent fund. This presentation covered the statehood act, the 1976 constitutional amendment, Alaska's first permanent fund dividend and the *Zobel* case. (The Department of Law's presentation and the verbatim transcript are attached in the appendix).

After the Department of Law concluded its presentation, Co-Chair Bishop invited the director of the Permanent Fund Dividend Division in the Department of Revenue to provide testimony on the mechanics of the permanent fund dividend program. The director covered the statutes dictating the eligibility, application process, garnishments, distribution, and deadlines for the permanent fund dividend program. (The director's presentation and the verbatim transcript are attached in the appendix).

Representatives from the Department of Law followed with an historical analysis of the various court cases and legal challenges involving the permanent fund dividend program going back to its creation. Presenters began by outlining the contents of their presentation which entailed a

thorough review of the Permanent Fund statutes, the calculation and eligibility requirements of the permanent fund dividend program and the history of all pertinent statutes. (Legislative Legal Services' presentation and the verbatim transcript are attached in the appendix).

After a brief lunch break, the gavel was passed to Co-Chair Johnston who directed Legislative Legal Services to continue their presentation as the last item on the agenda. Upon conclusion of that presentation, the Department of Law and the Department of Revenue were invited back to provide any closing comments. Co-Chair Johnston adjourned the meeting at 3:50 p.m.

Meeting Four – June 28, 2019

Topic: Alaska Permanent Fund Corporation history and mission; three PFD scenarios; state budget and revenues.
Presenters: Angela Rodell, Alaska Permanent Fund Corporation; David Teal, Alaska Division of Legislative Finance; Bruce Tangeman, Alaska Department of Revenue.
Presentations: Untitled presentations by Alaska Permanent Fund Corporation, Alaska Division of Legislative Finance, and Alaska Department of Revenue.

Co-Chair Johnston called the fourth meeting of the Bicameral Permanent Fund Working Group to order at 10:07 a.m. on June 28, 2019, in the Anchorage Legislative Building. All members were present except for Co-Chair Click Bishop, who was excused, and Senator Bert Stedman.

Angela Rodell, executive director of the Alaska Permanent Fund Corporation, provided a presentation on the history and mission of the Alaska Permanent Fund, starting with voter approval of an amendment to create the fund in the state constitution in 1976 and legislative approval to create the corporation in statute in 1980. She then outlined how investment strategies have changed over time, from more cautious strategies of yesteryear limited to things such as certificates of deposit to more diversified portfolios of today of stocks, bonds, real estate, and private equities. The permanent fund, she noted, received its initial deposit in 1977 of $734,000 in oil revenues. By June 30, 2019, the fund was expected to be worth nearly $66.1 billion.

David Teal, director of the Alaska Division of Legislative Finance, presented three budget scenarios based on three different permanent fund dividends: one based on statute valued at nearly $3,000 per qualified Alaskan; another equal to the $1,600 dividend that residents received in 2018; and, the last based on revenues available after funding government services. He outlined various scenarios, including one that showed that if the state were to spend $4.4 billion in unrestricted general funds, there would be a surplus of $800 million – enough to pay out a dividend of $1,178 per Alaskan. If, on the other hand, state spending was nearly $3.3 billion, there would be more than $1.9 billion to use for a dividend of $2,977 per resident. Teal demonstrated that paying a statutory dividend while maintaining state spending at current levels – while allowing for growth in inflation – would result in the depletion of permanent fund earnings in about ten years. Using similar budget assumptions, permanent fund earnings would grow slowly while paying out an annual dividend of $1,600 and more significantly while

providing dividends based on surplus revenues – the amount available after funding government services.

Bruce Tangeman, commissioner of the Alaska Department of Revenue, presented revenue models to explain how permanent fund earnings had grown to $19 billion. In fiscal years 2017, 2018, and 2019, more than $4.7 billion would have been paid out in dividends based on the current statutory formula, but only $2.4 billion was appropriated – leaving an amount of $2.3 billion that was not distributed. By not paying out full statutory dividends over those three years, the permanent fund earned $389 million in interest.

Tangeman said there are many ways to address the fiscal issues that the state faces. Cutting dividends, he noted, is the most regressive option. A fiscal crisis, he said, may not exist because of promising oil development on Alaska's North Slope, and he cautioned that "we may be trying to solve a temporary problem with a permanent solution." He recommended gathering more information before making drastic changes. Co-Chair Johnston adjourned the meeting at 4:12 p.m.

Meeting Five – July 8, 2019

Topic: Presentations by working group teams on three PFD scenarios.
Presenters: Sen. Shelley Hughes & Rep. Jonathan Kreiss-Tomkins; Sen. Donny Olson & Rep. Adam Wool; Sen. Bert Stedman & Rep. Kelly Merrick.
Presentations: Sen. Hughes & Rep. Kreiss-Tomkins – Statutory $3,000 PFD; Sen Olson & Rep. Wool – $1,600 PFD; Sen. Stedman & Rep. Merrick – Surplus PFD.

Co-Chair Bishop called the fifth meeting of the Bicameral Permanent Fund Working Group to order at 9:04 a.m. on July 8, 2019, in the Senate Finance Committee Room of the Alaska State Capitol. All members were present except for Senator Olson. Three working group teams presented their work on the fiscal impacts of having three different sizes of permanent fund dividends: one based on the current statutory formula; another that reflected the $1,600 checks residents received in 2018; and, one based on surplus funds left over after balancing the state budget with traditional revenues and an amount of permanent fund earnings limited by the current law that was enacted in 2018. Working group team reports, are in this report in "5. Working Group Team Assignments." Co-Chair Bishop adjourned the meeting at 9:51 a.m.

Meeting Six – October 7, 2019

Topic: Models and scenarios on permanent fund earnings and the budget.
Presenters: Alexei Painter, Alaska Division of Legislative Finance.
Presentations: Permanent Fund Working Group: Models and Scenarios; Permanent Fund Dividend Interactive Model.

Co-Chair Bishop called the sixth meeting of the Bicameral Permanent Fund Working Group to order at 9:59 a.m. on October 7, 2019, in the Anchorage Legislative Building. All members were

present except for Senator Olson. Co-Chair Bishop announced that the working group has a website, www.pfalaska.org, that has videos, presentations, working group team reports, fiscal models, minutes, and other documents from each meeting.

Members heard from Alexei Painter, fiscal analyst with the Alaska Division of Legislative Finance, who presented various models and scenarios on permanent fund earnings and the state budget. He also unveiled a permanent fund dividend interactive model based on the Fiscal Year 2020 budget to allow members of the public to see how figures they choose for oil prices and dividends affect the state budget and the size of the deficit. For more on this, see "6. Working Group Models." Co-Chair Bishop adjourned the meeting at 11.40 a.m.

5. Working Group Team Assignments

On June 13, 2019, the co-chairs assigned white paper reports to pairs of workgroup members that would discuss paying three different PFD amounts. The partners and assignments were as follows:

Working Group Teams	PFD Amount
Senator Hughes & Representative Kreiss-Tomkins	Statutory PFD (Statutory Net Income)
Senator Olson & Representative Wool	$1600 PFD (Fixed amount)
Senator Stedman & Representative Merrick	Surplus/net-dividend (POMV)

Each report was to consider:

- Fund sources available for the assigned dividend amount
- Potential budget consequences of assigned dividend amount
- Economic impacts of assigned dividend amount
- Social impacts of assigned dividend amount
- Opportunity costs and/or gains associated with the assigned dividend amount
- Assigned dividend amount compared to historic dividend payouts
- Sustainability of assigned dividend amount, considering current budget needs

On July 8, the teams presented their work. What follows are papers on:

- **The Statutory $3,000 PFD** by Sen. Hughes & Rep. Kreiss-Tomkins (Links to appendices from their work are in the appendix of this report. Their appendices also are available at www.pfalaska.org)
- **The $1,600 PFD** by Sen. Olson & Rep. Wool
- **The Surplus PFD** by Sen. Stedman & Rep. Merrick

Statutory Permanent Fund Dividend

By Senator Shelley Hughes and Representative Jonathan Kreiss-Tomkins
July 7, 2019

Economic Impacts of Statutory $3,000 Dividend

- According to an Institute of Social and Economic Research (ISER) Study "Short-Run Economic Impacts of Alaska Fiscal Options" at Table III-6, supplying the multiplier accounting effects due to dollars in the hands of citizens versus government,[4] a transfer of $1.9 billion from the Earnings Reserve to the Permanent Fund Dividend (PFD) program could result in the following:
    - Between $2.47 and $2.83 billion in total Alaska additional income
    - Positive impacts to 10,602 and 16,948 total jobs in Alaska
    - Between 36,000 and 45,000 Alaskan incomes raised above poverty level
- Examining Alaska's fiscal gap and its impacts on Alaska families, of all the options for revenue generation (PFD cut, sales tax, flat-rate income tax, property tax, graduated income tax), PFD cuts are "by far the costliest measure to Alaska families"[5] and the only option of those listed born solely by state residents.

(Economic impacts of $3,000 PFD analyzed independent of other budget decisions.)

Social Impacts of Statutory $3,000 Dividend

- Employment: It is estimated that a $1,000 increase in the amount of the PFD per person "increases the probability of employment by 1.8 percent among men" and a reduction in hours worked by 0.9 hours per week among women.[6] By extrapolation, $3,000 would increase the probability of employment by Alaskan males by 5.4% and the reduction in the workplace of women by 2.7% fewer hours. (Some women may choose to take on tasks outside of the workplace when PFD provides some income.)
- Consumption: "On average, the marginal propensity to consume non-durable goods out of the PFD is 25 cents out of each dollar."[7] A $3,000 dividend would result in $750 per dividend spent on non-durable goods, or $480 million total.
- Poverty: "The PFD provides an income floor and therefore, perhaps, one of its most important contributions is in eliminating poverty."[8] According to the cited report, in 2000 roughly 12.4% of rural Alaskan Natives were lifted out of poverty due to the PFD.

---

[4] Gunnar Knapp, Matthew Berman, & Mouhcine Guettabi, Short-Run Economic Impacts of Alaska Fiscal Options, INSTITUTE OF SOCIAL AND ECONOMIC RESEARCH, at III-9 (Table III-6) (Mar. 30, 2016). [Appendix A] (On File with Office of Senator Shelley Hughes)
[5] Matthew Berman & Random Reamey, *How Much Might Closing the State Budget Gap Cost Alaska Families?* Research Summary No. 83, at 1 (Feb. 2017). [Appendix C]
[6] Mouhcine Guettabi, What Do We Know About the Effects of the Alaska Permanent Fund Dividend?, INSTITUTE OF SOCIAL AND ECONOMIC RESEARCH, at 2 (May 20, 2019) (citing Bibler, A., M. Guettabi, & M. Reimer, Short-term Labor Responses to Unconditional Cash Transfers (2019) (working paper)). [Appendix E]
[7] Id. at 7 (citing Kueng, L., Excess Sensitivity of High-Income Consumers, Quarterly Journal of Economics 133 (4), at 1693-1751 (2018)). [Appendix E]
[8] *Id.* at 7 (citing Berman, M., *Resource Rents, Universal Basic Income, and Poverty Among Alaska's Indigenous Peoples*, WORLD DEVELOPMENT 106, 161-172 (2018)). [Appendix E]

- Crime: A study examining criminal reports and the PFD distribution from 2000 to 2016 indicates a 10% increase in substance abuse incidents and an 8% decrease in property crimes in the four weeks following PFD distribution.[9]

Context of Historical Dividend Payments

The average dividend payment since the inception of the PFD program, adjusted for inflation, is $1,700.[10] The largest dividend Alaskans received, adjusted for inflation, was $2,864 in 2000.[11] The smallest, adjusted for inflation, was $801 in 1984.[12] Gov. Hammond's original proposal for a PFD, based on 21 years of state residency, was up to $1,050 in 1980 dollars which is $3,264 in 2019 dollars; the first PFD paid under the statutory formula in 1983 was $386, or $978 in 2019 dollars.

Statutory PFD under Current FY 2020 Budget

Distribution of $3,000 PFD and FY2020 Budget Consequences

- 5.25% POMV revenue (drawn from ERA): $2.93 billion[13]
- Amount required for PFDs, if funded at statutory $3,000 level: $1.94 billion[14]
    - POMV remaining: $990 million
- Unrestricted revenue (derived primarily from oil): $2.30 billion[15]
    - Total funds available: $3.29 billion
- Amount needed for operating and capital budgets, absent any vetoes and assuming capital budget fund source changes occur: $4.65 billion[16]
    - Additional funds needed to fill budget gap: $1.36 billion

Options to Fill FY 2020 Budget Gap

1. $460 million (approximate) in budget reductions through gubernatorial vetoes, assuming no override
2. Available fund sources[17] (assuming funds are not swept into the CBR)
    - Constitutional Budget Reserve (CBR): $2,268.5 million
    - Statutory Budget Reserve (SBR): $172.4 million
    - Alaska Higher Education Investment Fund: $340.7 million
    - Community Assistance Fund $90 million
    - Power Cost Equalization Endowment (PCE): $989.4 million

---

[9] *Id.* at 8 (citing Watson, B., M. Guettabi, and M. Reimer, *Universal Cash and Crime*, REVIEW OF ECONOMICS AND STATISTICS ACCEPTED (2019)). [Appendix E]

[10] *See* Legislative Research Services, Alaska Permanent Fund Dividend Amounts Adjusted for Inflation to 2018 Dollars (June 2019). [Appendix F]

[11] *Id.* [Appendix F]

[12] *Id.* [Appendix F]

[13] *See* Department of Revenue, Tax Division, Spring 2019 Revenue Forecast, at 7. (On file with Office of Senator Shelley Hughes)

[14] *See* Legislative Finance Division, LFD Fiscal Model, Full Statutory PFD – Current FY20 Budget, at page 2 (FY20 "POMV Amount for PFDs") (June 25, 2019). [Appendix L]

[15] *See* Department of Revenue, Tax Division, Spring 2019 Revenue Forecast, at 7 (reflecting Total Unrestricted Revenue of $5,237 million and Alaska Permanent Fund Investment revenue of $2,933 million, for a difference of $2,203 million). (On File with Office of Senator Shelley Hughes)

[16] *See* Legislative Finance Division, LFD Fiscal Model, Full Statutory PFD – Current FY20 Budget, at page 2 (FY20 "UGF Budget") (June 25, 2019). [Appendix L]

[17] Account balances confirmed by Legislative Finance Division on 6/27/19. (On file with Office of Senator Shelley Hughes)

- Alaska Housing Capital Corporation Fund: $0.2 million
- Alaska Capital Income Fund: $11 million
- Permanent Fund Earnings Reserve Account (ERA): $19 billion*

3. Revenues (the PFD Working Group co-authors disagree on the advisability of revenues at this time)
   - Only existing revenue sources can be increased in FY2020

**Additional Draw from ERA:*
The PFD Working Group co-authors agree that drawing an unsustainable amount (in excess of 5.25% POMV) from the Permanent Fund's ERA is the worst of all the available options. Increasing the draw from $2.93 billion to $4.25 billion would equal a 7.6% POMV draw which is 2.325% above the 5.25% allowed under AS 37.13.140 (b), which is already on the outer bounds of sustainably managing the Permanent Fund.

PLEASE NOTE: In addition to presenting the short-term financials above for a full $3,000 statutory PFD based on the current budget, the following short-term financials are included in the Appendix:

1. *Short-term financials for a full statutory PFD based on a FY21 (Barnhill) right-sized budget* [Appendix G]
2. *Short-term financials for a 50/50 POMV PFD based on current FY20 budget* [Appendix H]
3. *Short-term financials for a 50/50 POMV PFD based on a FY21 (Barnhill) right-sized budget* [Appendix I]

<u>Sustainability of Statutory PFD FY 2021 and Beyond</u>
Without exceeding the POMV draw,[18] the legislature should make wise decisions on other fiscal options like additional budget reductions or sensible revenue measures.[19]

PLEASE NOTE: The following are included in the Appendix

1. *Long-term projections for full statutory PFD based on current FY20 budget* [Appendix L]
2. *Long-term projections for full statutory PFD based on FY21 (Barnhill) right-sized budget* [Appendix M]
3. *Long-term projections for 50/50 POMV PFD based on current FY20 budget* [Appendix N]
4. *Long-term projections for 50/50 POMV PFD based on FY21 (Barnhill) right-sized budget* [Appendix O]

[18] As of 2018, AS 37.13.140(b) limits the amount withdrawn from the Earnings Reserve to the POMV, which is 5.25% for three fiscal years then 5.0% thereafter, providing: "The combined total of the transfer under (b) of this section [(establishing the transfer to the dividend fund)] and an appropriation under (e) of this section [(establishing maximum amount that may be transferred to the general fund)] may not exceed the amount available for appropriation under AS 37.13.140(b) [(establishing the POMV)]."
[19] *See* Legislative Finance, LFD Fiscal Model, Full Statutory PFD – Current FY20 Budget, at page 2 (June 25, 2019). [Appendix L]

Potential Revenue Sources

The PFD Working Group co-authors disagree on the advisability of revenue at this time, and have diverging opinions on the need, timing, and type of options most suitable. In the future, if the budget is not reduced and/or oil revenues drop for a sustained period, the legislature may wish to explore the following:

- Diverting the oil and gas property tax plus the raw fish tax from municipalities (as proposed by the governor this year) for $450 million
- A 3% sales tax for $480 million
- 2% flat income tax of adjusted gross income for $500 million
- $1/gallon added to motor fuel tax for $500 million
- Eliminating the $8 per-barrel oil tax credit for $1.2 billion
- A progressive income tax for $700 million
- An expanded tax base through economic diversification

Closing Remarks

The PFD provides social and economic benefits to Alaskans, particularly Alaskan families. While the PFD Working Group co-authors disagree about the *net* impact of a $3,000 PFD in conjunction with a budget that has been substantially reduced, the co-authors agree that, considered on its own, the full statutory PFD would increase Alaskans' income and reduce poverty. Due to the assurance of the annual payments, one of the most significant impacts of the PFD is that Alaskan shareholders have been watchdogs over the Permanent Fund.[20]
The budget gap can be reasonably closed, perhaps through a "grand compromise," by a combination of budget reductions and increased revenue. The PFD Working Group co-authors agree that the PFD issue must be resolved so that the Permanent Fund is truly protected and the 5.25% draw is not exceeded.

The five-year impasse in the legislature over the amount of the annual dividend is largely attributed to three philosophical perspectives: *(1) the budget itself is unsustainable and needs to be reduced to exist within the current level of revenues thereby allowing payment of a statutory PFD; (2) the size of the PFD is unsustainable and must be changed in order to fund services; and (3) Alaska needs to enact more revenue to pay a statutory PFD and to fund services.*

[20] Governor Hammond, urging passage of PFD legislation as an ongoing program, explained that the idea some had of a one-time-only benefit "does nothing to create a constituency which will safeguard against invasion of the Permanent Fund," and "does nothing to recognize that oil wealth is our children's legacy and belongs not just to those here today." Jay Hammond, Governor, Letter to Al Adams, House Finance Committee Chairman (Apr. 1, 1982). [Appendix J] "I wanted to encourage contributions into the investment account and to protect against its invasion by politicians by creating a *militant ring of dividend recipients* who would resist any such usage if it affect their dividends." Jay Hammond, DIAPERING THE DEVIL: A LESSON FOR OIL RICH NATIONS 16, 2d Ed. (2011) (emphasis added). (On file with Office of Senator Shelley Hughes)

Based on a review of historic documents dating back to 1975, below are key points considered in establishment of the PFD[21] which legislators today should bear in mind.

- Only 1% of Alaska land is available for private individual ownership.
- Subsurface rights became jointly owned at statehood.
- Annual PFD payouts cause Alaskan shareholders to be watchdogs, protecting the fund and ensuring its growth.
- PFD dollars distributed to Alaskan shareholders benefit Alaskans equitably.

The co-authors of this $3,000 PFD white paper believe that in order to achieve a lasting agreement on a PFD "grand compromise," elements of all three viewpoints must be considered to achieve a sustainable budget: budget reductions; revenue measures; and a PFD/government split that does not overdraw the Permanent Fund and that is fair and agreeable not only to legislators but to the people of Alaska. While the co-authors do not concur on how to weight each of these three elements, both agree that it is necessary to settle the PFD matter so it is not a recurring legislative battle each year.

Very special thanks to Buddy Whitt, Chief of Staff to Senator Hughes, for preliminary draft concepts related to social and economic impacts, for preparation of short-term financial reference sheets, and for appendix assembly assistance; to Kevin McGowan, Legislative Aide to Representative Kreiss-Tomkins, for preliminary draft concepts related to budget consequences and final editing; to Ken Alper, Legislative Aide to Representative Chris Tuck, for FY2020 financial data as well as information on potential revenue sources; to Sonja Kawasaki, Chief of Staff to Senator Wielechowski, for preparation of long-term financial reference sheets and inflation chart, for editing, historic research, and all citation/reference work. Acknowledgments to Legislative Finance, Dept. of Revenue, Office of Management & Budget, and Legislative Director's Office for their expert assistance.

[21] *See* policy statements, *supra* notes 34, 35, & 37. The plan for the Permanent Fund Dividend program was foremost rooted in the constitutional principle that Alaska's natural resources are held collectively in trust for the Alaskans as the beneficiaries. "The legislature shall provide for the utilization, development, and conservation of all natural resources belonging to the State . . . for the maximum benefit of the people." ALASKA CONST. art. IIIX, § 2. As Jay Hammond once said, "I believed the best, perhaps the *only* way to meet our constitutional mandate to manage our natural resources for the maximum benefit of all the people was to grant each citizen an ownership share in Alaska's resource wealth to be used as they, not the government, felt was for their maximum benefit." Jay Hammond, DIAPERING THE DEVIL: A LESSON FOR OIL RICH NATIONS 16, 2d Ed. (2011). (On File with Office of Senator Shelley Hughes)

Alaska with a $1,600 dividend

By Senator Donny Olson and Representative Adam Wool
July 8, 2019

Introduction:
The Alaska Permanent Fund Corporation (APFC, or APF) began disbursing dividends in 1982. Since that time the Permanent Fund has become a fixture in Alaska society. This Working Group has convened because points of view differ greatly on what the future of the Permanent Fund should look like. Regardless of one's stance most agree that the Permanent Fund has changed the way Alaskans perceive the role of their government over the years since its establishment. Notably, Alaska does not have any kind of a broad-based tax, such as an income or sales tax as a source of revenue, and the Permanent Fund is the only fund of its kind that delivers dividend payments directly to its citizens. The Permanent Fund dividend program wasn't created as a needs-based program to inject cash into the hands of low-income families, nor was it created with a percentage of overall income as a parameter, it was created as a way to keep citizens more involved in the workings of the Permanent Fund and to incentivize them to prevent the government from reckless spending down of the fund that is meant to provide for generations to come.

Economic impacts:
A 1984 paper published by UAA's Institute of Social and Economic Research (ISER) titled "The Alaska Permanent Fund Dividend Program: Economic Effects and Public Attitudes" outlines many positive economic impacts of the Permanent Fund Dividend (PFD) program and described general support among Alaskans for the program. The report finds that lower-income households are more greatly impacted by the dividend program than higher income households. Adjusted for inflation, the average payout of the dividend has been about $1100 since its inception. Actual payment amounts range from about $300 in the beginning to a high of just over $2000 in 2015. The amount of $1600 was the amount paid out in 2018 and is higher than the average of the dividend payment amount over the last 10 years. Although there are certainly positive economic impacts of putting $1.5B into the economy there are also negative outcomes. Anecdotally, we know in recent times many more purchases are done online and go to companies headquartered outside of Alaska, so the money often does not stay in Alaska to help local businesses. Even purchases of airline tickets and box-store purchases have little effect on the local economy.

Social impacts:
As a sovereign wealth fund the Alaska Permanent Fund is something of an anomaly, being the only one to disperse dividends. This has created a unique perspective about the purpose of the fund among Alaskan residents, which has been noted by Angela L. Cummine of The University of Oxford. In a research article published in Basic Income Studies, Volume 6, issue 1 "Overcoming Dividend Skepticism: Why the World's Sovereign Wealth Funds Are Not Paying Basic Income Dividends," general support of universal income is offered: "The PFD program

runs irrespective of whether the State of Alaska is in surplus or deficit. Also, Universal Income programs are generally needs-based so that they help those that need the income and don't go out to every man, woman and child as the PFD does."

Every year, at least 25% of mineral resource royalties must be put into the corpus or principal of the Permanent Fund, regardless of whether Alaska can balance its budget. During several years over the past decade, the APF has grown while the state budget of Alaska has faced deficits. Despite a deficit in 2000, the Legislature appropriated an extra $250 million for the Permanent Fund principal from the earnings reserve. From the Norwegian perspective, such an arrangement means the APF is not achieving its purpose of being a savings fund. The savings are built on a fiscal illusion of surplus where the obligation to pay dividends becomes detrimental to the long-term financial health of the state. The Legislature becomes constrained, as the dividend becomes an expected component of an individual's income. An October 2003 poll by Dittman Research Corp. found that 64% of Alaskans believed that they were entitled to their dividend, even if Alaska has a budget deficit (Lewis, 2004, P. 81.)"

Middle ground can be found in this debate; there are options to provide funding for adequate state services such as K12 education, public safety, infrastructure, Alaska Marine Highway System, and Pioneer Homes, and still provide funding for a reasonable, sustainable Permanent Fund dividend program to disburse checks to eligible Alaskans to spend as they desire.

Funding sources:
What funding sources are needed to get to a $1600 PFD? With the operating budget that the House and Senate passed to the Governor, there exists a $600 million surplus, which would allow for a $1000 PFD. To reach $1600, we'd need an additional $400 million.
Where available funding sources are to get the needed $400 million?

1. Permanent Fund earnings reserve account
2. General Fund
3. CBR
4. Instituting a school head tax
5. Abolishment of oil tax credits
6. Instituting Income Tax

Given the above sources, it seems the CBR is the only one that can be achieved. Tapping into the earnings reserve goes against SB26 and also will overdraw the fund and put it at risk. Tapping into the general fund will cut programs beyond a reasonable level. Any type of tax increase is very difficult politically and likely will be vetoed by the Governor.

Opportunity cost or gains with that level of dividend:
A $1,600 dollar dividend is a negotiated amount, and doesn't directly correlate to any specific equation. It matches the dividend disbursed in 2018. It is obtainable without making cuts to state operations because we don't foresee having a surplus of $1 billion for PFD checks given our current revenue/budget situation.

New equation proposal from Rep. Wool:
If an equation is needed for a $1600 PFD I may have something that strikes a good compromise. HB132 is a bill I introduced that would use oil revenue for the basis of the PFD and not use the earnings of the fund itself. This would allow the PFD to fluctuate as the price and production of oil does and would only allow large checks to be paid out as long as large revenue was coming into the state from the resources that we export. This would prevent the state from being obligated to pay a large PFD in the event that oil revenue is low, similar to the situation we are in now.

I understand that many people are reluctant to make such a large change in how we calculate the PFD and feel that the PFD should be more of a guaranteed disbursement regardless of state resource revenue. This answers the question: "Should we pay out a PFD check if oil revenue goes to zero?". Some would answer no and in that case a PFD based on oil revenue is appropriate. HB132 uses the value of 40% of oil revenue, which would generate a PFD of about $1400 based on this year's oil revenue.

If people feel that a PFD check should be disbursed even if oil revenue is zero then I suggest the "20:20 Plan." The 20:20 plan would use a value of 20% of oil revenue and 20% of POMV draw to both contribute to the PFD check. The POMV draw value is very stable and predictable and isn't as volatile as oil revenue and would provide a guaranteed base for the PFD. The oil component would add to the POMV portion depending on how the state's #1 industry is performing that year. People equate the PFD to oil revenue and creating a more substantial link to oil and possibly gas production is a good way to keep the public involved. The 20:20 plan would yield a $1600 PFD using current revenue and POMV values.

A Surplus Permanent Fund Dividend for 2019

By Senator Bert Stedman and Representative Kelly Merrick
July 8, 2019

Introduction

We were tasked with analyzing the impacts of a "surplus dividend." A "surplus dividend" is a permanent fund dividend amount calculated annually after appropriations have been made for the next fiscal year's operating and capital budgets. Using the amount of "surplus" funds to set an annual dividend would also be guided by statutory principles in SB 26 (2018). Funds not spent in the earnings reserve continue to be invested. This approach makes appropriations for state government the highest priority in budgeting.

In this brief analysis, we have attempted to avoid a general discussion on the Permanent Fund Dividend, and focus on the outcomes for a "surplus dividend" in 2019, with acknowledgment of future impacts were this policy to be set in statute.

A Surplus Dividend

Unlike our colleagues in the working group, our proposal did not come with a specified dollar amount for a dividend. If this policy were long term, the "surplus dividend" amount would change depending on the volatility of the oil and gas industry that provides revenue to the state, annual appropriation amounts by the Legislature, and vetoes by the Governor.
Effects on the dividend year currently under discussion are highlighted by several scenarios and estimates from Legislative Finance, based on budget expenditures. Legislative Finance estimates the present "surplus" amount at roughly $800 million. Depending on vetoes and the final capital budget funding, the "surplus" scenario provides a dividend of between $865 and $2,977[22], with a 50/50 POMV model estimated at $2,220. Other possible dividend numbers could result, based on revenue, appropriation levels, and vetoes.

Fund Source, Budget consequences, and Sustainability

The Legislature has authority over all fund sources, including the permanent fund Earnings Reserve Account, the Constitutional Budget Reserve and the General Fund. Under the given scenario, the fund source for the dividend would be the General Fund and would use the amount of funds available after appropriations for the FY 20 operating and capital budgets, use of the statutory POMV draw, and other revenues.

Because the amount of the "surplus dividend" is calculated after appropriations for operating and capital expenses, there are no budgetary consequences. Funds expended on dividends come after all other budget considerations have been funded, thus there is no effect on agency budgets. This makes a "surplus dividend" an extraordinarily sustainable option, if such a plan

[22] We left off discussion of this dividend amount in our study, as the impacts and consequences of a near-$3000 dividend are under consideration by our colleagues from Sitka and Palmer.

were to be adopted moving forward, as only funds not otherwise used for state agency spending would be distributed to Alaskans as a dividend.

Economic impacts

The economic impact of the Permanent Fund Dividend comes from a personal choice to save, invest, or spend by every Alaskan. The private sector is where economic value is created, as mentioned by Ed King in the House Finance Committee. There is no question that the dividend is an important source of disposable income for many Alaskans. A recent report on the economic effects of any dividend by ISER's Mouhcine Guettabi, Ph.D. and his presentation to the Senate Finance Committee are attached. This report indicates the dividend has a limited, short-lived impact on employment and shows an increase for purchases of goods and services between 22 and 24 cents for every dividend dollar during the three months post distribution. However, King Economics speculates that "more than 90% of PFD distributions don't enter Alaska's economy at all." He speculates that the money gets put in college savings accounts, is used for vacations, gets spent online, pays federal taxes, or on "other things."

Social impacts

Please see the report by Dr. Guettabi mentioned above. How Alaskans choose to spend their dividends and the social effects of that spending is not scrutinized. Dr. Guettabi's report does detail that the dividend does have an impact on crime, and while property crime rates decrease around the time of the payout and don't vary with the amount of the dividend, the increase in substance abuse related crimes does vary with the size of the PFD. We can surmise, then, that the lower end of the surplus PFD spectrum would result in a lower uptick in the substance abuse crime rate than the amounts under consideration by our colleagues in the working group. His report also indicates that the PFD may have a positive impact on birth weight and childhood obesity, poverty reduction, particularly for rural Alaska Natives and the elderly, but worsens income inequality (possibly because higher-income individuals can afford to save the PFD).

Opportunity costs and/or gains

As the "surplus dividend" does come directly from the earnings of the Permanent Fund, the opportunity gain is the retention and investment earnings on the difference between a surplus dividend and a statutory dividend payment from the ERA. Retained earnings would remain invested and generate additional earnings at an average rate of 8.9% a year. This decreases current economic activity but sustains and grows the balance of the earnings reserve for future investment and use.

In terms of opportunity loss, higher permanent fund dividends result in higher dollar amounts leaving the state as federal taxes. Federal taxes will be deducted, however, from any dividend amount, regardless of size.

Historic Comparison

Legislative Finance has estimated the average dividend payout over the last 36 years, given inflation, at roughly $1,660. This leaves the low end of the surplus spectrum near the inflation

adjusted amounts for the early 1980s PFDs. The largest possibility would be the highest dividend ever distributed[23].

Conclusion

As mentioned in our introduction, the "surplus dividend" concept puts a higher priority on funding state government and saving funds to generate future returns than providing currently eligible Alaskans and Alaskan families with a full statutorily calculated dividend.

In addition to the conclusions about the dividend itself, further research may be warranted in relations to the impact of the dividend on Alaskans, to better understand the state's largest expenditure.

[23] While lower than the $2,390 statutory 2017 dividend, the amount distributed for that year was $1,100.

6. Working Group Models

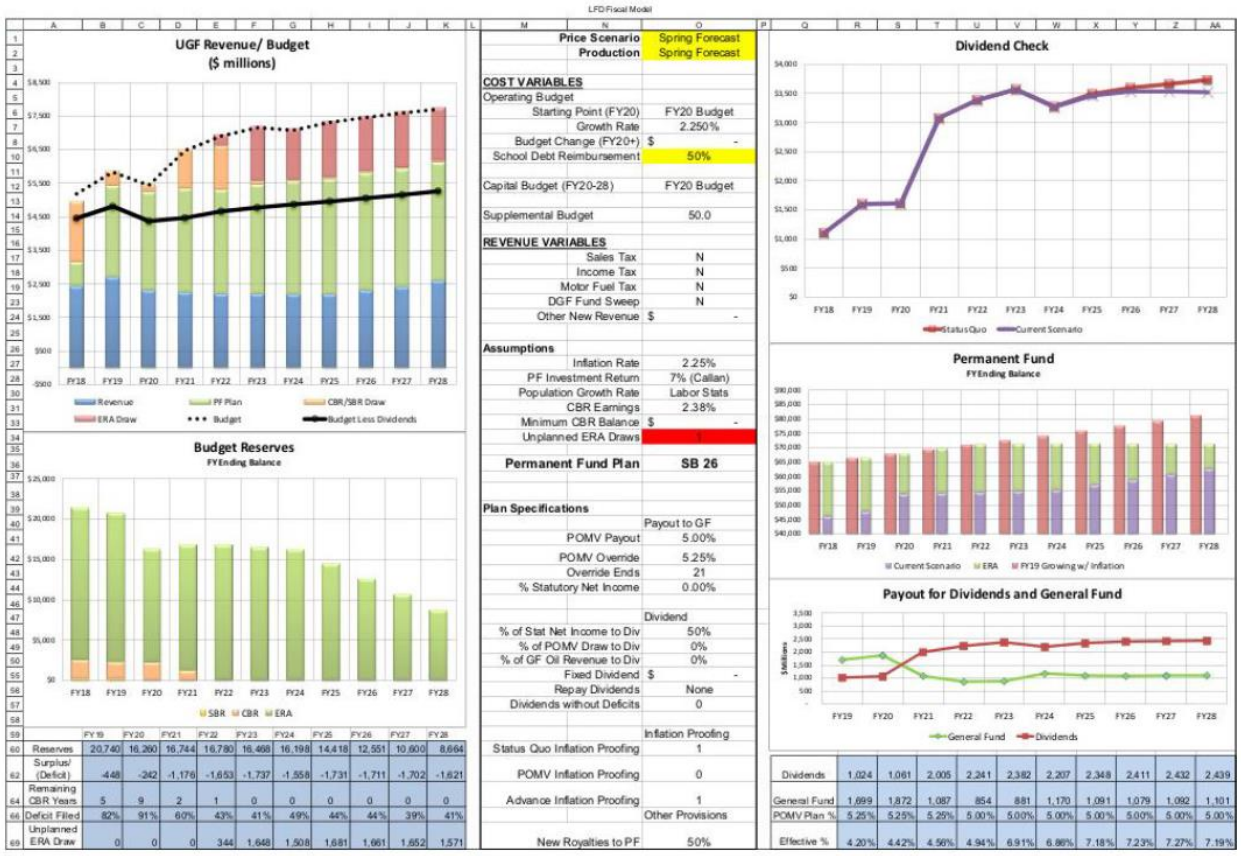
On October 7, 2019, the Permanent Funding Working Group met to discuss additional scenarios related to the use of permanent fund earnings, examining specifically the effect on state budgets, the size of permanent fund dividends, and the long-term sustainability of the fund. Before the meeting, the co-chairs gave members the opportunity to request certain scenarios, allowing the Alaska Division of Legislative Finance the opportunity to prepare for the meeting. During the meeting members asked questions and additional models were created as a result of the dialogue. This report includes the models discussed.

The following assumptions were made to ensure that the outputs of all models were consistent:

- Budget assumptions were based on the Fiscal Year 2020 enacted budget growing with inflation and statewide items followed established projections
- A $50 million placeholder was included for supplemental appropriations
- Oil revenue was based on the FY 2020 Alaska Department of Revenue Spring Revenue Forecast of $66 per barrel, although some scenarios did contemplate different oil prices
- Based on Callan's (a consultant to the Alaska Permanent Fund Corporation) projections, the model assumes 7 percent growth of the permanent fund
- No inflation proofing was included for the next four years due to the $4 billion transfer in FY 2020

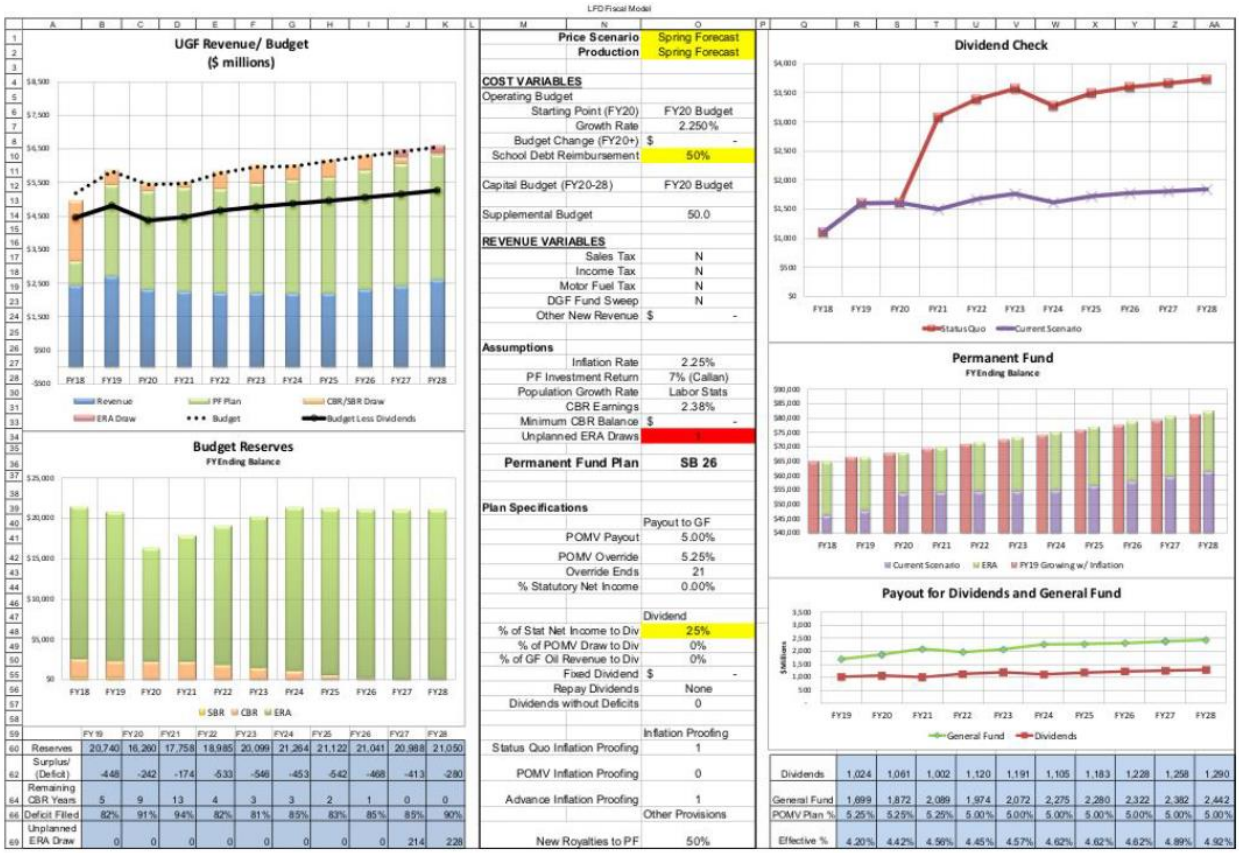
The model variables discussed most during the hearing were the size of the dividend, the size of deficits under various scenarios, and whether the permanent fund value kept up with the pace of inflation. These are the variables that are referenced most in this report.

50% of Statutory Net Income (Current Law):



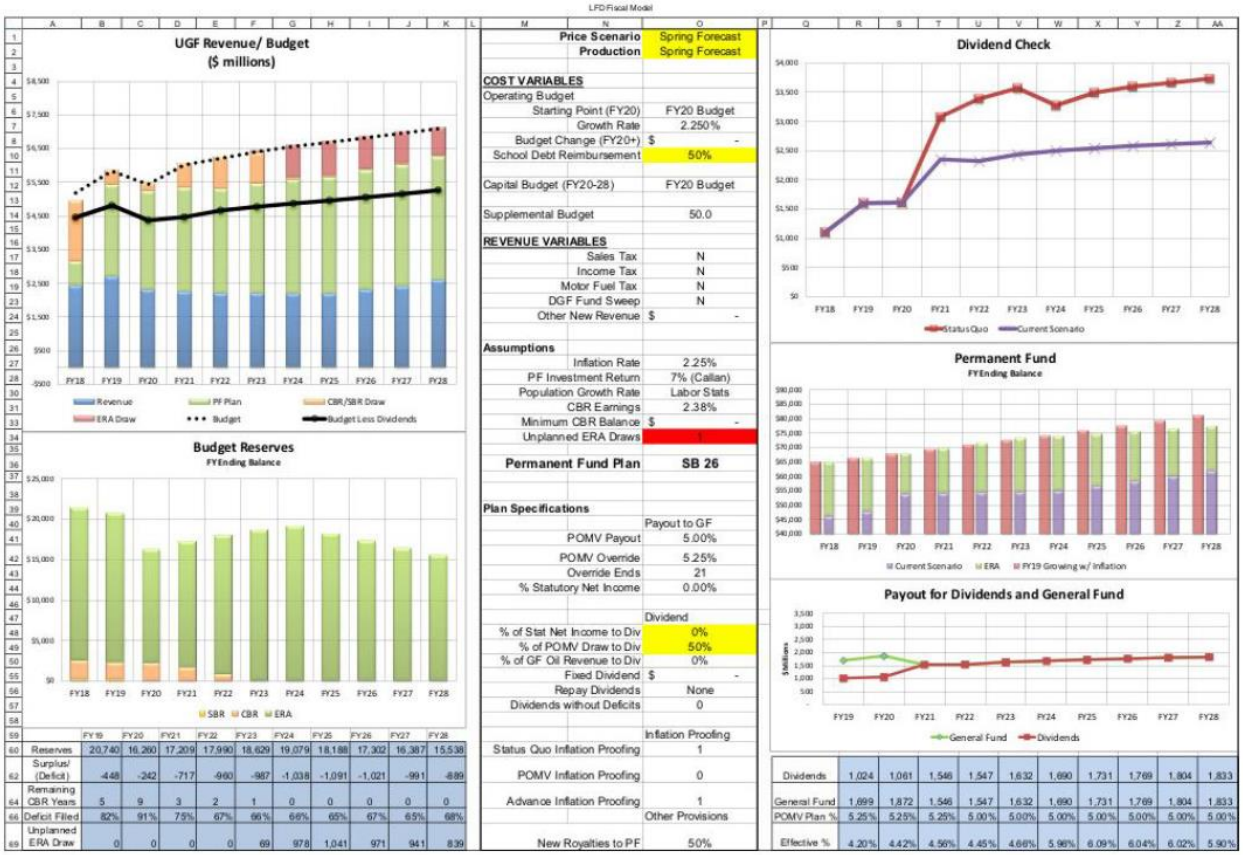
The working group hearing began by reviewing a scenario in which a dividend is paid based on current law and the POMV structure that was created with the passage of SB 26 is maintained. The current dividend formula pays an approximately $3,000 dividend rising to about $3,500. This scenario creates a deficit of about $1.5 billion - $1.7 billion, which results in the need for either new revenue sources, cuts to government spending or unplanned draws from permanent fund earnings. The model assumes that unplanned draws from permanent fund earnings will be used to fill the deficit, resulting in eventual dividend reductions of about $100-$200 starting in FY 26. The unplanned draws also result in the overall value of the permanent fund eroding due to inflation.

25% of Statutory Net Income:



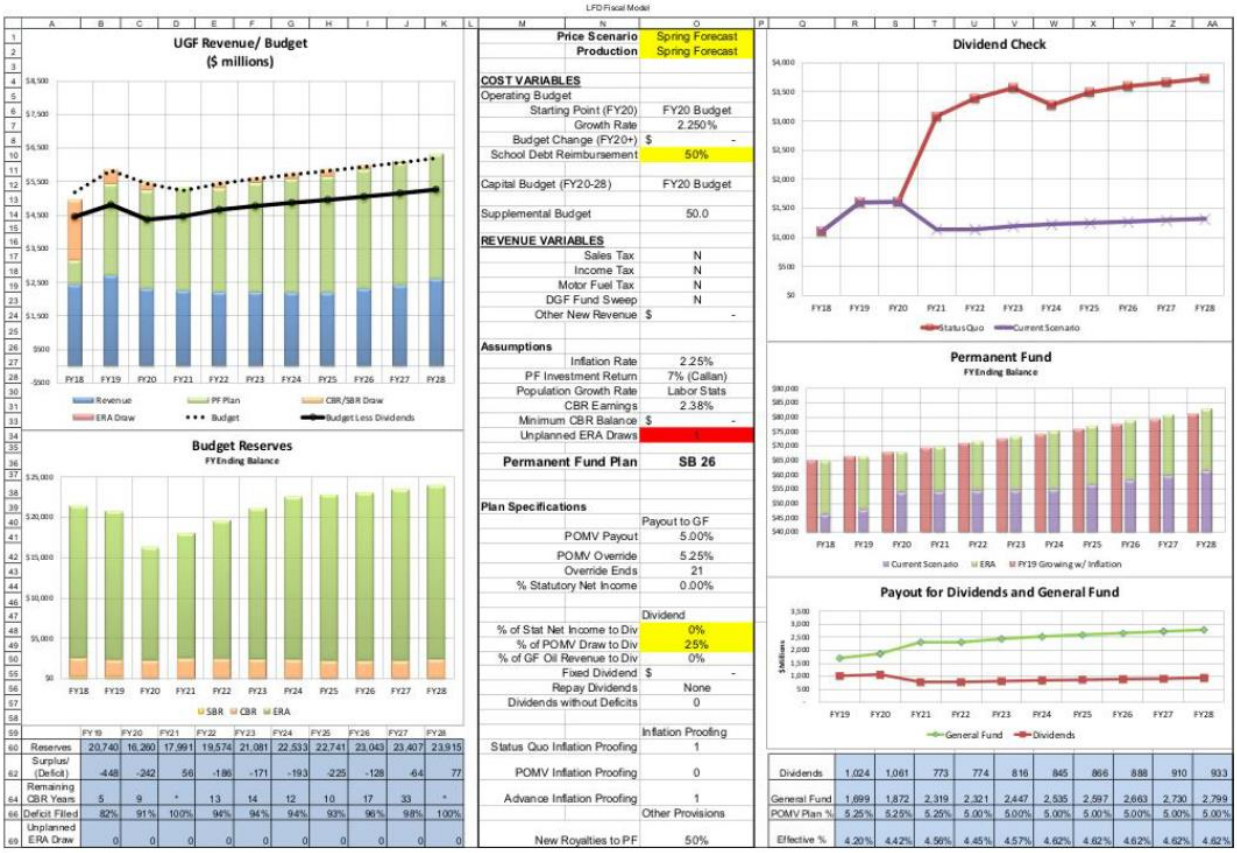
The 25 percent of statutory net income scenario illustrates a dividend reduction of 50 percent from the current statutory formula, which equates to approximately $1,500. Less of the POMV draw goes to pay a dividend, so the deficits are smaller (roughly $500 million a year). However, absent other policy decisions, there will be a need for unplanned draws from permanent fund earnings starting in FY 27. Due to the unplanned draws being delayed and less significant than the previous scenario, the overall value of the permanent fund slightly increases beyond the value inflation. The constitutional budget reserve is depleted in FY 27.

50% of Percent of Market Value:



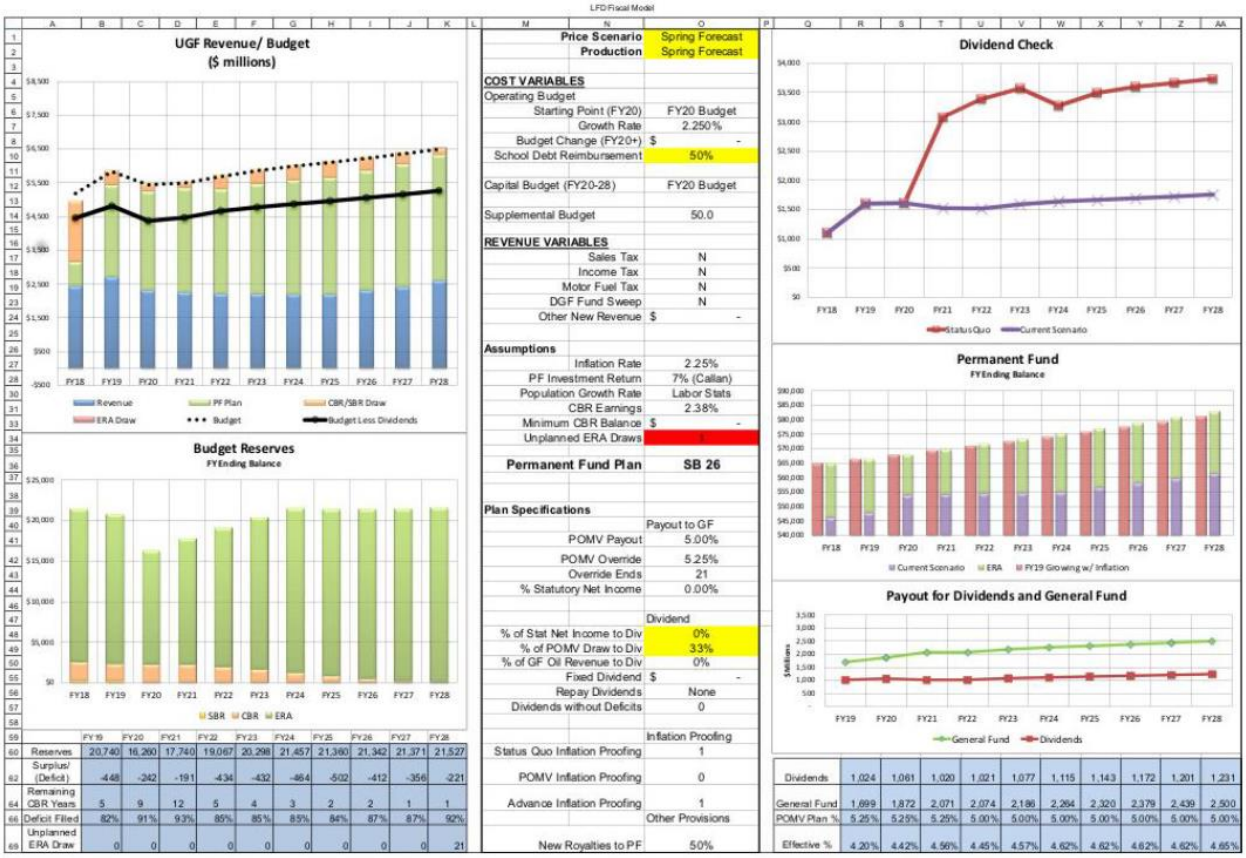
The dividend under this scenario would be half of the POMV draw resulting in a dividend of about $2,350. The remaining deficit would be about $1 billion. Absent additional policy decisions that could impact the size of the deficit, under this scenario unplanned ERA draws are necessary starting in FY 24. The additional draws on permanent fund earnings result in the overall value of the permanent fund not keeping pace with inflation.

25% of Percent of Market Value:



This scenario creates a dividend of about $1,100 rising to about $1,300 over ten years. The budget under this scenario is nearly balanced and the constitutional budget reserve maintains the amount necessary to continue its cash flow responsibilities and its balance remains essentially the same. The value of the permanent fund keeps up with the rate of inflation and the state's overall budget reserves could grow.

33% of Percent of Market Value:

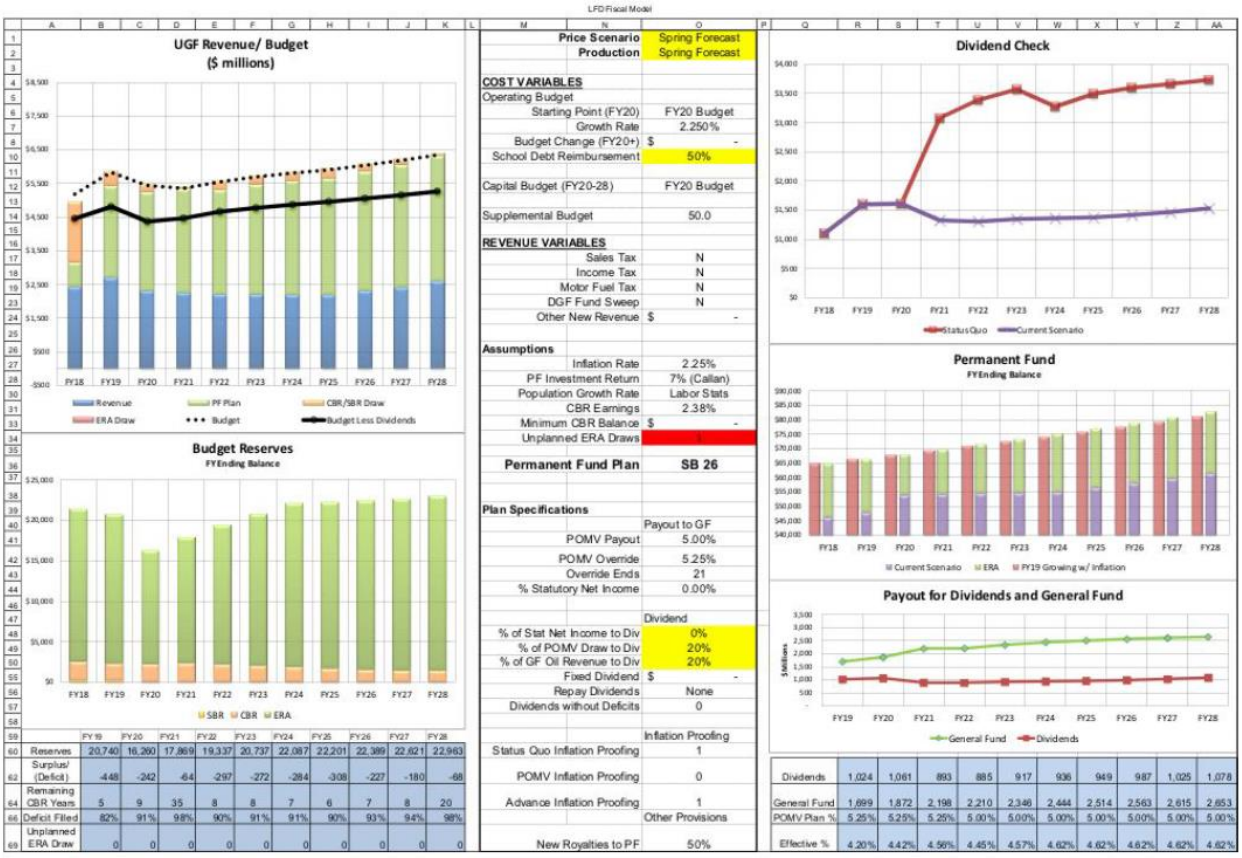


	FY19	FY20	FY21	FY22	FY23	FY24	FY25	FY26	FY27	FY28
Reserves	20,740	16,260	17,740	19,067	20,298	21,457	21,360	21,342	21,371	21,527
Surplus/ (Deficit)	-448	-242	-191	-434	-432	-464	-502	-412	-356	-221
Remaining CBR Years	5	9	12	5	4	3	2	2	1	1
Deficit Filled	82%	91%	93%	85%	85%	85%	84%	87%	87%	92%
Unplanned ERA Draw	0	0	0	0	0	0	0	0	0	21

Dividends	1,024	1,061	1,020	1,021	1,077	1,115	1,143	1,172	1,201	1,231
General Fund	1,699	1,872	2,071	2,074	2,186	2,264	2,320	2,379	2,439	2,500
POMV Plan %	5.25%	5.25%	5.25%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Effective %	4.20%	4.42%	4.56%	4.45%	4.57%	4.62%	4.62%	4.62%	4.62%	4.65%

Under this scenario the dividend would be about $1,500 growing to about $1,750 in FY 27. There are continuing deficits of $400 million to $500 million if there are no other policy decisions made to further reduce the deficit. The deficits under this scenario can mostly be managed by the constitutional budget reserve; however, it will be completely depleted by FY 28. Unless it is used to supplant constitutional budget reserve spending in an unplanned manner, the value of the permanent fund keeps up with the pace of inflation under this scenario.

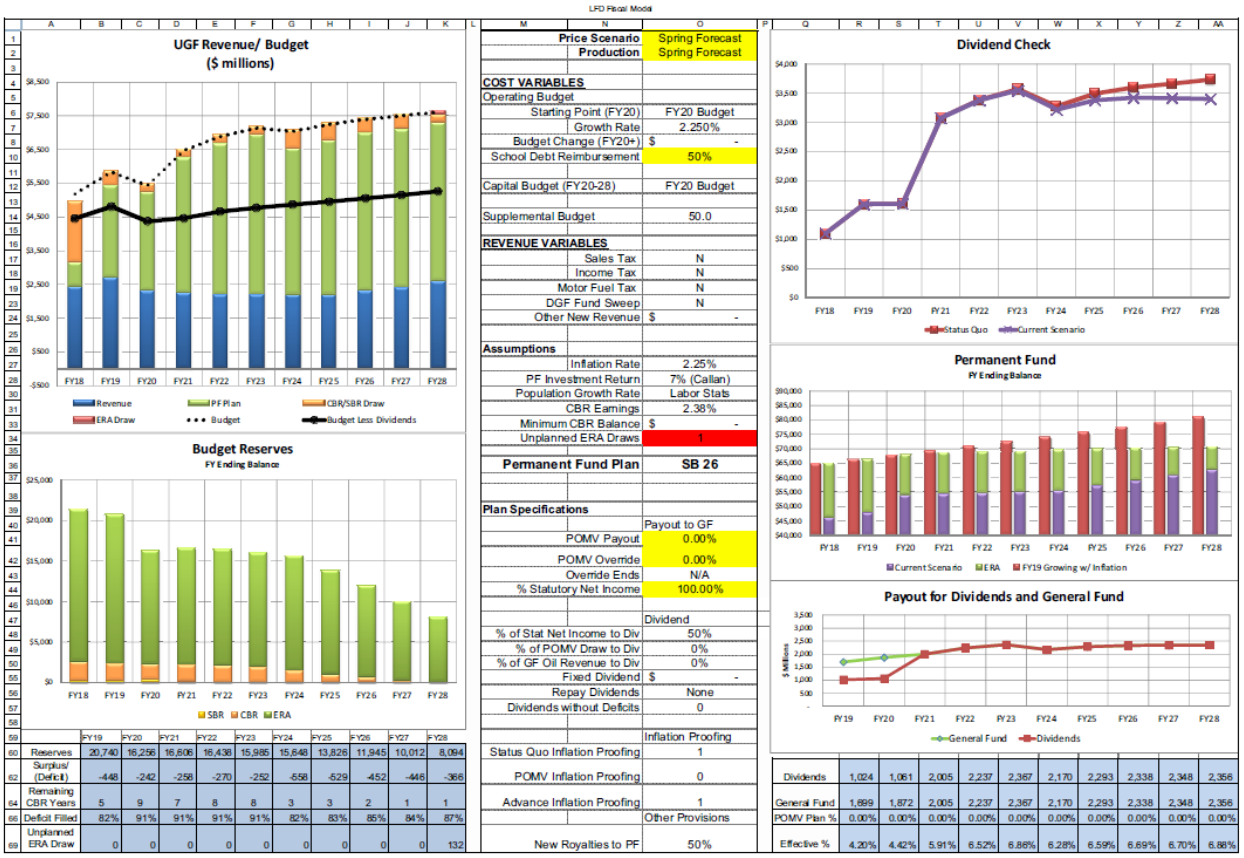
20% of Percent of Market Value, 20% of Oil Revenue:



This scenario results in a dividend of about $1,300 immediately, which gradually increases overtime. Similar to the 25 percent of POMV approach, the constitutional budget reserve could fill this scenario's deficits without other policy decisions being made to reduce the budget or increase revenue. The permanent fund's value keeps up with the pace of inflation and unplanned draws on permanent fund earnings are not necessary to balance the budget.

Additional Scenarios:

100% Statutory Net Income, 50% to PFD:



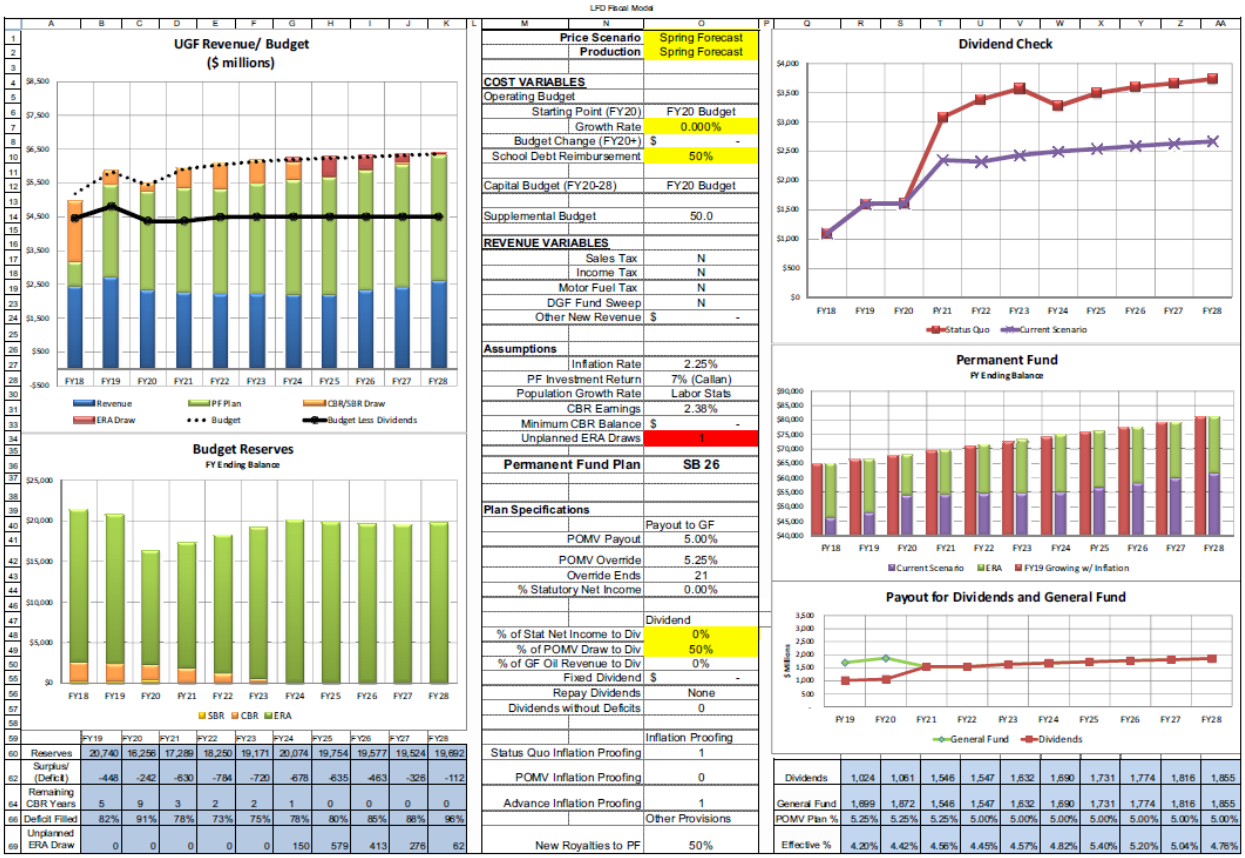
Price Scenario	Spring Forecast
Production	Spring Forecast
COST VARIABLES	
Operating Budget	
Starting Point (FY20)	FY20 Budget
Growth Rate	2.250%
Budget Change (FY20+)	$ -
School Debt Reimbursement	50%
Capital Budget (FY20-28)	FY20 Budget
Supplemental Budget	50.0
REVENUE VARIABLES	
Sales Tax	N
Income Tax	N
Motor Fuel Tax	N
DGF Fund Sweep	N
Other New Revenue	$ -
Assumptions	
Inflation Rate	2.25%
PF Investment Return	7% (Callan)
Population Growth Rate	Labor Stats
CBR Earnings	2.38%
Minimum CBR Balance	$ -
Unplanned ERA Draws	1
Permanent Fund Plan	**SB 26**
Plan Specifications	
	Payout to GF
POMV Payout	0.00%
POMV Override	0.00%
Override Ends	N/A
% Statutory Net Income	100.00%
	Dividend
% of Stat Net Income to Div	50%
% of POMV Draw to Div	0%
% of GF Oil Revenue to Div	0%
Fixed Dividend	$ -
Repay Dividends	None
Dividends without Deficits	0
	Inflation Proofing
Status Quo Inflation Proofing	1
POMV Inflation Proofing	0
Advance Inflation Proofing	1
	Other Provisions
New Royalties to PF	50%

	FY19	FY20	FY21	FY22	FY23	FY24	FY25	FY26	FY27	FY28
Reserves	20,740	16,256	16,606	16,438	15,985	15,848	13,826	11,945	10,012	8,094
Surplus/ (Deficit)	-448	-242	-258	-270	-252	-558	-529	-452	-446	-388
Remaining CBR Years	5	9	7	8	8	3	3	2	1	1
Deficit Filled	82%	91%	91%	91%	91%	82%	83%	85%	84%	87%
Unplanned ERA Draw	0	0	0	0	0	0	0	0	0	132

	FY19	FY20	FY21	FY22	FY23	FY24	FY25	FY26	FY27	FY28
Dividends	1,024	1,061	2,005	2,237	2,367	2,170	2,293	2,338	2,348	2,356
General Fund	1,899	1,872	2,005	2,237	2,367	2,170	2,293	2,338	2,348	2,356
POMV Plan %	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Effective %	4.20%	4.42%	5.91%	6.52%	6.86%	6.28%	6.59%	6.69%	6.70%	6.88%

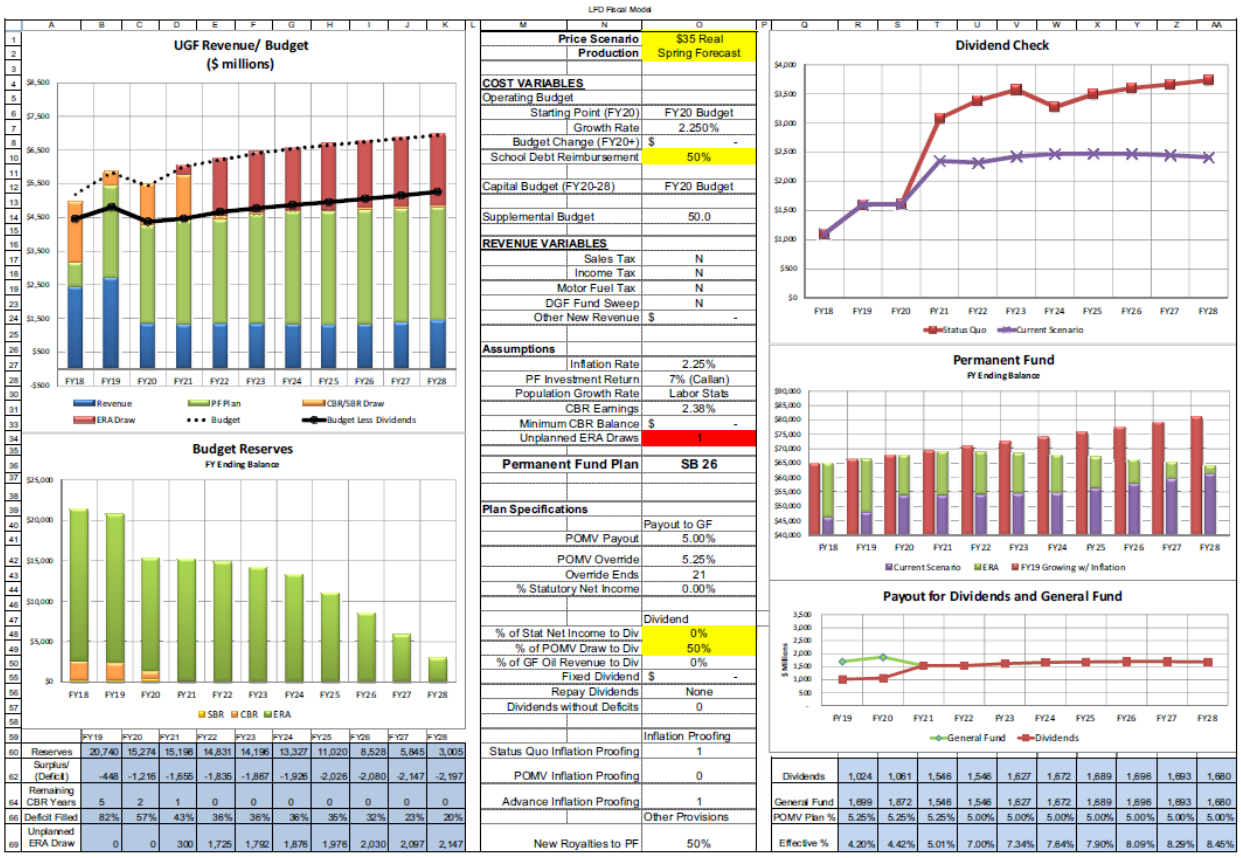
One of the scenarios that was discussed during the committee, was a model proposing spending 100 percent of the statutory net income of the permanent fund with 50 percent going to the dividend. Some refer to this as the historic payout although it is worth noting that until recently, none of the payout under this scenario has been used to support government services. All of the earnings are spent, and the permanent fund value does not keep up with the rate of inflation. The deficit is mostly filled under this scenario by the draw that is excess of the POMV established by SB 26. The constitutional budget reserve would be completely depleted in FY 28.

50% of Percent of Market Value, No Budget Growth:



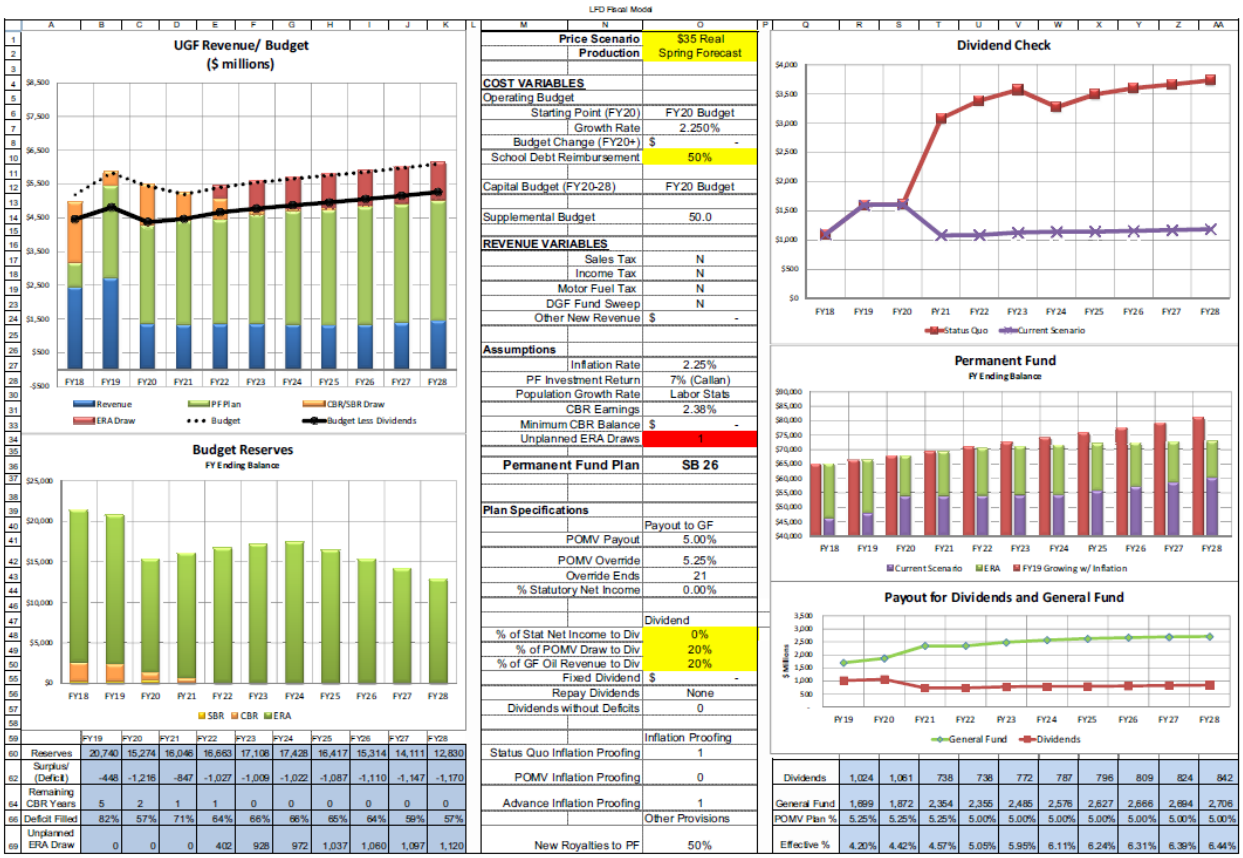
Under this scenario, deficits decrease overtime from about $700 million to $400 million. The dividend in this scenario would be $2,350 growing to about $2,600. Without making further policy decisions the constitutional budget reserve would be exhausted in FY 24 and unplanned draws from permanent fund earnings would be necessary in FY 25. The permanent fund's value is almost maintained because the deficit shrinks over time.

50% of Percent of Market Value to dividend, $35 Oil Prices:



The working group also contemplated scenarios where oil prices could decrease significantly more than the revenue forecast's predictions. In a hypothetical scenario where 50 percent of the POMV draw is used for a dividend and oil prices have dropped to $35 a barrel, the dividend would be $2,350 and grow to $2,600, while deficits would increase significantly over time. Under such a low oil price scenario, the deficit would be about $1.6 billion growing to about $2.2 billion. The constitutional budget reserve would be completely spent in FY 20 and unplanned draws would be necessary starting FY 21, absent other policy decisions being made. The permanent fund's value does not keep up with the pace of inflation under this scenario.

20% of Percent of Market Value and 20% of petroleum revenue to dividend, $35 oil:



In a scenario where oil prices drop to $35 a barrel and where the dividend amount is based on a combination of 20 percent of the POMV draw and 20 percent of collected petroleum revenue, the dividend would be about $1,100, growing slightly over time. Without further policy decisions the constitutional budget reserve would be depleted by FY 21 and unplanned permanent fund earnings draws would be necessary starting in FY 22. The deficit in FY 21 would be about $850 million growing to about $1.1 billion in 10 years. The value of the permanent fund would not keep up with the pace of inflation.

7. Appendix

Documents are arranged by meeting dates and may be found on the Bicameral Permanent Fund Working Group's website, www.pfalaska.org. Many are so large that only links to them are provided here in this report.

First Meeting – June 12, 2019

- Bicameral Permanent Fund Working Group Transcript, Meeting, 12 June 2019.pdf
- HCR 101 Bicameral Permanent Fund Working Group.PDF

Second Meeting – June 13, 2019

- Bicameral Permanent Fund Working Group Transcript, Meeting, 13 June 2019.pdf
- Alaska Division of Elections Advisory Votes, Propositions, and Questions Appearing on the Ballot in Alaska.pdf
- September 14, 1999, Special Election Official Election Pamphlet Ballot Language.pdf
- September 14, 1999, Statement in Support of Ballot Question, Governors Cowper, Hickel, Sheffield.pdf
- September 14, 1999, Statement in Opposition to Ballot Question, Governor Hammond.pdf

Third Meeting – June 19, 2019

- Bicameral Permanent Fund Working Group Transcript, Meeting, 19 June 2019.pdf
- Presentation History of the Permanent Fund and Payment of Dividends.pdf
- Presentation Permanent Fund Laws.pdf
- The First PFD Statute, 1980.pdf
- 1976 Permanent Fund Ballot Proposition & Statements of Support and Opposition.pdf
- Zobel v Williams, 1982.pdf
- Wielechowski v State, 2017.pdf
- Permanent Fund Dividend Division Statutes.pdf
- Permanent Fund Law Booklet, Legislative Legal Services, 25 June 2019.pdf
- HCR 101 Bicameral Permanent Fund Working Group.PDF
- Federal Land Ownership, Overview and Data, Congressional Research Service, 3 March 2017.pdf
- Federal Land Ownership of Original 13 U.S. States, Alaska, Permanent Fund Working Group staff, 26 June 2019.pdf
- Why was 21 percent of PF net income in 1986 law, Legislative Research Services, 20 March 2018.pdf
- Residency requirements for voters, PFDs, longevity bonus, Legislative Research Services, 12 December 1996.pdf
- PFD Hold Harmless Program, Legislative Legal Services, 6 April 2016.pdf
- PFD hold harmless program audit, Legislative Audit, 4 October 1993.pdf

- Alaska Administrative Code Alaska Pioneers' Homes, Eligibility for Admission.pdf
- Law and Revenue responses to June 19 meeting, 28 June 2019.pdf
- CBR Investment History, Department of Revenue, 21 November 2018.pdf

Fourth Meeting – June 28, 2019

- Minutes HPFG2019 06 281007.pdf
- Alaska Permanent Fund Presentation for June 28, 2019, meeting.pdf
- Legislative Finance Presentation to Permanent Fund Working Group, 28 June 2019.pdf
- DOR Presentation to Permanent Fund Working Group, 28 June 2019.pdf
- Angela Rodell response to June 28 working group questions, 2 July 2019.pdf

Fifth Meeting – July 8, 2019

- Minutes HPFG2019 07 080904.pdf
- Surplus PFD Permanent Fund Working Group Assignment 8 July 2019.pdf
- $3,000 PFD Permanent Fund Working Group Assignment, 8 July 2019.pdf
- $1,600 PFD Permanent Fund Working Group Assignment 8 July 2019.pdf
- Appendix A ISER 2016 Economic Impacts.pdf
- Appendix B Berman 2018 Resource Rents Among Alaskas Indigenous Peoples.pdf
- Appendix C ISER 2017 Families Study Research Summary.pdf
- Appendix D ITEP 2017 Revenue Study.pdf
- Appendix E ISER 2019 Summary of PFD Effects Socio Economic Well Being.pdf
- Appendix F PFD Values Adjusted for Inflation 2018.pdf
- Appendix J Hammond Letter to House Finance Chair Al Adams April 1 1982.pdf
- Appendix K House Finance Chair Al Adams Committee Letter of Intent May 14 1982.pdf
- Appendix L Long term Projections Full Statutory PFD Current FY20 Budget.pdf
- Appendix M Long term Projections Full Statutory PFD $1.3 Billion Cut.pdf
- Appendix N Long term Projections 50% POMV PFD Current FY20 Budget.pdf
- Appendix O Long term Projections 50% POMV PFD $1.3 Billion Cut.pdf
- Appendix P Hammond 1980 PFD Application Statement to Alaskans.pdf
- Appendix Q Financials Current Budget 50 50 POMV PFD.pdf
- Appendix R Financials Current Budget Statutory PFD.pdf
- Appendix S Financials Right Sized Budget 50 50 POMV PFD.pdf
- Appendix T Financials Right Sized Budget Statutory PFD.pdf
- What do we know about the effects of the Alaska PFD Mouhcine Guettabi 20 May 2019.pdf

Sixth Meeting – October 7, 2019

- Permanent Fund Working Group Minutes, October 7, 2019
- Presentation - PF Earnings and the Budget, Models and Scenarios – 10/7/19
- Legislative Finance - Additional Scenarios – 10-7-19
- Legislative Finance Permanent Fund Dividend Interactive Model – Excel – 10/7/19