



SJR 6: Amending Constitution to Transition Permanent Fund to an Endowment

Mike Barnhill
Deputy Commissioner
(907) 465-3669
mike.barnhill@alaska.gov

SJR 6: Amends Article 9, section 15 of the Alaska Constitution

- SJR 6 amends article 9, section 15 of the Alaska Constitution:
 - Transitions Permanent Fund to an Endowment Structure
 - Goal of Endowment:
 - Invest the assets of the endowment, and spend from the endowment:
 - Sustainable forever
 - Fund the objectives of the endowment today and in the future
 - Elements of an endowment:
 - One account
 - Diversified investments with long-term investment horizon
 - Long-term capital appreciation
 - Distribution rule that balances spending with preserving inflation-adjusted value of the deposited funds
 - Preserves inter-generational equity



SJR 6: Brief History of Fund Structures – How We Got Here

- Historic Trusts – often had two account structure
 - Principal account and Income account
- Traditional trust spending rule
 - Save the principal; spend the income
 - Income = cash (stock dividends, fixed income coupons, real estate rents)
 - Realized capital gains retained in principal
- Problem with Historic Trust Structure
 - Assets weighted to fixed income to get cash that can be spent
 - Missed opportunity for capital growth
 - Late 1950s academics raised concerns that these portfolios were “inefficient”
 - Solution to inefficient principal and income trust structure: Endowment



SJR 6: Permanent Fund – Steady but Long Path to Endowment

- 1976-1980: PF created with the traditional principal and income account structure; fixed income investments; capital gains retained in principal
- 1980s: Legislature expands list of permissible investments; realized capital gains flow to income account, with inflation proofing back to principal
- 1980s – 1990s: Legislature continues to expand list of permissible investments
- 2005: Legislature abolishes legal list of investments; replaces with “prudent investor rule”
- 2018: SB 26 distribution rule (5% of lagging 5yr average market value can be spent)

- Each of these was an important step toward a modern endowment that is sustainable forever



SJR 6: Final Step to Make PF an Endowment

- SJR 6 transitions the PF to a modern endowment by establishing a one-account structure in the Alaska Constitution
- Why is this important?
 - With the current two account structure, there is a risk that the Earnings Reserve Account can be exhausted
 - If exhausted, the legislature may not appropriate from the principal account
 - So, no PFDs and no revenues for government spending
- A one account endowment structure + sustainable distribution rule
 - Permanent Fund is sustainable forever
 - No risk of abrupt inability to provide a distribution



SJR 6: Considerations for Distribution Rule

- Under SB 26 (2018) the distribution rule for the Permanent Fund is set at 5% of the lagging 5yr average market value
- SJR 6 provides the legislature the power to set and revise the distribution rule
- Distribution rules are intended to limit spending, while allowing the fund to grow to keep up with inflation
- Spend only the real return. Example:
 - Total return: 7%
 - Inflation: 2%
 - Real return: 5%
 - So, limit spending to 5%
- Should compare spending and real return regularly; consider comparisons over moderate to long time horizons



SJR 6: Considerations for Distribution Rule

- Distribution rules
 - Static. Fixed 5%
 - Dynamic. Floats based on inflation and market returns
 - Hybrid. “No more than” 5% (Public School Trust, HB 213 2018)
 - APFC Trustees discuss in Trustee Papers No. 9 (2020)
- All distribution rules are designed to meet the needs of the present while protecting the needs of the future
 - Guarantee inter-generational equity
- SB 53 implements SJR 6 with a 5% of lagging 5yr average market value distribution rule
 - Projected inflation expected to be 2%
 - Would require projected annual returns to be 7%
 - Should regularly compare experienced real return with spending, make adjustments to distribution rule as necessary to preserve the inflation-adjusted value of the PF



SJR 6: Allocation of the Distribution

- SJR 6 provides the legislature the power to allocate the PF distribution between PFD and government spending
- SB 53 implements this
 - 50/50 allocation between PFD and government spending
 - Fair compromise for Alaska
- SJR 6 requires a vote of the people for any change to the PFD allocation



SJR 6: Summary

- Protects Alaska's primary source of state general fund revenue
- Preserves long-term value of the fund by limiting annual draw
- Preserves the critical link between the people and their government by providing every Alaskan a share of the state's natural resource wealth
- Ensures that Alaskans have a voice in future decisions regarding the permanent fund
- Provides the Legislature with the flexibility to adjust the distribution rule to adjust to different market and economic environments

