THE STATE of ALASKA
GOVERNOR MIKE DUNLEAVY

Department of Revenue

COMMISSIONER'S OFFICE

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January 31, 2023

The Honorable Lyman Hoffman
Senate Finance Committee, Co-Chair
Alaska State Legislature
State Capitol, Room 518
Juneau, AK 99801

The Honorable Donald Olson
Senate Finance Committee, Co-Chair
Alaska State Legislature
State Capitol, Room 516
Juneau, AK 99801

The Honorable Bert Stedman
Senate Finance Committee, Co-Chair
Alaska State Legislature
State Capitol, Rooms 508
Juneau, AK 99801

Dear Co-Chairs Hoffman, Olson, and Stedman,

Thank you for providing us the opportunity to address some of the questions that were raised during the Department of Revenue's (DOR) presentation surrounding the savings reserves and investment funds to the Senate Finance Committee on January 23, 2023. Please find below the questions and corresponding responses.

1. **Provide historical information on the asset allocation and performance of the Power Cost Equalization fund and additional information to the Co-chairs to assist in evaluating the future investment of the fund.**

   As requested, Attachment 1 presents 5 years of quarterly target and actual asset allocations as well as quarterly performance compared to benchmarks. Average annual performance over the past 5 years ending was 2.43%, slightly ahead of the benchmark of 2.42%. The annual performance of the Power Cost equalization for the past 5 calendar years is as follows:

1 Year ending	PCE returns	Benchmark	Relative
12/31/2018	-5.63%	-5.63%	0.00%
12/31/2019	21.67%	21.71%	-0.03%
12/31/2020	7.76%	7.79%	-0.03%
12/31/2021	7.12%	7.35%	-0.23%
12/31/2022	-14.95%	-15.20%	0.24%
Cumulative 5 year	**2.43%**	**2.42%**	**0.01%**

Additionally, to assist in evaluating future investment of the fund, Treasury is preparing information for the Co-chairs on prospective return, risk, and the impact of downside return scenarios on spending using both 3-year smoothing and 5-year smoothing. Treasury just received updated 2023 capital market assumptions and it will take some additional time to incorporate them.

2. Did the restructuring of airport system debt extend the amortization period? What was this savings due to? Amortization changes, lower interest rates, or something else?

Bond refinancing or refunding are used by state and local governments to achieve debt service savings on outstanding bonds. In some cases, the refunding of bonds can also be issued to removed or bond covenants or to restructure debt service payments. In this case, through authorization from the State Bond Committee and the AIAS, in August 2021, AIAS issued $85.5 million of Series 2021 A, B, and C revenue refunding bonds, which in conjunction with the contribution of $40.0 million of cash and prior debt service funds on hand of the AIAS, defeased/refunded $154.4 million of par of then outstanding AIAS revenue bonds. The transaction resulted in an $81.8 million gross reduction in total scheduled debt service payments between FY2022 and FY2036 and net present value savings of approximately $24.9 million associated with the refunding portion. The transaction was structured to frontload maximum benefit of airline rate reductions over the first two years in order to provide immediate pandemic relief support to AIAS customers. The restructuring of outstanding debt of the airport system reduced future debt service payments from FY2022 through FY2036 without extending the amortization. Debt service savings from the restructuring were realized due to lower interest rates, and the cash contributions of the airport system.

3. Are there any GeFONSI funds that are having problems or are doing really well?

There are currently 185 funds that are invested within the GeFONSI funds. The Treasury manages the GeFONSI as one investment fund and each fund that is allowed to receive earnings by statute is assigned earnings on a daily basis. The Treasury does not, however, analyze how every individual fund within the GeFONSI is being used by agencies. Rather, it is the Division of Finance, the Office of Management and Budget and Legislative Finance that monitor balances to ensure that the funds are not over appropriated.

4. How many other funds have asset allocations like the Alaska Higher Education Investment fund?

There are five funds with the State's highest risk/return asset allocation, and they are the Power Cost Equalization Fund, The Public Schools Trust Fund, The Alaska Higher Education Investment Fund, the Education Endowment Investment Fund, and the Illinois Creek Mining Reclamation Fund. All five funds are invested in the same underlying asset class building blocks, but they are not commingled at the fund level and do not need to have the same asset allocation.

5. How exactly is a benchmark decided? Are we using the right ones?

Asset class benchmarks are selected to best represent the risk and return that could be produced by passively investing in each underlying asset class. The State used the following industry-standard benchmarks for each asset class:

Asset Class	Benchmark
Domestic Equity	Russell 3000 Equity Index
International Equity	MSCI All-Country World Index ex-US
REITs	NAREIT Equity Index
Core U.S. Fixed Income	Bloomberg US Aggregate Bond Index
Government 1-3 year Bonds	Bloomberg US Government 1-3 Year Index
Cash Equivalents	3-Month T-bill Index

The process for selecting these benchmarks was transparent and independent and ultimately the fund fiduciary went through a diligent process to make sure they were the right benchmarks. All of the benchmarks are subject to ongoing scrutiny by compliance, independent consultants, and investment advisors.

Fund benchmarks are calculated using a combination of the asset class benchmarks and each fund's asset class target weights over time. Performance measurement is the responsibility of Treasury's middle office/compliance group and is independent of the investment process.

6. Which funds have missed benchmarks?

All of the underlying asset classes outperformed for the 1-year ended 12/31/2022. This is not common and is the byproduct of a combination of investment skill and fortuitous cash flow timing. Both broad market fixed income and short-term fixed income had the highest outperformance and benefited from skillful active investment management by Treasury staff during a difficult market environment. Staff has a long history of adding value by actively managing these portfolios and expects to continue to do so moving forward.

The equity strategies are invested in index funds that are expected to closely track their respective benchmarks. However, cashflow timing can result in modest deviations from the benchmark over time that are outside Treasuries control. During 2022 these differences turned out to be positive, but this is not expected to repeat with frequency. As you can see in the following schedule, relative performance was positive for the 1-year period, but there were some negative deviations over other periods:

DOR Commissioner's Report: Net Pool Performance for Month Ending 12/31/2022

Pool Performance (Net of Fee)	1 Month	3 Month	FYTD	1 Year	3 Year	5 Year	7 Year	10 Year
Broad Market Fixed Income Pool	-0.57%	2.20%	-2.51%	-12.24%	-2.30%	0.30%	1.15%	1.24%
Domestic Equity*	-5.86%	7.21%	2.45%	-19.08%	7.08%	8.79%		
Intermediate-term Fixed Income Pool	0.17%	0.85%						
Internally Managed REITs	-4.94%	4.17%	-7.07%	-24.86%				
International Equity*	-0.74%	14.24%	2.89%	-15.92%	0.10%	1.03%		
Short-term Fixed Income Pool	0.43%	0.95%	1.50%	1.60%	0.83%	1.39%	1.27%	0.96%
Tactical Bond Pool	-0.48%	2.74%	-0.03%					
Benchmark Performance	**1 Month**	**3 Month**	**FYTD**	**1 Year**	**3 Year**	**5 Year**	**7 Year**	**10 Year**
Broad Market Fixed Income Pool	-0.45%	1.87%	-2.97%	-13.01%	-2.71%	0.02%	0.89%	1.06%
Domestic Equity*	-5.86%	7.18%	2.40%	-19.21%	7.07%	8.79%		
Intermediate-term Fixed Income Pool	0.18%	0.73%						
Internally Managed REITs	-4.97%	4.14%	-7.14%	-24.95%				
International Equity*	-0.75%	14.29%	2.96%	-16.00%	0.07%	0.88%		
Short-term Fixed Income Pool	0.36%	0.84%	1.31%	1.46%	0.72%	1.26%	1.07%	0.76%
Tactical Bond Pool	-0.45%	1.87%	-2.97%					
Relative Performance (Net of Fee)	**1 Month**	**3 Month**	**FYTD**	**1 Year**	**3 Year**	**5 Year**	**7 Year**	**10 Year**
Broad Market Fixed Income Pool	-0.12%	0.32%	0.46%	0.77%	0.42%	0.27%	0.26%	0.18%
Domestic Equity*	0.00%	0.03%	0.05%	0.13%	0.01%	0.00%		
Intermediate-term Fixed Income Pool	-0.01%	0.12%						
Internally Managed REITs	0.03%	0.03%	0.07%	0.09%				
International Equity*	0.01%	-0.05%	-0.07%	0.09%	0.03%	0.14%		
Short-term Fixed Income Pool	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	0.20%
Tactical Bond Pool	-0.03%	0.86%	2.94%					

At the fund level, GeFONSI II was the only fund that did not outperform since it had a higher level of initial cash due to cash transfers at the start of the fiscal year. All of the other funds benefitted from the outperformance of the underlying asset class building blocks discussed above. The breadth of this outperformance is uncommon. Treasury manages these portfolios with tight risk controls and material underperformance is not expected moving forward, but modest levels of both outperformance and underperformance due to cashflow timing is normal.

DOR Commissioner's Report: Net Plan Performance for Month Ending 12/31/2022

Relative Performance (Net of Fee)	1 Month	3 Month	FYTD	1 Year	3 Year	5 Year	7 Year	10 Year
2008 Transportation Project Government Bonds (AY2Q)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	0.20%
2013B Tax Exempt Education (AY3Z)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	
2016A - 2012 Transporation Bond Act (AY3Y)	0.07%	0.11%	0.19%	0.14%	0.08%	0.12%	0.19%	
2016B - 2012 Transportation Bond Act (AY3Q)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%		
Alaska Higher Education Investment (AY3L)	0.01%	0.12%	0.19%	0.26%	0.06%	0.04%	0.03%	
Alaska Mental Health Trust Reserve (AY2L)	0.00%	0.11%	0.24%	0.40%	0.30%	0.18%	0.17%	0.33%
ASLC Investment Fund (AY3S)	-0.03%	0.22%	0.51%	0.39%				
Constitutional Budget Reserve Fund (AY19)	0.07%	0.11%	0.19%	0.14%	0.15%	0.12%	0.20%	0.16%
Education Endowment Fund (AY3G)	0.01%	0.12%	0.19%	0.26%	0.06%			
EVOS Habitat Investment (AY2H)	0.02%	0.11%	0.62%	0.85%	0.34%	0.17%	0.17%	0.32%
EVOS Research Investment (AY02)	0.02%	0.11%	0.44%	0.58%	0.27%	0.13%	0.10%	0.28%
GeFONSI I (AY01)	0.06%	0.12%	0.18%	0.18%	0.10%	0.12%	0.17%	0.15%
GeFONSI II (AY3F)	0.05%	0.11%	0.00%	-0.01%	0.00%			
Illinois Creek Mine Reclamation (AY9J)	0.01%	0.12%	0.19%	0.26%	0.06%	0.02%	0.01%	0.11%
International Airports 2006 Non-AMT (AY9X)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	0.20%
International Airports Repair & Replacement Fund (AY05)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	0.20%
International Airports Revenue Fund (AY04)	0.06%	0.11%	0.16%	0.14%	0.11%	0.11%	0.20%	0.17%
International Airports Series 2002 Reserve Account (AY2E)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	0.20%
International Airports Series 2003 Reserve (AY2U)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	0.20%
Investment Loss Trust Fund (AY28)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	0.20%
PCE Endowment Fund (AY13)	0.01%	0.12%	0.19%	0.24%	0.01%	0.00%	0.02%	0.14%
Permanent Fund Dividend Holding Account (AY2G)	0.07%	0.11%	0.13%	0.08%	0.08%	0.15%	0.28%	0.24%
Public School Trust Fund (AY08)	0.00%	0.11%	0.18%	0.26%	0.07%	0.02%	0.03%	0.09%
RHIF LTC Insurance (AY11)	0.00%	0.13%	0.27%	0.32%	0.14%	0.07%	0.11%	0.16%
RHIF Major Medical (AY03)	0.07%	0.11%	0.19%	0.14%	0.10%	0.13%	0.20%	0.20%

7. Provide a copy of the Cash Deficiency MOU.

Cash in the State's General Fund is essential to ongoing day-to-day operations. Without cash in the fund, the State cannot pay its bills and the daily operations of the State come to a halt. The State's daily cash need can be as much as $200 million in a single day. For purposes of this operating plan, a cash deficiency situation exists any time the General Fund cash balance is projected to, or does, drop below $400 million and is expected to stay below $400 million for five days. In the 1990s, the Departments of Law, Revenue, Administration, and the Office of Management and Budget jointly developed a Cash Deficiency Operating Plan to accomplish this goal. This document is updated as needed. The most recent update is provided as Attachment 2.

8. Provide timing of the call for POMV disbursement.

The POMV amount and how it will be used to pay out dividends and support operations is known at the start of the fiscal year based on the budget, as approved by the legislature. For fiscal year 2023, $1.68 billion was transferred on 7/15/22 to pay dividends. The remaining $1.68 billion will be transferred to the general fund during the second half of the fiscal year and is somewhat dependent on when transfers from the general fund to the CBRF occur. For fiscal year 2024, the total POMV draw will be $3.52 billion. The Governor's budget reflects $2.47 billion to be used to pay dividends leaving $1.05 billion for operations. The timing of the transfer will again depend on cash projections as the new fiscal year approaches.

9. **The presentation mentioned 14 defined benefit funds. Could you let us know what these 14 funds are?**

The 14 defined benefit funds include the following:

Public Employees' Retirement System (PERS)

- Retirement Pension Trust
- Retirement Health Care Trust
- Occupational Death and Disability*
- Police and Fire Occupational Death and Disability*
- Retiree Medical Plan*
- Health Reimbursement Arrangement*

Teachers' Retirement System (TRS)

- Retirement Pension Trust
- Retirement Health Care Trust
- Occupational Death and Disability*
- Retiree Medical Plan*
- Health Reimbursement Arrangement*

Judicial Retirement System (JRS

- Retirement Pension Trust
- Retirement Health Care Trust

National Guard/Naval Militia Retirement System (MRS)

- Retirement Pension Trust

*Defined benefit component of the defined contribution plans

10. **Provide a break down the $1.37 billion balances on slide 13.**

The $1.37 billion as of June 30, 2022, represents the cash balance of $910 million in the Constitutional Budget Reserve Fund (CBRF) and $410 million in the Statutory Budget Reserve (SBR) fund. The accrued balances of these funds in the state's Annual Comprehensive Financial Report (ACFR) available for appropriation on June 30, 2022, are in the process of being audited. Based on discussions with the Division of Finance and Office of Management and Budget (OMB), the accrued balance of the CBRF as of June 30, 2022, is estimated to be $2.2 billion, resulting from transfers from the general fund to the CBRF for fund surpluses and sweep amounts. The SBR is expected to have an accrued balance of $370 million as of June 30, 2022.

11. Provide a minimum balance or minimum range for the Constitutional Budget Reserve Fund (CBRF).

This is an OMB policy and will be addressed accordingly in their response/presentation.

12. How would rating agencies view a $500 million CBRF balance?

The rating agencies view of the State's credit rating profile as very unique compared to other States within the U.S due to the State's economic concentration and dependance on a volatile oil and gas industry. That being said, rating agencies have viewed the State's rating outlook as stable/positive due to its financial standing (i.e. low debt profile, reduction in pension obligations and other post-employment benefits obligations including the State's sizeable constitution budget reserve).

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

Sincerely,

Adam Crum
Commissioner

Enclosures:
Attachment 1-PCE quarterly data
Attachment 2-Cash Deficiency Operating Plan

PCE Quarterly Data

	FY23		FY22				FY21			
Target	**QTR 2**	**QTR 1**	**QTR 4**	**QTR 3**	**QTR 2**	**QTR 1**	**QTR 4**	**QTR 3**	**QTR 2**	**QTR 1**
Cash & Cash Equivalents	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%
Core US Fixed Income	30.00%	30.00%	43.00%	43.00%	43.00%	43.00%	60.00%	60.00%	60.00%	60.00%
High Yield Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Broad Domestic Equity	39.00%	39.00%	32.00%	32.00%	32.00%	32.00%	24.00%	24.00%	24.00%	24.00%
Global Equity	25.00%	25.00%	20.00%	20.00%	20.00%	20.00%	15.00%	15.00%	15.00%	15.00%
REITs	5.00%	5.00%	4.00%	4.00%	4.00%	4.00%	0.00%	0.00%	0.00%	0.00%
	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Change in Target										
Cash & Cash Equivalents	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	1.00%
Core US Fixed Income	0.00%	-13.00%	0.00%	0.00%	0.00%	-17.00%	0.00%	0.00%	0.00%	28.00%
High Yield Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Broad Domestic Equity	0.00%	7.00%	0.00%	0.00%	0.00%	8.00%	0.00%	0.00%	0.00%	-17.00%
Global Equity	0.00%	5.00%	0.00%	0.00%	0.00%	5.00%	0.00%	0.00%	0.00%	-12.00%
REITs	0.00%	1.00%	0.00%	0.00%	0.00%	4.00%	0.00%	0.00%	0.00%	0.00%
Actual										
Cash & Cash Equivalents	1.36%	0.47%	1.03%	1.80%	0.93%	0.93%	0.86%	1.22%	0.63%	0.93%
Core US Fixed Income	28.70%	30.45%	45.55%	42.34%	41.34%	43.36%	59.97%	59.23%	60.11%	60.63%
High Yield Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Broad Domestic Equity	38.48%	40.08%	29.91%	31.72%	33.67%	32.17%	24.38%	24.71%	24.09%	23.68%
Global Equity	26.67%	24.22%	19.63%	20.10%	19.59%	19.47%	14.80%	14.84%	15.17%	14.76%
REITs	4.80%	4.78%	3.88%	4.04%	4.47%	4.08%	0.00%	0.00%	0.00%	0.00%
	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Relative (Actual - Target)										
Cash & Cash Equivalents	0.36%	-0.53%	0.03%	0.80%	-0.07%	-0.07%	-0.14%	0.22%	-0.37%	-0.07%
Core US Fixed Income	-1.30%	0.45%	2.55%	-0.66%	-1.66%	0.36%	-0.03%	-0.77%	0.11%	0.63%
High Yield Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Broad Domestic Equity	-0.52%	1.08%	-2.09%	-0.28%	1.67%	0.17%	0.38%	0.71%	0.09%	-0.32%
Global Equity	1.67%	-0.78%	-0.37%	0.10%	-0.41%	-0.53%	-0.20%	-0.16%	0.17%	-0.24%
REITs	-0.20%	-0.22%	-0.12%	0.04%	0.47%	0.08%	0.00%	0.00%	0.00%	0.00%
Quarterly Returns										
Total Plan Return	7.27%	-6.11%	-10.79%	-5.34%	3.91%	-0.68%	3.96%	-0.15%	6.44%	3.57%
Benchmark Return	7.15%	-6.18%	-10.69%	-5.54%	3.98%	-0.60%	3.89%	-0.02%	6.42%	3.54%
Relative Return	0.12%	0.07%	-0.10%	0.20%	-0.08%	-0.09%	0.07%	-0.12%	0.02%	0.03%

PCE Quarterly Data

	FY20				FY19				FY18			
Target	**QTR 4**	**QTR 3**	**QTR 2**	**QTR 1**	**QTR 4**	**QTR 3**	**QTR 2**	**QTR 1**	**QTR 4**	**QTR 3**	**QTR 2**	**QTR 1**
Cash & Cash Equivalents	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Core US Fixed Income	32.00%	32.00%	32.00%	32.00%	31.00%	31.00%	31.00%	31.00%	28.00%	28.00%	28.00%	28.00%
High Yield Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	5.00%	5.00%	5.00%	5.00%
Broad Domestic Equity	41.00%	41.00%	41.00%	41.00%	40.00%	40.00%	40.00%	40.00%	38.00%	38.00%	38.00%	38.00%
Global Equity	27.00%	27.00%	27.00%	27.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%
REITs	0.00%	0.00%	0.00%	0.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Change in Target												
Cash & Cash Equivalents	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	N/A
Core US Fixed Income	0.00%	0.00%	0.00%	1.00%	0.00%	0.00%	0.00%	3.00%	0.00%	0.00%	0.00%	N/A
High Yield Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	-5.00%	0.00%	0.00%	0.00%	N/A
Broad Domestic Equity	0.00%	0.00%	0.00%	1.00%	0.00%	0.00%	0.00%	2.00%	0.00%	0.00%	0.00%	N/A
Global Equity	0.00%	0.00%	0.00%	3.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	N/A
REITs	0.00%	0.00%	0.00%	-5.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	N/A
Actual												
Cash & Cash Equivalents	0.00%	0.17%	0.12%	0.15%	0.00%	0.08%	0.01%	0.00%	0.00%	0.00%	0.00%	0.00%
Core US Fixed Income	35.86%	31.89%	31.25%	31.60%	30.75%	30.91%	32.32%	30.71%	28.03%	29.39%	27.36%	27.98%
High Yield Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	4.17%	4.52%	4.70%	4.64%
Broad Domestic Equity	41.12%	41.11%	41.27%	41.00%	40.11%	39.95%	38.97%	39.91%	39.20%	37.07%	37.92%	37.94%
Global Equity	23.02%	26.83%	27.36%	27.25%	24.32%	23.88%	23.87%	24.47%	23.17%	24.00%	24.73%	24.28%
REITs	0.00%	0.00%	0.00%	0.00%	4.82%	5.18%	4.83%	4.91%	5.42%	5.02%	5.28%	5.16%
	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Relative (Actual - Target)												
Cash & Cash Equivalents	0.00%	0.17%	0.12%	0.15%	0.00%	0.08%	0.01%	0.00%	0.00%	0.00%	0.00%	0.00%
Core US Fixed Income	3.86%	-0.11%	-0.75%	-0.40%	-0.25%	-0.09%	1.32%	-0.29%	0.03%	1.39%	-0.64%	-0.02%
High Yield Bonds	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	-0.83%	-0.48%	-0.30%	-0.36%
Broad Domestic Equity	0.12%	0.11%	0.27%	0.00%	0.11%	-0.05%	-1.03%	-0.09%	1.20%	-0.93%	-0.08%	-0.06%
Global Equity	-3.98%	-0.17%	0.36%	0.25%	0.32%	-0.12%	-0.13%	0.47%	-0.83%	0.00%	0.73%	0.28%
REITs	0.00%	0.00%	0.00%	0.00%	-0.18%	0.18%	-0.17%	-0.09%	0.42%	0.02%	0.28%	0.16%
Quarterly Returns												
Total Plan Return	14.32%	-14.49%	6.09%	0.90%	3.57%	9.74%	-8.40%	3.03%	1.17%	-1.17%	3.87%	3.54%
Benchmark Return	14.16%	-14.30%	6.15%	0.84%	3.52%	9.83%	-8.35%	3.05%	1.21%	-1.27%	3.85%	3.61%
Relative Return	0.16%	-0.19%	-0.06%	0.06%	0.06%	-0.09%	-0.04%	-0.02%	-0.04%	0.10%	0.02%	-0.07%

MEMORANDUM OF UNDERSTANDING
Between the
DEPARTMENT OF ADMINISTRATION,
the
DEPARTMENT OF REVENUE,
the
OFFICE OF MANAGEMENT AND BUDGET,
and the
ATTORNEY GENERAL

WHEREAS the Department of Administration, the Department of Revenue, the Office of Management and Budget, and the Attorney General agree that the State needs a Cash Deficiency Operating Plan and agree that:

1. The State of Alaska's Cash Deficiency Operating Plan is this plan, dated December 1, 2017;

2. Each party will assist the others in providing information necessary to carry out the plan;

3. The Department of Administration, the Department of Revenue, the Office of Management and Budget, and the Alaska Attorney General endorse the plan and agree to operate by the plan.

This agreement takes effect December 1, 2017.

Leslie Ridle

Leslie Ridle, Commissioner
Department of Administration

11-20-17
Date

Sheldon Fisher, Commissioner
Department of Revenue

11/14/17
Date

Pat Pitney, Director
Office of Management and Budget

Nov. 14, 2017
Date

Jahna Lindemuth, Attorney General
Department of Law

11/21/17
Date

STATE OF ALASKA
CASH DEFICIENCY OPERATING PLAN
DECEMBER 2017

Executive Summary

The State recognizes that cash deficiencies commonly occur and that a plan is necessary to ensure state government continues to operate in these situations. Cash in the state's general fund is essential to support ongoing day-to-day operations of state government. Without cash in the fund, the state cannot pay its bills and the daily operations of the state come to a halt. The state's daily cash need can exceed $200 million. For purposes of this operating plan, a cash deficiency situation exists any time the general fund cash balance is projected to, or actually does, drop below $400 million and is expected to stay below $400 million for five business days. Past experience demonstrates that cash deficiencies occur, even in years with a balanced budget, and that a mechanism must be in place for the state to borrow in the event that a cash deficiency has been identified.

For 17 of the past 25 years, the general fund has needed to borrow funds from the Statutory Budget Reserve Fund (SBRF) or the Constitutional Budget Reserve Fund (CBRF) to meet its daily obligations for disbursements. Even in years of surplus, the difference between receipts flowing in and disbursements flowing out of the state general fund causes periodic cash deficiencies and annual budget gaps. The general fund's cash requirements routinely exceed its balance at points throughout each fiscal year, especially early in the fiscal year. The reasons for this include a disparity in timing between revenues received and funds disbursed, fluctuating oil prices, falling oil production, and an increase in designated subfunds within the general fund. The state has developed methods of identifying potential deficiencies and drawing upon financial reserves to compensate for them. The state created this plan to document the methods used when cash deficiencies first began to occur between FY1992 and FY1994. The agencies involved decided to revise the plan in FY2000, and again in FY2004, FY2007, FY2011, FY2014 and FY2018 to recognize that the state's fiscal situation and methods of identifying potential deficiencies have evolved over time, and to accommodate changes in administration as the signatories of this plan leave state service.

The Departments of Law, Revenue, Administration, and the Office of Management and Budget have jointly developed and updated this Cash Deficiency Operating Plan to accomplish this goal. This plan outlines how the state identifies when a cash deficiency is likely to occur and the steps taken to resolve that deficiency. Treasury makes projections of cash flow patterns for each fiscal year that will identify potential deficiencies. Steps to resolve deficiencies are detailed in a hierarchical list, including accessing funds from legislatively authorized sources, such as the SBRF, CBRF, ERA, subfunds of the general fund, and other temporary funding mechanisms. The plan also sets out a procedure for seeking legislative relief if all borrowing sources are exhausted, and discusses the differences between funding for cash flow and funding for budgetary needs.

Background and History

From the beginning of statehood through the completion of the Trans-Alaska Pipeline in 1977, oil comprised a relatively small proportion of state revenues – averaging just 30 percent of total general fund revenue. Once North Slope oil production began, sizable sums began flowing into the state treasury and state dependence on oil revenues increased to approximately 85 percent. Notwithstanding these increased revenues, the state still required intra-year borrowing to meet cash flow obligations – even in years of surplus. The main reason for this is that the timing of cash outflows do not match the timing of general fund receipts. Many large cash expenditures, such as funding retirement plans, are made early in the fiscal year while general fund revenues are collected at a more consistent rate throughout the year. Simply put, the state's annual revenue does not all appear on the first day of the fiscal year. Generally, cash expenditures in the first quarter of any fiscal year will exceed the cash receipts for that quarter – creating cash deficiency situations.

It is also important to note the difference between cash-flow borrowing and deficit borrowing. Deficit borrowing is simply the annual difference between revenues and expenditures – transfers are made from the SBRF or CBRF to fill this gap and carry over beyond fiscal year borders. Cash-flow borrowing is the amount required to ensure that the general fund has a sufficient balance to meet obligations and must be repaid by the end of each fiscal year. It has been determined, through cash-management analysis, that a minimum of $400 million in working capital is required at any given point in time to avoid a cash-flow deficiency.

By necessity, state government must borrow in order to operate without interruption. Cash-flow borrowing, traditionally from the CBRF and SBRF, allows the state to avoid more costly cash management tools such as issuing revenue anticipation notes, which carry interest rate payments, and borrowing from higher earning investment funds such as the ERA or other general fund subfunds. However, the balances of the SBRF and the CBRF have fallen from FY2013 highs of $16.3 billion and could be exhausted by late FY2019. In light of these challenges, the plan reflects revised procedures to contend with cash-deficiencies absent the ability to borrow from the SBRF and CBRF.

Additionally, redirection of revenues from the general fund to other funds has occurred gradually since the 1990s, increasing the frequency of cash-deficiency situations. Prior to 1990, most unrestricted revenues flowed directly into the general fund where they were available to pay for the day-to-day costs of operating state government. Over time, the legislature has established many subfunds of the general fund, listed in Appendix B, which are designated for specific purposes (although most are still subject to annual appropriation). In 1990, a popular vote amended the state constitution to establish the CBRF for deposit of oil tax settlements, funds that had historically been destined for the general fund.

The legislature has historically addressed both the cash deficiencies and the budget shortfalls by including in the language section of the appropriation act(s) authority for the executive branch to either take cash from the SBRF or borrow cash from the CBRF . This appropriation language is necessary to avoid some of the extreme consequences of implementing cash deficiency procedures 5, 6, 7, or 8 listed in Appendix A.

Legislative Benchmarks

Legislative policy surrounding borrowing has also evolved over the years. Outlined below is a list of various legislative mandates surrounding borrowing from the CBRF.

- In FY1999 the legislature placed a cap on the total amount of cash-flow and deficit borrowing that could occur. This created an artificial crisis and led to the cap being lifted shortly thereafter.
- Through FY2004, appropriations allowing CBRF borrowing were made without a cap but language was included in budget legislation to allow the general fund to repay the CBR interest equal to investment gains lost as a result of borrowing.
- In FY2004 the CBRF was accessible with a simple majority vote due to a provision in the constitution (Article IX, Sec. 17(b)), which allow funds to be drawn more easily as a crisis looms (when the amount available for appropriation falls below the amount appropriated in the previous fiscal year). But under this subsection, the amount available for borrowing is also limited to the difference between the amount appropriated for the previous fiscal year (excluding supplementals) and the amount available to appropriate in the current fiscal year, an amount that cannot be known until the fiscal year ends.
- In FY2006 this interest provision was stripped from the bill, but fortunately FY2006 through FY2010 were balanced budget years, so the state did not have to resort to one of the options outlined in this document.
- This interest appropriation was restored in FY2011 but again stripped out of the bill in FY2013 and subsequent years. The FY2013 bill did however include clarifying language that borrowing could occur either for cash-flow borrowing purposes or for deficit borrowing.
- Since FY2016, deficit borrowing has been made from the CBRF, authorized with a three-fourth vote as set out in Art. IX Sec. 17(c) of the Alaska Constitution:

> *"An appropriation from the budget reserve fund may be made for any public purpose upon affirmative vote of three-fourths of the members of each house of the legislature."*

Review Requirements

The previous iteration of the plan, dated July 2014, directs the signatories of the plan to reevaluate the plan when cash flow needs for the next two years exceed the CBRF balance. After five consecutive years of budget gaps, the CBRF balance is projected to be depleted in late FY2019. Moreover, over time, the parties that executed this agreement had changed and legislative authority and economic conditions change every year. For this reason, it was determined that an updated agreement should be signed to reflect cash-deficiency tools necessary to operate in the current environment and potentially absent available balances in the CBRF and SBRF.

Plan Overview and Initiation Criteria

In order to continue operating on a daily basis, the state must be able to reliably predict when a cash flow deficiency will occur and must have a planned response to manage the deficiency. This plan includes both the procedures used to project future cash balances and a response plan for resolving cash flow deficiencies.

The Cash Deficiency Operating Plan begins with a series of daily operations in both the Departments of Revenue and Administration. Depending on daily conditions, the plan evolves into a series of strategic steps designed to ensure the availability of adequate cash balances to meet day-to-day expenses. Conditions at the time will trigger the course of action to meet the identified cash problem.

Both the Departments of Revenue and Administration have improved their procedures for monitoring daily general fund cash balances and developed reliable cash flow projections. Using an internally developed model, the Department of Revenue produces revised cash balance projections monthly, and compares them to actual balances on a daily basis. The model can be used to quickly develop new cash projections if major changes occur in any of the key components of the projection model including oil prices and production receipts.

Execution of the plan is dependent on the availability of a broad range of information relating directly to the flow of cash in and out of the state's general fund. Critical elements include:

- oil prices - current and projected
- production levels - current and projected
- oil receipts - taxes and royalties
- other receipts
- historical spending patterns
- projected cash balances
- legislative limits on borrowing from CBRF and other funds

Several procedures make up this plan, some of which are executed on a regular basis while others may, or may not, ever be executed. Appendix A provides a list of each of these procedures and the action that triggers their execution.

APPENDIX A

CASH DEFICIENCY PROCEDURES

PROCEDURE l: Develop monthly cash projections

PROCEDURE 2: Monitor daily general fund cash balances

PROCEDURE 3: Determine specific course of action to address deficiency

PROCEDURE 4: Execute appropriated transfers from the SBRF, CBRF, ERA or other funds to the general fund

PROCEDURE 5: Execute procedure to authorize temporary interfund borrowing

PROCEDURE 6: Execute other transfers from within the general fund group (subfunds) to the general fund or elect to borrow short term funds from financial institutions

PROCEDURE 7: Seek legislative action

PROCEDURE 8: Prioritize disbursements and restrict expenditures of the state because borrowing is unavailable

PROCEDURE 9: Reevaluate Cash Deficiency Operating Plan when cash flow needs for the next two years exceed the CBRF and SBRF and ERA balances

CASH DEFICIENCY PROCEDURES
DETAIL

PROCEDURE l: Develop monthly cash projections

The Department of Revenue executes the cash projection model, which calculates revised general fund cash projections for the next 12 months based on the current set of variables. The Department of Revenue reviews the new projections and predicts if and when the cash balance will drop below the $400 million threshold level for cash deficiencies. The updated projections are posted online.

PROCEDURE 2: Monitor daily general fund cash balances

Both the Departments of Revenue and Administration retrieve daily cash balances from IRIS to evaluate for adequate available cash. Cash Management posts daily balances to projection model and posts online.

PROCEDURE 3: Determine specific course of action to address deficiency

If the general fund cash balance is projected to be less than $400 million, and revenues are not projected to bring the balance above this mark within five business days, or disbursements are anticipated to deplete the cash balance, a cash deficiency situation has been identified. At this point, a decision will be made by the Cash Manager and the Accounting Services Supervisor to execute an appropriate funding procedure. Treasury will update the cash flow projection model to reflect that action.

PROCEDURE 4: Execute appropriated transfers from the SBRF, CBRF, ERA or other funds to the general fund

If a deficiency is identified by the Cash Manager and Accounting Service Supervisor, unless specific guidance is provided, appropriated transfers will be performed in the following order:

1. Transfer from SBRF
2. Transfer from CBRF
3. Transfer from ERA
4. Transfer from other funds

The Cash Manager and Accounting Service Supervisor will determine a funding amount necessary to avoid a deficiency. They will review appropriated transfers that have been made to date from authorized sources and identify amounts that may still be transferred. The Cash Manager will work with the Portfolio section of Treasury Division to determine the best day to perform a cash transfer to minimize investment losses, and coordinate with the Accounting Service Supervisor for Department of Administration to perform the transfers on this date.

If the CBR and SBR are depleted, or if legislation authorizes an appropriation from the ERA as the first source of transfer, Cash management may borrow from the ERA, to meet short-term cash deficiencies – similar to prior year CBR borrowing. If an appropriation exists for the ERA, the Cash Manager shall provide the Permanent Fund Corporation with an anticipated transfer schedule, approved by the Chief Accountant and Financial Officer, for their planning purposes, before any borrowing from the ERA may occur.

Additionally, Treasury and Division of Finance may elect instead to borrow from the SBRF or CBRF, in order to minimize investment losses or provide the Permanent Fund Corporation with additional planning time. These funds shall be replenished, with interest, by the end of the fiscal year when the appropriated ERA transfer is finally made. The Cash Manager and Accounting Services Supervisor will work with the Permanent Fund Corporation to determine the best day to perform a cash transfer to minimize investment losses.

PROCEDURE 5: Execute procedure to authorize temporary interfund borrowing

The state may need to borrow additional funds from the other available funds. Such borrowing can only occur if the signatories of the plan certify that anticipated receipts are sufficient to pay the debt, with interest, before the end of the current fiscal year. If anticipated receipts are certified sufficient, the borrowing may occur. If the Commissioners of Revenue and Administration, the Attorney General, and the Director of the Office of Management and Budget have certified that there will be sufficient money in the general fund to repay the amount borrowed, including interest, by the end of the fiscal year, Department of Administration will execute the interfund borrowing as directed.

PROCEDURE 6: Execute other transfers from within the general fund group (subfunds) to the general fund or elect to borrow short term funds from financial institutions

In implementing this procedure, Department of Administration will analyze the balances in all subfunds of the general fund as identified in Appendix B and determine possible sources for transfer excluding mental health trust funds and any funds containing bond proceeds. This list will be reviewed and approved by the Chief Accountant and Financial Officer and the Director of OMB.

Absent appropriated or available balances in the CBR or SBR or other funds, Treasury may borrow from financial institutions. Because borrowing from the general fund group (subfunds) carries the opportunity cost of lost investment earnings and due to the administrative burden of identifying available general fund balances, Treasury may instead elect to borrow short-term funds such as revenue anticipation notes from a financial institution. If this election is made, Treasury will notify the signatories of the MOU, and the Departments of Administration and Revenue will perform the necessary transactions.

PROCEDURE 7: Seek legislative action

If a cash deficiency is projected and the state has already executed all appropriated, internal and other borrowing procedures, it will be necessary to seek legislative relief to correct the cash deficiency problem. All signatories of the plan will present current cash position, forecasted cash position, cash deficiency plan, and recommendation to the Governor for approval. The Governor may act on the recommendation of all signatories of the plan by submitting a proposal for correcting the problem to the legislature and request action in either the current legislative session, the upcoming session or in special session.

PROCEDURE 8: Prioritize disbursements and restrict expenditures of the state because borrowing is unavailable

When all sources of appropriated and temporary borrowing are exhausted, the signatories of this plan need to prioritize disbursements and restrict expenditures of the state subject to available cash by prioritizing payments to vendors, grantees, municipalities, and employees. The Chief Accountant and Financial Officer will lead this effort, but all plan signatories will evaluate disbursement activity and identify expenditures to restrict until cash sufficiency is restored. The Chief Accountant and Financial Officer is responsible for working with affected agencies and ensuring the accounting system has controls in place to implement the prioritization plan.

PROCEDURE 9: Reevaluate Cash Deficiency Operating Plan when cash flow needs for the next two years exceed the CBRF and SBRF and ERA balances

The signatories to this agreement will consider additional steps when the SBRF, CBRF and ERA balances fall below estimated borrowing and cash flow needs for two fiscal years. At that time, the Office of Management and Budget will coordinate a meeting of the plan signatories to reevaluate the Cash Deficiency Operating Plan. The plan signatories will make recommendations to the Governor to address this cash flow problem.

APPENDIX B
GENERAL FUND SUBFUND BORROWING

Fund Description	Authority	IRIS Fund #
Abandoned Vehicle Fund*	AS 28.11.110	3223
Adak Airport Operations Fund	PL 101-510	1190
Alaska Capital Income Fund *	AS 37.05.565(a)	1197
Alaska Children's Trust	AS 37.14.200	3231
Alaska Comprehencive Health Insurance Fund	AS 21.55.430	1248
Alaska Debt Retirement*	AS 37.15.011	1044
Alaska Gasline Inducement Act Reimbursement Fund	AS 43.90.400	3218
Alaska Higher Education Investment Fund	AS 37.14.750	1226
Alaska Historical Commission Receipts Account *	AS 41.35.380	3205
Alaska Marine Highway System	AS 19.65.060	3224/3225
Alaska Marine Highway System Vessel Replacement *	AS 37.05.550	1082
Alaska Senior Care Fund (former Senior Care Fund) *	AS 47.450.360; SLA 2005, CH89 (HB106)	1189
Alaska Surplus Property	AS 37.05.500(a)(2) and 44.68.130	1033
Alaska Technical and Vocational Education Program Account*	AS 23.15.830	1151
Alaska Transportation Infrastructure Bank	Section 350 of the NHSD Act of 1995 Federal Law	3227/3229
Alaska Veterans' Memorial Endowment	AS 37.14.700(a)	1181
Alcohol and Other Drug Abuse Treatment and Prevention Fund*	AS 43.60.050	1013
Anatomical Gift Awareness Fund	AS 13.50.160(a)	1202
Art in Public Places	AS 44.27.060	1145
Assistive Technology Loan Guarantee	AS 23.15.125	3213
Building Safety Account*	AS 44.31.025	1172
Civil Legal Services Fund*	AS 37.05.590	1221
Commercial Passenger Vessel Environmental Compliance*	AS 46.03.482	1166
Commercial Vessel Passenger Tax Account	AS 43.52.230(a)	1206
Community Assistance Fund	AS 29.60.850	3220
Correctional Industries*	AS 33.32.020	1059
Crime Victims Compensation Fund*	AS 18.67.162	1220
Disaster Relief	AS 26.23.300	1116
Donated Commodity Fee	USC 7 CFR, Part 250	1014
Educational Facilities Maintenance and Construction *	AS 37.05.560	1083
Election Fund	Federal H.R. 3295	1185
Employment Assistance & Training Program Account *	AS 23.15.625	1054
Exxon Valdez Oil Spill Unincorporated Rural Community Grant	AS 44.33.115 (prior to 7/1/99 AS 44.47.051)	3386
FHWA - Airspace Leases	Section 156 of the USSTURAA of 1987	3207
FICA Administration	AS 39.30.050	1023
Fisheries Disaster Fund	PL 108-7, Sec 2, Division N, Title V, Fisheries	3216
Fuel Emergency	AS 26.23.400	3206
Fund for the Improvement of School Performance	AS 14.03.125	3210
General Fund*	State operating fund	1004
Large Passenger Gambling Tax Fund*	AS 43.35.210-220	1211

Fund Description	Authority	IRIS Fund #
Major Maintenance Grant	AS 14.11.007	1193
Memorial Education Revolving Loan Fund	AS 14.43.255	3226
Mental Health Trust Income Account*	AS 34.14.011	3230
Municipal Capital Project Matching Grant*	AS 37.06.010	1087
Municipal Harbor Facility Grant Fund	AS 29.60.800(a)	3217
NTSC Bonds Funding		1167
Oil & Gas Tax Credit Fund	AS 43.55.028	3219
Oil and Hazardous Substance Release Prevention Account*	AS 46.08.010(1)	3389
Oil and Hazardous Substance Release Prevention Mitigation	AS 46.08.020(b)	3388
Oil and Hazardous Substance Release Response Account	AS 46.08.010(2)	3388
Oil and Hazardous Substance Release Response Mitigation	AS 46.08.025(b)	3388
Originator Surety Fund*	AS 06.60.500	3221
Permanent Fund Dividend	AS 43.23.045	1050
Public Education Fund	AS 14.17.300	3201
Railbelt Energy*	AS 37.05.520	1012
Randolph - Sheppard Small Business	AS 23.15.130 and 20 USC 107-107(f)	1117
Real Estate Surety	AS 08.88.450	1040
Regional Cruise Ship Impact Fund	AS 43.52.230(c)	1207
Regional Educational Attendance Area School Fund	AS 14.11.030	1222
School Construction Grant	AS 14.11.005	1080
School Trust Land Sales	Attorney General Opinion	3215
State Insurance Catastrophe Reserve	AS 37.05.289	3209
State Land Disposal Income*	AS 38.04.022	1153
State Land Reforestation*	AS 41.17.300	1019
Statutory Budget Reserve Fund *	AS 37.05.540	3200
Storage Tank Assistance	AS 46.03.410	
TAPS Rebate	Federal Public Law 101-380	
Tobacco Use Education and Cessation Account*	AS 37.05.580	1168
Training and Building	AS 23.20.130(d)	1049
Trauma Care Fund*	AS 18.08.085	3222
Unincorporated Community Capital Project Matching Grant*	AS 37.06.020	1088
Vaccine Assessment Account	AS 18.09.230	1238
Vocational Rehabilitation Small Business Enterprise Revolving*	AS 23.15.130	
Workers' Compensation Benefits Guaranty Fund*	AS 23.30.082	1203
Workers' Safety and Compensation Administration Account*	AS 23.05.067	1157

* A subfund which has been identified as general fund available for appropriation and will be the first subfunds from which borrowing would occur. Within this category, the amount available to borrow will be determined based on several factors, including fund sufficiency balance, existing appropriations, federal statutes, other restrictions that may have been placed on the funds, and anticipated expenditure and revenue flows. All other funds would be considered the second priority to draw from and would fall under the same evaluation described above.

GLOSSARY OF TERMS

IRIS	Integrated Resource Alaska Statewide Accounting System
AS	Alaska Statute
Cash Deficiency	The General Fund sufficiency balance has dropped below $400 million
CBRF	Constitutional Budget Reserve Fund
Disbursements	A decrease in the State's current financial resources due to warrant or nonwarrant disbursal
Expenditures	Disbursements reported on a modified accrual basis
Fund	A fiscal and accounting entity with a self-balancing set of accounts used to manage the income and outflow of the State's financial resources
ERA	Earnings Reserve Account – realized earnings of the Permanent Fund (spendable portion)
Fund Sufficiency Balance	A measure of a fund's ability to pay for disbursements, calculated as cash held by the fund less any warrants outstanding
General Fund	The State's primary operating fund that is used to account for all of the State's financial resources except for those accounted for in a special purpose fund
Receipts	An increase in the State's current financial resources due to receipt of cash
Revenues	Receipts reported on a modified accrual basis
SBRF	Statutory Budget Reserve Fund
USC	United States Code
Warrants purchase	Warrants that have been issued, but not yet presented to the State for Outstanding