Senate Bill 107

Percent of Market Value Split / Permanent Fund Dividend

Senate Finance Committee
March 21, 2023

What Does SB107 Do?

Establishes a split for the annual "Percent of Market Value" draw

- The split would be 75% for the General Fund, and 25% to pay Permanent Fund Dividends

When SB26 passed in 2018, establishing the POMV formula for using Permanent Fund earnings, the bill did not update the 1980s dividend formula. SB107 would replace that formula.

The Senate Finance Committee has addressed this topic several times:

- The version of SB26 that passed the Senate in 2017 included a "75/25" split. The split was removed by the bill's Conference Committee.
- SB103, from 2019, included a "50/50" split
- SB199, from 2022, included a "75/25" split
- SB53, from 2022, included a smaller dividend that increased to a "50/50" split once a certain amount of new revenue was received

Why is this necessary?

- The Permanent Fund was initially set aside for when oil would no longer be able to cover all budgetary needs.
- Not having a PFD formula creates uncertainty in the budgeting process.
  - The POMV was passed in part to stabilize the state's revenue.
  - If the dividend amount is unknown until late in session, the remaining POMV draw going to the General Fund is also unknown.
  - Without knowing how much revenue is available, it is difficult to make budget decisions.

Why is this necessary? *(continued)*

- A PFD based on a percentage of the POMV adds stability to both the budget and the dividend
  - The POMV is based on the <u>overall value</u> of the Permanent Fund, which is relatively stable and predictable.
  - In contrast, the current statutory dividend formula is based on Permanent Fund <u>earnings</u>, which are much more volatile.
  - If the general fund portion of the annual POMV payout is "whatever is left" after funding a volatile dividend, all that revenue volatility is transferred to the general fund- compounding fiscal uncertainty.

Why 75 / 25?

It is fiscally prudent

This table is from OMB on February 20th

- Next year's "Governor's amended" budget is $433 million in deficit.
- That's before:
  - Fixing Community Assistance
  - Basic deferred maintenance
  - Any legislative additions to the capital budget
  - Any adjustment to education funding
  - Any bills that pass with fiscal notes
- There are no available savings pools to draw from. A CBRF draw requires a supermajority vote which hasn't occurred since 2020

Uses Of Funds	UGF	FY2024 Total
Expenditures:		
Total Operating	**4,592.0**	**9,424.8**
Total Capital	**303.6**	**2,569.1**
Supplementals and RPLs	**-**	**-**
Subtotal - Expenditures	**4,895.6**	**11,994.0**
ERA Draw Used For PFD	2,470.9	2,470.9
K-12 Forward Funding Deposit	-	-
Total Uses of Funds	**7,366.5**	**14,464.9**

Sources Of Funds	UGF	FY2024 Total
Unrestricted Revenue	3,410.1	3,410.1
POMV ERA Draw	3,526.1	3,526.1
Restricted Revenue	-	7,098.4
Draws, Deposits, and Adjustments	(3.2)	(3.2)
Total Sources of Funds	**6,933.0**	**14,031.4**
Surplus/(Deficit) To/From Reserves	**(433.5)**	**(433.5)**

Other Unmet Budget Needs

Slide is from Legislative Finance on February 7th

It details over $13 billion in current state obligations

To summarize:

- Pension obligations $7.1b
- Capital and maintenance needs $4.4b
- Debt service $1.6b

Obligations and Funding Needs of the State of Alaska

- This is not an exhaustive list. The total for these items is about **$13.1 billion**
- PERS/TRS Unfunded Liability: **$7.1 billion**
  - Payment plan: annual payments though FY39. FY24 payment is $140.3 million
- General Obligation Bonds and State Supported Debt: **$1.1 billion**
  - Payment plan: annual payments through FY41. FY24 Governor's Budget includes $90.9 million UGF
- State Share of Municipal School Debt Service: **$457.0 million**
  - Payment plan: annual payments through FY39. FY24 Governor's Budget includes $67.2 million GF
- Oil and Gas Tax Credits: **$42.7 million**
  - Payment plan: remaining payment in full is in FY24 Governor's Budget.
- Deferred Maintenance: **$2.2 billion**
  - Payment plan: annual appropriations using Alaska Capital Income Fund ($32.3 million in FY24).
- State Share of School Major Maintenance and Construction Lists: **$413.5 million**
  - Payment plan: FY24 Governor's Budget does not include an appropriation for this. REAA fund can also be used for some projects
- Rural Alaska Sanitation Funding Need (per DEC FY21 list): **$1.8 billion**
  - Payment plan: Village Safe Water capital program. FY24 Governor's Budget includes $25.0 million UGF, $247.7 million all funds

Why 75 / 25? *(continued)*

Later this week we'll see several fiscal updates, which will be mostly negative:

- The price of oil is trending several dollars below the Fall forecast for FY2024 of $81 / bbl. DOR uses the "futures" market to set the price forecast
- Production is also trending a bit below forecast
- The combined impact will likely reduce FY24 revenue by a few hundred million
- Although the Willow project will produce substantial tax revenue in the future, during the period of major construction spending it will result in several years of substantial negative cash flows.

The net effect of these will likely result in about a $1 billion shortfall

- Oil price forecast for future years are also likely to be adjusted downwards
- Weak current-year earnings will reduce the size of future POMV draws

The 75 / 25 Scenario Was the Most Stable and Balanced

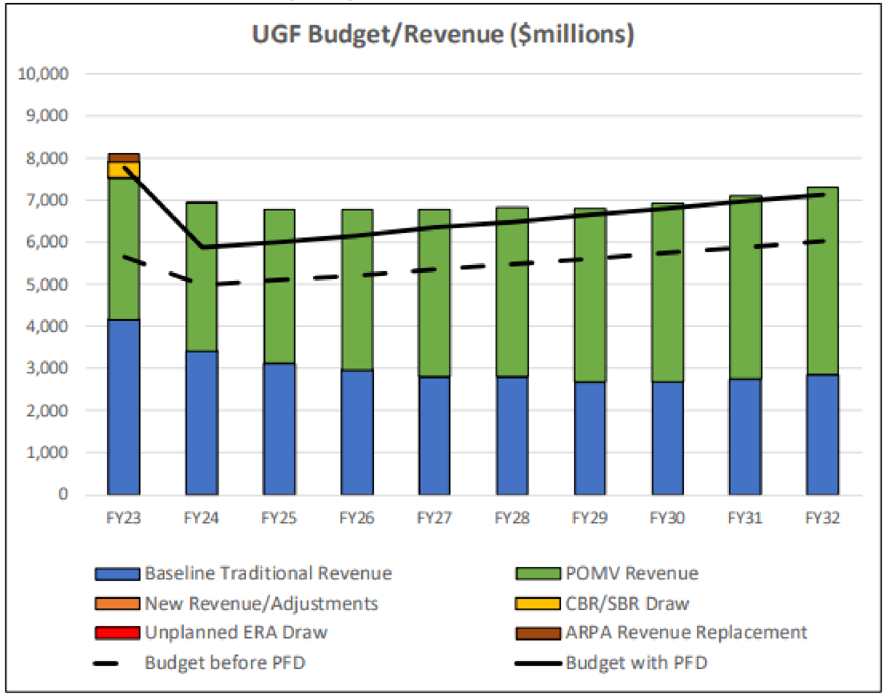
This is a Legislative Finance slide from Feb. 7

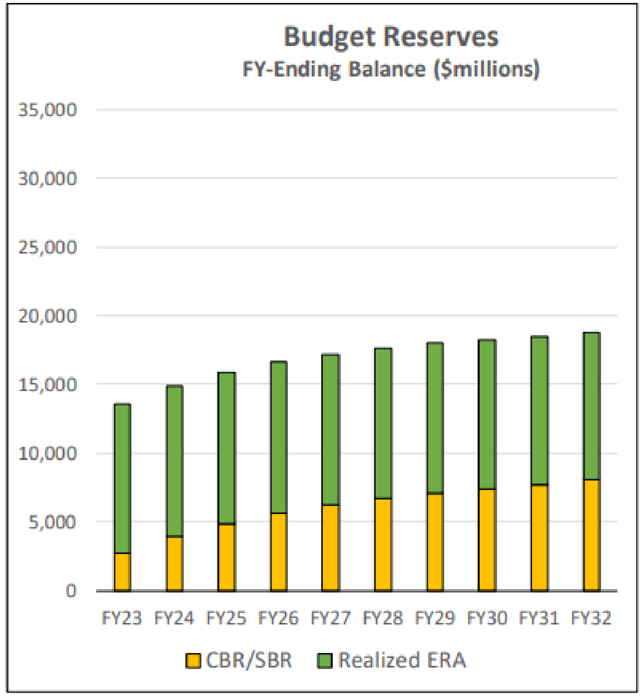
We will see this and similar scenarios with the updated forecast information on Friday

Senate Finance Baseline Budget
25% of POMV to PFD

APFC Returns: 7.05% FY24+
Oil Price: DOR Fall FC
Agency Ops: Governor Budget + $30m
Comm. Assist FY24, 2.5% Growth
Capital: $400m FY24, 2.5% Growth

Surplus/(Deficit) ($millions)	FY23	FY24	FY25	FY26	FY27	FY28	FY29	FY30	FY31	FY32
	(233)	1,063	779	630	444	343	168	119	135	175





Effective POMV Draw Rate	FY23	FY24	FY25	FY26	FY27	FY28	FY29	FY30	FY31	FY32
	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%

Sectional Analysis

Sec. 1. Repeals the current formula the describes the "amount available for distribution" as 21% of the past five year's Statutory Net Income. Amends the current 5% Percent of Market Value (POMV) statute to confirm that the appropriation may not exceed the amount in the Earnings Reserve Account.

Sec. 2 Modifies the Permanent Fund Dividend statute, from being based on 50% of the former "21% of earnings" formula, to being based on 25% of the annual Percent of Market Value draw.

Sec. 3 Conforming language to clarify that the annual inflation proofing of the Permanent Fund principal is by legislative appropriation.

Sec. 4 Conforming language related to the exclusion of Amerada Hess earnings from both the POMV and dividend calculations.

Sec. 5 Conforming language related to the exclusion of Mental Health Trust earnings from the POMV and dividend calculations.

Sec. 6 Conforming language related to the annual appropriation to the dividend fund.

Sec. 7 Conforming language repealing sections no longer needed due to the elimination of the former statutory formula and the new language in Sec. 3.

Sec. 8 Immediate effective date ensuring the changes impact the Fall 2023 dividend.

THANK YOU

Feel Free to Call or Email with Any Questions

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