

SENATE FINANCE COMMITTEE
FOURTH SPECIAL SESSION
June 6, 2016
3:04 p.m.

3:04:08 PM

CALL TO ORDER

Co-Chair MacKinnon called the Senate Finance Committee meeting to order at 3:04 p.m.

MEMBERS PRESENT

Senator Anna MacKinnon, Co-Chair
Senator Pete Kelly, Co-Chair
Senator Peter Micciche, Vice-Chair
Senator Click Bishop
Senator Mike Dunleavy
Senator Lyman Hoffman
Senator Donny Olson

MEMBERS ABSENT

None

ALSO PRESENT

Senator Cathy Giessel; Laura Cramer, Staff, Senator Anna MacKinnon; Rob Carpenter, Analyst, Legislative Finance Division; Alexei Painter, Analyst, Legislative Finance Division; Randall Hoffbeck, Commissioner, Department of Revenue; Chris Poag, General Counsel, Alaska Permanent Fund Corporation, Juneau.

SUMMARY

SB 128 PERM. FUND:DEPOSITS;DIVIDEND;EARNINGS

CSSB 128(FIN) was REPORTED out of committee with a "do pass" recommendation.

#sb128

SENATE BILL NO. 128

"An Act relating to the Alaska permanent fund;
relating to appropriations to the dividend fund;

relating to income of the Alaska permanent fund; relating to the earnings reserve account; relating to the Alaska permanent fund dividend; making conforming amendments; and providing for an effective date."

3:05:02 PM

Vice-Chair Micciche MOVED to ADOPT the committee substitute for SB 128, Work Draft 29-GS2859\U (Wallace/Martin, 6/6/16).

Co-Chair MacKinnon OBJECTED for DISCUSSION.

3:05:20 PM

AT EASE

3:08:45 PM

RECONVENED

Co-Chair MacKinnon explained that the committee substitute could be found online.

LAURA CRAMER, STAFF, SENATOR ANNA MACKINNON, discussed the Summary of Changes (copy on file):

Section 8: Excludes the Amerada Hess funds from the POMV calculation

Removed inflation adjustment on the \$1,200,000,000 revenue limit

Section 9: The Amerada Hess funds which are deposited into the capital income fund are not available for distribution under the POMV calculation

Section 11: Added a Savings Rule:

Sec. 37.13.148 Appropriation of Revenue: Creates a savings rule that the legislature may annually appropriate unrestricted general fund revenue in excess of the unrestricted general fund appropriations. Fifty percent would be deposited into the Permanent Fund and the remaining 50 percent would be deposited into the constitutional budget reserve fund

Section 23: Management of the CBR is transferred to the Permanent Fund Corporation effective July 1, 2016

Title: Added the language: relating to unrestricted state revenues available for appropriation - this relates to the savings rule found in Sec. 11

Section 4: Removed the repeal of the Capital Income Fund

Co-Chair MacKinnon WITHDREW the OBJECTION. There being NO further OBJECTION, the proposed committee substitute (CS) was adopted.

[3:11:44 PM](#)

RECESS

[3:30:18 PM](#)

RECONVENED

Co-Chair MacKinnon discussed the budget shortfall, and informed that funds would be drawn from the constitutional budget reserve (CBR) to fill the gap. She relayed that the administration had alleged that if a draw from the CBR were to take place, it would create an opportunity cost loss of between \$50 million and \$200 million. She asked for a comment on the opportunity cost of a \$3 billion draw from the CBR.

ROB CARPENTER, ANALYST, LEGISLATIVE FINANCE DIVISION, replied that under the plan being proposed in the CS, the cost was negligible due to the fact that management of the CBR was being transferred to the Alaska Permanent Fund Corporation.

Co-Chair MacKinnon relayed that Department of Revenue Commissioner Randall Hoffbeck would discuss the subject. She stated that CSSB 128(FIN) examined use of the state's pooled assets.

Mr. Carpenter discussed the presentation, "LFD Fiscal Model" (copy on file). He explained that slide 1, which showed 4 graphs, was a status quo scenario.

[3:33:16 PM](#)

Co-Chair MacKinnon asked for an explanation of the four graphs, which the committee was using as criteria through for evaluating the success of any proposals. She explained that one graph showed the operating budget, one pertained to budget reserves, one showed the permanent fund dividend (PFD), and the final graph depicted the overall health of the permanent fund.

Mr. Carpenter indicated that the upper left graph depicted the unrestricted general fund (UGF) budget with a bar graph that indicated what revenue sources were being used. He drew attention to the column for FY 17, which showed use of the CBR for a large part of the budget. He noted the CBR use in other years, and the projected elimination of the funds by FY 19. The graph showed use of the earnings reserve account (ERA) after the CBR was expended. He added that the ERA would decline and be gone by FY 23, and the graph showed a blank space to signify a deficit in its place. He noted small red bars that indicated earnings in the ERA, but pointed out there would be no ongoing balance to fill the deficit.

Co-Chair MacKinnon wondered if the graph demonstrated the administration's assertion that the dividend program was in jeopardy if the ERA fell to zero.

Mr. Carpenter pointed out the graph in the upper right entitled "Dividend Check," and noted that the graph did not depict the PFD going to zero. Rather, the graph showed the status quo of dividends. He directed attention to the graph on the lower left of slide 1, called "Budget Reserves." He noted that the graph showed the balance of the CBR gone by FY 18, and the balance of the ERA gone by FY 21; thereby the dividend would have to be eliminated.

[3:36:23 PM](#)

Senator Dunleavy remarked that part of the input to the graphs on slide 1 assumed that state spending remained the same.

Mr. Carpenter directed attention to a column in the middle of the slide that showed some growth in the operating budget, as well as some growth in the capital budget. He added that there was an assumption of oil and gas tax credits being paid at \$250 million per year, given that there was earned credits projected at approximately \$2

billion over the following 8 years. He concluded that the black line on the first graph depicting the budget was flat.

Senator Dunleavy looked forward to hearing from the administration regarding the aforementioned opportunity cost and what went in to the calculation. He thought it was certain that if spending remained the same, there was no opportunity cost; and if spending was reduced by \$100 million, it could be argued that there was opportunity cost. He wondered about the assumptions of status quo spending. He reminded the committee about opportunities to reduce the size of the budget in the following years.

Co-Chair Kelly queried scenarios that showed what happened in the FY 17 budget as a baseline. He thought the slide assumed the spring forecast and the FY 16 management plan for a spending baseline.

Mr. Carpenter relayed that the slide used the FY 17 budget as it was in conference committee.

Senator Olson referred to the bottom right quadrant of slide 1, which showed the graph "Permanent Fund - FY Ending Balance," and asked if the depiction of the fund being flat for the next 10 years was accurate.

Mr. Carpenter thought that given the use of the ERA, the state would be earning money but pulling from the ERA in an amount that would flatten out the fund. He continued that once the ERA was exhausted in FY 21, the permanent fund was predicted to grow again.

Senator Olson found it bothersome that there had been a significant rise in the corpus of the fund over the past ten years, yet the fund was predicted to lack growth in the near future. He wondered if there was a way for the fund to grow even if the ERA was down.

Mr. Carpenter was not sure how to answer the question, and stated that the slide assumed a certain rate of return based on the asset allocation of the permanent fund.

[3:40:16 PM](#)

Mr. Carpenter looked at slide 2, which showed the same 4 graphs as slide 1, reflecting the passage of CSSB 128(FIN).

He pointed out the budget graph in the upper left, with a new bar depicting use of the Percent of Market Value (POMV) payout to the general fund (GF). The POMV payout significantly filled the budget deficit under the new scenario. In the lower left quadrant, he pointed out the graph depicting the life of the CBR extending to FY 23; and a healthy ERA through FY 25. He drew attention to the "Dividend Check" graph in the upper right, noting that the bill set the PFD at \$1000 for the first three years, then falling into the formula thereafter with dividends at roughly \$1000.

Mr. Carpenter continued discussing slide 2, highlighting the "Permanent Fund - FY Ending Balance" graph in the bottom right corner. He pointed out that the balance of the fund itself [under the CSSB 128 scenario] had grown to a larger balance of over \$60 billion versus the status quo scenario on slide 1 that showed a flat balance. He noted that for FY 17, even with a POMV payout of almost \$2.4 billion, there was a remaining deficit of \$1.5 billion that could be seen on the table on the lower left of the slide. He added that the remaining deficit amount would be filled by the CBR in FY 17.

Co-Chair MacKinnon turned to slide 1, and drew attention to the table at the bottom left of the slide. She looked at the row "Years to Exhaust," and explained that the numbers (starting with 4 in FY 17 and moving steadily down to zero in FY 22) indicated how in many years until budget reserves would be gone. She compared it to the same table on slide 2, which reflected what would happen under conditions of the proposed plan. The "Years to Exhaust" row on slide 2 showed the reserves starting at 9 for FY 17, and growing steadily because of the change in the use of the funds.

Co-Chair MacKinnon continued to compare the tables at the bottom left of slide 1 and slide 2, and pointed out the "Deficit" row. She noted that the status quo table on slide 1 showed approximately \$3.3 billion of deficit in FY 17; and the same figure on slide 2 [reflecting implementation of the proposal in the CS] showed a much lower deficit of \$1.5 billion. She explained that the committee was looking to extend the health of the state's budget reserves, as well as keeping the corpus of the permanent fund healthy.

Senator Hoffman asked if both scenarios assumed a capital budget of approximately \$185 million from FY 19 through FY

25. He asked Mr. Carpenter to remind the committee of the standing of the current capital budget.

Mr. Carpenter relayed that the capital budget was currently at \$96 million.

Senator Hoffman noted that the amount for FY 19 through FY 25 was double what the capital budget was currently.

Mr. Carpenter concurred.

[3:44:00 PM](#)

Senator Dunleavy discussed federal matching funds, and wondered if the state doubled its capital budget if it would also double the receipt of federal funds.

Co-Chair MacKinnon stated that the proposal had tried to leverage as many dollars as possible with the money allocated from the GF, but there was not an excess of federal funds. Rather, there was a Department of Transportation and Public Facilities funding match. She thought there might be a bit more federal funds, but not a doubling of expenditures by the state.

Mr. Carpenter confirmed that the state had leveraged every federal dollar that was possible.

Senator Hoffman asked if doubling the capital budget over the proposed period of time was a good start in leveraging federal dollars.

Co-Chair MacKinnon stated that many Alaskans believed that the capital budget, if it remained low for too long, would mean increased costs though deferred maintenance. She relayed that state assets were struggling with maintaining repairs.

Senator Bishop thought the deferred maintenance problem would only worsen if it were not addressed. He added that it was important to consider fixing what the state already owned rather than investing in new capital purchases.

Mr. Carpenter addressed slide 3, "20/20 Plan Cash Flow." He drew attention to the circled area, which encompassed boxes for the permanent fund principal, the ERA, and the CBR. He explained that the funds were shown inside a circle to

denote an investment pool, while other cash flow sources (royalties, production tax, and other UGF revenue) were outside the circle with arrows toward the GF. He noted that the royalties were split between the public school trust, the principal of the permanent fund, and the GF; while the other two fund sources flowed toward the GF at 100 percent. He relayed that the graph showed the POMV payout coming from the ERA to the GF; while a dotted line on the diagram illustrated CBR draws (as necessary to fill deficits) flowing to the GF. Finally, the diagram showed 20 percent of royalties and 20 percent of the POMV paid out for PFDs.

[3:47:35 PM](#)

Co-Chair MacKinnon clarified that the slide depicted where the money currently resided, and how the bill proposed to manage and direct the money.

Senator Olson asked about PFDs and observed that the bill proposed a dividend at a flat amount near \$1000 over the next 3 years. He wondered what would happen to the dividends after FY 19.

Mr. Carpenter returned to slide 2, which showed a projected dividend at roughly \$1000 under the bill formula.

Senator Olson thought the graph illustrated that the dividend amount was projected indefinitely at the same amount.

Mr. Carpenter stated that the amount was projected for the time period shown on the graph, and if production and royalty were to decline there would be a drop in the dividend. He added that growth of the permanent fund and the POMV amount would offset the decline in royalty.

Co-Chair MacKinnon asked if it was accurate that there was a variety of variables under the proposal that would affect the dividend.

Mr. Carpenter agreed.

Co-Chair MacKinnon surmised that the permanent fund earnings and the royalties were part of what would affect the dividend. She thought the forecast was based on spring projections, and asked if the spring projections were above or below what the state was currently experiencing.

Mr. Carpenter thought the projections were below what was expected, but growing in line with the spring projections.

Co-Chair MacKinnon thought the committee could get more information from Commissioner Hoffbeck to enhance understanding of the variables affecting the PFD.

Senator Olson commented on the variables and thought it would be helpful to be able to communicate more information to his constituents.

[3:51:01 PM](#)

Mr. Carpenter looked at slide 4, "PRPA Payout/Revenue Limit," which showed two graphs depicting the UGF revenue limit, which he explained was put in place against the POMV payout. He noted that the graph to the left portrayed what would happen without the payout limit. The bar graph showed non-volatile revenue (such as corporate income tax), the POMV payout, the volatile revenue (such as oil and gas), and the deficit (which indicated CBR use). He explained that the graph used FY 17 revenue under the spring forecast. He pointed out the black line that depicted the budget. He noted that the POMV payout was consistent across the oil price scenario (the values on the bottom). As the price of oil grew, the total volatile revenue grew as well. He indicated that at a certain price point on the graph, the budget line showed surplus revenue.

Mr. Carpenter continued discussing slide 4, and relayed that there had been concern over what to do with the forecast surplus revenue, therefore the revenue limit had been proposed by the governor's office. When volatile revenue reached \$1.2 billion, the POMV would be reduced on a dollar-per-dollar basis, as illustrated by the graph on the right, "UGF Revenue with Payout Limit." He directed attention to the point of oil revenue (at \$75 to \$85) where the POMV started to decline as the volatile revenue started to increase beyond a certain point. He added that the payout limit proposal would mean that oil had to be \$110 before there would be surplus revenue.

Co-Chair MacKinnon asked if the POMV was reduced and not paid out, if it would sit in the ERA. Mr. Carpenter turned to slide 5, "Savings Rule." He pointed out surplus revenue

on the graph, which showed 50 percent going to the CBR and 50 percent going to the permanent fund principal.

[3:54:18 PM](#)

AT EASE

[3:55:49 PM](#)

RECONVENED

Co-Chair MacKinnon referred to her earlier question about POMV funds. She looked at the green bars on slide 4, which represented the POMV with a payout limit, and understood that the excess funds would stay in the ERA. She asked what would happen when the funds remained in the ERA.

Mr. Carpenter detailed that as the revenue limit was put into effect and the POMV payout was reduced; the funds would stay in the ERA and the permanent fund, provide additional assets for investment and grow the permanent fund, and then cause the dividend to grow.

Co-Chair MacKinnon restated that the excess POMV funds would be saved to help drive the dividend up.

Senator Olson asked what would happen to the dividend if there was a financial crisis such as in 2008.

Mr. Carpenter replied that any financial crisis would impact the dividend negatively.

Senator Olson asked if the effect would be significant.

Mr. Carpenter recounted that there had been potential for the state to have a zero ERA with no dividend in 2008; and thought the possibility still existed.

Co-Chair MacKinnon stated that the difference in the dividend formula (under the proposed plan of 20 percent market value and 20 percent royalty) diversified risk. She thought the worst case scenario was if the price of return on investment dropped significantly. She continued that if oil production remained the same and the price stayed up, then the dividend would be higher than if it were only based on a percentage of market value from the permanent fund earnings.

Senator Olson understood that the risk would still be significant, but not as significant as it had been under the existing formula.

Co-Chair MacKinnon reiterated that the PFD would be blended from two sources, therefore the risk should be diversified. She added that under the proposed plan, the dividend would not swing upwards as dramatically as in the past.

Senator Hoffman asked about the dividend amount, as well as the diminished volatility of the dividend under the proposal in the bill compared to the current plan.

Mr. Carpenter replied that the current dividend formula was based on 20 percent of the previous five years earnings calculation, and recounted historic low PFD amounts as well as spikes due to dramatic fluctuations calculated into the average. Under the new scenario, the amount of the dividend would maintain, given that the formula would be a 5-year payout of a calculation based on the entire balance of the permanent fund.

Senator Hoffman surmised that the people of Alaska could better predict the range of the PFD under the proposed plan.

Mr. Carpenter replied in the affirmative.

[4:00:42 PM](#)

Co-Chair MacKinnon shared that the administration had proposed an annuity-style draw, as a way to close part of the fiscal gap and diversify the revenue stream. She asked if the commissioner of the Department of Revenue had any comments on the CS that was before the committee.

RANDALL HOFFBECK, COMMISSIONER, DEPARTMENT OF REVENUE, stated that the CS was different than the bill that was originally proposed, but it did accomplish the purpose that the administration had set out within the bill. He continued that the original intent had been to have a systematic way to use the ERA that protected both the corpus of the permanent fund and the PFD. He affirmed that the administration was pleased with the CS, and thought it represented cooperation. He thanked the committee, and particularly Co-Chair MacKinnon for the work on the bill.

He echoed the governor's comments about the bill being subject to change.

Co-Chair MacKinnon stated that the committee had questions about the opportunity cost of not moving forward with the proposed plan. She recounted passing a balanced budget including a significant draw from savings. She relayed that there had been bipartisan support in the Senate and House for the necessary three-quarter vote to access the CBR, which had a lower rate of return than the ERA. She asked the commissioner if he had the same understanding.

Commissioner Hoffbeck answered in the affirmative.

Co-Chair MacKinnon asked for explanation of how the opportunity cost was calculated, so that the committee members could contemplate the calculation in consideration of the bill.

Commissioner Hoffbeck replied that there was three components that drove the change in the equation. The primary issues were: how much the state spent on the budget, what other revenue sources were available, and how much would be spent for supporting government versus the PFD program (considering the Permanent Fund Protection Act (PFPA)). He continued that when the administration had considered the opportunity cost, it had looked at a \$700 million difference between the dividend payout as it currently was versus under the PFPA. Additionally, the administration had reviewed \$300 million to \$400 million in new revenues, as well as the impact of the oil and gas tax credits.

Commissioner Hoffbeck continued, and summarized that there was a \$1 billion to \$1.5 billion difference between the status quo and the implementation of the PFPA and other programs. He elucidated that the biggest issue with the PFPA would be the \$700 million investment return difference; which at a 7.25 percent rate of return, would equate to \$50 million of lost revenue. He added that considering other components, there would be \$100 million that would not be recovered for the future.

Co-Chair MacKinnon noted that the bill proposed to move \$3 billion from the CBR, and asked what the opportunity cost loss was on spending the funds.

Commissioner Hoffbeck stated that the loss was in the \$50 million range, due to the fact that the bill did not have the adjustments associated with the components that had been proposed earlier. He clarified that the totality of the governor's proposed finance package (including additional revenues and credit reform) was in the \$100 million range.

Senator Dunleavy mentioned an earlier reference to the amount of \$200 million, and asked for an explanation.

[4:05:35 PM](#)

AT EASE

[4:07:00 PM](#)

RECONVENED

Co-Chair MacKinnon shared that she had requested the Legislative Finance Division (LFD) to provide additional dialogue on the subject. She wanted to provide greater understanding about the assertion from the administration that there was a \$200 million opportunity cost if the state used \$3 billion from the CBR.

ALEXEI PAINTER, ANALYST, LEGISLATIVE FINANCE DIVISION, considered that the \$200 million was the difference between if the deficit were filled with the CBR rather than the ERA (without a permanent fund plan). He recalled that there had been discussion in the legislature about using the ERA instead of the CBR. He furthered that, in the absence of the PFFPA, which allowed the CBR to be invested for a higher return, there would be a significant difference (an estimated \$200 million) in investment revenue between using the ERA and the CBR.

Senator Dunleavy asked if the calculation had been based on the CBR being invested differently.

Mr. Painter replied in the affirmative.

Co-Chair MacKinnon added that the calculation also considered the elimination of the \$3 billion and the earning potential.

Senator Dunleavy wondered if it was possible to isolate the investment in order to get the desired return without having to do anything with POMV.

Mr. Painter replied in the affirmative, but advised that the scenario would require statutory change. He explained that currently the CBR had to be invested conservatively if it was going to be used within the following five years.

Senator Dunleavy thought some had alleged that passage of the bill would cause the opportunity cost loss, but thought the legislature could make the necessary changes through legislation to change how the CBR was invested.

Mr. Painter concurred, considering the difference between using the CBR and the ERA. He added that there was an opportunity cost, as the commissioner had mentioned, of the dividends and other factors.

Senator Dunleavy stated that there was also an opportunity cost of not reducing the budget further.

Vice-Chair Micciche discussed the difference between investing the CBR and the ERA, and asked if not passing the bill under consideration (or another) would mean a difference of between \$800 million and \$900 million.

Mr. Painter replied in the affirmative.

[4:10:07 PM](#)

Co-Chair MacKinnon acknowledged that the administration had a different outline for opportunity cost as well as an assertion of a \$200 million difference in returns. She reiterated that she wanted to edify the subject to aid in considering the bill.

Co-Chair MacKinnon stated that the bill being considered would establish a POMV, and pooled all the state's assets to generate revenue. She furthered that the revenue would pay the dividends at 20 percent of the POMV, plus 20 percent of royalties. Additionally, the bill would guarantee a dividend of \$1,000 for three years. The bill would also set a revenue limit of \$1.2 billion, above which the POMV spending would be reduced by whatever amount was earned. Funds above the revenue limit would stay in the ERA to help drive up future dividends.

Co-Chair MacKinnon continued discussing the bill, noting that it would create a savings rule that stipulated that in

a high-price environment, legislators may contribute 50 percent of excess funds to the permanent fund and 50 percent to the CBR to pay back the money that had been spent. The bill transferred management of all funds to create pooled assets under the management at the Alaska Permanent Fund Corporation (APFC) to receive a higher rate of return.

Vice-Chair Micciche relayed that he had asked DOR to provide him with a scenario illustrating the difference if the legislature had changed the CBR investment protocol 10 years previously. He recalled the difference was about \$1.6 billion. He pondered how investments worked over the long term, and thought the state should have made the change a long time ago. He recognized the effort to keep the CBR more liquid, but thought the practice had cost the state considerably.

Commissioner Hoffbeck stated that the numbers were accurate, and pointed out that the management mandate for the CBR was different (than for the permanent fund) as the state had to remain more liquid, particularly during years where the state had substantial draws. He acknowledged that the constraints had held down rates of return. He hoped that by co-managing the funds within the permanent fund, returns would be generated similar to those of the permanent fund. He noted that some liquidity measures would have to be taken in the current year to ensure that the cash calls could be met.

Senator Olson discussed management of the permanent fund, and wondered if the commissioner thought it was wise to have the management of the CBR transferred to the APFC.

Commissioner Hoffbeck thought that there was an opportunity available by transferring the CBR management to the APFC. He thought his staff did a very good job managing the fund, but recognized there were opportunities available through merging the funds. He noted that he had discussed looking at opportunities for co-management of funds with Co-Chair MacKinnon before the matter was in the bill.

Senator Olson asked if the governor had strong feelings on the matter.

Commissioner Hoffbeck replied in the negative.

4:15:28 PM

CHRIS POAG, GENERAL COUNSEL, ALASKA PERMANENT FUND CORPORATION, JUNEAU, invited the committee to pose questions about APFC as it related to the bill.

Co-Chair MacKinnon asked if Mr. Poag was up for co-managing pooled investments for Alaskans.

Mr. Poag answered in the affirmative and expanded that the sole responsibility of APFC was to invest and manage assets. He explained that by making the pool larger, there would be better investments and returns. He added that a POMV draw was very common among endowments and universities, and typically ranged from 4 percent to 5 percent. He noted that the proposed POMV was 5.25 percent, and was based on five of the preceding six fiscal years, so the effective rate was not likely to be 5.25 percent. He informed that the trend was for markets to incline, therefore one would artificially deflate the value.

Mr. Poag continued discussing the bill, noting that Section 1 gave the APFC comfort in that in three years the legislature would reevaluate the use of the ERA, to determine whether there was over-consumption or under-consumption. He thought the reevaluations were important, and ventured that in three years the state would be able to determine whether 5.25 percent was the right level.

Vice-Chair Micciche asked if Mr. Poag envisioned the reporting of the performance of the co-mingled funds to become a sub-set of the annual report of the permanent fund, or if it would be reported through DOR.

Mr. Poag believed the bill addressed the subject. He referred to Section 5, line 13; which outlined a requirement that APFC provide a report to the legislature by March 15, communicating the balance of the fund at the beginning and end of the fiscal year. He expanded that APFC would communicate the nominal, real, and realized returns of the CBR portion of the managed assets. He noted that there was already pooling of the main permanent fund and the ERA, as well as some portion of mental health trust funds. If the legislation were to pass, there would be four pools that made one large asset pool.

4:18:44 PM

Vice-Chair Micciche asked if Mr. Poag envisioned a separate asset allocation, or similar investment of all of the funds in the pool.

Mr. Poag stated that the APFC board had discussed holding a special board meeting if the legislature acted to change the way the ERA was accessed; at which it would consider the current asset allocation and determine whether or not to make adjustments. He discussed the necessity of determining the rate of spend for the CBR, in order to decide if the current asset allocation would be liquid enough. He noted that APFC's intention was to start by using the same asset allocation for the main fund and the ERA. He stated that APFC was hopeful that it could manage the cash needs that the legislature had for a fixed draw or any CBR appropriations.

Vice-Chair Micciche asked if APFC maintained a portion of the permanent fund corpus in liquidity.

Mr. Poag answered in the affirmative, and noted that APFC had 6 percent of the fund in cash and interest.

Vice-Chair Micciche wondered whether the liquidity could be transferred for a draw from one account to another without affecting the various asset allocations.

Mr. Poag stated that the board had set up a "risk dashboard" with allocations, which established authority to act within the boundaries. He expanded that there were levels which necessitated different involvement of the chief investment officer, chief executive officer, and the board. He explained that if the cash draw was within the established boundaries it would not be a problem, however a larger cash draw would possibly necessitate accommodations by realizing an investment. Alternatively, it was possible to utilize a line or letter of credit to solve a short-term cash need while allowing less liquid assets to maintain in the current profile.

Co-Chair MacKinnon understood from past meetings that the bill would allow DOR to work cooperatively with APFC to establish a smooth transition of the management.

Mr. Poag concurred.

Senator Dunleavy asked if APFC had any concerns about the bill.

Mr. Poag expressed that the decision to access the ERA was a policy decision that was outside the purview of APFC. He noted that the board had a meeting in January at which it evaluated the legislation and had given input. He thought APFC had been afforded a great opportunity to advise the state on how to make an informed decision on how to spend funds at a sustainable level. He communicated that APFC was in support of the proposal, and looked forward to reevaluating the success of the asset pool in three years' time.

[4:22:43 PM](#)

Co-Chair MacKinnon stated that the new fiscal notes would not be adopted, but she wanted to discuss them with the committee. She shared that because of the sequence of events, the committee could not incorporate new fiscal notes in to the budget. She informed that the notes would be advisory only, and would have to come back in the form of a supplemental request to the legislature. She wanted to highlight the difference in approach that the fiscal notes represented.

Vice-Chair Micciche explained that both fiscal notes were related to the projected change (increase and decrease) in management fees due to the modifications in investment proposed in the bill. He explained that the first fiscal note was for DOR, with an appropriation for APFC, APFC Operations. The note proposed operating expenditures of \$14,800,000 from the 1105 permanent fund gross fund for FY 17 through FY 22. The funds were for a projected increase in management fees due to a change in how the fund would be managed.

Vice-Chair Micciche discussed the second fiscal note for DOR Taxation and Treasury, for the Treasury Division. The note proposed a decrement of \$130,000 in external management fees for managing the CBR from FY 17 through FY 22. He detailed that the decrement had been included in the governor's FY 17 request. The fiscal note analysis detailed that the total cost of managing the CBR was approximately \$1.4 billion, and with the exception of the \$130,000 decrement, the costs would be allocated to other funds in the Treasury.

Co-Chair MacKinnon relayed that the committee would be looking for actual costs for managements, and if the department was managing quite a bit of the work internally, she would expect to see a downturn in staffing positions at DOR.

[4:25:30 PM](#)

Senator Dunleavy remarked that there were different ways of looking at opportunity costs, which he thought had been demonstrated during the meeting. He thought many committee members shared the concern that there were opportunity costs to realize through continued reduction of the budget. He thought there would be less pressure to reduce the budget if new revenue streams were found. He thought some believed the Senate had cut too much from the budget, and others thought not enough had been cut.

Senator Dunleavy continued discussing the bill. He personally believed there was much to be done in cutting the budget. He noted that with the passage of the bill, the state would still have \$1 billion gap between revenues and expenditures. He questioned how the gap would be filled, and expressed concern about keeping the growth of government in check. He questioned taking funds out of the economy (with capping of the dividend) and thought it presented an opportunity cost as well. He thought state government would keep growing at the expense of the private sector. He was concerned that the plan would take pressure off the legislature in tackling budget issues the following year.

Senator Hoffman stressed that the current issue was the budget deficit. He felt that without the legislation the state would be in a worse financial situation. He recalled the last time he saw a piece of legislation of the same magnitude was when the legislature passed the bill establishing the CBR account. He discussed the importance of the legislation and noted that without putting the settlement funds into a fund, the dollars would have been spent instead of utilized to meet the state's needs.

Senator Hoffman continued to discuss the bill, and commented that the restructuring of the permanent fund did several things: it protected and stabilized the permanent fund, and it gave the state long-term cash flow to meet its

needs. He emphasized the need for action on the fiscal gap, but acknowledged that the plan would not fill the complete gap. He thought the vast majority of Alaskans were looking to the legislature to come up with a fiscal plan.

4:30:25 PM

Vice-Chair Micciche shared that he had listened to transcripts of the meetings from when the permanent fund was created. He had gleaned that the fund was designed to help support government when times were difficult. He acknowledged the bill did not fill the fiscal gap, and thought it was imperative to continue to cut the budget and make government more efficient. He emphasized that he did not feel reduced pressure to cut the budget. He thought that without taking action, the PFD would likely go away in about five years; whereas with passage of the bill it could be maintained in perpetuity.

Vice-Chair Micciche discussed opportunity cost and the vast earnings differential if the allocation of the funds were changed. He mentioned oil and gas tax credit legislation. He thought there were more cuts to make on the budget. He thought the key to surviving a fiscal downturn was to use all the tools available. He thought the investment of the last forty years was being used to continue to manage down the size of government. He was not enthusiastic about passing the bill but saw the necessity of passing it.

Vice-Chair Micciche MOVED to report CSSB 128(FIN) out of Committee with individual recommendations. There being NO OBJECTION, it was so ordered.

4:34:33 PM

AT EASE

4:37:22 PM

RECONVENED

Co-Chair MacKinnon thanked the Legislative Finance Division team, her own staff, and the Legislative Legal department. She thanked the Department of Revenue, Commissioner Hoffbeck, Mr. Alper, and associated staff. She thanked Attorney General Richards, and expressed appreciation for Governor Walker and Senator Lesil McGuire.

CSSB 128(FIN) was REPORTED out of committee with a "do pass" recommendation.

#

ADJOURNMENT

4:39:48 PM

The meeting was adjourned at 4:39 p.m.