

HOUSE FINANCE COMMITTEE  
February 2, 2017  
1:31 p.m.

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CALL TO ORDER

Co-Chair Foster called the House Finance Committee meeting to order at 1:31 p.m.

MEMBERS PRESENT

Representative Neal Foster, Co-Chair  
Representative Paul Seaton, Co-Chair  
Representative Les Gara, Vice-Chair  
Representative Jason Grenn  
Representative David Guttenberg  
Representative Scott Kawasaki  
Representative Dan Ortiz  
Representative Lance Pruitt  
Representative Cathy Tilton  
Representative Tammie Wilson

MEMBERS ABSENT

Representative Steve Thompson

ALSO PRESENT

Randall Hoffbeck, Commissioner, Department of Revenue.

SUMMARY

HB 61 PERM. FUND:DEPOSITS;DIVIDEND;EARNINGS

HB 61 was HEARD and HELD in committee for further consideration.

Co-Chair Foster addressed the meeting agenda.

#hb61

HOUSE BILL NO. 61

"An Act relating to the Alaska Permanent Fund Corporation, the earnings of the Alaska permanent

fund, and the earnings reserve account; relating to the mental health trust fund; relating to deposits into the dividend fund; relating to the calculation of permanent fund dividends; relating to unrestricted state revenue available for appropriation; and providing for an effective date."

1:32:22 PM

RANDALL HOFFBECK, COMMISSIONER, DEPARTMENT OF REVENUE, provided a PowerPoint presentation titled "Permanent Fund Protection Act" (copy on file). The Permanent Fund Protection Act was a key part of the governor's fiscal plan to resolve the state's budget deficit. He referred to two companion documents: a white paper called The Alaska Permanent Fund and the Permanent Fund Protection Act dated January 2017 (copy on file) and a single page document titled Permanent Fund Protection Act dated January 31, 2017 (copy on file). He addressed slide 2 of the presentation.

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Commissioner Hoffbeck moved to slide 3 and provided a presentation overview. He addressed the problem facing the state on slide 5:

1. Low oil revenues
2. Persistent deficit
3. Diminished budget reserves

Commissioner Hoffbeck elaborated on slide 5. From 2014 to 2017, the state was in a "low oil price environment." He thought this was the new norm. He spoke to the need for an alternative revenue source in order to avoid depleting savings. He moved to slide 6 and spoke to low oil revenue. From 2005 to 2014, over 90 percent of the undesignated general funds (UGF) revenues came from petroleum. Between 2012 and 2015, oil revenue had fallen 88 percent or \$7.8 billion. He spoke to the net impact of lower oil prices on slide 7 titled "Deficit Spending." Although the UGF budget had been cut by 44 percent since 2013, the deficit persisted. The state had used its savings to cover the deficit, leaving only one more year in which such action would be possible. He pointed to the blue dashed line on the graph, representing the UGF budget, the yellow bar representing the UGF revenue displayed the aforementioned sharp drop, and the red hatch marks representing the

overall deficit. He provided detail about the chart on the slide. Revenues had dropped due to decreased price and production. Long before the state ran out of the deficit, it would run out of savings.

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Commissioner Hoffbeck moved to slide 8 titled "Diminished Budget Reserves." In 2013 the state had about \$16.3 billion in the combined Statutory Budget Reserve (SBR) and the Constitutional Budget Reserve (CBR). For the end of FY 17, he projected \$4.6 billion, and \$2.1 billion at the end of FY 18, which would be the last budget year to rely on savings before they were depleted. The status quo would mean the state would run out of time. He spoke to the need to save money in the CBR for unexpected expenditures, to meet budgetary expectations in a given year, and as a liquidity bank in order to pay the state's bills on a daily basis. The best way to do this was to use the CBR as the liquidity portion for the Permanent Fund Earnings Reserve to pay back as gains are realized so the fund is not forced to realize gains artificially to cover cash draws.

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Commissioner Hoffbeck addressed the question of how to best solve the fiscal crisis with a sustainable draw and dividend on slide 9. He turned to slide 11 and addressed the Permanent Fund structure, which included the principle (\$39.4 billion non-spendable funds plus \$4.7 billion in unrealized gains), and the earnings reserve account (\$8.6 billion), which was available for expenditure. He directed attention to slide 12 and addressed how the Permanent Fund worked. He referred to statutory net income, which included realized gains from dividends, fixed income, real estate investments, sold equities, and anything that generated cash on an annual basis; it flowed from the principle of the fund to the Earnings Reserve Account (ERA) for a total of about \$3 billion annually. He explained a five-year average was used to determine the amount available for appropriation. Half of that amount paid the dividend. The remainder was used to inflation-proof the Permanent Fund.

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Commissioner Hoffbeck moved to slide 13 titled "The Permanent Fund: Earnings." He shared the money generated by the fund far exceeded oil and gas tax and other unrestricted revenues. He stated it was unlikely the oil price would exceed earnings from the fund, with the exception of a few anomalous years. The Permanent Fund was the state's largest asset and would continue to be going into the future. He addressed the problem on slide 14. He detailed that absent change, the earnings reserve would also be depleted by 2023. It would create a situation where the state could not pay the bills or pay the dividend. Something more forward-looking was needed.

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Commissioner Hoffbeck spoke to slide 16 titled "Why Use Permanent Fund Earnings?" The current UGF budget was about \$4.2 billion, which created a \$2.8 billion budget gap in FY 18. He addressed potential tools to address the gap including a motor fuel tax increase, another broad-based tax increase, a corporate income tax increase, oil tax credit reform, and maximum proposed cuts of \$750 million. The items totaled \$1.6 billion. The only thing capable of solving the total problem was using earnings from the Permanent Fund.

Representative Wilson asked which of the options fell under current or future proposed legislation. She asked for clarification on the items listed on slide 16.

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Commissioner Hoffbeck replied the motor fuel tax bill was currently in play. There was no broad-based tax bill at present. The corporate income tax legislation had been prepared by the governor and another related bill had been proposed by Vice-Chair Gara. As he understood it, the House was talking about introducing a bill related to oil and gas tax credit reform. The cuts proposed item was based on modelling. The cuts proposed on the slide used the Senate's number.

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Commissioner Hoffbeck moved to slide 17 titled "How Should We Use the Permanent Fund?" He referred to significant discussion about the reason for the establishment of the

fund. He read language from the ballot initiative that had established the constitutional amendment for the Permanent Fund:

"This proposal, if approved, would amend the Constitution of the State of Alaska by ... establish[ing] a constitutional permanent fund into which at least 25 percent of all [mineral royalties] received by the State would be paid. The principal of the fund would be used only for income-producing investments permitted by law and the income from the fund would be deposited in the general fund of the State and be available to be appropriated for expenditure by the State unless otherwise provided by law."

Commissioner Hoffbeck highlighted that the constitutional language does not include availability of the income from the fund for appropriation for expenditure, but had been on the ballot initiative.

Co-Chair Foster recognized Representative Kawasaki had joined the meeting.

Commissioner Hoffbeck moved to slide 18 and addressed how the state should use the fund. He stated the fund was intended to be multi-generational and needed to be sustainable over the long-term; the fund needed to grow at the rate of inflation at a minimum. The fund needed to provide a dividend. As long as the earnings reserve was being utilized as a conduit for the cash for appropriation, the account had to be able to bridge years with lower earnings.

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Representative Grenn asked if there would be an investment philosophy change within the Alaska Permanent Fund Corporation (APFC) regarding the management of the fund if the funds began to be used for the state.

Commissioner Hoffbeck answered the modelling did not assume a change in fund management. He outlined that the dividend was the only draw and that inflation-proofing was the other large draw but went back into the corpus, whereas what was proposed was twice that size. He believed it would be possible to work out a plan where the CBR was used for

daily expenditures and when gains were realized they would be transferred to DOR to pay back the CBR. Currently, the projections from the APFC showed that it earned around 90 percent of its earnings every year. The fund should be realizing more than enough annually without having to change its structure.

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Commissioner Hoffbeck continued to address slide 20 related to how the fund should be used. He stated that the plan needed to be rule-based. It need to have rules for saving, spending, and paying out the dividend. He thought that once new rules were in place, the legislature would follow those rules, which were international best practice. He briefly highlighted slide 21 that included examples of rule-based frameworks used for other sovereign wealth funds. Examples included Singapore, Kazakhstan, and Norway.

Vice-Chair Gara asked for verification the administration was proposing a 5.5 percent draw from the Permanent Fund. He referred to talk about whether it should be a 4.25 percent or other draw. He asked for verification that none of the numbers would work in a catastrophic year.

Commissioner Hoffbeck answered that in the event of multiple catastrophic years in a row, it was a fair statement, but that it was not the history of the market for this to occur. In the proposal, there was a provision for a three-year review which would act as a safety net, allowing for adjustment. It would not work with three or four years of catastrophic returns in any number.

Vice-Chair Gara stated he was not being critical, it was just the reality. He spoke to the structure of the ERA, which was based on realized earnings rather than the actual growth of the Permanent Fund. He noted that net earnings would present a problem regardless of whether the draw was moved by a quarter percent.

Commissioner Hoffbeck answered "fair enough."

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Commissioner Hoffbeck moved to slide 22 and continued to address how the Permanent Fund should be used. He stated that the system needed to remove volatility. The graph

presented UGF revenue in the yellow line and the blue dashed line represented UGF budget. The volatility was apparent, particularly in the revenue. He specified that FY 07 and FY 08 showed \$11 billion [in UGF revenue], and by FY 16 revenues had been about \$1 billion. The change meant that ten years later the state had to figure out how to deal with \$10 billion less revenue. Flattening out some of the volatility was a desirable result that should be sought in any proposed plan. He spoke to volatility that had been shown to create slower economic growth within the market. With nearly 100 percent reliance on a commodity with highly volatile prices, there is a situation of tremendous volatility. Returns were volatile too, but that could be accounted by using a five-year lookback and a draw component.

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Commissioner Hoffbeck turned to slide 23 and spoke to the need to maximize the use of Permanent Fund earnings. The modelling mantra was to fill as much of the gap as possible, yet even with that method there was still a significant gap of \$700 million to \$1 billion to be filled. Leaving significant money on the table was not using the fund as effectively as possible.

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Commissioner Hoffbeck addressed the bill summary on slide 25. The plan before the committee was essentially the result of the hearing process from the previous year. The bill included language that had passed the Senate the previous year.

Last year, the 29th Legislature held 39 hearings on the Alaska Permanent Fund Protection Act (SB128, HB245, and SB5001):

- SSTA: 10 hearings, including 2 days of public testimony
- SFIN: 10 hearings, including 1 days of public testimony
- HFIN: 19 hearings, including 4 days of public testimony

Other bills addressing the use of permanent fund earnings were also considered:

- SB114 (Sen. McGuire): 7 hearings in SSTA, 9 hearings in SFIN
- HB303 (Rep. Millet): 4 hearings in HFIN
- HB224 (Sen. Hawker): 4 hearings in HFIN

HB61 is the same as the CS for SB128, but without provisions re.:

- CBR management
- APFC procurement
- Spending cap

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Vice-Chair Gara requested projections for how each of the items would impact future dividends.

Commissioner Hoffbeck spoke to modelling that would be presented in the committee the following day.

Representative Wilson asked why the CBR management, APFC procurement, and the spending cap had been removed from the current bill.

Commissioner Hoffbeck answered there had been concern the CBR was not generating great enough returns and that the Permanent Fund could generate higher returns if the CBR was moved there. He referred to a study done that stated that it was inconsequential whether the money stayed where it was or moved to the Permanent Fund, with similar costs and returns. It had earned more the previous year because it needed to be set aside in a safe and liquid fashion as it would be needed for government services. If it were sitting in the Permanent Fund, the same restrictions would apply. One of the things the Permanent Fund was not set up for was cash management on a daily basis - there was only one draw annually to pay the statutory net income into the earnings reserve. The DOR had to pay bills daily, and had a sophisticated cash management system in place. The structure would have to be recreated in the Permanent Fund, and did not exist at present. Once a fiscal plan had been developed, it could be approached much more aggressively and see similar strong returns.

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Commissioner Hoffbeck continued to answer the question from Representative Wilson. He addressed Permanent Fund procurement and the spending cap. The department agreed that the Permanent Fund should have the procurement exemptions, but felt that it did not need to be addressed in the current proposed legislation. The spending cap dealt with issues other than oil and gas revenues and the Permanent Fund dealt with a spending cap on other revenues that came into the UGF. It did not impact restructuring of the Permanent Fund but was a broader cap for all government spending and it was felt that it should be heard outside the current legislation.

Representative Wilson thought the spending cap was one of the most important parts of a current plan. She wondered why using the existing structure could not get to the same point, perhaps with a check in place in the form of a set amount.

Commissioner Hoffbeck replied he would address the question later in the presentation.

Representative Pruitt asked if the intent was to move money once per year or whether some kind of cash management of the ERA would be put in place.

Commissioner Hoffbeck answered that the idea was to create a structure where cash could be accessed as needed, rather than a large pool. The CBR could be the liquidity bank. The Department of Revenue (DOR) could borrow money from the CBR as long as it paid back the money by the end of the fiscal year. Once gains were realized, the money would be transferred over. A portion of the CBR would not have great returns due to the liquidity.

Representative Pruitt surmised the CBR could be managed by APFC as long as the money was paid back. He asked whether the issue was ensuring that DOR maintained control of the money. He spoke to the provision that the funds needed to be liquid. He wondered if the provision was statutory or constitutional.

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Commissioner Hoffbeck answered the department could manage the CBR without legislative action. The department had a robust cash management system for around \$400 million per

month, and tried to have liquid as short a period of time as possible. In order to move the CBR to the Permanent Fund, it would have to establish a process for doing the same thing, so it was a simpler process to leave it where it was.

Commissioner Hoffbeck turned to slide 26 and continued to address the bill summary. The bill outlined a long-term plan with three formulas. There were two components to the sustainable draw: 5.25 percent Percent of Market Value (POMV) draw and a draw limit. The sustainable dividend formula was 20 percent of UGF and 20 percent of the POMV to pay dividends. Inflation-proofing would become a four times draw process.

Commissioner Hoffbeck turned to slide 27 and continued to address the bill summary.

Co-Chair Seaton pointed to slide 26 and the 5.25 percent POMV sustainable draw formula. He pointed to the white paper, page 4, which gave average return of 5 percent. He asked the commissioner to address the average return.

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Commissioner Hoffbeck replied he would address the question on slide 28.

Vice-Chair Gara discussed the constitutional requirement to put 25 percent into the CBR. He furthered that at some point the amount for new fields had been changed to 50 percent, but former Representative Norm Rokeburg had subsequently reduced the requirement back to 25 percent. He asked why that did not succeed.

Commissioner Hoffbeck answered the previous bill had a trigger which calculated that the reduction in the deposit into the corpus would reduce an individual's dividend by \$7 and had an automatic trigger which shut it off after a few years.

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Commissioner Hoffbeck addressed slide 27 and highlighted that 25 percent of the royalties would go into the principle of the fund. As with the current structure, statutory net income would be how the money from the principle of the fund moved into the ERA. The ERA would pay into the General Fund rather than into the dividend fund

under the legislation, making it available for appropriation, and under the 20/20 formula, 20 percent of the POMV draw and 20 percent of the monies outside the corpus would create the dividend. Money would flow through the General Fund into the dividend fund, rather than directly into the dividend fund. The other difference was in the inflation-proofing transfer from the ERA back into the principle, where in the current legislation there was a four times draw structure. The reason they had tried to limit the number of changes as much as possible was to give confidence to the public of the plan's durability.

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Commissioner Hoffbeck moved to slide 28 and spoke to the 5.25 POMV draw. The average fund value was calculated by using the first five of the last six years and the 5.25 percent was applied to that average to determine the fund draw. For 2012 to 2017, the average fund balance was \$48.1 billion, 5.25 percent of which was \$2.5 billion for paying dividend and government expenditures.

Representative Guttenberg asked about the reasoning behind the formula.

Commissioner Hoffbeck answered that using the first five of the six years avoided trying to calculate for the most recent year, which would not be fully audited and closed out when it was needed. He returned to addressing slide 28 stating 5.25 percent of \$48.1 billion was \$2.5 billion. As long as the fund was increasing in value, that equated to a 4.7 percent draw for 2017. He conceded the method was aggressive, but thought it was sustainable.

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Commissioner Hoffbeck turned to slide 29 and addressed what would happen if there was a POMV draw that was added to current revenue. The chart showed the impact of oil revenues. The bottom line of the chart represented oil prices. The full earnings reserve draw was needed in order to get to the high \$3 billion and to close the gap enough. If oil prices reached \$95 to \$100 per barrel, the draw would not be needed; the draw would be shut off during those times.

Representative Wilson did not understand why all of the other changes were necessary. She believed the yellow portion of the chart reflected the 5.25 percent.

Commissioner Hoffbeck answered in the affirmative: the yellow represented the 5.25 percent POMV draw. The blue was current revenues from oil and gas, and the green represented other revenues.

Representative Wilson asked whether there would be a sustainable budget without all of the other changes in the bill.

Commissioner Hoffbeck answered in the affirmative. He stated that few were forecasting oil prices higher than \$55 per barrel. He underscored that the graph was not a time series, but represented various price points for oil per barrel.

Representative Wilson stated the way she read the chart meant they were not that far off. She did not believe they needed to go much further and could reach a sustainable budget without necessarily making all of the changes in the legislation.

Commissioner Hoffbeck answered that current oil prices were about \$55 per barrel. They were not facing \$65 per barrel in future years. The average price for the current year was \$50 per barrel. The chart represented a spot in time. He pointed out the yellow bar was net a \$1,000 dividend.

Representative Wilson requested the actual dollar amount for 6 percent or other. She stated it was difficult to determine in the present graph.

Commissioner Hoffbeck replied that at \$60 per barrel oil (higher than current prices) and current spending, they were looking at a \$700 million gap, with a \$1,000 dividend, and \$1.3 billion gap with a \$2,000 dividend.

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Commissioner Hoffbeck mentioned that the draw limit was a very elegant solution that was developed in the hearing process, in Senate State Affairs committee during the previous legislative year. He explained that the draw limit reduced the POMV draw by a dollar-for-dollar basis, once

the UGF production taxes and royalties exceed \$1.2 billion. After that, the draw on the dividend would be reduced on a dollar-for-dollar basis on any additional oil and gas taxes and royalties that the state received, thereby slowly turning off the dividend draw as those revenues increase.

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Co-Chair Seaton asked if he was including the liability the state currently had for production tax credits.

Commissioner Hoffbeck responded in the negative.

Co-Chair Seaton clarified that the state would be limiting its revenue although the liability for tax credits could be increasing, depending upon expenditures decided on by third parties.

Commissioner Hoffbeck responded that the actual liability would come out of appropriation and would not slow when the above-mentioned trigger occurred. The amount of \$1.2 billion was actual severance tax and royalties without a deduction for credits.

Co-Chair Seaton was concerned with the idea of credits running the state into additional deficits. If the price of oil increased, one would expect more liability for the state, and it should be factored in.

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Representative Pruitt asked if credits were determined when DOR put out the Revenue Sources Book, or were deemed a UGF expenditure.

Commissioner Hoffbeck responded that it was portrayed in different ways in the book. He added that credits against liabilities were a revenue reduction and not an expenditure, and would appear as less revenue from oil and gas.

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Vice-Chair Gara was concerned about not being able to use the excess state revenue. He was wondering when the state would reach oil prices of \$70 per barrel.

Commissioner Hoffbeck was unsure if the state would cross the \$70 price point in the coming years.

Vice-Chair Gara asked if it was fair to assume it would be a least five years before the state saw \$70 per barrel.

Commissioner Hoffbeck agreed.

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Commissioner Hoffbeck continued to slide 31. Under the legislation, when the earnings reserve exceeds four times the annual POMV draw, the extra money gets deposited back into the corpus of the fund. The feedback loop becomes the inflation-proofing mechanism for the corpus of the fund. The draw would shrink as oil prices rise, the earnings reserve would grow faster, and the feedback loop would be reached earlier, giving more money into the corpus. As the corpus grows, the 5.25 percent draw increases. Eventually the fund begins to grow at a faster rate. It did restrict revenues early on, and \$1.2 billion was a compromise made with the Legislative Finance Division. There was a limited amount of money in the system. He agreed that the bill did not allow for a capital program. There was not enough money to cover it and expenditures.

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Commissioner Hoffbeck spoke to a sustainable dividend formula on slide 32. The bill guaranteed a \$1,000 dividend for the first two years. Subsequently, it would be 20 percent of UGF royalties, plus 20 percent of the 5.25 percent POMV draw. He moved to slide 33 titled "Inflation Proofing Transfers":

- AS 37.13.145(c) currently provides for annual inflation proofing transfers from the ERA to corpus
- The ERA needs a sufficient balance to be able to meet the draw each year ("ERA durability" concern)
- Bill provides that the ERA balance over 4 times the maximum 5.25 percent draw (after current year draw) is transferred to corpus instead

Commissioner Hoffbeck elaborated on slide 33. He referred to a question from Vice-Chair Gara earlier related to

multiple years of bad returns. The four times draw coupled with the three-year review period allowed the department to take corrective action if needed before the fund was fully depleted.

Representative Pruitt asked how long it would take to get to the point illustrated, under the current scenario. He asked if it could be an ongoing scenario.

Commissioner Hoffbeck replied that he would follow up.

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Commissioner Hoffbeck turned to slide 34 titled "Timing Matters":

- Review framework in three years
- Immediate effective date (potentially in FY17)
- Timing of transfers:
  - In the past, appropriations from the ERA occurred in the FY prior to using the money, i.e., the dividend was forward-funded. For example, money for the October 2015 dividend (paid during FY16) was appropriated on June 30, 2015 - the last day of FY15.
  - To accommodate the UGF use, the appropriation from the ERA will now occur in the same FY. In other words, instead of the FY18 ERA appropriation being used in FY19, it will be used for FY18.

Commissioner Hoffbeck spoke to an accounting anomaly that had occurred in FY 16. The dividend payment for FY 16 had been funded in the FY 15 budget. In the FY 16 budget the legislature had stopped forward-funding the dividend; the FY 17 dividend had been paid in FY 17. There was a hole in FY 16, which did not show a transfer of the dividend. Some of the slides showed a different balance related to the dividend. The LFD and OMB followed the statutory provisions, which is the transfer did not occur in FY 16, but the Permanent Fund records reflect a transfer in FY 15, resulting in a difference in numbers.

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Commissioner Hoffbeck provided a conclusion on slide 36:

- Sustainably provides billions to the general fund (when needed)
- Preserves the dividend program
- Stabilizes the budget to give investors confidence in our future

Commissioner Hoffbeck elaborated on the slide. As long as a fiscal plan was not complete, there would always be investor concern. The private sector was very clear that it wanted to see a complete fiscal plan. Slide 37 included a sectional analysis:

- Section 1: Review framework in 3 years
- Section 2: Royalties to the principal
- Section 3: Conforming Amendment (CA)
- Section 4: POMV and draw limit formulas
- Section 5: CA
- Section 6: Appropriations from ERA to general fund and principal
- Section 7: Dividend appropriation (20/20 formula)
- Section 8: CA
- Section 9: CA
- Section 10: \$1,000/person dividend in 2017 and 2018
- Section 11: CA
- Section 12: CA
- Section 13: CA and repeal language re. CBR investment

- Section 14: CA
- Section 15: Immediate effective date

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Co-Chair Foster pointed to slide 28 that included a POMV calculation. He asked for an example of how all the calculations worked and how they would be equated to how the dividend was paid out. He was interested in the spreadsheet that had been used to model the information.

Vice-Chair Gara referred to his earlier request related to a 10-year projection for dividends under each of the bills and asked for a spreadsheet.

Commissioner Hoffbeck answered in the affirmative.

Representative Ortiz asked for a quick summary on the draw limit.

Commissioner Hoffbeck pointed to slide 30. Once \$1.2 billion is received through severance taxes, royalties not going into the corpus, for every additional dollar received from oil taxes and royalties, the draw from the dividend is reduced by one dollar.

Representative Ortiz asked how tax credits related to the formula, and how often the \$1.2 billion marker was reached.

Commissioner Hoffbeck replied that he would bring modelling in to present to the committee.

Representative Guttenberg asked about production tax and royalties. He wondered whether modelling would show what it would look like if it had been raised above \$1.2 billion. He asked about the extent of an artificial spending cap.

Commissioner Hoffbeck answered in the affirmative. The answer came with a secondary calculation as in order to allow for a larger cap, it would start at a lower point and required less than 5.25 percent draw due to the feedback loop.

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Representative Grenn pointed to slide 33 regarding inflation-proofing. He asked about the decision for the bill to provide that the ERA balance over four times the maximum 5.25 percent draw, which would be transferred to the corpus instead.

Commissioner Hoffbeck answered there was no downside to having at least one extra year's revenue in the fund so the fund would not be depleted in the three-year time period. The department chose the time period because it wanted the review to occur within one gubernatorial term, to avoid new staff having to make decisions at the time of the deadline.

Representative Pruitt referred to the presentation's mention that 5.25 percent was aggressive. He asked if the risk in the current budget resided with oil taxes and the volatility of oil prices.

Commissioner Hoffbeck answered in the affirmative.

Representative Pruitt asked about putting risk in the Permanent Fund by being aggressive with the POMV number. He asked what pressure was placed on APFC.

Commissioner Hoffbeck answered it would change the dynamic at APFC and would add scrutiny to its annual returns. He did not believe it was overly aggressive but simply used as much revenue as possible under the existing process. The corporation would feel pressure in a down year. He did not want to be so concerned that the fund ended up being underutilized.

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Representative Pruitt asked for verification that he would agree with giving some of the procurement tools to the Permanent Fund.

Commissioner Hoffbeck answered "absolutely."

Vice-Chair Gara had been surprised the four times draw was a political calculation.

Commissioner Hoffbeck answered that the four times draw was not political calculus, just the three-year review period. They wanted to ensure that there was at least one review period within every gubernatorial cycle.

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Co-Chair Seaton surmised that inflation-proofing would not take place for a number of years. He asked for the calculus behind the method.

Commissioner Hoffbeck answered if the Permanent Fund met its 6.95 percent projected return, the fund would grow with inflation, even with the draw occurring. Without the inflation-proofing loop, putting money into the corpus, eventually the earnings are realized and would flow out of the fund. Even though there would not be a deposit back into the corpus in the first few years, it is expected that the fund would grow at a rate that would account for inflation and for the draw. The feedback loop is needed to take the money from where it can be spent to the corpus where it would be locked up for perpetuity. The fund itself would grow with inflation, but the corpus is not inflation-proofed without that feedback loop.

Co-Chair Seaton pointed to page 2 of the legislation where distributable income was deleted but not net income. He asked if the POMV was just to have transfers to the earnings reserve and the draw was not based on the item. He was trying to determine the calculation. He pointed to page 2, Section 3, line 17.

Commissioner Hoffbeck asked for clarification.

Co-Chair Seaton referred to the calculation of net income. He asked if the sole purpose of the net income calculation was to determine what went into the earnings reserve.

[3:04:00 PM](#)

Commissioner Hoffbeck answered in the affirmative. He detailed the statutory net income calculation is for how much is moved out of the fund for appropriation. The entire POMV process could be done without that component. They left it in to ensure the public that they were not jeopardizing the fund and in fact the bill would be cleaner if it were simply 5.25 percent of the five-year average was available for appropriation. It had been included to give comfort that the administration was not doing something sneaky.

Co-Chair Seaton looked at slide 29 of the presentation related to the POMV draw and restriction. He asked if the purpose was to limit future legislatures' ability to carry out infrastructure and deferred maintenance so that any other monies had to come from other revenue sources.

Commissioner Hoffbeck answered in the negative. The purpose was to avoid hyper-inflating spending in years with high oil prices. It flattened revenues available for government spending. It allowed the feedback loop for inflation-proofing. It allowed to draw more knowing that the earnings reserve would feed back into the corpus and kept from overheating government spending. There was only so much available to spend in a given year.

[3:07:01 PM](#)

Representative Kawasaki mentioned capital budget years and suggested there were also large operations budget additions. He referred to an extra \$1,200 dividend provided by former Governor Sarah Palin [for energy costs]. He discussed the spike in the price of energy with oil prices at \$80 to \$90 per barrel.

HB 61 was HEARD and HELD in committee for further consideration.

Co-Chair Foster addressed the schedule for the following day.

#  
ADJOURNMENT

[3:08:40 PM](#)

The meeting was adjourned at 3:08 p.m.