

HOUSE FINANCE COMMITTEE
January 31, 2022
1:38 p.m.

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CALL TO ORDER

Co-Chair Foster called the House Finance Committee meeting to order at 1:38 p.m.

MEMBERS PRESENT

Representative Neal Foster, Co-Chair
Representative Kelly Merrick, Co-Chair (via teleconference)
Representative Dan Ortiz, Vice-Chair
Representative Ben Carpenter
Representative Bryce Edgmon
Representative DeLena Johnson
Representative Bart LeBon
Representative Sara Rasmussen (via teleconference)
Representative Steve Thompson
Representative Adam Wool

MEMBERS ABSENT

Representative Andy Josephson

ALSO PRESENT

Brian Fechter, Deputy Commissioner, Department of Revenue;
Pam Leary, Director, Treasury Division, Department of Revenue.

SUMMARY

PRESENTATION: SAVINGS ACCOUNT/BUDGET RESERVES/INVESTMENT FUNDS

Co-Chair Foster reviewed the meeting agenda.

^PRESENTATION: SAVINGS ACCOUNT/BUDGET RESERVES/INVESTMENT FUNDS

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BRIAN FECHTER, DEPUTY COMMISSIONER, DEPARTMENT OF REVENUE, introduced himself.

PAM LEARY, DIRECTOR, TREASURY DIVISION, DEPARTMENT OF REVENUE, provided a PowerPoint presentation titled "Update on Investment Funds and Cash Flows," dated January 31, 2022. She began on slide 3 with an update on state investment funds. She planned to discuss historical asset balances of state funds and pension funds. Additionally, the presentation addressed key investment statistics. She noted the funds were all managed at the Treasury.

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Ms. Leary moved to slide 4 and reviewed a chart showing the Constitutional Budget Reserve Fund (CBRFF) and historical invested assets since inception in 1990. The blue section of the chart reflected the main fund, and the yellow section reflected the sub-fund. She noted the sub-fund had been created in 2000, but substantially funded in 2008 with a \$4.1 billion deposit. The CBRFF had been used to fund temporary cashflow expenses as well as budget revenue shortfalls. She detailed that \$960 million from the fund had been used in 2021 to help with a revenue shortfall. She highlighted appropriations from the fund were required to be repaid. As of the FY 20 year end financial statements, the fund was owed \$12.8 billion. She relayed there was no time period for the repayment and no interest accrued to the fund.

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Ms. Leary advanced to slide 5 showing key investment statistics. Currently the CBRFF target asset allocation was funded to 100 percent cash equivalents (i.e., money markets, treasury bills, etcetera). The fund had a very short investment horizon, meaning the Department of Revenue (DOR) anticipated funds could be used within a very short time period. As of December 31, 2021, the market value was nearly \$1.1 billion. She noted the slide showed the fund's market value history for the past five years. As of the end of December, the rolling one-year return was 0.09 percent and the short-term projected return for the year was 0.05 percent.

Representative Edgmon stated it was his understanding that the CBRF was the state's checking account. He detailed that

money flowed in and out of the account monthly to deal with needs around the state.

Ms. Leary clarified that the General Fund acted as the state's the checking account and the CBRF was the savings fund. She explained that money had been transferred from the CBRF to the General Fund in the past five years to make the state's payments. She noted that the CBRF was sometimes referred to as the "rainy day" fund.

Representative Edgmon believed that in the past the CBRF had been used as a source to fund the state's needs for cash flow purposes. He remarked he had been at the House Finance Committee table when the discussions had taken place. He stated that no one could answer how much money should be in the account to provide certainty funds were available in the event of a drop in oil prices or other. He highlighted appropriating funds from the CBRF required a three-quarter vote by the legislature. He remarked that DOR did not need the legislature's approval to use funds in the short-term on a monthly basis. He stated that a frequently asked question was how much money should be in the CBRF. He wondered if an \$800 million balance was sufficient as a safeguard if the Higher Education Investment Fund was lost. He wondered whether the balance should be higher in case oil prices fell.

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Mr. Fechter replied that DOR was comfortable with a balance of about \$1 billion for cash flow. He relayed the department considered the amount to be sufficient to weather two years of oil price volatility. He noted there would be additional detail later in the presentation. The presentation would address revenue anticipation borrowing and other mechanisms to assist the state if it was not possible to maintain a \$1 billion minimum CBRF balance.

Vice-Chair Ortiz asked if the December 31, 2021, CBRF balance of approximately \$1.1 billion reflected the sweep balance.

Ms. Leary answered in the negative, the amount reflected cash balance only. She elaborated that the June 30 sweepable fund transfer had not yet been done on a cash basis. The department was awaiting guidance from the state's annual financial report coming out in February to

help identify where funds should be moving and in what amounts.

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Ms. Leary addressed Power Cost Equalization (PCE) historical invested assets on slide 6. She detailed that the PCE Endowment Fund had been funded in 2000, 2007, and 2012. The purpose of the fund was to provide stable financing for affordable levels of electric utility costs in otherwise high-cost service areas of the state. She relayed that the target allocation had moved from 7 percent to 5 percent, which coincided with a change to a 5 percent percent of market value (POMV) appropriation for the fund. She detailed that if prior year earnings exceeded the target, 70 percent of the difference could be spent on related identified programs, including community assistance programs, renewable energy grants, and bulk fuel revolving loan funds. She noted the amount could not exceed \$55 million annually. The amount had been \$1.15 billion at the end of June 30.

Ms. Leary discussed PCE Fund investment statistics on slide 7. She detailed that the fund was longer-term [than the CBRF] with an intermediate investment horizon. The fund was targeted with a higher risk return with a 56 percent equity/44 percent bond asset allocation. As of the end of December, the market value was about \$1.1 billion and one year return was 7.12 percent. The projected 10-year return was 5 percent.

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Ms. Leary advanced to slide 8 and discussed the Alaska Higher Education Investment Fund. The fund had been created in 2012 with a capitalization of \$400 million. She detailed that the fund was to be swept as of June 30 and DOR was awaiting guidance. She elaborated that the fund was still invested as it had been previously. Once DOR received guidance, it would determine how the funds could move over to the CBRF.

Ms. Leary moved to slide 9 showing investment statistics for the Higher Education Investment Fund. She detailed that the fund was invested for a high risk return with a long investment horizon (despite any forthcoming changes to the fund). As of the end of December, the fund balance was \$422

million, the one-year return was 12.55 percent, and the projected 10-year return was 5.62 percent.

Representative Wool asked for the withdrawal rate on the Higher Education Investment Fund. He asked if there was a set formula. He observed the fund had been capitalized with \$400 million in 2012 and the current balance was \$422 million. He asked how much of the earnings were taken annually.

Ms. Leary believed the allowable appropriation amount was up to 7 percent annually. She estimated the annual withdrawal amount to be in the \$30 million to \$40 million range.

Mr. Fechter added that the amount varied but tended to be \$30 million to \$40 million per year.

Representative Wool asked if the spend was based on need by the given number of students. He observed that the projected 10-year return was 5.62 percent, while the appropriation amount could be up to 7 percent. He wondered whether it depended on how many students applied and qualified. He added that he certainly wanted the funds to go out.

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Mr. Fechter answered that over the years there had been a number of discussions about the long-term sustainability of the withdrawal rate. He relayed the money was only spent if there were enough seats in the Washington, Wyoming, Alaska, Montana, and Idaho (WWAMI) program and students qualifying for the [performance] scholarship. He explained that any unspent funds at the end of a year would lapse back into the Higher Education Investment Fund. He elaborated that the Office of Management and Budget (OMB) and the Legislative Finance Division (LFD) were monitoring the situation on an ongoing basis to ensure the fund was not drawn beyond its long-term earning capability.

Representative Thompson remarked that 10 additional students were being added to the WWAMI program. He asked if it would have a substantial impact on the draw from the fund.

Mr. Fechter responded that because many of the sweepable funds had been swept, the governor had replaced the spending items with unrestricted general funds (UGF) in his proposed budget. He explained that it would not be an additional draw from the Higher Education Investment Fund because in theory it had already swept. The administration viewed the situation as positive for some of the students because there was a cost benefit between General Fund and Higher Education Investment Fund funding of the programs. He expounded that because the fund was designated general fund (DGF) it did not receive the level of scrutiny that a UGF appropriation would. On the other hand, funding through DGF made it susceptible to the three-quarter reverse sweep. The department believed funding the program with UGF provided a bit of certainty to students relying on the scholarships.

Representative Thompson referenced a pending lawsuit. He provided a scenario where the lawsuit reversed the sweep of the funds back into the Higher Education Investment Fund. He asked if it was necessary to add language to the budget stating that the funding source would be reversed if the lawsuit were to occur.

Mr. Fechter answered the question was purely mechanical and related to the budget structure, which was at the will of the legislature.

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Representative Edgmon thought it was an excellent point in terms of a contingency measure because the outcome of the court case was not yet known. He asked for verification that the funds would remain in the CBRF if the lawsuit determined the Higher Education Investment Fund was swept.

Ms. Leary replied affirmatively.

Representative Edgmon remarked that the program had started in 2013, but he did not believe the Higher Education Investment Fund had been considered sweepable in its first six to eight years. He asked if his understanding was accurate.

Mr. Fechter replied that he would have to look into the question. He noted there had been a number of iterations

across multiple administrations about what the legal analysis of the moment deemed sweepable or not sweepable.

Representative Edgmon believed his previous statement was accurate. He stated that the Dunleavy administration had determined the fund to be sweepable, but it had not been considered sweepable during the Parnell or Walker administrations. He remarked there was an uncertain arbitrary nature in terms of what was or was not sweepable. He highlighted that if the courts decided the fund was part of the CBRF and was to be swept, it meant the legislature had to come up with the money annually. He pointed out that it was adding \$20 million or more to the budget annually because the legislature's only recourse was to pay the money out of UGF. He asked if he was missing something.

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Mr. Fechter agreed that in the absence of having the endowment to fund the programs, another funding source would need to be identified. In the current budget, the governor had selected UGF.

Representative Edgmon observed that the change effectively meant switching the \$400 million pot of money from an expected return rate of 5.6 percent [in the Higher Education Investment Fund] to a rate of 0.05 percent [in the CBRF]. He remarked that it was unfortunate.

Vice-Chair Ortiz referenced Representative Wool's question related to the amount withdrawn from the account annually. He highlighted that Mr. Fechter had stated the number of people who qualify for the scholarship fund or the WWAMI program had an impact on the withdrawal amount. He asked if the number of individuals receiving funding could be cut off at a certain point in order to maintain the fund's health and avoid an overdraft. Alternatively, he wondered if it was purely dictated by the number of people who qualified each year.

Mr. Fechter believed it was a flat dollar amount put into the budget where the Department of Education and Early Development and Alaska Commission on Postsecondary Education (ACPE) developed an estimate of the amount needed to fully fulfill the earned scholarships and WWAMI slots. He elaborated that if student numbers came in low, the money would remain in the fund for future use. Conversely,

he believed there was a buffer built into the numbers if the student numbers came in high. The buffer was aimed at avoiding a situation where there were more obligations than spending authority. He noted the supplemental budget process was an option as well.

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Representative Wool remarked that 10 to 20 WWAMI students represented a small portion of the overall fund draw. He surmised the majority of the fund recipients were undergraduate students at the University of Alaska Fairbanks.

Mr. Fechter confirmed that the lion's share of the funds went to the performance scholarship recipients and largely prospective University of Alaska students. Over the years there had been some off-designation appropriations from the fund. For example, one year, the funding for the Public Employees' Retirement System (PERS) and Teachers' Retirement System (TRS) pension obligations came from the fund. He elaborated that periodically over the years some related programs such as Online with Libraries and Live Homework Help had been appropriated from the fund. He noted it depended on the year and how the budget process progressed.

Representative Wool stated that he had not been aware of the anomalies. He stated that perhaps the appropriation use was perfectly within the defined use of the fund. He referenced a line item in the FY 23 budget to fund all of the scholarships without the withdrawal from the fund. He remarked that if the fund was swept, it would contain no earnings available to pay for the scholarships. He stated the amount currently in the budget was for performance scholarships and WWAMI. He asked for the number.

Mr. Fechter replied that he did not have the number on hand but would follow up with the information. He noted the figure was in the normal range. He added that a few seats had been added to the WWAMI program; therefore, the amount would be an uptick from the previous year.

Representative Wool asked if paying PERS and TRS and other things from the fund was an anomaly or something that occurred more frequently.

Mr. Fechter answered that the payment had occurred under the previous administration and was an anomaly. He elaborated that for the most part, the legislature tended to stick with designations written in statute. He furthered that occasionally for ease of budgeting there were anomalous funding events.

Representative Wool could understand how online libraries could be attached to education. He thought paying for PERS and TRS was a larger leap.

Representative Edgmon remarked that the state was looking at having some surplus funding in the current year. He asked if it would take statutory change to put some of the surplus funding into the Higher Education Investment Fund. He did not believe the action would require statutory change; however, he believed expanding the purpose of the fund would likely take statutory language.

Mr. Fechter agreed that changing the designation of the fund would take a statutory change. He noted that the legislature was permitted to spend funds outside of the designation due to the anti-dedicated funds clause within the state constitution.

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Representative Edgmon stated his understanding that the legislature would not be prohibited from capitalizing the fund further.

Mr. Fechter agreed.

Ms. Leary advanced to slide 10 showing historical invested assets of the General Fund and Other Non-Segregated Investments (GeFONSI). She explained there were two GeFONSI components. She detailed that GEFONSI II was created in 2018 to target a higher risk return profile for a subset of funds. There were approximately 180 funds managed together in the two GeFONSI components, but they were accounted for separately. As of December 31, 2021, there was about \$3.5 billion in total GeFONSI funds. She elaborated that the General Fund was included in the group of GeFONSI funds and had been about \$1.6 billion at the end of June; however, the fund had been reduced to about \$600 million by July because it was the state's working capital account.

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Ms. Leary turned to investment statistics on slide 11 for GeFONSI I and II investments. She highlighted that GeFONSI II had a 6 percent allocation to equity and a slightly higher fixed income allocation slated for a slightly higher return. The combined total in the two GeFONSI components was \$2.8 billion at the end of December. The returns for the year ending December 31 were -0.35 percent for GeFONSI I and 0.85 percent for GeFONSI II. The short-term return projections were 0.27 percent for GeFONSI I and 0.91 percent for GeFONSI II.

Representative Edgmon referenced the location of the community assistance funds. He clarified he was asking about the fund itself and not the money that came from PCE in the event of a surplus. He asked if the community assistance funds resided in the GeFONSI accounts.

Ms. Leary responded affirmatively.

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Ms. Leary addressed the Public School Trust Fund on slide 12. The fund was funded by one half of one percent of state receipts from the management of state lands, mineral leases, rentals, and royalties. The fund was established in 1978. She detailed that it had previously been managed as two separate principal and interest funds, but it was currently managed as one fund. She elaborated that the fund was managed under a POMV method. She explained that 5 percent of the average market value for the five years preceding the last previous fiscal year was used to make payments from the fund to provide an offset to the K-12 formula funding. The amount was roughly \$32 million for FY 23.

Representative Wool asked if the \$32 million was used to augment other general funds used to fund education.

Ms. Leary agreed.

Ms. Leary turned to slide 13 showing the Public School Trust Fund investment statistics. The fund had a long investment horizon with a target asset allocation of 69 percent equity and 31 percent fixed income. As of December 31, the balance was \$850 million with a rolling one-year

return of 12.56 percent, and a ten-year target return of 5.62 percent. She noted the previous year there had been discussion about the introduction of a state investment review board started by the DOR commissioner. She relayed the board was coming up on its sixth meeting to go over the investments under the commissioner's fiduciary care. She elaborated that the Investment Advisory Council for the state's pension funds had been providing guidance separately to the state funds. She explained that meetings included discussion on the asset allocations. She noted that meeting information and minutes were available on the DOR website.

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Ms. Leary advanced to slide 14 showing historical assets for PERS and TRS including pension and health Defined Benefit plans, totaling \$31.7 billion on June 30, 2021. Slide 15 showed investment allocations for the retirement funds. She highlighted there was a much more diverse target asset allocation for the retirement funds when compared to many of the state funds. She detailed that 49 percent was allocated to public equity, 30 percent was allocated to private equity, and 21 percent was allocated to fixed income. At the end of December, assets for defined benefit and health care plan were \$22.5 billion for PERS and \$10.8 billion for TRS. She pointed to the 24.64 percent returns at the end of September, which were calculated by DOR's performance consultant Callan Associates. She noted that as of December, DOR's internal returns were closer to 19 percent.

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Ms. Leary discussed cash flows on slide 17. She reminded committee members that the Cash Management Section and Treasury Division managed all of the banking relationships and cash flows in and out of the state, in addition to forecasting all of the expected cash positions on a daily basis. She clarified that discussions about funds or money movement within the Treasury pertained to cash balances, not the amounts in the annual financial report or the budget. She explained that the cash balance was the money in the bank at a given point in time.

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Ms. Leary moved to an illustration on slide 18 reflecting money moving in and out of the General Fund into the Division of Treasury. Cash inflows included tax revenues and federal dollars for things like Medicaid and grants on their way to various funds.

Representative Edgmon asked for verification that the initial Coronavirus Aid, Relief, and Economic Security (CARES) Act federal funding had been deposited into the state Treasury in 2020.

Ms. Leary agreed.

Representative Edgmon asked if the same was expected with the federal infrastructure money.

Mr. Fechter answered that he would confer with the infrastructure lead Miles Baker and would follow up with the committee.

Representative Edgmon stated he would be very interested in the response. He was interested to find out if there was a sense of timing.

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Ms. Leary moved to slide 19 and addressed cash flow deficiencies. She noted that historically many of the incoming funds went into the General Fund and remained there for working capital account purposes. She explained that the monies were put into the budget to spend money from the General Fund for different purposes; however, many sub-funds had been created over time to segregate cash for specific purposes, which had resulted in less cash available to pay day-to-day operating costs. She explained that expenditures could occur prior to the receipt of revenue, resulting in cash flow timing mismatches. She highlighted federal programs required expenditures before reimbursement for things like Medicaid and transportation costs.

Representative Edgmon asked if there were any sub-funds associated with the Statutory Budget Reserve (SBR).

Ms. Leary answered that the SBR was part of the sub-funds within the GeFONSI.

Representative Edgmon asked for verification that the SBR was not considered sweepable based on the court case the previous August.

Ms. Leary agreed.

Representative Wool asked for verification that a balance was needed in the CBRF in the event of cash flow deficiencies. He surmised funds could be used from the CBRF when the state was short on cash and repaid when revenues came in.

Ms. Leary confirmed the CBRF was one of the sources for filling gaps in addition to the ERA. She intended to address the issue in more detail later in the presentation.

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Ms. Leary advanced to slide 20 and discussed cash deficiency memorandum of understanding (MOU) developed between DOR, OMB, the Department of Administration, and the Department of Law. She explained that the MOU walked through the process DOR would take when dealing with the deficiencies. She detailed that the target cash flow balance had a floor of \$400 million. She explained that the number had been developed over time and provided coverage for two days of high volume outflows in the event cash calls all occurred at one time. She elaborated that the MOU addressed temporary interfund borrowing including transfers from the SBR, CBRF, Permanent Fund Earnings Reserve Account (ERA), or General Fund sub-funds.

Ms. Leary explained that the transfers were targeted at temporary short-term cash flow mismatches where DOR anticipated incoming revenue that would be used to make the funds whole again. She explained that in the event of a revenue shortfall without a backstop in the budget bills, measures would need to be taken to address the issue. The department would first seek legislative action [through the governor] to access additional funds through an appropriation, supplemental, or other cash reserves. She explained that disbursements may have to be limited if additional funds could not be secured.

Representative Edgmon recalled committee discussion the previous summer about the possibility of a government shutdown and the administration's ability to move money around outside of the legislature's appropriation authority. He remarked that DOR had the ability to move money around. He believed DOR had the ability to tap into the CBRF. He asked about the process of using funds from the CBRF without an appropriation from the legislature.

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Mr. Fechter believed the situation Representative Edgmon was referring to for a variety of previous government shutdown scenarios spoke to the fact that DOR could only access the CBRF for inter-year cash flow "lumpiness" without the three-quarter vote temporarily. He explained that the method could not be used to fill a systemic ongoing deficit; DOR would need to have some certainty the revenues would eventually come in within that fiscal year to use the CBRF as a cash management tool.

Representative Edgmon provided a hypothetical scenario where the effective date for the annual operating budget failed to get the required two-thirds vote. He stated that DOR would still have some tools to move money around to cover expenses to some degree until the effective date naturally came into law in 90 days [after the passage of the budget].

Mr. Fechter replied affirmatively, but with a number of caveats. He explained there were borders for interfund borrowing. For example, DOR could not borrow more than it could anticipate coming in. For example, if there was an issue with funding appropriations supported by tobacco fund, DOR could use the interfund borrowing tool, but not to a greater degree than anticipated incoming tobacco receipts.

Representative Edgmon remarked the state had some tools at its disposal [to cover expenses] in the event the operating budget effective date clause did not pass. He thought the subject may bear further examination by the committee as a contingency measure because it was unknown whether the two-thirds vote could be obtained.

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Representative Wool referred to Representative Edgmon's mention of the potential for the effective date clause to fail. He considered the situation was a legislative roadblock and not a cash flow deficiency. He remarked that it was not a shortage of revenue problem. He referenced Representative Edgmon's statement that the bill would become law after a given number of days [without the passage of the effective date]. He remarked that the revenue would be available, but the issue was about giving the authority to spend the money. He thought it was a different problem than cash deficiency.

Mr. Fechter agreed it was a bit of a different problem and there had been competing legal opinions on the topic over the years.

Representative Wool asked if temporary interfund borrowing from the SBR, CBRF, and ERA was arbitrary or written in a descending order of preference. He stated that the committee heard [throughout time] that the CBRF was the "slush fund" where cash could be used up to a certain amount and replaced. He was not aware the ERA could be used for that purpose.

Ms. Leary answered that it had changed over the years depending on the department's borrowing authority. She stated that with the ERA providing much of the state's revenue for the past several years, it was generally the first source DOR utilized at present unless there had been an anticipated deficit. For example, in 2021, DOR had borrowed money from the CBRF first up to the anticipated deficit amount. Subsequently, DOR had taken money from the ERA in order for the money to earn more with the Alaska Permanent Fund Corporation (APFC) for a longer period of time.

Representative Wool stated his understanding of Ms. Leary's response. He asked for verification that the ERA was the first go-to for necessary funds because it was already funding government. He asked if it lessened the importance of maintaining a higher CBRF balance. He thought the [recommended] \$1 billion CBRF balance was for cash flow needs.

Ms. Leary answered she did not know that it had an impact on what the state wanted to keep as a rainy day fund. She elaborated there was change continuing to occur annually in

terms of what the ERA would be used for. She noted that the amount going to state government was not quite decided. She highlighted the importance of a rainy day fund and noted there were many ways to calculate what the amount should be. The current view was the balance should be about \$1 billion.

Representative Wool stated that having a rainy day fund was an appropriate and apt concern. He recalled when oil prices had been in the negative. He thought the situation would potentially qualify as a need for a rainy day fund and other circumstances.

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Ms. Leary moved to slide 21 and continued to discuss cash flow deficiencies. The use of budget reserve funds had been the solution for cash flow mismatches and revenue shortfalls for many years. She noted that the solution had shifted more to the ERA. She highlighted that the CBRF balance had been fully repaid by 2010 and borrowing had recommenced in FY 15. As of the annual financial report in FY 20, the amount owed to the CBRF was \$12.8 billion.

Representative Edgmon recalled there was no requirement for a payment plan or a date. He described money owed as a "big IOU out there" with really no specificity attached.

Ms. Leary agreed.

Representative Wool asked for verification that paying the \$12.8 billion back would not really change anything. He surmised it meant there would be \$12.8 billion sitting there [in the CBRF] that the legislature could use for the next rainy day.

Mr. Fechter agreed. He detailed it was a debt the state owed itself. To the extent there were ongoing deficits annually, it would make the need to balance the CBRF go on in perpetuity. Whereas, if a sustainable fiscal plan was achieved resulting in a balanced budget, the \$12 billion would far exceed the amount needed for revenue volatility management.

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Representative Edgmon remarked the situation was another example of how the legislature was bound by laws passed in a different era. He believed the CBRF language had passed in 1990. He highlighted that if the legislature recapitalized the \$12.8 billion, it would be foregoing the ability to put money in the Higher Education Investment Fund (with a 5.62 percent target return) or putting money into the ERA that earned close to 30 percent the previous year. He pointed out that from an investment perspective, the situation was a little out of kilter.

Ms. Leary highlighted the concept of the sub-fund for the CBRF. She detailed that currently the CBRF had a 100 percent cash equivalent target asset allocation. She explained that there had been a much different asset allocation in the past, including monies going to the sub-fund in 2008, which had a significantly higher target return. She stated there were mechanisms to invest the money, but the sub-fund could only be utilized if the funds were not needed for about five years.

Representative Edgmon pointed out that the CBRF was also bound to certain liquidity thresholds, meaning the fund could not be invested as a more diversified portfolio like the pension funds. He stated in essence the department was bound to a low earning, stable, and low risk fund.

Ms. Leary agreed it was true for the main [CBRF] fund.

Representative Edgmon thought it was interesting that the state's primary savings account appeared to be outdated relative to other existing funds that were nimbler and had a higher earning capability. He recalled in 1990 when the CBRF was viewed as the state's fiscal plan where every last dollar was swept into the "concrete vault" the legislature could not access without a three-quarter vote. He stated that times changed and continued to change. He pointed out that the Permanent Fund may have been in its best return decade possibly ever, which everyone hoped was not the case.

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Representative Wool recalled a court decision had been made that settlement money was deposited into the CBRF, which helped build up its balance. He stated it was different than the original fund structure. He used a hypothetical

example where the funds from a \$50 million settlement between the state and an oil tax corporation were deposited into the CBRF. He believed the court decision had helped build up the CBRF.

Mr. Fechter agreed the mechanism existed; however, he clarified it was written into the constitution and was not the result of a court decision. He explained that any settlement of mineral leases, bonuses, rents, and other natural resource type revenues were to be deposited into the CBRF. He detailed that any court cases he was aware of dealt with more definitional type matters such as what counted as a bonus sale.

Representative Wool asked if there were events that caused the CBRF to grow apart from any deposits by the legislature. He remarked that the graph [showing the CBRF balance] was flat for many years and then shot up.

Mr. Fechter answered there had been some sizable settlements deposited into the fund over the years. He relayed that in previous years, when the CBRF balance had been much higher, the sub-fund had a substantially more aggressive asset allocation. The fund had benefited from positive investment earnings over the years until it had been drawn down to the current level. He stated the situation had precluded the fund from having a more aggressive, long-term asset allocation.

Representative Wool thought there was a court interpretation as to what defined a settlement. He would look into it.

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Ms. Leary addressed revenue volatility on slide 23. She relayed that projected FY 22 revenue was comprised of approximately 65 percent investment earnings and 25 percent petroleum revenues. She detailed there was uncertainty every year regarding petroleum revenues due to price and production fluctuation and volatility. There was certainty related to investment fund earnings for FY 23 due to the lagging POMV formula associated with money coming from the ERA; however, there was investment return uncertainty in FY 24 and beyond. She noted that volatility had played its part over the years in terms of the amount of revenue coming into the state.

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Ms. Leary moved to slide 24 and reviewed volatility management techniques. She detailed that access to savings funds and other funds had helped with the situation. She remarked that fiscal tools could be modernized to include lines of credit in addition to revenue anticipation notes. She noted there was current legislation that would add lines of credit. Other techniques included managing the timing of ERA transfers to the General Fund and managing timing of expenditures. She elaborated that the Cash Management team closely managed cash flows and money was only taken from the ERA when it was needed. The department managed the timing of expenditures as it had done in the past with the Public Education Fund, which used to be an annual draw at the beginning of July but had moved to a quarterly and monthly draw.

Co-Chair Foster noted that Representative LeBon had joined the meeting.

Representative LeBon asked about the status of HB 92 and SB 73 related to lines of credit and revenue anticipation notes.

Mr. Fechter answered that the bills had passed the House and were currently in the Senate Finance Committee.

Ms. Leary turned to slide 25 and provided takeaways on cash flows. She stated that even with balanced budgets and if all revenue was received, cash flow timing mismatches would continue to occur throughout the year. She highlighted that like most forecasting, cash flow forecasting was always wrong. She relayed that revenue shortfalls could occur if forecasted assumptions were wrong. Additionally, higher revenue volatility required greater cash reserves until volatility decreased. She stated the good news was volatility management techniques were available.

Co-Chair Foster noted that Representative Carpenter had joined the meeting.

Representative Edgmon thought it would be interesting to see the historical percentage of UGF funding for state government, beginning the late 1970s when oil first flowed through the pipeline and the state income tax had been

repealed around 1982. He referenced the current UGF revenue estimated at 65 percent investment earnings, 25 percent petroleum revenues, and 10 percent non-petroleum revenues. He thought someone along the way, including the legislature, deserved a pat on the back for playing a big role in reducing the volatility. He reasoned that the Permanent Fund performance had been great, and the legislature had put a significant amount of money into the fund via special appropriations and inflation proofing. Additionally, the legislature had not taken the allowable 50 percent each year for spending on the capital and operating budget. He believed it was significant that the state's volatility picture had been reduced via sound financial management.

[2:45:11 PM](#)

Representative Edgmon looked at slide 15 related to the PERS and TRS investment allocations and returns. He pointed to the bottom of the slide, which showed an actuarial assumed rate of return of 7.38 percent. He asked if the rate was higher than the Permanent Fund.

Ms. Leary answered that the actuarial assumed rate of return was part of the economic assumptions that went into identifying the funding status of the pension plans. The number was one of the department's targets and there was another target of 6.89 percent based on the asset allocation, which differed from APFC. She elaborated that APFC was at CPI plus 5 percent (above 6 percent). She continued that the pension funds and the Permanent Fund had well-diversified allocations, but each had different purposes, liquidity needs, and structures. She informed the committee that the 7.38 percent had been derived in the last experience study the pension plans and Alaska Retirement Management Board (ARMB) were currently going through to determine the number for future actuarial determinations.

Representative Edgmon thought it illustrated the unpredictability of inflows and outflows. He pointed out that healthcare costs could rise unexpectedly. He referred to money coming in from Tier I and II employees. He guessed there were still over 30,000 people participating in the plan. He compared the pension plans to the Permanent Fund with the predictable 5 percent annual payout. He observed there was much more unpredictability built into the pension

plans, which he speculated was the reason for the difference in investment strategy.

Co-Chair Foster thanked the department for its presentation. He reviewed the schedule for the following day.

ADJOURNMENT

2:48:57 PM

The meeting was adjourned at 2:48 p.m.