

ALASKA STATE LEGISLATURE
HOUSE JUDICIARY STANDING COMMITTEE

Anchorage, Alaska

June 4, 2021

1:04 p.m.

MEMBERS PRESENT

Representative Matt Claman, Chair
Representative Liz Snyder, Vice Chair
Representative Harriet Drummond (via teleconference)
Representative Jonathan Kreiss-Tomkins (via teleconference)
Representative David Eastman (via teleconference)
Representative Christopher Kurka
Representative Sarah Vance (via teleconference)

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE JOINT RESOLUTION NO. 7

Proposing amendments to the Constitution of the State of Alaska relating to the Alaska permanent fund, appropriations from the permanent fund, and the permanent fund dividend.

- HEARD & HELD

PREVIOUS COMMITTEE ACTION

BILL: HJR 7

SHORT TITLE: CONST. AM: PERM FUND & PFDS

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

02/18/21	(H)	READ THE FIRST TIME - REFERRALS
02/18/21	(H)	STA, JUD, FIN
04/20/21	(H)	STA AT 3:00 PM GRUENBERG 120
04/20/21	(H)	Heard & Held
04/20/21	(H)	MINUTE(STA)
05/04/21	(H)	STA AT 3:00 PM GRUENBERG 120
05/04/21	(H)	Heard & Held
05/04/21	(H)	MINUTE(STA)
05/06/21	(H)	STA AT 3:00 PM GRUENBERG 120
05/06/21	(H)	Moved CSHJR 7(STA) Out of Committee
05/06/21	(H)	MINUTE(STA)
05/10/21	(H)	STA RPT CS(STA) 4DNP 2NR 1AM

05/10/21	(H)	DNP: CLAMAN, EASTMAN, VANCE, TARR
05/10/21	(H)	NR: STORY, KREISS-TOMKINS
05/10/21	(H)	AM: KAUFMAN
05/14/21	(H)	FIRST SPECIAL SESSION BILL
05/14/21	(S)	FIRST SPECIAL SESSION BILL
05/24/21	(H)	JUD AT 1:00 PM GRUENBERG 120
05/24/21	(H)	Heard & Held
05/24/21	(H)	MINUTE (JUD)
05/26/21	(H)	JUD AT 1:00 PM GRUENBERG 120
05/26/21	(H)	Heard & Held
05/26/21	(H)	MINUTE (JUD)
06/02/21	(H)	JUD AT 1:00 PM ANCH LIO DENALI Rm
06/02/21	(H)	Heard & Held
06/02/21	(H)	MINUTE (JUD)
06/04/21	(H)	JUD AT 1:00 PM ANCH LIO DENALI Rm

WITNESS REGISTER

ANGELA RODELL, Chief Executive Officer
 Alaska Permanent Fund Corporation
 Juneau, Alaska

POSITION STATEMENT: During the hearing on CSHJR 7 (STA), provided a PowerPoint presentation, titled "The Alaska Permanent Fund," dated 6/4/21.

CURTIS THAYER, Executive Director
 Alaska Energy Authority
 Anchorage, Alaska

POSITION STATEMENT: During the hearing on CSHJR 7 (STA), provided a PowerPoint presentation, titled "Power Cost Equalization," dated 6/4/21.

MIKE BARNHILL, Deputy Commissioner
 Department of Revenue
 Juneau, Alaska

POSITION STATEMENT: Provided testimony and answered questions during the hearing on CSHJR 7 (STA).

RICK HALFORD
 Aleknagik, Alaska

POSITION STATEMENT: Provided invited testimony pertaining to CSHJR 7 (STA).

ACTION NARRATIVE

[1:04:28 PM](#)

CHAIR MATT CLAMAN called the House Judiciary Standing Committee meeting to order at 1:04 p.m. Representatives Drummond (via teleconference), Snyder, Kreiss-Tomkins (via teleconference), Eastman (via teleconference), Vance (via teleconference), and Claman were present at the call to order. Representative Kurka arrived as the meeting was in progress.

HJR 7-CONST. AM: PERM FUND & PFDS

[Contains discussion of SJR 6.]

[1:05:43 PM](#)

CHAIR CLAMAN announced that the only order of business would be HOUSE JOINT RESOLUTION NO. 7, Proposing amendments to the Constitution of the State of Alaska relating to the Alaska permanent fund, appropriations from the permanent fund, and the permanent fund dividend. [Before the committee was CSHJR 7(STA).]

[1:06:45 PM](#)

[Due to technical difficulties, sound was lost briefly.]

[1:08:24 PM](#)

ANGELA RODELL, Chief Executive Officer, Alaska Permanent Fund Corporation, provided a PowerPoint presentation, titled "The Alaska Permanent Fund" [hard copy included in the committee packet]. She recalled that in the late 1990s, the generally accepted accounting principles changed to include the fair market value concept into the definition of income, which meant that the concept of unrealized gains and losses had to be included as well. She said that created an "interesting conundrum" for the permanent fund and how it was accounted for, ultimately leading to the two-account structure that is used today. She directed attention to slide 2, "two Account Structure," which read as follows [original punctuation provided]:

Principal

- is constitutionally established as the permanent part of the Fund
- grows through royalty contributions, special appropriations, and inflation proofing
- is to be used only for income-producing investments

Earnings Reserve Account

- is statutorily established to hold the net income from the Fund's investment portfolio
- grows through the receipt of statutory net income - monthly cash inflows from investments and net income from asset sales
- is available for Legislative appropriation

MS. RODELL noted that the principal account cannot shrink through changes in market value.

[1:10:42 PM](#)

MS. RODELL continued to slide 3, "Principal Contributions," which read as follows [original punctuation provided]:

\$17.8 Billion Royalty Deposits - AS 37.13.010(a)(1) and (a)(2)

The constitutionally minimum required 25% of royalty proceeds, and the statutorily mandated deposits of 50% for leases after 1979.

\$18.0 Billion Inflation Proofing - AS 37.13.145(c)

The inflation proofing calculation is based on deposits into the Principal of the Fund and the inflation rate as calculated per statute.

\$11.0 Billion Special Appropriations - AS 37.13.010(a)(3)

Legislative Deposits from both the General Fund \$2.7 B and the ERA \$8.3 B.

MS. RODELL stated that the principal has grown as a result of the appropriation activity that has taken place around it. She further noted that \$4 billion of the \$8.3 billion in special appropriations was the appropriation that came through in fiscal year 2020 (FY 20).

[1:12:28 PM](#)

MS. RODELL proceeded to slide 4, "ERA: Statutory Net Income," which read as follows [original punctuation provided]:

AS 37.13.140 (a) directs the net investment earnings of the Fund to the ERA and excludes unrealized gains and losses.

Statutory Net Income is the direct result of investment activity, and includes:

- Monthly cash inflows from stock dividends, bond interest, and real estate
- Realized Capital Gains/Losses: All the net income (i.e., realized gains minus realized losses) generated by the sale of investments.

FY21 as of April 30, 2021

- Statutory Net Income = \$5,995,200,000

MS. RODELL pointed out that the graph on slide 4 demonstrates how statutory net income (SNI), which is how the earnings reserve account (ERA) grows, moves differently than total return. She explained that the total return reflects the volatility in the market, as indicated by the yellow line, while the SNI steadily increases after a withdrawal, as indicated by the black line. She noted that as of April 30, 2021, the SNI is almost on par with 2018 at nearly \$6 billion. In 2018, the increased SNI was due to a specific asset sale that generated a large gain whereas the current SNI in FY 21 is due to a rebalancing effort to manage risks appropriately.

[1:13:55 PM](#)

MS. RODELL advanced to slide 5, "Investment Management," which read as follows [original punctuation provided]:

Constitutional and Statutory Mandates

- Principal provides permanent savings
- ERA holds the investment income for appropriation
- Prudent rules govern Saving, Spending, and Growth

APFC Stewardship

- Quasi-independent
- Long-term horizon -Prudent Diversification
- Accountability
- Resources

MS. RODELL pointed out that the permanent fund is managed as if it were one total fund; therefore, the investment management strategy does not differ for the ERA versus the principal. She related that investment allocation is looked at from a 10-plus-year view rather than day-to-day or month-to-month. She added that this strategy requires the Alaska Permanent Fund Corporation (APFC) to be accountable and ensures that the necessary resources are available to work effectively.

[1:15:30 PM](#)

MS. RODELL progressed to slide 6, "Asset Allocation." She explained that in 1980, the [investments were comprised] almost entirely of bonds. In 1983, APFC was allowed to invest in U.S. real estate and stocks, which over time, expanded into international markets. In 2005, statutes were passed that allowed APFC to take more risks and to invest in private equity, absolute return, and private income. She reported that today, the FY 21 target allocation is 39 percent stocks and [21] percent bonds. She added that the entirety of assets managed by APFC, including the Alaska Mental Health Trust, ERA, and the principal, are all invested in the asset allocation with each pool of money owning a pro rata share of every investment. She reported that reconciliation takes three to four weeks, as there are over 700 accounts with multiple investments.

[1:17:34 PM](#)

MS. RODELL turned to slide 7, "Resolutions 03-05, 04-09," which read as follows [original punctuation provided]

POMV

- Supporting a constitutional amendment to limit the annual Fund payout to not more than a 5% POMV averaged over a period of 5 years.
- Implementation of a constitutional POMV spending limit for the Fund, has the accompanying benefit of assuring permanent inflation proofing of the Fund.

MS. RODELL explained that the constitutional amendment under current consideration [CSHJR 7(STA)] would transition the fund from a two-account structure to a single account structure, which has been a priority of the trustees since 2000. She reminded the committee that the accounting rules changed in the late 1990s, at which time, APFC realized the importance of holding on to its gains; therefore, appropriations for inflation would no longer be needed and spending would be limited naturally as result of the percent of market value (POMV) structure.

[1:18:57 PM](#)

MS. RODELL detailed the fund's current structure on slide 8. She proceeded slide 9, which illustrated the proposed endowment structure. She explained that under the endowment structure,

all of the funds that come in would be constitutionally protected and remain that way while continuing to be invested into income-producing investments. Furthermore, gains and losses would stay with the fund while POMV and corporate expenses would move out. She emphasized that the proposed endowment structure is a simpler and more straightforward way to manage the fund.

[1:20:36 PM](#)

REPRESENTATIVE KREISS-TOMKINS pointed out that Ms. Rodell had mentioned the Alaska Mental Health Trust's pro rata ownership. Further, he referenced an amendment to the operating budget that pertained to other state assets that could be managed for return by APFC. He questioned the pros and cons of placing additional state accounts or public assets under management of the Alaska Mental Health Trust under APFC management.

MS. RODELL said APFC is prepared to manage additional state assets should it be necessary. She explained that depending on what the assets are, they could be placed in the asset allocation unless the money that comes in has different usage requirements, such as statutory duration limits. She said APFC could make it work, but it requires resources.

[1:24:41 PM](#)

REPRESENTATIVE EASTMAN inquired about the costs that are withdrawn from the fund by APFC, as well as the POMV withdrawals, and their associated timelines.

MS. RODELL responded that the APFC operation and investment management moneys are taken in accordance with the adopted budget documents, which serve as the cap/limitation. She added that APFC withdraws them throughout the fiscal year as needed; for example, for APFC's personal services, the required distribution is taken out of the ERA every couple of weeks for the purpose of payroll. Regarding the POMV withdrawal, she said that those moneys are taken out in accordance with a memorandum of understanding by the Treasury Division under the Department of Revenue (DOR). She reported that each year since the POMV statutes were adopted in 2018, APFC has worked with the Treasury Division to set up the withdrawals based on the division's expected cash needs. She noted that the division has the ability to change those withdrawals.

[1:27:20 PM](#)

CHAIR CLAMAN asked if unrealized gains are included in the calculation of the fund and the ERA's total value.

MS. RODELL answered yes. She noted that the next slide [slide 10] shows that figure. She added that calculation is based on net market value, which includes unrealized gains/losses.

CHAIR CLAMAN asked whether the change to the definition of earnings that occurred in the late 1990s impacted how the fund looked at unrealized and realized gains for purposes of earnings versus the principal.

MS. RODELL explained that it required the legislature to come up with the definition of SNI to better understand what was considered income and what would be moved into the ERA. She said there were times when all of the gains/losses were recognized in the ERA and a time when they were recognized in the principal; however, for the past few years, they have been shared pro rata between the two accounts until they're realized due to the different interpretations that have been received from the Department of Law (DOL). She relayed that investing grew more sophisticated compared to what was contemplated when the original constitutional amendment was passed, which became part of the challenge. She emphasized the importance of the POMV structure to the permanent fund because it recognizes all the different asset classes that are currently invested.

CHAIR CLAMAN questioned whether the income account was originally named the ERA or if it was given that name at a later point in time.

MS. RODELL said as long as she has been aware of it, the account has been named the ERA.

[1:31:03 PM](#)

CHAIR CLAMAN asked whether the deposit of \$18 billion for inflation proofing pursuant to AS 37.13.145(c) has been made every year.

MS. RODELL noted that inflation was zero in 2010, so there was no inflation proofing deposit. Additionally, there were no inflation proofing appropriations in 2017, 2018, and 2019. In FY 20, she said, the \$4 billion that was moved from the ERA to the principal had legislative intent language to forward fund inflation proofing. Furthermore, she pointed out that there is

no inflation proofing in the FY 21 budget or either version of the operating budget for FY 22, which is currently in conference committee.

CHAIR CLAMAN sought to clarify that in 2017, 2018, and 2019, there was inflation; however, the legislature did not make the deposit pursuant to AS 37.13.145(c).

MS. RODELL confirmed [that the legislature did not make that deposit in 2017, 2018, and 2019.]

CHAIR CLAMAN asked for verification that the ERA, because it needs to be available for appropriation, consists of more liquid appropriations and may not realize the same gains as the principal.

MS. RODELL said that is incorrect. She explained that every single asset is owned on a proportional pro rata share by the principal, the ERA, and the Alaska Mental Health Trust. She said the ERA has a long-time horizon on its asset allocation based on statutory directive.

CHAIR CLAMAN questioned whether sales are made consistent with the asset allocation or if the liquid assets are sold when cash is needed for state operations.

MS. RODELL stated that the POMV structure allows for the surety of knowing what the cash calls by the state are going to be, so APFC can plan ahead. She remarked:

If we know, for example, we are going to make a \$480 million payment at the end of June, as we're receiving cash this month, we'll hold on to it rather than investing it in the asset allocation in order to make that payment, so that we don't have to sell something at a gain or a loss in order to make those payments.

MS. RODELL noted that 60 percent of the fund is invested in highly liquid stocks and bonds that could be liquidated within three days.

[1:35:06 PM](#)

CHAIR CLAMAN referred to slide 6 and asked how [APFC] has the authority to change the asset allocation and what legislative action allowed that.

MS. RODELL explained that in APFC's enabling statutes, the legislature included a specific list of allowable investments. She expounded that in 1980, the statutes specified that APFC was only allowed to invest the fund in bonds. The list was amended over the years to include investments in U.S. stocks and U.S. real estate, for example. In 2005, she said, the statute was completely revised, and the allowable list of investments was repealed and replaced by the prudent investor rule, meaning that APFC could invest in anything a prudent investor of similar size and scope would invest in. Subsequently, that revision required APFC to adopt regulations outlining the types of allowable investments. She stated that now, APFC has regulations outlining and defining their investments; additionally, the corporation continues to follow the prudent investor rule, which led to the change in asset classes that appears in FY 21.

CHAIR CLAMAN concluded that in 1980, [investments were comprised] entirely of bonds, which changed over the years. Going forward, the legislature would periodically change the statute giving APFC the authority to invest in other types of investments. Finally, in 2005, APFC changed to the prudent investor rule, which gave APFC's board the authority to establish regulations that established how investments were made.

MS. RODELL confirmed.

CHAIR CLAMAN surmised that APFC has not been back to the legislature to change that authority since 2005.

MS. RODELL said that's correct. She said APFC does not require additional authority.

[1:37:41 PM](#)

MS. RODELL resumed the presentation on slide 10, which read as follows [original punctuation provided]:

Percent of Market Value -AS 37.13.140 (b)

- Based on market value, rather than realized income
- Subject to annual appropriation
- Predictable
 - average market value of the Fund for the first five of the preceding six fiscal years

5.25% -July 1, 2018, FY19; Effective Rate

- FY19 POMV \$2.72 billion; 4.13%

- FY20 POMV \$2.93 billion; 4.52%
- FY21 POMV \$3.09 billion; ~4.68%

5.0% -July 1, 2021, FY22; Effective Rate

- FY22 POMV\$3.07 billion; ~4.55%
- FY23 POMV~\$3.21billion; ~4.66%
- FY24 POMV~\$3.29billion; ~4.68%

MS. RODELL explained that as the fund grows or has flat growth, such as in FY 21 to FY 22, the POMV structure prevents "wild swings" in revenue for the state.

[1:38:59 PM](#)

MS. RODELL continued to slide 11, which highlighted the fund's growth from FY 16 to FY 21. She pointed out that the principal is unable to grow without support of the special appropriations. She added that once unrealized gains in the principal become realized, they move into the ERA. She advanced to slide 13, "Callan's Capital Market Projections," noting that Callan is the board's general consultant. She related that Callan's 10-year projection indicates that the total fund is expected to generate 6.75 percent, which will decrease to 6.2 percent. She stated that the forecast suggests that the fund will enter a 10-year period of much slower growth, adding that the bulk of the earnings will come from private equity and public equity. She said in order to run a diversified portfolio with a balance of risks, there needs to be (indisc.) absolute returns and fixed income. She added that at 2.25 percent, bonds are not going to generate much income in return over the next 10 years.

[1:42:19 PM](#)

MS. RODELL proceeded to detail the fund's performance as of April 30, 2021, on slide 14. She informed the committee that to date, the total fund is at 25.02 percent, which is a big difference in performance from 2 percent in FY 20. She stated that for the most part, the fund is meeting all its performance benchmarks. She highlighted that the board's long-term objective is to generate 5 percent real return plus inflation, which at 2.05 percent versus 5.65 percent, was not met last year.

[1:43:41 PM](#)

REPRESENTATIVE SNYDER asked how the fund's performance compares to similar funds in other locations. She questioned whether

there are any lessons the state could learn from similar funds and how Alaska's fund performance benchmarks an objective matchup with other funds across the nation.

MS. RODELL offered to follow up with the requested information. She noted that Callan conducts reviews of funds across the country such as endowments, foundations, and pension funds.

1:45:00 PM

REPRESENTATIVE EASTMAN inquired about the 5 percent POMV. He recalled that he had heard the perception that 5 percent is too high, and that 4.25 percent would be more sustainable. He acknowledged that the state could go forward with the 5 percent POMV and discover that it is not sustainable. He noted that Ms. Rodell had provided the committee a letter surrounding the "loyalties issue" and the legislature not meeting the statutory obligations regarding loyalty and asked whether she has another letter surrounding the inflation proofing to which the 5 percent might be eroding the corpus.

MS. RODELL responded that the concepts of having a corpus and the need for inflation-proofing would have to be eliminated in order to implement a constitutional amendment. She noted that these concepts are in place due to the two-account structure and a requirement for an appropriation to put money back into the principal. She explained that the only way the principal can grow today is through the action of the legislature. Under the endowment structure contemplated by HJR 7, she said that there would be no need for these concepts. She identified that the importance of the endowment structure in HJR 7 is that it eliminates the need for these concepts and there will be no need for legislative action to grow the fund. She emphasized that, regarding inflation-proofing, it's important to respect the legislative intent language. She acknowledged the concerns that "inflation will get away from us" [if inflation-proofing is not present].

REPRESENTATIVE EASTMAN asked whether Ms. Rodell has a number readily available as far as what the legislature could do under the current system to (indisc.) inflation-proofing obligations already in place.

MS. RODELL responded that she doesn't have the number in front of her at the moment but that she will follow up and provide that information to the committee.

REPRESENTATIVE EASTMAN asked Ms. Rodell whether it can be expected that, if the 5 percent figure passes and is revealed to be too high, the corporations will argue for a lower threshold. He asked what she thinks would occur in this situation.

MS. RODELL explained that the 5 percent is supported by the data on slide 14 [entitled, "Performance"] and the projections depicted therein show that it is a realistic number. The idea is that the growth of the fund smooths out over time and creates more stability for the fund. She noted that APFC has supported the 5 percent number for over 20 years.

REPRESENTATIVE EASTMAN asked Ms. Rodell whether the asset allocation currently includes future contracts and derivatives, and if so, how the assets would be classified.

MS. RODELL responded that derivatives and future contracts are included and usually happen within the same portfolio. She offered the example of currency exposure, which would be done through futures contracts. She noted that all of the exposures listed can be found in APFC's annual report.

[1:52:31 PM](#)

MS. RODELL resumed the presentation on slide 16, "Evolving Role of the Fund," which read as follows [original punctuation provided]:

Successful SWFs operate within a rules-based system that allows them to perform a combination of saving, stabilization, and income-generation functions.

In Alaska, the latter function has come into sharper focus, as the Fund income supports the State budget in an era of lower oil revenues.

This paper proposes a number of reforms that will strengthen the stability and sustainability of Alaska's Permanent fund:

LESSON # 1: MISSION CLARITY
LESSON #2: THE IMPORTANCE OF RULES
LESSON #3: SUCCESSFUL ENFORCEMENT OF SAVING RULES
LESSON #4: DESIGNING A POMV SPENDING RULE
LESSON #5: REFORMING THE ERA

[1:53:14 PM](#)

MS. RODELL advanced to slide 17, "Revenue Generation," and acknowledged that this type of revenue generation [referenced on the slide] is a different concept "culturally" for everyone and it is not common to think of the permanent fund as the primary source of revenue for the state. The slide read as follows [original punctuation provided]:

Now, more than ever, the State is dependent upon APFC's effective management and investment of the Alaska permanent fund, one of Alaska's primary sources of renewable revenue.

The POMV draw from the Earnings Reserve Account now supports ~70% of Alaska's undesignated general fund budget.

APFC's stewardship fulfills dual roles -

Protecting the Principal of the Fund for the benefit of current and future generations of Alaskans.

Providing a predictable revenue stream to help balance the State's budget.

[1:54:32 PM](#)

REPRESENTATIVE KREISS-TOMKINS asked Ms. Rodell if she could restate the historic figure of the real return of the permanent fund [seen on slide 14, "Performance"], and how that number compares to the projections done by Callan.

MS. RODELL responded that the Callan's projections are looking at a 4.2 percent real return for the next 10 years. She stated that the intention of the APFC Board of Trustees is to be able to meet Callan's forecasts. She acknowledged that it is going to be a challenge to meet the 5 percent real return in a low growth and slow return environment, and there is concern about that, but APFC is not recommending any changes to the 5 percent number.

[1:58:08 PM](#)

REPRESENTATIVE VANCE asked Ms. Rodell what trustees would consider when evaluating whether a one-time unstructured draw can be taken without undermining the health of the growth of the fund.

MS. RODELL answered that the trustees are adamant in the recommendation that there be no unstructured draws on the fund at all, no matter the size or the reason. She said that part of the concern is that every year, if there are unstructured draws, the POMV would lose all of its effectiveness.

[1:59:16 PM](#)

REPRESENTATIVE SNYDER, regarding the proposed \$3 billion bridge draw that's referred to in HJR 7, asked Ms. Rodell to specify the particular losses that would be incurred with a draw of that size.

MS. RODELL responded that it is important to recognize that the role of the APFC is to manage the assets it has. She noted that the withdrawal would have a cost impact on the fund. She shared that the Legislative Finance Division has run various scenarios on potential losses to give a sense of their magnitude. These are the decisions that are beyond APFC, she said.

CHAIR CLAMAN announced that the committee would proceed to a presentation on power cost equalization (PCE) from the Alaska Energy Authority (AEA).

[2:01:18 PM](#)

CURTIS THAYER, Executive Director, Alaska Energy Authority, provided a PowerPoint presentation, titled "Power Cost Equalization" [hard copy included in the committee packet]. He began on slide 2, "Who We Are," which read as follows [original punctuation provided]:

Created in 1976 by the Alaska Legislature, the Alaska Energy Authority (AEA) is a public corporation of the State of Alaska governed by a board of directors with the mission to "reduce the cost of energy in Alaska." AEA is the state's energy office and lead agency for statewide energy policy and program development.

MR. THAYER advanced to slide 3, "Power Cost Equalization," which read as follows [original punctuation provided]:

The PCE Program was established in 1985 as one of the components of a statewide energy plan to help "equalize" the high cost of electricity in rural communities with the lower costs in more urban areas.

MR. THAYER advanced to slide 4, "What is PCE?" which read as follows [original punctuation provided]:

- PCE helps ~82,000 Alaskans in ~200 rural communities with their high energy costs.
- The program seeks to reduce the high costs of electricity paid by rural consumers to a level comparable to an average of rates paid in Anchorage, Fairbanks, and Juneau.
- PCE ensures the financial viability of rural communities.
- Reliable lower-cost energy enhances the quality of life, the standard of living, and the economic strength of the communities.

[2:03:29 PM](#)

MR. THAYER proceeded to slide 5, "PCE Eligible-Communities," which depicted a map of Alaska showing eligible PCE communities, and read as follows [original punctuation provided]:

Residential and community facility customers in approximately 200 communities are eligible for PCE Credits

[2:03:57 PM](#)

MR. THAYER continued to slide 6, "PCE Program in Fiscal Year 2020," which read as follows [original punctuation provided]:

81,700
Alaskans benefited from PCE Credits
192
Communities were eligible for PCE Credits
\$29.6
In Fiscal Year 2020, \$29.6 million was disbursed

[2:04:27 PM](#)

MR. THAYER advanced to slide 7, "PCE Endowment Fund," which read as follows [original punctuation provided]:

- PCE disbursements are funded from the PCE Endowment Fund.
- Created and capitalized in Fiscal Year 2001, the

- PCE Endowment Fund is managed by the Department of Revenue.
- Alaska Statute 42.45.085 provides that five percent of the PCE Endowment Fund three-year average market value may be appropriated to the program.

MR. THAYER moved to slide 8, "PCE Endowment History (Thousands)," which included a table that tracked the history of PCE from 2016 through 2020. He noted that the fund is currently close to \$1.1 billion and has remained fairly consistent during the last five years.

[2:05:59 PM](#)

MR. THAYER stated that it is important to note that when one looks at the PCE endowment and sees \$1.1 billion [PCE fund balance for 2020], it is not evident that there has been a large amount of money invested by the state into urban infrastructure, which helps to lower the rates for everyone on the Railbelt [region in Alaska]. He added that AEA owns and operates the large "hydro" project in Alaska, which provides 10 percent of the Railbelt energy needs. He added that it was the result of an investment from the state of \$300 million. He noted this investment saves the Fairbanks consumers about \$40 million annually on energy costs. He reiterated that the \$1.1 billion figure is misleading due to the multitude of investments included in that number, which also include tax credits.

[2:07:39 PM](#)

CHAIR CLAMAN asked Mr. Thayer if he could speak about the governor's proposal to put these PCE funds into the permanent fund and manage it from the permanent fund.

MR. THAYER responded that this is something a subsequent testifier plans to address, but that inserting the PCE endowment into the corpus of the permanent fund is something that the Board of Directors of AEA has unanimously endorsed. He noted that when legislators decided not to reverse the sweep around three years ago and the PCE endowment got swept into the constitutional budget reserve, it caused concern in rural Alaska regarding energy costs. By putting the endowment into a "safe place," he shared his understanding that those concerns would be alleviated.

CHAIR CLAMAN invited questions from the committee.

[2:09:54 PM](#)

REPRESENTATIVE DRUMMOND shared her understanding that nearly 82,000 Alaskans benefit from PCE credits through residential energy costs. She asked about the cost of energy for institutions, such as schools, and whether these institutions benefit from a reduction in energy costs.

MR. THAYER asked for clarification on Representative Drummond's question.

CHAIR CLAMAN restated the question and asked whether community groups or organizations, such as schools, benefit from PCE credits.

MR. THAYER stated that strictly residential customers benefit from the PCE credits.

REPRESENTATIVE DRUMMOND pointed out that energy costs are so high in schools that staff members are being laid off. She asked Mr. Thayer what it would take to extend energy benefits to organizations, such as schools, that must function in the same high-cost environments as the residential energy consumers that benefit from the PCE credits.

MR. THAYER replied that it would take a statutory change and would possibly "double if not triple" the costs of the PCE program in Alaska.

[2:13:04 PM](#)

REPRESENTATIVE EASTMAN asked whether there is an available list of communities that are currently benefitting from the PCE credits, and what percentage of people residing in those communities are receiving the subsidies.

MR. THAYER answered that the list of currently benefiting communities is public information, along with other relevant statistics about these communities, and he would be happy to provide this information to Representative Eastman's office.

[2:13:58 PM](#)

REPRESENTATIVE SNYDER explained that she reviewed AEA's PCE program guide, updated in 2019, and pointed out that it states that 7 percent of the 3-year monthly average market value could

be appropriated. She asked Mr. Thayer whether this has been updated in statute, as that that number is 5 percent now.

MR. THAYER said the information that he has also identifies the 5 percent standard.

REPRESENTATIVE SNYDER referred to slide 8 of Mr. Thayer's presentation [titled, "PCE Endowment History (Thousands)"] and asked if he could speak about 2019 and 2020 "transfers and appropriations to other funds."

MR. THAYER replied that in FY 19, under statute, the first (indisc.) is May 1, and then up to \$30 million in community assistance is provided. He added that if there is additional revenue generated from that, it would be (indisc.), or it would go into the powerhouse upgrades. In this example, two years later, \$30 million was available. In 2020, there was \$14 million allocated by the legislature for non-rural investments, he explained, with around \$7 million to \$8 million of that investment going to the Department of Corrections (DOC). He offered to provide a breakdown of the FY20 statistics to the committee.

[2:17:23 PM](#)

REPRESENTATIVE VANCE asked for a description of AEA's past and future plans for energy solutions, specifically the original purpose of the endowment, and if there are any plans for energy solutions beyond subsidies in the future.

MR. THAYER replied that the endowment was originally established to help lower the cost of power in rural Alaska through the PCE program. The AEA as an entity intends to continue to look for ways to lower the cost of power in rural Alaska with renewable energy. He noted that these rural communities are often far apart, not connected by a grid, and lack the ability to receive energy via hydro power. For these reasons, the "backbone" of rural Alaska continues to be diesel, which requires powerhouses in order to have the most efficient diesel program as possible. He reiterated that the PCE program was established to help lower those costs, and the endowment intends to help rural Alaska to offset the costs of higher energy.

CHAIR CLAMAN noted that the committee would now hear invited testimony from Mike Barnhill of the Department of Revenue.

[2:20:47 PM](#)

MIKE BARNHILL, Deputy Commissioner, Department of Revenue (DOR), noted that for the purpose of his testimony, he would be referring to CSSJR 6(JUD), which proposed that the balance of the PCE endowment fund on June 30, 2023, would be transferred to the principal of the permanent fund and would be co-mingled with the assets of the permanent fund. It also proposes a constitutional dedication of revenue from (indisc.) to the purposes of power cost equalization in the state. He directed attention to language on page 2 [lines 7-11] of CSSJR 6(JUD), which read as follows:

(d) Each year, the legislature shall appropriate a portion of the amount appropriated under (b) of this section for power cost equalization. The amount appropriated shall be the amount necessary to equalize the cost of power in the State, according to State law, but may not exceed fifty percent of the amount appropriated under (b) of this section.

MR. BARNHILL explained that this is a mandatory representation of PCE, the details of which are intended to be provided by legislators through statute.

CHAIR CLAMAN invited questions from the committee.

[2:23:09 PM](#)

REPRESENTATIVE KURKA shared his understanding that PCE funds are used for the purpose of infrastructure projects to lower the cost of energy. He stated that it seems to him that this proposal would preclude [the energy cost saving measure] from happening by "locking up" the fund in the constitution. He whether this is correct.

MR. BARNHILL explained that the details of the implementation process would be specified by the legislature in statute. He shared his understanding that (indisc.) wouldn't "offend the language" in the constitution as proposed.

REPRESENTATIVE KURKA noted Mr. Barnhill's earlier comment that the PCE fund would be co-mingled with the permanent fund. He asked what the long-term consequences of that might be in terms of contributions to future dividends, and what would be preventing the endowment from pulling from the (indisc.) fund at large.

MR. BARNHILL offered clarification that if the PCE endowment fund balance were to be deposited and co-mingled with the permanent fund balance, there would no longer be a separate way to track the balance of each fund; it would simply be the permanent fund. In exchange, an important change is proposed for the constitution, and that is (indisc.) dedication. He noted that currently, the only revenue dedicated that is proposed in the constitution is 25 percent (indisc.) that is dedicated to the principal of the permanent fund. He explained that this would be a new dedication for which the legislature would specify the details, and the revenue would be dedicated from the permanent fund for the purpose of power cost equalization. He reiterated that the two accounts would become one and would no longer be separately trackable.

REPRESENTATIVE KURKA stated that it seemed to him that would make the PCE appropriation an unstructured draw. He argued that [the legislature] does not know what the dollar amount would be if (indisc.) could grow (indisc.).

MR. BARNHILL said the revenue dedication happens within the context of the POMV distribution. In other words, he continued, it is a portion of that, so it is entirely within the structured draw that is established, and CSSJR 6(JUD) indicates that 5 percent (indisc.) of the permanent fund.

[2:27:54 PM](#)

REPRESENTATIVE KURKA pointed out that when one looks at the Constitution [of the State of Alaska], the rights, benefits, and privileges are for all Alaskans. He recognized the original purpose of the PCE endowment in the fund is to bring a balance towards government investment for infrastructure for rural communities. He opined that this would be a dramatic change in the nature of the constitution because [the legislature would be] enshrining a subsidy program that is selective for certain regions of the state, for select Alaskans, not for all Alaskans. He expressed concern about going down the road of segregating people and treating them differently and having that major departure from current (indisc.)

MR. BARNHILL replied that the governor has suggested that the legislature consider the policy, and if the legislature supports it by a super-majority, it would be placed before the people for consideration in amending the constitution. Ultimately, he said, the constitution reflects the will of the people and, if the people decided to achieve equality or equalization in power

costs throughout the state, that is a fair topic to take up in the constitution.

2:30:27 PM

REPRESENTATIVE EASTMAN said currently, the PCE is addressed in statute (indisc.) reference to in the constitution. He asked if CSSJR 6(JUD) were to pass, which would add this dedicated appropriation to the constitution, would that create an entitlement to the constitution.

MR. BARNHILL expressed that his preference is to use the word dedication, because that is what it creates. He said he would leave it to others to decide if it also falls under the characterization of an entitlement. But, he said, as a constitutional dedication of revenues to a purpose, it has the force of constitutional law, which presumably could be enforced by the courts. He noted that the language as drafted, said "shall appropriate"; therefore, it cannot be circumvented by the legislature.

REPRESENTATIVE EASTMAN sought to clarify whether the intention of the governor, through CSSJR 6(JUD), was to create an expectation of a subsidy. He asked if the legislature were to maintain or update the statutes, what is to stop a person from coming in and saying that the expectation is bigger in the future than [what is] currently under statute. He maintained that [the current] language in CSSJR 6(JUD) is very broad. He stated his understanding that the language in CSSJR 6(JUD) indicates that the law is going to explain how the cost of energy is balanced throughout the state. He noted that there are only 191 communities that are currently in that program; nonetheless, he said he could see someone going to court because his/her costs are higher than the community next door, so he/she might want to be part of the program.

MR. BARNHILL suggested that Representative Eastman was proceeding into legal areas to which the DOL could speak. He offered his belief that in this particular case, the court would draw from the fact that PCE has been in statute for some decades. He said the court would probably interpret the constitutional provision from the statutory history to the extent that it appears the people sought to constitutionalize a particular program.

REPRESENTATIVE EASTMAN surmised that the governor's intent was to add what [is currently in statute] into the constitution;

therefore, he stated his belief that the language in [SJR 6] would not be so broad. He suggested discussing that with DOL. He questioned what would happen to the community assistance program, asking if that would go away under this new constitutional plan.

MR. BARNHILL clarified that the community assistance program is separate from the constitutional resolution. He explained that currently, it is funded by PCE. He added that funding the program in the future would remain a prerogative of the legislature's appropriation power. It is the administration's expectation, he answered, that the community assistance program would continue in its current form and continue to be funded.

[2:35:46 PM](#)

REPRESENTATIVE SNYDER asked if the legislature were to do the POMV draw with a 50/50 split between the dividend and the government, which would require satisfying the PCE payment, would that result in a lower amount of money being available for government services if [the PCE fund and the permanent fund] were combined as opposed to separate.

MR. BARNHILL replied that the amount that would (indisc.) be for PCE would essentially be what the legislature decided through statute and appropriations. He explained that the constitution requires amounts sufficient to equalize power. He added that the legislature decides what that amount is, so it could be greater or less than the amount today. He reiterated that it is committed to legislative discretion, and the balance of funding available to provide funding for PCE is the same before and after. In other words, he stated, there is money in the permanent fund that distributes POMV that would be added to the balance of the PCE fund, which is \$1 billion. He said it is up to the legislature to decide whether to do it formulaically, like it does now. He concluded that it would be up to the legislature to implement that through statute.

REPRESENTATIVE SNYDER pointed out that now, [the legislature] is in a situation where it is drawing from the same funds and doing a 50/50 split; further, it is funding both government and PCE from that split. She added, "Had the calculations been done to compare if there is any difference, however small, the distribution would be, if PCE maintained its own fund.

MR. BARNHILL said if he understood her correctly, in order to do that, [the legislature] would have to maintain some internal

separate balance for the PCE fund once it's shifted into the permanent fund, because right now, the PCE endowment fund has a POMV structure similar to what is being proposed for the permanent fund in the constitution. He explained that [the formula] is 5 percent of a three-year market value average of the fund. In order to maintain that formula, he said, [the legislature] would have to maintain some internal balance for the PCE fund once it was deposited into the permanent fund. Alternatively, he offered, [the legislature] could come up with a formulaic approach that would divide the POMV distribution every year, which is intended to equate to what is currently [being calculated by] the statutory formula. He suggested that there are mathematical ways of achieving a similar number before and after the deposit.

[2:40:04 PM](#)

CHAIR CLAMAN recalled earlier testimony from Ms. Rodell about APFC managing the Alaska Mental Health Trust funds and how essentially, they are mixed, but they are also segregated. He said APFC knows how much is allocated towards the Alaska Mental Health Trust. He then asked if [the governor] is proposing a similar proposal for the PCE. He suggested using similar structure in which [APFC] manages the money in the same way as the Alaska Mental Health Trust with certain percentage allocation of the total value of the permanent fund, which is managed by the PCE. He added that big dollars are managed by the fund but still kept separate from both the permanent fund monies and the Alaska Mental Health Trust monies.

MR. BARNHILL said he has not speculated why the proposal does not do that. He stated that perhaps, [there are] reasons that [the legislature] could spend more or less than (indisc.) today. He relayed that by not continuing the statutory formula in its current form, it provides greater legislative flexibility with respect to appropriation for PCE. He noted that the flexibility is governed by the "shall" language in this measure, which could result in a greater or smaller amount of money available for PCE, as long as it complied with the "shall" amount necessary.

CHAIR CLAMAN considered a scenario in which the legislature wanted to treat the PCE fund like other funds, such as the Alaska Mental Health Trust funds, and let [APFC] manage those funds, but also keep them on their own in the same way the Alaska Mental Health Trust funds are on their own. He questioned whether [the legislature] would need a constitutional change to do that by statute today.

MR. BARNHILL confirmed that the legislature could do that by statute today. He remarked that the benefit of [APFC's] method is that it's not maintaining separate massive allocations for the three accounts.

CHAIR CLAMAN interjected, concluding that essentially, the legislature would be creating a fourth account.

MR. BARNHILL continued by noting that as more accounts are added to the permanent fund, a potential issue would arise wherein [the accounts] may need different asset allocations because they have different risk preferences and different investment horizons. He posited that if the decision were that the risk preferences, risk tolerances, and investment horizons amongst the permanent fund, the Alaska Mental Health Trust, and the PCE fund are the same, [the legislature] could co-mingle it as it did today.

[2:44:28 PM](#)

RICK HALFORD, former Senate President in the Alaska State Legislature, informed the committee of his background and provided a history of the permanent fund and the dividend. He stated that he came to Alaska in the mid-1960s and graduated from Alaska Methodist University (AMU) in 1968. Subsequently, he went into the National Guard and became the owner/operator in an air-taxi business, as well as a guide. He shared that he was originally elected to the [Alaska House of Representatives] in 1978 and was the House Majority Leader when the final dividend passed in 1981. He was elected to the Alaska State Senate in 1982, where he was the Senate Minority Leader for one term, the Senate Majority Leader for four or five terms, Senate president, and a Senate Finance Committee Co-Chair.

MR. HALFORD opined that some people who advocate for the history of the permanent fund think [the legislators who first implemented the fund] are smarter than [the current legislators]; however, he claimed that that it is the opposite. He pointed out that [the current legislature] has forty years of information and history and the ability to carry the Library of Congress in [its pocket]. He declared that he is very grateful that [past legislatures] were able to pass on some of the largess.

MR. HALFORD said [the permanent fund] is a very important asset. He recalled that Alaska had a fairly aggressive state income

tax. He said [the state] was behind on a lot of things, but Alaska was getting the income tax and about one-third of the value of the oil. Today, he declared, [Alaska] is in a very different situation.

[2:47:05 PM](#)

MR. HALFORD mentioned that former Governor Jay Hammond is given a lot of credit for [the establishment of] the permanent fund, adding that he certainly deserves it "in the political push." Nonetheless, he noted, Elmer Rasmuson was a huge factor in how it was organized and how it worked. He said Mr. Rasmuson went around the state trying to get people to decide what it was for and there was never agreement. It is written in the permanent fund papers, he cited, that the only agreement was to have a savings account. He stated that people have added a lot of intent that really wasn't there.

MR. HALFORD said that initially, people who opposed the creation of the permanent fund were very quick to say that it was a loan fund, or they meant it was a subsidy to the government, or a dividend fund, [amongst other suggestions]. He reiterated that there was no agreement on what it was for. He then deferred to Chair Claman for questions.

[2:48:42 PM](#)

CHAIR CLAMAN inquired about the history of dividend formula. He asked Mr. Halford to divulge more about the original dividend formula and what changes the legislature made, both while the Zobel lawsuit was pending and before the decision, as well as what happened after that decision.

MR. HALFORD said the original formula gave [Alaskans] a share for every year since statehood using a differential residency formula that was struck down in the Supreme Court. He offered his belief that in 1981, the legislature passed what Governor Hammond considered "the backup formula," which was equal dividends for everyone.

MR. HALFORD said there were parts [of the dividend negotiations] that were contentious, such as the inclusion of minors, welfare, hold harmless, and inflation-proofing. He explained that looking back, the repeal of the state income tax probably represented a dividend of \$100,000 per year to the top one thousand taxpayers in the state of Alaska. He recalled that the first dividend was \$1,000, which was intended to make up for

three years that [the legislature] was in court. After that, the dividend went down to \$300-\$400. Today, that dividend would be somewhere over \$3,000, he suggested, if factored for inflation. He explained that it wasn't easy to make decisions, with regard to minors and the hold harmless aspect. He added that it had to be looked at in the context of everything else going on. He noted that [the state] was spending huge amounts of money on housing subsidies that, in some cases, were as much as \$15,000 to \$20,000 a year to people that could afford to build very expensive houses.

[2:51:41 PM](#)

CHAIR CLAMAN stated his understanding that after the passage of the first permanent fund constitutional amendment, there were some efforts to pass other constitutional amendments in the early 1980s to provide more structure in the constitution for the permanent fund. He asked Mr. Halford to discuss those efforts.

MR. HALFORD said in the late 1980s, there was a serious bump in the price of oil and the state's income. Jay Hammond was still alive, he noted, and the Senate put together a package that was sent to the House. He explained that the package included a constitutional spending limit update, the creation of the constitutional budget reserve [CBR], and a permanent fund allocation amendment, which the Senate called "40/30/30." He indicated that the plan specified that 40 percent of the income went to dividends, which matched what the actual amount going to dividends was at that time. He noted that because the balance was going up rapidly, it was based on a five-year average.

MR. HALFORD said the package passed the Senate and went to the House, but the House passed the CBR with a floor amendment that increased the required two-thirds majority to a three-fourths majority and did not pass either the spending limit or the constitutional amendment with regard to the permanent fund. So, he said, it has been a continuous debate. At that time, Governor Bill Sheffield had been elected after Governor Hammond. He recalled that the first place Governor Sheffield wanted to go for shortages was the permanent fund system; however, because that was so unpopular, he didn't do it. Mr. Halford then said that Governor Steve Cowper offered an education endowment to sideline some of the permanent fund's income. He said that if that had happened, the permanent fund would be worth about half of what it is worth today. Governor Hickel, he continued, said

that he would go to the ballot before he did anything, as well as Governor Tony Knowles.

[2:55:00 PM](#)

CHAIR CLAMAN inquired about the "40/30/30" plan.

MR. HALFORD replied that the legislature had maintained the realized income formula. He said it was 30 percent for inflation proofing, 30 percent for government appropriations, and 40 percent for dividends.

[2:55:40 PM](#)

CHAIR CLAMAN inquired as to the role of the dividend in the structure of Alaska's government today.

MR. HALFORD replied it is a huge benefit. He stated that Alaska has become very fortunate with all the oil value, adding that if Alaska is an owner-state, the shares of that ownership should be equal. One of the things that is not pointed out enough, he argued, is that there is not significant tax money in any of the permanent fund system; it is ownership money. If Alaska is an owner-state with owner-individuals, he continued, then the ownership should be just as important to somebody who holds a sign standing by Northern Lights Boulevard as somebody else. He stated that it is not tax money, and it never has been in any significant amount; furthermore, it is not taking from one person to give to another person. He explained that it is sharing the common property resources of an owner-state. He opined that when dealing with non-renewable resources, it is important to make a serious effort to look out for not just oneself, but [future generations].

[2:57:16 PM](#)

CHAIR CLAMAN questioned how to balance protecting the principal of the fund with paying a dividend.

MR. HALFORD opined that eventually, the statutory POMV will become unconstitutional when the reserve is gone, because one cannot reduce the value of the principal. He said that is at stake in this equation. He offered his belief that the solution must be a constitutional solution, which would bring the people into a final decision.

MR. HALFORD said the permanent fund must be permanent, which means whatever percentage or mechanism the legislature uses should never reduce the real value of the fund. Further, he stated his belief that it must be connected to the people. He recalled that when an elementary student used to announce the [annual] amount of the PFD on television, people did not argue if it went down because they recognized it was following the market. He said they felt included in the process. He went on to state that power, position, age, and longevity all help the rich get richer and the poor get poorer. He declared that [the legislature] tried to circumvent that as much as it could with the PFD, the hold harmless provision, and the minors' provision - and it worked. He said according to data, the difference between the rich and the poor in Alaska did not grow as astronomically as it did in the rest of the country.

CHAIR CLAMAN invited questions from the committee.

[3:00:29 PM](#)

REPRESENTATIVE SNYDER pointed out that Mr. Halford had acknowledged the utility and importance of constitutionalizing the permanent fund and putting it before the people as a way to finalize this ongoing conversation. She asked if that would include specifying within the constitution how it would be divided between the dividend and government services.

MR. HALFORD noted that the governor proposed the 50/50 [plan] and the 5 percent [POMV draw limit]. He said the 50/50 plan sounds good but expressed concern about the 5 percent. He suggested wording the 50/50 plan as follows: "No more may be appropriated for government than is appropriated to individuals through an equal dividend." He said that would give the legislature a defense against an entitlement argument. He went on to state that Alaska is "spoiled." He said there has been a complete generation [that didn't have to pay for government] because the cost was going somewhere else. Now, he said, [Alaskans] must recognize that they should have to pay for part of it; furthermore, they should make certain they are getting a fair share of resources. He said Alaska will have to look to its savings. He then argued that everyone has their own budget priorities and will defend the dividend until they are personally going to see a cut. He noted that those in high tax brackets believe that the dividend is their tax money going somewhere else. Alaska must face all these issues, he said, but it never will until the PFD and the fund itself are off the table. He offered his belief that people could go backwards

over time with court participation and destroy the entire system.

[3:04:40 PM](#)

CHAIR CLAMAN said he didn't know about the 40/30/30 plan and asked if there is merit to including inflation-proofing in the calculation.

MR. HALFORD offered his belief that [the legislature] should include inflation-proofing, particularly with a realized income formula. He suggested that [the legislature] could include a provision that said, "Every 'X' year, the inflation rate shall be adjusted to whatever the real inflation rate is." He stated that the term "permanent," which went before the voters, means just what it says. He argued that it is a lie to tell people they have a permanent fund if inflation "eats" it.

CHAIR CLAMAN thanked Mr. Halford for taking the time to testify before the committee.

[3:06:39 PM](#)

CHAIR CLAMAN announced that CSHJR 7(STA) was held over.

[3:07:09 PM](#)

ADJOURNMENT

There being no further business before the committee, the House Judiciary Standing Committee meeting was adjourned at 3:07 p.m.