

SENATE FINANCE COMMITTEE
February 4, 2021
9:01 a.m.

[9:01:19 AM](#)

CALL TO ORDER

Co-Chair Bishop called the Senate Finance Committee meeting to order at 9:01 a.m.

MEMBERS PRESENT

Senator Click Bishop, Co-Chair
Senator Bert Stedman, Co-Chair
Senator Lyman Hoffman
Senator Donny Olson (via teleconference)
Senator Natasha von Imhof
Senator Bill Wielechowski
Senator David Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Lucinda Mahoney, Commissioner of Revenue, Juneau; Angela Rodell, Executive Director, Alaska Permanent Fund Corporation.

SUMMARY

CONFIRMATION HEARING - COMMISSIONER OF REVENUE

ALASKA PERMANENT FUND CORPORATION

^CONFIRMATION HEARING - COMMISSIONER OF REVENUE

[9:02:46 AM](#)

LUCINDA MAHONEY, COMMISSIONER OF REVENUE, JUNEAU, provided the committee with her background and education.

[9:11:44 AM](#)

Co-Chair Stedman asked for information about the testifier's spouse, and his cooperation in the "Chinese wall" that was created to make it clear that there was a separation.

Acting Commissioner Mahoney replied that she was originally hesitant to accept the role of commissioner due to her husband's role as an oil and gas attorney. She stated that it was determined that an ethics screen would be established to screen her from any decisions made by the Department of Revenue (DOR) related to any case where her husband was the attorney.

Senator Wielechowski remarked on the issue regarding the Coronavirus Aid, Relief, and Economic Security (CARES) Act provision, which allowed corporations to apply for refunds on the net operating losses. He wondered when the department became aware of that issue, and asked about the expected costs to the state.

Acting Commissioner Mahoney responded that as soon as the provision was announced by the federal government, the department began analytics to estimate the impact. She recalled a presentation to the committee in 2019 where Dan Stickel [Chief Economist, Economic Research Group, Tax Division, Department of Revenue].

[9:14:54 AM](#)

Senator Wielechowski wondered whether any action should be taken to for a correction.

Acting Commissioner Mahoney replied that it was currently under evaluation. She shared that there were different options available for assistance, and stressed that it was more related to timing. She stated that there would be a potential positive revenue impact in 2022, but it would then be reduced in future years.

Senator Wielechowski remarked that it had been almost a year since the initial presentation, and wondered how much more time was needed for evaluation.

Acting Commissioner Mahoney replied that there may see a result from the evaluation offered in the coming weeks.

Co-Chair Stedman shared that his staff was currently engaging with DOR to bring forward a presentation on the issue.

Senator Wielechowski remarked that there was a new producer, HilCorp, which paid no corporate income tax. He queried an estimate of the cost to the state, as opposed to BP.

Acting Commissioner Mahoney responded that the current corporate tax estimate was \$23 million that the state would not receive.

Senator Wielechowski wondered whether HilCorp should pay the \$23 million.

Acting Commissioner Mahoney replied that there may be a future addressing of that issue.

Senator Wielechowski queried an estimate of the cost to the state when oil producers write off their development costs on state land on their taxes.

Acting Commissioner Mahoney agreed to provide that information. She furthered that there was a plan to do an order of operations presentation on the production tax.

[9:20:00 AM](#)

Senator Wielechowski wondered whether the issue should be corrected. He asserted that the development of Alaska National Wildlife Refuge (ANWR) would cost the state billions of dollars in revenue.

Acting Commissioner Mahoney replied that DOR would provide assistance, but would not come forward with that type of change.

Senator von Imhof remarked that there was an order of operations.

Senator Wielechowski wanted to know the position on raising revenue, and queried a plan on additional revenue measures.

Acting Commissioner Mahoney replied that the revenues needed to be addressed using a phased approach. She felt that taxes should be supported by a vote of the people.

Senator Wielechowski remarked that there was a recession, a deficit, and a forecast of a deficit and recession. He assumed that the plan was to use the Permanent Fund for the state costs, which meant lower Permanent Fund Dividends. (PFD).

Acting Commissioner Mahoney replied that the governor's position was that it was an anomaly year due to the pandemic. Therefore, it was not the time to raise new tax revenues.

Senator Wielechowski wondered whether the governor believed that taking part of the PFD was considered a "tax."

Acting Commissioner Mahoney felt that the question should be directed toward the governor.

Co-Chair Stedman FORWARDED the appointment of Lucinda Mahoney for consideration in accordance with Alaska Statute. He relayed that this did not reflect an intent by any member of the Senate Finance Committee to vote for or against the confirmation of the individuals during any further sessions. There being NO OBJECTION, it was so ordered.

[9:26:14 AM](#)

AT EASE

[9:28:27 AM](#)

RECONVENED

^ALASKA PERMANENT FUND CORPORATION

[9:29:16 AM](#)

ANGELA RODELL, EXECUTIVE DIRECTOR, ALASKA PERMANENT FUND CORPORATION, (APFC) discussed "Senate Finance Committee, The Alaska Permanent Fund, February 4, 2021" (copy on file). She looked at slide 2, "1969 The Debate Begins":

Alaska receives \$900 million in Prudhoe lease sale.

FY 1970 state budget: \$173 million.

Ms. Rodell highlighted slide 3, "The Alaska Constitution":

In 1976, Alaskans voted, 75,588 to 38,518, in favor to amend the Constitution of the State of Alaska and created the Alaska Permanent Fund.

Alaska Constitution Article IX, Section 15

Alaska Permanent Fund

At least twenty-five percent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses received by the state shall be placed in a permanent fund, the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for permanent fund investments. All income from the permanent fund shall be deposited in the general fund unless otherwise provided by law.

Ms. Rodell addressed slide 4, "The Corporation":

Four years after the Alaska Permanent Fund was approved by voters, the Alaska State Legislature passed SB 161 in 1980, establishing the Alaska Permanent Fund Corporation.

APFC's Mission

To manage and invest the assets of the permanent fund and other funds designated by law in accordance with AS 37.13.010-37.13.190.

Alaska Permanent Fund

-Principal -Constitution and AS 37.13.010

-Earnings Reserve Account -AS 37.13.145 (a)

Amerada Hess Fund -AS 37.13.145 (d)

-AK Capital Income Fund -AS 37.05.565

Alaska Mental Health Trust Fund -AS 37.13.300

-Alaska Mental Health Trust Authority

Ms. Rodell looked at slide 5, "Board of Trustees":

A six-member, governor-appointed Board of Trustees is entrusted with the fiduciary oversight of the Fund.

As the fiduciaries, the Trustees have a duty to Alaskans in assuring that the Alaska Permanent Fund is

managed and invested in a manner consistent with legislative findings in AS 37.13.020.

-The Fund should provide a means of conserving a portion of the state's revenue from mineral resources to benefit all generations of Alaskans.

-The Fund's goal should be to maintain safety of principal while maximizing total return.

-The Fund should be used as a savings device managed to allow the maximum use of disposable income from the Fund for the purposes designated by law.

A fiduciary is a person or organization that acts on behalf of another person or persons to manage assets. Essentially, a fiduciary owes to that other entity the duties of good faith and trust. The highest legal duty of one party to another, being a fiduciary requires being bound ethically to act in the other's best interests. -Investopedia

Ms. Rodell pointed to slide 6, "Investment Management":

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

A robust, healthy Permanent Fund is important to all generations of Alaskans.

Ms. Rodell looked at slide 7, "Key Questions...":

- How much do we make?
- How do we invest?
- How does Principal grow?
- How does the ERA grow?
- How much can we draw?

[9:35:02 AM](#)

Ms. Rodell highlighted slide 9, "Monthly Reporting":

-Accountability and transparency have driven our operations from our very beginnings as an independent state corporation accountable to the public.

-Financial and performance reports are produced monthly to ensure point-in-time accuracy of data and compliance with policies and laws.

-APFC finance staff reconcile values for the Principal and ERA accounts at the close of each month. The Fund has more than 700 investment accounts, each represents anywhere from one private investment to hundreds of public equity holdings.

Ms. Rodell looked at slide 10, "Values in Billions." She shared that on December 31, 2020, which was the mid-year point of fiscal year 2021, the total principal was \$57.8 billion. She explained that it was comprised of \$46.7 billion of contributions. The contributions came from royalties, inflation proofing, and special appropriations. She explained that there was \$11.1 billion included as unrealized gain.

Senator Hoffman looked at the \$3.1 billion, which was the statutory amount in law. He wondered why there was no reflection of the additional draw proposed by the governor.

Ms. Rodell replied that proposals were not included in the financial statements. She stated that the display showed liabilities and responsibilities. She explained that the auditors included the amount, because the statute was written to use a one-year gap. Therefore, there was an exact amount prediction using the statute. She stated that the trustees did not want any ad hoc draws.

Ms. Rodell pointed to slide 11, "Sources of Change in Value." She remarked that the market had been helpful to the fund over the previous six months.

Senator von Imhof wondered whether \$2.9 billion had been moved to the ERA or the general fund.

Ms. Rodell replied that it was the ERA.

Senator von Imhof wondered how much had been moved to the general fund of the normal POMV draw for the current year.

Ms. Rodell replied that \$1.5 billion had been moved, and the next payment would be in March.

Senator von Imhof surmised that the state taking half of the POMV draw was in cadence with taking equal increments throughout the year.

Ms. Rodell agreed.

[9:45:17 AM](#)

Senator Wielechowski wondered how much was made with the recent Gamestop issue.

Ms. Rodell replied that Gamestop experience caused an increase of about \$30 million.

Senator Wielechowski wondered whether the corporation invested the POMV assets in cash, and assumed that they were invested at a much lower risk.

Ms. Rodell replied that it was an incorrect assumption. She stated that all assets were invested together in one allocation. She explained that every asset was owned at a pro rata basis by the principal and ERA.

Ms. Rodell looked at slide 12, "Financial Statements":

APFC issues monthly financial statements for the Fund that reconcile values for the total Fund, the Principal, and ERA.

Includes monthly values for -

- Contributions to Principal
- Known commitments from the ERA, and the net realized earnings that remain unspent
- Unrealized gains for both accounts
- Statutory net income to the ERA
- Asset valuations
- Revenues and expenditures

Ms. Rodell highlighted slide 13, "Performance":

Monthly performance report includes 6 pages of -

- Market Values
- Performance:
 - 1mo, 3mo, FYTD, CYTD, 1Yr, 3Yrs, 5 Yrs
 - Total Fund
 - Benchmarks
 - Asset Classes
 - Holdings
 - Index Comparisons

[9:50:26 AM](#)

Ms. Rodell discussed slide 14, "Performance as of December 31, 2020." She explained that FY 20 generated a 2.01 percent return.

Co-Chair Stedman asked whether the 2.01 percent was gross or net of fees.

Ms. Rodell replied that it was net of fees.

Ms. Rodell pointed to slide 16, "Fund Total Value and Returns in millions":

1977 Initial Legislation permitted an investment list that included only fixed income securities such as treasury bonds.

1983 Following changes to the statutory investment list, the Fund makes its first investment in the stock market, and later that year, indirectly held real estate.

1990 After the Legislature expands the statutory investment list, the Fund begins to invest in stock and bond markets outside the United States.

2005 The Legislature makes a significant change in how Permanent Fund investments are determined, by removing the allowed investment list from state law.

The Trustees will make investment decisions under the guidelines of the prudent investor rule.

Co-Chair Bishop wondered whether there was an anticipation of another market correction.

Ms. Rodell replied that, fundamentally, there was no anticipation of a correction. She explained that there would be an entering of a period of very slow growth.

[9:55:50 AM](#)

Senator Wilson asked about the regulatory changes related to real estate investments.

Ms. Rodell replied that the funding was gaining in assets, so there was more comfort with investment strategies. She also stated that there was a need to seek out returns in other ways than the traditional assets.

Senator von Imhof remarked that there were significant cash reserves, which might overheat the market after the pandemic. She pointed out that the U.S. was in debt, so taxes might increase. She felt that there may be a volatile and steep counterforce, which could significantly affect the fund.

[10:00:05 AM](#)

Senator Wielechowski wondered whether the Permanent Fund engaged in short sales.

Ms. Rodell replied that it did not.

Co-Chair Stedman asked for a definition of short sale.

Ms. Rodell replied that short sales were when there was a belief that a stock was overvalued, so there was a belief that the stock would decline in price. Therefore, the stock was borrowed at the high price in anticipation of selling it at the lower price. She explained that it would make the profit on the bet. She felt that maybe she explained it incorrectly. She stated that there was an investment in hedge funds, which were designed to be market neutral.

Senator Wielechowski recalled that the governor had suggested that the state maybe not invest in banks that did not invest in Arctic oil exploration. He wondered whether the Permanent Fund invested in any banks that did not invest in Arctic oil exploration.

Ms. Rodell replied that that the Permanent Fund and the Permanent Fund Corporation relied on worldwide

partnerships, which included partnerships with banks that had made statements about not investing in Arctic oil. She felt that it would be difficult to conduct business without those banks.

Co-Chair Bishop wondered how much of the portfolio was moving into renewable energy.

Ms. Rodell agreed to provide that information.

Ms. Rodell pointed to slide 17, "Asset Allocation." She noted how the asset allocation had changed over time. She pointed that, currently, there was exposure to eight different asset classes, including 2 percent for cash. She pointed out that the asset allocation was the Board of Trustees statement on return and risk.

Ms. Rodell discussed slide 18, "Projections FY 21." She stated that the slide showed a low- mid- and - prediction. She remarked that a long-term ten-year return was also included in the projections.

Co-Chair Stedman remarked that there was a statutory 5 percent draw rate on the POMV, but noted that the real return on the slide was 4.23 percent. He wondered how that related to the 5 percent POMV.

Ms. Rodell replied that the POMV was 5 percent, but was over an average, therefore the effective rate was different than the 5 percent.

Ms. Rodell looked at slide 19, "History and Projections":

Issued monthly in conjunction with financial statements.

Values based on historical actuals, current fiscal year status, and projections for -

- Principal, ERA and Total Fund Balances
- Principal contributions: royalties, inflation proofing, special appropriations
- ERA statutory net income, dividend and POMV withdrawals, transfers to Principal
- AK Capital Income Fund -Amerada Hess
- Callan's 10-year capital markets forecast
- Forecasted Total and Real Returns

- POMV Distribution Calculations
- Statutory Dividend Transfer Calculation
- YTD Statutory Net Income Tracking

[10:10:53 AM](#)

Co-Chair Stedman wondered whether the target value for 2030 was \$80 billion.

Ms. Rodell replied in the affirmative.

Ms. Rodell looked at slide 20, "Callan's Long-Term Capital Market Projections." She noted that there were assumptions used on the slide used for the returns.

Co-Chair Stedman felt that Callan should present to the committee to discuss the expectations looking forward in the upcoming years.

Ms. Rodell noted that there would be a real return of 4.2 percent POMV for ten years.

Ms. Rodell addressed slide 22, "Principal":

- Constitutionally established as the permanent part of the Fund
- Grows through
 - royalty contributions
 - special appropriations
 - inflation proofing
- Is to be used only for
 - income-producing investments

Ms. Rodell pointed to slide 23, "Principal Contributions":

\$17.7 Billion Royalty Deposits -AS 37.13.010 (a) (1) and (a) (2)

The constitutionally minimum required 25 percent of royalty proceeds, and the statutorily mandated deposits of 50 percent 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.

10:15:01 AM

Co-Chair Stedman wondered whether the funds that were allocated by the committee, representative on a display check in the committee room, were utilized into fruition.

Ms. Rodell replied in the affirmative.

Co-Chair Stedman wondered whether the amount was "locked up on the corpus."

Ms. Rodell replied in the affirmative.

Co-Chair Stedman may have another discussion about issuing more funds depending on the budget and will of the committee.

Co-Chair Bishop will help keep the oil well pumping after the oil well is gone.

Ms. Rodell stated that it was almost 45 years since the creation of the Permanent Fund.

Ms. Rodell looked at slide 25, "Earnings Reserve Account (ERA)":

- Statutorily established under AS 37.13.145 (a) as a separate account in the Fund to hold the investment income
- Is to be invested in investments authorized under AS 37.13.120
- Grows through receipt of statutory net income
- Is available for Legislative appropriation

Ms. Rodell pointed to slide 26, "Renewable Resource":

Historically, the Alaska Permanent Fund has been used as a savings device to generate revenues and pay dividends to eligible Alaskans.

Today, the Fund is used to support the State's General Fund through the POMV Draw for statewide services and programs, including the dividend.

Ms. Rodell addressed slide 27, "ERA: Statutory Net Income":

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 December 31, 2020

- Statutory Net Income = \$2,880,800,000

[10:20:54 AM](#)

Ms. Rodell looked at slide 29, "Earnings Reserve Account." She explained that the slide detailed the current image of the ERA.

Co-Chair Bishop queried the reason for the downgrade.

Ms. Rodell replied that the numbers were from the DOR oil production forecast.

Senator Wielechowski surmised that the legislature forward funded inflation proofing for several years.

Ms. Rodell replied that the \$4 billion had intent language for eight years of inflation proofing. She explained that, due to the veto action, the amount was closer to four years of inflation proofing.

Co-Chair Stedman announced that the intent language was a part of the marketing of the large transfer. He felt that, in retrospect, it was possibly not necessary.

Ms. Rodell remarked that only earning four to five percent, with an eight percent draw would cause larger draws more quickly.

Ms. Rodell pointed to slide 30, "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

[10:31:40 AM](#)

Senator von Imhof stressed that FY 23 and FY 24 showed the POMV growing at \$3.21 billion and \$3.29 billion, but there was an assumption that there was no 9 percent draw. She remarked that the POMV would decrease with high draws.

Ms. Rodell agreed.

Senator von Imhof felt that the slide showed that the deficit would widen without revenue.

Co-Chair Stedman furthered that there was not a consideration of the management impact on the Permanent Fund and its total numbers.

Co-Chair Bishop noted the effective rate on the out years with the proposed draw, and assumed that rate would increase over time.

Co-Chair Stedman asked for a modeling of that impact.

Senator von Imhof felt that Legislative Finance Division could do that model.

[10:35:28 AM](#)

Ms. Rodell replied that there was work with the Legislative Finance Division to review the modeling assumptions.

Ms. Rodell addressed slide 31, "Trustees' Resolution 18-4":

In providing guidance on withdrawals for the Fund and to help ensure the long-term sustainability of using Fund earnings for the benefit of all generations of Alaskans, the Board passed Resolution 18-04 at a special meeting on October 17, 2018.

-This resolution affirms the importance of formulaic management of transfers into and out of the ERA to ensure sustainability and long-term growth of the Fund, by identifying four key principles: Adherence -Sustainability -Inflation Proofing -Real Growth

Sustainability ... requires annual formulaic withdrawals from the Earnings Reserve Account at an amount that the long-term balance of the account is able to fund. The Board has long supported the percent of market value (POMV) concept, including a constitutional amendment that would ensure no more than a sustainable amount was taken from the annual earnings of the Permanent Fund (Resolutions 00-13, 03-05 and 04-09).

Ms. Rodell pointed to slide 32, "Primary Source of UGF Revenue-POMV."

Ms. Rodell looked at slide 33, "ERA Monthly Values since POMV."

Ms. Rodell discussed slide 34, "20 Year Look back."

[10:40:44 AM](#)

Ms. Rodell addressed slide 35, "Use of Fund Earnings."

Senator Wielechowski wondered whether the Permanent Fund was investing more in Alaska.

Ms. Rodell replied that the Board of Trustees set aside \$200 million in the private equity asset allocation for an "Invest in Alaska Program", which was different than any of the other types of money that might be rolled into the state. She remarked that there was a deployment of approximately \$50 million.

Co-Chair Stedman wondered whether the reports included the Alaska investment comparisons.

Ms. Rodell replied in the affirmative.

Senator von Imhof queried the length of the deployment.

Ms. Rodell replied that it could range as high as five years.

Senator von Imhof wondered why the deployment was slow.

Ms. Rodell replied that it was slower as a result of the due diligence required for the pipeline.

[10:45:56 AM](#)

Ms. Rodell pointed to slide 37, "Evolving Role of the Fund":

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

Co-Chair Stedman stressed that there was a concern about the temptation to use the ERA for appropriation.

Ms. Rodell remarked that the ERA was fully invested in all the asset classes, so as it was drawn down, its portion of unrealized gains would also down.

Ms. Rodell discussed slide 38, "Revenue Generation":

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 percent 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.

Ms. Rodell stated that there was information about the APFC on its website.

Co-Chair Stedman discussed the following day's agenda.

#

ADJOURNMENT

[10:53:55 AM](#)

The meeting was adjourned at 10:53 a.m.