

SENATE FINANCE COMMITTEE  
March 21, 2023  
9:02 a.m.

9:02:00 AM

CALL TO ORDER

Co-Chair Olson called the Senate Finance Committee meeting to order at 9:02 a.m.

MEMBERS PRESENT

Senator Lyman Hoffman, Co-Chair  
Senator Donny Olson, Co-Chair  
Senator Bert Stedman, Co-Chair  
Senator Click Bishop  
Senator Jesse Kiehl  
Senator Kelly Merrick  
Senator David Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Ken Alper, Staff, Senator Donny Olson; Alexei Painter, Director, Legislative Finance Division; Senator Cathy Giessel.

SUMMARY

SB 107 PERMANENT FUND DIVIDEND; POMV SPLIT

SB 107 was HEARD and HELD in committee for further consideration.

#sb107

SENATE BILL NO. 107

"An Act relating to the Alaska permanent fund; relating to income of the Alaska permanent fund; relating to the amount available for appropriation and appropriations from the earnings reserve account;

relating to the permanent fund dividend; and providing for an effective date."

[9:03:21 AM](#)

KEN ALPER, STAFF, SENATOR DONNY OLSON, discussed the presentation, "Senate Bill 107; Percent of Market Value Split / Permanent Fund Dividend" (copy on file). He pointed to slide 2, "What Does SB107 Do?"

Establishes a split for the annual "Percent of Market Value" draw

- The split would be 75 percent for the General Fund, and  
25 percent to pay Permanent Fund Dividends

When SB26 passed in 2018, establishing the POMV formula for using Permanent Fund earnings, the bill did not update the 1980s dividend formula. SB107 would replace that formula.

The Senate Finance Committee has addressed this topic several times:

- The version of SB26 that passed the Senate in 2017 included a "75/25" split.  
The split was removed by the bill's Conference Committee.
- SB103, from 2019, included a "50/50" split
- SB199, from 2022, included a "75/25" split
- SB53, from 2022, included a smaller dividend that increased to a "50/50" split once a certain amount of new revenue was received

[9:05:53 AM](#)

Mr. Alper highlighted slide 3, "Why is this necessary?"

- The Permanent Fund was initially set aside for when oil would no longer be able to cover all budgetary needs.
- Not having a PFD formula creates uncertainty in the budgeting process.
  - The POMV was passed in part to stabilize the state's revenue.
  - If the dividend amount is unknown until late in session, the remaining POMV draw going to the General Fund is also unknown.

- o Without knowing how much revenue is available, it is difficult to make budget decisions.

Mr. Alper addressed slide 4, "Why is this necessary? (continued) "

- A PFD based on a percentage of the POMV adds stability to both the budget and the dividend
  - o The POMV is based on the overall value of the Permanent Fund, which is relatively stable and predictable.
  - o In contrast, the current statutory dividend formula is based on Permanent Fund earnings, which are much more volatile.
  - o If the general fund portion of the annual POMV payout is "whatever is left" after funding a volatile dividend, all that revenue volatility is transferred to the general fund- compounding fiscal uncertainty.

Co-Chair Olson looked at slide 3, and noted that the Permanent Fund was initially set aside for when oil revenue would not be able to cover all budgetary needs. He remarked that for a long time in the recent past, oil revenue has not covered the state's budgetary needs. He stressed that the Permanent Fund's earnings, or the Earnings Reserve Account (ERA), has covered the budgetary needs.

Mr. Alper replied that before the passage of SB 26 in 2018, the ERA was not used for general government. He stated that rather than funding the PFD, the earnings went to a few Permanent Fund management related tasks. He stressed that the CBR would cover the needed government funding.

[9:10:27 AM](#)

Mr. Alper pointed to slide 5, "Why 75 / 25?"

It is fiscally prudent

This table is from OMB on February 20th • Next year's "Governor's amended" budget is \$433 million in deficit.

- That's before:
  - o Fixing Community Assistance
  - o Basic deferred maintenance
  - o Any legislative additions to the capital budget
  - o Any adjustment to education funding

- o Any bills that pass with fiscal notes
- There are no available savings pools to draw from. A CBRF draw requires a supermajority vote which hasn't occurred since 2020

Mr. Alper addressed slide 6, "Other Unmet Budget Needs":

Slide is from Legislative Finance on February 7th

It details over \$13 billion in current state obligations

To summarize:

- o Pension obligations \$7.1b
- o Capital and maintenance needs \$4.4b
- o Debt service \$1.6b

Mr. Alper looked at slide 7, "Why 75/25 (continued)":

Later this week we'll see several fiscal updates, which will be mostly negative:

- The price of oil is trending several dollars below the Fall forecast for FY2024 of \$81 / bbl. DOR uses the "futures" market to set the price forecast
- Production is also trending a bit below forecast
- The combined impact will likely reduce FY24 revenue by a few hundred million
- Although the Willow project will produce substantial tax revenue in the future, during the period of major construction spending it will result in several years of substantial negative cash flows.

The net effect of these will likely result in about a \$1 billion shortfall

- Oil price forecast for future years are also likely to be adjusted downwards
- Weak current-year earnings will reduce the size of future POMV draws

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Co-Chair Olson queried the approximate shortfall with the Willow Project.

Mr. Alper replied that the total capital spend would probably be around \$5 billion. He stated that the price of

oil needed to be high enough to be above the minimum tax crossover. He stated that then all the spending would reduce the owner's profits.

Co-Chair Olson wondered whether the profit and shortfall would be equally distributed over the period of time.

Mr. Alper replied that the Department of Revenue (DOR) would provide a presentation related to the question.

Mr. Alper addressed slide 8, "The 75/25 Scenario Was the Most Stable and Balanced":

This is a Legislative Finance slide from Feb. 7

We will see this and similar scenarios with the updated forecast information on Friday

Co-Chair Olson wondered how that would affect a person who relied on the PFD for basic necessities.

Mr. Alper replied funding a larger dividend would be overdrawing the Permanent Fund, which would result in future overdrafts of the fund.

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Senator Bishop asked about the American Rescue Plan Act (ARPA) overdraw.

Mr. Alper shared that the slide showed the tail-end of the approximately \$1 billion that the state received from the pandemic relief funds. The remainder of that money was used to balance the FY 23 budget.

Senator Kiehl asked about the impact on 75/25 split on the PFD and how it compared to the ten- or fifteen-year average.

Mr. Alper replied that at 75/25, the PFD in the current year would be \$1350, which was roughly in alignment with the historic average.

Co-Chair Olson stressed that the previous year's PFD included an energy rebate.

Mr. Alper agreed, and stated that the actual statutory construction of the PFD in the budget was that there be a 50/50 PFD.

[9:25:30 AM](#)

Co-Chair Hoffman felt that the decision to finally decide the PFD split was the most important piece of legislation to stabilize government and spending. He noted that there was awareness that the amount of the PFD was politically and emotionally charged. He stressed that the number continued to be north of what the legislature eventually decided. He noted that many people felt that the current formula believed that it was state law, and that they were obligated to that money. He felt that the current legislation was a good starting point. He stressed that the current session should result in a final decision.

[9:31:13 AM](#)

Co-Chair Stedman noted that the 50/50 concept went back several decades. He remarked that the split between the citizens and the treasury resulted in the state reinvesting its share over many years. Thereby, allowing the Permanent Fund to increase substantially. He noted that the savings component was mandated by not taking the share in the past.

[9:36:43 AM](#)

Senator Bishop remarked that the \$9 billion deposit was a result of the state's reinvesting of its 50 percent share.

Mr. Alper highlighted slide 9, "Sectional Analysis":

Sec. 1. Repeals the current formula that describes the "amount available for distribution" as 21 percent of the past five year's Statutory Net Income. Amends the current 5 percent Percent of Market Value (POMV) statute to confirm that the appropriation may not exceed the amount in the Earnings Reserve Account.

Sec. 2 Modifies the Permanent Fund Dividend statute, from being based on 50 percent of the former "21 percent of earnings" formula, to being based on 25 percent of the annual Percent of Market Value draw.

Sec. 3 Conforming language to clarify that the annual inflation proofing of the Permanent Fund principal is by legislative appropriation.

Sec. 4 Conforming language related to the exclusion of Amerada Hess earnings from both the POMV and dividend calculations.

Sec. 5 Conforming language related to the exclusion of Mental Health Trust earnings from the POMV and dividend calculations.

Sec. 6 Conforming language related to the annual appropriation to the dividend fund.

Sec. 7 Conforming language repealing sections no longer needed due to the elimination of the former statutory formula and the new language in Sec. 3.

Sec. 8 Immediate effective date ensuring the changes impact the Fall 2023 dividend.

[9:40:02 AM](#)

Co-Chair Stedman stressed that the Permanent Fund would have an adjustment on its earnings for FY 23, which would reduce the statutory dividend calculation.

Co-Chair Hoffman understood that a 50/50 split would not currently work for the state. He noted that decisions would address how to get to a different split. He stressed that the conversations would be difficult, but the solution needed to work for everyone. He felt that in order to come to a solution, there would be very hard financial conversations and decisions.

Senator Wilson wondered whether the proposal would prohibit an additional energy fund rebate in the future.

Mr. Alper remarked that it would not, because the legislature controls the appropriations.

Senator Merrick wondered whether the POMV was a spending cap.

Mr. Alper replied that it was a revenue cap and could be broken, but it was not recommended, and stated that by extension was a spending cap.

Co-Chair Olson asked whether there was a fiscal note attached to the bill.

Mr. Alper replied that there was a zero fiscal note from DOR related to implementation.

[9:44:31 AM](#)

ALEXEI PAINTER, DIRECTOR, LEGISLATIVE FINANCE DIVISION, presented, "Fiscal Modeling: SB 107; Senate Finance; Committee Scenarios" (copy on file). He pointed to slide 2, "Outline":

- Review of Senate Finance Committee Modeling Assumptions
- Constitutional Budget Reserve Target Balance
- SB 107 Deterministic Model Using Committee Assumptions
- Review of LFD Probabilistic Model
- SB 107 Probabilistic Model Using Committee Assumptions

[9:45:43 AM](#)

Mr. Painter addressed slide 3, "Review of Committee Modeling Assumptions":

Revenue Assumptions

- LFD's baseline revenue assumptions are the Department of Revenue's Fall Revenue Forecast.
  - This assumes \$81 oil in FY24, following futures market thereafter.
  - DNR oil production forecast projects that Alaska North Slope production will increase from 503.7 thousand barrels per day in FY24 to 543.3 thousand barrels per day in FY32.
- For the Permanent Fund, we use Callan's return assumption of 7.00 percent total return in FY23 and 7.05 percent thereafter.

Mr. Painter highlighted slide 4, "Review of Committee Modeling Assumptions (cont.)":

#### Spending Assumptions

- For agency operations, assumes that the FY24 Governor's budget including amendments through 2/14 grows with inflation (2.50 percent).
- For statewide items, assumes that all items are funded to their statutory levels in FY24 and beyond.
  - This includes School Debt Reimbursement, the REAA Fund, Community Assistance, oil and gas tax credits.
- For the capital budget, assumes a \$400 million capital budget in FY24, growing with inflation thereafter (2.50 percent).
- For supplementals assumes \$50.0 million per year. This is based on the average amount of supplemental appropriations minus lapsing funds each year.
- For Permanent Fund Dividends, assumes 25 percent of the POMV draw is appropriated for dividends based on SB 107.

Senator Wilson wondered whether there was a better number for future modeling.

Mr. Painter replied that the \$50 million was based on the average amount of supplemental appropriations after considering lapsing funds each year. He stated that each year there were two adjustments that were used to move from the original budget to the actual budget.

Senator Wilson queried the historical average of the capital budget.

Mr. Painter replied that it varied greatly due to fluctuations in revenue.

[9:49:32 AM](#)

Co-Chair Stedman asked for an analysis of the historic capital budget from the recent 20 years, and separate out the federal match.

Mr. Painter replied that he would provide that information.

Mr. Painter discussed slide 5, "Evaluating Risk: Constitutional Budget Reserve Target Balance":

- \$500 million is needed for cashflow. How much is needed as a shock absorber? Alaska does not have a

formal reserves target. OMB told this committee that they are targeting \$2 billion in the CBR.

- A challenge in Alaska is that we do not have a structurally balanced budget to start with, so reserves are needed not just as a shock absorber but also to fill structural deficits.

- Many states do have formal reserves targets. For example, Minnesota targets a reserves level such that there is a 95 percent probability that the budget could be funded for the next two years based on projected revenue volatility.

- Applying the Minnesota rule to Alaska, based on a hypothetical budget that balances at projected revenue for FY24, Alaska would need a CBR balance of \$3.5 billion.

Co-Chair Olson wondered why there was a \$1 billion difference between the Office of Management and Budget (OMB) model and the \$3.5 billion Minnesota model.

Mr. Painter replied that the \$500 million was baseline funding to pay the bills covering the within year volatility. The next page would cover the between year volatility.

[9:55:05 AM](#)

Mr. Painter pointed to slide 6, "Senate Finance Baseline Budget 25 percent of POMV to PFD."

Mr. Painter displayed slide 7, "Probabilistic Modeling":

- LFD has two versions of the fiscal model: a linear model which assumes that revenue matches DOR's forecast, and a probabilistic model that shows the impact of revenue volatility
- The probabilistic model allows for variation in three variables:
  - Oil prices (using a range centered on DOR's forecast)
  - Oil production (using the range between DNR's "high" and "low" production forecast)
  - Permanent Fund investment returns (using the ranges developed by Callan for APFC)
- This leaves out potential variation in non-oil revenues and inflation

Mr. Painter highlighted slide 8, "Example: 25th Percentile Result":

- Example of a single case, for which 25 percent of total cases see greater overall deficits.
- Example case has average oil price of \$67.20 and average Permanent Fund return of 7.4 percent.

[9:59:19 AM](#)

Mr. Painter addressed slide 9, "Senate Finance Budget 25 percent of POMV to PFD." He noted that the median surplus deficit numbers were similar to the linear model.

Senator Merrick stated that in Article 9, Section 16 of the Alaska Constitution addressed appropriation limits, with at least one-third reserved for capital projects and loan appropriations. She wondered whether the legislature always complied with that requirement.

Mr. Painter replied that the legislature had not always complied with that requirement. He stated that the limit was ambiguous with the calculation.

[10:05:12 AM](#)

Co-Chair Olson wondered whether there was ever a challenge by Alaska to that non-compliance.

Mr. Painter replied, "not to my knowledge."

Co-Chair Olson asked what the current Attorney General opinion was on the subject.

Mr. Painter replied that the current opinion was based on an interpretation of the constitution, and the conflicting constitutional responsibilities of the legislature to fund state government and comply with the limit.

[10:05:43 AM](#)

Co-Chair Stedman asked for a review and commentary with the historic capital budget presentation.

Mr. Painter agreed to provide that information.

Senator Kiehl surmised that the presentation did not include additional funding for public schools.

Mr. Painter agreed, because it was based on the governor's amended budget, which did not include fiscal notes for legislation.

Senator Kiehl stressed that funding education was in Article 7, Section 1 of the constitution.

Co-Chair Olson discussed housekeeping.

SB 107 was HEARD and HELD in committee for further consideration.

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ADJOURNMENT

[10:07:47 AM](#)

The meeting was adjourned at 10:07 a.m.