ALASKA STATE LEGISLATURE
LEGISLATIVE BUDGET AND AUDIT COMMITTEE
March 4, 2025
9:01 a.m.

MEMBERS PRESENT

Senator Elvi Gray-Jackson, Chair
Representative Zack Fields, Vice Chair
Senator Bert Stedman
Senator Cathy Giessel
Senator Lyman Hoffman
Senator Bill Wielechowski
Representative Neal Foster
Representative Andy Josephson
Representative Chuck Kopp
Representative Cathy Tilton
Senator Scott Kawasaki (alternate)
Representative Bryce Edgmon (alternate)

MEMBERS ABSENT

All members present

OTHER LEGISLATORS PRESENT

Senator Kelly Merrick
Senator Gary Stevens
Senator Mike Cronk

COMMITTEE CALENDAR

PRESENTATION(S): THE IMPACT OF THE POMV ON ALASKA'S BUDGET

- HEARD

PRESENTATION(S): ALASKA PERMANENT FUND CORPORATION'S TRUSTEES' PAPER #10

- HEARD

PREVIOUS COMMITTEE ACTION

No previous action to record

WITNESS REGISTER

ALEXEI PAINTER, Director
Legislative Finance Division
Legislative Agencies and Offices
Juneau, Alaska
POSITION STATEMENT: Gave the Impact of the POMV on Alaska's Budget presentation.

JASON BRUNE, Chair
Board of Trustees
Alaska Permanent Fund Corporation
Anchorage, Alaska
POSITION STATEMENT: Co-offered the Alaska Permanent Fund Corporation's Trustees Paper #10 presentation.

DEVEN MITCHELL, Executive Director
Alaska Permanent Fund Corporation
Anchorage, Alaska
POSITION STATEMENT: Co-offered the Alaska Permanent Fund Corporation's Trustees Paper #10 presentation.

ACTION NARRATIVE

9:01:24 AM

CHAIR ELVI GRAY-JACKSON called the Legislative Budget and Audit Committee meeting to order at 9:01 a.m. Representatives Foster, Josephson, Kopp, Tilton, Edgmon (alternate), and Fields and Senators Stedman, Wielechowski, Hoffman, Giessel, Kawasaki (alternate), and Gray-Jackson were present at the call to order. Also present were Senators Merrick, Stevens, and Cronk.

PRESENTATION(S): The Impact of the POMV on Alaska's Budget

9:02:11 AM

CHAIR GRAY-JACKSON announced that the first order of business would be a presentation on the Alaska Permanent Fund.

9:03:05 AM

ALEXEI PAINTER, Director, Legislative Finance Division (LFD), Legislative Agencies and Offices, directed attention to a PowerPoint presentation, titled "POMV in Alaska's Budget" [hard copy included in the committee packet], that began with a bar chart on slide 2, "UGF Revenue and Budgets, FY 14-25," showing how the percent of market value (POMV) draw has influenced the state budget. The adoption of the POMV draw in Fiscal Year 2019

(FY 19) significantly changed the budget picture by reducing the average pre-transfer deficit from $3 billion to $250 million, which has been filled using federal funding from the COVID-19 Pandemic and the remainder of the Statutory Budget Reserve (SBR). Major draws from the Constitutional Budget Reserve (CBR) have largely been avoided, as the legislature works to rebuild that balance. He stated that adding the POMV draw helped stabilize state revenue despite the existing structural deficit.

9:05:04 AM

MR. PAINTER paraphrased slide 3, "Earnings Reserve Account (ERA) Sufficiency," which read as follows [original punctuation provided]:

> • APFC's Statutory Net Income projection for FY25+ is 6.25%, compared to inflation of 2.50% and a 5.00% POMV draw. This leads to a projected decline in the balance of the ERA balance.
> • APFC's projections show that the year-end ERA balance will drop below the following year's POMV draw amount in FY32, assuming statutory inflation proofing each year. That means that when the year begins, the ERA won't have enough money to pay out the entire POMV draw for the year and will have to rely on current-year earnings.
> • LFD's probabilistic modeling shows an 46% chance of having an insufficient ERA balance to make the full POMV draw over FY26 - FY35, assuming full inflation proofing and statutory POMV draws. If inflation-proofing is suspended when the ERA balance drops below the following year's POMV draw, that drops to 33%.

9:08:34 AM

MR. PAINTER paraphrased slide 4, "Policy Levers to Reduce ERA Sufficiency Risk," which read as follows [original punctuation provided]:

> • Failure rate reflects the percentage of simulations where the ERA balance is insufficient to pay the full POMV draw at least once during the ten-year period
> • "Statutory Inflation Proofing" refers to full statutory inflation proofing occurring annually. "Partial Inflation Proofing" means that full statutory inflation proofing occurs, except the amount is reduced if the FY-end ERA balance is insufficient to

pay the following years POMV. “No Inflation Proofing” means that there is zero inflation proofing in any year from FY26-FY35.

MR. PAINTER described the chart on slide 4, which showed ERA failure rates with different levels of inflation proofing and POMV draw percentages. He noted that even with no inflation proofing, the probabilistic modeling shows that the ERA may still be insufficient to fully fund the POMV draw. The far-right column reflected the impact of changing the draw rate on the FY 26 deficit. He explained that decreasing the POMV draw to 4 percent would increase the deficit by $759.7 million, thereby solving one problem and creating another.

PRESENTATION(S): Alaska Permanent Fund Corporation's Trustees' Paper #10

9:10:30 AM

CHAIR GRAY-JACKSON announced that the final order of business would be the Alaska Permanent Fund Corporation's Trustees' Paper #10 presentation.

9:10:50 AM

JASON BRUNE, Chair, Alaska Permanent Fund Corporation (APFC), co-presented a PowerPoint, titled "Trustees' Paper Volume 10 Modernizing the Alaska Permanent Fund: A Single-Fund Endowment Model" [hard copy included in the committee packet]. In reflecting on Mr. Painter's statement that there's a 46 percent chance that the ERA balance would be insufficient to make a full POMV draw, he said combining the Alaska Permanent Fund's accounts, as proposed in the trustees' paper volume 10, titled "A Rules-Based Permanent-Endowment Model for Alaska" [included in the committee packet], would bring predictability.

9:12:16 AM

DEVEN MITCHELL, Executive Director, Alaska Permanent Fund Corporation (APFC), directed attention to a PowerPoint, titled "Trustees' Paper Volume 10 Modernizing the Alaska Permanent Fund: A Single-Fund Endowment Model." He began on slide 2, "A Legacy of Intergenerational Resource Contribution," which read as follows [original punctuation provided]:

In 1976 -

Alaskans chose to permanently forgo immediate use of at least 25% of oil and mineral revenues, saving instead to create a renewable financial resource for generations —the Alaska Permanent Fund.

Today, the Fund -

- Leads the Nation
  The largest U.S. sovereign wealth fund, globally recognized as a model for converting finite natural resources into lasting wealth.
- Supports Alaska
  Provides over 50% of the state's unrestricted general fund revenue for dividends and essential services through the annual Percent of Market Value (POMV) draw.

9:13:39 AM

MR. MITCHELL paraphrased slide 3, "To Benefit All Generations...," which read as follows [original punctuation provided]:

- 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 purposes designated by law.

MR. MITCHELL added that the fund is invested for total return, which doesn't always align with statutory net income (SNI) and has resulted in some of the stresses pointed out by Mr. Painter.

9:15:11 AM

MR. MITCHELL moved to slide 4, which illustrated the fund's current two-account structure. The Principal provides permanent savings to be used only for income-producing investments, with realized earnings deposited into the ERA for appropriation by the legislature. Realized earnings, which are rents, stock dividends, interest payments on fixed income securities, and sales from assets that have increased in value, are the spendable portion. Unrealized earnings do not flow to the ERA and are not spendable under the current construct; however, they are allocated on a pro rata basis between the Principal and ERA. Inflation proofing is the intergenerational component and a lever that's controlled by the legislature when the ERA is under stress. Any amount can be drawn from the ERA with a simple majority of the legislature and the governor's concurrence.

9:17:26 AM

MR. MITCHELL turned to slide 5, which illustrated the proposed single-fun endowment construct. In this model, contributions would enter the Alaska Permanent Fund with one payout, thereby eliminating the ability for one generation to overuse the fund and the mismatch between total return and SNI.

9:18:31 AM

SENATOR STEDMAN recalled prior testimony from a sovereign wealth advisor who named the Alaska Permanent Fund as one of the largest sovereign wealth funds in the world relative to the state's budget and its population. He commented on the vastness of the wealth that Alaska's forefathers created.

MR. MITCHELL acknowledged that there are larger international sovereign wealth funds that exist; however, they're smaller than the Alaska Permanent Fund on a per capita basis.

9:19:47 AM

MR. MITCHELL paraphrased slide 7, "Global Investment - maximize a risk-adjusted return," which read as follows [original punctuation provided]:

> Through prudent asset allocation and strategic decision-making, APFC has robust performance across asset classes, reinforcing our commitment to deliver sustainable value for our stakeholders—the people of Alaska.
>
> 1980
> Investments: Bonds - Fixed Income
> Payout method: Based on realized income
>
> Today
> Investments: Diversified - Public & Private Markets
> Payout method: Based on % of the Fund’s total value

9:22:12 AM

MR. MITCHELL, paraphrased slide 8, "Investing for the Longe Term," which read as follows [original punctuation provided]:

> Real Return
> Annual investment performance adjusted for inflation indicates sustained value and purchasing power.
>
> The Board's objective for the Fund:
>
> - Investment Performance
>   Ability to generate an annualized return of inflation (CPI) + 5% over a 10-year period.
> - Investment Risk
>   Ability of the Fund to achieve the long-term target while conforming to the Board's approved risk appetite metric.

MR. MITCHELL referenced the bar chart on slide 8 that showed total return, real return, and return objective, which is Consumer Price Index (CPI) plus 5 percent. Mr. Mitchell stated that 5 percent is a difficult target to hit on an ongoing basis.

9:23:06 AM

SENATOR STEDMAN asked whether the 5 percent draw rate pushes the asset allocation more aggressively than a 4.25 or 4.5 percent draw would.

MR. MITCHELL said Callan's Capital Market Assumptions (CMA) diminished expectations for equity markets over the next 10 years. With the updated capital market assumptions, the fund is slightly below CPI plus 5 percent at 4.8 percent, so risk must be added to the portfolio's asset allocation to increase the probability of achieving 5 percent.

9:24:14 AM

MR. BRUNE added that the 5 percent draw has not impacted the Board of Trustees' aggressivity.

9:24:45 AM

SENATOR WIELECHOWSKI shared his understanding that the S&P 500 returned 40 percent over the past two years. He asked how that compares to the fund's performance.

MR. MITCHELL did not know the answer. Over the past 10 years, however, a passive asset allocation would have cost the fund $14 billion.

SENATOR WIELECHOWSKI pointed out that the S&P 500 averaged 8.9 percent over the past 100 years. He sought to verify that the fund has not averaged that same amount.

MR. MITCHELL cited an analysis by APFC's chief risk officer, which found that in a draw scenario, the internal rate of return diminishes in a 100 percent S&P 500 model.

9:27:57 AM

SENATOR WIELECHOWSKI asked how much the fund has paid in fees over the past two years.

MR. MITCHELL said the fee structure is high due to the private market exposure. He explained that in private markets, a 2 percent annual fee is required to participate in a partnership. Nonetheless, the private equity portfolio is the fund's strongest performing asset class over the past 10 years, which has outperformed the S&P 500. He indicated that the high fees are paid in exchange for outsized returns.

SENATOR WIELECHOWSKI pointed out that in the past several years, the fund has underperformed the market and paid extraordinarily high fees.

MR. MITCHELL said a broader conversation on the issue would be beneficial. He acknowledged that private equity is in a trough relative to investment in public equities.

9:30:26 AM

MR. MITCHELL resumed the presentation on slide 9, "Saving Wealth, Investing, & Providing Income," which read as follows [original punctuation provided]:

> From the first deposit of $734,000 of Trans-Alaska pipeline royalties the Alaska Permanent Fund has –
>
> • Grown to over $80.8 billion, as of Jan. 31, 2025
> • An annualized total return of 8.71%, as of Dec. 31, 2024
> • Generated more than $91.0 billion in realized earnings as of Dec. 31, 2024, that have supported -

the dividend, the General Fund, and inflation-proofing for intergenerational benefit.

9:31:58 AM

VICE CHAIR FIELDS asked what the size of the fund would be if dividends had never been paid and, instead, reinvested into the fund.

MR. MITCHELL said if all the earnings had flowed to the general fund and been spent, the fund would be at $20 billion. He added that including unrealized gains, earnings total around $106 billion for the life of the fund, of which an estimated $40 billion were expended on the POMV or Permanent Fund Dividends (PFDs).

VICE CHAIR FIELDS requested a follow-up response on the compounded returns had the money not been spent on dividends.

9:33:17 AM

MR. MITCHELL resumed the presentation on slide 10, which highlighted the volatility of Alaska's revenue on a historical basis since the discovery of oil on the North Slope. He noted the creation of the CBR after the 1980s acted as a natural shock absorber until the price dropped in late 2014 and didn't recover for 5 or 6 years. In 2019, the creation of the POMV transfer created a huge stabilizing factor for state revenue on an annualized basis despite volatility with the underlying oil revenue.

9:35:22 AM

MR. MITCHELL turned to slide 11, which showed the nuances of the two-account structure. The fund's total value as of January 31, 2025is $80.8 billion with $71.4 billion in the Principal, of which $12.8 billion is unrealized gains that are allocated to Principal in the aforementioned pro rata basis. To the extent those earnings are realized, that money shifts over to the ERA. Consequently, $58.6 billion is truly protected as Principal. The ERA totals $9.4 billion of which $3.8 billion is committed to the FY 26 POMV transfer, $1 billion is committed to FY 25 inflation proofing, and $1.7 billion is a pro rata share of total unrealized gains. Consequently, as of January 31, 2025, there is $2.9 billion of spendable realized earnings in the ERA available for FY 26 inflation proofing and FY 27 POMV.

9:37:28 AM

MR. MITCHELL turned to slide 12, "Key Drivers in the ERA," which read as follows [original punctuation provided]:

> ERA's Decreasing Availability
>
> The ERA AS 37.13.145 (a) is available for Legislative appropriation through a simple majority vote.
> It grows through the realized investment income that is defined as Statutory Net Income (SNI) AS 37.13.140 (a).
>
> Looking Forward
> FY27 POMV Draw = $4.0B
> (to be committed in FY26 financials)
>
> Inflation Proofing for FY26 = $1.5B est.
> (to be committed based on appropriation, with final calculation at the close of FY26)
> --
> Total Commitments in FY26 = $5.5B
> ERA Realized Avail FYTD 25= $2.9B as of Jan Statutory Net Income FY25 = $4.2B projected

MR. MITCHELL explained that at the start of FY 25, for the first time ever there was a shortfall of $400 million in the ERA after providing for FY 25 inflation proofing and POMV, and FY 26 commitments.

9:38:09 AM

MR. MITCHELL continued to slide 13, "Spending is Limited to the ERA," which read as follows [original punctuation provided]:

> The Earnings Reserve Account faces the risk of depletion due to annual withdrawals for state revenues and the need for inflation protection of the Principal for future benefits to Alaskans.
>
> Long-Term Investment Focus
> • Realized earnings generated through investment activity are prioritized by maximum long-term return mandates, not realized gains.
> • The ERA grows through the realization of investment income, which is inherently volatile and unpredictable.

Limited Realized Earnings Availability
• Due to the two-account structure, spendable amounts are limited to what's available in the ERA, which is subject to commitments based on appropriations and known obligation at the beginning of each fiscal year.
• Inflation-proofing has been inconsistent, given the state's need for predictable revenue to provide for general fund services and programs.

9:39:01 AM

REPRESENTATIVE EDGMON asked whether the legislature has the authority to appropriate the fund's unrealized earnings.

MR. MITCHELL said the appropriation of unrealized gains would be a legal question and potentially litigable.

MR. BRUNE pointed out that a simple majority of each body would allow access to those funds.

SENATOR STEDMAN cautioned against overlooking the benefit of the endowment concept, which would restrict the ability to appropriate over the limit of the POMV draw.

9:41:27 AM

MR. MITCHELL paraphrased slide 14, "Manual Inflation Proofing," which read as follows [original punctuation provided]:

FY 16: Inflation proofing not funded for the first time

FY 20: Special $4B appropriation with intent language for inflation proofing the Principal
Ch 1 FSSLA 2019 amended. … It is the intent of the legislature that the amount appropriated in this subsection not include associated unrealized gains; and be used to satisfy the inflation proofing requirement under AS 37.13.145(c) for the next four fiscal years.

FY 22: Special $4B appropriation. Deposited to Principal
Ch 1 SSSLA 2021. …(f) The sum of $4,000,000,000 is appropriated from the earnings reserve account (AS

37.13.145) to the principal of the Alaska permanent fund.

9:42:46 AM

MR. MITCHELL paraphrased slide 16, "The Need for Reform," which read as follows [original punctuation provided]:

Consolidation to a Single-Fund endowment model would align the Permanent Fund with best practices for intergenerational wealth funds.

For the Present

- Ensure the option of an annual payout to support dividends and government services.
- Maintain stable payouts from year to year.
- Make payout method compatible with investment strategy.

For the Future

- Prevent overspending in the good years.
- Maintain purchasing power for the entire Fund.

The two-account structure is outdated and conflicts with best practices in sovereign wealth fund management.

The ERA is at risk of depletion given the annual draws to support government services and the divided program, as well as inflation proofing the Principal for intergenerational Alaskan benefit.

9:44:09 AM

MR. BRUNE paraphrased slide 17, "Constitutional Amendment," which read as follows [original punctuation provided]:

The Board of Trustees has been on record for more than twenty years supporting the transition to a Single-Fund endowment to protect its intergenerational sustainability and ensure that it provides for all generations.

Board Resolutions 2000-13, 2003-05, 2004-09

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

MR. BRUNE added that the endowment model would resolve the inflation proofing issue.

9:45:19 AM

MR. BRUNE summarized the Trustees' Paper Volume 10 on slide 18, which proposes a change from the two-account structure - The Principal and the ERA - to one account.

9:46:03 AM

MR BRUNE turned to slide 19, "Proposed Single-Fund Endowment Model," which read as follows [original punctuation provided]:

> Adopting this model, which would include a Constitutionally established spending limit, would strengthen the Fund's long-term stability and purchasing power for future generations.

- Merge the Principal and the ERA into a Single-Fund.
- Limit annual distributions through a Constitutional Percent of Market Value Rule.
- Ensure automatic inflation proofing by adhering to a long-term sustainable withdrawal rate.
-

> The change to a Single-Fund would ensure that an annual POMV transfer would be available each year but would not affect the discretion in deciding how to spend the money.
>
> The power of appropriation remains with the Legislature, while the annual draw from the Fund would be limited.

9:46:49 AM

MR. MITCHELL paraphrased slide 20, "Benefits of the Single-Fund Model," which read as follows [original punctuation provided]:

Aligned with global best practices, strengthening Alaska's financial position through sustainable withdrawals & limited to the Fund's long-term real return

Total-Return Investing:
Maximizes long-term growth without liquidity constraints.

Predictable & Sustainable Spending:
A maximum draw POMV rule prevents overspending.

Automatic Inflation Proofing:
Eliminates need for manual and ad hoc legislative adjustments.

Alignment with Prudent Investor Standards:
Follows best practices for endowments and trusts.

A Single-Fund Endowment is permanently inflation-proofed and ensures the Fund's real value is maintained over time while supporting its intended beneficiaries.

The key principles behind this are:

- Growth in the Fund's value keeps pace with or exceeds inflation.
- A prudent spending rule/limited draw rate ensures sustainability.
- Returns above the draw rate are reinvested.

9:47:31 AM

MR. MITCHELL paraphrased slide 21, "Comparing Fund Structures," which read as follows [original punctuation provided]:

The Endowment Model is not constrained in providing the set annual POMV draw, while the two-account structure is limited to the ERA's available balance.

Endowment Retains Earnings

- Under the Single-Fund Endowment Structure, income would be calculated according to generally accepted accounting principles, meaning all earnings (realized and unrealized) would be retained within the Fund.

- All earnings are retained and reinvested in the Single-Fund, thus eliminating the need for inflation proofing.

MR. MITCHELL explained that under the current two-account structure, 73 percent of the fund is constitutionally protected, whereas 95 percent of the fund would be protected under the proposed endowment model. He refuted the idea that the shift to one account would add additional risk to the invasion of Principal.

9:48:38 AM

MR. MITCHELL paraphrased slide 22, "Policy Recommendations," which read as follows [original punctuation provided]:

> The Board of Trustees recognizes that implementing policy reform requires legislative action and widespread public support.
>
> Constitutional Amendment (Preferred Approach)
> • Enshrine a Single-Fund permanent endowment model with a limited POMV spending rule in the Alaska State Constitution - Ensures long-term sustainability and intergenerational equity.
>
> Statutory Reforms
> • Combine the two accounts and establish the permanent endowment model in statute
> - Rules-based mechanisms require consistent discipline.
> • Suspend inflation proofing when the ERA balance approaches minimum levels
> - Impacts intergenerational benefit.
> • Force realization of capital gains to stabilize ERA balances
> - Impacts APFC's ability to manage the portfolio to a maximum risk-adjusted return over the long term and erodes intergenerational benefit.
>
> A constitutional amendment to establish a Single-Fund endowment - the ultimate solution
>
> "The combination of a single-account structure and a Constitutional limit on POMV draws linked to the Fund's long-term real return…will complete the

transition to a permanent-endowment model, with the following attractive features and characteristics:

- Total return investing
- POMV spending and automatic inflation proofing
- Alignment with the Prudent Investor Law and best practices.
- Fit for purpose”

\- Trustees’ Paper Volume 10 Dr. Malan Rietveld Sovereign Wealth Fund Expert

9:51:23 AM

MR. MITCHELL concluded on slide 23, which featured the graphic from slide 5 showing the flow of funds in the single fund endowment model.

MR. BRUNE explained that APFC's statutory mandate is to maximize risk adjusted returns for the people of Alaska. Consequently, the focus is on diversification rather than going all in on the stock market, which in a down year, would not have allowed the legislature to fund state services or the PFD. He acknowledged that some private equity funds have large fee structures, but the overall cost of the Alaska Permanent Fund is much smaller than most funds. He concluded that a single-fund endowment would bring more predictability than the current two-account structure.

9:53:16 AM

VICE CHAIR FIELDS questioned the best way to describe this proposal to the public.

MR. MITCHELL described it as the protection of the state's most important revenue source for future residents of the state while recognizing past sacrifices. He compared the fund to fish and wildlife resources, explaining that those resources are managed in a way that ensures their longevity for future Alaskans.

MR. BRUNE quoted a past mentor who said, "It must fit on a bumper sticker." He said the focus should be on two words: predictability and sustainability.

9:55:35 AM

REPRESENTATIVE JOSEPHSON asked how many years the extra contributions would suspend inflation proofing.

MR. MITCHELL said the additional $1.95 billion of inflation proofing would cover the coming year.

9:56:31 AM

SENATOR STEDMAN emphasized the importance of inflation proofing the fund for future generations of Alaskans. He suspected that a discussion would be had during this budget cycle on how much to inflation proof.

9:57:14 AM

VICE CHAIR FIELDS considered whether the public should be given the option to go beyond inflation proofing and grow the fund to sustain state operations in a post-oil environment. If the legislature were to assume long-term declines in oil revenue over the next 30 years, he asked what draw percentage would grow the fund while simultaneously funding operations.

MR. MITCHELL said that calculation would require an identifiable target. He explained that drawing less from the fund would create an expectation of growth, adding that annual deposits from royalty revenue are still being made in the amount of $400 million. He stated that the question would need to be answered from a policy perspective and offered to follow up with the requested information.

MR. BRUNE returned to slide 8 and reiterated that CPI plus 5 percent is a difficult objective; however, endowments typically target a 4 to 5 percent threshold. He reiterated that smaller draws leave more to be grown for future years.

9:59:47 AM

SENATOR STEDMAN pointed out that the Alaska Mental Health Trust's target of 4.25 percent has been predictable and stable. He recommended that the legislature consider that for comparison.

10:00:32 AM

ADJOURNMENT

There being no further business before the committee, the Legislative Budget and Audit Committee meeting was adjourned at 10:00 a.m.