

HJR

48

HFIN

FILE

Alaska State Legislature



House of Representatives
House Judiciary Committee

State Capitol, Room 120
Juneau, Alaska 99801-1182
(907) 465-4990

LETTER OF INTENT

After reviewing HJR 48 (Restructuring the Permanent Fund) the subcommittee decided that before the legislature embarks on a new method of budget funding many policy issues must first be addressed. The decision was made after carefully evaluating the premises of HJR 48, in addition to information provided from individuals knowledgeable in evaluating financial proposals.

This Letter of Intent contains 1) A Basic Outline of HJR 48, 2) Policy Questions That Must Be Asked and 3) A Proposal For Further Action by the Legislature

Brian S. Porter

Brian S. Porter, Chairman

House Judiciary Committee

1) A Basic Outline of HJR 48 "The Cremo Plan"

The purpose of the plan is to stabilize state resource revenues at a sustainable level, to increase the size of the Permanent Fund, and to minimize the negative consequences of the fiscal gap. The plan requires this session's legislature to propose - and the voters in the fall election to approve - an amendment to the State Constitution to provide that beginning July 1, 1995 and henceforth, all natural resource revenues be deposited in the Permanent Fund along with the assets of the state's two budget reserve accounts and the Railbelt Energy Fund. All future income earned by the Fund would be retained in the Fund, but there would be an annual withdrawal from the Fund based on its average market value over the past 12 quarters. The first year, the withdrawal would equal 20 percent, but then would be reduced geometrically each year until the permanent withdrawal rate of 6 percent is reached in the year 2006.

2) Policy Questions That Must Be Asked

There are major policy and technical questions which must be thoroughly researched and answered before we are in a position to present any plan to the voters. Those issues include:

1. Revenue Allocation - If only resource revenues are used to determine the budget amount available, and our entitlement programs continue to grow, won't most of the available revenues eventually go into the entitlements and less into resource development, thereby reducing the revenue source which funds the cycle? Additionally, what about the negative impact to natural resource development by encouraging high severance and other taxes in order to generate enough income to support the growing needs of an expanding population?

2. Effect on Bonds - How will a budgetary funding mechanism such as this affect the State's current bond rate? If adopted, could it impair the State's credit and, thereby impair the ability of the State, state agencies and local governments to fund capital improvements through bonds?

3. Emergency Relief - The amendment makes perhaps 90 percent or more of the recurring unrestricted revenue of the state "not appropriable." The amendment then prescribes a set percentage for expenditure each year. There is no allowance of amounts necessary to

meet unforeseen disaster emergencies. The State needs to have a rainy day fund for atrocities such as earthquakes and other natural disasters.

4. Assumptions - The plan is based on the Department of Revenue's fall 1993 mid-case revenue projections, and assumes an annual total rate of return for the Permanent Fund of 10 percent and an annual inflation rate of 4 percent. The Alaska Permanent Fund Corporation's projections are based on the low-case revenue projections, and assume a long-term average rate of return for the Permanent Fund of 9 percent and a long-term average rate of inflation of 6 percent. Long term market history does not support conservative investments returning 2 1/2 times the inflation rate. The "Cremo" plan assumes some combination of state spending cuts and revenue increases. Given the plan's assumptions, a 12 percent annual increase in conventional revenues and a \$30 million cut in annual state spending would eliminate the fiscal gap. This is a tremendous statement when no one has the ability to predict future deposits into the fund up to the year 2006.

5. Appointments to the Board of Directors - The directors of the corporation should not be subject to confirmation. Under the present approach used in the constitution, only department heads and the heads of quasi-judicial boards are subject to confirmation. The corporation would be the trustee of the source of most of the expendable money of the state. There could be an inherent conflict of interest if the legislature shares the power to make appointments to the board.

6. The Transition Period - The plan provides for a higher but gradually reduced withdrawal rate during a 10-year transition period in order to minimize the negative consequences of the fiscal gap. The proposed constitutional amendment states that the withdrawal rate shall decrease geometrically throughout the transition period, but does not provide specific details. This ambiguity should be cleared up. We lack sufficient information to know whether the percentages proposed beginning in fiscal year 1996 and thereafter will have the effect of depleting the corpus, or leave it unprotected from the effects of inflation.

7. Relevant Taxation - There needs to be a more cogent clarification of the kinds of taxes that go into the fund under this proposal. Resource related personal income should not be included.

3) A Proposal For Further Action By the Legislature

Before the legislature and the citizens of this state will approve this plan, they need to be convinced that it is clearly an improvement over the status quo. While there are some positive and intriguing aspects of HJR 48 there are also a number of undesirable outcomes which might occur should actual conditions in the future vary significantly from the assumptions upon which the plan is based. Indeed, the consequences for Alaska of this plan are too serious to rush a study. The subcommittee believes that it would be beneficial to the state and its citizens to establish a long-range plan that organizes the state's approach to handling its finances. It is for these reasons and the aforementioned concerns that the subcommittee proposes the establishment of a blue ribbon task force comprised from all branches of government, as well as technical experts in the field, that would thoroughly investigate the concept contained in HJR 48 and other feasible long-term financial plans. Unfortunately, there is not time enough during the current legislature to complete the study and think the task force should meet during the interim. We feel that further action, at this time, on this issue falls under the purview of the Finance Committee.

FISCAL NOTE

BILL NO. _____

**STATE OF ALASKA
1994 LEGISLATIVE SESSION**

Revision Date: _____
 Title: Amendment to the Constitution RE:
 Restructure Permanent Fund
 Sponsor: Finance Committee
 Requestor: _____

Department Affected: Office of the Governor
 BRU: Division of Elections
 Component: General and Primary Elections
 COMPONENT SERIAL NO. 22

EXPENDITURES/REVENUES:

OPERATING	FY 95	FY 96	FY 97	FY 98	FY 99	FY 00
PERSONAL	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	2.2*	0	0	0	0	0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LAND &	0	0	0	0	0	0
GRANTS.	0	0	0	0	0	0
MISCELLANEOUS	0	0	0	0	0	0
TOTAL	2.2*	0	0	0	0	0

CAPITAL	0	0	0	0	0	0
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REVENUE						
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FUNDING:

1002 Federal	0	0	0	0	0	0
1003 GF Match	0	0	0	0	0	0
1004 GF	2.2*	0	0	0	0	0
1005 GF/Program	0	0	0	0	0	0
1006 GF/MHTIA	0	0	0	0	0	0
OTHER	0	0	0	0	0	0
TOTAL	2.2*	0	0	0	0	0

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

Estimate of current year (FY94) impact: 0

ANALYSIS: (Attach a separate page if necessary.)*This figure covers cost of inclusion of information about this issue in the Official Elections Pamphlet as required by AS 15.58, and programming for DataVote counting of votes cast on the measure. However, only 4 measures can be printed on a single ballot card. Should this measure require printing an additional ballot card, the fiscal impact would be 53.4.

Prepared by: Joseph L. Swanson, Director Phone: 465-4511
 Division: Division of Elections Date: 2/1/94
 Approved by Commissioner: Lt. Governor John B. Coghill
 Agency: Office of the Lt. Governor Date: 2/1/94

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FISCAL NOTE

No. 2
 Bill Version: HJR 48
 (H) Publish Date: 4/8/94

STATE OF ALASKA
1994 LEGISLATIVE SESSION

BILL NO.

Revision Date: _____	Dept. Affected: <u>Revenue</u>	Revenue _____
Title: <u>Proposing amendments to the Constitution of the State Alaska</u>	BRU: _____	<u>Revenue Operations</u>
<u>relating to revenues from natural resources</u>	Component: _____	<u>Treasury Management</u>
Sponsor: <u>House Finance Committee</u>	COMPONENT SERIAL NO. <u>#121</u>	
Requestor: <u>House Judiciary</u>	_____	

Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY95	FY96	FY97	FY98	FY99	FY00
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0

CAPITAL						
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REVENUE FUND SOURCE:						
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FUNDING: (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	0	0	0	0	0	0

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year (FY94) impact: \$ 0.0

ANALYSIS: (Attach a separate page if necessary.)

The resolution would not impact the operations of the Treasury Division. Since the essential functions of the Division would not change, no change in staffing requirements or contractual services would be expected as a result of this resolution.

Prepared by:	Laraine Derr, Deputy Commissioner <i>Laraine Derr</i>	Phone: <u>465-2350</u>
Division:	Treasury	Date: <u>1/18/94</u>
Approved by Commissioner:	Darrel J. Rexwinkel <i>Darrel J. Rexwinkel</i>	Date: <u>1/19/94</u>
Agency:	Department of Revenue	

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