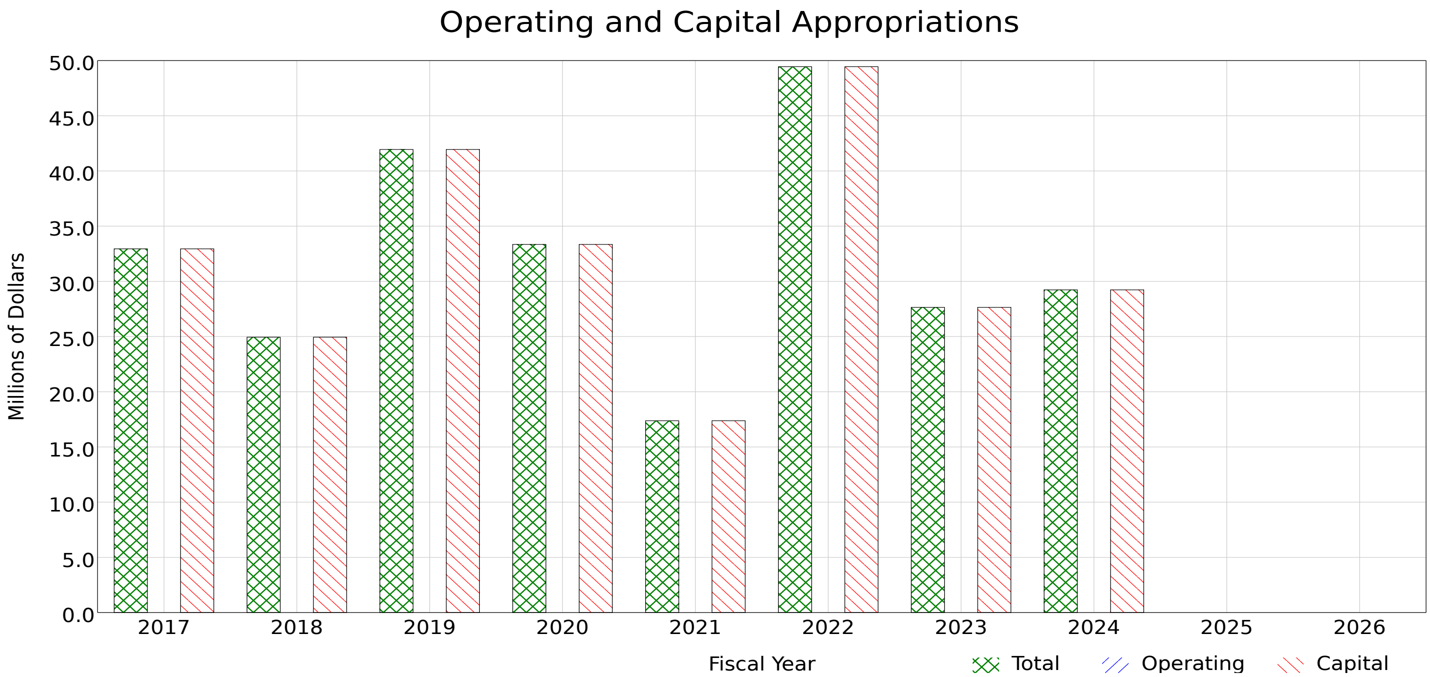
Fund Source Report

1197 AK Cap Fnd Alaska Capital Income Fund

Year Authorized	Year Repealed	Active?	Mental Health?	Duplicated?	Fund Group
FY05		Yes	No	No	Designated General



Legal Authority
AS 37.05.565

Source of Revenue
Money deposited to the fund under AS 37.13.145(d) and appropriations to the fund. AS 37.13.145(d) refers to earnings on the proceeds (with past interest and inflation proofing) of the Amerada Hess oil pricing settlement. At the time of the creation of the Capital Income Fund, the "fenced off" portion of Permanent Fund principal known as the Amerada Hess account was approximately $425 million and will remain at that level in the future.

Restrictions on Use
Money may be appropriated for state facilities preventive or deferred maintenance as of FY19. Prior to FY19, money could be spent for any public purpose, including to cover annual debt service and reserves for debt service on bonds authorized by state law.

Description and History
AS 37.13.145(d) states that money (and associated earnings) received as a result of State v. Amerada Hess (a dispute on oil pricing) are to be treated in the same manner as other earnings of the Permanent Fund except that money associated with the Amerada Hess case shall be excluded from the calculation of dividends. From 1992 until 2005, the law placed Amerada Hess earnings in a segregated account within the Permanent Fund in order to ensure that no judge or juror would be disqualified from service solely because of the case's impact on the dividend program.

When the case was settled out of court, the Alaska Supreme Court had no opportunity to issue the determination required to implement a conditional repeal clause. Because the legislature annually appropriated Am-Hess earnings to the corpus, the Am-Hess portion of principal continued to grow even after settlement of the case. Arguably, continued segregation of Am-Hess earnings is necessary to ensure that no judge or juror would be disqualified from a similar case in the future.

The Governor proposed (in the FY06 budget) issuing bonds secured by future earnings on the Am-Hess balance. The legislature instead created the capital income fund and appropriated Am-Hess earnings to it. Capital expenditures are viewed as being insufficiently direct or significant to affect a potential judge or juror.

Although the balance of the capital income fund is available for any purpose, FY05 and FY06 Amerada-Hess fund earnings were spent for capital projects, with an expectation that future earnings would also go toward capital projects via the capital income fund.

July 2010
The designation in AS 37.05.565--"any public purpose"-- is arguably too weak to justify classification as a designated fund. However, the intent of the

legislature was that the fund would be used for capital projects. In addition, because deposits of earnings show as transfers from the PF ERA, the capital income fund is classified as designated general funds (to match the original fund source). Expenditures from the capital income fund do not affect the UGF surplus/deficit because the ERA is excluded from the UGF revenue stream.

In 2009, the PF opted to recover 2008 market losses by declining to transfer Am-Hess earnings to the CIF until the Am-Hess balance was returned to the pre-loss value. A September 5, 2009 discussion paper (Teal to Finance Co-Chairs) reviews the situation. Although contrary to appropriation language, the legislature declined to challenge or approve the PF's actions. Transfers to the capital income fund were not made in FY09 or FY10, and a partial transfer occurred in FY11.

December 2016
As noted in the description of fund code 1041, the ERA is available to spend for any purpose at any time. By definition, the ERA is unrestricted general funds. Its pre-FY17 classification as DGF was due to (1) tradition limiting use of the ERA to paying dividends and inflation-proofing and (2) potential distortion associated with reporting earnings of the permanent fund as general fund revenue while also classifying the earnings as "not available for spending." Under any statute or plan that envisions payouts to the general fund, the ERA must be classified as UGF.

Implications of this change include:
1. Appropriations from the ERA (other than to the PF corpus) are classified as UGF regardless of whether an appropriation is directly from the ERA or passes through the general fund.
2. Distortion in reporting a surplus/deficit is avoided by reporting an amount equal to ERA appropriations as UGF revenue. Note that neither the available balance of the ERA nor unappropriated current earnings are to be reported as revenue.
3. Although appropriations from the ERA to the corpus are inter-fund transfers; they appear as revenue and appropriations in keeping with the change in the status of the money from spendable ERA to unspendable corpus.
4. Code 1171 (PFD appropriations in lieu of dividends to criminals) is a secondary appropriations of UGF and must be classified as "other duplicated."
5. Code 1197 (capital income fund) is "renamed ERA" and shows as a zero transfer (UGF ERA to UGF CIF) and as a UGF appropriation from the CIF.

Various CIF transfers make keeping track of the deficit difficult. All ACIF transfers are now reflected in the Fund Transfers section.
-The transfer to the fund from the ERA is noted as a revenue adjustment on the fiscal summary;
-Transfers into the fund from the ERA and gambling tax are shown as transfers into the fund (positive fund transfers);
-Spending using fund code 1197 is shown as a transfer out (negative fund transfer);
-The fiscal summary or an allocation summary shows the net.

This avoids any impact to the deficit from transfers or spending with the fund. It requires more transactions, but should have the cleanest result.

May 2018
With the passage of SB107, designated uses of the CIF became limited to preventive and deferred maintenance of state facilities. In combination with AS 37.13.145(d), which diverts a source of revenue to the CIF, two changes to budget reporting are required:
1. Amerada-Hess earnings should be identified in the Revenue Sources book as DGF revenue (rather than as UGF revenue). Deposit of Am-Hess earnings to the CIF occurs without a transaction--the CIF is simply spent as DGF code 1197. Neither Am-Hess earnings nor 1197 CIF appropriations affect the UGF deficit.
2. Budget structure requires an allocation for the CIF only if money other than Am-Hess earnings goes into the CIF (because that money should not be spent as code 1197, which applies only to the designated Am-Hess revenue stream).
a. If the CIF were an allocation under fund capitalization (duplicated), money would be counted on the way into the fund. This may discourage deposits (because they would add to the level of spending in the current year) and distort the timing of cash flows leaving the treasury.
b. If the CIF were an allocation under fund transfers, money would be counted on the way out of the fund. This may encourage deposits (because they would not add to the level of spending in the current year). However, spending past deposits could reduce the apparent size of a future budget, which could create a hole in the budget the following year.

While there are advantages and disadvantages to both approaches, a fund transfer allocation is the lesser of two evils because it is consistent with an attempt to report the timing of money leaving the treasury.

In order to allow future non-Am-Hess deposits into the CIF to be reported as transparently as possible, a new fund code (1258) will allow UGF appropriated to the CIF to retain the UGF classification as it is appropriated from the fund.

There will be no attempt to clean up past deposits to the CIF; future CIF account balances will be tracked by spreadsheet but will not have tracking transactions in the budget system.

July 2020
Ch. 88, SLA 2018 (SB 107) changed the appropriation to the AK Capital Income Fund from UGF to DGF while the deposit of Amerada Hess revenue occurs without a transation. Appropriations from the AK Capital Income Fund are reported as fund code 1197 (DGF). Starting with the FY21 fiscal summary, the UGF fund transfer is no longer reflected, consistent with the May 2018 description of the budget impact resulting from SB107.