Alabama

Alabama Trust Fund
Synopsis

Market Value
Albania Trust Fund
$2.96 billion

Santiago Compliance Index
Not rated

Resource Governance Index
Natural Resource Fund Score
Not yet rated

Truman Sovereign Wealth Fund Scoreboard
67 / 100

Fund Highlights

- The Alabama Trust Fund was established in 1985 to capture oil and gas royalties and revenues from drilling rights. It was designed to fund government expenditures from the financial return on invested natural resource revenues.

- In addition to the state budget, oil and gas revenues directly finance seven funds, including the Alabama Trust Fund. The Alabama Trust Fund, in turn, directly finances five funds, plus the state budget. A set percentage share of revenues is allocated to each fund.

- Withdrawals from the fund are supposed to equal investment income over a 3-5 year period, ensuring that the Fund’s principal is maintained or grows over the long-term.

- The Fund is managed by a Board of Trustees which includes the Governor. It is overseen by the Alabama Legislature and its audit department.

- The Fund releases quarterly reports which contain extensive information about investments and investment managers, including their returns and fees charged.
## Timeline and Fund Objectives

### Fund Inception
- The Alabama Trust Fund was created in 1985 through Amendment 450 of the Alabama State Constitution.²
- The Alabama Trust Fund replaced the Alabama Heritage Trust Fund by absorbing the Heritage Trust Fund’s remaining funds in 2001.³

### Fund Objectives
- The Alabama Trust Fund was created as a saving fund to manage revenues from offshore oil and gas resources.⁴
- The Alabama Trust Fund is used to help fund state budget expenditures through the state’s General Fund.
- The Fund is also used as a development fund whose income is used to finance various other trust funds including:
  - Forever Wild Land Trust Fund
  - Alabama Senior Services Trust Fund
  - County Government Capital Improvement Fund
  - Municipal Government Capital Improvement Fund
  - Education Trust Fund

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1. **TIMELINE**
   - 1978: Natural gas is discovered in Mobile Bay off the coast of Alabama.
   - 1982: Amendment 450 creates the Alabama Trust Fund. The new Fund captures revenues from royalties and sales of drilling rights and, unlike the Alabama Heritage Trust Fund, is irrevocable.
   - 1985: Amendment 543 creates the Forever Wild Land Trust Fund. The amendment redirects the 10% of the Alabama Trust Fund’s income that was previously reinvested into the new Fund.
   - 1992: The Alabama Heritage Trust Fund officially ceases to function and all its remaining assets are transferred to the Alabama Trust Fund.
   - 2000: 35 percent of oil and gas revenues previously deposited into the Fund are diverted to two new funds (see page 5), reducing the Alabama Trust Fund’s share of revenues to 65 percent. The Fund’s Board of Trustees is also permitted to withdraw up to 75 percent of the Fund’s equity capital gains.
   - 2001: Amendment 709 creates an Education Trust Fund Rainy Day Account within the Alabama Trust Fund.
   - 2002: Amendment 856 establishes the current withdrawal rules for the Fund.
   - 2008: A General Fund Rainy Day Account within the Alabama Trust Fund is created by amendment 803.
   - 2012: The Alabama Heritage Trust Fund officially ceases to function and all its remaining assets are transferred to the Alabama Trust Fund.
Good Governance Standards and Gaps in Regulation

**OPERATIONS**
- Objectives are Clear
- Rule for How Much Can be Withdrawn in Any Given Year
- Rule for Which Revenues Must be Deposited and When
- Exceptions to Rules are Clarified

**INVESTMENT**
- Use of Resource Revenues as Collateral
- Domestic Investment is Explicitly Prohibited
- Investment Risk Limitations
- Publication of Specific Investments

**MANAGEMENT**
- Penalties for Misconduct by Fund Managers & Staff
- Ethical & Conflict of Interests Standards for Managers & Staff
- The Detailed Responsibilities of Fund Managers & Staff
- The Role of Government Agencies in Fund Management

**TRANSPARENCY AND OVERSIGHT**
- Public Disclosure of Independent External Audits
- Public Disclosure of Internal Audit Results
- Formalized Oversight Mechanism
- Public Disclosure of Regularly Compiled Fund Reports

Each box represents a regulatory standard essential for promoting consistent use of and safeguarding resource revenues. White boxes highlight regulatory gaps in fund governance.

**12/16**
Good Governance Standards Met
Money from the Alabama Trust Fund is disbursed to six different funds.

Operational Laws, Rules and Policies

**Fund Deposit Rules**

- Revenues deposited into the Alabama Trust Fund consist of oil and gas capital payments. Alabama’s Constitution defines this as any payment, including royalties, received by the state from the sale or lease of exploration and drilling rights to offshore oil, gas and hydrocarbon minerals. However, this excludes taxes.5

**1985 – 1999**

- One percent of oil and gas revenue is transferred to the Department of Conservation Lands Division with the remainder deposited into the Alabama Trust Fund.6

**2000 – 2011**

- The Alabama Trust Fund’s share of oil and gas revenues is reduced to 65 percent as the remainder is diverted to two newly created funds. 7 percent of oil and gas revenues is transferred to the County and Municipal Government Capital Improvement Trust Fund. 28 percent to the Alabama Capital Improvement Trust Fund. These new funds were created to finance infrastructure spending and economic development.7

**2012 – present**

- The Alabama Trust Fund’s share of oil and gas revenues is reduced further to 32 percent. Half of the revenue previously deposited into the Fund is diverted to the Forever Wild Land Trust Fund (10 percent of revenues), the County Government Capital Improvement Trust Fund (10 percent), the Municipal Government Capital Improvement Trust Fund (10 percent), and the Alabama Senior Services Trust Fund (one percent). The remainder goes to the state’s General Fund.8

**Fund Withdrawal Rules**

**1985 - 1992**

- 90 percent of the Fund’s interest and dividend income is transferred to the state’s General Fund for budget expenditures with the remainder reinvested in the Alabama Trust Fund.9

**1993 - 2011**

- The amount that was originally reinvested in the Fund is instead diverted to the Forever Wild Land Trust Fund, a newly created fund for the purpose of protecting and preserving the State’s natural lands and waters. The transfer to the Forever Wild Land Trust Fund is capped at $15 million per year.10

**2000 - present**

- If the Fund’s income exceeds $60 million in a given fiscal year, 10 percent of income is transferred to the County Government Capital Improvement Fund, 10 percent to the Municipal Government Capital Improvement Fund, 0.25 percent to the Alabama Senior Services Trust Fund (not to exceed $5 million a year) and the remainder to the state’s General Fund.11
Operational Laws, Rules and Policies

Fund Withdrawal Rules (continued)

• The Fund’s Board of Trustees may also withdraw up to 75 percent of the Fund’s capital gains on equity investments and distribute 10 percent to the County Government Capital Improvement Fund, 10 percent to the Municipal Government Capital Improvement Fund, 10 percent to the Forever Wild Land Trust Fund and the remainder to the state’s General Fund.¹²

2012 - present¹³

• Income from the Alabama Trust Fund is no longer defined as being the interest and dividends on the Fund’s investments. Income is now defined as 5 percent of the average annual market value of the Fund’s investment over the prior three fiscal years.
• The current annual transfer from the Alabama Trust Fund to the Forever Wild Land Trust Fund is now set to cease in 2032.
• If financial conditions are such that withdrawals from the Fund would be harmful to preserving the Fund’s investment assets, the Board of Trustees may vote to reduce any withdrawal amounts.
• Beginning in fiscal year 2012-2013 and ending in fiscal year 2014-2015, the Alabama Trust Fund transfers $145,796,943 to the state’s General Fund each year.¹⁴

Rainy Day Accounts¹⁵

• The Education Trust Fund and the General Fund are the only two funds that can actively withdraw more than what is allowed under the fund withdrawal rules from the Alabama Trust Fund, essentially treating the Fund as a zero-interest line of credit. However in both cases, the money needs to be paid back.
• The Education Trust Fund can withdraw as much as 6.5 percent of its previous year’s budget from an account within the Alabama Trust Fund called the Education Trust Fund Rainy Day Account. Any withdrawals from the Rainy Day Account must be repaid within six years.
• The General Fund can withdraw as much as 10 percent of its previous year’s budget from another account within the Alabama Trust Fund called the General Fund Rainy Day Account. Any withdrawals from the Rainy Day Account must be repaid within ten years.
Flow of Funds

Alabama Trust Fund

- Optional 6.5 percent of Education Trust Fund's previous year's budget (must be repaid in 6 years)
- One percent of Fund's income (not to exceed $5 million a year)
- One percent share of 33 percent of oil and gas capital payments

Education Trust Fund

- One percent of Fund's income (only until 2032 and not to exceed $15 million a year)
- 10 percent share of 33 percent of oil and gas capital payments
- 10 percent share of 33 percent of oil and gas capital payments

Alabama Senior Services Trust Fund

- 10 percent of Fund's income
- 10 percent share of 33 percent of oil and gas capital payments
- 50 percent of the income of the County and Municipal Government Capital Improvement Trust Fund

Forever Wild Land Trust Fund

- 10 percent of Fund's income
- 10 percent share of 33 percent of oil and gas capital payments
- 50 percent of the income of the County and Municipal Government Capital Improvement Trust Fund

County Government Capital Improvement Fund

- 10 percent of Fund's income
- 10 percent share of 33 percent of oil and gas capital payments
- 50 percent of the income of the County and Municipal Government Capital Improvement Trust Fund

Municipal Government Capital Improvement Fund

- Remainder of Fund's income
- Remainder of 33 percent of oil and gas capital payments
- Optional 10 percent of the General Fund's previous year's budget (must be repaid in 10 years)
- Additional $146 million a year for three years ending in 2015

General Fund

1 percent of revenues
32 percent of revenues
28 percent of revenues
7 percent of revenues

Oil and Gas Revenues

Department of Conservation Lands Division

Education Trust Fund Rainy Day Account

General Fund Rainy Day Account

Alabama Capital Improvement Trust Fund

County and Municipal Government Capital Improvement Trust Fund

33 percent of revenues
Investment Laws, Rules and Policies

Investment Authority
Responsibility for the Fund’s management rests solely with the Alabama Trust Fund’s Board of Trustees. In turn, the Board of Trustees contracts an Investment Consultant to assist with developing, implementing and reviewing investment policy. The Board also contracts investment managers to manage assets and a custodian institution to hold the Fund’s assets.

Investment Objectives
The Fund’s investment objective is to preserve the purchasing power of its assets and income. Under the Fund’s investment policy, returns should at minimum equal the sum of the inflation rate and the rate that funds are spent. The Fund seeks to minimize the risk of falling short of this requirement over rolling three- and five-year periods.

Investment Strategy
• The Alabama Trust Fund’s target asset allocation is reviewed periodically, with the current breakdown as follows:
  • 32 percent U.S. equity
  • 24 percent non-U.S. equity
  • 35 percent fixed income
  • 9 percent real estate
• Fixed income securities must be dollar-denominated and have at least a rating of Baa3 or BBB- from Moody’s, Standard and Poor’s or Fitch.
• No more than 15 percent of fixed income may be invested in a single industry, with no more than five percent invested in a single corporation.
• Investments should not exceed one percent of a domestic corporation’s total outstanding equity capital.
• No more than five percent of the Fund’s stock portfolio may be invested in any one non-U.S. corporation.

Policy on In-State Investments
Fund assets may be invested in Alabama.
### Allocation by Asset Class

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Allocation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real Estate</td>
<td>4%</td>
</tr>
<tr>
<td>Fixed Income</td>
<td>39%</td>
</tr>
<tr>
<td>U.S. Equity</td>
<td>34%</td>
</tr>
<tr>
<td>Non-U.S. Equity</td>
<td>23%</td>
</tr>
</tbody>
</table>

As of June 2013

### Non-U.S. Equity Allocation

<table>
<thead>
<tr>
<th>Non-U.S. Equity Allocation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Emerging Markets</td>
</tr>
<tr>
<td>Developed Europe</td>
</tr>
<tr>
<td>Other Developed Markets</td>
</tr>
<tr>
<td>Developed Asia</td>
</tr>
</tbody>
</table>

As of June 2013

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**Investment Laws, Rules and Policies**
Management and Accountability

Management and internal accountability

The Board of Trustees has ultimate responsibility over Fund management. It consists of the Governor, the Director of the Alabama Department of Finance, the State Treasurer, three additional members appointed by the Governor, two additional members appointed by the Lieutenant Governor and one member appointed by the Speaker of the House of Representatives.

The Board of Trustees contracts an external investment firm to serve as an Investment Consultant and assist the Board with developing, implementing and reviewing investment policy.

The Board of Trustees contracts external investment managers to handle day-to-day management of funds.

External accountability

The Department of Examiners of Public Accounts performs an audit that is released to the public. It operates as a part of the State Legislature under the direction of the Legislature’s Committee on Public Accounts. The Chief Examiner is appointed by the Committee.
Oversight and Safeguards

Oversight Mechanisms

• The Board of Trustees, which includes the Governor as its Chair, is empowered by the law to monitor and evaluate external investment managers to ensure compliance with investment objectives and the relevant regulations governing the Fund.

• Arbitrary withdrawals from the Fund are not allowed; transfers are set constitutional amendments. However, the Board of Trustees may vote to decrease withdrawal amounts if it is determined necessary to preserve the Fund’s investment assets.

• The Alabama Legislature oversees regular and independent external audits through its Department of Examiners of Public Accounts.

Common Oversight Mechanisms or Safeguards Not Present in Alabama

• Finances are not subject to regular and comprehensive internal audits.

• Aside from heightened public interest each time an amendment that impacted the Alabama Trust Fund was considered, there is little regular monitoring by citizens or civil society organizations.
### Transparency Laws, Rules and Policies

There is public disclosure of the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Yes/No</th>
</tr>
</thead>
<tbody>
<tr>
<td>When or how often Fund reports are published and made publicly available</td>
<td>yes</td>
</tr>
<tr>
<td>Which individuals or organizations are responsible for publishing Fund reports</td>
<td>yes</td>
</tr>
<tr>
<td>Size of the Fund(s)</td>
<td>yes</td>
</tr>
<tr>
<td>Deposit and withdrawal amounts</td>
<td>yes</td>
</tr>
<tr>
<td>Returns on investments</td>
<td>yes</td>
</tr>
<tr>
<td>Detailed asset allocation – geographic location</td>
<td>yes</td>
</tr>
<tr>
<td>Detailed asset allocation – asset class</td>
<td>yes</td>
</tr>
<tr>
<td>Detailed asset allocation – specific assets</td>
<td>yes</td>
</tr>
<tr>
<td>Natural resource prices and other fiscal assumptions used to calculate deposit and withdrawal amounts allowed under fiscal rules</td>
<td>no</td>
</tr>
</tbody>
</table>
Annex:
List of Applicable Laws

Amendment 450 of the Alabama State Constitution

Amendment 543 of the Alabama State Constitution

Amendment 666 of the Alabama State Constitution
http://alisondb.legislature.state.al.us/acas/CodeOfAlabama/Constitution/1901/CA-569853.htm

Amendment 803 of the Alabama State Constitution
http://alisondb.legislature.state.al.us/acas/CodeOfAlabama/Constitution/1901/CA-1842681.htm

Amendment 856 of the Alabama State Constitution
http://alisondb.legislature.state.al.us/acas/CodeOfAlabama/Constitution/1901/CA-2517997.htm
1. History of the Alabama Trust Fund, Alabama State Treasurer. Available at: http://www.treasury.state.al.us/Content/Documents/History%20of%20the%20Alabama%20Trust%20Fund%202006%2022%202012.pdf
Endnotes

22. Investment Policy Statement for the Alabama Trust Fund  
   February 2013, p. 15. Available at: http://www.treasury.state.al.us/ 
   Content/Documents/ATF%20Documents/ 
   SIGNED%20ATF%20Investment%20Policy%20February%202013.pdf

23. Investment Policy Statement for the Alabama Trust Fund  
   Content/Documents/ATF%20Documents/ 
   SIGNED%20ATF%20Investment%20Policy%20February%202013.pdf

   Review, Callan, June 2013, p. 9. Available at: 
   http://www.treasury.state.al.us/Content/Documents/ 
   ATF%20Documents/Meeting%20208212013/ 
   Agenda%20Item%204a%20-%20Quarterly%20Performance%20Report.pdf

25. Alabama Trust Fund Investment Measurement Service Quarterly  
   Review, Callan, June 2013, p. 55-69. Available at: 
   http://www.treasury.state.al.us/Content/Documents/ 
   ATF%20Documents/Meeting%20208212013/ 
   Agenda%20Item%204a%20-%20Quarterly%20Performance%20Report.pdf