

# AMHS STRATEGIC BUSINESS AND OPERATIONAL PLAN

## Phase Two Final Report

Prepared for: Southeast Conference • Juneau, AK

Ref: 17027-002-030-0

Rev. -

November 9, 2017



Table 18. AMHS F&2018 Enacted Budget (\$000)

Funding Source	General Fund (UGF)	Marine Highway (DGF)	CIP Receipts (other)	Motor Fuel (DGF)	Totals
Vessel Operations	\$26,407.6	\$71,263.6		\$3,552.4	\$101,223.6
Marine Vessel Fuel	\$15,379.6	\$4,844.0			\$20,223.6
Marine Engineering	\$53.1	\$1,514.0	\$1,711.9		\$3,279.0
Overhaul		\$1,647.8			\$1,647.8
Reservations & Marketing	\$56.3	\$2,003.0			\$2,059.3
Marine Shore Operations	\$108.9	\$7,768.3			\$7,877.2
Vessel Operations Management		\$4,005.4	\$138.1		\$4,143.5
<b>Totals</b>	<b>\$42,005.5</b>	<b>\$93,046.1</b>	<b>\$1,850.0</b>	<b>\$3,552.4</b>	<b>\$140,454.0</b>

Source: State of Alaska OMB

1.2.1.2 Capital Budget

State General Funds are also used to support AMHS capital projects, including direct allocation for vessel overall and maintenance, matching funds to secure federal dollars, and other project-specific needs. The \$11 million in the enacted FY2018 budget is described as funding for "vessel overhaul, annual certification, and shoreside facilities rehabilitation" [14]. Other state and federal capital project funding is described in some detail below.

Table 19. AMHS Annual General Fund Capital Expenditures (\$000), FY2012-2018

	2012	2013	2014	2015	2016	2017 Authorized	2018 Enacted*
<b>GF Capital Expenditures</b>	\$13,517	\$15,036	\$14,863	\$14,584	\$5,999	\$12,480	\$11,000

Note: Overhaul and maintenance, including deferred maintenance. Source: AMHS and OMB. 2018 enacted is funds UGF from the Statutory Budget Reserve (SBR).

1.2.1.3 Stability and Predictability of State Funding for AMHS

Today there is little certainty in any aspect of State government operations and program funding, presenting significant challenges for all organizations that depend on that funding, whether a school district or the ferry system. The unpredictable and sometimes last-minute nature of State General Fund budgeting for AMHS is often noted as a particular management challenge for the system. It is generally believed that with greater predictability and/or advance funding AMHS could publish schedules with greater lead times and offer more consistent service year-to-year. In fact, the importance of stable service levels underlies the creation of the Alaska Marine Highway System Fund, as described by the legislation and legislative intent language:

**AS 19.65.060. Alaska Marine Highway System Fund**

(a) There is created, as a special account in the general fund, the Alaska Marine Highway System Fund, into which shall be deposited

(1) the gross revenue of the Alaska Marine Highway System;

- (2) money that is appropriated to the Alaska Marine Highway System Fund by the legislature in an amount that is consistent from year to year and is the amount necessary, after consideration of gross revenue, to provide stable services to the public consistent with the provisions of AS [19.65.050](#) (b)(4), which appropriations are not one-year appropriations and the balances of which do not lapse under AS [37.25.010](#); and
- (3) any other money that is appropriated to the Alaska Marine Highway System Fund by the legislature, which appropriations are not one-year appropriations and the balances of which do not lapse under AS [37.25.010](#).
- (b) Nothing in this chapter exempts money deposited into the Alaska Marine Highway System Fund from the requirements of AS [37.07](#) (Executive Budget Act) or dedicates that money for a specific purpose.

### **AS 19.65.050. Legislative Findings, Purpose, and Intent**

- (a) The legislature finds that
- (1) the Alaska Marine Highway System is an essential part of the state transportation system, and that it warrants continued and predictable state support;
  - (2) many communities' economies are dependent on a steady and stable marine highway system service level;
  - (3) the state's tourism industry is greatly enhanced by a dependable marine highway transportation network; and
  - (4) efficient and prudent management of the system will benefit the state's economy and foster economic development.
- (b) It is the purpose of AS [19.65.050](#) - [19.65.100](#) to
- (1) enable the Alaska Marine Highway System to manage and operate in a manner that will enhance performance and accountability by allowing the system to account for and spend its generated revenue;
  - (2) provide the management tools necessary to efficiently operate the Alaska Marine Highway System;
  - (3) within constitutional constraints, provide for a predictable funding base for system operations; and
  - (4) provide for predictability and stability in the service level furnished to communities served by the system.
- (c) It is the intent of AS [19.65.050](#) - [19.65.100](#) to

- (1) encourage prudent administration through cost management and accurate budgeting by managers of the Alaska Marine Highway System;
- (2) increase revenue from the operation of the system consistent with the public interest, increase service consistent with sound fiscal policy, and assist the prudent management and operation of the system; and
- (3) achieve stability in the level of service communities can anticipate through accurate planning and scheduling.

Over the past few years as Alaska has struggled to adjust to sharply declining oil revenues, through budget cuts and expenditure of savings. Clearly, existence of the AMHS Fund has not been sufficient to "provide for a predictable funding base for system operations."

### 1.2.2 Governance and State General Fund Support

With regard to AMHS Reform, the question is, "how might a change in system governance enhance the predictability and stability of General Fund support?"

One potential remedy, forward funding, is independent of governance model. While there would be benefits associated with forward funding (discussed below), whether there is political will to restore the AMHS Fund with an amount sufficient for AMHS managers to plan with confidence a year in advance is unclear. The related but unanswerable questions are whether the legislature will continue to provide in the near term \$85 million to \$90 million in the General Fund for support of AMHS operations and in the longer-term, an annual amount sufficient to keep pace with inflation.

Forward funding could come in the form of a one-time capital or operating appropriation to substantially reconstitute the Alaska Marine Highway System Fund, or a larger capital appropriation that serves as a multi-year source of AMHS operating funds. Similar benefits could be realized by giving AMHS direct spending authority over its own operating revenues.

Greater political support for forward funding might be generated with clearer goals. For example, coupled with forward funding, annual General Fund support could be capped at its current level (with future adjustment for inflation only), which is already down by more than a quarter over the past five years. This would mitigate the concern that AMHS might require an ever-increasing amount of General Fund support, and provide some certainty to system management about future General Fund support. An overall farebox cost recovery goal could be established to guide the budgeting process, along with a stable funding amount. Great care would be required to develop a mechanism that incentivizes system management to enhance revenue (perhaps by allowing AMHS to use its own revenues without legislative appropriation) and carefully control costs so that such bottom-line improvements would not be met with an equal decline in General Fund support.

Another potential remedy would be better facilitated through the public corporation model. A multi-year fee-for-service (or contract for service) model might provide more state funding certainty for AMHS. The key assumption is that a multi-year contract between the state of Alaska and an AMHS public corporation would provide a higher level of certainty (though still

subject to annual legislative appropriation) than the current appropriation mechanism for providing AMHS with necessary General Fund support.

Such a contract might be structured to support some minimum level of service each year, with additional General Fund support provided annually, to fully fund the system, via customary legislative appropriation. Whether a contract for service framework would provide greater funding certainty for AMHS or not, would depend on the terms of the contract. A key question regarding the utility of the contract-for-service concept is whether it is legally practicable for the state to contract with itself, which would be the case with the state of Alaska contracting with an AMHS public corporation.

The contract for service concept is akin to the BC Ferries contract with the provincial government. The Coastal Services Contract is a binding 60-year agreement (signed in 2003) that defines BC Ferries routes and service levels. The contract is reviewed and updated at regular intervals [15].

#### 1.2.2.1 Benefits of State of Alaska Forward Funding for AMHS

Whether via long-term contract or other mechanism through the traditional legislative appropriation process, it is important to recognize the benefits of forward funding. While difficult to forecast, it is certain that for the same level of service, scheduling consistency from one year to next, and scheduling well in advance, would support more AMHS traffic and result in more revenue. Other systems recognize the importance of scheduling predictability. BC Ferries is required by its Coastal Ferry Services Contract to publish its schedule two years in advance.

As outlined below, better advance scheduling would have a variety of traveler and industry benefits.

##### 1.2.2.1.1 Additional Revenue from Alaska Visitors

The Alaska visitor industry and Alaska visitors in general would be the AMHS markets most likely to respond to earlier publication of schedules and more consistent schedules over time. Non-residents represent a large share of AMHS travelers, and a larger share of revenues, accounting for 42 percent of AMHS operating revenue from passenger, vehicle, and stateroom sales in FY2015. A large portion of non-resident revenue is from visitors traveling to Alaska for vacation/pleasure purposes (other non-resident AMHS travelers include seasonal workers, military transferees, students, and others relocating to Alaska for employment or other reasons). According to the Alaska Visitors Statistics Program (AVSP) VII, 44,000 visitors entered or exited Alaska via ferry, or used the ferry to travel between Alaska communities [16].

Many Alaska visitors make trip decisions well in advance of their travel. For example, more than a third (37 percent) of visitors that traveled on AMHS during the summer of 2016 made their trip decision more than eight months in advance [16]. It is clear that earlier booking opportunities would stimulate traffic among the independent travelers who prefer to plan and book well in advance.

Most Alaska visitors prefer to purchase travel as part of package, including transportation, lodging, and often excursions and tours. However, it is now virtually impossible to include the

marine highway in a package. Tour companies print brochures 18 months in advance and need pricing, routing and scheduling information a few months in advance before printing. With prices and schedules available two years in advance, AMHS would once again position itself as an attractive, high-value component in Alaska travel packages. AMHS could leverage the national marketing campaigns conducted by cruise lines, which highlight the appeal of coastal Alaska.

More non-resident AMHS riders would mean more revenue for the system and greater economic benefit to the state and communities from that travel. In 2016, visitors travelling by ferry stayed in the state an average of 13.9 nights, longer than the other markets and they spent an average of \$1,914 per person while in Alaska (almost twice the all-visitor average of \$1,057). Non-resident visitors using AMHS traveled (and spent money) throughout the state. More than half (51 percent) visited Anchorage and a quarter (25 percent) visited Fairbanks.

#### 1.2.2.1.2 Other Business and Economic Development Benefits

During the public outreach process conducted for purposes of the AMHS Reform project, it was often noted how important AMHS is to the economies of communities served by AMHS, particularly communities without connection to road networks or regional service and supply hubs. The visitor and seafood industries, as well as transportation or basic consumer goods, were noted as areas where more predictable, reliable service could better sustain local economies or support economic development.

No data is available on the volume or value of seafood shipped by AMHS, however it is evident that the system serves an important role in filling the service gap between barge and airfreight. The primary ports where AMHS supports seafood shipping are Kodiak, Cordova, Petersburg, Wrangell, and Juneau. From these ports seafood is shipped to AMHS ports with road access like Homer, Whittier, Skagway, Prince Rupert, and Bellingham [17]. More predictable service year-to-year could facilitate market development and spur additional shipment of seafood on AMHS.

#### 1.2.3 Federal Funds

The federal government is an important source of capital funds for AMHS. Federal-aid funding is not available for operation and routine maintenance of ferries.

##### 1.2.3.1 Ferry Boat Program

The Ferry Boat Program (FBP) provides federal funding for the construction of ferries and ferry terminal facilities. Projects that extend the useful life of ferry facilities are also eligible. The FBP requires a 20 percent match. The program has provided a steady and generally predictable annual source of funds for AMHS-related vessel and terminal improvements.

Under MAP-21 (Moving Ahead for Progress in the 21<sup>st</sup> Century), program funds were distributed to eligible entities based on the number of passengers carried (20 percent), vehicles carried (45 percent), and total route miles (35 percent). The December 2015 Fixing America's Surface Transportation (FAST) Act changed the funding formula to 35 percent based on the number of ferry passengers (including passengers in vehicles, carried by each ferry system); 35 percent based on the number of vehicles carried by each ferry system; and 30 percent based on the total route nautical miles serviced by each ferry system. The FAST Act continues total