



THE STATE
of **ALASKA**
GOVERNOR BILL WALKER

Office of the Governor

OFFICE OF MANAGEMENT AND BUDGET
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October 23, 2015

The Honorable Pete Kelly
Co-Chair, Senate Finance Committee
Alaska State Legislature
State Capitol, Room 518
Juneau, AK 99801-1182

The Honorable Anna MacKinnon
Co-Chair, Senate Finance Committee
Alaska State Legislature
State Capitol, Room 516
Juneau, AK 99801-1182

Dear Co-Chair Kelly and Co-Chair MacKinnon,

Thank you for the opportunity to answer the Committee's questions about the Governor's budget philosophy before the Senate Finance committee on October 5, 2015. The following is in response to questions posed by the committee during the hearing for distribution to the members.

1. What is the daily "burn rate" on our savings accounts? Given a price of \$50 per barrel of oil scenario, what date will our savings accounts be depleted?

Based on \$50/bbl oil, the expected FY16 CBR draw is about \$3.2 billion, which is equivalent to spending about \$8.8 million daily ($\$3.2 \text{ billion} / 365 = \$8.76 \text{ million per day}$).

If the price of oil stays at \$50/bbl, we estimate savings account will be depleted by early September, 2018.

NOTE: Division of Finance and the Department of Revenue do cash projections, "burn rates", projected daily spending, and cash transfers from savings (CBR) to the GF based on actuals. There are often timing and other differences to budget. Our response provides a mathematical calculation of the daily budget spend and the anticipated CBR depletion date. This is important in case a different number on the daily "burn rate" is provided and there is confusion.

2. Will your administration introduce legislation this session that will utilize the Permanent Fund to help balance future budget shortfalls?

The Administration is in the process of developing an overall plan and will be introducing legislation.

3. Has the administration reevaluated its revenue forecast given the current price of oil? What is the current budget deficit projected at current oil prices?

Based on \$50/bbl, FY16 budget deficit is projected at \$3.2 billion. The table below shows the projected deficit at various oil prices.

Oil Price (per barrel)	FY16 Projected Deficit (\$billion)
\$75	\$2.5
\$70	\$2.6
\$66 (official Spring Forecast)	\$2.7
\$65	\$2.8
\$60	\$2.9
\$55	\$3.1
\$50	\$3.2
\$45	\$3.3
\$40	\$3.4

4. What price per barrel are you using to budget for FY 2017 and what shortfall will it create?

The Fall Revenue Forecast will be released soon. It will likely reduce oil price projections from the spring. We are using \$45 - \$60 as our range in the budget development process.

5. Provide an update on current bargaining agreements and their financial impact on future budgets. In addition, what impact did the unallocated reduction, used to pay for FY16 salary increases, have on the rest of the budget?

An update on current bargaining agreements is summarized in the table below.

Contracts currently in negotiations (expired June 30, 2015)	
Labor, Trades and Crafts (LTC)	State's last proposal contained a zero COLA for each of the three years
Teacher's Education Association of Mt. Edgecumbe (TEAME)	State's last proposal contained a zero COLA for each of the three years
Marine Engineers Beneficial Association (MEBA)	Expired July 1, 2014. MEBA has not sent the contract to its members for a ratification vote. A zero COLA is in effect until the contract is ratified.
Contracts that will be negotiated this fall (expire June 30, 2016)	
Alaska State Employees Association (ASEA)-representing the General Government Unit (GGU)	ASEA has sent a request to begin negotiations at the end of October
Alaska Public Employees Association (APEA)-representing the Supervisory Unit (SU)	
Confidential Employees Association (CEA)	
Contracts currently under agreement	
Public Safety Employees Association (PSEA)	Expires June 30, 2017 2% COLA due for FY17
Alaska Vocational Technical Center Teachers' Association (AVTECTA)	Expires June 30, 2017 1% COLA due for FY17
Masters, Mates and Pilots (MM&P)	Expires June 30, 2017 2% COLA due for FY17
Inland Boatmen's Union of the Pacific (IBU)	Expires June 30, 2017 2% COLA due for FY17
Alaska Correctional Officers Association (ACOA)	Expires June 30, 2018 1% COLA due for FY17; 2.25% COLA due for FY18

The executive branch absorbed the entire \$29.8 million unallocated reduction, thus the legislative and judicial branches were held harmless. Each agency has gone through and identified individual reductions to accommodate the reduction. The unallocated reduction on the budget means a \$29.8 million reduction on top of the \$340 million cut in the agency operations.

FY2016 Enacted Department Summary
Unallocated Reduction

	UGF		COLA by Dept.	Dist of Unalloc.	FY2016 w Dist.of Unalloc.	% UGF FY15 Mgt Plan to FY16 w Unalloc.
	FY2015 Management Plan	FY2016 CCHB2001 From Leg Finance				
Non-Formula						
Administration	86,030.2	76,383.9	994.6	-1,216.6	75,167.3	-12.6%
Commerce	40,454.3	27,707.3	339.1	-1,100.0	26,607.3	-34.2%
Corrections	297,654.4	281,178.0	2,450.1	-3,891.5	277,286.5	-6.8%
Educ & Early Devel	57,419.6	42,363.3	329.8	-674.8	41,688.5	-27.4%
Environ Conservation	22,472.1	20,468.5	375.2	-375.2	20,093.3	-10.6%
Fish and Game	79,387.8	66,443.3	1,347.9	-1,347.9	65,095.4	-18.0%
Governor	33,609.5	23,538.9	388.9	-388.9	23,150.0	-31.1%
Health & Social Svcs	388,277.2	368,277.9	4,666.5	-5,864.3	362,413.6	-6.7%
Labor & Workforce	33,448.0	26,249.6	235.3	-418.1	25,831.5	-22.8%
Law	61,275.3	53,973.3	927.7	-927.7	53,045.6	-13.4%
Alaska Aerospace Corp	6,084.3	100.2		-100.2		-100.0%
Military & Veterans Affairs (Except AAC)	18,105.3	16,765.8	274.2	-274.2	16,491.6	-8.9%
Natural Resources	88,072.8	71,464.3	1,062.0	-1,138.3	70,326.0	-20.2%
Public Safety	171,553.2	163,274.3	1,457.7	-2,600.6	160,673.7	-6.3%
Revenue	33,831.4	29,515.2	532.2	-532.2	28,983.0	-14.3%
Transportation	278,604.6	247,963.9	1,393.9	-3,949.5	244,014.4	-12.4%
	27,000.0	-29,800.0				-100.0%
Executive Agencies Non-Formula	1,723,280.0	1,485,867.7	16,775.1	-24,800.0	1,490,867.7	-13.5%
University of Alaska	370,599.7	355,787.0	10,073.0	-5,000.0	350,787.0	-5.3%
Judiciary	111,866.3	110,402.9	2,279.5		110,402.9	-1.3%
Legislature	77,622.0	73,397.9	1,171.3		73,397.9	-5.4%
				-29,800.0		

6. Update the committee on any privatization activities the administration is pursuing at this time and the potential savings they may achieve.

Health & Social Services

DHSS is currently discussing the privatization option and feasibility for the Alaska Pioneer Homes and the Alaska Psychiatric Institute (API). They are intending on having a Request for Letters of Interest prior to the start of session.

Pioneer Homes (6)

Anchorage	Ketchikan
Fairbanks	Palmer
Juneau	Sitka

Labor and Workforce Development

Given the reduced federal funding available to support physical Job Centers, the Department is going to look for opportunities where private, non-profit, or local governments can take over providing Job Center services in their communities. For example, as of July Job Center services in Barrow are being offered through the North Slope Borough Mayor's Job Program. The Department is also developing a partnership with the library in Mt. View to better reach the individuals in that community without creating another Job Center, which is not financially feasible.

Under the federally-funded Workforce Innovation and Opportunity Act, the Vocational Rehabilitation program must provide more pre-employment and training services to disabled youth transitioning from high school, and we are doing this through private and non-profit community service providers.

The Department is also participating in the cross-department review of collections, and this will likely result in the privatization of collection activities (mostly from overpaid unemployment benefits).

Department of Administration and the Shared Services Model

In May we held an all-department retreat to consider cross-departmental efficiency initiatives. Eleven initiatives were adopted which are shown below.

Initiative
Train and implement process improvement principles statewide
Travel process revamp
Renegotiate Procurement / Lease Contracts for 10-20% Savings Statewide
Implement IRIS
Smart Justice
Unified facility maintenance management
Central collections office for agency fines, debts and attachments
Re-examine charge back system between departments
Streamline billing for Law
Minimize the number of prisoner transports through better use of technology
Statewide IT consolidation; call centers, disaster recovery, helpdesk staff, data storage

In September, the Department of Administration entered into a contract with a public sector shared services consultant.

- Several of the 11 initiatives are candidates for Shared Services
 - Travel process
 - Implement IRIS (fiscal, accounts payable, procurement)
 - Unified facility maintenance
 - Centralized collections (see next page for details)
 - Charge back system

- IT consolidation

Shared services targets administrative or support functions performed by multiple departments in a silo-ed and non-standard way.

- Standardizes the function
- Incrementally takes down the silos, and consolidates the function into a shared services organization
- Improves the function; eliminates unnecessary processes
- Ultimately automates the function
- Establishes daily performance metrics for the function

Shared services does not generally privatize the function.

- We are evaluating outsourcing for state debts not currently being collected.
 - In Ohio, the shared services organization outsourced uncollected debt.
 - New cash flow from uncollected debt was used to defray the rates of the shared services organization.

Shared services can reduce costs

- 30% cost-reduction estimates

Shared services can improve quality

- In Ohio, if performance metrics are met, bonus pay; if not met, termination in 60 days

Shared services can reduce delay

- In Ohio, reduction of accounts payable from 56 days to 1.7 days

Collections

- Collections for FY2015: about \$39.2 million
- Total unpaid balance: about \$398 million
- Number of accounts: about 387,400
- Current number of employees: 30

These totals include debts owed to the State and victim restitution which may be owed to a third party. Note that a significant portion of the unpaid balance is not viably collectible. Most of the accounts are debts ordered in criminal cases and many debtors may be in jail or simply do not have any money. For example, one debtor owes over \$17 million in restitution for shooting the pipeline.

7. Has your administration taken any additional budget reductions since the end of the second special session?

There have been no other budget reductions besides the allocation of the \$29.8 million unallocated reduction.

8. What is the administration's best guess estimate on an FY16 Supplemental?

There are four supplemental requests known at this time. However, it is early in the fiscal year and difficult to know how many more to expect. Two are identified in the Department of

Health and Social Services, Office of Children's Services, and Division of Juvenile Justice; TransCanada buyout and related gas line costs; and an organizational grant for Big Lake per AS 29.05.180 to the Department of Commerce, Community and Economic Development.

9. Is the Administration going to pursue Pension Obligation Bonds the session? If so, please provide information on their impact to the operating budget and the unfunded liability.

The Administration has not made a decision on whether Pension Obligation Bonds (POB) will be a part of FY17 budget request. Decisions on POB will require a significant level of due diligence and assessment of market timing.

The Department of Revenue is analyzing the savings possibilities through an issuance of POB. Depending on the size of the issue we would expect annual budget savings of \$20 million or more.

POB is a state supported taxable issuance of debt. It can save the state money over the long term if the investment return on the bond proceeds exceeds the debt service costs

Current estimate of debt costs is 5.3% and current investment return assumption is 8.0%.

POB may make sense, for instance, where the state is already paying for unfunded pension liabilities (past service costs). For example, the State pays the majority of TRS past service costs through GF funded state assistance in the operating budget. TRS state assistance will be approximately \$131 million in FY17 increasing to \$332 million by FY39. POB debt service on remaining TRS unfunded liability (\$2.3B) would be approximately \$153 million fixed for 30 years.

Funding up TRS could help system deal with liquidity demands as benefit cash flow increases in this closed plan.

Also, it can provide additional security for constitutionally secured promise in low oil price environment.

The Alaska Pension Obligation Bond Corporation was legislatively established in 2008, and authorized to issue up to \$5B in pension obligation bonds.

Currently a variety of PERS/TRS approaches under consideration and the risk is real because investment proceeds at some point will earn less than 8.0% in a particular year. The current 25 year pension system return is 7.97%.

*10. Please update the committee on the impact of the recently adopted expansion of the Medicaid Program.
a. Has the Xerox system been certified by the Federal Government? If not, when?*

As of September 27, 2015, there were 1,775 individuals enrolled in the new Medicaid expansion group. Four hundred thirty-seven of these were formerly on the 100% state funded program Chronic and Acute Medical Assistance (CAMA) so their medical costs have shifted to 100% federal funding.

The number of Medicaid applications received in September doubled compared with July or August. The new electronic method of applying for Medicaid is seeing results. Twenty-seven percent of the September applications were electronic compared with fifteen percent in July and eighteen percent in August.

Due to the lapse of time involved for providers to bill Medicaid, we have not yet begun to calculate actual expenditures. (This is not a Xerox issue, rather a timing issue.)

The Department plans to apply for system certification in December. We expect CMS to come on-site the first quarter of next calendar year.

11. Will the Administration be requesting additional money for the AKLNG project, including a proposal to buy out TransCanada?

A request for additional funding for the AKLNG project, including a proposal to buy out TransCanada, will be proposed during the special session.

12. Does the Administration anticipate implementing a hiring freeze in the future?

We do not anticipate implementing a hiring freeze because every business unit has different needs. Instead of a hiring freeze, each agency is scrutinizing every vacancy and not filling positions that become vacant when viable. Formal guidance will be provided for this process. Though we are facing extremely challenging times, people still retire or move to other jobs. When this occurs, every effort is used to take advantage of the vacancy for savings; however some positions must be replaced.

Also, in these challenging times, flexibility to restructure is necessary to increase efficiencies. This may require elimination of some positions, while creating the need for other, yet fewer, positions. In order to reduce the overall workforce, it may be necessary to hire workers with a different set of skills. We do not want to impede any department efficiency, streamlining, or cost reduction efforts with additional administrative requirements.

Other Cost Saving Measures being used by Departments

The table below shows which departments are currently using furloughs to realize savings. These were imposed by the agencies.

	# of Positions	# of Days	Savings
DNR	45	5	\$117,800
Law	278	22	\$238,800
DOA	197	2-4	\$206,000
HSS	Has not yet decided how to implement		

Please let me know if you have additional questions.

Sincerely,



Pat Pitney
Director

cc: David Teal, Director, Legislative Finance