THE STATE of ALASKA
GOVERNOR MICHAEL J. DUNLEAVY

Office of the Governor

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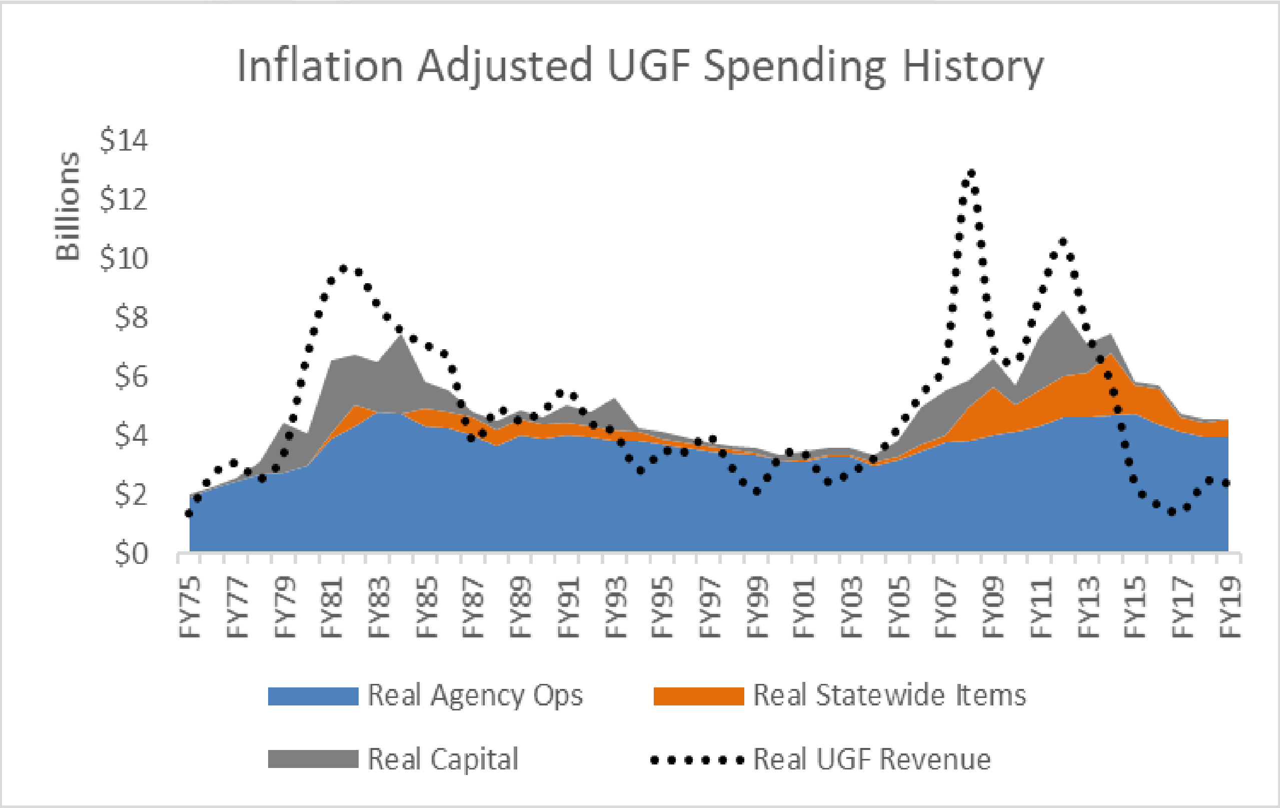
March 25, 2019

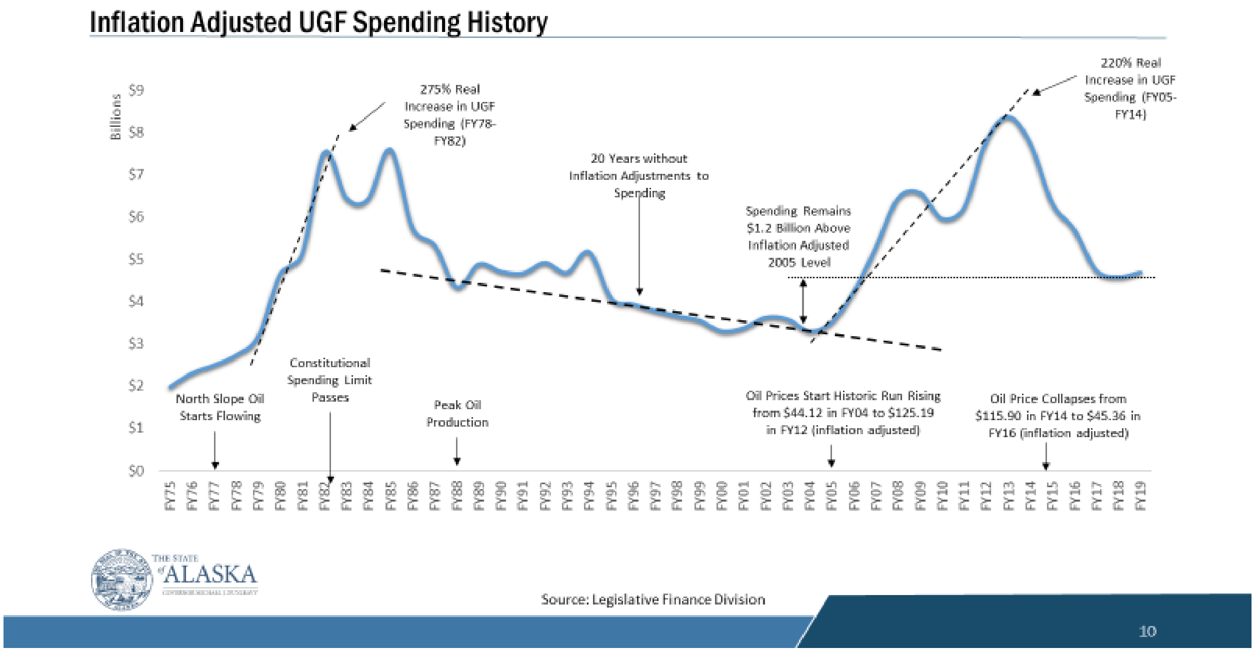
The Honorable Mike Shower
Chair, Senate State Affairs Committee
State Capitol Room 510
Juneau, AK 99801

Dear Senator Shower:

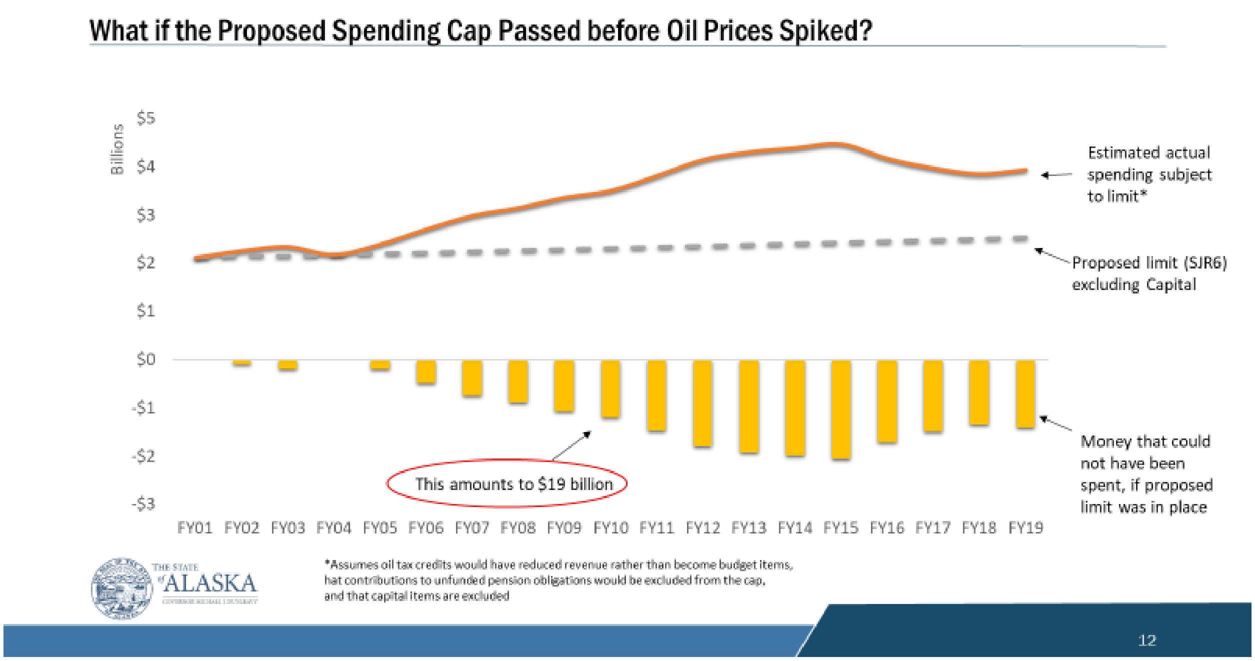
The purpose of this letter is to provide you with responses to the questions asked during the March 21st, 2019 committee hearing regarding Senate Joint Resolution 6 (SJR 6). Please see the questions in ***bold italics*** and our responses immediately below the questions.

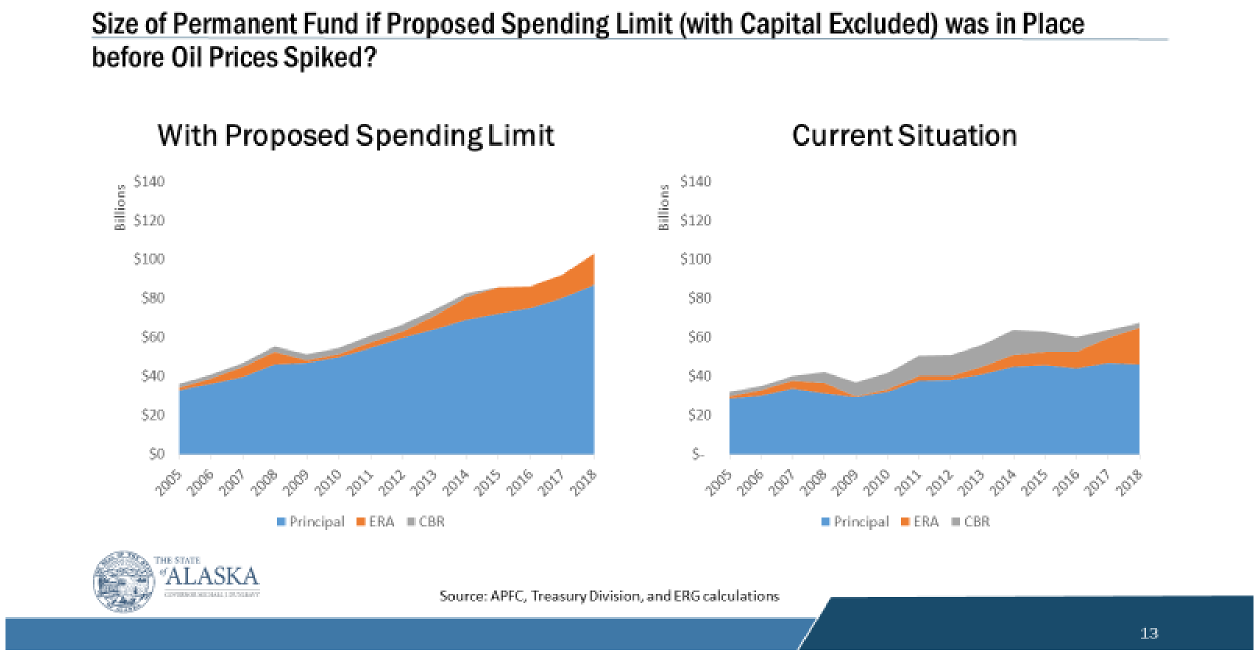
1. ***Senator Micciche requested an alternate graph to the ones provided on slides 9 and 10 of our presentation, which adjusts the values for inflation. Here are those graphs:***






2. ***Senator Coghill requested slides 10 and 11 to be updated to reflect capital expenditures as an excluded item from the proposed spending cap. Here are those graphs:***

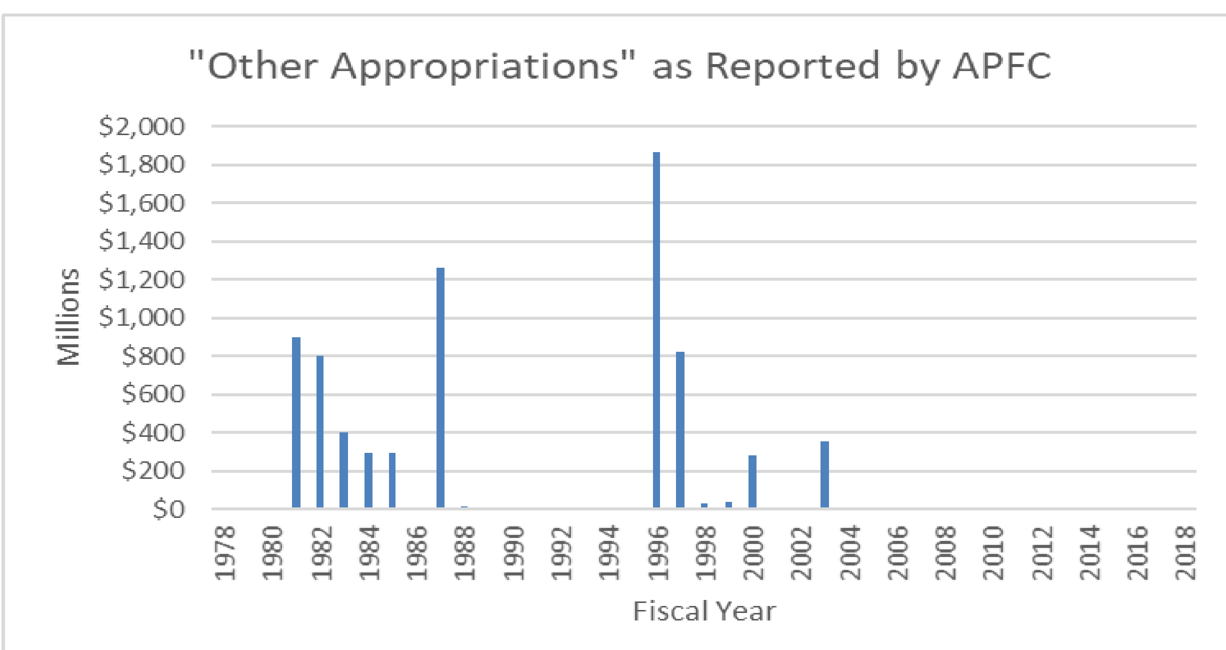




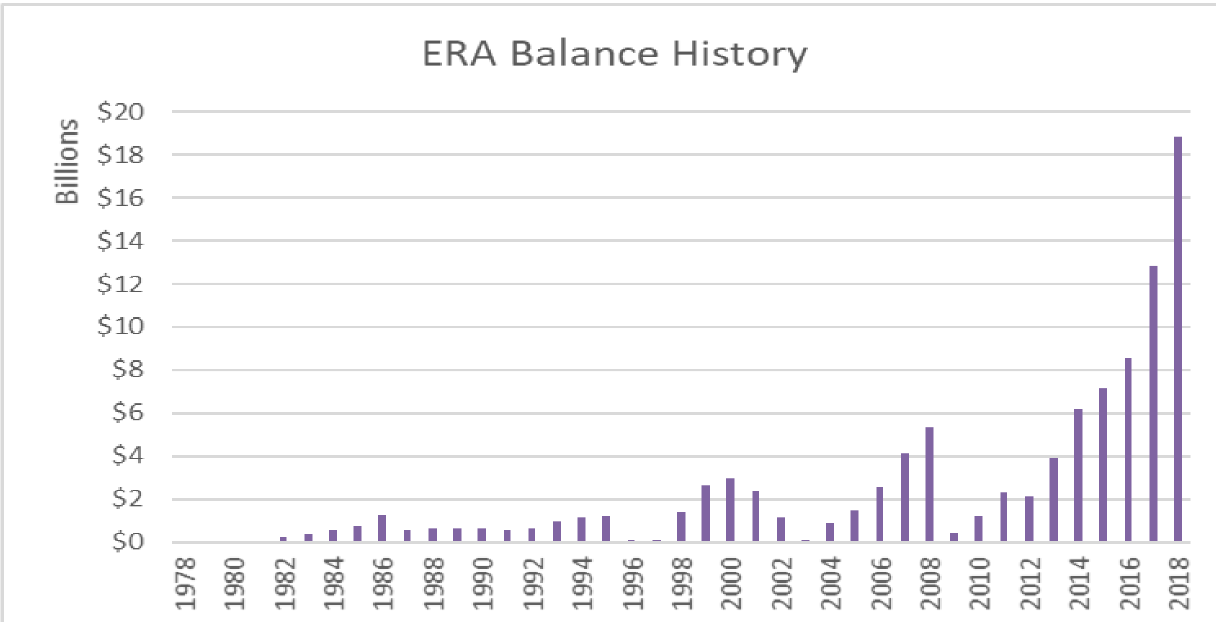

3. ***Senator Micciche asked what the Permanent Fund Principal account balance would be today, if the legislature had not elected to make special appropriations in the past.***

As background, all earnings from the Permanent Fund are placed in a holding account known as the “earnings reserve account” or ERA. Each year, the legislature decides what to do with those earnings. They typically use about half of them to pay dividends and transfer a portion to the ERA to offset inflation. The remaining amount has historically been either held in the ERA or has been transferred to the principal account. When those additional transfers are made, they are considered “special appropriations.”

The following is a graph of historical special appropriations:



The 1981 appropriation is often considered the original capitalization of the fund, with an amount similar to the 1969 lease sale. Special appropriations stopped in the 1990's, until the legislature swept the ERA balance into the principal account in 1996. Between 1981 and 2003, a total of $7 billion of "special appropriations" have been made to the principal account.




No special appropriations have been made since 2003. From 2016 through 2018, the legislature also elected not to transfer the amount for inflation proofing. Instead, the excess earnings have remained in the ERA, allowing the balance to build to over $18 billion.

In total, from 1978 to 2018, $16.9 billion worth of royalty deposits were made to the principal account. Another $16.2 billion has been transferred to avoid the erosion of value from inflation. This totals $33.1 billion out of $40.2 billion of the principal account.

In a hypothetical scenario in which the legislature made no transfers to the principal account, other than for inflation, and assuming they made the inflation proofing transfers each year, the current balance would be $26.4 billion.

This implies that nearly $14 billion of the current principal account balance is attributable to special appropriations and the inflation proofing of those additional deposits. However, this scenario says nothing about whether that $14 billion would currently be sitting in the ERA or would have been used for some other purpose.

4. ***Senator Kawasaki asked a question regarding the reasons for the $5 billion of budget growth from 2005 to 2013.***

While this question was answered in committee, it may be worth providing additional information on that topic. As stated, the larger capital budgets during this period account for nearly $2 billion of budget growth. Statewide items, including contributions to unfunded pension obligations and purchase of oil tax credits under AS 43.55, added another $1 billion of budget growth.

The other $2 billion of growth is attributable to increases in agency operations. Here are how the departmental General Fund budgets changed between FY05 and FY13 (Note: Inflation over the same period totals 23.6%):

| Total General Fund Expenditures (millions) | 2005 | 2013 | Change | % Change |
|---|---|---|---|---|
| Health & Social Services | $490 | $1,000 | $510 | 104% |
| Education | $813 | $1,287 | $474 | 58% |
| Transportation | $103 | $311 | $208 | 202% |
| University of Alaska | $230 | $362 | $133 | 58% |
| Corrections | $154 | $278 | $124 | 80% |
| Public Safety | $84 | $172 | $87 | 104% |
| DCCED | $7 | $74 | $66 | 883% |
| Fish and Game | $28 | $82 | $54 | 190% |
| Administration | $51 | $99 | $48 | 95% |
| Alaska Court System | $59 | $105 | $46 | 79% |
| Law | $35 | $64 | $29 | 81% |
| Legislature | $37 | $61 | $25 | 68% |
| Labor & Workforce Dev | $14 | $38 | $24 | 171% |
| Revenue | $13 | $32 | $20 | 156% |
| Environmental Conservation | $13 | $27 | $14 | 114% |
| Natural Resources | $96 | $110 | $14 | 14% |
| Military & Veterans' Affairs | $10 | $23 | $13 | 134% |
| Governor | $20 | $31 | $11 | 56% |

In total, 2013 agency operations increased from the 2005 levels by $1.4 billion more than inflation.

If we can be of further assistance to the committee as it considers SJR6, please let us know.

Sincerely,

Ed King

Ed King
Chief Economist