

ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON WAYS AND MEANS

April 13, 2007

7:06 a.m.

MEMBERS PRESENT

Representative Mike Hawker, Chair
Representative Anna Fairclough, Vice Chair
Representative Bob Roses
Representative Paul Seaton
Representative Peggy Wilson
Representative Sharon Cissna
Representative Max Gruenberg

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE JOINT RESOLUTION NO. 5

Proposing amendments to the Constitution of the State of Alaska limiting appropriations from certain mineral revenue, relating to the balanced budget account, and relating to an appropriation limit.

- HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: HJR 5

SHORT TITLE: CONST. AM: APPROP. LIMIT/MINERAL REVENUE

SPONSOR(S): REPRESENTATIVE(S) KELLY

01/25/07	(H)	READ THE FIRST TIME - REFERRALS
01/25/07	(H)	W&M, JUD, FIN
04/04/07	(H)	W&M AT 7:00 AM HOUSE FINANCE 519
04/04/07	(H)	<Bill Hearing Canceled>
04/11/07	(H)	W&M AT 7:00 AM HOUSE FINANCE 519
04/11/07	(H)	Scheduled But Not Heard
04/13/07	(H)	W&M AT 7:00 AM HOUSE FINANCE 519

WITNESS REGISTER

REPRESENTATIVE MIKE KELLY
Alaska State Legislature

Juneau, Alaska

POSITION STATEMENT: Testified as sponsor of HJR 5.

DEREK MILLER, Staff

to Representative Mike Kelly

Alaska State Legislature

Juneau, Alaska

POSITION STATEMENT: Presented portions of HJR 5 on behalf of sponsor Representative Mike Kelly.

ROB CARPENTER, Fiscal Analyst

Legislative Finance Division

Legislative Affairs Agency

Juneau, Alaska

POSITION STATEMENT: Answered questions on HJR 5.

ACTION NARRATIVE

CHAIR MIKE HAWKER called the House Special Committee on Ways and Means meeting to order at [7:06:27 AM](#). Present at the call to order were Representatives Hawker, Roses, Gruenberg, Seaton, Cissna, Wilson, and Fairclough.

[7:07:24 AM](#)

HJR 5-CONST. AM: APPROP. LIMIT/MINERAL REVENUE

CHAIR HAWKER announced that the first order of business would be HOUSE JOINT RESOLUTION NO. 5, Proposing amendments to the Constitution of the State of Alaska limiting appropriations from certain mineral revenue, relating to the balanced budget account, and relating to an appropriation limit.

REPRESENTATIVE MIKE KELLY, Alaska State Legislature, testified as sponsor of HJR 5. He reminded the committee of the state's dependence on fluctuating revenues from steadily declining oil production. He expressed concern that future revenues would diminish until the start of a gas pipeline. He suggested that HJR 5 could provide significant assistance to the state's budget process by establishing a mechanism to control spending. The resolution would require the legislature to incorporate oil revenue into the budget "in any given fiscal year on a five-year rolling average. That is we look back four years, and we also look a year forward" He opined that there is pressure on the legislature to spend money, but little push to require a balanced budget. However, he suggested that the legislature should take steps to control the amount available for the state

to spend, especially in light of the numerous demands made upon it to increase funding in many areas.

7:13:53 AM

CHAIR HAWKER clarified that the "mineral revenue" in HJR 5 would include revenues from oil and gas, as well as from the extraction of other mineral resources of the state.

REPRESENTATIVE KELLY agreed with the aforementioned statement, and went on to say there was some consideration given to expanding the resolution to include all state resources.

7:15:01 AM

DEREK MILLER, Staff to Representative Mike Kelly, explained the process by which the balanced budget process of HJR 5 would work. He referred to a PowerPoint presentation which was provided to the committee and explained that slide 2 pictorially represents the mechanics of HJR 5. Once a five-year average of mineral revenues is calculated, the legislature has the ability to move funds from a Balanced Budget Account (BBA) to fund any shortfall in the five year average. For example, if the five year average is \$3 billion, but the state only receives \$2.5 billion one year, the legislature by majority vote can transfer \$500 million from the BBA into its available funds. The BBA is available only to receive funds in excess of the five-year average, or to fund shortfalls should revenue fall below the five year average. If the legislature wants to spend above the five year average, it must take the money from the Constitutional Budget Reserve Fund (CBRF) or other sources. If the revenues received are more than the five-year average, the excess is automatically transferred to the BBA-no vote is required, he explained. He said that the BBA only has the capacity to hold two year's worth of appropriations; when the balance exceeds two years of appropriations, the excess will be transferred into the CBRF.

REPRESENTATIVE FAIRCLOUGH relayed her understanding that the payment into the CBRF is a "repayment" of past draws.

MR. MILLER agreed with the aforementioned statement.

MR. MILLER further expanded on the method of calculating the five-year average, referring to slide 4. Based on petroleum revenues from the past four years and the predicted revenue for the next year, the five year average for fiscal year (FY) 2008

would be \$2.9 billion. He reiterated that since the BBA is limited to a maximum amount equal to oil appropriations for two years - any excess will be transferred to the CBRF.

REPRESENTATIVE WILSON asked what happens once the CBRF is paid back.

REPRESENTATIVE KELLY replied that the excess funds would continue to go into the CBRF.

[7:21:28 AM](#)

MR. MILLER explained that HJR 5 does not touch the "sacred cows," such as any aspect of the Permanent Fund or Amerada Hess account. It is also not "subject to the CBRF sweep." He summarized that HJR 5 is a fiscal responsibility resolution that encourages "a better budgeting system." It provides a simple but effective mechanism to help save budget surpluses and avoid deficits and eliminates the need for complicated "parking" of excess funds to avoid the three-quarter legislative vote required to access the CBRF. He opined that a constitutional amendment is recommended because the legislature can overpower, ignore, or change statutory appropriation constraints. Further, this approach lets the citizens voice their opinion concerning this simple fiscal framework. He suggested the HJR 5's approach would be compatible with the Percent of Market Value (POMV) approach should that concept be adopted with regard to permanent fund earnings.

[7:23:45 AM](#)

REPRESENTATIVE ROSES asked about the how the mechanisms in HJR 5 would accommodate a POMV approach.

REPRESENTATIVE KELLY indicated that the approach in HJR 5 would accommodate a POMV approach, and would not prevent or affect it.

REPRESENTATIVE ROSES asked how the state would provide an infusion of cash for emergency situations.

REPRESENTATIVE KELLY suggested that in an emergency situation, the state could access the CBRF, although he recognized that process could be slow, especially if the emergency arose when the legislature was not in session.

MR. MILLER opined that it may be possible to insert a provision in HJR 5 to allow fund access in emergency situations. He

stated that the sponsor does not desire a "laundry list" of exceptions however.

[7:26:56 AM](#)

REPRESENTATIVE ROSES asked whether there would be a mechanism by which to ever adequately fund the education account so as to forward fund education if the approach in HJR 5 was passed prior the full funding of the education account.

MR. MILLER said no.

REPRESENTATIVE GRUENBERG noted that there have been similar constitutional resolutions proposed in the past, and that these prior resolutions had spending exceptions within them.

REPRESENTATIVE KELLY opined that if a fund is established with very few exceptions, it will be more likely to remain a solvent fund.

REPRESENTATIVE GRUENBERG offered that the legislature is a reactive institution and therefore many of its spending decisions are based on the legitimate needs of its constituents. He noted that the Alaska Constitution provides for a strong executive branch, and that the approach in HJR 5 "ratchets it up" one step further as it makes revenues unavailable to the executive branch as well as to the legislature.

[7:33:24 AM](#)

REPRESENTATIVE SEATON opined that this approach may require the legislature to access the CBRF in more instances.

REPRESENTATIVE KELLY said that the approach of HJR 5 imposes discipline on the legislature and will keep the legislature from having to draw from the CBRF. He relayed his understanding that accessing the CBRF is contentious, difficult, and costs approximately \$20 million.

REPRESENTATIVE SEATON clarified that his understanding is that the legislature can only constitutionally appropriate out of the BBA to the five-year average amount. If the needs of the state are greater, the CBRF is "100 percent available on an three-quarter vote." He suggested that the effect of the resolution is to constitutionally "rat hole" funds away in the CBRF. He questioned whether the effect is to provide budget discipline,

or whether it just directs the legislature to a different source of funds.

REPRESENTATIVE KELLY referenced HB 125 and opined that the message behind that bill is that constituents desire a fiscal plan. He opined that this resolution is positive step in the move towards long-term fiscal planning. He opined that the legislature tends to spend any surplus funds. The resolution directs the legislature to make spending decisions based on a five-year income average, he indicated.

[7:41:25 AM](#)

REPRESENTATIVE SEATON asked whether the spending limitations in the resolution would have any effect between now and when the revenues start coming in from the gas pipeline, noting that, since future revenues are projected to decline, the average income will be higher than current income. He opined that the resolution would not really have an effect until the gas pipeline begins operation since the average income is expected to decline after FY 07.

REPRESENTATIVE KELLY indicated agreement with the aforementioned point. He reminded the committee that the price of oil is volatile, and noted that world events can cause significant fluctuations in the price of oil. He opined that it is impossible to anticipate when and how much oil prices may fluctuate, therefore his proposal is more of a "50 year plan" to accommodate the varying, but unpredictable price of oil.

[7:44:54 AM](#)

CHAIR HAWKER noted that under this approach, money is set aside during times of high revenues to offset shortfalls in times of low revenues.

REPRESENTATIVE CISSNA reminded members that the legislature has a history of regularly depositing money into the permanent fund. She expressed concern about a possible dampening effect on some issues, such as improvement of mental health care, if there are too many limits on spending.

REPRESENTATIVE KELLY opined that the bill supports sustainability of spending decisions and lessens the state's reliance on the fluctuating price of oil by establishing funds that provide a regular method of spending. This may result in

an improved ability to structure long-range policy goals, he noted.

7:52:35 AM

REPRESENTATIVE WILSON noted that there are significant deferred maintenance issues in the state and expressed concern that leveling the budget too much will continue to make it difficult for agencies to address maintenance issues.

REPRESENTATIVE KELLY offered his belief that imposition of spending discipline will allow the legislature to address chronic problems such as deferred maintenance because it will allow for more money to go into the CBRF, which would then be available for a big "catch up" on issues such as deferred maintenance. He suggested that certain items, such as maintenance, should be in the operating budget, not the capital budget.

REPRESENTATIVE FAIRCLOUGH spoke in favor of HJR 5, noting that that its approach allows policymakers to design future long-term spending plans. She opined that this approach does not hamper the ability of the state to use POMV to manage the permanent fund. She suggested that the approach of HJR 5 forces the legislature and the governor to look at revenue sources besides oil and mineral sources which would promote diversity in the state's revenue stream. She also expressed support for repayment of funds back into the CBRF. She suggested that a budget surplus in the next few years could be directed towards some forward funding concerns, such as education and health issues.

8:00:54 AM

REPRESENTATIVE CISSNA asked who would manage the investment account referred to in HJR 5 page 2, lines 8-9.

ROB CARPENTER, Fiscal Analyst, Legislative Finance Division, Legislative Affairs Agency, explained that the Treasury Division of the Department of Revenue currently manages the CBRF and he assumes that the same mechanism would apply to management of the BBA.

MR. MILLER agreed that the intent was for the BBA to be managed like the CBRF.

REPRESENTATIVE ROSES relayed that while he supports the concept in HJR 5, he has some concern regarding the relationship of this approach with other serious financial issues facing the state, such as the Public Employees' Retirement System (PERS) and Teachers' Retirement System (TRS) liabilities. He said that the state may need to be able to provide an infusion of cash in certain unpredictable situations wherein the state may have greater liability than anticipated.

[8:05:59 AM](#)

REPRESENTATIVE KELLY opined that if the legislature accepts the discipline imposed by the bill, it will be able to build the funds necessary to support a long-term spending plan. He suggested that his approach is more of a 50 year plan. He said he supports forward funding of education needs, yet indicated that the current budgeting mechanisms will not provide a solution to all looming long-term financial issues. He offered that the people of the state may be reluctant to allow the legislature to use permanent fund earnings until spending discipline like that proposed in HJR 5 has been in place and operated for a time. He indicated that fiscal discipline by the legislature would engender public trust in the legislature's spending decisions.

REPRESENTATIVE ROSES reminded the committee that the legislature is working very hard to come up with a solution to the unfunded pension liabilities. If the legislature puts forth some mechanism to reduce the pension fund liabilities, it will become part of the budget process. He offered that once included in the budget, the spending to pay down pension liabilities becomes sustainable if the assumptions are correct. He suggested the fixes to the pension plan and other issues should be determined prior to implementation of the mechanism suggested by HJR 5 so that the spending is built into the five year plan.

REPRESENTATIVE KELLY replied that "with something like this, there's never the perfect year to put it in place." He suggested it may be possible to use the CBRF to fund other looming financial issues, such as payment of the PERS\TRS liabilities.

[8:13:28 AM](#)

CHAIR HAWKER relayed that since a proposal to change the constitution is a profound and serious matter, it requires a very detailed examination of all aspects of the proposed

changes. He expressed support of the concept presented in the resolution, but indicated it needed further examination. He noted that the resolution does not propose changing the three-quarter vote requirement to access the CBRF, which may be an aspect that could use further consideration. He suggested the concept in HJR 5 could be a starting point to craft a constitutionally structured fiscal plan.

[8:17:16 AM](#)

REPRESENTATIVE SEATON clarified that recently the legislature has not appropriated money from the permanent fund earnings reserve account. He noted that there are currently proposed large resource development projects in the state, and expressed concern that the revenues from those projects may not be available to pay off the impacts of those projects since the revenue stream would be limited to the five year average from oil and gas revenues. He offered that his understanding of the mechanism in HJR 5 is that any income above the five-year average would not be available to the legislature, but would roll to the CBRF.

REPRESENTATIVE KELLY opined that the sequestered part of revenues would be considered in determining the five-year average.

[8:22:05 AM](#)

REPRESENTATIVE ROSES noted that once a revenue stream starts, it would be included in the determination of the five-year average. The five-year average also includes revenue predictions for the next year. The revenue would be "sequestered" only if it were not calculated into the projection of the next year's revenue income, he explained.

REPRESENTATIVE SEATON referred to HJR 5, page 2, lines 9-10, which seems to indicate that the money in the BBA is not available for spending.

REPRESENTATIVE KELLY agreed that the money is to be used to make up shortfalls and is limited to twice the annual earnings. He said that the point of HJR 5 is to take the operating revenues and put restrictions on spending so as to level the state's spending patterns.

REPRESENTATIVE SEATON asked if the only way to access the BBA fund would be by another constitutional amendment.

REPRESENTATIVE KELLY answered yes, but went on to say that if one assumes the CBRF is exhausted, one could also assume that the BBA would not have much money in it. He predicted that situation would indicate the state is in serious financial straits.

[8:27:45 AM](#)

CHAIR HAWKER explained that it would require a constitutional amendment to invade or change the corpus of permanent fund. He reminded the committee that only the earnings are available for appropriation.

REPRESENTATIVE WILSON expressed support for the concept in HJR 5 and agreed that it is necessary to implement some kind of fiscal planning structure. She suggested that the resolution requires a fiscal note to educate the public as to the bill's effect.

REPRESENTATIVE GRUENBERG expressed some reservation with amending the constitution and with limiting the legislature's options. He suggested that the fiscal restraint proposed by the bill may be at the expense of being able to pay for other worthwhile causes. He said he is more receptive to looking at options that allow for more flexibility.

[8:38:25 AM](#)

REPRESENTATIVE ROSES offered that what is being proposed is a balanced income resolution because it does not address spending, it addresses only income. He noted that the legislature could still go to the CBRF or other sources for funding. He opined that this type of approach may have an effect similar to a municipal tax cap. He relayed that municipalities did not stop spending money because of tax caps, but instead used bonds or other mechanisms to pay for projects.

REPRESENTATIVE KELLY opined that tax caps are like a sledgehammer, while the approach in HJR 5 is more finely tuned and responsive than a tax cap. He set forth that his proposal responds to times of prosperity and times of lowered revenues by leveling spending. He said this approach does require discipline and fiscal planning in a simple, straightforward manner.

[8:44:27 AM](#)

REPRESENTATIVE SEATON opined that the resolution seems to be a levelized income resolution more than a balanced budget resolution. Furthermore, it only concerns resource income but does not effect other revenue sources. He suggested that other income sources, such as taxes, can provide a more predictable income stream. He indicated that the legislature would likely need to consider ways to "fill in" income gaps.

[HJR 5 was held in committee.]

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Ways and Means meeting was adjourned at [8:51:28 AM](#).