

HOUSE FINANCE COMMITTEE  
February 19, 2009  
1:39 p.m.

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CALL TO ORDER

Co-Chair Hawker called the House Finance Committee meeting to order at 1:39 p.m.

MEMBERS PRESENT

Representative Mike Hawker, Co-Chair  
Representative Bill Stoltze, Co-Chair  
Representative Bill Thomas Jr., Vice-Chair  
Representative Allan Austerman  
Representative Harry Crawford  
Representative Richard Foster  
Representative Les Gara  
Representative Reggie Joule  
Representative Mike Kelly  
Representative Woodie Salmon

MEMBERS ABSENT

Representative Anna Fairclough

ALSO PRESENT

Karen Rehfeld, Director, Office of Management and Budget, Office of the Governor; Pat Galvin, Commissioner, Department of Revenue

PRESENT VIA TELECONFERENCE

None

SUMMARY

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^GOVERNOR'S FY10 OPERATING BUDGET AMENDMENTS

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KAREN REHFELD, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET, OFFICE OF THE GOVERNOR indicated that Commissioner Galvin would introduce the interim revenue forecast numbers to preface the discussion of the proposed budget amendments.

PAT GALVIN, COMMISSIONER, DEPARTMENT OF REVENUE presented an overview of the interim revue forecast for FY10. The commissioner signified that the oil price per barrel has

been revisited as it is now significantly lower than projected in November/December 2008. He indicated that from July 2009 until July 2010, the average North Slope price for oil is being projected at \$57.87. The production volumes are estimated at 659,000 barrels per day, a decrease of 6,000 barrels from the fall forecast. The projected unrestricted revenue for FY10 is just under \$3.2 billion, a \$2.1 billion decrease from the fall forecast. Commissioner Galvin declared one positive is that oil revenue is now 82 percent of unrestricted revenue down from the low 90 percent a year ago.

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Co-Chair Hawker appreciated the follow-up from the fall forecast due to last year's volatile price fluctuation in the oil market. He referred to the present period of relative stasis in oil market pricing and asked the commissioner what sense of confidence the department had in the present projections.

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Commissioner Galvin responded that previously the department depended heavily on the modified Delphi forecasting system, but projections have been updated blending with other publically available resources to provide a timelier forecast. Confidence in oil price expectations is directly related to overall feelings regarding the U.S. and global economy. He stressed that expectations cross a wide spectrum in terms of what is being seen in the near and longer term for the global economy and, by reflection, oil prices. The commissioner agreed that the past 2 months have been relatively stable compared to the prior 6 months, but stressed the complicated nature of projecting an average price while trying to predict the oil price progress over the next few years. More will be known during the next two months due to the introduction of the stimulus package together with other big ticket items influencing global markets over the next 18 months. The commissioner admitted that the unknowns created less optimism today than several months ago.

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Co-Chair Hawker pointed out that during the relative stasis of the past 60 days, an anomalistic circumstance developed where Alaska North Slope crude, typically trading on the west coast at a several dollar discount to the benchmark West Texas Intermediate or Texas Light Sweet has reversed and now West Texas Intermediate is selling at a substantial discount to Alaska North Slope crude. He wondered if this was a long term trend and if it affected the budget analysis.

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Commissioner Galvin responded that Alaska historically sold oil at a long-term \$2.50 discount on the west coast, but during the fall there was a deep \$6 discount over a long period. The commissioner explained that when the market is in stress buyers turn to the preferred quality of the Light Sweet product. Alaska crude sells in large quantity lump sales, so the question to determine is if this is a long term phenomena or a quirk in the market; the trend has not sustained long enough to establish its course. Commissioner Galvin indicated that the \$2.50 discount is still being projected, but there is an overall pessimistic feeling as the department monitors the trend leading to the spring forecast.

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Representative Crawford asked if the FY10 figures take into account the loss of the standard deduction and, if so, what is the projected loss.

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Commissioner Galvin responded that the standard deduction has been built in, but specific numbers will need to be confirmed at a later date.

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Commissioner Galvin informed the committee of a recommended change in the approach to the budget relating to the oil tax credits. Tax credits are accruing for any company investing in exploration and development, but companies with existing production will have a tax obligation deducted off the top. The commissioner reported that the credit, showing up in the budget as an appropriation amount, is strictly the anticipated amount owed to companies that do not have sufficient or any production to establish an obligation to the state. He impressed upon the committee that a factor in the projections is having credits available when they are due, so companies will not worry about payment being subject to subsequent appropriation. He noted a range of obligations on the high end has been built in to keep the money flow so no one will be turned away in down times. This has resulted in the department continually adjusting downward over time as better information is received. Commissioner Galvin suggested an alternative course is to change the language of the authorization to have the amount necessary to pay the tax credits and then DOR would provide the estimate to be built into the budget. He declared this would secure that payments are made, but retain the obligation to return to the legislature with the actual numbers. The commissioner

believed this to be a better balance in experience where a more accurate prediction can be made without being under, resulting lower cash flow.

Co-Chair Hawker remarked that the commissioner was looking to change the language from a limited appropriation to an open-ended appropriation, but still require a report back to the legislature. Commissioner Galvin agreed and stressed it would only be open-ended for the tax credits established in law. Co-Chair Hawker asked Ms. Rehfeld if there was a precedent for this open-ended appropriation.

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Commissioner Galvin responded that the resource rebate last year was written in this manner. Co-Chair Hawker questioned if an open-ended appropriation rescinded the legislature's finite responsibility to appropriate. Commissioner Galvin responded that when the resource rebate decision was made, it was assessed as not being open-ended if it was for a defined purpose.

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Ms. Rehfeld interjected that another precedent for the open-ended appropriation had been in judgments and claims within the Department of Law.

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Representative Crawford questioned the difference in the credit allowing for \$200 million instead of \$300 million. He recalled testimony during the Alaska's Clear and Equitable Share (ACES) debate indicating that price per barrel would be the greatest predictor as to future activity. He asked if the drop in price caused the reworking of the money held out for the credit or if they were unable to anticipate the amount of needed exploration and development credits.

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Ms. Rehfeld remarked that the budgeting discussion has been on timing and tax credit amounts. She explained that because it is a new program, the revenue projected in the end process is eligible for the tax credit, but found the time to process and audit the applications was slower than originally anticipated. In last year's budget, the authorized amount was increased to \$400 million as the application process was expected to turn around faster, but given recent timing, the DOR took it back down in the supplemental bill to \$200 million. In the FY10 budget, the department left the credit at \$300 million because of the capped nature of the appropriation to give companies more flexibility but it was decided to reduce it back to \$200

million in the current year with a change in the language. She reported that a great deal of exploration is going on in the state that has not been impacted from the drop in oil prices, but she reiterated that from the budget side it appears to be more of a timing consideration. Ms. Rehfeld concluded that this is a new program and if the legislature is amenable to restructuring the appropriation DOR will be able to make better determinations after the upcoming third year.

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Co-Chair Hawker indicated that the committee had requested a more complete analysis of the credit calculation projections instead of just moving money around for budgetary purposes. Ms. Rehfeld responded that revenue is working to provide that information.

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Ms. Rehfeld emphasized that over the past few months the Office of the Governor has been struggling with the projected revenue forecast to determine the necessary budget adjustments. She stressed the administration's concern to manage during the downturn and extend the life of the savings account. There are some proposed reductions in the supplemental bill that in the current year's appropriations minimize a draw on the reserves. In FY09 there is a proposed \$1.36 billion draw at the end of the fiscal year added to \$1.25 billion for the proposed amendments resulting in a total \$2.6 billion draw on reserves. The question is what can be reasonably reduced while still providing needed services and minimizing the draw from reserves.

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Ms. Rehfeld referred to the State of Alaska, Fiscal Year 2010 Governor's Amended Fiscal Summary (copy on file). She remarked that the December budget is compared with the newly released Governor's amended budget. The change in the revenue forecast with the adjusted price of oil at \$57.78 reflects a drop in revenue of \$2.1 billion (line 3). The total revenue picture for FY10 is \$3.2 billion. The proposed amendments, in the general fund column, would reduce December's spending plan by \$445 million. At the end of FY10 this would be a proposed projected draw on reserves of \$1.25 billion.

Ms. Rehfeld highlighted some items on the fiscal summary. She pointed out the reduction in the direct deposit to the retirement systems (line 15). The original figure reflected the anticipated amount to prepay down on the unfunded liability. She emphasized this will not impact the employer rate; the state is still committed to pay the PER/TRS

obligation. Ms. Rehfeld commented that due to the revenue shortfall it was not believed appropriate to fund any additional payments into the unfunded liability.

Co-Chair Hawker contended that some media outlets were reporting that the state was going to short fund the pension obligations in the retirement program. He wanted it clearly understood that the state was living up to its actuarial obligations and not short funding the retirement program.

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Ms. Rehfeld agreed there had been confusion but emphasized that the state is committed to pay the statutory determined rates for PERS/TRS but due to the \$2 billion revenue shortfall there will be no hoped-for additional prepayment of the unfunded liability.

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Representative Gara noted that more money has been put into the retirement obligations than required but asked for clarification on how the required minimum amount is calculated. Ms. Rehfeld replied that the Alaska Retirement Management Board (ARMB), with an actuary, determines the rate for PERS/TRS and the state, and under SB 125, is committed to pay the difference between the 22 percent and the actuarial defined rate. Co-Chair Hawker interjected that the state is fully funding the retirement obligation to the rate determined by the actuaries. Representative Gara asked if the amount shown in the fiscal summary sheet reflects the amount recommended by the ARMB. Ms. Rehfeld agreed it reflects the required payment rate.

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Representative Gara analyzed that the projected debt to fully fund the system goes up when stock market goes down, therefore if less is being put into the short fund, the debt is now bigger. Ms. Rehfeld agreed that the numbers are adjusted annually. The amount should be adjusted to show the decline in the market when the ARMB meets again to project the unfunded liability. She indicated several options available to pursue paying down the unfunded liability such as adding additional cash or issuing pension obligation bonds.

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Ms. Rehfeld continued with the federal reimbursement adjustment to Medicaid under the stimulus package (line 11). The federal money increases 6.2 percent over 9 quarters, starting this year and extending into FY11. Ms. Rehfeld emphasized that the federal government is very specific that

the states not reduce services due to revenue shortfall but maintain payment on existing programs. Co-Chair Hawker remarked that both the administration and the legislature want to keep the economic stimulus activities separate from the operating budget but in this case it merits inclusion into the operating budget. He asked if this is the only component of the economic stimulus package that has been incorporated into the operating budget.

Ms. Rehfeld replied that is the only component at this time. She emphasized that the stimulus bill is very large document targeting many programs therefore it takes time to understand the requirements, impacts, and changes to existing programs. The stimulus bill will also affect capital and operating funds and how those funds flow to the state. Co-Chair Hawker requested that the stimulus package be kept separate from the budgeting process.

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Ms. Rehfeld signified that as components are pulled out of the federal bill they will be brought before the legislature. She spoke of the \$100 million in tax credits mentioned earlier by Commission Galvin and the decision to back out the placeholders for future supplementals and amendments. Co-Chair Hawker clarified that these are not items in any budget simply notational entries on the summary documents, not reductions in any previously budgeted item.

Ms. Rehfeld explained that these are components of the overall spending plan which are being reduced because of the \$2 billion shortfall. She indicated that no other spending will be brought to the legislature for consideration. She noted one of major changes made on the capital side was the reduction in the renewable energy fund grants from \$50 million to \$25 million. Ms. Rehfeld indicated the \$238 million proposed spending out of Alaska housing capital corporation fund had been reduced to \$128 million.

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Representative Gara asked about the \$709 million and \$711 million in Duplicated Authorizations (line 13). Ms. Rehfeld defined duplicate authorization as a technical term where something appears in two places in the budget but it is not counted twice in the spending plan. Representative Gara asked for the amount of extra Medicaid (FMAP) money the state is expected to receive. Ms. Rehfeld indicated that the federal authorization replaces Medicaid in the general fund, not reducing state dollars (line 11). Co-Chair Hawker interjected that the stimulus adjustment is restoring the enhanced FMAP rate enjoyed in the state for many years before the federal government removed it last year.

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Ms. Rehfeld moved to the Governor's FY2010 Operating Budget Amendments (copy on file). She indicated adjustments to several departments of varying sizes. There is a \$1 million proposed increase for the Public Defender Agency due to a projected increased case load (page 1, line 3). There are few changes in the Department of Commerce; not dealing with cost allocation plans within the department. She moved to the Department of Corrections adjustment for the Goose Creek Correction Center that proposed the hiring of a private contractor for the construction of the prison. The receipts would come from the Mat-Su Borough (page 2, line 19).

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Representative Salmon asked Co-Chair Hawker if the affected departments will be coming before the committee. Co-Chair Hawker responded that Ms. Rehfeld will be available to the departments and each amendment will be sent to individual subcommittees for a detailed review.

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Ms. Rehfeld moved to three increase requests for the Department of Fish and Game: the proposed increase in the Lower Yukon River salmon fisheries, the Bering Sea Crab research program, and the wildlife pilot program of urban response teams. The Bering Sea Crab research program has federal funds attached to it under the federal stimulus package which would replace the general fund request. In the wildlife program, there was a proposed movement of \$190,000 from the FY10 capital budget into the operating budget to address some of these issues.

Representative Gara requested more information on the Wildlife Conservation pilot program of urban response teams. Ms. Rehfeld responded that the specifics were to try and address brown bear situations in urban areas. This request has been reduced from \$750,000 to \$190,000.

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Representative Kelly expressed his hope that the Department of Fish and Game would not hire more government employees for this program. Ms. Rehfeld responded that Representative Kelly should contact the department directly concerning their plans. Ms. Rehfeld moved to the \$1 million for reduction of fuel allocation from the executive branch agencies (page 2, line 33). Most of the affected changes in Health and Social Services (HSS) involved the \$74 million in federal money for Medicaid (page 2-4, line 34-63). Ms. Rehfeld referred to a recent determination of error in the billing methodology related to nursing (line 52). She added

that some transactions throughout the budget were specific to the Mental Health Trust.

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Representative Gara asked if all the HSS line items add up to \$74 million. Ms. Rehfeld agreed, with a few exceptions. Representative Gara asked if there was any consideration given to use some of the saved state money being replaced by the federal stimulus money to assist in foster care issues. Ms. Rehfeld responded that there were some budget increases in a few areas in the FY10 budget but no plans to revisit and further increase any of them at this time. Representative Gara revealed that for a very small amount of money foster children could be helped with transitional housing. Ms. Rehfeld responded that the federal law is clear about not taking federal money just to save state money; the state must continue programs and not reduce services. Representative Gara alleged that if the state was saving money then some of that money could be spent to resolve existing problems.

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Ms. Rehfeld continued with the Department of Labor (page 4, line 65-68). She referred to unemployment insurance and asserted this was not related to the federal stimulus bill (line 67). Co-Chair Hawker reiterated this was not part of the federal stimulus package but in the ordinary operations of the federal appropriation process. Ms. Rehfeld highlighted several areas of increase for the Department of Law (page 4-5, lines 69-75). The department was asking for \$1.9 million for the Trans Alaska Pipeline (TAPS) Strategic Reconfiguration (line 73), \$600,000 for Endangered Species Act litigation, and \$3.5 million for the BP Corrosion Issue (line 74, 75).

Co-Chair Hawker asked if the BP corrosion litigation funding in the original budget was pushed as a reduction item but now is being restored. Ms. Rehfeld responded that BP had originally been put forth as a lapse extension, but the committee had requested it be considered in the FY10 budget as an amendment.

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Ms. Rehfeld moved on to the Department of Public Safety (page 5-10, lines 82-109). She indicated the \$8.5 million request included state troopers, wildlife troopers, and the implementation of the Phase 2 of the Village Public Safety Officer (VPSO) study. She noted that recruitment efforts have been successful and the money would fund the existing 15 positions. Vice-Chair Thomas announced that the VPSOs are not licensed to carry weapons.

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Ms. Rehfeld announced a few safety related and maintenance items in the Department of Transportation (page 6-8, lines 115-124). The largest increase was \$2.3 million for the FY10 Bargaining Unit Contract terms of the Inland boatmen's Union of the Pacific (line 124). There are shifting funds for the University capital budget request into the operating budget (page 8-9, lines 125-134). Ms. Rehfeld reviewed the debt reimbursement and debt retirement for a school in Cordova and some adjustments for some issued bonds (page 9, lines 140-142).

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Ms. Rehfeld reported power cost adjustments were due to an expected decrease in interest revenue in the PCE Fund which required additional general funds to fully fund the program (line 143). She moved to the Fund Capitalization for tax credits and the reductions in the PERS/TRS contributions (page 10, lines 145-146). The Spring Creek Expansion Line reflects a reduction as it has not proceeded as expected and there is also a reduction on the Bethel project (line 153, 155).

Co-Chair Hawker asked about the proposed language addition to the CBR to balance the FY10 budget (page 10, line 158). He felt the FY10 budget would fall under the sub section B exemption clause for accessing the CBR and questioned if this had been determined differently. Ms. Rehfeld responded the department is presently looking at calculating that information.

Representative Salmon referred to line 20 and remarked that the focus should be on more edible fish. Co-Chair Hawker suggested that Ms. Rehfeld have someone from the Department of Fish and Game contact Representative Salmon.

Representative Crawford questioned if the Bethel Prison project appropriation was on hold or cancelled.

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Ms. Rehfeld indicated that the financing mechanism under SB 65 made it impossible to finance a project based on the limitations in this bill. There was uncertainty if the people of Bethel wanted a prison expansion, but the new city council indicated a desire to move forward. The Department of Corrections is working with them to define the project.

Representative Crawford noted that the administration had made a great case on why the expansion in Bethel made good

investment sense. Ms. Rehfeld indicated the project may not go away but was just not fully defined yet.

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Representative Austerman referred to the stimulus package regarding Medicaid and wondered what would happen in the FY11 budget when there was no longer \$74 million from the stimulus bill. Ms. Rehfeld noted that the federal funds would be available through part of FY11 but then the state would have to replace general funds after that time. Representative Austerman commented that he was nervous watching the state's savings account disappear as the state tries to balance the budget over the next few years.

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Co-Chair Hawker observed a similar situation in federal funding of the Federal Medical Assistance Percentage (FMAP) rate that established an entitlement program that in the past few years the state had to fund. He expressed his concern about creating new programs under the federal stimulus bill that the state will have to pay for later.

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Representative Kelly remarked that the governor talked about the difficulty and the trap in accepting stimulus funds that will grow the operating budget in the future. He requested that each time the federal stimulus package offends the governor's or a legislator's sensibility that a complete explanation and justification be given when stimulus money is used to start new programs. Co-Chair Hawker shared Representative Kelly concerns.

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Representative Gara remarked that much of the stimulus funds provide for renewable energy, construction, and teachers. He expressed interest in discovering what programs in the bill increase services requiring state funds in the future.

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Ms. Rehfeld remarked that the administration is gathering that information now. She hoped to have a preliminary summary of the allocations for the legislature soon. Each item in the stimulus bill will have its own requirements. Representative Gara expressed his concern that the state will receive the money, but not scrutinize it thoroughly. He requested the committee listen to as many different proposals as possible in order to select the best projects.

#

ADJOURNMENT

The meeting was adjourned at 3:03 PM