

HOUSE FINANCE COMMITTEE
January 18, 2012
1:34 p.m.

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CALL TO ORDER

Co-Chair Thomas called the House Finance Committee meeting to order at 1:34 p.m.

MEMBERS PRESENT

Representative Bill Stoltze, Co-Chair
Representative Bill Thomas Jr., Co-Chair
Representative Anna Fairclough, Vice-Chair
Representative Mia Costello
Representative Mike Doogan
Representative Bryce Edgmon
Representative Les Gara
Representative Reggie Joule
Representative Tammie Wilson

MEMBERS ABSENT

Representative Mark Neuman
Representative David Guttenberg

ALSO PRESENT

Karen Rehfeld, Director, Office of Management and Budget (OMB), Office of the Governor; Senator Alan Austerman; Representative Lance Pruitt.

SUMMARY

^OVERVIEW OF THE GOVERNOR'S FY 2013 BUDGET: OFFICE OF MANAGEMENT and BUDGET

Karen Rehfeld, Director, Office of Management and Budget, Office of the Governor

Co-Chair Thomas introduced staff.

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KAREN REHFELD, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET (OMB), OFFICE OF THE GOVERNOR, provided members with a list

of OMB staff and a power point presentation: FY2012 Budget Overview, January 18, 2012 (copy on file). She emphasized that approving an annual operating and capital budget for the state of Alaska is one of the most important things, if not the most important thing, that the legislature does each session. She stressed the time and effort that goes into the preparation of the budget. The Administration worked with state agencies and the university to review budget requests and challenges in order to meet the state's most pressing needs, while holding the line on state spending by focusing on key principles, priorities and results.

Ms. Rehfeld observed the committee's intent to include discussions with state agencies about their mission, core services, and results in the budget subcommittee process. She maintained that it is an important discussion: "to be accountable for the public dollars we spend and to be able to communicate what the state is receiving for the investment it makes in programs and services". She added that it also needs to be a meaningful tool for agencies and program managers that links budget to results, and provides the targets and strategies for continuous improvement in service delivery. She observed that Governor Parnell's vision of economic growth and strengthening families has been his way of communicating his priorities with Alaskans.

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Ms. Rehfeld stressed that Alaska's future rests on responsibly developing the state's natural resources and creating jobs and economic opportunity for families. The budget supports the governor's vision in several key priority areas.

Ms. Rehfeld reviewed the guiding principles used by the governor to develop his budgets:

- Fiscal Restraint - Spend less and save more for the future;
- Strategic Investments - Invest in infrastructure to grow Alaska's economy;
- Cash Reserves: The state will need to rely on cash reserves to provide state services over time with declining oil production. There is nearly 13 billion in the Constitutional Budget Reserve and Statutory Budget Reserve Accounts.

- Focus on Results - agency missions, core services, and results.

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Ms. Rehfeld noted that the governor's budget priorities support the investment strategy and are based on the state's constitutional priorities:

- Resource Development - create Jobs for Alaskans
- Education - prepare students for college for success in college or postsecondary education
- Transportation/Infrastructure - support economic development
- Public Safety - for homes and families
- Military - strengthen military missions and support military families

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Ms. Rehfeld reviewed the revised fall forecast for FY 12 and FY 13 on slide 5. She noted that the chart shows the projected revenue, the proposed spending plan, and the projected balances at the end of each fiscal year. The FY 12 and FY 13 fall revenue forecast was revised upward. She observed that 90 percent of Alaska's unrestricted general fund (GF) revenue comes from oil production. Oil production continues to decline faster than originally forecast. She noted that high oil prices tend to mask the effect of the decline, but provides an opportunity to save. In FY 12, revenues are projected at \$8,981.5 billion, while spending is projected at just over \$7 billion. This leaves a projected balance of just over \$1.9 billion for FY 12. In FY 13, revenues are projected at \$8.2 billion with a projected spending plan of \$6.4 billion, which leaves a projected balance of nearly \$1.8 billion. She concluded that the FY 12 and FY 13 savings and/or investment opportunity is over \$3.7 billion.

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Ms. Rehfeld reviewed slide 6, which was a high level snapshot of the governor's total budget request of \$12.1 billion. Fund sources are broken out:

- Unrestricted General Funds \$6.43 Billion - 53%

- Federal Funds \$2.87 Billion - 24%
- Permanent Funds DGF \$1.48 billion - 12%
- Designated General Funds (DGF) \$834.5 million - 7%

Ms. Rehfeld observed that DGF included:

- General fund program receipts \$113.8 million
- University Receipts \$341.0 million
- Renewable Energy Grant Funds \$25.0 million

Ms. Rehfeld noted that other funds amount to \$505.5 million or four percent of the budget and included:

- Permanent Fund Receipts \$126.5 million;
- Permanent Fund Corporation Operating costs of \$11.1 and management fees of \$108.2;
- International Airport - \$110.9 million;
- Statutory Designated Receipts - \$66.4 million; and
- Postsecondary Education Receipts - \$12.9 million.

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Ms. Rehfeld discussed the governor's FY 13 budget priorities. The first priority is resource development - positioning the state's economy for growth. The governor's proposed budget includes \$28.5 million for Roads to Resources. The appropriation would continue work on the following projects:

- \$10 million for Umiat Foothills West road
- \$10 million for Road to Tanana in Northwest Alaska
- \$4 million for Ambler Mining District
- \$4.5 million for Klondike Industrial Use Highway that goes from Skagway to the Yukon along with other roads to resources

Ms. Rehfeld continued discussing the governor's priorities:

- \$3.3 million to the Department of Natural Resources to streamline the permitting application process;
- \$2.7 million GF for oil rare earth elements and strategic minerals assessment;
- \$1.1 million GF for shale oil assessment; and

- \$3.7 million GF for a statewide digital mapping initiative, which could capture another \$12 - \$13 million in federal funds to support the project.

Ms. Rehfeld emphasized the importance of elevation data to resource development, aviation safety, routes for roads, and emergency response.

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Representative Gara asked why the state would spend funds on a road to Umiat unless development was assured. Ms. Rehfeld emphasized that the potential all along the foothills is known and that the road would open up the opportunity to develop some of that potential. The road would be industrial, not an open access road, which would help make access to the resources more cost effective.

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Representative Joule noted that communities close to the proposed Umiat road are in opposition to the road. He asked if multiple routes that the community may support would be considered. Ms. Rehfeld noted that different routes are being reviewed and that the state is in discussion with local communities. Representative Joule stressed that the borough and Regional Corporation try to be supportive of development efforts on the North Slope, which is difficult with local opposition.

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Representative Costello noted that the legislature funded additional positions in the Department of Natural Resources to address the 2,500 permitting backlog. She asked if the appropriation would get rid of the backlog entirely. Ms. Rehfeld noted that the \$3.3 million is for the unified permitting project, which is the information system that manages all the permitting applications. The FY 12 funding included six new positions and some vacant positions, which have made a huge difference to the department. She understood that the backlog was reduced by 20 percent at the end of the calendar year. The department is continuing to streamline the process. Representative Costello asked if the process has been made easier for the public to access. Ms. Rehfeld suggested there would be a web based component.

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Ms. Rehfeld noted that there is continuation funding for the Alaska Gasline Inducement Act (AGIA) Reimbursement Fund (\$60 million); and the Alaska Gasline Development Corporation project (\$21 million). She expected considerable discussion regarding gas line development and acknowledged that adjustments in the budget would be necessary.

In response to a question by Representative Doogan, Ms. Rehfeld clarified that of the \$4.5 million request: \$2.5 million would be used for the road between Skagway and the Yukon; and \$2 million would go to smaller resource roads that are not specifically identified. The funding would not support roads in Canada.

In response to a question by Co-Chair Stoltze, Ms. Rehfeld clarified that the funding for the Klondike road would be on the Alaska side.

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Ms. Rehfeld discussed funding for education. The budget includes: full funding of K-12 education and pupil transportation (\$62.2 million) at \$1.1 billion; and forward funding of K-12 education and pupil transportation at \$1.1 billion. The K-12 funding formula is based on current statutory Base Student Allocation (BSA) of \$5,680. The budget includes an \$8 million request for Alaska Performance Scholarships (APS). The class of 2011 was the first to qualify for these scholarships. Nearly 2,400 students qualified for APS in the first year. Over 900 Alaskan high school graduates from the class of 2011 received the scholarship. The remaining students will be eligible to receive the scholarship over the next 5 years. The Alaska Commission on Postsecondary Education (ACPE) is preparing a report to the legislature, which is due on the 10th legislative day (January 27, 2012) that will provide detailed information on APS, and the students that qualify in the inaugural class.

Ms. Rehfeld observed that the budget includes two school construction projects. Earlier this fall, the administration successfully resolved the long-standing Kasayulie litigation with a pledge to support funding of the five highest priority rural school construction

projects over the coming years. The first two school construction projects on the list are in Emmonak and Koliganek. She added that \$24.0 million was also included for the first 14 projects on the Department of Education and Early Development's major maintenance priority list.

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Representative Wilson asked for more information regarding the size of new schools. She noted concerns regarding heating costs in schools with low enrollment. Ms. Rehfeld noted that Emmonak is significantly over capacity and promised to provide more information. Representative Wilson asked how school size would be determined. Ms. Rehfeld explained that the project ranking takes overcapacity into account.

Representative Gara expressed concern with the flat funding of education and noted that the Average Daily Membership (ADM) level has not increased in two years. He stressed that schools are facing layoffs. Ms. Rehfeld observed that the governor is concerned with the ability to sustain growth in formula funding programs. The governor is focusing on performance scholarships that will improve academic rigor and success of students. The governor is not opposed to some targeted funding. She expected more discussions would occur on formula funding. There have been increases for intensive students and the BSA. She added that FY 13 is the last year for inclusion of district cost factors.

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Representative Gara asked if the governor would support legislation that would prevent layoffs. Ms. Rehfeld could not respond.

Co-Chair Thomas spoke to the Teacher Retirement System's (TRS) 22 percent cost factor, which he pointed out, is also growing. Ms. Rehfeld agreed.

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Ms. Rehfeld discussed public safety and the governor's Choose Respect program, Division of Domestic Violence and Sexual Assault Prevention Initiative for \$11.8 million GF. She observed that the governor is requesting \$3.3 million

for prevention and intervention, which includes public education and outreach, community level prevention projects and rural pilot projects. She noted sixty-four communities held "Choose Respect" events in 2011, and the goal for 2012 is for 100. She maintained that the program is sending a strong message of support to victims and survivors. The governor also included \$3.2 million for the Support for Survivors program, which includes shelter services for victims, services for children exposed to violence, trauma services for victims, and housing.

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Vice-chair Fairclough expressed concern that prevention is being tied to intervention. Although she recognized the importance of intervention, she indicated that her focus has been primary prevention. She asked if there are any unexpended funds from FY 12 appropriations that would be available for prevention programs in FY 13. Ms. Rehfeld promised to research the matter.

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Ms. Rehfeld observed that \$5.3 million was requested for a continued law enforcement presence in communities. The request would provide for an additional 15 VPSOs and 1 support trooper; housing for VPSO's; sex offender management and supervision; cold case prosecutor; and limited English proficient victims' assistance.

Ms. Rehfeld noted that the governor is committed to improve the state's ability to respond to a disaster. The legislature approved just under \$5 million for emergency power generation and water purification in the FY 12 budget. The FY 13 budget requests funding for emergency food supplies for several locations around the state (\$4.9 million). The governor has also requested funding for an Interior search and rescue helicopter (\$3.0 million). Interior and Northern Alaska's geography and extreme weather conditions create enormous challenges to quick and effective response to emergencies. She pointed out that it is critical for Alaska State Troopers to be able to access remote areas during adverse weather conditions with a helicopter that is adequately equipped to complete the mission.

Co-Chair Stoltze referred to disaster preparedness and the interface with private entities that has occurred in his district. He felt that efficiencies could occur with state and private cooperation. Ms. Rehfeld expressed interest in more discussions.

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Representative Wilson asked for statistics on helicopter use and billing procedures. Ms. Rehfeld agreed to provide additional information.

Vice-chair Fairclough noted that her office had calls regarding emergency food supply funding and wanted more information on cost and how supplies will be replenished. She observed the need to keep food fresh. Ms. Rehfeld offered to have a presentation for the committee.

Co-Chair Thomas referred to his service experience eating sea rations. Representative Joule interjected that Alaskan products could be used.

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Ms. Rehfeld discussed transportation infrastructure. She observed that \$1 billion for statewide infrastructure projects was included to build and maintain Alaska's infrastructure, which included funding for:

- Highway & Aviation \$938.3 million;
- DEC 16 Municipal water/sewer projects \$32 million GF; local match;
- Village Safe Water - \$51 million, \$8.7 million state GF match; and
- Municipal Harbor Grant Fund 10 projects \$23.1 M GF; local match.

Ms. Rehfeld noted that the governor has also introduced a ports GO bond package (HB286/SB163), which included six projects totaling \$350.0 million:

- Port of Anchorage \$200.0 million;
- Port Mackenzie Rail Extension \$110.0 million; and
- \$10 million each for Bristol Bay, Emmonak, Seward, and Ketchikan (Ward Cove).

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Representative Joule noted that off shore development is on the horizon and expressed disappointment that forward basing was not considered in Western or Northern Alaska. He stressed that there is an opportunity to send a message to Congress. Ms. Rehfeld noted that there are FY 12 funds and additional funding in FY 13 for consideration of an Arctic port.

Representative Alan Austerman questioned if the \$32 million for water/sewer projects would only match federal dollars. Ms. Rehfeld explained that the \$32 million is for municipal water/sewer projects. She explained that 16 projects are included in the \$32 million, which matches local funds. The Village Safe Water Program is also in the governor's budget proposal at \$50 - \$51 million; \$8.7 of this amount is a general fund match for federal funds. The program is divided by first time projects, and repair and upgrades to existing projects.

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Co-Chair Stoltze observed that most of his district doesn't want to be on a sewage system.

Ms. Rehfeld discussed energy funding. The governor's proposal included:

- Round five for Renewable Energy Grant fund - \$25 million; and
- Weatherization and home energy rebates - a little over \$50 million: Home Energy Rebates - \$20 million GF; and Weatherization - \$31.5 million GF.

Co-Chair Thomas asked why the target of \$50 million for renewable grants was not reached. Ms. Rehfeld explained that not all the projects they evaluated were ready for investment. Co-Chair Thomas stressed that the program is working. He noted that 10 million gallons of diesel have been saved in Gustavus and that the community energy costs have been reduced.

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Representative Gara noted that \$50 million of the \$100 million in appropriations to the Renewable Energy Fund was

vetoed by the governor in FY 12. He expressed concern that there are communities in need of the funding. Ms. Rehfeld stressed that round five has not been completed by the Alaska Energy Authority (AEA). The legislature will receive a list of projects evaluated in round five and their dollar amount. The list will show the projects that would be funded with the request and the amount needed to fund the entire list. A number of projects have been funded in the previous four rounds. She noted that there are questions that need to be answered, such as should the state reinvest in already funded projects that resulted in savings.

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Co-Chair Thomas observed that funding targets proved energy projects from viable sources as opposed to investing in research. He emphasized the importance of finding projects that work.

Representative Costello asked whether it was possible to change the process so the timing would coincide with the introduction of the governor's budget. Ms. Rehfeld acknowledged that adjustments are possible.

Co-Chair Stoltze agreed that viability was a good standard.

Representative Edgmon looked forward to the debate on HB 250. He discussed disagreements over multiple projects in the past and talked about the Renewable Energy Fund. He mentioned the additional funds added by the governor for the Low Income Home Energy Assistance Program (LIHEAP) and stressed the program's importance.

Representative Doogan wondered if there was independent auditing of the projects. Ms. Rehfeld noted that any entity that receives state funds is subject to the single audit requirement. She did not know if the projects were audited.

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Co-Chair Thomas remarked that there was a list of items that had to be checked off in order to receive the funding.

Representative Gara agreed that projects need to be viable and smart.

Ms. Rehfeld returned to slide 10, transportation and infrastructure. She concluded discussion of slide 10 by pointing out that full funding for Power Cost Equalization is requested at \$38.2 million

Ms. Rehfeld observed that it is year three of the deferred maintenance package. There are 2,200 facilities statewide, with 17.2 million square feet of space, and a replacement cost of \$7.8 billion. The administration is getting more consistent in their definition of deferred maintenance projects. She concluded that there is better identification of the universe of deferred maintenance projects. Facility managers are comparing notes and sharing information. There are facility condition index standards that can be applied to measure success. All of the year one funding will be expended by the end of the current fiscal year. Year two funding is in the hopper. Year three is in the request before the legislature. She stressed the improved ability to plan for and complete deferred maintenance projects.

Ms. Rehfeld discussed slide 11, military support. Funding is continued for army and air guard facilities, veterans' services and outreach, and an Interior veteran cemetery (\$2 million in federal authorization in the capital budget. A portion of the operating costs will be in the FY 13 budget. The full cost will be in FY 14.)

Ms. Rehfeld noted the Alaska Aerospace Development Corporation request for \$8 million in the operating budget. The corporation's funding stream from missile defense has changed dramatically. The Alaska Aerospace Development Corporation is working to secure other customers for the Kodiak launch facility. She observed that funding has been included in the budget to keep the Alaska Aerospace Development Corporation viable.

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Vice-chair Fairclough referred to the request for the Alaska Aerospace Development Corporation. She observed that they did not receive anticipated contracts and questioned how much and how long the state will need to invest to keep the facility operational. She also wondered where mid-term customers were being sought and when the state would know if contracts would be secured. Ms. Rehfeld noted that the facility was not successful in competing for the bid out of

Fort Greely. Another vendor is interested in the Kodiak site. She hoped to have commitments in the amended budget.

Vice-chair Fairclough expressed support for the facility and acknowledged that state support is needed for what is a global competition. She recognized that many in the community depend on the facility for their livelihood, but wanted to better understand the state's opportunities.

Representative Austerman observed that he serves on the Alaska Aerospace Development Corporation board. He explained that the Fort Greely bid was for a missile defense contract with the federal government. The Alaska Aerospace Development Corporation tried to outbid their competition and failed. They hoped to enhance the overall scope of the aerospace business in Alaska, not the rocket launch facility itself, although it would have helped the facility. The Alaska Aerospace Development Corporation is still in negotiations with two companies to launch mid-size rockets. Currently, the facility only launches smaller satellites. The funding request would only support operations for one year. The facility would need to be expanded for mid-sized launches at a cost of \$125 million. Contracts must be in place before the legislature would consider the \$125 million needed for expansion. Building a facility would be at least a two year process.

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Vice-chair Fairclough noted that opportunities may exist for a United States market with decrease federal funding going toward space exploration. She expressed support but stressed the need for further discussions regarding the cost of capital investment in an "all in" number.

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Ms. Rehfeld reviewed the pie chart in slide 12. She explained that the left side of the pie chart represents non-discretionary funding: formula programs, permanent fund dividend, statewide operations and requirements. The right side of the pie chart is discretionary funds: agency non-formula components of the capital and operating budgets. She observed that the general fund component was separated from the agency nonformula funds and other funds to allow them to look at the agencies' general fund request.

Ms. Rehfeld referred to the K-12 education formula. She observed that they are in the fifth year of the implementation of district cost factors.

Ms. Rehfeld noted that other formula funds total \$1.96 billion, which includes Medicaid at \$1.64 billion. Other components include shared taxes, Power Cost Equalization and Public Assistance.

Ms. Rehfeld observed that statewide appropriations represent about 12 percent of the governor's request at \$1.44 billion. The retirement system unfunded liability direct deposit for FY 13 of \$610.5 million is included in this amount and is up from \$479.5 million in FY 12. The total retirement system unfunded liability is \$11 billion: Public Employees' Retirement System (PERS) - \$7.0 billion, and Teachers' Retirement System (TRS) - \$4.1 billion. She noted other statewide budget requests: \$400 million - oil exploration tax credits; \$301.4 million - debt service (down \$25.0 million); \$60 million - Revenue Sharing; \$1.48 billion or 12.2 percent of the total budget - Permanent Fund; and \$572.0 million - Permanent Fund dividends and operations (\$25.0 million for PFD and hold harmless).

Ms. Rehfeld highlighted components of the \$1.8 billion capital budget request: transportation infrastructure, Roads to Resources, energy, deferred maintenance, and public safety.

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Representative Doogan asked what portion of the \$1.8 billion are federal funds. Ms. Rehfeld observed that there are \$820 million in federal funds. She added that \$882 million are unrestricted general funds, which includes \$60 million for the AGIA reimbursement amount. The AGIA reimbursement is not technically a capital expenditure, but is a reimbursement for capital expenditures. There are also \$81 million designated funds and \$20 million other funds. Representative Doogan concluded that there are \$1 billion in state funds and \$800 federal funds. Ms. Rehfeld agreed.

Representative Joule wondered if there was a way to see if the infrastructure built in the capital budget comes back in the operating budget under operations. Ms. Rehfeld referred to the university science building and agreed that the on-going operating expense would come into the budget.

Representative Joule observed that the cost of operating school buildings is born by the districts. Ms. Rehfeld pointed out that efficiencies are found in major maintenance projects, which would result in savings from improvements to existing facilities.

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Ms. Rehfeld highlighted the governor's FY 13 operating budget request. She emphasized that growth was restrained. The administration deleted 288 positions (full and part-time, long-term vacant positions). She concluded that personal services lines would be in better shape. Funding sources in personal services were also cleaned up. She acknowledged the net result would be good but stressed that a significant effort was required on the part of the departments.

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Vice-chair Fairclough questioned if vacancy and position eliminations would reduce the formula used to pay down the PERS and TRS liability. She also wondered whether cost shifting of the 22 percent liability would occur in communities that reduce positions, which would require the state to pick up more of the pension liability. Ms. Rehfeld noted that conversations have occurred on the issue with municipalities and that there would be more discussions.

In response to a question by Representative Gara, Ms. Rehfeld reiterated that the total unfunded liability is \$11 billion. The governor's budget for FY 13 includes a \$610 million direct deposit into the unfunded liability.

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Ms. Rehfeld noted Medicaid growth of \$130.5 million (\$45.0 million in general funds), which is an approximately 8.6 percent projected increase. The Department of Health and Social Services estimates that 150,279 Alaskans are projected to enroll. She stressed that enrollment, utilization, and costs driver the total cost.

Ms. Rehfeld noted the proposed opening of the Goose Creek Correctional facility over FY 13 and the first quarter of FY 14. By the end of this time, out-of-state prisoners will be returned and the facility will be fully operational. The

cost of current out-of-state contracts will help fund the operations of the Goose Creek facility. The facility is ready to go.

Ms. Rehfeld noted that the governor's request includes \$16.0 million for tourism marketing. There are also salary and benefit increases of \$66.0 million for the University of Alaska, Alaska Court System, Legislature, and Executive Branch.

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Ms. Rehfeld discussed slide 14. She emphasized that Alaskans benefit from state spending. She noted that 60 percent of the budget benefits Alaskans in communities, organizations and individuals through grants, direct payments, capital, and salary costs. Programs affecting Alaskans include: Medicaid, Permanent Fund dividends, Revenue Sharing, School Funding, retirement system unfunded liability, capital projects, and named recipient grants.

Ms. Rehfeld observed that 21 percent of the state's budget goes to purchased services such as travel, hotels, professional services, fuel and equipment - some of this funding is internal to state agencies but a significant amount is for services purchased from Alaska's private sector businesses.

Ms. Rehfeld noted that 19 percent of the total budget represents salaries and benefits for state employees who are tasked to deliver core services and programs efficiently and effectively to Alaskans.

Co-Chair Thomas reviewed the House Finance Subcommittee on the operating budget assignments. He observed that the committee is adopting new finance subcommittee standards.

ADJOURNMENT

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The meeting was adjourned at 2:59 PM