

HOUSE FINANCE COMMITTEE
February 12, 2015
1:33 p.m.

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CALL TO ORDER

Co-Chair Neuman called the House Finance Committee meeting to order at 1:33 p.m.

MEMBERS PRESENT

Representative Mark Neuman, Co-Chair
Representative Steve Thompson, Co-Chair
Representative Dan Saddler, Vice-Chair
Representative Bryce Edgmon
Representative Les Gara
Representative Lynn Gattis
Representative David Guttenberg
Representative Scott Kawasaki
Representative Cathy Munoz
Representative Lance Pruitt
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Pat Pitney, Director, Office of Management and Budget, Office of the Governor; David Teal, Director, Legislative Finance Division.

SUMMARY

HB 72 APPROP: OPERATING BUDGET/LOANS/FUNDS

HB 72 was HEARD and HELD in committee for further consideration.

HB 73 APPROP: MENTAL HEALTH BUDGET

HB 73 was HEARD and HELD in committee for further consideration.

#hb72

#hb73

HOUSE BILL NO. 72

"An Act making appropriations for the operating and loan program expenses of state government and for certain programs, capitalizing funds, making reappropriations, and making appropriations under art. IX, sec. 17(c), Constitution of the State of Alaska, from the constitutional budget reserve fund; and providing for an effective date."

HOUSE BILL NO. 73

"An Act making appropriations for the operating and capital expenses of the state's integrated comprehensive mental health program; and providing for an effective date."

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Co-Chair Neuman called the meeting to order, and explained that members of the public should consider the FY 16 Governor's endorsed budget as a starting point for budget discussion. He added that the committee was expecting some amendments to come from the administration.

PAT PITNEY, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET (OMB), OFFICE OF THE GOVERNOR, clarified that she was speaking from a summary document entitled "FY 2016 Governor Endorsed Budget Summary by Department" (copy on file). She added there was an additional packet of detail that she would not be addressing. She mentioned that she had brought individuals from the department to assist in answers questions of a detailed nature.

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Co-Chair Neuman recognized the department commissioners and staff and thanked them for their availability.

Ms. Pitney gave some background on the budget process to date. She stated that the new governor had used the work-in-progress (WIP) budget of the previous administration to meet a statutory deadline. Several amendments had been put forth, which resulted in the endorsed budget before the

committee. She pointed out that the endorsed budget was very close to the overview budget she had provided two or three weeks previously, with only minor changes.

Ms. Pitney highlighted reductions illustrated in the budget summary: 6.1 percent for non-formula related agency operations (\$134 million for all agencies except the legislative component); and 4.8 percent (\$106 million) for formula-related agency budgets. In total between non-formula and formula agency budgets there was a reduction of nearly \$240 million from the previous fiscal year. She clarified that the entirety of the savings in the operating budget came from agency operations.

Ms. Pitney drew attention to the "Statewide Functions" section of the summary, explaining that they included debt service, direct payments to the retirement fund, and oil and gas tax credits; with an increase of \$129 million from the previous year. She summarized that the increase, in combination with the decrease in agency operations, totaled an operating reduction of two percent.

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Ms. Pitney explained that when OMB went from the work-in-progress budget to the endorsed budget, it asked department commissioners to consider 5 percent and 8 percent reduction scenarios. Additionally, departmental priorities and priorities of the administration were considered; as well as reductions and additions from prior years. Other impacts to services and impacts such as the fuel trigger mechanism were considered. She explained that OMB did not do a strict across the board cut, but rather reflected on trends to make different levels of reductions based on priorities of state functions. She pointed out the reductions listed by department on the budget summary, and highlighted some of the decreases in different areas that were anticipated to generate dialogue and questions.

Ms. Pitney discussed two areas of reduction within the Department of Administration (DOA), including the Alaska Land Mobile Radio (ALMR) program. She felt that the reductions could be accomplished in the contractual services area by contract savings and equipment manufacturing changes.

Co-Chair Neuman asked Ms. Pitney if OMB was totally defunding ALMR, and asserted that there had been issues with the program in the legislature for years. He discussed the history of ALMR, recounting that the military had initially developed the communications program, and the state was going to take over parts of it before the military ended its affiliation with it. The state then picked up functions previously done by the military. It was his understanding that fire departments and other emergency services did not use the system.

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Ms. Pitney responded that ALMR was alive and well; there would be cost reductions to the program, but it was a system that many emergency services relied on.

Co-Chair Neuman wondered if there would be additional funding needed in the future. Ms. Pitney responded that she could not guarantee future costs due to changes in technology and the next iteration of ALMR. She did not anticipate additional costs in FY 17.

Representative Gara pointed out two parts of the budget summary that did not make sense to him, and thought that there was a bigger cut that was not reflected. Within the "Statewide" section, he pointed out the 'Direct Appropriation to Retirement Account' item for \$257,278.30 and suggested it was a "fake increase" due to the \$3 billion from the previous year spent from the Constitutional Budget Reserve (CBR). Ms. Pitney attributed credit to the legislative body for putting the \$3 billion in funding into the retirement accounts, which were long-term liabilities. The alternative plan had been for the contribution of \$1 billion in the current and prior year. She concluded that the action taken the previous year [funding the \$3 billion] put the state in a better position for meeting its retirement liability in the long run.

Representative Gara reiterated his point that despite how the funding was shown on the budget summary, the retirement account spending had not gone from zero to \$256 million. He noted that many legislators had supported the \$3 billion in additional funding from the CBR.

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Representative Gara highlighted education under the "Formula" section, and referred to the previous year's three-year education plan. He asserted that he would do whatever he could to avoid school cuts and that there would be a continuing conversation. He recounted how the legislature had added funding in the Base Student Allocation for three years, as well as a plan for a step-down of money that would be distributed through the foundation formula but was not foundation formula. He thought that the additional funding was approximately \$40 million; and was planned to reduce by \$12 million in year two and \$12 million in year three to total roughly \$90 million. He pointed out that the first installment had already been spent in the current school year, and wondered if the \$91 million indicated on the budget summary were the same funds that were sent through the foundation formula (yet was not foundation formula money). He questioned as to how the \$91 could be cut when half of it had already been spent.

Ms. Pitney referred to the supplemental budget that had been presented earlier in the week, and noted that the component was reduced by \$32 million in the current year and \$19 million for the following year. She continued to explain the difference between the increase in the BSA in the formula and forward-funding at 90 percent for FY 17.

Representative Gara asked if it was correct that there was roughly \$50 million being taken from year two and year three, and the additional \$40 million was coming from forward funding at 90 percent instead of 100 percent, to add up to \$90 million. Ms. Pitney clarified that the \$52 million was only showing up on the FY 15 supplemental budget.

Representative Gara asked if the \$90 million was the forward-funding at 90 percent instead of 100 percent. Ms. Pitney answered in the affirmative.

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Co-Chair Neuman discussed the issue of the forward-funding of education, making note of the \$1,269,430.60 indicated on the budget summary for education in the FY 16 WIP budget. He relayed that the Governor decided to fund the amount at 90 percent, with 10 percent (\$126 million) unfunded. He asked Ms. Pitney if any of her materials reflected the

reduction in the current year's expenditures. Ms. Pitney noted that there was two components: the amount of funding that education had for use in FY 16 (formula funded in FY 15), less the one time funding of \$32 million. She clarified that the education funding for FY 16 proposed in the combination of the supplemental and current budget was the full BSA, but not funding for the additional one-time amount. She explained that the budget before the committee reflected the amount of money being banked for FY 17, rather than intention (of the administration) for FY 17 education funding. She continued that the forward-funding of education was merely moving funds from one bank to another. She noted that this administration did not plan to forward-fund education as much, pending discussion over the student formula anticipated to take place the following summer to inform how much the administration would endorse for the FY 17 education budget.

Co-Chair Neuman related that the legislature (in around 2006) had established the education fund in order to fund education a year ahead to ensure that school districts had an idea of their budgets even though their fiscal year did not adhere to that of the legislature. By only funding it at 90 percent in the current year, there would be a gap the following year when there was sure to be a deficit and even less available funds. He noted his intention of establishing whether forward funding was a best practice. He considered it important to provide some clarity in the current budget. He thought that the will of the legislature might be to ensure that it showed the education community that it did intend to fund education. He referred to the fiscal summary, which showed draws on the constitutional budget reserve (CBR) and a difference of \$127 million which would be a forthcoming expense the following session. He was not sure that forward funding was an appropriate budgeting tool, and wondered if other members had similar concerns. He asked Representative Gattis to comment on the matter.

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Representative Gattis remarked that such budgeting (forward funding) had been a concern with subcommittees, and also thought it was important to bring some clarity to the process. She thought it was difficult for people to understand, and related that her constituents perceived the budget process as "a shell game."

Co-Chair Neuman noted that the expense drew less from savings in the current year but would be present the following year, and even more would need to be withdrawn. He stated the committee would work with the department to identify the concerns and plan for moving forward.

Representative Pruitt added his support for what was stated with regard to forward-funding for education. He referred to the aforementioned discussion that would take place in the summer, and felt that it was a dubious and doubtful task to engage in productive discussion regarding the education formula during the time frame mentioned. He stressed the critical importance of clarity for the public as well as school districts. He highlighted the importance of discussion of education funding, but was not optimistic about "fixing the formula" over the summer. He thought that the one-time funding should be funded in its entirety, or not at all.

Co-Chair Neuman supposed that the legislature could not fund the one-time money and say that it cut \$1.27 billion out of the current year's budget.

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Representative Wilson asked if the \$240 million decrease included the \$91 million. Ms. Pitney said that OMB could provide the numbers to clarify.

Representative Wilson referred to the Department of Labor and Workforce Development (DLWD) budget, which reflected a reduced authorization, and asked if it was a "real" budget cut. She noted that many of the budget cuts on the budget summary were related to reducing authorizations. She recounted her experience with reducing authorizations in the budget, which she considered to make it appear as if there were budget cuts when there were not, and asked if that was what was shown on the budget summary. Ms. Pitney explained that DLWD was being reduced by almost \$4.3 million on a \$33 million unrestricted general fund (UGF), which was an almost 13 percent UGF reduction. She added that it was fortunate that DLWD operated heavily with federal funds, so the reductions were not relative to their entire operation. She pointed out two areas being reduced in the immediate sense: the allied health programs in the Alaska Vocational Technical Center (AVTEC); and a

reorganization of business partnerships and a reduction of staff. She noted that the decreases combined with a decrease in federal funding for job centers would have a real service impact for DLWD. She summarized that while there was authorization reductions, the \$4.2 million was also a reduction in real services.

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Representative Wilson expressed her understanding of the cuts, and highlighted the importance of the public understanding the difference between authorization and actual funds. She described authorizations as money that departments may have gotten but did not necessarily have at the current point.

Ms. Pitney replied that for every state agency, the budget process required authority to expend, regardless of the fund source. She used a hypothetical scenario about a federal project to illustrate the concept of authorization. She continued that there were some authorization reductions, but when UGF was discussed it represented cash in the bank and real service reductions of revenue that was no longer available.

Ms. Pitney explained her intention to highlight larger reduction components of each department, and wondered if she should continue in the same way. Co-Chair Neuman asked that she continue discussing the highlights.

Ms. Pitney discussed reductions in Department of Commerce, Community and Economic Development (DCCED) within the Tourism Marketing Program, the Alaska Seafood Marketing Institute (ASMI), and internal departmental changes, to equal a nearly \$5 million decrease from the previous year. She pointed out a \$24 million reduction in Department of Corrections (DOC); a key component of which was a reduction of the Community Jails Program.

Ms. Pitney referred to Department of Education and Early Development (DEED) and discussed a reduction to some of the grant programs on the non-formula side including digital learning, network, and broadband programs. She listed a reduction in food and water inspections in the Department of Environmental Conservation (DEC), resulting in fewer inspectors. She pointed out a reduction in the Department of Fish and Game (DFG), part of which was made up with fund-source shift to other DFG receipts.

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Ms. Pitney pointed out a reduction in the Office of the Governor, including one-time reductions in the Division of Elections, and with primary reductions in reduced staffing levels from previous years. She pointed out one of the changes from the recently presented overview budget; originally there were non-formula programs that were being reduced that shifted to some formula programs being reduced. She discussed reductions in Department of Health and Social Services (DHSS) due to some office streamlining, and grant program reductions. Additionally in DHSS, there were two components related to Medicaid expansion; including a state to federal cost shift for the Catastrophic Acute Medical Assistance (CAMA) program, a program for individuals who would be eligible for Medicaid. She noted three primary offsets in the budget due to Medicaid expansion: CAMA, a \$1.5 million reduction in behavioral health grants, and cost savings from additional eligibility of the Medicaid expansion population for some prisoners transported to medical facilities.

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Ms. Pitney addressed a "fairly significant" reduction to the Department of Law (DOL), which reflected the number of lawyers and support staff and pooling of resources. She pointed out that Department of Military and Veterans Affairs (DMVA) had been split in to two components on the budget summary, and that it was largely federally funded. She explained that although the reduction of 4.5 percent would have an impact, because its operations were largely federally funded, the department would continue to operate well. She specified that the Alaska Aerospace Corporation, shown on a separate line on the budget summary, had been zeroed out for general fund. She furthered that OMB had asked the aerospace board and the chief executive officer to look at opportunities for privatizing the operation.

Ms. Pitney pointed out a reduction of 2.5 percent to the Department of Natural Resources (DNR). She explained that DNR was a fairly high priority due to the nature of the revenue capacity that they supported for the state. Similar to DOL, there would be pooling of resources through minimizing stand-alone offices and having expertise in a more general pool of resources.

Ms. Pitney addressed the Department of Public Safety (DPS) and noted the biggest reduction in transitioning from a stand-alone highway patrol division to having all troopers serve the full scope of a trooper requirement. She clarified that transition would require all troopers to work in the whole breadth of the trooper component rather than specializing in highways alone. She pointed out a reduction in the specialized special emergency reaction teams (SERT), who would also be required to work in full trooper duty. She noted that the number of troopers would be impacted across the board.

Ms. Pitney stated that reductions to the Department of Revenue (DOR) were much more on the administrative side, with the reduction of some administrative duties, as well as in the tax area including elimination of the film tax credit division.

Ms. Pitney discussed components in the Department of Transportation and Public Facilities (DOT) with a reduction in the Alaska Marine Highway system, a reduction in the various maintenance and operations areas for surface transportation, and consolidation in the IT divisions. She specified that the overall reduction totaled \$10.8 million. She referred to a 2.5 percent reduction in the University of Alaska, driven by recommendations from the Board of Regents. She added that the reduction was similar to what the reduction in K-12 education would be.

Ms. Pitney addressed a reduction to the fuel utilities mechanism (commonly known as "the trigger mechanism"), noting that the mechanism was being eliminated. She added that with the price of oil going down, the mechanism would not have been invoked in the first place.

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Ms. Pitney referred to the branch-wide unallocated reserve, and explained that the administration was proposing a \$10 million contingency fund of sorts. The funds were planned to mitigate effects of the large reductions that were being made, some of which may have unintended consequences or may inadvertently impact another agency. She noted that relative to a \$134 million reduction among agency non-formula operating budgets, the \$10 million was to correct any errors. She referred to a proposed decrease of just

under \$500,000 to Judiciary. She left the legislative budget for the body to work out.

Co-Chair Neuman asked if the \$10 million reduction when the fuel trigger was eliminated was the same \$10 million being moved to the governor's office for the contingency fund. Ms. Pitney replied that the description of the \$10 million was correct, whether it was part of the \$24 million reduction in DOC versus the \$27 million reduction in the fuel trigger mechanism. She did not think the \$10 million for the contingency fund could be attributed to any one of the reductions. She added that the purpose of the \$10 million was to address cuts that may not have been in the best interest of Alaskans; or to "shore up the edge" until future plans could be made.

Co-Chair Neuman stated that he had done a similar funding maneuver in the past in DHSS. He noted that there was a legal opinion stating that the maneuver was unconstitutional since it was unallocated funds from the legislature. He stated that the supplemental could be better used to address any issues that arose. He referred to the current year's supplemental budget, which was left at zero, and shared that normally it would be at around \$20 million. He mentioned that in times past it had been up to \$50 million, but was reduced to minimize draws on the budget. He reiterated that it appeared as though the \$10 million would be housed under the governor's office, and asked Ms. Pitney to discuss reasons why.

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Ms. Pitney replied that the \$10 million was for the flexibility of providing for unintended consequences of a reduction.

Co-Chair Neuman indicated there would be further discussion on the subject.

Co-Chair Thompson noted he was not looking to criticize but felt there were items he did not feel were actual reductions. He referred to Medicaid expansion and pointed out that many reductions listed on the budget summary were based on the assumption that it would go through. He referred to the Kotzebue community jail and used it as an example to discuss expenses that were a result of reductions. He expressed the need for responsible cuts but

was concerned about having "real numbers" listed in the budget.

Vice-Chair Saddler asked about the governor's statement that the fiscal situation demanded a response of 16 percent budget cuts, and stated that he did not see cuts to that amount in departments or budget-wide. He asked if Ms. Pitney could explain the discrepancy. Ms. Pitney responded that she was not aware of the exact quote, and that OMB had asked the commissioners to forecast service delivery three or four years in the future in the case of a reduction of 25 percent in state funding. She qualified that it would be a multi-year process to make the reductions, and they would inevitably identify particular areas that the government would not want to reduce to 75 percent of the current level of surface. In other areas, it may be possible to cut 25 percent or even 30 percent through drastic changes in how business was done. She stated that the reality of the funding in a deficit environment of \$3.5 billion, even at a 25 percent reduction, left an inability to reach the deficit level. She postulated that there were two conversations going on: what would the state look like if its footprint was much smaller; and what was the right size of government for Alaska, given the services expected and the uniqueness of the state and its geography. She furthered that Alaska had the largest airport system in the world, and the largest marine highway system in the world. She added that there was a third item to be aware of, whether the state would be fortunate in the price of oil, or would it have to pull out different tools going forward.

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Co-Chair Neuman asked Ms. Pitney to clarify that the aforementioned 25 percent reduction was for non-formula funds. Ms. Pitney stated she would like to challenge the reduction for all areas, but reiterated that it was likely there were certain areas that couldn't be 25 percent smaller. She thought that without asking for the challenge, things would not be looked at differently.

Co-Chair Neuman agreed and stated that his understanding was the governor's request to the departments was for a 25 percent over four years on non-formula funds, which would be equivalent to a \$550 million reduction from \$2.2 billion in formula funds, and would clearly not deal with a \$3.5

billion deficit. He characterized the governor's statement as "everything is on the table."

Vice-Chair Saddler noted that he thought the expectation was raised for a 16 percent reduction, and wondered how well the state would be served by not making the harder cuts sooner. He echoed Ms. Pitney's statements regarding more budget cuts being necessary in the future, and stated that he looked forward to working with Ms. Pitney and OMB to make the reductions sooner rather than later.

Representative Edgmon referred to a previous conversation with Co-Chair Neuman and alluded to his subcommittee budgets for DOC and DPS; he noted that in the subsequent week he would be having a joint meeting between two subcommittees to fully measure the cutting of community jails in particular and the corresponding impact on DPS. He noted that there would be representatives from the court system and DOA to be present to help further delineate the overall supply chain of costs that included prisoner transport and video conference. He also noted they would be addressing videoconferencing as a means of cost savings. He spoke to the impact of budget cuts and that sometimes the impacts of the cuts were very different than they were initially perceived to be.

Co-Chair Neuman stated that Representative Edgmon made a good point and that subcommittees were working on a process to break down silos between departments.

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Representative Gara opined that when the budget was regarded by the public, the cuts would be characterized in different ways. He discussed the funding of the retirement system, and reiterated that he thought it was inaccurate to call the \$257,278.30 direct appropriation an increase in spending because of the previous year's expenditure of \$3 billion spent from the CBR. He asked the administration to consider that school districts wanted early and adequate funding; explaining that of the two, schools would rather have adequate funding for the coming year. He considered "adequate" funding to be beyond what was done the previous year, and beyond what was being proposed in the governor's budget. He would consider adequate funding to be not cutting any more teachers, and not cutting any more staff. If the state was not going to do early funding, he hoped it

would do at least adequate funding after facing years of teacher and staff cuts that could drive people from the state.

Ms. Pitney acknowledged Representative Gara's remarks.

Representative Wilson revisited the idea of a 16 percent cut as heard from the governor. She shared that her constituents had communicated that they did not want to pay for additional revenue. She asked if the administration was looking at a maximum amount of savings it was looking at taking out for the following year. Ms. Pitney restated that OMB had asked departments to look at what their current operations would look like at a 25 percent reduction. She highlighted the importance of making the reductions in an informed manner, with knowledge of current issues and cost ramifications; and the impact to the overall economy. She stated that the 25 percent target was being considered over time, with agency operations being reduced 6 percent this year and the following two years. She commented that the overall reduction being reflected at 2 percent was due to increased tax credits and increased retirement savings. She emphasized that making the budget reductions was a balance, and added that this was the first year (with the exception of the university) that agencies were faced with a GF budget that was less than the prior year. She characterized the timeline as a prudent balance, and asserted that the legislative body had the ability to go faster. She stated that the cuts affected people and did push off to other entities.

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Representative Wilson stated she would like to see the departmental plans and noted that she would soon be working in budget subcommittee. She commented that she had received little information from the departments about program and budget specifics.

Co-Chair Neuman remarked that he had discussed related matters with Ms. Pitney and hoped to address them later in the meeting.

Representative Wilson clarified that she was referring to the plans that showed what the departments would look like at 20 to 25 percent less. She wondered why the committee could not view the plans in order to help make the

judgement as to what cuts to make. Ms. Pitney explained that the target was given to the departments, with the expectation that the commissioners begin considering the scenario. They had gotten through the 5 percent and 8 percent reduction scenarios, but the plans looking at a longer term reduction of 25 percent were not currently available. She furthered that the plans, when available, would inform how to take the next steps in budget reductions where appropriate.

Co-Chair Neuman stated that he had a similar understanding and that it was the goal set to work on through the summer.

Vice-Chair Saddler made note of the long-term trend of increased education funding, and asserted that the legislature was not firing teachers.

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Representative Munoz asked for clarification on the overview and if Ms. Pitney would explain areas in which there was a funding deletion that was also added back in. Ms. Pitney gave the example of the Alcohol and Beverage Control Board (ABC) and the marijuana law as one of the important operations that needed to happen despite budget reductions. She explained there was a reduction throughout DCCED, however there was also an increase of approximately \$1.4 million for the ABC board. She furthered that there were increments for all of the bargaining unit salary adjustments, and the reduction target had to be met after the increases. For each entity to meet their reductions, there were additional cuts to make in order to meet the salary obligations.

Representative Munoz pointed out \$850,000 of restored funding in the DEED budget for the Language Network, and a line below it indicating the reversal of the amount; and stated that such examples were seen throughout the document. Ms. Pitney explained that the scenario was reflecting when a particular entity was given a three-year program, in this case \$2.5 million to spread across three years.

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DAVID TEAL, DIRECTOR, LEGISLATIVE FINANCE DIVISION (LFD), noted that he would be presenting the budget, and thought

it might be helpful to ensure there was a common understanding of terms. He went on to explain the column known as "governor's endorsed budget," which was also sometimes called the "governor's amended budget." He stated that LFD did not use the latter term, as it was reserved for the budget as the governor submitted amendments on February 18th. He furthered that the WIP budget was "dead," and was merely a budget submitted to meet a statutory deadline, and had now been replaced by the governor's endorsed budget. He did not see the need for comparisons between the previous year's budget and the WIP budget, nor between the WIP budget and the governor's endorsed budget. He considered that it would simplify things immensely for the committee if they would consider the governor's endorsed budget only.

Mr. Teal explained that he would be working from the document "State of Alaska Fiscal Summary-FY 15 and FY 16" (copy on file). He noted the purpose of a fiscal summary was to provide clear and concise comparison of spending by category across fiscal years. He thought that emphasizing the categories was important because LFD looked at agency operations differently than they looked at statewide, because of the ability to control the agency operating budgets much more readily than statewide costs. He added that cash flow surplus and deficit was also reflected in a fiscal summary, as well as deposits and withdrawals from reserve accounts. He stated that OMB had adopted a format very similar to LFD several years previously, however in the current year the format had become more challenging to compare on a line by line basis. He argued that it did not need to be compared on a line by line basis, but the summaries matched on the bottom of the documents, for total state spending as well as each of the categories. He qualified that the summaries did not exactly match; there was a \$20 million difference due to the fact that OMB did not have a supplemental placeholder on its document. He pointed out line 45 of the fiscal summary, which showed pre-transfer authorization of \$5,624.9 million for FY 16; and OMB's fiscal summary indicated \$5,604.9 million for pre-transfer authorization.

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Mr. Teal discussed the \$20 million supplemental placeholder, and wondered if it was a problem that it was not reflected in OMB's materials. He pointed out that the

fiscal summary listed the supplemental budget for FY 15 on line 15 for about \$45 million; and clarified that did not mean it would be the same every year. He pointed out the predictability of some supplemental budget items such as fire suppression (could run \$20 million or more), and judgements and claims (\$6 million for the current year). He stated that LFD was more concerned about areas such as the Public Defender's Office and the Office of Public Advocacy (OPA), in which there was a supplemental request of about \$300,000. In the past such supplemental requests had an accompanying request for the following year. In the current budget this was not the case, in fact there was a deficit. He shared that LFD was concerned about the ability of such agencies, which were case-load driven, to be able to really absorb the cuts. He thought perhaps the inconsistency was on purpose. He expressed that he knew the executive branch was working to reduce costs. He acknowledged that they may have been aware of missing things from the supplemental budget to the FY 16 budget requests, and were considering them as planned reductions for FY 16 or FY 17.

Mr. Teal pointed out Section 4 of the HB 72 Operating Budget:

Sec. 4. LEGISLATIVE INTENT. (a) It is the intent of the legislature that the amounts appropriated by this Act are the full amounts that will be appropriated for those purposes for the fiscal year ending June 30, 2016.

Mr. Teal thought there was an issue with Section 4, and asserted that some managers could manage with the budget they were given, and some could not. He considered it not a management flaw, but rather that certain areas had costs that were uncontrollable. He used Medicaid as an example, as well as fire suppression. He noted a few other concerns, including a \$10 million unallocated appropriation, and a legal opinion pertaining to the unallocated "contingency funds" discussed earlier. He clarified that it was not merely an opinion; rather it had been tested in 1983 and declared by the Superior Court of Alaska to be unconstitutional. LFD was concerned that the funds could not stay in the bill the way it was presently drafted. He pointed out that if those funds are removed, the governor would have no money to meet what might be supplemental needs. He summarized it as an argument for the supplemental

"placeholder" to be in the budget, at whatever amount was chosen.

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Mr. Teal referenced the public education fund, and recognized there had been some confusion. He referred to line 49 of the Fiscal Summary, which showed a negative number of \$113.5 million. He explained that normally a negative number indicated a withdrawal from savings, however in this case it indicated a negative cash flow. He discussed forward-funding and pointed out the amount going in for FY 17 was \$126 million less than was projected to be needed for FY 17. He explained that there was nothing technically incorrect about the situation, but it brought up the issue of transparency. He favored making the amount of spending and the amount of the deficit as clear and simple as possible, and alleged that the deficit and the CBR draw were essentially the same thing. He iterated that when the legislature started drawing money or failing to fully fund something in a reserve account, so that it appeared as if savings were being used, the fiscal gap appeared to be reduced and it was harder to understand the balance of surplus and deficit. He went on to describe a hypothetical scenario of short-funding the education fund for FY 17 to make the deficit appear smaller. He voiced the concern that the public education fund, if not filled, would no longer be available as reserves.

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Mr. Teal commented that he was not aware of the governor's intent with regard to the public education fund, however the amount of short-funding would not matter and disguised the amount of the deficit. He emphasized the importance of not understating the deficit for the public or other entities. He opined that it was not clear to the public that the short-funding was distorting the deficit.

Mr. Teal pointed out line 46 of the "OMB vs LFD UGF Fiscal Summary," (copy on file) showing a pre-transfer surplus deficit of \$3.428 million for FY 16; and noted that OMB emphasized the post-transfer deficit (line 65 of the comparative fiscal summary) and did not have a pre-transfer deficit printed on its summary. He considered the pre-transfer figure to be more important in communicating how the current year's revenues compared to spending the

current year's money before pulling money from savings accounts. He extrapolated that money was pulled from savings accounts, it would easily reduce the deficit by \$1 billion; however, in the long term nothing had been accomplished as the \$1 billion in other reserves was not available to spend.

Mr. Teal remarked that it was not easy to simplify the budget due to political considerations. He discussed the challenge of incomplete budget information conveyed by the press and the challenge for the public to understand what the press did not report.

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Mr. Teal explained the third issue was reappropriations. He noted that there were always reappropriations and it was not merely a governors issue or an OMB issue. He explained that reappropriations could be from one capital project to another; from capital budget to operating budget, or the reverse. He thought that capital to capital reappropriations were fairly easy, simple to understand, were like changing the scope of a project, and there was no new money involved. He noted that confusion could arise because reappropriations crossed fiscal years, and did not receive the scrutiny that other funds did. He argued that in the present fiscal climate, perhaps the funds should go back to the GF in order for any potential projects to compete for the funds with all other projects. He considered that such a process could be a way to reduce spending because of a change in methodology.

Co-Chair Neuman clarified that the point of putting funds back into the GF rather than reappropriating would provide clarity on explaining the budget, particularly in the current fiscal situation. He highlighted that public money was being spent, and clarity in explaining the budget was crucial. He added that when there were reductions in an agency, and they used other funds to backfill agency operations, the agency was not really reduced. He expressed concern and asked Mr. Teal if it was a normal practice. He noted that he had seen a lot of agencies participating in the activity by using special use funds and other means of backfilling.

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Mr. Teal thought that it muddied the water to use funds in such a way. He used the example of creating a Medicaid fund with \$500 million in it, and the subsequent finance DHSS subcommittee's budget would not reflect the \$500 million of GF. He summarized that the process would not give the subcommittee all the information about the funding that was used in that department. He urged the committee to avoid running money through funds, and appropriate general funds for shortages in agencies rather than filling a fund and creating a different picture for the subcommittee. Mr. Teal reiterated the need for transparency in order to have the clearest budget picture.

Co-Chair Neuman noted the approximate 25 percent turnover in the finance committee and reflected that it was important to have a system in place with clear accounting practices.

Ms. Pitney commented that she agreed with Mr. Teal in some cases but considered there to be some cases that were different, such as direct-service items. She compared the difference in funds and thought that the funds acted differently. She thought that to the degree that offline funds could be reduced and made to be UGF, there would be a lot more clarity.

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Vice-Chair Saddler stated that in the DHSS budget he was working with were several million dollars of unallocated reductions; and asked if Mr. Teal could address the use of unallocated reductions as a way to cut the budget. Mr. Teal considered the weak point to be lack of opportunity for the legislature to deliberate the effects of the budget cut. He furthered that in using unallocated reductions, the legislative body would be ceding the power of appropriation to the executive branch. He asserted that it was the legislatures job to determine how much money was appropriated for what purpose, and by simply saying "cut somewhere," the legislature was failing to do its job. Conversely, the unallocated reduction gave the executive branch the flexibility they needed to absorb a cut. He reminded the committee that after the budgets were prepared, the administration needed time to determine where the cuts could be taken.

Mr. Teal referred to the time needed to formulate cuts and described the scenario as a "huge offsetting balance." He considered that as long as unallocated reductions were used with that in mind, they were not bad, as long as they were left unallocated within a restricted area. He furthered that an unallocated reduction or increment in the governor's office, with no sideboards, was unconstitutional. An unallocated reduction within a department had some legal challenges with it, but was much less legally problematic when it had confines and could be spread between multiple allocations.

Representative Gara asked about a number he had heard regarding a potential \$1.5 billion in savings through cutting all state employees. Furthermore, he had heard discussion about a \$3.5 billion cut from the \$5.6 billion UGF budget and wondered if Mr. Teal viewed the cut as realistic. Mr. Teal responded that both numbers were factual, and explained there was roughly \$2.6 billion spent on personal services. He clarified that only about half of state government positions were funded with GF, with some being only partially GF funded. Mr. Teal discussed the hypothetical \$3.5 billion cut and referred to an introduction in the governor's overview which included a list of "hard to cut items" items, including K-12 formula funding (roughly \$1.3 billion), Medicaid (roughly \$700 million), and debt service (roughly \$200 million). The items totaled \$2.2 billion, which was equal to the amount of UGF revenue that the state had. He concluded that if the legislature was going to try and cut \$3.5 billion from the budget in order to match revenue, the state could have the three items listed and nothing else, or find cuts in the "hard to cut" areas. He did not think it was possible to cut \$3.5 billion from the budget.

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Co-Chair Neuman commented that the departments had worked hard to uphold the governor's proposed reductions. He acknowledged the difficulty of reducing the budget by \$1 billion, and recounted that the previous year's operating budget had been reduced by \$70 million. He opined that cutting the state government drastically could result in inefficiency. He stated that the committee would look at the Governor's amended budget and have a discussion to ensure clarity in the budget process. He referred to DHSS and a bubble chart they created to reflect their priorities

and use as a budgeting tool. The chart also illustrated the cross-overs between departments which enabled them to identify efficiencies. He concluded that his suggestion was to try and utilize the same methodology with departments and then create a budget from the work.

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Co-Chair Neuman continued to note that he had asked LFD and the commissioners to examine laws, regulations and policies for opportunities for savings. Statutes and regulations could be examined for additional personnel costs and procedures that did not make fiscal sense. He added that the committee would be unlikely to pass any legislation with a sizeable fiscal note unless it was very good. He forecast that by the subsequent year there would be more information on the price of oil, the revenue forecast, and a profile of the size of government the state could afford to fund. He stressed the need for building a government based on the funds that were available rather than continuing to use the state savings, would last about 2.5 years without utilizing the permanent fund. He thought the committee needed a current plan to address the deficit in forthcoming years as well as the current deficit. He supported giving the departments the tools they needed for a strategy to identify and protect core missions.

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Representative Guttenberg relayed that he appreciated Co-Chair Neuman's statement and goals. He stressed the importance of defining the core function of government. He expressed concern with some of the cuts being proposed; and mentioned prisons, job training, therapeutic programs, and the system of dealing with societal woes. He discussed stresses on society in the long run, and elaborated that perhaps in the future the state would see resultant increases in corrections. He wondered how it would be possible to get through the work in a 90-day session, and noted the difference in what could be accomplished and examined in a 120-day session. He discussed the depth of understanding needed to understand the cascading effects of a diminished budget. He mentioned the concept of "silencing."

Co-Chair Neuman noted that next week the committee would be hearing about a recidivism/reduction group and its goals.

Co-Chair Neuman thanked the testifiers, as well as department staff in attendance.

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ADJOURNMENT

3:27:19 PM

The meeting was adjourned at 3:27 p.m.