

HOUSE FINANCE COMMITTEE  
January 18, 2018  
1:31 p.m.

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CALL TO ORDER

Co-Chair Seaton called the House Finance Committee meeting to order at 1:31 p.m.

MEMBERS PRESENT

Representative Paul Seaton, Co-Chair  
Representative Les Gara, Vice-Chair  
Representative Jason Grenn  
Representative David Guttenberg  
Representative Scott Kawasaki  
Representative Dan Ortiz  
Representative Lance Pruitt  
Representative Steve Thompson  
Representative Cathy Tilton  
Representative Tammie Wilson

MEMBERS ABSENT

Representative Neil Foster, Co-Chair

ALSO PRESENT

Pat Pitney, Director, Office of Management and Budget, Office of the Governor; Neil Steininger, Chief Budget Analyst, Office of Management and Budget, Office of the Governor.

SUMMARY

FY 19 BUDGET OVERVIEW: OFFICE OF MANAGEMENT AND BUDGET

Co-Chair Seaton reviewed the meeting agenda.

^FY 19 BUDGET OVERVIEW: OFFICE OF MANAGEMENT AND BUDGET

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Co-Chair Seaton asked if Ms. Pitney would prefer questions throughout the presentation or at the end.

PAT PITNEY, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET, OFFICE OF THE GOVERNOR, replied that asking questions throughout the presentation was preferable.

NEIL STEININGER, CHIEF BUDGET ANALYST, OFFICE OF MANAGEMENT AND BUDGET, OFFICE OF THE GOVERNOR, provided a PowerPoint presentation titled "State of Alaska FY2019 Budget Overview" dated January 18, 2018 (copy on file). He began on slide 2 and addressed key budget items beginning with public safety investments totaling \$34 million and 18 positions. The funding was allocated to enhanced trooper and prosecutor presence in rural Alaska, substance abuse treatment grants, Department of Corrections (DOC) prison operations, a statewide drug prosecutor, support positions to free up trooper time, additional public defender support, and prosecutor and investigator positions in Anchorage. The proposed budget would fully fund the Medicaid budget based on the Office of Management and Budget (OMB) FY 19 projections. The budget included health care funds for continued work towards the health care authority to try to arrest some of the rising costs of health care in Alaska.

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Vice-Chair Gara asked if the public safety information would only be addressed at the current time. Mr. Steininger responded affirmatively.

Vice-Chair Gara remarked on the lack of state troopers, which he believed was dangerous. He stated the budget had included authority to hire additional troopers; however, the state had not been able to hire the troopers for numerous reasons. He asked about the approach in the proposed budget to address the issue. He reasoned that adding more positions would not result in additional troopers.

Ms. Pitney replied there was funding in the trooper budget for trooper recruitment and hire. The items in the budget [on slide 2] included two drug investigators collocated with prosecutors. The administration did not want the items to compete with current troopers and it wanted added capacity. The intent was to fill the available trooper

positions that were funded and available. Funding would be short once the positions were filled if the funding was not requested in the budget. Given limited trooper time, the desire was to have staff positions to get the report turned around in a 48-hour period. She detailed that troopers were addressing such a high number of crime incidents there was a time lag in the reporting. The \$600,000 would go to hiring staff to enable the reports to be filed within 48-hours. She relayed that hiring the support positions and additional troopers would mean funding would be short. The administration continued to aggressively use available funds to recruit as many troopers as possible to get fully staffed. The funding would also be utilized for trooper retention to retain as many troopers as possible.

Representative Wilson asked what the statement on slide 2 meant by "Medicaid fully funded." She asked for the total funding and the number of individuals currently in the Medicaid program.

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Mr. Steininger replied that fully funding Medicaid would be about \$691 million undesignated general funds (UGF), which was an increase of about \$127 million over the FY 18 management plan. There was a slide later in the presentation showing the total projections. Factoring in the supplementals, the proposed budget included about \$27 million over what OMB projected to actually spend in FY 18. The projections were based on modest continued increase in the Medicaid population. The population had increased significantly, but OMB anticipated the increase to somewhat plateau. He added there was a slide later in the presentation showing the total population projections.

Representative Wilson pointed to the \$18 million for substance abuse treatment grants (slide 2). She asked how the grants were monitored. She remarked that behavioral grants and others had been prior to Medicaid expansion. She thought that it appeared there were the same number of grants. She asked who was serviced by the \$18 million for substance abuse treatment grants.

Ms. Pitney replied that Attorney General Lindemuth and all agencies had come together to develop a public safety action plan, which had been released in October. She stated it had been primarily related to the criminal justice

population. There were many people going into prison and most of what they needed was substance abuse treatment. The increment was focused on the population coming into the state's court and legal systems. The intent of the increment was to determine - prior to putting an individual in jail - if their issue was only related to substance abuse, which could be treated and enable the person to have a productive contribution.

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Representative Wilson was concerned they were not using community centers/halfway houses. She stated that under Medicaid expansion, if a person was on electronic monitoring or in a halfway house, the federal government would pay. However, there had been a decrease in the usage of the options. She asked if there was anything in the works by DOC that would enable a large portion of the \$18 million to fall under Medicaid or Medicaid expansion.

Ms. Pitney responded that the state had a lack of substance abuse treatment operations. Part of the grant would go towards ensuring the state had a place for people to go for substance abuse treatment. The operating dollars, to the extent possible, would be covered by Medicaid.

Representative Ortiz asked if the \$34 million for public safety reflected a direct increase from the Department of Public Safety (DPS) FY 18 budget or replacement money. He asked how the increment compared to FY 18.

Mr. Steininger replied that the \$18 million in substance abuse treatment grants was a multi-year supplemental. The remainder of the items in the public safety action plan would add to the FY 19 operating budget.

Representative Ortiz asked if the FY 19 operating budget had been flat funded or increased from FY 18. Mr. Steininger replied that the increment reflected an increase from FY 18.

Ms. Pitney added that the DOC increment was an increase over the supplemental included for DOC health care.

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Representative Guttenberg referred to the \$2.9 million for enhanced trooper and prosecutor presence. He asked if the increment included Village Public Safety Officers (VPSO). Ms. Pitney replied in the negative.

Representative Guttenberg remarked that the VPSO grant recipients had greater restrictions on grants than troopers had when they received appropriations. He detailed that there was not the same ability available to hire VPSOs as there was for hiring troopers. He wondered if there was anything in the works to make VPSO hire more efficient instead of merely giving troopers more money in rural Alaska. He reasoned that hiring the correct number of VPSOs would be less expensive and more effective than troopers.

Ms. Pitney suggested speaking with DPS Commissioner Walt Monegan about the issue. She relayed that the commissioner was well prepared for the conversation. The administration's interest was a broader presence in the public safety arena, first utilizing the dollars available in the budget.

Representative Guttenberg asked if the increase in Medicaid cost was due to an increase in Medicaid recipients or an increase in health care cost.

Ms. Pitney replied that the number of Medicaid recipients was growing; the total was currently just under 200,000. The increase over the past few years had been split equally between Medicaid expansion and traditional Medicaid. The administration was projecting the same expenditure for FY 19 from a state perspective as there had been in FY 15. The number of recipients was about 30 percent more at present than in FY 15 and the administration anticipated about 34 percent more for FY 19. She mentioned holding down state cost while serving 75,000 additional people (about half were Medicaid expansion); OMB believed the increase was exacerbated by the recession.

Representative Guttenberg asked for more detail about the \$1 million for continued work towards health care authority [slide 2].

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Ms. Pitney replied that \$750,000 of the \$1 million would go to working towards implementation on health care authority

and \$250,000 was a broader legislative administration provider stakeholder effort to begin looking at the broader cost of health care in the state. She relayed that the public comment period on the feasibility study for the health care authority had concluded and the administration was currently engaging with public employer's union trusts on how to move forward on a win-win basis. The \$750,000 would largely be for additional analysis (comparing a union trust package with an AlaskaCare package and University of Alaska package) and review of actuarials to determine how to combine public employers appropriately and what the structure would look like from a governance perspective. Employees wanted a voice and assurance they were somewhat in control of their healthcare. Through the health care authority studies, best practices had been witnessed at the union health trust and good practices had been seen at the University and in AlaskaCare. The goal was to look at all of the best practices for use going forward. She considered the governance structure for considering all of the groups combined; the \$750,000 began to address the right plan and how everyone had a voice in the plan moving forward.

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Co-Chair Seaton recognized Representatives Geran Tarr and Dan Saddler in the audience. He reminded committee members that the current presentation was a budget overview. He asked members to consider that detailed questions could be answered by individual departments. He communicated that he was not trying to stifle questions.

Representative Grenn would hold his question for the department at a later date.

Representative Kawasaki asked if someone would present on the Public Safety Action Plan specifically at a later time.

Co-Chair Seaton replied that the committee would hear a presentation as a unit.

Representative Kawasaki would hold his questions until that time.

Vice-Chair Gara spoke to the Medicaid funding increase. He remarked that during recessions Medicaid spending went up and when the economy was good Medicaid spending stabilized.

He asked if the Medicaid increase pertained to additional services, the number of recipients, or a combination.

Ms. Pitney replied that the increase was due to new Medicaid recipients. She elaborated that the state had reduced its reimbursement rates the previous year to drive costs down. Additionally, the state had reduced hours of time for certain categories of disability day care and it had discontinued payment of new codes. The state was paying less and for the third consecutive year it had offered no inflationary cost increases on rates. Much had been done to drive the service cost down; the increase was primarily driven by the increased number of recipients.

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Co-Chair Seaton recognized Representative Andy Josephson in the audience.

Mr. Steininger advanced to slide 3 and addressed additional key budget items. He highlighted oil and gas exploration credits. The administration had proposed debt refinancing, which would allow small explorers the opportunity to receive payment immediately for their oil and gas exploration credits starting at a 10 percent discount. The discount enabled the state to cover the financing costs through a general obligation bond package that would cover the upfront payment of the exploration credits.

Co-Chair Seaton asked if there would be additional detail about the increment later on.

Ms. Pitney answered in the affirmative. She relayed the legislation would come to the committee the following week. The proposal was designed as a win-win opportunity for the state and explorers. The cost of capital for small companies could exceed 15 percent or more; the ability for companies to get cashable credits up front was better than waiting five to seven years to receive the statutory minimum. She detailed that the discount would mean the state's net present value (NPV) was neutral (no additional cost from the Treasury) to the current year to year payments. Cash payments would be more aligned with the state's cash flow. There would be smaller cash payments at present that would be a bit larger in the future. The administration's interest was to have funding redeployed in Alaska to the extent possible. There were numerous

opportunities on the horizon for exploration and the administration believed paying the credits immediately would have a better impact on jobs.

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Co-Chair Seaton referred to testimony that general obligation bonds were generally restricted to capital projects. He asked if the statement was generalized.

Ms. Pitney clarified that it was not a general obligation bond, but a subject to appropriation bond. The bond would take the liability for explorers to a debt liability to the state.

Co-Chair Seaton stated that a 10 percent discount at 3.25 percent meant that in three years the interest rate would eat up the entire discount and would cost the state more for further payments. He discussed converting from a payment based on received revenue from production tax and reasoned that if oil prices declined again the state would still be stuck with payment of a bond issue with very little revenue to pay with. He wanted to ensure the presenters covered the items when discussing the bond issue.

Representative Pruitt wanted to understand how the subject to appropriation bond would work. Additionally, he wondered if there was an expectation that the administration would come forward with a request for an increase in another way if the legislature chose not to appropriate funds for the bond. He remarked the \$27 million included in the budget was lower than what statute would indicate.

Ms. Pitney answered that the subject to appropriation bond would be explained [at a later date]; the legislature would have to pass a piece of legislation to approve the bond. The governor's plan was that the debt refinancing was the appropriate way to go. She furthered that if the legislation was not passed, the legislature would have to determine at what level to pay the tax credits. She did not anticipate an amendment from the administration; its proposal was the debt refinancing.

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Vice-Chair Gara stated that in the past the legislature had passed legislation allowing the purchase of credits to small companies at whatever BP, ConocoPhillips, and ExxonMobil; and the small explorer agreed to. For example, BP could purchase \$1 million in tax credits; at the present cost of \$500,000 they could pay 50 percent and an explorer could take it immediately instead of holding onto it. He stated they could pay half or whatever was negotiated. He about the benefit of a bill specifying that the state would pay all of the funds without the flexibility to negotiate with explorers or companies holding credits. He hoped it was a policy question people would think about when developing legislation.

Ms. Pitney pointed out that if a small producer sold \$50 million to a large producer, the state would see \$50 million less revenue because the producer could write it off. The small explorer was disadvantaged, and the money did not come back into the small explorer's capital to be reinvested and the state was no better off because it lost the revenue. She agreed that the company could sell its credits to a larger producer that was paying tax, but the state revenue would be reduced by that full amount. Without the governor's proposal, the state would still pay the full amount whether the explorer sold at a discount to a large producer or not.

Vice-Chair Gara clarified that his point had been that statute had been written so a small explorer and a large company like BP could negotiate where BP paid 50 cents on the dollar. He understood that the state would not get any benefit out of the arrangement. He wondered why the state was not given the same flexibility to negotiate a lower price if a company wanted to be paid immediately.

Ms. Pitney understood.

Mr. Steininger continued with slide 3 related to the Alaska Liquefied Natural Gas Pipeline project. A five-party agreement had recently been signed and interested natural gas buyers were coming to the table for the first time. The administration anticipated the project would create 12,000 jobs and \$2 billion in annual economic activity and a future revenue stream for the state. The governor's budget included the authority to accept third-party investor funds, but no additional state funds were committed to the project at present.

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Mr. Steininger moved to slide 4 and briefly addressed the proposed base capital budget. He characterized the capital budget as constrained and relayed it prioritized matching federal funds. The budget included housing, energy, maintenance, and key information technology investments. He turned to slide 5 and discussed the Alaska Economic Recovery Act. The act focused on investing in deferred maintenance and energy projects with an emphasis on projects that would get money out on the street quickly. The goal was to get Alaska's economy working again. The recovery act would commit \$800 million over three years, which included \$280 million in FY 19 for capital projects. The funding would be generated through a 1.5 percent wage tax, which would be capped at two times the Permanent Fund Dividend. The act would sunset in 2.5 years, at which point it would be reassessed.

Mr. Steininger advanced to slide 6 and provided detail on projects included in the Alaska Economic Recovery Act. The package primarily included deferred maintenance funding for the University, the K-12 Major Maintenance Grant Fund, and other state items. The package also included critical infrastructure repair projects, community needs, and the reinstatement of some road projects. The idea was to get Alaska working again and to get the economy back on track. The proposed revenue package that would accompany the recovery act was revenue neutral over three years. The first year included \$280 million in appropriations and \$160 million in revenue. The idea was to include shovel-ready projects. With cashflow on projects, they would be able to stay within the \$160 million in the first year as the projects got rolling.

Representative Wilson stated that the plan would tax people and she did not understand how that was revenue neutral.

Ms. Pitney surmised a better term was deficit-neutral. She detailed that the wage tax was the same tax the administration had proposed during special session except it was time limited and would sunset at the end of June 2021. The revenue from the 1.5 percent payroll tax was projected at \$800 million; the recovery act was contingent on a broad-based tax producing \$800 million. The act would require the revenue commitment in order to advance. By

investing in deferred maintenance, the contingent liability of state and public facilities would be addressed. She elaborated that deferred maintenance also employed local contractors. The construction industry had been hit particularly hard and it would require everyone pitching in to put the individuals back to work. In three years there were many potential construction jobs on the horizon, but up to that point if more construction companies and workers left the state would hinder the construction restart time in the future. She reiterated that the plan was deficit-neutral, and the expense would be covered by a directed source of revenue (i.e. payroll tax).

Representative Wilson asked what model the administration had used to determine that taxing people would enhance economic growth into the future. She reasoned that everyone would not be pitching in because not everyone worked. She highlighted retired people receiving income from other places as an example. She believed a small portion of the state's residents would participate in the tax.

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Ms. Pitney answered that many communities used the model for reinvesting in their facilities. She cited revenue bonds that increased community residents' property tax assessment. The idea for taxing for infrastructure investment was common. She acknowledged that it was not a perfect solution, but the tax had been proposed as a compromise solution during special session the past fall. The payroll tax had not been accepted, but there were many indications that tying a payroll tax to an investment or directing it towards something in particular, it became more palatable. She stressed that the state had been in recession longer than at any other point in Alaska's history. She surmised that the recession may not be as sharp as the one in 1988, but it had lasted longer. The administration wanted to put Alaskans back to work immediately to prepare for positive opportunities on the horizon. The administration believed there was sufficient commitment by Alaskans that a sunsetted payroll tax was a reasonable approach.

Representative Wilson remarked that the subject would come before the committee in the form of legislation. She would hold her questions until the legislation was heard by the committee.

Vice-Chair Gara agreed with Ms. Pitney that part of the recession was a result of no fiscal plan, which was damaging the state terribly. He found it hard to stomach that people earning less would have to carry a heavier burden than those earning more. He had been told the administration was trying to find a proposal that the other legislative body would accept. He underscored that due to the proposed wage cap, a person earning \$1 million would pay one-seventh the tax rate of someone earning \$20,000 who was struggling to get by. He stressed that everything did not have to hit poorer people harder than wealthy people. He did not buy the line that wealthier people were the job creators and the state could not ask them to contribute at the same rate.

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Representative Thompson remarked that the citizens of the state were skeptical about a temporary tax. He detailed that Alaskans felt it was a way to pass a tax that would end up being permanent and increasing. He was concerned about the proposal and believed there would be many reactions from state residents. He did not know many places that had a temporary tax that did not become permanent. He believed many questions would come forward throughout the process.

Mr. Steininger turned to slide 7 titled "Cost Avoidance - Efficiency." He relayed the administration had several initiatives it had been pursuing for cost avoidance. He detailed the administration was centralizing the Office of Information Technology in order to better leverage purchasing power as a single state organization rather than having each department negotiating for IT contracts. The centralization would also allow some central control over IT standards and would create efficiencies. The Shared Services Initiative had resulted in 10 percent savings in the first year; an additional 10 percent savings in FY 19 was projected. The Facilities Consolidation Initiative would manage all state facilities instead of managing them by department. For example, instead of having two electricians go out to different facilities in one town, there would be one electrician for a centralized facilities services division in order to generate efficiencies. A chart at the bottom of the slide showed projected savings for FY 19 through FY 21. He pointed out expected savings of

\$12 million in the Office of Information Technology in FY 21.

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Representative Guttenberg stated that the committee saw slides like slide 7 all of the time. He remarked the committee never saw line items showing the cost of delivering the state's broadband internet services. He noted that places without sufficient broadband could not do telemedicine, e-rate for schools, criminal justice, and other. He explained that broadband access could allow a person to be processed over the internet through a teleconference with a judge and would avoid sending a couple of troopers out to a rural area to bring someone in. He asked if there was anyone actually working on the issue; it was his impression the state had no policy dealing with the issue. He spoke about the efficiencies and costs that could be driven down through modern ways of delivering services in rural Alaska. He asked to hear from Commissioner Ridle on the state's plan to drive down costs and provide affordable, reliable broadband throughout Alaska.

Co-Chair Seaton requested additional information about savings [inaudible].

Mr. Steininger spoke to the primary drivers of cost in the state on slide 8. He elucidated that health care accounted for almost \$1.4 billion of state spending. Medicaid accounted for close to half the total. Other substantial areas were employer health plan contributions, worker's compensation, and the University health plan. Smaller amounts were associated with the Alaska Reinsurance Program and inmate/juvenile justice health care.

Representative Wilson asked if the contribution of \$30 million for the University health plan was in addition to the grant allocated in the state operating budget.

Ms. Pitney answered that the amount reflected an estimate of the general fund portion of the University's health contribution.

Representative Wilson had heard on the news earlier in the day that CHIP [Children's Health Insurance Program] had still not been funded; she assumed it was Denali KidCare.

She asked what happened if the program was no longer funded. She wondered if the state would pay for the program and what the cost would be.

Mr. Steininger replied that in FY 18 the effect to the state would be approximately \$7 million to \$7.5 million. The effect was a result in the drop in the Federal Medical Assistance Percentage (FMAP) from 88 percent for Denali KidCare to 50 percent. He elaborated that in FY 19 there would be a full year of the drop if CHIP was not reauthorized, which would result in a cost of \$14 million to \$15 million. The governor's proposed budget included two separate supplemental items for Medicaid - one broke out the cost to the state if CHIP was not reauthorized.

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Representative Wilson surmised that it would mean \$690 million for the Medicaid program and an additional \$14 million to \$15 million if the CHIP reauthorization did not occur. She estimated the state's cost for Medicaid alone would be around \$705 million.

Mr. Steininger answered in the affirmative. He added that OMB's FY 19 estimate assumed reauthorization of the CHIP program.

Representative Wilson commented on the high expense.

Mr. Steininger turned to slide 9 and addressed Medicaid enrollment growth. He directed attention to a chart at the bottom of the slide that showed unduplicated Medicaid enrollment with expansion shown in yellow [orange]. While expansion had grown since coming online in FY 15, there had also been growth in the regular Medicaid program of about 32,500 people. Slightly less than half the growth in Medicaid was related to non-expansion regular Medicaid growth. He referenced children in the CHIP program or disabled single parents as examples.

Mr. Steininger moved to slide 10 and discussed work the administration was doing to avoid the cost increases. He detailed that \$25.5 million would be saved through retiree payments through the Medicare Part-D Employee Group Waiver Plan (EGWP). Additionally, the administration had continued work on the individual market through HB 374 (the reinsurance program), which achieved success in keeping

health insurance premiums down. He briefly mentioned items for the health care authority that he had discussed earlier. The state covered health care for 340,000 people directly or indirectly.

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Mr. Steininger turned to slide 11 and detailed that the current trend showed a 5.2 percent increase in spending on health care, but the administration was setting a target to keep to inflation at 2.25 percent. The target left a gap that needed to be filled. He elaborated that EGWP covered a portion of the gap at \$51 million in FY 20 and \$25.5 million in FY 19. The administration projected \$10 million in savings from the health care authority activities in FY 20. As the economy recovers, the administration was hoping to see savings in Medicaid enrollment declines.

Mr. Steininger moved to slide 12 and relayed that state government employment was below 2002 levels. There were 3,000 fewer state government employees in November 2017 than at the peak in 2014. When developing the budget, OMB had reviewed any position that had been vacant for three months or longer. The administration was continuing to put pressure on state employee counts. He moved to a budget summary on slide 13, which included FY 18 management plan supplementals to acknowledge the enacted budget in FY 18 had underfunded things such as Medicaid and correctional health care. To see a true comparison between FY 18 and the FY 19 budgets it helped to include supplementals. As OMB had developed the budget, it considered supplementals in FY 18 and had tried to incorporate those into the FY 19 budget as well.

Vice-Chair Gara referenced loss of jobs in the public sector on slide 12. He asked if the figure included lost University jobs. Ms. Pitney answered that the figure included the University.

Mr. Steininger moved to slide 14 and provided a budget summary. The slide included the FY 19 capacity budget in addition to some items the administration had chosen to directly fund with appropriations out of the Constitutional Budget Reserve (CBR). The capacity budget included items that had more repercussions if not passed in a timely manner. He cited pink slips going out to teachers as an example of the type of items included in the capacity

budget. The structure allowed the passage of a capacity budget with a simple majority. The items funded by the CBR were no less important; it would be inconvenient for the items to not receive funding on time, but it would not be as disruptive.

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Co-Chair Seaton addressed slide 13. He spoke about looking at the FY 18 management plan and adding in FY 18 supplementals and comparing it to the proposed FY 19 budget. He asked how to keep from bulking up supplementals in order to show a good relationship to the proposed budget. He asked if it would be a problem the legislature could anticipate accelerating because it showed the administration had not increased the budget much.

Ms. Pitney addressed why the administration believed supplementals were a key part of expressing the spend total. She explained there had been areas of known underfunding that existed in the prior year. The administration believed there should be scrutiny on supplementals as there should be on all spending. She believed supplementals should be accounted for and should be part of the comparison and trend. She recalled that during special session Representative Wilson had asked what the picture looked like when including the "full view." Since Medicaid expansion in FY 15, the legislative budget and the governor's budget had not accounted for the federal increase for Medicaid. Part of the transparency process should be to include the information. In FY 17 there had been a supplemental that allowed open-ended authority to accept all federal funds for Medicaid; in FY 18 the amount had not been included in the overall budget. The administration believed the information needed to be included. She stated that from an industry standpoint the only place with jobs in Alaska's private economy was health care during the recession; it was offsetting job loss in other areas, but it was all federally funded.

Ms. Pitney continued that all of the spending needed to be on the books. Additionally, the reconciliation between the designated general funds (DGF) and UGF needed to be included in the view. She explained that when looking at a traditional report from the Legislative Finance Division (LFD) or the OMB budget system, because of the direct appropriation of CBR, it showed up as "other funds." Slide

13 corrected for that and classified it as UGF spend. The goal was to get all of the spending out on the table. She believed Co-Chair Seaton's question had been whether showing supplementals [in the budget] would encourage supplementals. She did not believe so. She reasoned that ignoring supplementals meant leaving the focus off of them. She stated, "a spend is a spend is a spend."

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Co-Chair Seaton responded that it seemed that the supplementals from one year were built into the base for the next year and showed a very slight difference between the two budgets. If supplementals came in after that time, they would not be shown until the following year. He discussed that a budget could be bigger than the prior year's without showing an increase. He wanted members to look at the issue carefully.

Vice-Chair Gara referred to slide 13. He remarked it was almost impossible to compare budgets because of situations like adding the supplementals to a prior year budget and comparing that budget to one that did not yet have supplementals. The bulk of the supplementals for FY 18 were the incorrect estimate of how many people would apply and use Medicaid. He asked for verification that the amount was about \$100 million.

Ms. Pitney responded that the \$100 million was included and additional funds for the Alaska Marine Highway System (AMHS).

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Representative Wilson asked how much UGF money went to municipalities for schools, revenue sharing, and other.

Ms. Pitney scrolled to slide 25. Of the \$10.6 billion all funds, 52 percent went directly out the door. She moved to slide 26 and listed items the funding went to including Medicaid payments to providers, K-12 schools, retirement payments, school debt reimbursement, oil and gas tax credits, Permanent Fund Dividends, and other. She noted that mostly the funds used were general funds.

Representative Wilson was uncertain how oil and gas tax credits fit in. She was talking about the Base Student

Allocation and Public Employees' Retirement System (PERS) reimbursement that someone else would have to pick up. She surmised that items such as foster care and public assistance went out to people, but she was trying to make a split between what individuals received versus what went to boroughs and cities. She wanted true numbers as opposed to percentages.

Mr. Steininger explained that slides 15, 16, and 17 addressed additional detail on categories of budget changes. The largest increase to the budget was for Medicaid. The slides showed the total difference from management plan, not merely the difference from the supplementals.

Ms. Pitney explained that the slides had been included as a reference to show all of the moving parts. The slides showed fund changes, mental health changes, one-time items, statewide and nonagency changes, and supplementals. The pages replaced hundreds of change records and provided a clean snapshot of the detailed changes.

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Mr. Steininger turned to slide 18 that showed a reconciliation between the LFD calculated deficit and the OMB calculated deficit. The LFD calculated deficit was \$671.7 million, and OMB calculated a \$477.4 million deficit. He detailed that LFD did not include the savings for the EGWP program (the board approved motion did not include actuarial estimates), but OMB included the savings. Additionally, LFD assumed a Statutory Budget Reserve (SBR) draw for the economic recovery plan cash flow difference. The governor's budget included \$18 million in adjustments to dividends. There was some inadvertent double counting on the revenue from the Alaska Capital Income Fund and a couple of other adjustments. Adjusting for EGWP and the economic recovery plan, OMB estimated the deficit at about \$525 million for FY 19.

Ms. Pitney returned to slide 14 and discussed the direct appropriation to retirement. She explained there were state "on-behalf" payments to PERS and Teachers' Retirement System (TRS) for a portion of the unfunded liability. The year-end 2016 actuarial had been \$299 million for PERS and TRS combined. The Alaska Retirement Management Board (ARMB) had accepted a resolution that the on-behalf payments

should be slightly over \$263 million, recognizing there had been significant increases in market return in FY 17. Subsequently ARMB had accepted the resolution to enter into the employee group waiver program with an estimated cost savings of \$25 million, which was applied to the retirement payment. Although the retirement payment was not the 2016 actuarial, it was the entire amount ARMB expected. The retirement on-behalf payments were scheduled out annually to 2039. The difference between the \$299 million and the governor's request for PERS and TRS on-behalf payments met the actuarial required contribution by ARMB. Therefore, OMB believed it fully funded the retirement on-behalf payment. She noted that LFD believed the amount should be funded at the old actuarial rate.

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Mr. Steininger moved to slide 19 showing a budget reconciliation to fall estimates. There were some slight differences between the fall estimates and the proposed FY 19 budget. Primarily, in the Medicaid program, OMB had estimated flat growth from FY 17; however, OMB had revised that estimate to include some enrollment growth. He noted that AMHS had remained the same. There was a large difference in the exploration credits fall estimate of \$118 million and the governor's proposed budget due to an exploration credit proposal that would result in a decrease of \$30 million. There was a total difference between the fall estimate and the proposed budget of \$157 million.

Mr. Steininger advanced to slide 20 and spoke about increasing transparency in state spending; to correct for different budget strategies and show a more accurate trend. He listed various strategies including the reclassification of unrestricted revenues to designated or other, offsets of general fund spending, supplemental items, reappropriations, and other. He detailed that OMB was working on developing a framework to present the numbers in a way that controlled for some of the strategies. He communicated that OMB was not set in stone on the framework it had developed; it wanted to work with the Legislative Budget and Audit Committee to codify and come to a consensus on what rules to apply.

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Mr. Steininger addressed slide 21 related to budget trends. The agency operating budgets had increased by less than 1 percent from FY 18 after accounting for supplementals. The increase was primarily due to investment in public safety, increased Medicaid formula costs, and higher than anticipated prison populations. Statewide items had declined 12.6 percent, driven by EGWP and exploration credit financing. Total operating and capital had been reduced by 3.1 percent. The budget was down by 1.7 percent or \$93.1 million when the dividend was factored in.

Mr. Steininger turned to a chart on slide 22 showing the UGF and transparent budget comparison for operating and capital. The chart made adjustments for supplemental items and reappropriations - UGF reclassified as DGF spending. As the budget had declined, the difference between the understatement of the budget had grown. It was important to change the framework in order to show the information as the UGF spend continued to be understated; finding a way to have transparent reporting on total state spending was important.

Mr. Steininger stated that slide 23 gave more detail on the difference between FY 15, FY 18, and FY 19 in transparent budget dollars. He pointed to the 1.7 percent decrease in the "Total Budget with Dividend" row.

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Mr. Steininger spoke about expenditure reductions by department in transparent dollars on slide 24. The Department of Commerce, Community and Economic Development had the highest percentage reduction. He noted that part of the reduction included shifting tourism and seafood marketing from state support to industry support.

Mr. Steininger moved to budget reform on slide 28 and addressed tackling the consequences of an untimely budget. He explained that an untimely budget resulted in teachers and employees receiving layoff notices, and AMHS was unable to publish their schedules on time resulting in foregone revenue and inconvenience to travelers. Additionally, agency staff within the departments spent a significant portion of their time planning for a potential government shutdown rather than focusing on providing services to Alaskans.

Mr. Steininger addressed the repercussions for failure to submit or pass a budget in a timely manner. Under budget reform legislation, if the governor failed to submit the budget by December 15 he/she would forego salary and per diem. Likewise, if the legislature failed to pass a budget by the 91st legislative day, legislators' salaries would be withheld and per diem would be forfeited. The legislation would shift to biennial budgeting, which would allow a two-year budget cycle. Two budgets would be passed in the first year of the two-year cycle. During the second session of the two-year cycle there would be a supplemental true-up to make small adjustments to the second budget. Biennial budgeting would allow more time to tackle policy issues, would avoid lengthy budget negotiations each year, and would give more time to plan ahead for the second year.

Representative Wilson asked how it was fair to compare the governor putting a budget out with 60 legislators putting a budget out.

Ms. Pitney answered that it had been modeled after an initiative in California. She elaborated that the California legislature had been late passing a budget 25 out of 30 years, which had caused the same disruption in state operations that had been seen in Alaska. She stated a pink slip was one level of disruption in terms of impact on morale. However, she pointed out that when there had been discussion on whether or not a commercial fishing opening would occur, it had impacted whether or not a fish processing plant would deploy its staff and open. There were many more repercussions. She recalled discussions on what to do with Permanent Fund assets if the government shut down. She explained that California had passed a biennial budgeting provision. The first year after passage the legislature had been 12 days late and on time ever since. She understood the point that the governor was one person and the legislature had 60 people. The governor's point was that if he expected it of the legislature, he should adhere to the same expectation himself. The point was to stop the disruption that had existed annually in recent years and to achieve a timely budget.

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Representative Wilson did not support comparing Alaska to California and its problems. She believed the comparison was unfair. She noted that the states were very different.

She elaborated that oil was one of Alaska's primary revenue sources. She commented on Alaska's local government. She was concerned that getting the budget done quickly seemed to be more important than doing it right and ensuring sustainability. She thought it seemed like a bullying attempt. She surmised the unintended consequences could be that the only people who could come down and afford to be a legislator would be wealthy enough that the pay did not matter. She believed it sounded good as a soundbite, but she wanted to do the job right.

Representative Pruitt referenced the statement on slide 28 "if the governor fails to submit the budget by December 15th." He asked if the provision would only apply to the governor. Alternatively, he wondered if it would include commissioners, deputy commissioners, administrative services directors, legislative liaisons, and other.

Ms. Pitney replied that the other individuals were not included.

Representative Pruitt stated that his child could do the job of getting a budget out by December 15. His concern was about when legislators requested information from an administration and did not get it. He thought the governor could put the legislature in a stranglehold if information was withheld that prevented legislators from passing a budget. He believed December 15th was disingenuous. He referred to 91 days in the legislature and stated that the governor, commissioners, deputy commissioners, administrative services directors, legislative liaisons, and other were also included. He thought there needed to be a conversation.

Mr. Steininger moved to slide 29 and addressed revenue for operating and base capital. The administration's existing revenue expectation was \$2 billion. The governor was proposing a compromise Permanent Fund Protection Act - 30 percent would go to the dividend and 70 percent would go to the government; the 70 percent was an additional \$2 billion. Other revenues totaled \$40 billion. The administration estimated \$477.4 million from the CBR/SBR, adjusted to \$525 million per its reconciliation with LFD. He detailed that narrowing the gap would reduce uncertainty. The Alaska Economic Recovery Act would help address the recession. He elaborated that the plan would require reassessment when the temporary tax expired.

Savings were anticipated to be depleted by FY 25 based on current trends. He concluded there would be a reassessment of oil price/production levels, the success of efficiencies, and market returns in FY 22 when the wage tax and the economic recovery act expired.

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Vice-Chair Gara asked about the \$2 billion related to the compromise Permanent Fund Protection Act [slide 29]. He asked if it was \$2 billion for public services and a dividend on top of that amount. He asked for the projected dividend amount in the proposed budget. He asked if it included a 5.25 percent draw or new actuarial recommendations that were closer to 4 percent.

Ms. Pitney responded that the budget took SB 26 [2017 legislation] provisions passed by the House and the provisions passed by the Senate and coming up with a compromise. The budget used the 5.25 percent over a lagging five-year average, which turned out to be in the range of about 4.5 percent on the current value. One of the major differences between the two plans was the size of the dividend. The House plan designated 33 percent of the draw to the dividend, while the Senate designated 25 percent of the draw. The governor's budget proposed a compromise of 30 percent.

Vice-Chair Gara asked if the proposed dividend was about \$1,200. Ms. Pitney answered that the proposed dividend was \$1,200, which would grow to \$1,500 over ten years based on projections.

Mr. Steininger moved to a chart showing revenue sensitivity based on price per barrel of oil on (slide 30). The chart showed a breakeven point at \$90 per barrel (without SB 26 or a similar plan). He highlighted the Senate plan, compromise, and House plan respectively:

- 75/25 Split - \$2.1 billion for government/Budget Balances just above \$65/bbl
- 70/30 Split - \$2.0 billion for government/Budget Balances just under \$70/bbl
- 67/33 Split - \$1.9 billion for government/Budget Balances at \$70/bbl

Mr. Steininger used the ANS West Coast price of \$69.02 per barrel as of 1/9/17 [1/9/18] as a point of reference. He noted that the numbers were based off of a year-long average, meaning the price would have to average around \$84 per barrel for the rest of the year in order to hit the average of just under \$70 per barrel.

Ms. Pitney added that the forecast was \$56 per barrel for FY 18 and \$57 per barrel for FY 19. The year-long average was very close to the FY 18 number. She noted that if the price remained at \$70 per barrel for the rest of the year, the state may inch up \$40 million to \$45 million or so.

Mr. Steininger turned to slide 31 and discussed a ten-year strategy. The table showed a ten-year projection. He pointed to the reassessment time period in 2022. In order to maintain a [minimum] balance of \$1 billion [in the CBR] it would be necessary to bring in an additional \$330 million to \$350 million beginning in 2023. It would be a good time to reassess the state revenue level once the wage tax expired and a review of what had transpired [since its implementation] took place.

Ms. Pitney answered that the ten-year plan included all ten years, but the slide represented an effort to fit everything on one page. She spoke to the break between 2024 and 2027 on the slide [years 2025 through 2026 were not shown]. She explained that with the growth of the Permanent Fund, the budget would begin to balance in 2026 and 2027 without additional revenue. The plan also assumed the state would receive revenue from the Alaska Liquid Natural Gas (AKLNG) project. She detailed it was the state's share of the production tax. The ten-year plan showed beginning to restore the CBR at the end of that timeframe. She referenced the \$1 billion CBR balance [in 2023 and 2024] and noted it was the lowest level the balance should go.

Ms. Pitney added that the administration did not want the balance to drop below \$2 billion, which she had testified to when discussing a wage tax during special session. She was not excited about going below \$2 billion, but if the balance dropped below \$1 billion there was risk of going into Permanent Fund earnings in an ad hoc manner. The administration's interest in the Permanent Fund Protection Act was only using earnings from the fund on a very structured basis that preserved the real value of the fund, so the earning power of the fund was the same in the future

as it was at present. The goal was to maintain the earning power across generations. The House and Senate versions [of SB 26] dropped the 5.25 percent to 5 percent in the near-term. The CBR and the SBR were the state's savings accounts and gave the state the ability to address any out of the ordinary problems without using the Permanent Fund Earnings Reserve Account on an ad hoc basis.

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Co-Chair Seaton asked for clarification. He wondered if the plan included a continuous 5.25 percent draw [from the Permanent Fund].

Ms. Pitney replied that the draw would drop. She detailed that on the Senate schedule the draw would drop from 5.25 percent after two years to 5 percent on a lagging five-year average.

Representative Guttenberg asked if budget projections included a capital budget, major maintenance, new ferries, and other things that had been deferred for years.

Ms. Pitney answered that the budget projection included known changes in debt service. The budget assumed the sunset provision on school debt reimbursement would be extended. Additionally, it assumed a \$150 million capital budget and that any time catchup or an infrastructure project took place the state would pay as it went like it had done on the deferred maintenance package. She stated if they did another deferred maintenance package shortly thereafter, it would come with its own funding source. All other budget items were inflation only.

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Mr. Steininger spoke to a bar chart on diversifying revenues on slide 32. The first bar represented the past Alaska experience where 85 percent of its revenue came from oil and gas and 15 percent came from other sources. The second bar showed the present where 30 percent of the state's revenue came from oil and gas revenue, 13 percent from non-oil and gas revenue, and 57 percent savings. The proposal for "tomorrow" was 44 percent coming from the Permanent Fund, 13 percent from savings, 11 percent from non-oil and gas revenue, and 26 percent oil and gas revenue. Going into the future as revenue streams from

AKLNG came in, the revenue would replace money coming from savings.

Ms. Pitney added there was an increase in the "non-oil and gas revenue" component, which could come from a broad-based tax, or something like a user fee assessment.

Mr. Steininger concluded with a bar chart on slide 33 that added the Permanent Fund Dividend to each of the bars.

3:08:20 PM

Representative Wilson pointed to slide 9 and asked if the Medicaid figures only included adults. She wanted to know whether Denali KidCare was a separate number of individuals.

Mr. Steininger answered that the information included CHIP; the data reflected all unduplicated Medicaid enrollees.

Ms. Pitney highlighted a scenario where an individual was only on Medicaid one month out of a year. That person would count as one in the count [shown on slide 9]. The data on slide 9 counted every person who had benefitted from the Medicaid program in a given year. Another common count on Medicaid was the average monthly enrollment; for a particular time that number was slightly lower. She added that CHIP was Medicaid expansion.

Representative Wilson asked if 33 percent of Alaskans were on Medicaid, Medicaid expansion, or Denali KidCare. Mr. Steininger replied in the affirmative.

Representative Wilson stated there was a big issue they needed to discuss.

Representative Guttenberg pointed to slide 11 and asked about health care authority savings of \$10 million in FY 20 and \$20 million in FY 21. He asked for additional detail later on.

Ms. Pitney nodded in agreement.

Vice-Chair Gara stated the presentation included a slide showing that FY 19 would be balanced if a certain amount was used from the Permanent Fund, the governor's tax proposal was adopted, and perhaps a fuel tax proposal was

adopted. The legislature had always been told that it took about one year to implement a statewide tax. He asked for an explanation.

Ms. Pitney answered that the governor's plan required use of the Permanent Fund in a structured, sustainable way. The plan required around \$500 million in continued use of the CBR in the near-term, which was declining slightly. By 2026 the CBR would increase. The governor's proposed broad-based tax was one-to-one connected with the economic recovery plan. The proposal was deficit-neutral and would appropriate funds from a 1.5 percent wage tax to infrastructure projects to put local contractors to work and reduce the state's liability on public facilities. She highlighted that the committee would hear from LFD that the legislature would be appropriating \$280 million, but the first year of revenue was only \$160 million. The pace of spend on capital projects would not outpace the revenue collection on the tax. The tax would take effect on January 1 [2019] and would end on June 30, 2021.

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Representative Ortiz spoke to the revenue projections of \$800 million over three years [slide 5]. He asked if it accounted for the cost of implementing the program. Ms. Pitney replied in the affirmative.

Co-Chair Seaton referenced an earlier question by Representative Wilson on Medicaid. He asked to receive a chart of percentages and actual amounts for each category.

Ms. Pitney agreed. She relayed that LFD was working on putting information together on health care costs. Additionally, Caroline Shultz in OMB and others were working on the executive branch for health care cost. The current presentation only showed a snippet of the health care cost. Others [from Department of Health and Social Services] would address the issue as well. She stressed the value of looking at the state's health care costs holistically. The topic would be a constant conversation for the foreseeable future.

Co-Chair Seaton wanted to ensure that when Department of Health and Social Services presented to the committee they had a list of the questions.

Co-Chair Seaton reviewed the schedule for the following day. He relayed that subcommittee lists had been posted online. He detailed that many subcommittee meetings would be held in the evenings to avoid interference with standing committee meetings. He shared that 360 North would be airing all subcommittee meetings on television.

Representative Thompson stated that he had been informed that the legislative television would not be airing in Fairbanks, which was unfortunate. He noted the conversation was continuing.

Co-Chair Seaton continued to discuss logistics about future meetings and the schedule.

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ADJOURNMENT

3:18:28 PM

The meeting was adjourned at 3:18 p.m.