

SENATE FINANCE COMMITTEE  
February 7, 2018  
9:02 a.m.

[9:02:42 AM](#)

CALL TO ORDER

Co-Chair MacKinnon called the Senate Finance Committee meeting to order at 9:02 a.m.

MEMBERS PRESENT

Senator Lyman Hoffman, Co-Chair  
Senator Anna MacKinnon, Co-Chair  
Senator Click Bishop, Vice-Chair  
Senator Peter Micciche  
Senator Donny Olson  
Senator Gary Stevens  
Senator Natasha von Imhof

MEMBERS ABSENT

None

ALSO PRESENT

Deven Mitchell, Debt Manager, Department of Revenue

SUMMARY

^PRESENTATION: STATE DEBT ANALYSIS

[9:03:29 AM](#)

DEVEN MITCHELL, DEBT MANAGER, DEPARTMENT OF REVENUE, discussed the presentation, "2018 Credit Review and State Debt Summary" (copy on file). He shared that the presentation had become an annual one that was provided to the state to facilitate the discussion on outstanding debt and the state's potential to issue debt.

[9:04:18 AM](#)

Mr. Mitchell addressed Slide 2, "Debt Affordability Analysis":

- Annual analysis required by AS 37.07.045 to be delivered by January 31
- Discusses credit ratings current levels and history
- Relies upon debt ratios for issued debt and debt that the state supports at the local level
- Identifies currently authorized, but unissued debt
- Establishes refinancing parameters
- Determines a long-term debt capacity at current rating level
- Discusses, but doesn't define a capacity for short term debt

-Revenue Anticipation Notes are limited by statutory definition and would not be included in capacity

[9:06:07 AM](#)

Mr. Mitchell highlighted Slides 3 and 4, "January 2017 Debt Affordability Analysis" and January 2018 Debt Affordability Analysis." The slides offered a chart that listed the Fall 2106 Unrestricted General Fund Revenue(UGF), Percentage of UGF Committed to State Debt (5 percent cap), Percentage of UGF Committed to Total State Supported Debt (8 percent cap), Percentage of UGF Committed to Expected Payment on Behalf of PERS/TRS, and Percentage of UGF Committed to State Debt or PERS/TRS, through fiscal years 2017 to 2026. Slide 4 contained the same analysis beginning 2018. He noted that the primary metric that was used for determining capacity was the percentage of UGF that the equated to the debt. He said that there was a 5 percent target for general obligation bonds and direct state obligations, the target was 8 percent for the more "lenient" obligations that were subject to appropriation. He shared that the percentage of payment for the PERS/TRS had been added in 2017, due to the significance of the percentage size. He highlighted that in 2017 the state was above target at 7.5 percent, which diminished to 3.75 percent by 2026, primarily to declining outstanding bond balance and associated debt service. He pointed out that the 8 percent target for 2017 was 15.6,

declining to 5.9 in 2026. He PERS/TRS percentage increased from 14.9 in 2017, to 19.3 in 2026. He relayed that the numbers for 2018 were better, due primarily to an increased projection in revenue in the Revenue Sources Book of approximately \$600 million. He said that the outstanding debt had remained static from 2017 to 2018. He related that the payment for PERS/TRS remained a substantial payment through 2026.

[9:09:37 AM](#)

Co-Chair MacKinnon requested comment on the governor's proposal to issue debt on the tax credit liability.

Mr. Mitchell replied that he had slide further in the deck that would speak to the question. He agreed that there would be some impact on capacity because of the issuance of debt to refinance the credits. He did not believe that the payment would be dollar for dollar because it was an existing liability that held an expectation of payment over an already defined period.

[9:10:53 AM](#)

Co-Chair MacKinnon stated that the governor had short the calculation for the payment on PERS/TRS in the proposed Operating Budget. She wondered how the sort funding would affect the analysis percentages.

Mr. Mitchell responded that he could not speak to why a lower number had been incorporated in to the proposed budget. He said that the numbers that had been included in the analysis were based on the actuarial analysis, payments otherwise due based on the percentages of payroll that had been predicted by the actuary based on the amortization of the unfunded liability.

[9:12:00 AM](#)

Co-Chair MacKinnon wondered what would happen if the legislature failed to appropriate the actuarial calculation.

Mr. Mitchell explained that not funding the actuarially determined contribution rate would reflect negatively on the state's scorecard from rating agencies. He felt that

the issue came down to a policy decision on the part of the legislature.

[9:12:59 AM](#)

Co-Chair MacKinnon advocated for the required payment recommended by the actuaries.

[9:13:16 AM](#)

Senator Micciche understood that the report focused on actuals and used the forecasted revenue set out in the Revenue Source Book.

Mr. Mitchell replied that the percentages in the report were based on the Revenue Source Book.

[9:14:02 AM](#)

Senator Micciche wondered whether the division embraced the energy prices projected by the administration that estimated that oil prices would drop \$20 per barrel across the board into the future.

Mr. Mitchell replied that the Revenue Sources Book was a product of the tax division, which was not under his purview. He said that ranges of projected price were in the sources book and a point within the range was generally chosen for the price predictions. He observed that oil as a commodity was inherently volatile and price prediction was very difficult.

[9:15:29 AM](#)

Vice-Chair Bishop echoed Co-Chair MacKinnon's support for the actuaries recommended pension plan funding. He warned that negative things happened to debt obligation when pensions went unfunded and cited the State of Illinois as an example.

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Co-Chair MacKinnon understood that the administration could put forward new numbers for PERS/TRS, but without the new numbers she felt that it was necessary to advocate for funding what the actuaries suggested was necessary for the pension debt.

[9:16:55 AM](#)

Mr. Mitchell addressed Slide 5, "Debt Capacity":

- Projected annual revenue increase of approximately \$600 million in FY 2018 vs FY 2017
- Ratios are still at or above capacity in both categories each of the next two years
- Increased capacity of approximately \$150 to \$200 million to total capacity of \$3-400 million
- Creating or using existing "restricted" revenues to fund state government will increase capacity.
- Historically, PF earnings have been classified as restricted by custom rather than unrestricted
- A shift of this revenue stream to unrestricted would have a significant impact
- For every \$100 million of recurring revenue that is added at this point we expect a current market increase in long term debt capacity of \$60-\$70 million

[9:19:19 AM](#)

Mr. Mitchell looked at Slide 7, "State Debt Obligation Process":

- All Forms of State Debt are Authorized First by law
  - May be a one-time issuance amount or a not-to-exceed issuance limit in statute
  - General obligation bonds must then also be approved by a majority of voters
- All State Debt must be structured and authorized by the State Bond Committee
  - Includes general obligation bonds, subject to appropriation issues, and state revenue bonds

- The State Bond Committee determines method and timing of debt issues to best utilize the state's credit and debt capacity while meeting the authorized projects cash flow needs

- The State has established other debt obligations

-Reimbursement Programs

- The School Debt Reimbursement Program or HB 528 reimbursement
  - Communities issue bonds and the State agrees to reimburse at a certain level
  - Not currently authorized for new debt and periodically partially funded

-Retirement Systems

- Unfunded actuarially assumed liability (UAAL) for defined benefit employees is guaranteed by the Constitution
- Annual payments on the UAAL of other employers is reflected as State debt in the CAFR
- Some flexibility in how payments are made

[9:21:33 AM](#)

Mr. Mitchell highlighted Slides 8 and 9, "Total Debt in Alaska at June 30, 2017." The page was lifted directly from the 2018 Alaska Public Debt book and ran through all categories of obligations that existed in through the state and its political subdivisions. He noted that there were 10 categories of debt, some of which were direct obligations of the state, and were layered on the table from highest to lowest priority of commitment to the state. General Obligation Bonds were the highest priority at \$776.8 million outstanding as of June 30, 2017. He discussed the details of the various types of debt.

[9:25:08 AM](#)

Co-Chair MacKinnon announced that Mike Barnhill, Deputy Commissioner, Department of Revenue and Ken Alper, Director, Tax Division, Department of Revenue were available in the gallery for backup.

[9:25:30 AM](#)

Co-Chair MacKinnon referred to Slide 8, she asked whether the state debt included unissued bonds.

Mr. Mitchell replied that it reflected outstanding debt. He said that the Alaska Public Debt Book contained projections of the debt outstanding on the School Debt Reimbursement Program from June 30 of the year of publication. He explained that the number could fluctuate based on experience after June 30th.

[9:26:26 AM](#)

Co-Chair MacKinnon returned to the issue of actuary payments on the unfunded pension liability. She understood that the numbers the division had used were from June 30, 2017 and that the administration could now have new assumptions for evaluation.

Mr. Mitchell replied in the affirmative.

[9:27:01 AM](#)

Senator Micciche queried Mr. Mitchell's thoughts on revenue versus debt and where Alaska measured in comparison to other states.

Mr. Mitchell replied that on a per capita basis, the state had sizable obligations relative to the population. He relayed that on a monetary basis, Alaska had obligations that were well within the realm of acceptable levels. He thought that the unfunded liability associated with the retirement system was a challenge and represented the state's largest liability. He said that when compared to other states, Alaska fell in the middle of the scale; not the best and not the worst. He noted that the state had been accounting for other post-employment benefits and had a fairly defined picture of the debt. He added that the state had also had opportunity to transfer funds into the trust, which had benefitted the funding of the trust.

[9:29:28 AM](#)

Mr. Mitchell highlighted Slide 11, "Current General Fund Annual Payment Obligation":

- GF Payment peaked in 2018 at \$225.2 million
- Declining payment in every year (50 percent of peak in 2029)
- PERS/TRS special funding payments grow every year
- PERS/TRS special funding is many times all other state commitments
- Existing Authorizations for \$300 million for Knik Arm Crossing, \$110 GO bonds, \$5 billion POB Corporation

He pointed out to the committee that the lower graph on the slide illustrated the retirement debt and made all the other state debt look relatively insignificant. He shared that the debt would grow into the future under the current methodology. He stressed that the debt was affordable, and the state had capacity otherwise within the payment structure, but was a liability that leadership needed to be aware of and plan for.

[9:30:24 AM](#)

Co-Chair MacKinnon interjected that the refinancing option had extended the debt further, the 22 percent that was capped from municipalities, had lengthened the shared burden. She shared that the payment was currently over \$500 million and could rise to approximately \$700 million. She \$3 billion cash infusion had brought the payments down from \$1 billion down to \$500 million.

[9:31:18 AM](#)

Vice-Chair Bishop commented that there should be a future discussion of a termination study on dropping the payment percentage for municipalities.

[9:31:36 AM](#)

Co-Chair MacKinnon retorted that municipalities would surely be interested in termination studies to reduce their liability to the trust; however, the state would still be responsible for the remaining payments.

[9:32:01 AM](#)

Mr. Mitchell observed that striking a balance was challenging; any choice that the state made in relation to how much it paid did not negate the requirement that a payment be made - someone else would have to pay and it would likely be municipalities.

[9:32:30 AM](#)

Vice-Chair Bishop pointed out that the debt was not so bad when compared to that of General Electric in Illinois.

[9:32:55 AM](#)

Co-Chair MacKinnon added that pension liability in America was significant. She believed that the cash infusion had been helpful and that municipalities had been protected by the 22 percent cap. She said that 60 percent of the PERS liability was the states responsibility, while 40 percent was the municipalities and other organizations using the system.

Mr. Mitchell replied that the percentages were generally accurate.

[9:33:54 AM](#)

Mr. Mitchell looked at Slide 10, "State Debt Obligations Outstanding." The slide illustrated the state's General Fund paid debt and total principal outstanding in millions from 2000 to 2036:

Annual Position as of June 30

Balance outstanding peaked in 2016 at \$1,919.9 million

Declining principal balances in every year (50 percent repaid by 2026)

\$110 million of unissued general obligation bond authority

Mr. Mitchell relayed that the decade of the 90s had seen revenue suppression, flat \$2.3 billion budgets, which had put a moratorium on School Debt Reimbursement program. He noted that the outstanding debt hit its peak in 2016, at approximately \$2 billion in total principal outstanding. He highlighted that the growth had occurred primarily in state general obligation bonds for transportation projects and education projects. He pointed out to the committee that the outstanding balance was predicted to decline every year forward from 2018. He felt that the issuance of additional debt in the future was a possibility.

[9:35:53 AM](#)

Co-Chair MacKinnon said that the legislature had placed the moratorium on School Debt Reimbursement, which she understood was a struggle for municipalities, but thought had been a good way to control the state's mounting debt.

[9:36:50 AM](#)

Senator von Imhof wondered how the graph on Slide 10 would be affected once the School Debt Reimbursement moratorium expired.

Mr. Mitchell replied that it would be expected that, after a period of not allowing participation, if there were an open authorization there would be some level of debt issued related to the pent-up demand. He shared that at certain periods in time in the past the legislature would have limited authorization for participation in the program and would craftily draft legislation that ranked eligibility by student body population - resulting in able participation by only one school district.

[9:38:39 AM](#)

Senator von Imhof surmised that those estimates could change depending on how the state behaved financially in the future.

[9:38:46 AM](#)

Senator von Imhof spoke to spending limits. She thought that if a spending cap had been in place in 2006 to 2014, approximately \$18 million would currently be available to pay down the debt. She mused on what could have been done differently in the past.

[9:39:46 AM](#)

Senator Micciche thought that it was important the people realize that school debt reimbursement was approximately half of the outstanding debt reflected on Slide 10. He queried Mr. Mitchell's thoughts on whether the state was doing the best it could managing the PERS/TRS debt. He wondered whether there could be a better management system for the outstanding liability.

Mr. Mitchell replied that the issue was complex and difficult. He said that he did not have solutions to the problem. He thought that there were alternatives that existed to the current payment methodology. He thought that paying immediately, rather than an "as-you-go" method would be most beneficial.

[9:42:16 AM](#)

Senator von Imhof added that it made more sense to spend now, rather than later, because of volatility in the stock market.

[9:43:00 AM](#)

Co-Chair MacKinnon referred to Slide 10 and clarified that the slide was not a reflection of not how the state behaved, but how municipalities behaved, concerning the largest component of debt. She said that municipalities indebted the state without checking to see if the state had the ability to pay the debt. She hoped that the moratorium would be helpful in the matter and that municipalities would be indebting themselves more, and the state less once the moratorium was lifted.

Mr. Mitchell said that if the program were to be renewed it would be beneficial to consider revamping it so that the state provided grants to local districts, that districts could match however they chose. He shared that occasionally districts would have a surplus and would pay cash for their portion of the debt. He stated that that could not happen

under the current program but had to borrow money for at least 10 years to participate in the program. He thought that this would give more flexibility to municipalities because they would not longer have to worry whether the state would appropriate for the program.

[9:46:04 AM](#)

Co-Chair Hoffman thought that the state should be addressing the municipalities ability to refinance the debt initiated at a 70/30 split, resulting in the state paying a higher percentage after refinancing.

Mr. Mitchell responded that the payment should be pro-rata applied whenever there was refinancing.

[9:46:44 AM](#)

Co-Chair Hoffman requested that the division research his question and get back to the committee.

[9:47:20 AM](#)

Co-Chair MacKinnon understood that if a municipality had a higher interest rate on their debt, it would be up to that municipality whether to refinance. She noted that there was nothing in state statute that required municipalities that are carrying debt to take advantage of lower interest rates.

Co-Chair MacKinnon referred to Senator Micciche's comments about what could be done, in a structured way, to help reduce the state's debt. She shared that the administration had proposed using pension obligation bonds, which was a tool that existed in state statute. She relayed that the legislature had been uncomfortable with the idea due to the volatility in the stock market.

[9:49:03 AM](#)

Co-Chair MacKinnon lamented that the committee would not likely finish the presentation due to time constraints. She asked Mr. Mitchell if he would be able to return the following Monday.

Mr. Mitchell replied in the affirmative.

[9:49:22 AM](#)

Mr. Mitchell addressed Slide 12, "Existing State Short Term Debt Obligation Alternatives":

- Bond Anticipation Notes (AS 37.15.300-390)
  - May be used when long term debt is authorized by law
  - While short term, it is expected to be a precursor of long term debt
  - May be used to avoid negative carry in construction funds, better match long-lived projects and their financing, or as an additional budget management tool
  - Directly impacts long term debt affordability
- Revenue Anticipation Notes (AS 43.08.010)
  - May borrow money when it becomes necessary in order to meet appropriations for any fiscal year in anticipation of the collection of the revenues for that year
  - All notes and interest thereon shall be paid from revenue by the end of the fiscal year next succeeding the year in which the notes were issued
  - May be tax-exempt if a bona fide revenue deficit occurs during the fiscal year
    - Earnings of the Permanent Fund and other available fund earnings, will need to be included in determining if a revenue deficit occurs
  - The State has not used since the late 1960's

[9:52:45 AM](#)

Senator von Imhof wondered whether the second to last bullet relating to earning of the permanent fund was dictated by federal law.

Mr. Mitchell replied in the affirmative. He furthered that it was purpose was for tax exemptions. Taxable securities could be issued that would not need to meet the same requirements.

[9:53:05 AM](#)

Senator von Imhof queried the difference in rate.

Mr. Mitchell replied that the difference in rate was currently fairly modest. He explained that if it were 20 basis points on a short-term play, credit risk would be necessary to yield at the same maturity levels.

[9:53:52 AM](#)

Co-Chair MacKinnon stated that the presentation would continue the following week. She discussed housekeeping for the following day.

#

ADJOURNMENT

[9:54:24 AM](#)

The meeting was adjourned at 9:54 a.m.