

ALASKA STATE LEGISLATURE
SENATE LABOR AND COMMERCE STANDING COMMITTEE

January 24, 2017

1:32 p.m.

MEMBERS PRESENT

Senator Mia Costello, Chair
Senator Shelley Hughes, Vice Chair
Senator Kevin Meyer
Senator Berta Gardner

MEMBERS ABSENT

Senator Gary Stevens

OTHER LEGISLATORS PRESENT

Senator Tom Begich
Representative Chris Birch

COMMITTEE CALENDAR

PRESENTATIONS ON ECONOMIC INDICATORS AND TRENDS

Alaska Travel Industry Association
Alaska International Airport System
Division of Insurance

- HEARD

PREVIOUS COMMITTEE ACTION

No previous action to record.

WITNESS REGISTER

SARAH LEONARD, President and CEO
Alaska Travel Industry Association (ATIA)
Anchorage, Alaska

POSITION STATEMENT: Delivered a presentation on the trends of tourism in Alaska.

COLLEEN STEPHENS, At-Large Representative
Alaska Travel Industry Association;

President, Stan Stephens Cruises & Tours
Valdez, Alaska

POSITION STATEMENT: Participated in the ATIA presentation.

JOHN BINDER, Deputy Commissioner
Alaska Department of Transportation and Public Facilities
Juneau, Alaska

POSITION STATEMENT: Discussed the Alaska International Airport System (AIAS) as an economic engine.

FRED PARADY, Deputy Commissioner
Department of Commerce, Community and Economic Development
Juneau, Alaska

POSITION STATEMENT: Participated in the update on the health care insurance market in Alaska.

LORI WING-HEIER, Director
Alaska Division of Insurance
Department of Commerce, Community and Economic Development
Anchorage, Alaska

POSITION STATEMENT: Provided an update on the health care insurance market in Alaska.

ACTION NARRATIVE

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CHAIR MIA COSTELLO called the Senate Labor and Commerce Standing Committee meeting to order at 1:32 p.m. Present at the call to order were Senators Gardner, Meyer, Hughes and Chair Costello. She noted that Senator Begich was in the audience.

PRESENTATIONS: ECONOMIC INDICATORS AND TRENDS

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CHAIR COSTELLO stated that the committee is continuing to look at the Alaska economy and the presentations today will be from industry. She said Alaska is in a recession that won't end anytime soon so it is important for the legislature to look at how its actions affect the economy.

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CHAIR COSTELLO invited Sarah Leonard and Coleen Stephens to come forward.

SARAH LEONARD, President and CEO, Alaska Travel Industry Association (ATIA), informed the committee that last year the state's marketing program was transitioned to be managed by the ATIA team. The goals are to provide efficient and effective marketing resources, professional development opportunities, advocacy statewide for members, and promote Alaska as a quality tourism destination.

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MS. LEONARD said she was invited to share Alaska's travel trends. She started by reviewing global travel trends, transitioned to national trends, and then moved to Alaska trends. Employment worldwide in the travel industry was forecast to grow nearly two percent in 2016 and continue that trend until 2026. The World Travel & Tourism Council predicts that within that timeframe, 25 percent of the world population will travel. A 2015 national report indicates that travel generated \$2.1 trillion for the U.S. economy. It supported more than 15 million jobs in the U.S. and accounted for \$928 billion in direct travel spending by domestic and international travelers. In Alaska, that translates to 47,000 peak-season jobs, over \$4 billion in economic activity, including \$1.39 billion in labor income. She emphasized that this upward trajectory reflects past strong investment in tourism marketing.

She described Alaska's tourism industry as a renewable natural resource and a major contributor to all three of Alaska's budgets: the family budget, city & borough budgets, and the state budget.

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MS. LEONARD reported that Alaska has had a competitive destination marketing program and a record 2 billion people visited the state in 2015. That was a 7 percent increase over the previous season. [According to the McDowell Group, 2015] the majority of Alaska leisure travelers came by cruise ship and air. These visitors spend money on a wide range of activities from lodging to gifts to transportation.

Initial indicators for 2016 show a 3 percent increase in cruise arrivals, a 14 percent increase in personal vehicle Canada-Alaska border traffic, and an increase of 3 percent in outbound enplanements. Alaska Marine Highway traffic dropped 9 percent and international air travel increased 4 percent. She noted the latter might be a conservative number. She emphasized that these positive economic indicators are partly due to the long-standing

competitive destination marketing program for Alaska. The marketing strategies to attract visitors to Alaska focus on the idea that Alaska is more similar to an international destination than a U.S. state.

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CHAIR COSTELLO recognized that Representative Chris Birch was in the audience.

MS. LEONARD discussed the trend of decreased tourism marketing funding from the state and how it impacts the economy. She pointed out that in 2013-2015 tourism marketing funding from the state was in the \$16 million range. Last year, legislative action and the governor's veto reduced the \$4.5 million budget to \$1.5 million. It also included language requiring the tourism industry to develop a plan to reduce reliance on state general funds. By contrast, competitor destinations are increasing their tourism promotion. Only the state of Washington spends less on tourism marketing than Alaska.

She said the tourism industry is healthy right now and that is expected to continue into 2017. However, Alaska requires more investment to compete with other domestic destinations because it is a long-haul, exotic yet safe destination that takes time to plan and visit. Alaska's marketing strategies have focused on these attributes and the economic benefits are being realized.

As destination marketing dollars diminish, the fear is this will affect Alaska's share of the market. It will reduce the number of visitors Alaska is able to attract generating less spending and less economic impact in 2018, 2019 and beyond. National trends also reflect the impacts of reduced statewide tourism marketing dollars. Case studies show that when destinations reduce their tourism marketing dollars, they lose market share and revenue. In 1993, Colorado repealed its tourism funding and within two years lost 30 percent of its U.S. visitor market share. Conversely, Michigan doubled its state tourism marketing funding during a recession and generated \$6.6 billion in visitor spending from 2006-2014. She provided two other examples of the impact of reducing tourism funding.

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MS. LEONARD reported that the ATIA Board of Directors and industry leaders at the Alaska Tourism Marketing Board met several times since the last legislative session to research and discuss different revenue options in an effort to meet the

legislative mandate to become less reliant on state funds. The focus was on three guiding principles: any new funding solution must be broad-based, not reliant on one industry or funding source; revenue should focus primarily on visitor activity with the least impact on Alaskans; and the plan would package new revenue with existing revenue from the current vehicle rental tax collected that can be allocated to tourism promotion.

These conversations gravitated to the Tourism Improvement District (TID) Concept. She explained that industry pays an assessment that is collected by government and the funding is allocated for tourism promotion. TIDs are governed by those who pay, managed by an existing nonprofit or industry association, and payers can vote to stop the assessment. She relayed that this concept has been shared within industry and a funding plan for Alaska destination marketing based on the TID concept was presented to the legislature just today.

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MS. LEONARD highlighted general trends in travel that can be connected to a destination like Alaska. The Adventure Travel World Summit was held in Anchorage in 2016 and attracted up to 750 tour operators, media and others. Partners at Visit Anchorage provided a statewide experience for this group and highlighted Alaska as an adventure travel destination. Multi-generational travel is increasing. There is also a continued interest in culinary and tasting tours that feature local foods and goods. An increase in highway travel may increase if the price of gas remains low. There is also an increase in Chinese visitors, particularly students who are interested in visiting Alaska and the Arctic. ATIA has also had discussions on tourism development in the Arctic.

MS. LEONARD said the industry believes there is value in statewide destination marketing for Alaska. Revenue is being generated from tourism-related activities that filters back to communities. She emphasized that maintaining a competitive marketing brand is crucial to capture market share domestically and worldwide. There are positive returns in infrastructure, revenue to local governments, and jobs that are benefiting Alaska communities and Alaskans. We want to remain a healthy industry that supports Alaska jobs and Alaskans, she concluded.

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CHAIR COSTELLO asked if ATIA expects fewer visitors two years from now and therefore fewer dollars in local economies, or is

the TID plan expected to bridge the more austere marketing budgets.

MS. LEONARD said she can't predict the lag time but there is a real fear that Alaska will see reduced economic activity because of the lower tourism marketing budget. She suggested Ms. Stephens offer her perspective but it's likely that anecdotal evidence will show that individual businesses will be affected. Also, it's likely that Alaska will see less general economic activity as fewer visitors come to the state.

CHAIR COSTELLO asked what percentage of the state's gross domestic product (GDP) comes from tourism. Ms. Leonard and Ms. Stephens agreed to follow up with an answer.

COLLEEN STEPHENS, At-Large Representative of Alaska Travel Industry Association, and President of Stan Stephens Cruises & Tours, said the smaller, mostly Alaskan owned tourism businesses will miss the outreach of the state program to the independent traveler. In rural Alaska, ATIA's current program will have less communication capabilities. The goal is to close that gap as soon as possible, but ATIA will be looking to the legislature to keep funding for marketing as high as possible for the next year, as it works to have a TID in place to be able to do those collections.

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SENATOR MEYER expressed optimism with the concept of TIDs and asked if a bill has been introduced.

MS. LEONARD replied there is draft legislation that could be ready to share next week.

SENATOR MEYER asked if tourism brings \$100 million to the state economy each year.

MS. LEONARD answered yes.

SENATOR MEYER commented that that number would go up substantially if there were a statewide sales tax.

MS. LEONARD said ATIA is always looking at ways to grow that pot through visitor contributed economic activity.

SENATOR MEYER asked if the different entities that market Alaska coordinate efforts to maximize the marketing dollar.

MS. LEONARD replied ATIA manages a statewide program to attract visitors to Alaska and it supports local organizations to highlight their amenities and attract visitors to those communities and regions. ATIA has very good partnerships with many, if not all, destination marketing and management organizations.

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SENATOR GARDNER asked if there is any data about how budget cuts have impacted tourism. She cited anecdotal reports of reduced maintenance and services and voiced concern about harming industries that are healthy.

MS. LEONARD replied the positive impacts of past healthy tourism budgets is still evident, but it's unclear what will happen in 2018 and 2019. The fear is that the cuts in destination marketing will result in reduced community services to support infrastructure. If we're not attracting visitors and paying the vehicle rental car tax, for example, there is less money to support state parks and roads, she said. ATIA is advocating for the tool for industry to assess itself so the industry continues to be healthy.

SENATOR GARDNER asked if ATIA had heard from communities that had been affected by the ferry cuts.

MS. STEPHENS replied ATIA did a survey of impacted members a year and one-half ago when ferry schedules started changing more drastically, and the anecdotal reports were shared with Alaska Marine Highway staff.

SENATOR GARDNER asked if the committee could get that data.

MS. STEPHENS agreed to supply the information.

CHAIR COSTELLO requested ATIA update slide [18] that shows the decline in tourism marketing funding from the state. Specifically, she asked how much revenue the industry brought in to the state and the number of tourists that visited Alaska for the years between 2013 and 2017.

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SENATOR HUGHES asked if ATIA had looked at the impact Alaska reality television shows have had on the tourism industry and if

the interest those stimulate might help bridge the gap until the TID program is up and running.

MS. LEONARD said ATIA has not had the resources to do that specific study but more importantly, the tourism industry doesn't control those marketing messages and often they are not authentic Alaska stories. She added that there the number of those shows might have decreased since the Alaska film office closed two years ago.

SENATOR HUGHES asked about the geographic distribution of tourism marketing funding and if the increased interest in Arctic travel will have a positive economic impact on rural communities. She asked the names of those communities.

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MS. LEONARD replied the funding is concentrated from Southcentral to Southeast, but it still has a large impact in the regions that receive a low percentage of the funding. "Where 1,500 jobs means a lot to Southwest Alaska, that would be a really low number for Southeast Alaska." She offered to follow up with the specific dollar amounts for each region. She said there is growing interest in the Arctic and she's heard anecdotally that tour companies have worked hard to partner with local communities. She acknowledged that some communities are not ready to host visitors and that may be a factor in where cruise ships visit.

SENATOR HUGHES asked when she thinks Arctic tourism will be at full throttle and economic benefits can be expected.

MS. LEONARD said the first cruise ship went through Arctic waters 18 months ago and it is a good idea for ATIA to include that area in the Alaska Visitor Statistics Program to be able to capture that data.

MS. STEPHENS added that there is more opportunity in the Arctic than just small cruise ships. Operators north of the Arctic Circle that offer land excursions are in their busiest months right now and they are seeing both national and international travelers.

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CHAIR COSTELLO said she is encouraged to hear that ATIA is discussing a statewide plan for tourism. The committee will hear

from ARDORs on Thursday and can ask if they have considered tourism as part of their regional economic development plan.

SENATOR GARDNER questioned the benefit of having the TID contributions collected and processed through the government. "Can you members not simply contribute to your functioning and then you don't have to worry about who's making the decision and governing, who pays and how it's spent? It's all up to you now."

MS. LEONARD replied that will likely be part of the discussion with the legislature going forward.

CHAIR COSTELLO thanked the presenters.

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CHAIR COSTELLO reconvened the meeting and invited Mr. Binder to come forward. She said Mr. Binder was invited to discuss air cargo, its impact on the economy, and any thoughts on how to keep that sector strong and thriving during this recession. She noted that Commissioner Luiken was present.

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JOHN BINDER, Deputy Commissioner, Alaska Department of Transportation and Public Facilities, reported that the Alaska International Airport System (AIAS) is thriving, largely due to low fuel prices. He agreed with the previous speakers that the tourism industry has a large impact on airport traffic and AIAS has benefited.

He informed the committee that the Department of Transportation and Public Facilities (DOTPF) owns and operates 242 airports. The airports in Anchorage and Fairbanks are separated by statute as international enterprise systems so they are self-sustaining. The remaining 240 airports are referred to as the rural system. The presentation today is focused on the international piece with a few references to the rural system.

MR. BINDER displayed the aviation mission statements for the Department of Transportation and Public Facilities, the Alaska International Airport System, and Statewide Aviation.

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He spoke to the AIAS vision and core values.

Our Vision:

By 2030, AIAS is a global nexus for aviation-related commerce

- We will be a model government-owned enterprise, adaptive and agile
- We will proactively address global changes and world markets
- We will operate safely while striving for efficiency
- We will optimize our contribution to Alaska's economy and quality of life
- We will involve, value, and balance the interests of stakeholders
- We will be a coveted place to work

Our Core Values:

Integrity: Honesty, dependability, unity, and a high ethical standard

Enterprising: Innovative, proactive, pioneering, business-centric airport system

Excellence: Commitment to improve and a passion to provide superior service and infrastructure

Respect: Professional regard for colleagues and customers

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MR. BINDER said the international airports work together and benefit each other. Carriers come to Anchorage knowing that Fairbanks is a ready alternate.

CHAIR COSTELLO related that the Ted Stevens Anchorage International Airport is in her district and some of her constituents have concerns about communication with the airport. She asked him to discuss how the enterprise management structure works to interact with the community.

MR. BINDER explained that as deputy commissioner, he serves as the executive director of the Alaska International Airport System. The managers of the two airports report directly to him, but have complete control of their respective airports. Regarding public engagement, the governor has an aviation advisory board that represents the various stakeholder groups. These include representatives for passenger airlines, cargo airlines, regional airlines, communities, the unorganized borough, and organized boroughs. The different aviation groups and air carriers also have avenues to both him and the airport

managers. Because DOTPF falls under the Administrative Act, all public engagement includes hearings and public notice.

CHAIR COSTELLO asked if he believes there is room for improvement or if he is happy with the way that process is working.

MR. BINDER replied he is generally happy with the way things are working, but believes that communication can always be improved.

CHAIR COSTELLO said, "I actually would be interested in making improvements to that in terms of outreach to the local community." She added that she would be very interested in meeting with him to pursue this further. "It might be time to give more confidence to those neighbors who live near the airport."

MR. BINDER said he would be happy to discuss that further.

He displayed a depiction of a world map to illustrate the strategic location of the Anchorage and Fairbanks airports. They are within 9.5 hours of 90 percent of the industrialized world and, except for 9/11, these airports have never been closed at the same time.

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MR. BINDER discussed what an economic engine AIAS is for the Alaskan economy. The Ted Stevens Anchorage International Airport accounts for 1 in 10 or 15,577 jobs. It has about \$724 million in direct annual payroll and another \$303 million in annual payroll for jobs in the community. Fairbanks International Airport accounts for 1 in 20 or 1,900 jobs. It has about \$225 million in economic output and in 2010 was ranked 85th in the nation in weight of total mail and freight.

He said a lot of that is fed by the regional impact. He listed the following: just 2 percent of Alaska's land area is accessible by road; 82 percent of Alaska communities are not connected to the road system; and year-round transport of people, freight and mail is primarily by air.

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CHAIR COSTELLO asked if any federal changes regarding weather reporting stations or the FAA have affected cargo delivery to communities that only have an aviation option.

MR. BINDER said DOTPF is always striving to get more weather reporting stations in Alaska and it continues to be a challenge. They continually strive for more stations. Most of the freight and all the mail is part of the USPS Bypass Mail System and is always subject to cuts.

CHAIR COSTELLO summarized that he is not aware of any recent or upcoming changes that would affect access to those communities.

MR. BINDER said that's correct.

He reviewed the economic contribution of aviation from 2009 to 2012. During that timeframe, aviation accounted for about \$3.5 billion or 8 percent of the gross state domestic product and almost 10 percent of the statewide annual average employment.

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MR. BINDER reviewed the attributes of the Anchorage International Airport. It has three 10,500-foot runways; 60 wide-body parking positions; CAT IIIb ILS; 24/7 operation for immigration, air traffic, and U.S. Customs; multiple fuel suppliers; and an in-ground fuel hydrant system. Anchorage is the number 2 airport in North America for landed cargo weight; number 1 for excellence for 5 years running; number 4 in the world for cargo throughput, and a five-time recipient of the award for excellent snow and ice control.

Anchorage International Airport has about 5 million passengers that enplane and deplane each year; cargo throughput is 2.4 million tons; and about 70 wide-body freight aircraft land and takeoff each day. It is a major gateway for FedEx and UPS, and most of the cargo traffic through Anchorage and Fairbanks are Asian carriers.

He displayed data from the Airports Council International that shows that Anchorage International Airport ranks second domestically and fourth worldwide for metric tons of cargo moved.

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MR. BINDER reviewed the attributes of the Fairbanks International Airport. It has one 11,800-foot runway; CAT IIIb ILS; 33 aircraft parking positions; 97 percent Visual Flight Rules (VFR); 24/7 operation for immigration, air traffic, and U.S. Customs; ground service, deicing, catering to all size

aircraft, a convenient 1,065,800 square foot cargo apron; and five heavy cargo parking positions.

Fairbanks International Airport has over 1 million passengers that enplane and deplane each year; is a vital connection to rural Alaska; is a popular winter tourism destination and the gateway to Denali Park; is a premier cold weather testing location; and has an active GA area with multiple surfaces including a 6,000-foot runway, a ski strip in the winter, a gravel strip in the summer and a float pond water strip.

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MR. BINDER explained that commencing July 1, 2013, 29 airlines signed a ten-year operating agreement with AIAS. The signatory carriers share financial risk in exchange for capital and operating input and they receive reduced landing rates and fees. The rates and fees are set to meet the anticipated budget each year. There are quarterly meetings during which there is a complete financial review.

He reviewed the cargo/passenger activity from FY07 to FY17. The peak was 2007 and 2008 and it's been down 20 percent to 30 percent since then. He pointed out that the slide is based on weight of aircraft and freight landed. As the industry has continued to upgrade, it takes fewer aircraft to move the same amount of cargo. Thus, the total landed weight has decreased while the amount of cargo, primarily international, has remained constant. Instate freight is constant at about 100 million pounds and international passenger traffic has slacked off as passenger carriers have improved their fleets to aircraft that don't need to stop to refuel.

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MR. BINDER explained that overall activity is measured based on certified maximum gross takeoff weight (CMGTW). This is how the carriers are assessed landing fees. He noted that things are going well in the current year (FY17).

He displayed a pie chart that depicts the FY16 carrier market share by CMGTW. He pointed out that Cathay Pacific Airways, UPS, China Airlines, and Korean Air tend to dominate, and that most carriers are not American. He displayed a depiction of the globe to illustrate why carriers stop in Anchorage for fuel. "You draw the lines connecting Asia and North America and you're flying right over the top of Alaska." Carriers have the option of flying half full and avoiding a stop in Anchorage to refuel or

flying completely full and stopping for fuel. Generally, it's more profitable to take on full weight and stop to refuel.

MR. BINDER pointed to data that illustrates the importance of the Asian market. He highlighted that almost 80 percent of all cargo that passes between North America and Asia, passes through Anchorage, and that most of the revenue comes from cargo. He displayed a chart showing that passenger activity was up about 4.5 percent in FY16 and is slightly down through December FY17. Alaska Airlines dominates the passenger market. He pointed to the domestic and global destinations that have direct service from Anchorage and Fairbanks. While there are quite a few direct flights to Asia, they are charters. The direct flights to Frankfurt and Reykjavik are scheduled, but seasonal.

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The AIAS FY16 revenue from airline and tenant customers was \$141.9 million. He reiterated that the system does not have a profit mindset; the revenue generated is based on projected costs. He noted that [revenue] exceeded the planned costs by about \$20 million; \$10 million was better than expected activity and the other \$10 million related to revenue that was collected for capital costs.

MR. BINDER reported that the FAA, through its Airport Improvement Program (AIP), allocates about \$200 million to DPTPF airports. About \$50 million goes to Anchorage and Fairbanks International Airports and the remaining \$150 million goes to the remaining 240 airports in the rural system. He explained that airports receive these funds based on how much cargo passes through as a percentage of the overall national total. There is also a passenger entitlement based on the national total. Another factor is airports that are not hubs. By law, Alaska receives a state apportionment and there is also an apportionment based on population. The FAA also apportions funds based on nationwide priorities. The current priorities in Alaska are rural access and safety.

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MR. BINDER described the economic development study that is underway and noted that he has been working on it with the Municipality of Anchorage. The goal is to find business areas where value can be added to the things that are happening at the airport. For example, it would benefit the airport and state to find ways to have more impact on the cargo that passes through the airport. Figuring out what those business propositions might

look like and finding the appropriate target is another piece of the challenge. Right now, they are working on an aircraft maintenance facility.

2:37:19 PM

MR. BINDER discussed the master plans. He explained that the AIAS Strategic Plan is focused on results based alignment, market indicators, revenue-expense ratios, and system optimization. The annual review is scheduled for February 2017. Lake Hood is also part of Anchorage International Airport. It is the largest seaplane base in the world. The Lake Hood Master Plan is a process required by the FAA every 10 years. The public comment period for the draft plan ended January 16, 2017 and the final plan will be released in early spring 2017.

CHAIR COSTELLO asked if Lake Hood is managed with more community input than the rest of the airport.

MR. BINDER replied the Lake Hood manager works for the Anchorage airport manager, and there is also a Lake Hood users group that is involved with the community groups.

He reviewed the future aviation challenges. These include fleet changes both international and instate, climate change impacts, and increasing federal compliance requirements.

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CHAIR COSTELLO cited the new \$40 million Alaska Airlines hanger and asked how he is actively trying to grow opportunities at the airport.

MR. BINDER replied the new Alaska Airlines hanger is the big news, but the department is encouraging opportunity by advertising that land is available to lease.

SENATOR MEYER asked if raising the fuel tax would impact the number of international flights that might land at the airport.

MR. BINDER said no because current statute exempts international traffic from the state fuel tax.

SENATOR MEYER asked if the state gets landing fees from all the airports.

MR. BINDER replied Anchorage and Fairbanks International Airports and airports that are run by the local communities all charge landing fees, but not the other state-owned airports.

SENATOR MEYER asked if the [board] continues to favor increasing the aviation fuel tax instead of the landing fees.

MR. BINDER said that was the discussion last year and the board still generally feels that a fuel tax for the industry is the most equitable way to collect revenue.

SENATOR MEYER said he isn't sure what the impact would be if a landing fee was charged at all the airports. He assumed that most of the maintenance costs are in the rural airports.

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SENATOR HUGHES asked if he has considered where to spend additional federal funds for airports if they do come about for Alaska.

MR. BINDER said AIAS has a prioritized list should those funds become available.

SENATOR HUGHES asked if economic benefit is part of the criteria to prioritize a project.

MR. BINDER replied that is one criteria, but safety and runway structural problems will dominate the scale.

SENATOR HUGHES said she understands that most iPhones that come into the U.S. come through Alaska and there is a lot of talk about the space that's available on the return flight. She identified that as an opportunity.

MR. BINDER replied that is a perfect example of the potential opportunity to have a distribution center in Alaska that would add value to a product. In general, aircraft flying east are full and have been partly empty on the return partly due to the lack of demand for North American goods. However, that is gradually changing.

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CHAIR COSTELLO thanked Mr. Binder.

Division of Insurance Presentation

CHAIR COSTELLO welcomed Ms. Wing-Heier and Deputy Commissioner Parady who were invited to talk about health care insurance.

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FRED PARADY, Deputy Commissioner, Department of Commerce, Community and Economic Development (DCCED), thanked the legislature for passing House Bill 374 during the last special session, and appropriating \$55 million to the Alaska Comprehensive Insurance Association fund to stabilize the individual insurance market. At that time, Alaska had just a single health insurance carrier and had experienced two previous years of 35-40 percent rate increases in the individual market. He said he is happy to report that the effort succeeded, and the anticipated 42 percent increase dropped to 7.3 percent.

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LORI WING-HEIER, Director, Alaska Division of Insurance, Department of Commerce, Community and Economic Development, said it's been an active time for the division since June 2016 when House Bill 374 passed and allowed for the Alaska Reinsurance Program. It was a lot of work to promulgate regulations and get the contract for the grant agreement with ACHIA to operate, but it has been completed and the program is operating.

She clarified that the program was intended to run on a calendar year and the funds were appropriated for a fiscal year so none of the \$55 million has been spent. The funds were appropriated on July 1, 2016 and the policies related to that appropriation began January 1, 2017. She explained that the money is being held by the state until Premera receives a claim. At that time, Premera would pay the claim and then it would be ceded to the Alaska Reinsurance Program.

MS. WING-HEIER agreed with Mr. Parady that passage of the bill had an immediate result. The anticipated 40-42 percent rate increase became an average 7.3 percent rate increase. It also gave the division the authority to apply for a Section 1332 waiver which will likely provide funding for the program going forward. The application was deemed complete a week ago.

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MS. WING-HEIER directed attention to slide 3 that contains language that repeals what was in the budget last year. Section 10 in the Governor's FY18 Budget re-appropriates the money in FY17 and asks for an additional \$55 million for FY18, but

allowing it to be spent over the calendar year when the insurance policies actually run. For example, if someone is treated December 30, 2017, that claim will not be paid in 2017. It will likely be ceded to the re-insurer in March 2018. She emphasized the importance of allowing time for that claim to be processed, ceded to the re-insurer and administered correctly.

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She turned to slide 4 that relates to the proposed budget and request for funding for FY17 and FY18. She clarified that the \$55 million for FY17 was to pay high-cost claims incurred in calendar year 2017.

MS. WING-HEIER discussed the Section 1332 waiver that the division could apply for under House Bill 374. This waiver was not allowed to be granted until January 2017. There have been just three applications: Hawaii was granted a waiver, California withdrew its application, and Alaska's was deemed complete. All the waivers have been different. Hawaii's had to do with the small group, California's had to do with immigration, and Alaska's has to do with re-insurance.

She directed attention to the description of a waiver on Slide 6 and noted that the language is ambiguous as to when to apply. "We were kind of going somewhat by the seat of our pants, hoping that we could convince them that our [reinsurance program] was going to be a viable waiver." What can be waived includes: benefits and subsidies, marketplace and qualified health plans, the individual mandate, and the employer mandate. Each waiver application must satisfy four criteria: 1) it must be budget neutral, 2) it cannot discriminate, 3) it must remain affordable, and 4) the coverage must remain comprehensive.

[3:02:05 PM](#)

MS. WING-HEIER explained that Alaska's application met all the requirements that the secretary of Health and Human Services asked the division to provide. This included a description of the legislation that passed and an analysis and overview of the program. She noted the link at the bottom of slide 9 for Alaska's 200-page waiver application.

During the deliberation on House Bill 374, Senate Finance asked the division to find alternative funding in two years to support the reinsurance program. "So, we knew we had our work cut out for us."

[3:03:24 PM](#)

MS. WING-HEIER directed attention to the Oliver Wyman Actuarial Report on slide 11 to explain Alaska's waiver. It shows that the estimated premium tax credits in Alaska were \$233 million for 2018, and with the waiver they are \$182 million. The department is asking the federal government to return that \$51.6 million difference to the state to fund the reinsurance program. She clarified that the entire \$51 million will not come back to the state, but that is what the waiver represented to the federal government.

She reported that this idea has stimulated tremendous interest because it worked so well and stabilized the market. The bill was innovative, and it was even more innovative to ask for the waiver. The argument was that the federal government would have paid this money to Alaska consumers if the state hadn't done this and the waiver is necessary because the Alaska legislature has said it wouldn't fund the program forever. The application was deemed complete by Health and Human Services Secretary Burwell a week ago.

[3:06:43 PM](#)

SENATOR HUGHES asked if the bill and the waiver were her idea.

MS. WING-HEIER replied, "I work with an incredible team."

SENATOR HUGHES asked if she is getting good vibes that the waiver will be approved.

MS. WING-HEIER answered yes. The Trump transition team reached out in December because they liked the idea and she took it as a positive sign that this reinsurance program and funding from the federal government has a chance of surviving.

SENATOR HUGHES asked if the division would come back to the legislature for continued funding if this weren't to come through.

MS. WING-HEIER replied, "There is a real possibility in that to stabilize the market."

[3:09:08 PM](#)

MR. PARADY directed attention to the January 17, 2018 letter from Secretary Burwell to Governor Walker that cautions that approval of the waiver is contingent on enacting legislation in Alaska that appropriates the funds for the Alaska Reinsurance

Program. He said the department is exploring ways to develop language that satisfies the federal government without requesting a blank check from the legislature.

He explained that the table on slide 14 that shows how the Alaska Reinsurance Program and the Section 1332 Waiver would work is for illustrative purposes. It combines the Oliver Wyman actuarial analysis and an ISER economic analysis to come up with an estimate of the savings to the federal government and what it may be willing to pass back to the state. The best estimate right now is there will be an \$11 million bill to the state and a \$44-45 million cost-share with the federal government.

He summarized that the hope is to see some sort of cost-share agreement with the federal government where 80 percent of the funds come back to the state and 20 percent remain a state obligation. Importantly, the individual market in Alaska is sustained for Alaskans. He said it isn't that you're subsidizing 500 of the sickest individuals, it's the 23,000 Alaskans who are in that market, a third of whom are not subsidized, who see insurance rates that are larger than their mortgage. He added that this also helps ensure that Alaska has a carrier available to provide coverage.

CHAIR COSTELLO asked Ms. Wing-Heier to talk about the 80 percent rule and how Alaska can get a handle on the rising cost of health care.

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MS. WING-HEIER explained that regulation says that insurers will pay out-of-network claims at the 80th percentile. That has led to allegations that providers that have little competition are setting the 80th percentile and driving up the cost of claims. "It's been a very emotional topic between the insurance industry and the medical providers and, of course, the consumers are left in the middle."

MS. WING-HEIER related that earlier this month the division held scoping hearings to find out what people thought about the 80th percentile and if it was benefiting Alaskans. The two hearings were well attended, and more than 60 written comments were submitted. The takeaway was that insurers are seeing that certain providers appear to be driving the market. However, providers who are not specialists testified that they are charging well below the 80th percentile and they are struggling to make ends meet. "So, you've got this mixed bag; you hear the

insurers on one part and you've got a divided medical community."

CHAIR COSTELLO asked if she is suggesting that the legislature should also address cost transparency.

MS. WING-HEIER replied it must be addressed at some point, but it may be taken care of depending on what comes out of Washington, D.C.

MR. PARADY added that while transparency is a major discussion point, the division is still sorting out the testimony on the 80/20 question and trying to develop ideas.

[3:19:22 PM](#)

SENATOR GARDNER asked how quickly the federal government would move if it decided to pick up on the transparency issue. "Do we have a couple of years in which we still have to address this locally?"

MS. WING-HEIER said she can't imagine that it would be less than a year. She added, "We are looking at it and I think that we were surprised by the number of comments that we received and the varying opinions from consumers and, certainly, transparency was one of them."

She related that she asked the House Labor and Commerce Committee to introduce the Governor's bill to update the Model 520 Act for the Alaska Life and Health Guarantee Association. This is the entity that would step in to pay claims if an insurer fails financially. The Model 520 Act was adopted by the National Association of Insurance Commissioners in 2009, but Alaska has yet to adopt those updates. The bill also asks that the state add hospital and medical service corporations to the list of those that can be assessed to pay these claims. She explained the reasoning.

Insurance companies that want to transact business in Alaska file in one of two ways: as an insurance company or as a hospital or medical service corporation. Alaska has one very large insurer in the individual market that has filed as a hospital and medical service corporation. If that insurer were to fail in medical, there are not enough remaining members to pay claims.

CHAIR COSTELLO asked if she had additional comments on the broad topic of health care.

MS. WING-HEIER replied things are coming fast and furious out of Washington, D.C. and the division is trying to stay abreast and provide comments to the Alaska delegation regarding health care for all Alaskans.

[3:24:38 PM](#)

CHAIR COSTELLO thanked Ms. Wing-Heier and Mr. Parady and reviewed the agenda for Thursday.

[3:25:20 PM](#)

There being no further business to come before the committee, Chair Costello adjourned the Senate Labor and Commerce Standing Committee meeting at 3:25 p.m.