

SENATE FINANCE COMMITTEE
February 26, 2019
9:01 a.m.

9:01:52 AM

CALL TO ORDER

Co-Chair Stedman called the Senate Finance Committee meeting to order at 9:01 a.m.

MEMBERS PRESENT

Senator Natasha von Imhof, Co-Chair
Senator Bert Stedman, Co-Chair
Senator Click Bishop
Senator Lyman Hoffman
Senator Peter Micciche
Senator Donny Olson
Senator Mike Shower
Senator Bill Wielechowski
Senator David Wilson

MEMBERS ABSENT

None

ALSO PRESENT

David Teal, Director, Legislative Finance Division; Senator Cathy Giessel; Senator Gary Stevens; Senator Mia Costello; Senator Chris Birch.

SUMMARY

SB 20 APPROP: OPERATING BUDGET/LOANS/FUNDS

SB 20 was HEARD and HELD in committee for further consideration.

Co-Chair Stedman relayed that the day's meeting would be comprised of a budget overview by the director of the Legislative Finance Division (LFD). He reminded that LFD was a non-partisan arm of the legislature that aided in analyzing and working with budgets. The presentation would be an overview of the governor's submitted budget. He

continued that LFD also worked with the legislature as it put its budget together.

#sb20

SENATE BILL NO. 20

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

[9:03:27 AM](#)

DAVID TEAL, DIRECTOR, LEGISLATIVE FINANCE DIVISION, introduced himself and shared that he had a staff of approximately six budget analysts and some Internet Technology (IT) staff that gave support needed to run the budget system that produced the part of the budget bills for the legislature.

Mr. Teal reiterated that LFD was non-partisan, and provided information primarily to the committee while also being available to the full body for questions regarding fiscal matters of any kind. He used the examples of past capital budget projects and help with preparation of amendments to appropriation bills. He had been in his current position for about 20 years. He commented that he had never seen a budget like the currently proposed governor's budget.

Mr. Teal remarked that it was known that the December 15th budget submitted by the governor had been a placeholder, and overviews prior to December 13th were primarily an overview of the fiscal situation as neither LFD nor the Office of Management and Budget (OMB) had a "real" budget to consider. The timeline had delayed the start of the budget analysis. He clarified that the committee had spent more time and engaged in greater detail with the operating budget than he could recall any time in the past. He did not think it was necessary to go through specific budget items that had already been reviewed by the committee and OMB. He thought it was wise to consider some of the policies and principles that drove some of the governor's budget proposals.

9:06:24 AM

Mr. Teal discussed the presentation "Overview of the Governor's FY20 Budget - Round 2" (copy on file).

Mr. Teal spoke to slide 2:

Governor Dunleavy said: My reality budget is based on five guiding principles:

1. expenditures cannot exceed existing revenue;
2. the budget is built on core functions that impact a majority of Alaskans;
3. maintaining and protecting our reserves;
4. the budget does not take additional funds from Alaskans through taxes or the PFD;
5. it must be sustainable, predictable and affordable.

An Honest Budget: Fiscal Year 2020

<https://gov.alaska.gov/an-honest-budget-2020/>

Mr. Teal noted that the OMB website contained a video and statement that accompanied the release of the budget, as well as five guiding principles. He thought everyone knew it was not possible to continue to use reserves.

Mr. Teal reviewed slide 3, "Real Per Capita Unrestricted General Fund Revenue/Budget History," which showed a line graph overlaid with a bar graph. He had used the graph in January and noted that expenditures equaling revenue was simply a mathematical relationship with policy implications. He noted that the bars represented expenditures at various times, and the green line graph represented revenue. It was possible to see that in recent years expenditures had exceeded revenues. The black portion showed what happened when a percent of market value (POMV) payout from the Permanent Fund Earnings Reserve Account (ERA) was added to revenue.

Mr. Teal noted that the graph excluded Permanent Fund Dividends (PFDs). He thought it was clear that revenues were insufficient to fund the budget for a number of years since FY 13. He questioned whether expenditures were too high, or whether revenue was too low. He stated he would let the committee be the judge. He recalled that the OMB director had clearly posited that the expenditures must be too high, but he thought the reverse could also be true. He

thought it was impossible to answer the question until the entire budget was reviewed, and spending priorities were determined.

[9:09:35 AM](#)

Mr. Teal returned to slide 2. He recalled that OMB Director Donna Arduin had stated that the budget was built on core functions and was built from the ground up. He stated that the budget was not zero-based budgeting, and if it had been there would have been analysis of fiscal impact and background information to justify reductions and inclusions in the budget. The director later clarified that it had not been zero-based budgeting; but rather was "core-based budgeting," and agencies had prioritized the services offered. He thought many legislators shared his disappointment in the lack of evaluation and analysis to support the governor's proposals.

Mr. Teal continued his remarks. He thought the budget shouldn't simply be a math problem; and that budgeting and policy were inseparable. He thought one could not make good budget decisions without full information. He asserted that all budget cuts were not equal and recalled that when budget cuts had been questioned the answer was to point out the deficit.

Mr. Teal addressed the third bullet point on slide 2, and thought maintaining and protecting the state's reserves was probably a goal everyone shared. He noted that the budget pulled \$436 million from the Statutory Budget Reserve Fund (SBR) and from other reserves. The FY 19 budget was expected to pull less than \$300 million from reserves. He pointed out that the governor's budget claimed not to take additional funds from Alaskans through taxes or the PFD. He contended that the proposed governor's budget did not rely on existing state revenue to balance the budget but pushed costs on to municipalities and shifted revenue from municipalities. Some, if not all the costs and revenues, would be passed on to citizens.

Mr. Teal continued to speak to slide 2. He addressed bullet 5, which asserted that the budget must be "sustainable, predictable, and affordable." He questioned how the budget would be any more predictable if expenditures equaled revenues while revenues were volatile. He wondered how the legislature would respond to oil price fluctuations. He did

not see how simply setting expenditures equal to revenue would make things more predictable.

[9:13:17 AM](#)

Mr. Teal displayed slide 4, "Traditional Budget Balancing Tools":

- ~~1. Add revenue~~
- ~~2. Pull money from reserves~~
3. Reduce expenditures

Mr. Teal pondered whether he was too literal and understood that people understood words differently. He thought it seemed as though the governor took two of the traditional budget balancing tools off the table and had said the \$1.6 billion deficit would be filled without new revenue and without pulling money from reserves. He suspected that many people considered that the budget was balanced because the governor cut \$1.6 billion from spending. He mentioned cuts to the Alaska Marine Highway System (AMHS), the University of Alaska (UA), and the Senior Benefits Payment Program.

Mr. Teal showed slide 5, "Abbreviated Fiscal Summary--UGF Only," which showed a table depicting a short fiscal summary. He thought the summary helped to put the budget in perspective. He suggested that a short fiscal summary was all that was needed; and pointed out that LFD had no technical issues with the OMB presentation of the budget and the numbers all agreed. He stated that LFD and OMB varied on presentation, and he thought it was important to note that presentation of the budget mattered a great deal. He used the example of depicting the PFD as "off-budget" as the governor had wanted to do. He argued that when dealing with the state's budget, the legislature should be aware of all expenditures and all revenues. He thought PFDs should be treated as a budgeted item. He pointed out the difference in revenue between the 'FY19 MgtPlan' column and the 'FY20 GovAmend' column as shown on the table.

Mr. Teal continued to address the fiscal summary table on slide 5. He commented that the revenues were down by a little over \$200 million due to expected lower FY 19 oil prices. He mentioned the drop in appropriations of about \$73 million in FY 20. He discussed the deficit shown on the table, which was before consideration of the governor's revenue measures. He mentioned the shift in petroleum

property tax of about \$420 million from municipalities to the state. There was another \$28 million in shared taxes that the state would retain instead of handing out to communities. He recalled that in his previous overview publication he had suggested that the governor would find it very difficult to reduce agency operating costs, and he may find he had to cut where the money was or shift costs to local governments. He did not think the statement was going too far out on a limb.

[9:17:29 AM](#)

Mr. Teal reviewed slide 6, "FY19 Management Plan to FY20 Governor' Amended Budget," which showed a table that depicted agency operating budgets were in FY 19 in comparison to proposed budgets for FY 20. The table excluded Medicaid and K-12 education and showed that FY 19 appropriations were just over \$2 billion. He noted that the governor was proposing a 13 percent cut, which was roughly \$260 million. He pointed out that there had been campaign statements that \$200 million or more could be cut with no impact on services, because agencies had funded but unfilled positions and could achieve efficiencies and other savings. He believed that cutting \$200 million from agency operations was a big stretch, and the governor had proposed to cut \$260 million. He had not foreseen a 41 percent cut to the UA budget, or an end to the AMHS as the people in coastal Alaska knew it. He stated that the detail on slide 6 was greater than he wanted to address in the meeting.

[9:19:39 AM](#)

Co-Chair von Imhof thought it was noticeable that the Department of Education and Early Development (DEED) budget did not include formula funding of \$1 billion that was payed to schools. She asked if the monies were paid from General Funds (GF).

Co-Chair Stedman asked Mr. Teal to address the forward funding mechanism from the previous year's budget in his answer to Co-Chair von Imhof's question.

Mr. Teal relayed that the slide showed agency operations and excluded Medicaid and K-12 education, which were big programs with statutory formulas to allocate money. He had taken the items off the slide because the rest of the

budget was what most people considered "day to day" operating costs of state government.

Mr. Teal addressed Co-Chair Stedman's question about education funding. He explained that the FY 20 funding of between \$1.2 and \$1.3 billion was already appropriated and could not be vetoed. The money was simply delayed and was available to school districts beginning July 1, 2019. He continued that in the governor's budget, it was proposed to repeal the provision from the previous year; deleting not only the formula money but an additional \$30 million, to be replaced with a pro-rated amount that was approximately a cut of \$300 million. Because the money was funded the previous year, the legislature could reject the repeal, and the money that was appropriated the previous year would remain in the budget.

[9:23:21 AM](#)

Co-Chair von Imhof had gleaned that the legislature had the liberty to pass the associated bill to repeal the formula funding for FY 20, and instead put forward a new appropriation. She asked if the same was true for Medicaid funding.

Mr. Teal stated that there was a funding interplay with Medicaid, but not in the same way. He detailed that the education funding had passed with a delayed effective date, but Medicaid funding had not. He thought there were statutes and requests to reduce Medicaid funding. He viewed the big formula programs as one of the areas where the money was and thought the governor may not be able to find the money that was needed (to cut) for day to day operating costs.

Senator Hoffman referenced supplemental budget requests for \$20 million and \$30 million. He asked what triggered the distribution of the \$20 million for FY 19 to be dispensed to school districts.

Mr. Teal stated there was no trigger; the money was simply available to school districts on July 1, 2019. The governor had chosen to say that the funds were "not distributed" and would withhold the funds until the legislature took some action on the money. He thought any trigger was a policy call rather than anything having to do with the availability of the money.

[9:26:20 AM](#)

Co-Chair Stedman asked about the latest date that the funds could be distributed to communities.

Mr. Teal thought it was expected that the funds would be distributed along with education formula funding beginning July 1. He did not know exactly what happened, but for some reason the administration had withheld the \$20 million, saying it would use the funds for "true-up" money with the revised student count. He emphasized that the funds had to go out before June 30, and he did not know why one would withhold the funds until that time. It was possible for school districts to balance the books after the fact, but he thought school districts would feel more comfortable knowing the money was coming.

Senator Wielechowski discussed the timing in which school district funds were historically released. He asked if Mr. Teal had seen a situation in which a governor had refused to release funds or waited until June 30.

Mr. Teal thought there may have been instances in which funds had been withheld. He referenced the 1987 Alaska Supreme Court case of State vs. Fairbanks North Star Borough; after former Governor Bill Sheffield had withheld education funding when oil prices fell. The court had ruled that the governor could not withhold appropriated funds and must distribute funds as appropriated. He did not think the ruling addressed timing during the fiscal year; he thought logically the funds should go out in order to be spent.

[9:29:44 AM](#)

Senator Shower reminded that there were constitutional statutory obligations, as well as other items that the legislature chose to spend money on. He asked if LFD considered all the obligations that were required in addition to spending choices. He asked if the governor was required to spend all money appropriated by the legislature.

Mr. Teal stated that the governor did not have to spend all the funds if there were good reasons that it could not be spent. He used the example of the Village Public Safety Officer (VPSO) program; which had remaining funds after

offering funds to grantees and fully funding. There was no requirement for the governor to spend remaining funds. Conversely, if the funds could be spent the governor could not unilaterally withhold the money. The funds must be spent as the legislature appropriated it.

[9:31:49 AM](#)

Senator Shower asked if Mr. Teal had considered constitutional statutory obligations when analyzing the budget.

Mr. Teal stated that LFD considered the statutory obligations and mentioned debt service and retirement costs and things that affected the state's credit rating. For many years, people had tried to break the budget into mandatory versus discretionary expenditures, hoping to control spending. He thought there had always been a problem; and that although education funding was a constitutionally mandated function of state government, nothing stated how much was required to appropriate. There was nothing in law to say whether funding was adequate or inadequate, and the matter could only be addressed by a lawsuit. He thought it was highly likely that there would be a lawsuit if the cut in the governor's proposed budget were to pass. He stated that it was difficult to break out "mandatory" items that did not specify funding levels.

Senator Wielechowski addressed the Base Student Allocation (BSA) and asked if there was any precedent for not funding to the level provided for in statute.

Mr. Teal stated that there was a provision in statute that stated that if under-funding occurred, the state would pro-rate education funding. He did not think the situation had occurred intentionally but recalled that more than ten to fifteen years ago there had been a dollar amount appropriated. In recent years the appropriation for education had been "the amount necessary to fund the formula." He stated that there had been no pro-rating; but it may have happened years ago that there was not enough to fund the full formula.

[9:35:16 AM](#)

Senator Micciche wanted to clarify Mr. Teal's last remarks for the public. He thought that budget requests submitted

by the school districts could be up to \$20 million, and a \$20 million appropriation was the current "law of the land"; but the governor was not breaking the law unless the funding was not provided by June 30th, 2019 unless the legislature changed existing law.

Mr. Teal answered in the affirmative.

Mr. Teal offered to review the largest of the proposed cuts in the governor's FY 20 budget. He addressed slide 6, and pointed out a \$30 million reduction to the Department of Corrections (DOC), due in part to substitution of Permanent Fund money from convicted criminals. When there was an increase in PFDs as there was the previous year, more of the funds were available. The primary reason for the reduction was the expectation that the state would be sending 500 prisoners out of state, which would result in savings. He wanted to know the criteria for identifying out of state prisoners and where they would be located. Additionally, he queried the amount of transportation costs as well as costs of the psychiatric and physical exams that would be needed. He questioned costs to move prisoners for resulting consolidation efforts. He thought there were a number of things that were important to know to back up the proposal.

Mr. Teal continued to address slide 6. He had done an abbreviated analysis and would not be surprised to see a supplemental request of \$7 million from DOC.

Mr. Teal discussed a proposed an \$87 million cut to various programs in Department of Health and Social Services (DHSS). He thought Pioneer Homes might appear to be unharmed but thought people were aware that there were major reductions to the UGF portion of the budget to be replaced with program receipts. He reiterated that the agency had not provided data that LFD would need to fully evaluate the proposed cuts.

Mr. Teal spoke to large cuts in behavioral health, temporary assistance programs, adult public assistance, tribal assistance, and senior benefits. He summarized that there were a number of social services programs other than Medicaid that were substantially reduced in the governor's proposed budget.

[9:40:05 AM](#)

Mr. Teal continued to discuss proposed reductions on slide 6. He pointed out a proposed \$57 million reduction to the Department of Transportation and Public Facilities, primarily for the AMHS. The system was only funded through October, which did not leave many options. He thought if the marine consultant had findings other than shutting the system down, there were no funds to implement other options. He mentioned the University of another example of zero impact on total GF, but there was a 41 percent reduction in UGF. He mentioned the UA president's testimony that the UGF cut was to "real money," while the ability to offset the cuts with tuition was "fantasy money."

Senator Micciche understood the reason and logic behind slide 6; but thought it provided a danger of misunderstanding. He wondered if there could be a slide which listed other reductions. He thought there would be a significant misunderstanding of the impacts of the budget document if only looking at slide 6.

Co-Chair Stedman asked if Senator Micciche was asking for LFD to combine slide 6 and slide 7 to give the public a better understanding of the impacts of the proposed budget.

Senator Micciche answered in the affirmative.

Co-Chair Stedman stated he would work with Mr. Teal to procure the information.

Senator Wielechowski addressed the proposed cut to AMHS. He noted that the ferry system had stopped taking reservations after September 30, 2019. He asked if it was possible for the governor to unilaterally stop the ferry system when the legislature was the appropriating body.

Mr. Teal stated that the governor had told AMHS to stop the reservations on after September 30, 2019. If the legislature appropriated money to the AMHS, the governor was obligated to spend it to run the AMHS. He thought the governor did not want the funds.

[9:43:52 AM](#)

Senator Hoffman stated the governor could also veto any proposed funding.

Senator Hoffman asked about the Department of Public Safety (DPS). He asked Mr. Teal to expound on the proposed \$3.2 million reduction. He wanted a synopsis of how each piece of the governor's proposed legislation would affect the budget if passed.

Mr. Teal addressed Co-Chair Stedman's point about changing slide 6 to include more information. He stated that such a slide was posted on the LFD website, and it was possible to observe the changes in revenue.

Mr. Teal addressed the proposed \$3.2 million cut to DPS, most of which (\$3 million) was to the VPSO program. He was not sure about the placement of the rest of the proposed reduction.

[9:46:24 AM](#)

Co-Chair von Imhof looked at Executive Branch-wide Appropriations for \$23 million. She understood that the administration had lump-summed salary increases from all state employees. She asked for Mr. Teal to comment.

Mr. Teal advanced to slide 9, which showed the \$23 million Co-Chair von Imhof had referenced. He informed that the governor had decided to consolidate all salary adjustments in one area, and to allocate them later. He had requested for OMB to provide LFD with greater detail with the normal breakdown by location and expected to get the information later in the week. He thought subcommittees were expected to incorporate all the salary adjustment funds into the agencies themselves.

Co-Chair Stedman asked members to hold questions pertaining to slides later in the presentation.

Mr. Teal thought the matter would be addressed in the subcommittee process.

Senator Wielechowski asked about the DHSS budget and the \$1 million per month contract issued to Wellpath Recovery Solutions. He did not think the legislature had ever appropriated the funds and wondered where the money came from.

Mr. Teal stated that the legislature had appropriated funds for the Alaska Psychiatric Institute (API). He stated that

the decision to go to a contract may be opposed by bargaining units but the executive branch had the freedom to move money within line items. If it chose to fulfill responsibilities at API or anywhere else by contracting instead of hiring employees, it was allowed.

[9:50:14 AM](#)

Senator Shower asked if Mr. Teal had communicated with AMHS to determine if the system had plans operating past October 1, 2019.

Mr. Teal had not heard of any other plans. He believed that OMB had communicated that the agency had hired a marine consultant to look into the matter. He did not know of any other option than shutdown as there was no funding to run the coastal runs under the proposed budget. He thought the ferry run from Bellingham, Washington; to Juneau in the summer was profitable and could continue to run under the proposed budget scenario. There were program receipts in the proposed budget, but no subsidy for the smaller coastal runs.

Co-Chair Stedman stated that DOT would be coming to the committee, including airports and AMHS.

Senator Wilson asked if Mr. Teal had obtained program priority listing from OMB that listed some reasons for the proposed reductions.

Mr. Teal answered in the negative.

Senator Wilson asked when the information would be available.

Co-Chair Stedman hoped that the prioritization information would come forward during the subcommittee process as promised by OMB.

Mr. Teal qualified that agencies had set priorities, but he was not aware of justification for the proposed cuts. He thought such decisions about discretionary spending were difficult for the legislature to make without information from the executive branch. He thought the administration would be providing more of such information in the current year. He thought by the time the subcommittee process was underway, agencies would likely be asked to provide impact

statements by program to outline what the proposed cuts would do to programs.

[9:54:47 AM](#)

Mr. Teal referenced slide 7, "Filling a \$1.6 Billion Deficit," which showed a data table. He thought the preceding agency overviews had provided good information for the committee to start its subcommittee work. He referenced blogs and media that had referenced LFD. He stated that the point of the slide showing what \$1.6 billion in cuts would look like was to show that agency budgets were not good hunting ground for finding \$1.6 billion in cuts. He thought the governor's budget proved the point by proposing only about \$260 million in cuts, many of them unvetted.

Mr. Teal thought slide 6 left a question of how to balance the budget if it was not through cutting agency budgets. He continued that slide 7 explained how the reductions added up to \$1.6 billion. The slide showed non-formula cuts to agencies, as well as DEED and HESS. He thought it was worth mentioning that when the OMB director was in committee, she had stated that local governments also contributed to education. He clarified that local government did contribute to education through mandatory contributions based on property tax values - which would not be affected by state funding. He explained that there were also voluntary contributions to education by local governments. He noted that voluntary contributions had a cap, which was 23 percent of "basic need."

[9:58:36 AM](#)

Mr. Teal continued to address slide 7 and education funding. He explained that if state funding was cut by 25 percent, then the cap on voluntary contributions also went down by 25 percent. For cities that were already funding to the cap (such as Anchorage or Juneau), a cut to state funds would also cause a cut to local contributions. He noted that areas such as Mat-Su did not fund to the cap and would not lose local funds in such a scenario. There were other complications such as the state not reimbursement school debt, which would result in less money to spend. He summarized that school funding was not as simple as "if you lose state funding, local governments would step up and pay more."

10:00:00 AM

Mr. Teal continued to address slide 7. He asserted that the cuts had been anticipated in some areas and were consistent with the governor's opinion that the state spent too much money. He discussed cost shifts to local government. He mentioned shifting debt service reimbursement onto local governments. He stated that there were some shifts that did not save the state money and brought in state revenue. He used the Petroleum Property Tax as an example. Under the governor's proposal, local governments would no longer have a share of the funds. He reminded that school debt reimbursement would not be paid to local governments under the governor's proposal. The impact on local governments would be \$106 million, \$68 million of which was UGF.

Mr. Teal continued to discuss cost shifts in the proposed budget. He cited some debt service that was proposed to be shifted on to municipalities or cooperatives that the state would no longer be reimbursing. He recounted that the governor suggested he had not wanted to use reserves, yet the budget pulled \$172 million from the SBR, and pulled \$264 million from reserves held by state corporations. He thought it was complicated since the governor crossed fiscal years with the appropriation.

10:03:05 AM

Mr. Teal explained that the governor had proposed to cut \$249 million from Medicaid but restored much of the money in a way that was less than transparent. He discussed the steps of appropriation from reserve funds in FY 19. The funds were available in FY 19 and allowed to carry forward in the subsequent two years. Using the money was contingent upon approval of waivers and other items from Centers for Medicare and Medicaid (CMS). He thought it was highly unlikely that the approvals would come during the next fiscal year; and saw the use of reserves to be nearly certain. If the CMS approval did not come, the state would have a supplemental appropriation of \$70 million or more if the governor's proposals were followed.

Mr. Teal stated that LFD's recommendation was to not use the budget reserves. He asserted that it was possible to reduce the \$172 million in FY 20, but it was likely to increase the supplemental budget by the same amount. He

discussed adding money to Medicaid if it was known the program was underfunded. The \$260 million in Alaska Industrial Development and Export Authority (AIDEA) receipts were spent directly, \$84 million of which was spent in FY 19 to make for a shortage, and the funds were to go into the account used to purchase oil tax credit certificates. The \$84 million in FY 19 was to make up for a shortage. He discussed \$27 million that had been appropriated for debt service (but not used, since bonds were not issued) which could be repurposed to purchase credits.

[10:07:03 AM](#)

Mr. Teal continued to discuss the use of reserves as listed on slide 7. He thought it was possible to ignore the legal and credit rating issues of taking money from AIDEA and just focus on transparency. He stated that excess cash held by state corporations was reserves, and the source of the reserves was the UGF that was used to capitalize the corporation. As with terminated loan programs, LFD preferred to see any recovery of the capitalization of loan funds simply go back to the GF and be spent as GF so the funds were shown in the budget as both revenue and expenditure.

Mr. Teal noted that as the budget appeared, AIDEA revenue did not appear in the budget as revenue or UGF spending but was simply invisible money. He commented that less than half of the \$1.6 billion deficit was filled by expenditure reductions. He asserted that there were revenue and reserve actions that were unexpected given the five principals outlined by the governor. He thought it could be argued that the governor (if following his asserted principals) should submit another bill that did not: cross fiscal years, use reserves, shift costs to local governments, or propose cuts that the legislature did not wish to implement. He would be shocked if amendments addressed the issues.

Mr. Teal thought OMB had suggested that if the legislature did not accept the governor's proposals, it needed to find alternative reductions because the budget had to be balanced. He pondered how the legislature would balance the budget if it didn't like the tax changes, use of reserves, and reductions proposed in the governor's budget. He addressed the possibility of revenue measures. He thought

it was proven that cutting agency expenditures was difficult. He thought there might be room for savings in state-wide items, but it was not enough to balance the budget. He discussed other items such as PFD cuts, and discussed the difficulty of various solutions. He thought there needed to be strong supporting justifications for any proposals by the legislature.

[10:12:12 AM](#)

Mr. Teal considered the lack of justification for the governor's proposed budget and had wondered if the budget had been designed to create chaos. He mentioned the sixteen bills associated with the proposed budget, which hadn't been seen yet. There had been no analysis of the effect of the proposed bills. He suggested that it would take time to see how the legislation meshed with the budget. He wondered if there was hope on the governor's part that the legislature would not have the time to evaluate the full proposal and come up with alternatives. He questioned whether the chaos-creating budget was a mechanism to force a necessary conversation.

[10:14:45 AM](#)

Senator Micciche referenced slide 7 and the school debt reimbursement. He referenced the *Kasayulie v. State of Alaska* court case [a court case settled in 1999 that held that education is a fundamental right and the state system of funding school facilities was racially dissimilatory against Alaska Natives, in violation of the federal Civil Rights Act] and asked if capital was part of the local school contribution cap. He asked if the school debt reimbursement line also impact the DEED local reduction.

Mr. Teal answered in the negative. He understood that the school debt reimbursement bill reduced the payments to municipalities; while the *Kasuyulie* case revolved around the state requirements to provide rural schools, which was done with the Regional Educational Attendance Area (REAA) Fund. The fund was based upon the amount of money that went to school debt and putting a proportionate amount toward rural schools. The formula broke when school debt reimbursement to local governments went to zero, and the deposits for rural schools would also go to zero. There was a provision in the bill that said the state would put money

toward rural schools anyway. He thought Kasuylie issue should be addressed.

Mr. Teal continued to address Senator Micciche's question. He thought if Anchorage implemented a sales tax, it could increase voluntary local contributions if the sales tax more than offset the loss of school debt reimbursement.

Senator Micciche asked why there wouldn't be a reverse lawsuit if urban schools were disadvantage with the administration paying the cost for the rural schools.

Co-Chair Stedman stated that the legislation being discussed may or may not go forward. He was sure the subject of the Kasuyulie case and its implications would be raised when discussing school debt reimbursement when DEED was before the committee.

[10:17:46 AM](#)

Senator Bishop thought there was much to discuss. He asked if the use of AIDEA revenues would be recurring.

Mr. Teal did not think the use of AIDEA revenues could be ongoing. There was a report produced that stated AIDEA had substantial cash reserves; and the budget would take a bit more than half, so there could be no continuation. He had heard discussion in the House pertaining to reducing AIDEA reserves. He explained that that AIDEA was an economic development engine and helped finance economic development in the state. He had heard testimony that there were banks to lend funds; but noted that AIDEA was often a participant in the project funding. Without AIDEA funding, a lot of capital to fund private development was removed. Even taking the amount of reserves being proposed, it could affect the money available for private sector development.

Senator Bishop stated that Mr. Teal had already addressed his follow-up question and he hoped the public had been listening.

Senator Shower asked Mr. Teal for LFD to list a breakdown of sources of DGF to get an idea what was required.

Co-Chair Stedman asked if Senator Shower wanted a breakdown of AIDEA funds.

Senator Shower reiterated that he wanted a list of DGF funds.

Mr. Teal offered to follow up with Senator Shower to get the requested information.

[10:20:46 AM](#)

Co-Chair von Imhof asked if Mr. Teal could talk about the interplay of the SBR and how it had been utilized as listed on slide 7. She thought it looked as though it was incorporated under HESS, and then it was added again. She asked how the math worked.

Co-Chair Stedman asked for an explanation of the SBR and reasoning for the use of the funds.

Mr. Teal explained that the SBR was intended to be used as a shock absorber and was similar to the CBR. The difference was the CBR required a supermajority vote to spend while the SBR required a simple majority vote. He noted that the proposed cuts to DHSS totaled over \$300 million. He had reduced the amount by \$172 million under the "Reductions in Agency Operations" category on slide 7, because the amount was listed in another place. He thought it was more appropriate to list the funds were a use of reserves. He thought Co-Chair von Imhof made a good point. He explained that the numbers worked out, and the slide could have just as well had shown that DHSS had cut \$300 million. If the reserves had been shown as savings, it would not have appeared as using reserves. He had tried to make the point that despite the claim that the governor wanted to maintain the reserves, he was in fact using them.

Senator Hoffman thought the numbers only worked for one year. He asked what funds would be left in the SBR after the expenditure of \$172 million.

Mr. Teal stated that there would be zero funds left.

Senator Hoffman reiterated his point that the numbers only worked for one year.

[10:24:34 AM](#)

Mr. Teal reviewed slide 8:

Are people aware that:

1. Dividends consume 37% of revenue?
2. The proposed FY20 UGF budget is \$123 million (2%) below the FY19 UGF budget?
3. Reductions to agency operating budgets address only \$650 million of the \$1.6 billion deficit?
4. The remainder of the deficit is filled by shifting costs to local government or draining reserves?
5. The impact of the proposed cuts to the operating budget is greater than the 350 positions shown in the OMB overview? Add 600 AMHS, 1,300 UA, and 3,000 school district employees to get over 5,000 jobs.

Mr. Teal explained that the slide was aimed at the conversation that was being caused by the budget proposal and listed some questions he did not think people were aware of. He thought it was astonishing that the state could spend over one-third of all available money on PFDs.

Co-Chair Stedman informed that the dividend being discussed was the statutory formula driven amount.

Mr. Teal answered in the affirmative and clarified that the dividend amount budgeted by the governor was \$1.9 billion.

Mr. Teal continued to discuss slide 8. He wanted to mention the economic impact of the proposed cuts. He recalled that the OMB director and others had referenced position counts and estimating the job losses totaling 150; which had not included significant job losses from AMHS, the University, and school districts, which he estimated to add up to 5,000 jobs. He thought the Institute of Social and Economic Research (ISER), Department of Labor and Workforce Development, and OMB economists would talk more about the indirect effects of the proposed cuts; and that it would be an interesting discussion. He considered government to include state, local, and school districts.

Co-Chair Stedman thought it was highly likely that the committee would begin the discussion the following week.

[10:28:11 AM](#)

Mr. Teal continued to discuss slide 8. He did not have any answers to the questions posed on slide 8 and did not know what the governor's intentions were. He pondered how flexible the governor's principals were, specifically regarding the PFD. He considered the forthcoming budget bills proposed by the governor, and hoped there was time to analyze each bill. He hoped that the governor would prioritize the bills, and thought governors typically focused on a few bills. He thought there was a fairly weak understanding of where the budget would take the state, and whether the budget proposal would stand up to scrutiny once there was time for analysis.

Senator Wielechowski referenced oil tax credits, which according to the Revenue Sources Book consumed \$1.9 billion in FY 20. He asked how LFD defined revenue, and if corporate earnings and earnings from the Permanent Fund were included in the calculation.

Mr. Teal relayed that LFD looked at revenue in the governor's budget proposal primarily as the two tax changes; including the Petroleum Property Tax, which required legislation and would generate about \$420 million. There was another \$28 million in shared taxes that did not require legislation to change, that was currently spent by distributing funds to local governments.

Senator Wielechowski clarified that he had been referring to the first point on the slide that had stated that dividends consumed 37 percent of revenue.

Mr. Teal stated that the first bullet included the traditional oil revenue and the entire POMV payout.

[10:31:57 AM](#)

Senator Wilson addressed the fifth bullet on slide 8 and asserted that it was not known if the UA system or school districts would cut the jobs as described by Mr. Teal. He suggested that the amount of the cut was known, but agencies and districts could restructure in any way to handle any reduction. He thought it was possible to frame the conversation in many ways and suggested that sometimes the information was framed in the most drastic way for shock and appeal.

Mr. Teal stated that Senator Wilson was correct in that it was not known how many jobs would be lost. He relayed that LFD was using a "rule of thumb" to equate approximately \$100,000 per job. He continued Senator Wilson had been correct in stating it was possible to restructure; however, he had simply translated dollar cuts into positions using the calculation.

[10:33:36 AM](#)

Senator Olson realized that Mr. Teal was not a policy analyst, and spoke to his experience in his role as budget analyst. He assumed that Mr. Teal agreed that the proposed budget was the most unrealistic that he had ever seen. He asked how crippling the proposed budget was to the state. He mentioned the proposed cuts to DHSS, which would affect the vaccine control program, and jeopardize public health. He mentioned students and faculty leaving the UA system due to funding uncertainty. He discussed the issue of the Petroleum Property Tax funding shift, which he thought was affecting the bonding rating of the North Slope Borough. He thought the borough might have bonds called in early. He referenced the proposed cuts to AMHS. He asked how unrealistic the budget was and if Mr. Teal had ever seen another budget like it.

Mr. Teal had never seen a budget like that proposed by the governor. He looked at the proposed budget as not unrealistic in budgetary terms, as the cuts could be made and the revenue measures could be adopted. He thought the unrealistic factor was any expectation that there was enough time for the legislature to really consider the budget proposal, especially considering the fact that the information was not available. He thought the proposed budget was a case of biting off more than anyone could chew. There were many proposals, and the proposals were not vetted.

Mr. Teal continued to respond to Senator Olson. He thought an unrealistic workload had been thrust upon the legislature. He thought the legislature would have a difficult time even if the proposal came with a budget analysis. He found it was completely unrealistic that the legislature would be able to complete an analysis of the proposed budget and make decisions in a regular session.

[10:37:41 AM](#)

Senator Micciche referenced the second bullet on slide 8, which referenced a two percent reduction in UGF, while slide 6 showed a 13 percent reduction. He referenced Senator Shower's earlier comments and wanted clarification of how the reduction might impact Alaskans. He asked if Mr. Teal would provide the information.

Mr. Teal explained that the difference in the numbers reflected the 13 percent reduction in agency operating costs listed on slide 6, which did not include formula funding. He returned to slide 8 and noted that the 2 percent cut referenced on slide 8 was for all UGF, including formula cuts, the capital budget, and fund transfers. He stated that at the fiscal summary level, there was a 2 percent reduction.

Senator Micciche noted that the UA budget showed almost no reduction, while there was a huge shift to DGF. He thought it was important to separate out the funding so that Alaskans could see the impacts.

Senator Bishop referenced Mr. Teal's earlier comment about an unrealistic workload on the legislature and thought there was also an unrealistic workload on the administration.

[10:40:08 AM](#)

Senator Shower discussed position reductions. He thought there was a mixture of discussion on positions versus jobs. He reported that the commissioner-designee had informed that there were 3,100 budgeted but unfilled positions. He discussed the PFD. He discussed DGF versus UGF, and thought it was important to discuss all fund sources to provide clarity for the public.

Mr. Teal thought that it was important to consider all kinds of funding, and understand that it was not all the same. He described UGF as "real money," and stated that DGF turned into real money if it could be collected. He addressed the classification of dividends as DGF. There was a time when the ERA had a designated purpose to pay dividends and inflation proofing. The account was not used for government, and the classification of the account had been argued for many years. He noted that the constitution and budgeting defined that the ERA was UGF and could be

spent at any time for any purpose. The state did not classify the ERA as UGF as dividends were considered to be "below the line." The dividends were on the fiscal summary, but not rolled into any totals; which changed under SB 26 [legislation passed in 2018 establishing a POMV draw from the Earnings Reserve Account of the Permanent Fund].

Mr. Teal continued to address Senator Shower's question. He thought that as soon as there was a payout from the ERA that could be used for general government purposes, the ERA was clearly identified as UGF revenue and any spending from it (including dividends) became UGF revenue. He mentioned the relationship between dividends and revenue. If there was \$3 billion in payout, one could pay dividends and the remainder went to the General Fund. He asserted that the amount paid for dividends was a choice to make. He thought it was simply impossible to continue to call dividends DGF. The funds were not designated any longer, and the amount that went to UGF was affected by the amount of the dividends. He thought many people believed that changing the accounting of the Permanent Fund was the reason for the deficit; but it had nothing to do with it.

[10:45:18 AM](#)

Mr. Teal showed slide 9, "A Comparison of the FY19 Budget with the Governor's Amended FY20 Budget Request (UGF only)," which showed a bar graph. He thought that even though there was about \$1 billion of the deficit filled by reserves or new revenue, the takeaway should be that the \$650 million in proposed cuts fell as anticipated. He pointed out small changes in funding for agencies on the right-hand side of the graph and noted that the cuts hit the big money programs as anticipated. The larger cuts were also larger percentage reductions.

Mr. Teal thought it was not a surprise that the governor cut where the money was; in areas many people would agree were core services. He referenced a remark by United States Senator Lisa Murkowski that stated core services were education, healthcare, and access to transportation; and stated that the proposed budget hit the core services hard.

Co-Chair von Imhof considered Mr. Teal's comments about the dividend being considered UGF. She asked about the percentage of the dividend within the entire UGF spend.

Mr. Teal stated that if one followed the proposed budget, the percentage was exactly the same because there was no deficit and no surplus, so revenue and expenditures were equal. The dividend showed to be 37 percent of revenue and 37 percent of expenditures.

Co-Chair von Imhof had considered what was allocated as UGF spend only was about \$3.5 billion for all agencies. If the state was spending \$1.9 billion to pay a \$3,000 PFD; it would be equivalent to 54 percent of the agency spending.

Mr. Teal thought Co-Chair von Imhof had posed a valid number. He stated that LFD had included dividend spending as part of the total.

[10:49:32 AM](#)

Senator Wielechowski agreed with Senator Shower and had never viewed the ERA as UGF. He asked if the PFD was in the governor's FY 20 amended budget.

Mr. Teal thought the governor had an interesting definition of the budget, and had said or implied the dividend was not in the budget. He stated the dividend was in SB 23, an appropriation bill for the dividend, which he thought would be before the committee soon. He looked at the budget as not simply the operating bill; but rather as the full fiscal plan to include all revenue measures, any associated bills, fiscal notes, and all appropriations. He thought it made no difference which bill an appropriation was in - it was still an expenditure. He argued that the governor's budget included all appropriation bills, including SB 23, which appropriated the \$1.9 billion for dividends.

Senator Wielechowski mentioned an appropriation bill seeking the back-payment of dividends. He observed that the appropriation was not listed in the chart on the slide.

Mr. Teal stated that the back payments would not use FY 20 money; and would be used in FY 21, FY 22, and FY 23. The chart was limited to FY 20.

Co-Chair Stedman thanked Mr. Teal for the presentation and asked if he had final comments.

[10:52:26 AM](#)

Mr. Teal pointed out that there was no language in the bill addressing a draw from the CBR.

Mr. Teal reiterated that the CBR was not mentioned in the operating budget. He thought some might argue that none was necessary because there was no deficit. He pointed out that the budget was passed as proposed, there would be a \$20 million surplus. A decline of even 50 cents in the price of oil would cause a deficit, and there would be no automatic way to fill a deficit and would necessitate a special session to address a revenue shortfall. He knew many states addressed revenue shortfalls with a special session, but he considered it to be inefficient. He reminded that the state had the most volatile revenue stream in the country and could not count on accurate projections.

Mr. Teal thought a second issue was that there was no reverse sweep. He explained that at the end of every year, any liability to the CBR was filled by any remaining funds in the General Fund and sub funds were swept in to the CBR. The reverse sweep provision was in the budget every year and returned all the money swept from the sub funds. If the reverse sweep did not happen, the funding for the sub funds was lost. He recalled that even in years with a controversial supermajority vote, the "reverse sweep" vote was not controversial. Rather, the practice avoided terrible accounting issues. He thought the committee might want to address the matter when it considered a committee substitute for the bill.

SB 20 was HEARD and HELD in committee for further consideration.

ADJOURNMENT
[10:56:49 AM](#)

The meeting was adjourned at 10:56 a.m.