

SENATE FINANCE COMMITTEE
April 29, 2019
1:38 p.m.

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CALL TO ORDER

Co-Chair Stedman called the Senate Finance Committee meeting to order at 1:38 p.m.

MEMBERS PRESENT

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

MEMBERS ABSENT

Senator Mike Shower
Senator David Wilson

ALSO PRESENT

Juli Lucky, Staff, Senator Natasha von Imhof; Caroline Schultz, Staff, Senator Natasha von Imhof; Vikki Jo Kennedy, Self, Juneau; Senator Cathy Giessel; Senator Mia Costello.

PRESENT VIA TELECONFERENCE

Adam Hykes, Self, Homer; Lynette Clark, Self, Fox.

SUMMARY

SB 104 APPROPRIATION LIMIT

SB 104 was HEARD and HELD in committee for further consideration.

#sb104

SENATE BILL NO. 104

"An Act relating to an appropriation limit; relating to the budget responsibilities of the governor; and providing for an effective date."

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Co-Chair Stedman discussed housekeeping.

Co-Chair von Imhof MOVED to ADOPT proposed committee substitute for SB 104, Work Draft 31-LS0804\U (Wallace, 4/28/19).

Co-Chair Stedman OBJECTED for discussion.

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JULI LUCKY, STAFF, SENATOR NATASHA VON IMHOF, discussed the proposed committee substitute (CS).

Ms. Lucky noted that there was a new section added on page 2 of the bill that allowed for an allowance outside of the cap for capital projects. She said that an amount equal to the 5 percent of the cap could be spent outside of the cap for projects within a year's time. She furthered that the erroneous language on Page 2, lines 16 and 17 would be removed in a future CS.

Ms. Lucky detailed that the first year of the spending limit would be \$5 million and the amount allowable would be up to \$250 million to be outside of the cap. She clarified that the capital budget would not necessarily be \$250 million, only that up to \$250 million would not be included under the cap. There were also technical changes that did not change the intent of the bill. The technical changes provided clarifying language.

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Co-Chair Stedman WITHDREW his objection. There being NO further OBJECTION, it was so ordered.

Ms. Lucky addressed the fiscal note, which was a statement of zero fiscal impact for various departments.

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CAROLINE SCHULTZ, STAFF, SENATOR NATASHA VON IMHOF, directed attention to the spreadsheet "Unrestricted General Fund Short-term budget expectations (1.5 percent inflation) 'A'," (copy on file). She clarified that the spreadsheet reflected a short-term cash flow analysis that would show the expected budget given the budget that had passed out of committee as well as other policy considerations currently in front of the committee.

Ms. Schultz looked at Slide A, which showed unrestricted general fund (UGF) spending in millions except for Line M, which showed the per capita permanent fund dividend. Line A represented the oil and other UGF revenue, which was projected at \$2.3 billion for FY20. Line B showed the SB 26 percent of market value (POMV) draw, which will be 5.25 percent until FY22, when it switches to 5 percent. Line C showed the UGF revenue, which was the sum of lines A and B and totaled \$5.23 billion. She continued to the 'Spending' section of the spreadsheet, which began on line D. She noted that the senate budget was \$3.785 for FY20 and grew at 1.5 percent inflation rate through FY22. Line E showed total debt payments. Line F clarified the debt subject to the cap; the bill explicitly clarified that the only debt considered debt issued by the state were excluded from the cap. Items such as school debt reimbursement and pension obligation would still be counted under the cap. She pointed to Line G, which showed the retirement payment and Line H was for fund capitalization and was held steady through FY22, as it was unclear what those numbers would be. She stated that Line I reflected that total operating budget at \$4.3 billion and Line J showed the placeholder capital budget of \$150 million. Line I and J added together reflected the total government UGF spending of \$4.46 billion. She said that the chart reflected a permanent fund dividend of only surplus; the total UGF revenue with subtracted UGF spending, which in FY20 was \$777 million and calculated to a dividend of \$1,200 for all qualified applicants. Chart B showed the 50 percent POMV split.

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Ms. Shultz moved to Line N, which showed the total expenditures, including the dividend, of \$5.237 billion. The deficit would be zero as the surplus would be used to pay the dividend. She moved to Line P, which showed

appropriations subject to the cap and was the total UGF spending, less the debt outlined in Line F, as well as capital as long it was less than 5 percent of what the cap allowed. She said that the cap would not apply in FY20 because the effective date of the bill was for the FY21 budget. She relayed that based on the modeling, in FY 21 the appropriation subject to the cap were \$82 million over the \$5 billion cap. She noted the estimated constitutional budget reserve (CBR) balance for FY21 and FY22 and shared that the estimated for the CBR balance for the beginning of FY20 was \$2.3 billion but was subject to change.

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Co-Chair Stedman asked how the legislature would address Line 'R'.

Ms. Schultz noted that the line suggested that the cap as written in the bill was lower can could be expected to be achieved in the first year.

Co-Chair Stedman wondered whether the state would have to have more revenue and less expenses, or less expenses because it was delinked from revenue.

Ms. Schultz stated that the cap was delinked from revenue, so even with a significant windfall in terms of oil prices or production, or remarkably large market returns on the permanent fund, it would not matter because the cap would still be set at \$5 million.

Co-Chair Stedman asked about the components driving the negative number on Line R when operating budgets were flat.

Ms. Schultz stated that the operating budget grew slowly, but it was important to take note that debt payments were expected to increase in FY21 and FY22. Additionally, the state's expected retirement payment should go up by \$125 million by FY21, based on the experience study.

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Co-Chair Stedman asked whether the actuarial assumptions and performance of the retirement portfolio could push the figures over the cap.

Ms. Schultz replied in the affirmative.

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Co-Chair von Imhof thought the key piece of information on the spreadsheet was on Line G, which pushed against the cap. She thought that Lines A through O were separate but interrelated. She believed that the work of the state was to decide what should be done with anticipated expenses over the next few years. She said that Line D looked steady, but other state services like debt, retirement, and capital made a significant impact on the cap. She affirmed that the state needed to adjust the amount of the cap or set more money aside to help fund the years of low cashflow.

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Senator Bishop referenced Page 2 of the bill. He asked whether Line E 'Total Debt Payments' was inside or outside of the cap.

Ms. Schultz explained that Line E included the state obligation for state debt as well as school and municipal debt reimbursement; Line F subtracted out school bond debt reimbursement.

Senator Bishop asked whether the \$103 million listed for FY21, on Line F, was outside the cap.

Ms. Schultz answered in the affirmative.

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Senator Wielechowski understood that the proposed appropriation limit did not apply to an appropriation to the principal of the permanent fund but would apply to the actual appropriation for the permanent fund dividend.

Ms. Schultz answered in the affirmative.

Senator Wielechowski cited the Alaska Constitution, Article 9, Section 16, which excluded appropriations for permanent fund dividends. He thought that in a conflict between statute and the constitution, the constitution would trump.

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Co-Chair von Imhof addressed Senator Wielechowski's question. She affirmed that the entire statute was a conflict.

Co-Chair Stedman relayed that there was a current spending cap, which was considerably higher than the recent spending level. To bring a statutory spending cap below the constitutional spending cap would lead to conflict between statute and the constitution.

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Senator Wielechowski wondered what ramifications there would be if there was a statute that was at odds with the constitution. He wondered whether the constitution would overrule the statute, rendering the statute meaningless.

Co-Chair Stedman thought that a statutorily mandated spending cap that was lower than the constitutionally spending cap would be a non-issue. He believed that there was an effort at hand to adjust the constitutional spending cap so that it was more viable to the current fiscal reality.

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Senator Wielechowski looked at the FY20 calculation for the dividend. He noted that the committee had recently passed at \$3,000 for FY19 and expressed curiosity as to how that would impact the FY20 calculations.

Ms. Schultz offered to provide the information later.

Ms. Schultz addressed a second spreadsheet "Unrestricted General Fund Short-term budget expectations (1.5 percent inflation) 'B'," (copy on file). She noted that the spreadsheet reflected the 50 percent POMV split.

Co-Chair Stedman noted that the original spreadsheet 'A' showed a per capita dividend of \$1,215. He thought the statutory number was more like \$3,000 or \$1.8 billion. He asked how much the statutory number effected the spending cap numeric.

Ms. Schultz stated that increasing the dividend payout would not affect the cap itself but would impact the appropriation subject to the cap by adding an additional

\$1.2 billion. She thought it was important to note the difference between cash flow constraints and cap constraints when discussing expenditures.

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Senator Micciche understood that spending over the cap for a full dividend would exceed the cap by \$800 million.

Ms. Schultz agreed that the full statutory dividend would put the state significantly over the cap.

Co-Chair Stedman asked that the full statutory dividend be added to the model.

Ms. Schultz agreed to provide the information.

Co-Chair Stedman recalled an earlier conversation on changing the statutory dividend calculation to a 50/50 split of the 5.25 percent between the dividend and the portion that would come to the state for core services. He said that the slide reflected the split.

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Ms. Schultz affirmed that slide 'B' showed everything from the prior slide except for line L, which reflected 50 percent of POMV split for the dividend, with the other 50 percent going to other government spending. She noted that lines A through K were unchanged in the second scenario. She pointed out that M was higher as well as Line N. She stated that the revenue less expenditures on Line O reflected a larger deficit due to the higher dividend payout. She thought it was important to note that Line O was a cash flow deficit, which was distinct from the cap; the appropriation subject to cap on Line P was also higher because the dividend amount was higher. The cap remained unchanged. Line R, the amount that appropriations were either under or over the cap, was higher due to the larger dividend payout.

Ms. Schultz shared that the model assumed that deficits would come from the CBR, and it was observable that the CBR balances depleted much more quickly with the larger dividend payout.

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Co-Chair Stedman looked at line O. He thought that in FY20, hypothetically, the state would be \$690 million short of meeting its obligations; in FY21 the shortfall would be \$865 million.

Ms. Schultz answered in the affirmative.

Co-Chair Stedman understood that the model used the 50/50 POMV split.

Ms. Schultz responded in the affirmative.

Co-Chair Stedman looked at line R. He surmised that the state would be approximately \$1 billion over the cap to balance the budget.

Ms. Schultz agreed.

Co-Chair Stedman thought there was a demonstrated benchmark error of where the starting number should be and asked how that could be fixed.

Ms. Schultz suggested that a way should be discovered to reduce the total expenditure by \$1 billion or add \$1 billion to the cap.

Co-Chair Stedman explained that in looking at the two models it was important to consider the impact on the legislation that would be made by a new statutory dividend structure.

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Co-Chair von Imhof agreed that the cap could be increased to reflect any scenario. She asserted that the cash flow was the real issue. The reason for a cap was to constrain spending, so that funds were saved in years of high cash flow. She thought the consideration was an academic experience. She thought reasons such as retirement and debt expenses were valid reasons to increase the cap.

Co-Chair von Imhof pointed out that the spending did not have to reach the cap, particularly if the revenue was unavailable. She noted that spreadsheet 'A' showed a dividend of \$1200 for FY20 and noted that there would be pressure on the dividend because of retirement and debt,

which left a weak capital budget. She lamented that the state was already short of funds for capital projects and noted that an additional \$20 million had just been spent on an emergency supplemental. She thought that a 50/50 split was fiscally unwise.

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Co-Chair Stedman noted that Co-Chair von Imhof pointed out the balancing of the spending cap and consideration of the net cash flow. He thought there would be great concern of taking the CBR below \$2 billion.

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Senator Olson agreed with Co-Chair von Imhof that it was not necessary to spend up to the cap.

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Senator Wielechowski wondered about the rationale for excluding debt obligation like refundable oil tax credits from the appropriation cap and not including state pension liability and school debt bond reimbursement in that exclusion.

Co-Chair von Imhof said that retirement could be excluded if it was the wish of the committee. She explained that her initial proposal was for anything that used UGF but that conversations with committee members had resulted in the exclusion of some things from the cap.

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Senator Wielechowski thought it looked like inflation was calculated on the average of the previous five years. He thought it was important to ack quickly to rising inflation.

Ms. Schultz stated that she had considered many different growth options for the cap. Personal income was considered, and several other factors. Given that inflation had been fairly steady over the preceding years, the window had been closest to the revenue forecasts for growth rate.

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Ms. Lucky added that as Senator Olson had previously stated, steady growth over time had been considered. Since the cap was not intended to be a "spend to" target but a rate of acceptable growth, the five-year average seemed the best fit for the model.

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Senator Micciche supported the five-year trailing average.

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Senator Wielechowski asked about the constitutional appropriation limit, and thought the bill proposed one-third set aside for capital projects and loan appropriations.

Co-Chair Stedman stated that the issue had come up over the years. He thought the issue was more complex than it appeared. He questioned how to embed the capital project needs of the state into a spending limit that was targeted for the growth of the operating budget. He suggested that the matter be considered by LFD and the Legislative Legal department.

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Senator Bishop stressed the importance of steady maintenance of the state's buildings and roads. He believed drawing down deferred maintenance in the state would help to smooth out the capital budget overtime.

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Co-Chair Stedman OPENED public testimony.

ADAM HYKES, SELF, HOMER (via teleconference), spoke in opposition to the bill. He did not believe that the POMV model was workable and did not have faith in a spending cap. He said that the role of the government was to promote the general welfare, not to provide for it, and that the state was going broke trying to provide for everyone's needs. He supported less government spending.

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LYNETTE CLARK, SELF, FOX (via teleconference), testified against the bill. She thought the bill was in aid of growing bigger government. She supported the cuts proposed by the governor.

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VIKKI JO KENNEDY, SELF, JUNEAU, was from Kodiak. She asserted that when it was time to act, it was too late to prepare. She expressed a general malaise with the seemingly redundant conversation surrounding balancing the budget while paying out a full dividend. She did not support further cuts to education or the ferry system. She feared that the legislature was overcomplicating the situation.

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Co-Chair Stedman CLOSED public testimony.

Co-Chair Stedman set the bill aside.

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Co-Chair von Imhof shared that the \$5 billion figure had been chosen because it was inline with the expected next few years revenue would be and what the past few years expenditures had been. She referred to Line K on both slides, which showed that expenditures had been below the spending cap, and only when the surplus was spent was the cap breached.

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Senator Micciche reiterated his support for the use of the 5-year average in the model. He said that the governor supported an appropriation limit. He stated that the committee supported an appropriation limit, which was a seed for the future.

SB 104 was HEARD and HELD in committee for further consideration.

Co-Chair Stedman discussed housekeeping.

#

ADJOURNMENT

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The meeting was adjourned at 2:33 p.m.