

HOUSE FINANCE COMMITTEE
March 10, 2021
1:35 p.m.

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CALL TO ORDER

Co-Chair Foster called the House Finance Committee meeting to order at 1:35 p.m.

MEMBERS PRESENT

Representative Neal Foster, Co-Chair
Representative Kelly Merrick, Co-Chair
Representative Dan Ortiz, Vice-Chair
Representative Ben Carpenter
Representative Bryce Edgmon
Representative DeLena Johnson
Representative Andy Josephson
Representative Bart LeBon
Representative Sara Rasmussen
Representative Steve Thompson
Representative Adam Wool

MEMBERS ABSENT

None

ALSO PRESENT

Alexei Painter, Director, Legislative Finance Division;
Connor Bell, Fiscal Analyst and Economist, Legislative Finance Division.

PRESENT VIA TELECONFERENCE

Megan Wallace, Director, Legislative Legal Services, Alaska State Legislature.

SUMMARY

PRESENTATION: ALASKA'S FISCAL POSITION, LOOK BACK, AND PROJECTIONS BY: LEGISLATIVE FINANCE DIVISION

Co-Chair Foster relayed the agenda for the meeting.

^PRESENTATION: ALASKA'S FISCAL POSITION, LOOK BACK, AND PROJECTIONS BY: LEGISLATIVE FINANCE DIVISION

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ALEXEI PAINTER, DIRECTOR, LEGISLATIVE FINANCE DIVISION, introduced the PowerPoint Presentation: "Alaska's Fiscal Position, Look back, and Projections." He began with an outline on slide 2. He would review the budget changes since FY 15, discuss the state's current position, and explore what might happen looking forward. He noted that the scenarios and adjustments in the presentation were developed for the March 4, 2021 meeting of the Senate Finance Committee. The Legislative Finance Division was a politically neutral entity and did not endorse a particular fiscal plan.

Mr. Painter discussed the reasons for the use of unrestricted general funds (UGF) on slide 3. The presentation would focus on UGF. He explained that the budget deficit existed solely in UGF. If there were appropriations from other fund sources that exceed revenue, it would cause hollow appropriations but would not actually cause a deficit. The only fund that contributed to the budget deficit was UGF. Narrowing the focus to UGF spotlighted the state's general fund (GF) cashflow issues. The focus did not mean other fund sources were not important. For example, designated fund sources (DGF) contributed to the deficit indirectly because of lapsing funds that could go into the GF. There were important policy calls to be made across all fund sources.

Mr. Painter continued that the GF numbers reflected the department activities and how they impacted the state's treasury. It did not reflect the size of government. Looking at the size of government would require a different discussion, one in which all funds would be reviewed. The presentation was not focused on the size of government. Rather, it was focused on the impact to the GF.

Mr. Painter moved to slide 4 to review the agency budget changes since FY 15. He mentioned there were handouts in members' packets of the following two slides in larger font. He referred to Handout A (copy on file). He noted that the key points on the following few slides were to show how agency budgets had changed since FY 15. Fiscal

Year 15 was chosen because it had been the peak year of the agency operations budget.

Co-Chair Foster asked for clarification about the handout. Mr. Painter indicated that Handout A had 3 pages and the other handout had 2. He highlighted there were \$651 million in UGF budget reductions between FY 15 and FY 18. All agencies had seen UGF reductions. Since FY 18 there had been a much different trend. Although there had been an overall reduction, there had been a mix of increases and reductions depending on the agency. He encouraged members to ask themselves whether the state had reached the maximum in UGF spending it could appropriate without having to make key structural changes to the state. Major legislation would be needed to address such items.

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Mr. Painter turned to the spreadsheet of agency budget changes since FY 15 on slide 5. The slide corresponded to page 1 of Handout A. The slide showed the total picture, agency budget changes since FY 15, between the FY 15 final budget and the governor's amended budget. He noted he was using the final budget rather than the management plan because it had the least number of distortions in agency spending. Neither were perfect. The final budget included supplementals, more accurately reflection true funding.

Mr. Painter pointed out that over the period the state was down \$700 million or 15.6 percent in agency operations in UGF over the period. The statewide items were down \$3.5 billion. The number was slightly inflated because of the extra \$3 billion transferred from the Constitutional Budget Reserve (CBR) to the retirement system in FY 15. The total, before considering the Permanent Fund and the capital budget, decreased by 49.5 percent. Much of the decrease had to do with the payment to the retirement system.

Co-Chair Foster noted there would be fiscal models in the later part of the presentation along with an opportunity to look at how different things affected the larger picture.

Mr. Painter focused on agency budget changes from FY 15 to FY 18 on slide 6. The slide corresponded to page 2 of Handout A. The period was one of substantial budget reductions. The red ink represented budget reductions to every agency's UGF. The total reduction was \$663 million or

a 15 percent reduction to agencies. The largest reduction in dollars was to the Department of Health and Social Services (down \$155.8 million) and to the Department of Transportation and Public Facilities (down \$160 million). There were other agencies down in the double-digit percentages in the same period. Substantial reductions had been made across the board. The agencies were sorted from the largest budget to the smallest rather than alphabetically.

Mr. Painter noted that in statewide items there were two major reductions. First, there were reductions to retirement payments. The way they were reflected showed the normal cost in FY 15 as state retirement payments. The special appropriations reflected the additional deposit into the retirement system above the normal cost. The second major reduction was in fund capitalization due to the change in oil tax credits. In FY 15, the state funded the full statutory amount of \$700 million. In FY 18 the state funded it at a significantly lower level because of the decline in oil prices.

Mr. Painter continued to the spreadsheet on slide 7 which corresponded to page 3 of the handout. The slide showed the agency changes from the FY 18 budget to the FY 22 governor's budget. Overall, the budget was down by \$41.4 million or 1.1 percent in agency operations. A clear trend did not exist from agency to agency. The Department of Health and Social Services (DHSS) was down about \$54 million, and the University of Alaska (UA) was down \$60 million. There were counterbalancing increases including \$60 million for the Department of Corrections (DOC) as well as significant increases for the Department of Public Safety and Judiciary.

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Representative Josephson cited an example within DHSS. He suggested that the Indian Health Service (IHS) reclaiming might have had an impact on bringing as many dollars into the overall system as there were at its peak. He did not think it was accurate to say that dollars circulated for a service were down by \$53 million.

Mr. Painter responded that the representative was correct. He indicated that tribal claiming and Medicaid expansion brought in a much higher match because of more people being

eligible for Medicaid. In looking at an "All Funds" report, it appeared that DHSS' budget had grown significantly - mainly due to the increase in matching federal funds.

Vice-Chair Ortiz asked Mr. Painter if he was referring to all funds or UGF. Mr. Painter responded that all of the slides in the presentation reflected UGF. He highlighted the bottom right of the slide showing that the state's operating budget for FY 22 was down by 1.4 percent of \$62 million from FY 18. However, the percentage did not apply across the board.

Mr. Painter moved to slide 8 to explain where the state's budget was currently and where it would be for the Governor's FY 22 budget. He indicated the circled numbers showed the CBR draws. He pointed to line 16 showing the pre-transfer deficit. It showed the true fiscal deficit of the state. He explained that the state could not run a deficit according to the Alaska Constitution. The pre-transfer deficit was the fiscal deficit; post-transfer, the state balanced its budget. The slide showed a pre-transfer deficit of about \$2.1 billion in both years based on the governor's budget. The governor made up those deficits as seen in line 17 with draws directly from the earnings reserve account (ERA): \$1.2 billion in FY 21 and \$2 billion in FY 22. The CBR draw was at the bottom of the slide which showed the remaining amounts: \$900 million in FY 21 and \$93 million in FY 22.

Mr. Painter also pointed out the other red circle on the slide showing the fund balances. He noted a couple of differences from past versions presented to the committee. He explained that the Legislative Finance Division (LFD) projected that the state would have about \$1.4 billion at the end of FY 20. In December, LFD and the Office of Management and Budget (OMB) projected a higher balance based on lapses they saw from different agencies. The projection by LFD showed a balance of \$1.76 billion at the end of FY 20. However, the state's comprehensive annual financial Report that came out a couple of weeks prior showed a CBR balance of \$1.4 billion or slightly lower. In previous years, the balance would have been about \$900 million in each year but had dropped by about \$400 million - leaving a balance of \$500 million in each year. He indicated that the change was primarily due to audit adjustments. He admitted that there was a substantial

difference from a more recent forecast, and LFD was working diligently to find out why it was so different.

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Representative Wool asked if the CBR balance of \$531 million in FY 21 was post-transfer of \$900 million, which would bring the balance to about \$1.4 billion. He asked if he had heard Mr. Painter correctly. Mr. Painter responded, "That's correct. Yes." Representative Wool wondered if the following year was \$463 million post the following reduction of \$93 million. He suggested there was not a line that showed \$1.4 billion balance pre-transfer on the graph. Mr. Painter responded in the negative.

Representative Josephson suggested that in the prior year the state had a balance of about \$1.4 billion and currently there was a balance of about \$500 million. He asked if he was correct. Mr. Painter responded that the amount was based on the governor's budget and the fall revenue forecast. It was the projected available balance at the end of the current fiscal year.

Representative Josephson asked why the number had change. Mr. Painter replied that the state's financials were audited, and a number of adjustments were made that reduced the available balance. He emphasized he was talking about the balance of the CBR available for appropriation. The legislature had made a number of direct appropriations from the CBR for capital projects. He indicated there would be a higher cash balance on the Division of Treasury's website than in the financial statements. The difference was attributed to the continuing appropriations out of the CBR as well as cash being used for cashflow. The projection was based on the fall forecast. He suggested that if prices were higher, the available amount would be higher because of a smaller deficit.

Representative Josephson suggested that if the legislature followed the administration's view of monies that should be placed in the CBR versus in the general fund, the balance would be higher. Since the auditor was part of the legislative branch, the legislature should subscribe to the audit version of the account. He asked if M. Painter agreed.

Mr. Painter responded that LFD and OMB agreed on the CBR balance. He explained that when he received the audit the projection became a firm number which was below LFD's projection. Both entities used the same methodology. There had been a disagreement in the prior year which had since been worked out.

Representative Josephson queried about the governor's vetoes and where the dollars went. Mr. Painter replied that they went to a reduced deficit in FY 21. He furthered that had the governor not vetoed the items, there would be a greater deficit.

Representative Josephson asked if the veto dollars went into the general fund or the CBR. Mr. Painter answered that if the appropriations were not made, the money would not be drawn out of the general fund and, therefore, the CBR draw would be smaller. The CBR was used as a deficit filler.

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Representative Josephson relayed that previously the Treasury Division testified that the state needed \$1.4 billion in reserves to cover the state's cashflow needs. The division most recently testified that the state needed \$500 million. Based on Mr. Painter's testimony, the account is not available to draw from because it was at \$500 million. He asked if he was correct.

Mr. Painter responded that based on the fall forecast the representative would be correct. He would not suggest going below the \$500 million mark for cashflow purposes. He suggested there were other alternatives for cash flow. However, the CBR was currently what the state used for cashflow.

Representative Carpenter asked if Mr. Painter had the total lapsed fund balance or a projected amount for the end of the year. Mr. Painter responded that on March 4, 2021, OMB sent a letter indicating that there would be an estimated amount of \$110 million in lapsed funding in FY 21: \$100 million in Medicaid funding and \$10 million in funding of other areas. The governor's budget grabbed some of the lapsed funding and reappropriated it elsewhere. He suggested that even with the governor's budget the state would lapse about \$45 million in FY 21.

Representative Carpenter clarified he was talking about unencumbered lapsed funds - funds that were not supposed to be used for other things. Mr. Painter remarked that Representative Carpenter was correct. He noted he did not adjust for projected lapsed funding but thought it would be a reasonable adjustment to add \$45 million to the CBR balance.

Representative Rasmussen asked if the state would be able to avoid any CBR draws with the passage of the federal COVID package. Mr. Painter responded that the federal bill directed just over \$1 billion to the State of Alaska directly plus amounts for education and particular purposes. The \$1 billion was analogous to the Coronavirus relief fund of \$1.25 billion the state received in the prior year. Avoiding any CBR draws would depend on how the legislature chose to use the funding. The money could be used in place of general funds to help avoid deficits and spent over several years.

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Representative Rasmussen thought there was more latitude in the second round of federal COVID funding. Mr. Painter thought Representative Rasmussen had provided a fair characterization. He added that the second round of funding could be used explicitly for revenue replacement. He qualified his statement. The funds could not be used for revenue replacement the state caused by reducing a tax or fee, for example. He concurred that there were less restrictions on the funding.

Representative Rasmussen asked if the loss of oil production in the early part of the prior year would qualify as a loss of revenue and, therefore, could be replaced with federal Covid dollars. Mr. Painter responded, given that oil prices presently were higher than they were before the pandemic, after the spring forecast the state would have minimal revenue replacement it could apply to the general fund.

Representative Wool suggested that everything in the FY 21 column had occurred except for the ERA transfer of \$1.2 billion. He wondered if that was in the supplemental. Everything else including the CBR draw of \$900 million had occurred. He asked if he was correct. Mr. Painter responded in the affirmative with the exception of line 9, the

supplemental appropriations in the operating budget, and line 12, the supplemental capital appropriations.

Representative Wool reviewed the numbers on the slide. He wondered why \$2 billion was being taken out of the ERA to pay the deficit. He asked if it only applied to the Permanent Fund Dividend (PFD) and the remaining deficit was \$93 million and had to be paid out of the CBR. He asked if it was the reason the two figures were not combined. Mr. Painter indicated Representative Wool was correct. He reported that the governor had an appropriation bill separate from the operating budget that paid the Permanent Fund Dividend (PFD). It had an additional draw directly out of the ERA to pay the dividend. The draw was not used to meet the general deficit. He would turn the presentation over to Connor Bell.

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CONNOR BELL, FISCAL ANALYST AND ECONOMIST, LEGISLATIVE FINANCE DIVISION, turned to slide 9. He relayed that the following slides were based on LFD's fiscal model. The Legislative Finance Division used revenue inputs from the Department of Revenue (DOR). The department's fall forecast was based on \$45 per barrel of oil in FY 21 and \$49 per barrel in FY 22. Since the fall forecast was released oil prices had climbed significantly. He would be using updated futures numbers leading to an average oil price of \$52 per barrel in FY 21 and \$59 per barrel in FY 22. He noted current prices were even higher. The Alaska North Slope (ANS) oil price Monday was \$68 per barrel. There was some uncertainty in the price, and futures markets seemed to anticipate that the price would moderate in the coming months. However, it was still possible that the price would be higher - the current price was higher than what he was showing in the presentation. Based on the numbers LFD was using compared to the fall forecast, the increase in the FY 21 price would increase FY 21 UGF revenue by \$250 million. Revenue would increase by \$300 million in FY 22 due to the \$59 per barrel projected price.

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Mr. Bell clarified that, regarding assumptions, LFD was using Callan's projected rates of return for the Permanent Fund and assumed they were consistent returns for all years. More volatile rates could have significantly

different outcomes even with the same overall average 10 years. The projections were 6.48 percent returns in FY 21 and 6.75 percent returns in FY 22. The model assumed that no inflation occurred through FY 24. Beginning in FY 25 inflation proofing of approximately \$1 billion would occur every year in the models but would not appear in the deficit numbers. It would appear in the form of decreased ERA balances. If there was a shift in the trends of the ERA balances it might be due to the introduction of inflation proofing.

Mr. Bell continued that he would be showing fiscal summaries alongside LFD's fiscal modeling outputs. They would differ slightly due to the fiscal models assuming \$50 million per year in supplementals. The model assumed that all deficits would first be filled with CBR funds until the CBR balance reached \$500 million. After that, funds would be drawn from the ERA. He had included a snippet of the model. The full model provided more outputs and had various tweaks to revenues and spending options. He was happy to work with any legislative office on specific modeling options. He could also provide a simpler model that offices could use on their own to model simple scenarios.

Mr. Painter turned to slide 10: "Fiscal Summary with Updated Revenue Assumptions." The summary added in an adjustment. The adjustment was made in February because he pulled the futures in February. The slide showed the revenues on line 3 - about an additional \$250 million in FY 21 and approximately \$300 million in FY 22.

Mr. Painter pointed to the CBR balance in the bottom right of the slide. Instead of \$500 million, there would be a balance of about \$800 million by the end of FY 21 and about \$1 billion by the end of FY 22 because the state's deficits would shrink. He further detailed that instead of drawing \$900 million from the CBR in FY 21 the state would only draw \$660 million. Also, there would be a post-transfer surplus of about \$200 million after the \$2 billion direct draw from the ERA. There would still be a deficit of about \$1.8 billion. However, after the state drew the PFD from the ERA, there would be a post-transfer surplus. However, the state would still have a fiscal deficit drawing an extra amount from the ERA and depositing money into the CBR.

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Representative Wool thought it would be a policy call. If the deficit was \$1.8 billion and the statutory PFD cost \$2 billion, he suggested that \$1.8 billion could be pulled out of the ERA without having to transfer money to the CBR. In other words, the amount of \$2.023 billion would not have to be pulled out of the ERA.

Mr. Painter agreed it would be a policy call. The governor's budget did not change the amount coming out of the ERA based on the projected deficit. He relayed that LFD did not change the governor's assumption, and the slide reflected the structure of the governor's budget. However, the legislature had the option of changing the budget's structure.

Mr. Painter reviewed the fiscal model for the Governor's Amended Budget before the PFD payment on slide 11. He noted the FY 21 deficit of \$661 million matched the previous slide. The deficit in FY 22 (or surplus) was different because of the supplemental assumption. The slide did not include the PFD payment. The idea behind the slide was to show the size of the gap or surplus before factoring in the PFD. In the following few slides, he would make a series of adjustments to the budget size to peel back the layers of the governor's budget. He would show the true size of the deficit without some of the one-time items in the governor's budget that would affect certain assumptions. He reiterated that the slide did not include a dividend payout to make a comparison more easily. It was not a policy suggestion. Rather, the slide did not include a dividend payment to show larger surpluses and a growing CBR going forward.

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Mr. Painter spoke of the unusual fund sources in the Governor's Budget totaling \$241 million on slide 12. There were several unusual fund sources within the governor's budget that were not necessarily bad or illegal in any way. However, by using them it made the budget look smaller than it would without the fund source items. He indicated he would be unwinding the fund sources in order to see the true size of the deficit.

Mr. Painter relayed that one category of unusual fund sources was the use of lapsing balances, which was higher

than in other years. There was \$35 million in lapsing Medicaid appropriations that the governor was carrying forward into FY 22. There was also \$5 million of fire suppression money that would potentially lapse. The governor wanted to appropriate it for the construction of fire breaks in the previous year. Originally, the legislature appropriated UGF dollars for fire breaks. It was essentially trying to get the same appropriation without having to count it towards the budget. Also, there was \$500 million to OMB for rate smoothing. He remarked that it was inline with how the state had used lapsing funds in the past. However, the legislature could simply appropriate UGF in the FY 22 budget making the budget more transparent. The governor was using lapsing balances which were in line with current practices.

Mr. Painter identified another category: the use of fund sources for non-designated purposes. The largest fund source in this category was \$60 million of AIDEA receipts for oil and gas tax credits. He indicated the fund classification for AIDEA receipts was "other" and did not show up as UGF spending, even though it was typically a UGF item. There was also \$10.5 million of Power Cost Equalization (PCE) funds that the governor proposed using for capital projects. The amount was greater than the draw level from the fund as laid out in statute. The governor's supplemental budget included \$4 million of Higher Education Funds for prosecutor recruitment and housing. Although the fund was for a designated purpose, there was no apparent link between prosecutors and higher education. Similarly, the governor had a fund change utilizing PCE funds in Alaska Energy Authority's (AEA's) operating budget - not a designated use as defined in statute. Also, the governor's budget used \$400,000 of Higher Education Funds for operations at the Alaska Commission on Postsecondary Education which was not a designated used in statute.

Mr. Painter continued that there were several one-time or temporary fund sources, most notably \$104 million of Alaska Housing Finance Corporation (AHFC) bonds in the capital budget for a federal match for both the Department of Transportation and Public Facilities (DOT) and the Department of Environmental Conservation (DEC). The state could not continue bonding \$100 million per year from AHFC, as that was AHFC's bonding capacity at present. He indicated there was \$16.3 million of Mental Health Trust

Reserve funds which was not a fund source expected to be available in the future.

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Representative LeBon referred to the middle of the slide regarding AIDEA receipts for oil and gas tax credits. He had heard in a previous presentation that AIDEA typically earned about half of the amount. They paid about half of their net profit in dividends to the state equaling about \$18 million. He suggested that \$60 million was a large overdraw - more than what they made in the prior year. He wondered about the sustainability of using AIDEA receipts to pay oil and gas tax credits on a long-term basis.

Mr. Painter reported that AIDEA's dividend in FY 22 was \$17.3 million based on earnings of twice that amount: \$34.6 million. Representative LeBon's math was correct, as it was twice the amount of AIDEA's earnings. He confirmed that AIDEA had about \$350 million in reserves. However, there was about \$60 million of outstanding tax credits. It would exhaust the reserves long before tax credits were paid back.

Representative LeBon suggested that it would impair AIDEA's ability to raise bonded money in the future because it weakened their capital position. The bond market would not be impressed with such a program. He suggested that the beneficiary of the \$16.3 million was the Alaska Psychiatric Institute (API). He thought the use of the funds was more logical. He asked Mr. Painter if he had an opinion about that use.

Mr. Painter did not have an opinion. He agreed that it was a designated use to the degree that the funds were designated for mental health purposes. The Alaska Mental Health Trust Authority (AMHTA) preferred not to do ongoing investments - the investment would be ongoing at \$6 million per year. It was not in line with the preferences of the trust, but it would impact trust beneficiaries.

Representative LeBon suggested that if AMHTA chose to reallocate their earnings reserve to their beneficiaries and included API it would be within the scope of their mission. He wondered if Mr. Painter agreed.

Mr. Painter remarked that the entire cost of API would be a significant portion of their budget. He thought it would be within the scope of their mission. However, the draw level would not be sustainable and would use up their reserves. In addition, AMHTA had indicated they might consider catching up with their inflation-proofing which they had not done since 2005. If they were to do so, very little of the reserve funding would be available.

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Vice-Chair Ortiz brought up the topic of oil and gas credits. He had heard that because oil prices had increased recently, there was a greater obligation for the state to pay a higher amount in oil and gas tax credits. He asked if he was accurate. Mr. Painter deferred to Mr. Bell.

Mr. Bell replied that if the price of oil was higher than expected the statutory calculation for the appropriation would be higher. The appropriation was based on the amount of the production taxes levied. The Department of Revenue interpreted that as the amount of tax levied before credits. Therefore, a price increase could raise the statutory calculation more than proportionately. In addition, if the price of oil was below \$60 per barrel, the statutory calculation would be 15 percent of taxes levied. If the price of oil was above \$60 per barrel, the calculation would be reduced to 10 percent. Based on a \$59 price per barrel in FY 22 he expected the calculation to be \$120 million. At \$60 per barrel, just one dollar more, the calculation would be \$80 million due to the percentage of 15 percent versus 10 percent.

Vice-Chair Ortiz suggested the lower price of \$59 would be more desirable for that particular calculation. Mr. Bell responded that he was correct. Vice-Chair Ortiz asked about an increase in the state's obligation. Mr. Bell replied that the statutory calculation would increase by about \$60 million subject to appropriation.

Representative Josephson spoke of AMHTA as an independent standalone body. However, Mr. Abbott testified that AMHTA was required to pay \$6 million for the current fiscal year (he noted the figure was really \$16 million in total). Effectively, they would have to reconfigure their own regular appropriation and would no longer be their own authors of what was good for the mental health needs of

their constituency. He thought it would be rife for a thread of litigation. He suggested a Superior Court Judge would ask whether it had been done before. At some point, AMHTA would just be passive while the legislature was being the appropriator without their guidance. He asked if Mr. Painter agreed. Mr. Painter deferred to Megan Wallace.

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MEGAN WALLACE, DIRECTOR, LEGISLATIVE LEGAL SERVICES, ALASKA STATE LEGISLATURE, clarified the question posed. She concurred that there was a chance of litigation anytime the legislature took action that AMHTA disagreed with. While AMHTA was being reconstituted as part of the Weiss settlement, the judge suggested that if the legislature did not follow the statutes or amended them, the only remedy for plaintiffs would be to reopen litigation. She thought there would be some litigation risk but could not speak to whether the litigation would be successful.

Representative Edgmon commented that at face value the additional deficit was \$241 million. However, he did not think the figure was correct. He pointed out there was the Alaska Housing Finance Corporation (AHFC) bond package of \$104 million that might put an annual dent in the dividend that the state received. He asked Mr. Painter to identify the funds on the slide that were not tied to federal funding. He thought it was clear that a third of the \$241 million that came from AIDEA receipts for oil and gas tax credits were not tied to federal funding. He asked Mr. Painter to walk through which of the figures were tied to federal funding sources.

Mr. Painter responded that Medicaid was tied to federal reimbursement. There was no federal impact to fire break construction, rate smoothing, or oil and gas tax credits. The Alaska Energy Authority capital projects would bring in additional federal funding. The other item that would bring in federal matching funds was the AHFC bond package of \$104 million.

Representative Edgmon asked what percentage of the \$241 million was federally funded. Mr. Painter responded that over half of the items were being used for match funding. He suggested that AFHC was one way to get the match. The legislature could also appropriate general

funds. The governor structured it so that it was tied to match funding.

Representative Wool referred to Representative LeBon's comments about AMTHA's \$6 million of the \$16 million that went to the Alaska Psychiatric Institute (API) beneficiaries. He also brought up AIDEA spending \$20 million to get the leases in ANWAR, and over the following 10 years leasing would cost an additional \$40 million totaling \$60 million for the oil and gas industry. He asked for a definition of receipts. He wondered if the \$60 million would come out of their [AIDEA] investment fund.

Mr. Painter responded that AIDEA had their dividend which was the amount they declared the state could spend. They also had their receipts which were their corporate receipts of ongoing revenue and was money they typically spent on their budget. In the current case, drawing from AIDEA receipts meant it would come from funds other than their dividend. The Alaska Industrial Development and Export Authority (AIDEA) had indicated that if the draw was enacted they would draw the money from their reserve funds.

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Mr. Painter advanced to slide 13 to examine the fiscal summary for the Governor's Budget with typical fund sources. In other words, UGF was added in place of the unusual fund sources. He highlighted that \$10 million was in the supplemental budget and the remainder was in the FY 22 budget. The intent of the slide was to show the true size of the budget if normal fund sources were used. It resulted in significantly higher operating and capital budgets and a much higher deficit from the CBR. Whereas previously it showed a surplus of about \$200 million. If the legislature were to draw the amounts from the general fund as opposed to the fund sources proposed by the governor, the CBR balance (shown on line 21) would be down to \$770 million in both years. If the other fund sources were used in place of UGF, the CBR balance would climb to \$1 billion.

Mr. Painter advanced to the bar charts on slide 14: "Fiscal Model: Governor's Budget with Typical Fund Sources." He highlighted that the spending line shifted up resulting in a deficit in FY 22 and a pre-PFD surplus in the out years with a CBR balance continuing to rise. In future years, the

state would be left with available funds before the dividend was paid.

Representative Josephson clarified that Mr. Painter meant funds available before the state paid the dividend. Mr. Painter concurred.

Mr. Painter moved to slide 15 to review how the federal COVID-19 relief package impacted Alaska's budget. He reported there were significant federal Covid-19 relief dollars in the state budget already. He noted the Federal Medical Assistance Percentage (FMAP) increase from 50 percent to 56.2 percent. It was the primary reason the state was seeing a projected lapse in Medicaid in FY 21 and why there was a lapse in FY 20. The higher rate saved the state about \$15 million to \$17 million UGF per quarter. It was likely that the percentage rate would be extended through the end of the current calendar year but was not yet certain. It was not built into the budget. The governor was making up the amount with \$35 million. In many cases, the Coronavirus relief fund was used before state funds which created lapsing funds to the CBR in FY 20.

Mr. Painter reported that the other lapsing funds projected in the OMB lapse report were primarily due to the use of federal offsets. There were ongoing federal funds to DOT for airports, highways, and transit authority grants. The governor's budget did not propose to use the money in place of UGF. The funds would be used to make up lost marine highway revenues and to pay for grants. Some of the funds had not been allocated to-date. The governor's budget had \$14.6 million in fund changes in order to utilize some of the airport funds. A reduction in UGF of the same amount resulted. Federal funding that helped the state's budget in the current year could not be counted on in future years. The state would have to adjust accordingly in terms of the true size of the fiscal gap.

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Mr. Painter continued with slide 16 which showed the fiscal summary that added the adjustment of \$14.6 (shown in green) which he thought was minor in the scheme of things. There was a slightly larger deficit and a slightly lower CBR balance on line 21.

Mr. Painter turned to the charts on slide 17: "Fiscal Model: Governor's Budget without COVID-19 Funding." The slide did not look much different [from slide 14] because it only reflected a small adjustment.

Mr. Painter moved to slide 18 which corresponded to Handout B. The slide showed FY 18 - FY 22 spending with adjustments for fund sources and Covid-19 (the governor's amended budget with the adjustments Mr. Painter had reviewed). He noted that without the one-time or non-designated fund sources in the governor's budget, the slide showed what the changes would have been. The largest difference was that instead of seeing a reduction in agency operations between FY 18 and FY 22 there was a slight increase due to higher amounts in the budget for the Department of Health and Social Services and in other agency budgets.

Mr. Painter advanced to slide 19 to provide an overview of obligations and funding needs of the State of Alaska. He reported that the list was not exhaustive. The Alaska Energy Authority had testified earlier their need for additional funding in the amount of \$800 million for the bulk fuel program for deferred maintenance which was not reflected on the slide. The purpose of the slide was to show that while many of the items were subject to appropriation, the state had large outstanding obligations or needs. The state had some sort of payment plan for most of the items, all of which were subject to appropriation.

Mr. Painter relayed that the largest outstanding obligation was to the retirement system. The state had an unfunded liability of over \$6 billion. An annual payment plan was in place and paid over \$300 million per year through FY 39. The state had outstanding existing debt including general obligation bonds, lease purchase agreements, and other sorts of state debt totaling about \$1.1 billion with payments extending to FY 41. The amount of the payment in FY 22 was \$91.3 million.

Mr. Painter continued that the state's share of outstanding municipal school debt (subject to appropriation) was nearly \$800 million stretched out through FY 39. The moratorium on new debt expired in FY 25. If the moratorium was not extended there would be future debt protracting out further. The full funding of municipal school bond debt was \$84 million in FY 22. He reported there was also \$760

million outstanding for oil and gas tax credits. A statute was in place that dictated how much to deposit but was subject to appropriation. The governor's budget included \$60 million for that purpose.

Mr. Painter reviewed that the state had approximately \$2 billion of deferred maintenance outstanding. Currently, the payment plan was to use the capitol income fund which earned about \$30 million per year - not enough to make a dent in deferred maintenance. The governor's budget included \$51.6 million by scooping some other funds into the capitol income fund. The state's share of school major maintenance and construction lists, lists of prioritized projects by the Department of Education and Early Childhood Development, was about \$350 million combined. The Regional Educational Attendance Area (REAA) Fund could be used for many of these projects, and there was an annual deposit made into the fund. However, the fund could not be used for all of the projects. He detailed that for projects in the REAAs and eligible schools the state had a payment plan of annual deposits. The state did not have an ongoing funding mechanism for the other projects.

Mr. Painter conveyed that the Department of Environmental Conservation (DEC) reported a rural sanitation need in the amount of \$1.8 billion that the state met in the capital budget through the Village Safe Water Program. He reiterated that the purpose of the slide was to show that much of the budget was devoted to ongoing large obligations. While the state's payments were subject to appropriation, the obligations existed and placed pressure on the state.

[2:36:25 PM](#)

Representative Josephson suggested that if Mr. Painter had prepared slide 19 in FY 13 the PERS amount would have been \$10 billion. He thought the information was troublesome. He wondered if every state had a similar slide. Mr. Painter responded affirmatively that every state had a list of obligations.

Representative LeBon knew every state did not have an REAA Fund. He asked if there was an actual REAA fund where money was set aside or whether it simply an appropriation.

Mr. Painter responded that the state made appropriations into the fund and DEED could, without further appropriation use the fund for projects on the list. The legislature appropriated money into the fund. If there were lapsing balances from those projects because they came under budget, the funds could be returned to the fund and used for other projects.

Representative LeBon asked if there were any lapsed funds sitting in the REAA fund. Mr. Painter was uncertain, since the department could spend the money without further appropriation, they sent the state a list each year of the obligations they make each year. At any given time, they might have funding in which they were waiting to get enough to meet the funding needs for the next project on the list. There might be a balance sitting in the fund waiting for additional funding to come in for the next project on the list.

Representative LeBon theorized that it was not likely a material amount money. Mr. Painter confirmed that generally, the money in the fund was obligated for the following project on the list.

Representative Rasmussen thought everyone should consider that the total amount was actually more than double the state's obligation because the state was constitutionally obligated to replenish the Constitutional Budget Reserve (CBR). She had heard people question how the state could possibly achieve repayment of the fund because of its already large budget deficit. She believed the state should be seriously discussing a repayment plan and the type of revenues it would take to meet the plan. She suggested that if the obligation was not considered, it would be akin to stealing from future generations. She requested that the issue be addressed in a future slide.

Mr. Painter indicated that he had debated putting the slide in the deck because it was an internal debt versus and external debt. He appreciated the legislator's point.

Representative Edgmon asked if the University was included in the deferred maintenance figure. Mr. Painter responded in the affirmative.

[2:40:29 PM](#)

Mr. Painter discussed the governor's budget and statutory formulas on slide 20. The governor's budget fully funded the statutory formulas. There were several other statutory formulas that the governor's budget did not fully fund. He noted school debt reimbursement. The governor was funding it at 50 percent of the statutory level. Full funding would add another \$41.8 million to the budget. The governor was also funding the REAA fund at 50 percent of the statutory level. The governor was proposing to put in \$12.4 million for community assistance. The statute indicated either \$30 million or the amount needed to get to a fund balance of \$90 million should be deposited. Another \$17.6 million or more would be needed to reach a fund balance of \$90 million. The governor was not funding municipal project debt service, an item subject to appropriation. He had vetoed funding for that the previous 2 years. If it were to be funded the amount would be \$2.4 million.

Representative Josephson indicated that at the federal level the House of Representatives concurred with the Senate regarding the American Rescue Plan. He thought Alaska's local governments were supposed to receive about \$227 million. He wondered if the monies could fund the bond debt.

Mr. Painter understood that the allocation for local governments would flow directly to those governments or at least as directly obligated. He did not know if the funds could be diverted to school debt reimbursement or other purposes rather than sending them directly for allowable related pandemic expenses. The state did not have guidance yet on how the funds could be used. He suspected the state would have more clarity in the following weeks.

Representative Josephson had talked to someone at OMB who indicated a clear nexus to a Covid need had to be demonstrated. He wondered, if the funds were sent directly to local governments, whether they could be used for that purpose.

Mr. Painter answered that the funds could be used either for direct Covid-19 expenses or assistance to businesses and families to make up for the economic impact of the pandemic. He did not know if the school bond debt would fall into that category. The local governments could use the funds for things other than specific expenses related to COVID-19 as was specified for the CRF [Community

Reinvestment Fund - part of the Coronavirus Aid, Relief, and Economic Security (CARES) Act].

Representative Edgmon asked Mr. Painter about the wave of money that would be coming to Alaska from the American Rescue Plan and the possibility of folding those funds into the budget process in the current session. Mr. Painter did not know. Guidance from the federal government was supposed to be distributed within 60 days. It would be a major policy call for the legislature and the governor on how to spend the money. The governor might come forward with amendments or the legislature might make its own plan. Nevertheless, it would be a major call for the legislature.

Representative Edgmon suggested that normally federal funding was largely predictable. He was seeing a large asterisk in terms of what the ARP could bring in and the involvement of the legislature in terms of appropriation power. He thought Mr. Painter would be addressing the topic in another slide.

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Mr. Painter turned the presentation over to Ms. Wallace.

Ms. Wallace advanced to slide 21 to compliment the discussion about statutory formulas and the legislative power of appropriation over expenditure of funds provided for statutorily. The Alaska Constitution, Article 9, Section 13 stated, "No money shall be withdrawn from the treasury except in accordance with appropriations made by law." She also relayed that the constitution had a dedicated funds prohibition in Article 9, Section 7 that prevented the legislature from dedicating the proceeds of any state tax or license for any special purpose. Reading the items together, an appropriation was required to carry out any statutory formula that the legislature enacted. A common question that her office received related to whether an appropriation was specifically required and whether the legislature had the power to differentiate from the Permanent Fund Dividend statutory formula. The issue was considered by the Alaska Supreme Court.

Ms. Wallace explained that in the case *Wielechowski versus the State of Alaska*, the Alaska Supreme Court held that legislature's use of the Permanent Fund income, which was used to fund the dividend, was subject to the normal

appropriation and veto process. Therefore, each year the legislature might appropriate from the earnings reserve account to the dividend fund any amount regardless of the language set forth in statute. She indicated that while the slide provided a general sense of the legislative power of appropriation, there might be specific funds or formulas outside of the generality. However, in general, unless an exception to the dedicated funds prohibition applied, each year the legislature could appropriate money from any available source for any public purpose it deemed appropriate.

Ms. Wallace went on to say that statutory formulas served as guidelines or policy suggestions that the legislature set forth as an expectation to follow but one that was subject to appropriation each year. Each year state programs were all subject to appropriation and competed amongst and against each other for funding by appropriation from the legislature. She was available for questions.

[2:49:15 PM](#)

Representative Thompson commented that it was interesting that both state taxes and licenses could not be dedicated to any special purpose. He noted that licensing fees, such as those for the Board of Accountants, were used for the members to meet three to four times per year. They paid extra licensing fees in order to pay for their travel. He asked if the money could be wiped out according to statute.

Ms. Wallace responded that ultimately Representative Thompson was correct. She indicated that when the legislature enacted statute it was setting guidelines or expectations for what the legislature would do through appropriations. For example, if the statute stated that the legislature might appropriate fees from licenses back to the corresponding board, it showed a policy decision that the legislature made that it was the intent that the fees collected would stay with the board or organization to fund the expenses of the board. It was typical of what she saw in the Alaska Statutes. She explained that some phraseology used in the statutes made a soft dedication such as the word "may." She continued that because the dedicated funds prohibition prevented the legislature from enacting statutes that used words such as "shall" the legislature had the authority to recommend where the fees were appropriated. However, if the legislature wanted to use the

funds for another purpose, it would have the constitutional power to make that decision.

Representative Thompson indicated that many of the boards, not just the example he gave, used licensing fees for travel and annual board meetings. He appreciated the information.

[2:52:12 PM](#)

Representative Edgmon argued that every day the committee grappled with how much money should be used for government services versus the PFD. He was annoyed by the remarks of the governor and others about the legislature was not following the law as it related to the PFD. However, it was up to the legislature on how to spend the state's coffers. He listed a number of government services. He noted it had been 5 years since the state had elected to pay a full PFD as reflected in the 1982 statute. However, the legislature, according to the Wielechowski case, had not broken the law because it ultimately had the power to appropriate. He asked if he had made any misstatements.

Ms. Wallace responded that Representative Edgmon was correct. The issue with respect to the power of the legislature to appropriate an amount for a PFD was squarely resolved in the Wielechowski v. State matter that was before the Alaska Supreme Court. The Alaska Supreme Court affirmed that the appropriation for the PFD was subject to the normal appropriation and governor veto process.

Representative Edgmon thought it was an important distinction to make that he continued to hear policy makers and people in high positions suggest that the 1982 statute overrode what the Alaska Supreme Court decided only a couple of years prior.

Representative Wool brought up the dedicated fund provision. The alcohol and marijuana taxes came to mind. He indicated that a large percentage of the taxes went towards alcohol and marijuana prevention programs. He asked if the soft dedication applied.

Ms. Wallace agreed that the revenue was subject to appropriation, and the statute set a policy guideline as to where the legislature might appropriate the fund. However, they would be subject to appropriations.

Representative Wool recalled the three rules of starting a new job. The first rule was the boss was always right. The second rule was the boss could be wrong. Rule number three was that if the boss was wrong, refer to rule number one. In other words, whatever the legislature did was the law.

[2:56:12 PM](#)

Representative Rasmussen [Audio cut out]. Ms. Wallace asked Representative Rasmussen to restate her question.

Representative Rasmussen asked if the legislature was technically breaking a statute by not following the formula in statute. Ms. Wallace opined that the statute had always been subject to appropriation. The Alaska Supreme Court had affirmed that notion in the *Wielechowski v. State Alaska Supreme Court* decision. In her opinion, if the current and previous legislatures chose not to follow the formula outlined in statute, she did not consider it a violation of law. The legislature had the constitutional power of appropriation to decide how much to appropriate to the program each year.

Representative Rasmussen asked if the legislature had the ability to either change or remove the section in statute [containing the PFD formula] within statute. Ms. Wallace responded in the affirmative. The legislature could amend the provision at any time.

Representative Wool mentioned the debt to the CBR. He recalled a presentation by Mr. Teal [previous director of the Legislative Finance Division]. The committee heard about the CBR balance. The debt the state owed to the account was whatever the highest balance was. If the legislature put \$16 billion and brought the balance to that amount, then forever and always the legislature would owe back up to \$16 billion. Whereas, if the legislature had never put that money in the CBR, the debt would not exist. He thought it was an odd way to structure debt - the legislature was being punished for saving money. He was not sure if the same applied to the SBR. He was unfamiliar why the state owed a savings account from which the legislature put money away and later spent when it needed to. He asked if the debt was similar to an appropriation. He asked if it was a statutory item like the other items being discussed or a separate category.

Ms. Wallace indicated that the repayment obligation to the CBR was a constitutional provision. She reported that Article 9, Section D of the Alaska Constitution had the sweep provision which provided that until the legislature reconstituted any amount that was paid out of the CBR fund, a sweep would occur. The repayment obligation was a constitutional mechanism rather than a statutory one. The same requirement did not apply to the SBR which was create in statute as opposed to the constitution.

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Representative Wool asked for clarification of Ms. Wallace's use of the word reconstituted. He queried that since the high-water mark for the CCR was \$16 billion, if the money was repaid, would that amount have to remain in the account forever. He wondered if there was a way to get rid of the \$16 billion. He thought he might have missed part of Ms. Wallace's answer. Ms. Wallace indicated that from a legal perspective the repayment requirement was a constitutional requirement. Therefore, when the legislature spent from the CBR, it was contemplated that the legislature would replace the money. She deferred to Mr. Painter for further clarification.

Mr. Painter stated that the repayment amount was not to reach the prior fund balance, it was to repay every dollar the legislature borrowed. There might be additional funds flowing into the account every year because of new oil settlements. There also might be some investment earnings. The legislature did not get to count that against its debt. The only thing the legislature could count against its debt was payments into the CBR through direct appropriations or allowing the sweep to occur. In FY 15 the legislature drew \$3 billion from the CBR and deposited into the retirement funds. In the same year there were deposits into the CBR. However, the legislature still owed the \$3 billion. If the legislature were to repay the entire debt, the CBR was at its peak at about \$12 billion and \$16 billion when combined with the SBR. If the state paid back the amount owed, the CBR would be larger than it had ever been. The governor had a constitutional amendment proposal that would eliminate the repayment provision.

Representative Josephson asked Mr. Painter what the legislature intended when the CBR provision was written in

1990. He asked what the money was being saved for at the time. Mr. Painter was not sure what legislators had anticipated when they wrote the amendment.

Representative Josephson indicated that when he looked at slide 19 it appeared the CBR repayment was one of the lowest priorities. He thought it might be a political matter. He pointed out the PERS/TRS unfunded liability. If the state did not pay the obligation, the legislature would hear from constituents because the state would have violated the constitution regarding pensions. If the state did not pay the general obligation bonds, creditors would come knocking. He continued that if the state did not pay the state's share of municipal debt, the local governments would cry foul. If the legislature did not pay deferred maintenance, buildings would collapse. If the state did not pay the CBR there would be no penalty or interest charged. It was simply a debt the state owed itself. He asked if he was correct.

Mr. Painter supposed the penalty would be the sweep occurring each year which either required getting rid of all of the state's subaccounts of the general fund or the $\frac{3}{4}$ vote. He confirmed that the state did not charge itself interest for the use of the CBR.

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Representative LeBon noted that on slide 21 Representative Thompson talked about a designated account whereby the Board of Accountants collected dues from accountants in the state for their special purpose. However, every June 30th the account was subject to the reverse sweep and the money was deposited into the CBR. He asked if he was accurate.

Mr. Painter thought carry forward language was used in the budget each year to avoid the sweep. The language stated that on June 30th the balance in those accounts could be carried forward and used in the following year essentially obligating the money before the sweep occurred.

Representative LeBon asked whether changing the legal language of the repayment of the CBR funds would require an amendment to the constitution.

Representative Rasmussen asked why prior legislators or legislatures moved money to the CBR knowing that the state

had a constitutional obligation to pay the money back. The legislature allowed the account to grow to its current level instead of utilizing the SBR.

Mr. Painter replied that during the years the state was repaying the CBR, it stopped at the level of its previous debt. Beyond that, the state began filling up the SBR. Legislatures at the time recognized the circumstances. One factor that allowed the account to grow was, because the state had surpluses in that era, the entire balance was able to be invested. There were some very strong market years that enabled the CBR to earn significant monies in the stock market. The legislature made the policy choice in the years of surplus that as soon as the state paid back the CBR, it would use the SBR and place money in the public education fund, the higher education fund, and other funds that did not have the CBR's strings.

Representative Rasmussen asked why, when there was an opportunity to invest money and to see large returns, the legislature chose to invest in the CBR instead of the ERA. She wondered if anything prohibiting the legislature from doing something like that.

Mr. Painter explained that the legislature would have had to appropriate the money out of the CBR. The earnings made by the CBR stayed in the account. If the legislature appropriated the funds out, it would owe the money back. At the time, when the balance of the SBR was several billion dollars, the state invested the funds. The earnings were counted as UGF in those years. The Constitutional Budget Reserve earnings were held by the CBR. The decision at the time was to build the CBR through investments. However, the money was still locked in the CBR.

Representative Rasmussen commented that as legislators it was often easier to do the right thing when the public was demanding accountability. Although the public was not screaming about replenishing the CBR, she felt policy makers had a moral obligation to make every effort to follow the constitution which was put in place by Alaskans in the 1970s.

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Representative Edgmon defended the legislature, as there were many years in which it chose to put money into the

Permanent Fund via special appropriations and not into the CBR. He indicated the CBR was capitalized largely in the 2000s when oil production was still fairly healthy and the price of oil was high. He noted Representative Wool talking the other day about how 10 years prior oil money brought the state over \$8 billion and in the current year anticipated oil revenues were expected to be about one-tenth of that amount. At one point money coming into the CBR largely from oil revenue was beyond extravagant.

Representative Edgmon remembered money being put into the Permanent Fund which currently had a balance of about \$76 billion. Large allotments of money being placed into the fund resulted from decisions made through the use of the appropriation process by the legislature. He did not believe the legislature had been dismissive of the future needs of Alaskans. He agreed with Representative Josephson that the repayment of the CBR was lower on the priority list for surplus funds. He mentioned the hey day of surplus funds in 2007 and 2008.

Mr. Painter continued to slide 22: "Fiscal Summary: Governor's Budget with Statutory Funding of Statewide Items." The slide showed what the governor's budget would look like if the statutory formulas were fully funded. The amount would be \$78.9 million increase shown in red. He noted the next fiscal model would use the amount, but future models by LFD would not show the amount. Adding the \$78.9 million to fully fund the other statutory formulas would increase the CBR draw to \$124 million causing the CBR balance to drop at the end of FY 22.

Mr. Painter turned to the charts on slide 23 showing the fiscal model of the governor's budget with statutory funding of statewide items. He highlighted that the fiscal model resulted in an FY 22 deficit. However, in future years it would have less of an impact. He explained that the largest amount was school debt reimbursement and with the moratorium on new debt was extended since 2015, the amount would drop off substantially over the following few years as prior debts were paid off. The division assumed that after FY 25 the state would not build in new projects. However, in reality, he assumed there would be additional projects.

Mr. Painter scrolled to slide 24: "Fiscal Model: Budget with Typical Fund Sources, No COVID Offsets, Statutory

PFD." The slide showed the budget with only the adjustments for unusual funds and Covid funding. The slide also reflected the statutory PFD from FY 22 through FY 30 and showed the gap. In FY 22 the state would be left with a \$2.1 billion deficit which would fluctuate in the out year. The gap would range from \$1.5 billion to \$1.9 billion. Assuming the state was paying the statutory PFD, it would need to overdraw the ERA and completely deplete the fund by FY 29. He suggested that the legislature was to pay a full statutory dividend, the slide showed the gap that would need to be filled each year. He was not suggesting that it was not affordable or impossible, he was reporting the size of the gap if the legislature were to pay the statutory dividend.

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Representative Josephson recalled Governor Walker stating that if the state continued to lack revenue, paid out the full dividend, and continued to rely on oil, it was unlikely there would be a dividend in the future. He suggested Mr. Painter was illustrating the PFD would end in about 6 years with a full dividend and status quo budgets. The state would no longer have \$3 billion to spend on basic services although there would still be income generated from the corpus into the ERA. He concluded that the dividend discussion would simply disappear, as there would be no money to pay it. He asked if he was accurate. Mr. Painter thought it was a policy decision about what the legislature would be cutting.

Representative Josephson asked what kind of new income the state could see in a typical year from the corpus without ongoing ERA to buttress the flow. Mr. Painter replied that LFD's models assumed no changes to APFC's investment policy. The Alaska Permanent Fund Corporation had stated that if the legislature consistently overdrew the ERA, they would have to make management changes in order to ensure they had the cash to make those draws. The changes might result in less earnings depending on the persistency of the overdrafts which might change the corporation's investment policy. A single draw might cause the corporation to stop investing in some of their riskier assets. Multiple overdrafts might lead them to move to a much more conservative cash-heavy portfolio.

Mr. Painter discussed the charts on slide 25: "Fiscal Model: Budget with Typical Fund Sources, No COVID Offsets, and 50/50 POMV Split." The slide reflected switching to a PFD in FY 23 of 50 percent of the POMV draw, the plan the governor was proposing. However, the slide did not reflect the governor's budget that also incorporated some reductions. He indicated that for a 50/50 POMV split, the size of the gap would be from \$1.3 billion to \$1.5 billion. It was a smaller gap than if the statutory dividend was paid, but a gap would still exist requiring other fund sources in order to avoid overdrawing the ERA. He reiterated that the 50/50 split dividend amount was lower than the current statutory dividend amount which would stretch the ERA farther out to FY 30 before being exhausted.

Mr. Painter reviewed slide 26: "Fiscal Model: Budget with Typical Fund Sources, No COVID Offsets, and \$1,000 PFD." The slide showed a dividend of \$1000 similar to the amount appropriated in the current fiscal year, \$992.00. It also showed a persistent gap each year of between \$240 million to \$600 million in FY 23. There would still be overdrafts from the ERA through the period reflected on the slide. However, the fiscal gap would not be as large as some of the other scenarios he had proposed. Even with a dividend of \$1000 and based on the current revenue forecast, the state would still have a fiscal gap of between \$300 million to almost \$800 million.

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Representative Carpenter suggested that the committee was currently talking about only cutting the PFD amount. He had just had a conversation in which the governor acknowledged he had several conversations with the medical community regarding the state's response to covid. The governor had an obligation to look both a medical response and a fiscal response. He could not bring up the issue of cutting the amount of the PFD without considering the private sector. He thought legislators also needed to look at cutting government. In other words, legislators should consider all of the options rather than just one. He cautioned members that some constituents were unhappy with the idea of only propping up government without propping up the private sector. He indicated the issue was a point of frustration for him.

Co-Chair Foster agreed that the legislature needed to look at all of the tools that were available.

Representative Rasmussen was wondering about additional revenue measures. She was trying to understand how different revenue measures would affect the gap. She mentioned the possibility of a sales tax or bringing in new industry. She noted it would take time to implement certain measures. She wondered if there was a point at which the state would not have a deficit even by paying a reasonable dividend of \$1000.

Mr. Painter indicated that if the state enacted new revenue measures or spending reductions it was possible to no longer have a deficit with a \$1000 dividend or larger. The point of the slides was not to say a larger dividend was not affordable. Rather, they were to point out the size of the other things that needed to be done in order to balance the budget. He referred to the previous slide that showed a dividend that was 50 percent of the POMV draw. He suggested the legislature would need to find \$1.3 billion to \$1.5 billion of budget reductions or new revenue in order not to have a deficit with that dividend level. It was the level of other changes that would need to happen if the legislature wanted to pay a dividend based on the 50/50 POMV split.

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Vice-Chair Ortiz agreed with Representative Carpenter that the current type of conversation did not happen very often. However, he opined that it was grossly inaccurate that government had been protected for several years. He referred to slide 5 which showed that budget reductions to government had already been made to all of the state agencies. He thought further reductions would be difficult. Education and health and human services would likely be the targets of additional reductions, as certain departments had already experienced significant cuts.

Representative Carpenter appreciated that the conversation would be difficult when considering reductions to any department. He wanted to remind members that it was important to have the discussion. He suggested that the legislature needed to weigh all of its options including additional revenues. Only reducing the PFD was not the only option. He thought it would be very helpful to keep a

long-term approach to solving the state's fiscal problems rather than myopically looking at the current year's budget. He thought it might be helpful to look at the period prior to the legislature's binge spending from about 2006 to 2014 due to oil wealth. There was a long period in which state revenues were less than the high spending years. He asserted that the state was trying to find its equilibrium and recommended looking at revenues, spending, and population prior to 2006.

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Representative Wool would be leaving for a separate committee and wanted to return to the topic of the CBR. He explained that the legislature drew down the CBR for several years because it did not eliminate the PFD or institute a broad-based tax. He suggested that if the legislature had not drawn down the CBR by \$14 billion, it would have had to institute revenue measures, eliminate the PFD, or both, as the state did not have the money. He understood that people wanted to right-size government to Alaska's current population (higher than 20 years prior). However, in 2010 oil brought in \$10 billion. Presently, oil revenues were one-tenth of that amount. He suggested that perhaps Alaska's government should be smaller but emphasized that revenues were much smaller. The state needed to make adjustments including new revenues. He reported that the federal government had been sending out checks in the amount of \$600 to \$1400 per person, like a divided check. Not everyone received a check; families that made more than \$150,000 did not receive checks. He also pointed out that some people put their checks into savings rather than spending it and stimulating the economy. He suggested the legislature had learned a significant amount from the federal government's dividend programs. He suggested that even the governor stated that \$1.2 billion in revenues would be necessary if the legislature wanted to maintain the PFD program. The legislature had to make these types of decisions in an economy in which oil revenues were one-tenth of what they were in prior times. Oil revenues made up 90 percent of the state's budget previously but only made up 20 percent of the state's revenues currently. He argued that the legislature would have to make some serious adjustments. There was no way around it.

Representative Josephson reported that LFD regularly displayed a single graph that showed, in real spending

terms, the state's bar on the right-hand side in FY 22, was at the height of the mid 1970s. He asked if he was correct. Mr. Painter replied that adjusted for inflation and population it was fairly close to the amount. He noted there were a series of peaks throughout the period. He suggested the state was back to a comparable spending level prior to the current peak in the early 2000s and comparable to the 1970s as well. He could provide a full version of the information.

Representative Josephson indicated that the graph showed that oil came on in the fall of 1977 and showed a parody with the period before oil if accounting for inflation and population. Mr. Painter thought the period before oil would be prior to the start of the pipeline construction. He believed the budget was lower. The period during pipeline construction, when the state was reaching parody, the state had a reserves tax on future production. The state was getting more revenue from oil during that period. Essentially the stat was comparable prior to the construction of the pipeline.

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Representative Josephson thought that when the administration came into power it sought restoration of all of the back dividends to calendar year 2016. The administration no longer talked about that. It talked about completing calendar year 2020 dividend, paying a full dividend in calendar year 2021, and finding \$1.3 million in additional revenue. He asked if his assessment was correct. The administration had changed the discussion because of the complexity of the problem, in his opinion. The administration no longer talked about thousands of dollars in dividends.

Mr. Painter indicated the governor's 10-year plan no longer reflected a payment of past dividends other than the current fiscal year. It was a shift from his plan at the beginning of his administration.

Representative Rasmussen thought it was disingenuous to Alaskans to suggest that an income-based welfare program established by the federal government was equivalent to a share of mineral wealth that was established in Alaska creating a relationship between Alaskans and the state's mineral rights. She had listened to the debate about the

dividends for several years. She thought it would be worth modeling the dividend being tied directly to royalties with a 25/25/50 percentage split. The split would be made up of 25 percent of royalties going directly into the ERA, the POMV draw being observed, and paying 50 percent to Alaskans in the form of a dividend. She thought the split would help build a relationship with Alaskans giving them a stronger desire for more royalties which would mean more production of Alaska's resources. She was very nervous when the legislature talked about income-based payments taking away from what the dividend was supposed to be: Alaskans' share of the state's resource wealth. She opined that it was not right to say that Alaskans could not own any mineral wealth, as they deserved their share.

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Representative Carpenter highlighted a slide from a recent Alaska Permanent Fund Corporation briefing that showed petroleum revenue, non-petroleum revenue, and POMV revenue. He suggested that when the legislature discussed needing to raise \$1 billion in revenue in order to balance the budget, it was talking about raising it from Alaskans. Some Alaskans worked in the petroleum industry and some in non-petroleum industries. The slide showed the period from 2015 to 2023. He thought what was striking about the slide was that state revenue fluctuated over the prior few years, yet non-petroleum revenue had stayed flat. He argued that the majority of Alaskans' incomes came from non-petroleum industries. He disagreed with the idea of raising taxes on Alaskans to pay for services without a plan of growing non-petroleum industries. He thought the state would be increasing the burden to Alaskans. He thought if the legislature was contemplating raising taxes or cutting the PFD, it should also be discussing what policies needed to be put into place to grow the economy. He opposed the notion of simply adding a tax because it would likely encourage people to move out of the state.

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Representative LeBon suggested that the perfect economic storm the state found itself in currently started at least 45 years prior when state leaders tied spending to a non-renewable resource with a finite life. The legislature started spending money based on oil revenue. In the early years of the program revenue was robust and sufficient

enough to cover the appetite of state spending and payout a PFD based on a statute passed in the early 1980s. The Permanent Fund Dividend program worked and government was funded at the level at the time government officials wanted. He thought the populous was likely lulled into a false sense of security because the PFD was being paid per the statute, government was being fed, and everything seemed to be working.

Representative LeBon recalled that there was a sense that the status quo had a longer life than people thought. He remembered when the vote was taken in 1976 to establish the PFD there had been a sense of urgency. Voters believed that oil was finite and the state needed to save some of it for future generations. Thus, the Alaska Permanent Fund was established.

Representative LeBon reported that currently oil still flowed through the pipeline, although it was a finite resource showing signs of decline. He thought the state was at a crossroads where something had to give. He thought it was too bad that 45 years prior the state did not dump all of the royalty earnings from the sale of Alaska's oil into the Permanent Fund and kept the state income tax in place and laid out a plan for the size of government. Currently, the legislature had to reconcile reality. He was afraid everyone would have to share in the pain.

Representative Rasmussen asked if it was possible for LFD to put together a chart together that showed the relationships with the decline in oil revenues and the size of the dividend payment. She thought it would be helpful. Mr. Painter responded in the affirmative.

Mr. Painter presented slide 27 which showed a fiscal model with a \$500 PFD. There was essentially no gap although there would still be a deficit in FY 22 and FY 23. In future years there would not be a gap based on the revenue forecast. He indicated the slide showed a surplus increasing because revenue was increasing with inflation.

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Mr. Painter continued to slide 28: "Fiscal Model: Budget with Typical Fund Sources, No COVID Offsets, 50/50 POMV PFD, FY 21 Supplemental PFD." The slide showed the governor's supplemental PFD as well as the 50/50 split POMV

going forward. The governor's proposed supplemental PFD for FY 21 and additional draws from the ERA would lead to the ERA running out earlier than the comparable version without the supplemental PFD.

Mr. Painter moved to the swoop graph on slide 29 reflecting all of the governor's proposed appropriations in the current session including supplementals and the regular budget ranked from largest to smallest. The two PFDs stacked together equaled more than \$3.2 billion and, by far, the largest item. d about \$

Mr. Painter discussed the final slide, slide 30: "Impact of FY 21 - FY 22 Overdraws on ERA Balance and POMV Draw." The slide showed the impact of the governor's proposed FY 21 and FY 22 overdraws of the POMV draw. It reduced the POMV draw in the future by reducing the value of the fund. Over the model period through FY 30, collectively there would be about \$1 billion less in the POMV draw than if the state did not do the overdraws. He concluded his presentation and was available for questions.

Co-Chair Foster thanked the presenters. He reviewed the agenda for the following day.

ADJOURNMENT

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The meeting was adjourned at 3:47 p.m.