

SENATE FINANCE COMMITTEE
January 31, 2022
9:02 a.m.

[9:02:42 AM](#)

CALL TO ORDER

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

MEMBERS PRESENT

Senator Click Bishop, Co-Chair
Senator Bert Stedman, Co-Chair
Senator Donny Olson
Senator Natasha von Imhof (via teleconference)
Senator Bill Wielechowski
Senator David Wilson

MEMBERS ABSENT

Senator Lyman Hoffman

ALSO PRESENT

Deven Mitchell, Executive Director, Alaska Municipal Bond Bank Authority, Department of Revenue; Ryan Williams, Operations Research Analyst, Department of Revenue, Juneau.

SUMMARY

^STATE DEBT and CREDIT RATING

[9:04:39 AM](#)

DEVEN MITCHELL, EXECUTIVE DIRECTOR, ALASKA MUNICIPAL BOND BANK AUTHORITY, DEPARTMENT OF REVENUE, introduced himself. He discussed, "January 2022 Credit Review and State Debt Summary" (copy on file). He addressed slide 3, "State of Alaska and Other 49 States' Ratings."

Co-Chair Stedman requested some historical data around credit ratings.

Senator Olson queried the main reason for the downturn in the credit rating.

Mr. Mitchell replied that the state was already in a difficult position because it did not conform to many metrics used by credit agencies. He stated that the state had a small population and a high revenue. The revenue was historically oil and gas driven, which had high volatility. He also noted that the state did not have a broad-based tax. He stressed that the combination resulted in a difficult analysis.

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Senator Olson gathered that a broad based tax would ensure a pathway to balance the budget.

Mr. Mitchell replied that he did not believe that he said that, but stated that the state had not yet instituted a broad based tax.

Senator Wielechowski wondered whether there should be an expectation of an increase in the state's credit rating because there had been an increase in the price of oil.

Mr. Mitchell replied that it was easier to "go down" in credit rating rather than "go up", but the increase in the price of oil was a part of the positive story that the state could tell the credit agencies.

Co-Chair Stedman pointed out that the numbers showed that the budget was balanced using federal funds, and not state revenue.

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Mr. Mitchell pointed to slide 3, "Municipal Market Update: Market Commentary":

From January 13th to January 20th, AAA MMD increased 8 to 10 basis points across the curve.

MMD/UST ratios for the 5Y, 10Y and 20Y increased to approximately 56 percent, 70 percent, and 84 percent respectively.

For the week ending January 20th, municipal bond funds experienced outflows of \$238 million after experiencing inflows of \$231 million the previous week. This marks the first reported outflows since March 2021.

The new issue calendar for next week shows approximately \$6.3 billion in total par, composed of \$5.1 billion in negotiated deals and \$1.2 billion in competitive sales.

Co-Chair Stedman queried the basis point.

Mr. Mitchell replied that the basis point was a hundredth of a percent.

Co-Chair Stedman remarked that the inverted yield curve had been a predictor of a recession, and asked for more explanation on that issue.

Mr. Mitchell replied that inverted yield curves typically occurred when investors felt that the future would have issues with the ability to obtain quality investments.

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Co-Chair Stedman surmised that there would be a flat curve if there was no prediction of a recession.

Mr. Mitchell agreed.

Senator Olson wondered whether the change in federal rates would have an effect on the state's credit rating.

Mr. Mitchell replied that the state would be making more on the invested fixed assets, but a loan would result in a higher interest expense.

Senator Olson wondered whether the bond bills would be good for the state in the long run.

Mr. Mitchell replied that the current interest rate environment was extremely low, and felt that a slight interest rate increase would still be very low.

Mr. Mitchell wondered whether the committee would like a verbal history.

Co-Chair Stedman replied in the affirmative.

Mr. Mitchell offered a brief history of the state's credit rating.

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Senator Olson remarked on the Senate Finance Committee chairmen at the time of the decline in the state's credit rating.

Co-Chair Bishop noted that Alaska did not fit the metrics of the rating agencies.

Mr. Mitchell discussed slide 4, "Long Term Challenges Remain, but Improvement in 2022":

Same Challenges:

- How to spend the structured percent of market value draw from the Alaska Permanent Fund -Permanent Fund Dividend versus State services
- How to manage the state's budget into the future, there is a general consensus that there is a need to either spend less or generate more revenue at the State level but finding common ground on options has proven difficult
- The 10 year fiscal outlook still reflects deficits from fiscal year 2024 through 2029
- Assumptions on investment income assumptions and budget inflation questioned
- Reserve flexibility diminished; Constitutional Budget Reserve balance was approximately \$1.2 billion on 6-30-21

Improvements since 2015:

- Significant reduction in state general fund spending
- The transfer from the Permanent Fund has been defined through a Percent of Market Value structure
- Even though they include one-time revenues, projected balanced budgets for fiscal years 2022 and 2023
- Improved oil price environment and production expectations in Fall 2021 Revenue Sources Book

- Significant improvement in the funding ratios of PERS and TRS which actuarially is 85.5 and 92.5 percent respectively
- The large balance of the Constitutional Budget Reserve Fund allowed decisions on how to change how (and how much) the State spends, or how it generates revenue to be deferred for the last six years

Long-term Rating Agency Concerns:

- Comparatively large net pension liability
- Narrow economy that is relatively small
- Perception that the majority of operating revenues and the State's economy are primarily reliant on petroleum development
- Difficulty in building consensus for financial structure change

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Senator Wielechowski wondered whether the long legislative session in the previous year had a negative impact on the credit rating.

Mr. Mitchell stated that there was a managerial component in the credit analysis, so difficulty in making managerial decisions would have an impact on the rating.

Co-Chair Bishop stated that North Carolina had a very good credit rating, but it took over two years to pass their operating budget. He wondered whether federal dollars were factored into the rating.

Mr. Mitchell replied that federal dollars were not considered in the rating, but had a GDP target.

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Co-Chair Stedman wondered whether the rating agencies examined the audited financial statements.

Mr. Mitchell replied in the affirmative.

[9:39:11 AM](#)

Mr. Mitchell looked at slide 5, "Alaska's Most Pressing Credit Rating Challenge":

- The CBRF receives additional dispute resolution deposits and restricted earnings
- Post FY2019, it was determined that adjustments to the CBRF account balance was necessary for dispute resolution deposits originally deposited to the General Fund
- In FY2021, GF expenditures include a transfer to the SBRF of \$325 million

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Co-Chair Stedman surmised that the net position of the state included the Earnings Reserve Account (ERA) of the Permanent Fund.

Mr. Mitchell replied in the affirmative.

Co-Chair Stedman wondered whether the SBR was included in the chart on the graph. He stated that Mr. Mitchell could provide that information at a later date.

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Senator Wielechowski queried the second bullet on the chart.

Mr. Mitchell replied that it was the legal dispute about certain deposits inappropriately placed in the CBR.

Co-Chair Stedman remarked that the discussion could be had with the auditor.

Mr. Mitchell remarked that the legislature had historically forward-funded education, so that was used in the timeframe since 2015.

[9:48:07 AM](#)

RYAN WILLIAMS, OPERATIONS RESEARCH ANALYST, DEPARTMENT OF REVENUE, JUNEAU, displayed slide 7, "State Debt Obligation Process":

All Forms of State Debt are Authorized First by law
-May be a one-time issuance amount or a not-to-exceed issuance limit in statute

-General obligation bonds must then also be approved by a majority of voters

General obligation bonds are the only debt secured by full faith credit and taxing authority

All State Debt must be structured and authorized by the State Bond Committee

-Includes general obligation bonds, subject to appropriation issues, and state revenue bonds

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

The State has established other debt obligations

-Reimbursement Programs

The School Debt Reimbursement Program or HB 528 reimbursement

Not currently authorized for new debt and periodically funded (was most recently partially funded in 2017, 2020 and 2022, and no appropriation in 2021)

Retirement Systems

Unfunded actuarially assumed liability (UAAL) for defined benefit employees is guaranteed by the Constitution

Annual payments on the UAAL of other employers is reflected as State debt in the CAFR

Some flexibility in how payments are made

[9:50:51 AM](#)

Co-Chair Stedman queried the numbers used for the slide.

Mr. Williams replied that there was reference to the annual Comprehensive Financial Report for 2021.

Co-Chair Stedman wondered whether the market return or actuarial smoothing was used in the presentation.

Mr. Williams agreed to provide that information.

Co-Chair Stedman noted that the committee would examine the status in the reports.

Senator Wielechowski wondered whether a failure to pay in the School Debt Reimbursement program would impact the credit rating.

Mr. Williams replied that those obligations were subject to appropriation, so he would not expect an impact on the credit rating.

Senator Wielechowski wondered whether a law to enable borrowing would impact the credit rating.

Mr. Mitchell replied that that unissued authorized debt would require a hedging process. He noted that there were a couple of items on the books that were no longer legal, so they were no longer considered impactful to the state.

[9:55:17 AM](#)

Co-Chair Stedman wondered whether the state could issue debt on the operating budget.

Mr. Mitchell replied that the constitution stated that there could only be general obligation debt to capital projects.

Co-Chair Stedman spoke of previous concerns about borrowing and spending. He expressed concern for the burn rate and depletion of state savings. He spoke of a negative figure of \$1 billion since the administration began and hoped that things would see improvement.

Senator Wilson asked whether there were debt borrowing laws on the books that were no longer legally effective.

Co-Chair Stedman mentioned the railroad and market risk levels issuing bonds.

Mr. Mitchell replied that the next slide would speak to three statutory frameworks created over the years for various funding through bonds that the construct of the financing.

[10:00:47 AM](#)

Senator Wilson asked whether the administration had language to fix the statute.

Mr. Mitchell replied in the negative.

Senator von Imhof was online and appreciated the conversation. She stressed the importance of examining of cash flow.

[10:02:01 AM](#)

Mr. Williams looked at slide 8, "Total Debt in Alaska at June 30, 2021." The slide listed various state debt and the state agency debt by type. The figures, in million, referred to principal outstanding, interest to maturity, and service to maturity.

[10:04:26 AM](#)

Co-Chair Bishop asked about the outstanding in the general bonds in state debt, and whether it was from the sale in 2012.

Mr. Mitchell replied that it was a combination of bond propositions over a range of time.

Co-Chair Bishop asked about AEA and the \$102 million to maturity Ms. Fowler those bonds to be paid off in 2022.

Mr. Mitchell replied that he could not speak to that issue.

Mr. Mitchell continued his comments about not using banks that did not support oil exploration.

Co-Chair Stedman requested in writing the list of banks.

Mr. Mitchell agreed to provide that information.

Mr. Williams looked at slide 9, "Total Debt in Alaska at June 30, 2021." The slide listed state and state agency debt by type and in millions. The total debt was \$11.9 billion.

[10:09:42 AM](#)

Senator Wilson asked whether the state had recently retired any debt.

Mr. Mitchell replied in the affirmative, and noted that upcoming slides would address those retired debts.

[10:10:38 AM](#)

Co-Chair Stedman asked about any bonds that would be considered "callable."

Mr. Mitchell replied that there was approximately \$55 million in debt that would be "callable" in 2022.

Senator Wilson asked about the 2006 Tobacco Settlement Asset back bonds.

Mr. Mitchell replied that Alaska, and 46 other states, entered into a settlement agreement with the tobacco companies in 2006. Those revenues were a way of funding capital budgets at the time, and a way for the state to divest from the majority of a partnership with the tobacco industry.

Senator Wilson recalled that the funds would be in accounts that were considered designated general funds (DGF).

Mr. Mitchell replied that the fund had been earmarked for smoking cessation efforts.

Senator Wilson asked whether sweeping those funds would put the state out of compliance.

[10:15:06 AM](#)

Co-Chair Stedman remarked that there was a concern about cash flow related to those funds.

Mr. Mitchell recalled that there was some concern because of the structure of the bonds, but stated that the refinancing stated that the settlement revenues would be sufficient to pay the debt service to maturity.

Co-Chair Stedman asked for more information at a later date on the subject.

Senator Wielechowski wondered whether the administration used revenue anticipation notes.

Mr. Mitchell replied that revenue anticipation notes had not been used since the 1960s.

Mr. Mitchell discussed slide 11, "Debt Affordability Analysis":

Annual analysis required by AS 37.07.045 to be delivered by January 31

Discusses credit ratings, current debt levels, history, and projections

Relies upon debt ratios, limit of 4 percent for directly paid state debt, and 7 percent when combined with municipal debt that the state supports

Identifies currently authorized, but unissued debt

Establishes refinancing parameters

Determines a long-term debt capacity at current rating level

Discusses, but doesn't define, a capacity for short-term debt

The 2022 analysis determined that the State conservatively had a debt capacity of \$1,350 million

-Adjustments made to base analysis to account for POMV split for PFDs vs state budget, special funding for PERS/TRS and future budget uncertainty

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Co-Chair Stedman asked about the risk adjustment.

Mr. Mitchell replied that the analysis currently did not have a "smoothing" type of input for revenue projection, which resulted in more volatility.

Mr. Mitchell addressed slide 12, "Authorized Bonding Authority and Outstanding Obligations":

- The State currently has no legally authorized but unissued general fund obligations
- As of June 30, 2021, the State had debt obligations secured and paid by the general fund of approximately \$663.0 million of general obligation bonds
 - \$18.7 million of Certificates of Participation
 - \$172.1 million of lease-revenue bond conduit issues of political subdivisions
- The State's liability under the SDRP was \$560.9 million
- Annual principal repayments over the next five years are:
 - GO bonds \$40 to \$50 million
 - Lease bonds \$14 to \$20 million
 - SDRP approximately \$60 million

[10:25:23 AM](#)

Senator Wielechowski asked about the \$110 million authorization in 2021.

Mr. Mitchell replied that it was transportation projects authorized in the in General Obligation Transportation Act.

Senator Olson queried the meaning of the first bullet on slide 12, "The State currently has no legally authorized but unissued general fund obligations."

Mr. Mitchell replied that it was general obligation funds paid, which included the lease on the list.

Mr. Mitchell pointed to slide 13, "Current General Fund Annual Payment Obligation":

GF Payment peaked in 2018 at \$225.2 million

FY2022 GF Debt service payments include approximately \$96.2 million in State GO and State Supported debt, and approximately \$35 million for State Supported municipal debt

PERS/TRS special funding is many times all other state commitments

[10:31:02 AM](#)

Senator Olson queried the frequency of the state assisting municipalities in debt.

Mr. Mitchell replied that there were a couple of instances where the state assisted communities in times of financial difficulty, but it was fairly rare.

Senator Olson wondered whether the graph should cause alarm from a liability standpoint.

Mr. Mitchell replied in the negative because there was declining debt in a mature portfolio.

Co-Chair Stedman discussed housekeeping.

#

ADJOURNMENT

10:38:23 AM

The meeting was adjourned at 10:38 a.m.