

HOUSE FINANCE COMMITTEE
January 24, 2024
1:34 p.m.

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CALL TO ORDER

Co-Chair Johnson called the House Finance Committee meeting to order at 1:34 p.m.

MEMBERS PRESENT

Representative Bryce Edgmon, Co-Chair
Representative Neal Foster, Co-Chair
Representative DeLena Johnson, Co-Chair
Representative Julie Coulombe
Representative Mike Cronk
Representative Alyse Galvin
Representative Sara Hannan
Representative Andy Josephson
Representative Dan Ortiz
Representative Will Stapp
Representative Frank Tomaszewski

MEMBERS ABSENT

None

ALSO PRESENT

Alexei Painter, Director, Legislative Finance Division

SUMMARY

OVERVIEW: FY 2025 FISCAL OVERVIEW BY THE LEGISLATIVE FINANCE DIVISION

Co-Chair Johnson reviewed the meeting agenda.

^OVERVIEW: FY 2025 FISCAL OVERVIEW BY THE LEGISLATIVE FINANCE DIVISION

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ALEXEI PAINTER, DIRECTOR, LEGISLATIVE FINANCE DIVISION, provided a PowerPoint presentation titled "Overview of the Governor's FY25 Budget," dated January 24, 2024 (copy on file). He reviewed the presentation outline on slide 2:

- Update on Fiscal Situation
- Fall Revenue Forecast
- FY24 Update - Energy Relief, Supplementals
- FY25 Governor's Budget
- Long-Term View

Mr. Painter turned to slide 3 titled "UGF Budget and Revenue, FY19-FY25 Governor's Budget." He explained that FY 19 was the first year of the percent of market value (POMV) draw from the Permanent Fund and reflected the start of the state's current fiscal system. The chart background reflected petroleum revenue in green, non-petroleum revenue in orange, and POMV revenue in purple. The bars reflected the budget for each fiscal year including undesignated general funds (UGF) agency operations (the day-to-day cost of state government) in blue, statewide operations (operating costs that did not fit into an agency budget e.g., debt service or retirement payments) in red, capital budget in gray, and the Permanent Fund Dividend (PFD) in light blue.

Mr. Painter detailed that when the budget exceeded revenue there was a deficit, whereas revenues exceeding the budget reflected a surplus. Since the implementation of the POMV draw there were two years with budget surpluses (FY 22 and FY 24) and four years with deficits (FY 19 through FY 21 and FY 23). The governor's budget proposed a deficit in FY 25. He relayed that despite the mixed results, the state's savings balances had been pretty steady over the period because the surpluses had made up for the deficits in terms of draws from reserves. In the beginning of FY 19 there was about \$2.7 billion combined in the state's two primary budget reserves the Constitutional Budget Reserve (CBR) and Statutory Budget Reserve (SBR). In the end of FY 23, the accounts were estimated to have a combined \$2.7 million. The slide showed there had been relatively balanced budgets since the implementation of the POMV draw. Particularly in the past several years when there had been difficulty obtaining a three-quarter vote for a CBR draw, it meant there had to be balanced budgets. He noted there had been a successful three-quarter vote in FY 23 when the

supplemental had resulted in a deficit; however, when the budget had been built it had to balance because there had not been sufficient votes for a CBR draw.

Mr. Painter explained that the result had been relatively balanced budgets. He relayed that there was still a structural budget deficit, which he would talk more about when discussing the long-term view. He elaborated that if all of the current statutes were followed, there would be a budget deficit. The governor's FY 25 budget included a statutory PFD, resulting in a deficit of approximately \$1 billion. In past years, the PFD and capital budget amounts had varied based on available revenue resulting in roughly balanced budgets. There was a gap between the reality of budgeting year-by-year based on available revenue (mostly varying the PFD and capital budget amounts) and the current statutes including a statutory PFD resulting in a deficit.

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Representative Galvin appreciated the slide and found it easy to read and interpret. She remarked it was easy to see when the budget was not balanced when the [light] blue portion of the bar moved above the purple [revenue]. She presumed the FY 25 bar reflected a statutory PFD. She understood that the PFD was north of \$1,000 in FY 24. She asked what FY 25 looked like with a statutory PFD and what the number would need to be to avoid a deficit.

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Mr. Painter answered that in FY 24, the legislature appropriated 25 percent of the POMV draw to the PFD. The total was \$881.5 million with a per person payout of \$1,312. In FY 25, the estimated statutory PFD was \$2.3 billion. He noted the amount was still an estimate because it relied on investment returns in 2024. He relayed that \$2.3 billion would pay about \$3,500 per person. He noted the exact number was included on a future slide.

Representative Galvin stated her understanding that with a statutory PFD there was a deficit of approximately \$1 billion in FY 25. She asked for verification that the number was not inclusive of discussions around public education and other items.

Mr. Painter agreed. The deficit under the governor's budget was slightly less than \$1 billion. He would discuss how the budget may increase throughout the legislative process on subsequent slides.

Mr. Painter moved to a chart on slide 4 titled "Daily ANS Price, November 2021 - January 2024." The chart reflected the volatility of Alaska North Slope crude prices ranging from \$70 to \$125. He detailed that in the past year prices had peaked near \$100 and were in the upper \$70s in the past several days. At current prices and under the current revenue forecast, the amount of revenue the state received for every dollar increase to the price of oil was about \$45 million to \$50 million. He highlighted that prices changed by \$1 daily. He explained that the legislature's challenge was turning the volatility into a more stable budget. He stated that it would seem the state would go from "broke to rich" on a month-to-month basis when following the trends from day-to-day; however, in reality there had been a relatively stable forecast for the period.

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Representative Stapp referenced Mr. Painter's remarks about a \$1 increase in oil price resulting in an additional \$50 million in revenue. He noted that the Department of Natural Resources (DNR) had recently presented to the committee and it had been noticeable that the current revenue in excess of the [forecasted] \$73 per barrel used in the budget was around \$210 million despite a \$9 increase in the average oil price. He estimated that because of lower production and capital expenditures for ongoing North Slope projects, it seemed \$1 per barrel resulted in closer to \$20 million as opposed to \$50 million.

Mr. Painter responded that he would answer the question when he addressed a future slide on the change in forecast.

Co-Chair Johnson noted that Co-Chair Foster had been present since the beginning of the meeting.

Mr. Painter addressed a chart on slide 5 titled "Investments: History and Projections." The slide showed a history of some of the state's investment revenue with the blue line reflecting actual investment returns of the Alaska Permanent Fund Corporation (APFC) and the red line reflected the performance of the Public Employees'

Retirement System (PERS) invested by the [Department of Revenue] Treasury Division. He highlighted that historically the two lines moved in tandem with markets and performed very similarly over the past decade. Going forward, PERS was slightly higher than APFC, while historically it had been slightly opposite. He emphasized that budgeting from year-to-year based on investment returns would result in extreme volatility in the availability of revenue. He elaborated that instead, the volatile revenue source was turned into a more stable source by applying a POMV of the Permanent Fund. He clarified that the budget was not based on returns from year-to-year, but on an average of the value over a given time period, which resulted in a stable draw.

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Mr. Painter turned to slide 6 titled "Percent of Market Value Draw from Permanent Fund." He explained that the FY 24 POMV was based on 5 percent times the average of the total balance of the Permanent Fund from FY 18 through FY 22. The result was \$3.5 billion. The FY 25 draw of \$3.66 billion was an average of the FY 19 through FY 23 balances. He remarked there had been substantial discussion in the building about whether a 5 percent POMV draw was the right number. It was often mentioned that while the fund was increasing, the effective amount drawn was less than 5 percent of the current balance because the formula averaged historical years. He elaborated that the FY 24 draw was about 4.6 percent of the last year of the average and the FY 25 draw was about 4.7 percent of the last year of the average. However, there was a large spike in value in FY 21; therefore, in two years the effective draw could be higher at 5 percent because the market spiked and then went back down. He explained that the rising market worked to have a reduced draw at present; however, in a couple of years if investment results did not improve, it was possible it would not result in a lower draw as it had in the past.

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Mr. Painter advanced to slide 7 titled "Earnings Reserve Account (ERA) Sufficiency." He noted that the House Finance Committee and the APFC Board of Directors had talked about the concern over the sufficiency of the ERA to make the POMV draws. The calculation was very stable, but the

ability to make the payments was not necessarily guaranteed each year because the value of the ERA had to be sufficient. He explained that that the Permanent Fund had two accounts including the principal, which could not be spent, and the ERA. The state could only spend realized income from the ERA. He explained the statutory net income calculation where investment returns were realized as assets were sold or dividends, interest, or rental payments were received. The projected statutory net income was currently lower than the total return. He noted it had not always been the case, but it often was. For FY 25 and beyond, APFC projected it would receive 6.65 percent of its value in statutory net income. He elaborated that inflation of 2.5 percent and a 5 percent POMV draw exceeded the 6.65 percent. The resulting forecast projected a decline in the ERA balance going forward.

Mr. Painter reviewed a graph at the bottom of slide 7 titled "Realized ERA Balance: FY22-FY33." The graph came from APFC's History and Projections Report from November. The blue portion of the bars reflected the following year POMV draw, and the red reflected the projected remainder of realized and expendable ERA funds. The chart showed the realized ERA balance was projected to decline year-over-year. He noted the large drop from FY 22 to FY 23 was due to very high inflation. He expounded that the inflation proofing transfer was based on actual inflation, which was 8 percent, resulting in a transfer of \$4.2 billion. The chart showed that by FY 33 based on a straight line projection, there would be \$4 million in the ERA beyond what was needed for the next year's POMV. He stated, "that's definitely cutting it close." However, in a probabilistic world where there were not straight line investments, there was a higher risk of an insufficient ERA balance.

Mr. Painter detailed that LFD's probabilistic modeling showed a 54 percent chance of having an insufficient ERA balance to make the full POMV draw over the FY 25 to FY 33 period assuming annual inflation proofing. The probability of an insufficient ERA balance dropped to 39 percent if inflation proofing was suspended when the ERA balance dropped below the following year's POMV draw. He clarified it was a policy intervention the legislature could make.

Mr. Painter noted that in 2023, the legislature recognized the problem and took action. The House Finance Committee

did not include inflation proofing in its budget and the Senate budget capped the inflation proofing transfer at the equivalent of 2.5 percent inflation. He elaborated that the U.S. Consumer Price Index (CPI) actual inflation for calendar year 2023 turned out to be well above 2.5 percent; therefore, the cap resulted in around \$1 billion remaining in the ERA rather than being transferred. He noted he did not assume the legislature would draw the balance to zero.

Mr. Painter addressed the reason realized income was low (in the last bullet point on slide 7). Much of the reason for low realized income was due to the APFC investment allocations. He elaborated that APFC's private equity investments had not dropped much during the negative markets of recent years because companies did not conduct investment rounds during down markets as their valuations would go down. As a result, 70 percent of the unrealized gains that could become future realized gains were in illiquid assets (private equity, private income, and real estate). He explained that APFC would not sell its mall investment in Virginia to realize income because it was an income producing asset, but part of the unrealized gain balance was the increase in the value of the property since its purchase.

Mr. Painter expounded that APFC did not necessarily control when it exited private markets because it wanted to wait to cash out its investment until a company went to an IPO [initial public offering]. He noted it may mean the investment may not generate income for the fund for years. The result had been less realized income in recent years because the fund did not have a stockpile of unrealized gains currently. The forecast going forward relied on a rising equity market to create realized gains. He believed the high likelihood of an insufficient balance reflected the chance that a poor performing equity market could mean the absence of gains for an extended period.

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Co-Chair Johnson noted that Co-Chair Edgmon had joined the meeting.

Representative Stapp asked if LFD had considered that the legislature may not take a full POMV draw. He stated that choosing to not take a full POMV draw would dramatically reduce the potential risk exposure down the road.

Mr. Painter answered that it was one of the ways to mitigate the risk. He emphasized that he was not including the slide to communicate the state was doomed. The purpose was to point out a potential problem that could be handled with a number of policy levers available to the legislature. One option would be to reduce inflation proofing and another was to reduce the state's draws. He stated that either could result in ameliorating the problem.

Co-Chair Edgmon believed the probability of the legislature not taking a full [POMV] draw was low. He thanked Mr. Painter for devoting a slide to the topic. He did not think enough legislators or decision makers in the general public really understood the full impact of the meaning of statutory net income and depending on the market how slippery a slope it could be if all of the factors went against the fund relative to liquidity, the value of the ERA, and the legislature's inability to take corresponding action. He believed it was the reason legislation to create an endowment was needed. He underscored the importance of the information on the slide.

Representative Ortiz asked to what degree the problem would be partially resolved if the ERA was eliminated to create one fund and the annual draw was limited to a certain amount of the fund's total value. He asked if the action would alleviate the issue.

Mr. Painter responded affirmatively. He stated that if the POMV draw was constitutionalized and the ERA was collapsed into a single endowment with the principal, there would be no ERA or sufficiency concern. The legislature would be able to take 5 percent from the fund, which was how most modern endowments were structured. He explained that the two account structure had been common when the Permanent Fund had been set up in the 1970s and was very uncommon in endowments at present. He highlighted that the legislature had taken a similar step with the Public School Trust Fund in 2018. He explained it was an endowment of the state and there had previously been two accounts. He elaborated that there had been numerous problems with how much to spend each year and determining whether there was sufficient funding available. The fund was collapsed into a single endowment and the process had been pretty automatic since then. He concluded that it was something the legislature

had done before and was fitting with the modern way most funds were managed.

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Representative Stapp stated that he believed in fiduciary responsibility. He referenced the ERA draw plus inflation exceeding the total value of the net income in the fund. He stated that if the fund was combined and the legislature took a 5 percent POMV draw on the entire value of the fund and the draw was less than inflation and fund performance, it would effectively draw down the entire Permanent Fund. He asked if his understanding was accurate.

Mr. Painter answered it was the risk with any of the draws. He confirmed that if the total return was less than inflation plus the draw, it would draw down the value of the fund if the full draw continued. He supposed that the ERA provided a limiting mechanism where the spendable money would run out before [the entire fund was depleted]. He hoped the legislature would adjust the draw if needed. He stated that generally when projections showed money would run out, they were really a prompt for the legislature to act. He stated that generally he had found the legislature did act. However, it was possible the legislature could continue drawing the balance of the fund with an unsustainable draw.

Representative Josephson suggested that one way to combat the threat of erosion was inflation proofing. He asked if his statement was accurate.

Mr. Painter answered that if there were a true endowment there would not be anywhere to inflation proof from and to. He believed the legislature would want to set the draw to be no more than the returns minus inflation. He explained that instead of a 5 percent draw it could be a moving target set at actual returns minus the impact of inflation or it could be reevaluated based on actual experience. For example, he had heard one option where the draw was capped in the constitution and the statute could be lowered and changed or a different formula could be established. There were mechanisms to use to ensure inflation was accounted for in the draw percentage.

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Co-Chair Edgmon noted it was not too many years ago that DNR and the Department of Revenue (DOR) forecasts for oil production and oil prices provided an entire revenue picture. He stated it had all changed since the passage of SB 26 [legislation establishing the POMV draw from the ERA]. He suggested that at some point perhaps the committee could have all three entities at the table including oil and investment sides. He stated that slide 7 underscored that the legislature should be budgeting very conservatively going forward.

Mr. Painter turned to slide 8 titled "Fall 2023 Revenue Forecast." He reported that compared to DOR's spring [2023] forecast, DOR's fall 2023 forecast showed higher oil prices in FY 24 and FY 25, but lower oil production, higher lease expenditures, and higher transportation costs. The result was an increase in projected revenue, but by less than price alone would explain. He pointed to the table on slide 8 and noted there was a revenue increase of \$221 million in FY 24, but prices increased by \$9.39 per barrel between the [spring 2023 and fall 2023] forecasts. When considering the price increase it appeared the revenue increase would be larger when multiplying \$9.39 by \$40 million or \$50 million; however, there were other factors to consider. Production was down by 26,100 barrels per day, lease expenditures, which were cost deducted by companies before they began paying their production taxes, were up by \$755 million. He added that transportation costs were also up.

Mr. Painter continued to review the table on slide 8. In FY 25, revenue was up by \$79.1 million, but the price was up by \$6.00. When considering the price increase it appeared revenue would be up by \$300 million; however, reduced production by 34,200 barrels per day and an increase in lease expenditures by \$1.6 billion resulted in less revenue. He remarked that sometimes the price could mask changes going on in the production forecast. He believed DOR and DNR had both indicated when presenting to the committee that the forecast reflected a shift in terms of where the oil would come from in the future and what the state was seeing in production. He stated it was a marked shift in the underlying variables of the production forecast from the prior year.

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Representative Josephson asked if the lease expenditures reflected the anticipation of Willow and Pikka projects.

Mr. Painter replied that he would answer the question on the following slide. He turned to slide 9 titled "Fall 2023 Revenue Forecast (cont.)." He addressed how the production forecast was calculated. He explained that DNR did not include 100 percent of lease expenditures and production for every potential future oil field. He elaborated that DNR used a process called "risking" where it reduced the amount in the forecast because there was a chance it would not happen or that the project would happen after the initial estimate. In 2023, there had been a great increase in certainty in the Willow and Pikka fields, particularly in the Willow project because it had cleared some federal hurdles and the final investment decision by the company, which meant it could be put in the forecast. As a result, the production and lease expenditures were not risked nearly as much as before. The change resulted in higher production in later years and higher costs every year. There was some increase in operating cost due to inflation and other factors in addition to capital expenditures. The big difference was that capital expenditures from the two large new fields were much more certain. As a result, production was far more certain (as shown on slide 10); however, in the short-term, where companies could deduct lease expenditures against their taxes, the state would receive less revenue. The state would receive more revenue once the production came online.

Mr. Painter turned to a table on slide 10 titled "Production FC Difference, Fall 2022 - Fall 2023 RSB (Thousands of BPD)." The slide compared the production forecast from fall 2022 to fall 2023 by unit. The chart highlighted where DNR was looking at more production on the North Slope versus less production compared to a year ago. He highlighted several notable trends. First, there was significantly lower production expected in the Prudhoe Bay and Kuparuk primary (legacy) fields; however, DNR was expecting more production from the Prudhoe Bay and Kuparuk satellites (newer fields). He detailed that the production increases in the outer years offset production declines in the early years. He pointed out that every barrel on the North Slope was not equal because of the gross value reduction (GVR) of new production and because of the differences of land ownership. He explained that the state

would not necessarily get as much from the new fields as it did from existing fields.

Mr. Painter highlighted the second trend in relation to the difference in the fall 2022 and fall 2023 production forecasts on slide 10. The currently producing Greater Mooses Tooth field within the National Petroleum Reserve-Alaska (NPRA) had a large reduction due to production difficulties with a new well. He noted the projected production for the field was much lower than the previous year. He elaborated that the state did not get royalties from the field because the NPRA was federal land; therefore, the impact on the state's revenue was less than it would be on state land. The table showed much higher production in later years due to the impact of Willow coming online beginning in FY 30. The other field on the table largely reflected Pikka increasing. He noted there were some other fields not included in the "other" category. Overall, the table showed lower production in FY 24 and FY 25, but much of it was due to the NPRA and the shift from Kuparuk and Prudhoe Bay [legacy fields] to their satellite fields. There was much higher production in later years, but much of the production was coming from satellites and the NPRA where there was less incoming revenue because of land ownership and potentially the GVR.

Co-Chair Johnson noted that Representative Cronk joined the meeting.

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Representative Josephson complimented LFD on the table on slide 10. He stated that GVR had been reformed by the legislature in 2017 to be time or price limited. He asked for a reminder of the details.

Mr. Painter replied that LFD's economist Conor Bell had compiled the chart based on data from the [DOR] Revenue Sources Book. He addressed the changes made to GVR by the legislature. He explained that if prices exceeded \$70 million for any 12-month period for three years, a field could graduate from the GVR early. Normally it took seven years to graduate from the GVR to the non-GVR production. He explained that DOR's price forecast shown on slide 11 dipped below \$70 starting in FY 28. Consequently, what qualified as GVR eligible and what did not was influenced in the outyears by the price forecast being at \$68 or \$69.

He explained there would be a very different result of what was GVR eligible and what was not if the entire price forecast was run at \$70. He stated that the \$70 number was a very important one because of the GVR calculation, which made it difficult to make a clear comparison of what would get a GVR and what would not. He had spoken with DOR about showing what production from GVR and non-GVR fields would be if prices were \$70 versus \$69. He believed the complicated system made it difficult for people to figure out what would be eligible for GVR or not.

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Mr. Painter advanced to slide 11 titled "Fall 2023 Revenue Forecast (cont.)." He began with a chart on the left showing an oil price forecast comparison from fall 2021 to fall 2023. He highlighted that the price forecasts were all relatively close in the later years with oil between \$65 and \$70 [per barrel] in FY 29. He noted the band was not large. He looked at the chart on the right showing a UGF revenue forecast comparison from fall 2021 through fall 2023 and remarked that revenue was even more tightly banded from the years because as price expectations increased, cost expectations had increased. The difference in revenue was only about \$500 million in the mid to later years between the high and low forecasts. He pointed out that while he had started with a slide showing extreme volatility in oil prices, the futures market the forecasts were based on had been giving a pretty consistent picture of the expectation for oil prices in five to ten years. For long-term fiscal planning, while there was volatility from oil, there had been surprisingly little variation in what the fiscal picture would look like in the medium to longer term, which aided the legislature in generating a long-term fiscal plan. He explained that oil may be going from \$70 to \$100, but the forecasts had not been quite as volatile as day-to-day prices.

Representative Galvin looked at slide 10 and referenced Mr. Painter's statement that each barrel of oil had a different value to the state. She noted that Mr. Painter had mentioned the price point of \$70 and she was thinking about other nuances. She remarked that the state was investing in the new fields by giving up near-term revenue in exchange for expected future revenue. She highlighted that Pikka costs were not immediately deducted because they did not have current production, but Willow costs were. She asked

how much more value the state would get from a Pikka versus a Willow project given the time value of money.

Mr. Painter answered that he was not prepared to weigh in on the time value of money associated with the projects. He confirmed that when Pikka entered production it would have a large amount of carried forward lease expenditures the operator could use against future production. Whereas Willow may have some [carried forward lease expenditures] if it went below zero production tax value, but most of the value of the credits would go against current revenue. He relayed there was a big difference to the state in terms of when the money would be received, but he could not speculate. He added that DOR was updating its Willow project analysis from the previous session for the coming spring forecast. He did not know whether DOR had done a similar analysis for Pikka, which would be very interesting to see.

Representative Galvin recalled that the committee had been told that the state would start seeing things turn around with Pikka in 2026. She remembered thinking the state could hold on and budget conservatively, but she thought the table [on slide 10] indicated the timeframe was more like 2027. She asked if the timeframe had changed or if she had misremembered it.

Mr. Painter recalled that DNR had presented there was a higher likelihood that Pikka would come online a bit later than previously thought as reflected in the large increase shown for FY 27 [in the "Other" row on slide 10]. He advised Representative Galvin to confirm details with DNR.

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Mr. Painter discussed key takeaways of the fall 2023 revenue forecast on slide 12:

Key Takeaways:

- The increased certainty of the Willow project is evident in the forecast: increased lease expenditures and increased future production.
 - The revenue impact to the State is negative while the project is under development and will become positive after it enters production.
- The Fall 2023 forecast anticipates lower production from legacy Prudhoe Bay and Kuparuk units, as well

as Greater Moose's Tooth, and higher production from the satellite units of those legacy fields.

- Despite significant shifts in the fundamentals behind the petroleum revenue forecast, overall anticipated revenue in the medium to long term has not changed substantially since the Fall 2021 forecast.

Mr. Painter elaborated on the last bullet point on the slide. He explained that despite significant shifts in the fundamentals behind the petroleum revenue forecast, the overall anticipated revenue was not significantly different because price increases canceled it out. He noted it was still a significant shift that was worth the committee's attention. He added that some of the impact could be seen in the next several slides on the FY 24 budget.

Representative Stapp highlighted the merits of the Willow project, which reflected the largest economic investment on the North Slope in the history of the state since its legacy fields. He stressed the capital investment was greater than \$10 billion with thousands of new jobs in his district. He had not seen as much activity in Fairbanks in a long time in terms of the staging and development of things going to the North Slope. He remarked that it would be a rough couple of years in terms of the state's revenue picture, but there was a bright light at the end of the tunnel.

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Mr. Painter turned to a graph on slide 14 showing the FY 24 budget at various oil prices. He reported that after the FY 24 budget and the governor's vetoes, there was a surplus of approximately \$292 million based on the spring [2023] forecast. He explained that the FY 24 budget included a provision that split the first \$636 million of UGF revenue received above the spring forecast 50/50 between the CBR and an energy relief payment [to eligible Alaskans] in FY 25. The energy relief payment was expected to pay about \$500 [per person]. He elaborated that if oil prices were higher and resulted in a larger surplus than \$292 million it did not result in an additional spendable surplus. He reiterated that the energy relief payment would top out at \$500 per person and the CBR would receive the remainder.

Mr. Painter continued to review the chart on slide 14. He explained that if prices were lower than the spring forecast, the surplus would be lower. He expounded that prices below \$71 per barrel would result in a deficit. Currently, DOR was estimating an average price of \$82 per barrel at the year-end; therefore, it would take a substantial drop in price to get down to the lower price scenario. At the close of the 2023 legislative session, based on the spring forecast, the forecasted revenue was estimated to start at \$73 per barrel and the split between energy relief and the CBR would top out at \$83 per barrel. He explained that because of the shifts in the revenue forecast, the trigger points had changed to \$78 per barrel and \$90 per barrel, respectively. Based on the fall forecast, LFD estimated that about \$110 million would go into the CBR and the energy relief payment, paying about \$175 per person. He highlighted there was still a budget surplus of \$292 million that would lapse to the CBR if not appropriated.

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Representative Stapp found the situation very concerning because the numbers reflected "huge revenue misses." He pointed to the initial expectation that the [FY 24] budget was based on and balanced at \$73 per barrel, only to find out it actually took \$78 per barrel. He stated, "That kind of house of cards can start getting away from you really quickly." He was interested in suggestions from LFD at a later date on how to ensure better forecasting in the future.

Mr. Painter highlighted that the final investment decision on the Willow project made a big difference to the state's revenue forecast. He thought it had been on the radar during the construction of the FY 24 budget and was part of the reason for the surplus, but there had been risk associated with it. He elaborated that when relying on oil, it was not merely possible to consider price only; the other factors were significant in terms of the amount of revenue available.

Representative Josephson asked for verification that the shift from \$73 and \$83 per barrel to \$78 and \$90 per barrel [highlighted on slides 13 and 14] was due to less production and higher lease expenditures.

Mr. Painter replied affirmatively. The two items mentioned by Representative Josephson were the primary factors. He noted that higher marine transportation costs also played a role.

Representative Hannan asked for verification that LFD depended on DOR and DNR to provide the data for its own analysis. She stated her understanding that LFD was not producing the numbers.

Mr. Painter agreed. He confirmed that LFD used the DNR and DOR forecasts. He explained that because of the nature of the state's revenue much of the data needed for accurate figures was company specific; therefore, LFD could not replicate it without access to confidential taxpayer specific information. He elaborated that the result of having relatively few oil taxpayers and strong confidentiality laws meant it was difficult for the public or LFD to match DOR's numbers.

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Mr. Painter advanced to slide 15 and reiterated there was \$292.7 million of spendable surplus in FY 24. The governor's supplemental request proposed to use \$17 million UGF, which had recently been presented to the committee by the Office of Management and Budget (OMB) director. He highlighted that more supplementals were due the following week. He noted OMB's fiscal summary included a placeholder for fire suppression. He added other potential supplemental items were Medicaid, the Department of Corrections, and other agencies.

Representative Josephson asked for verification that the FY 23 supplemental had been paid for with the CBR.

Mr. Painter confirmed that the FY 23 supplemental included a CBR vote because prices dropped. He explained that actual revenue came in a bit higher than forecast and based on the amount of lapsed appropriations due to high [agency] vacancy rates. He did not know that all or any of the deficit filling language ended up being used. He noted there would be a clearer idea when the state's Comprehensive Financial Report was released, which was statutorily due in December, but LFD was hoping for February or March as had been the case in the past six to seven years.

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Mr. Painter turned to slide 16 titled "FY25 Adjusted Base." He explained that the starting point for building the next year's budget was the adjusted base. He described the adjusted base as a stop between the prior budget and the governor's budget, which was equivalent to the prior year budget minus one-time items plus current statewide policy decisions (e.g., changes to formula programs and salary adjustments based on negotiated increases or health insurance costs) needed to maintain services at a status quo level. He noted it was a bit of a shift from the way the adjusted base was defined in 2023. He explained that removing one-time items and adding statewide decisions made the impact of the governor's policy proposals clear when compared to the adjusted base. He elaborated that the adjusted base provided a cleaner starting point and was typically used as the starting point in finance subcommittees and the legislative process.

Mr. Painter explained that LFD modified the adjusted base for FY 25 to include changes to formula programs. Previously, it was difficult to distinguish policy changes from changes in formula amounts. For example, if the governor was proposing to partially fund a piece of debt reimbursement, it was hard to tell the difference between the policy change and the formula change. He detailed that including the automatic formula changes in the adjusted base helped identify the governor's policy proposals that differed from the previous year's budget. The adjusted base reflected the current policy baseline. He believed OMB planned to use the adjusted base more with the changes as well; therefore, LFD and OMB should be using more similar terminology going forward. He noted that partially funded formula items would use the same formula as the prior year. For example, if school debt reimbursement was partially funded one year, LFD would show the impact of partially funding it again as the adjusted base. He cited the PFD as another example and explained that if it was funded by a (non-statutory) formula one year, the same formula would be used the following year as the adjusted base, which would clearly show the governor's shift back to the statutory draw.

[2:30:14 PM](#)

Mr. Painter turned to slide 17 titled "FY25 Adjusted Base (cont.)." The slide showed one-time items totaling \$165.3 million UGF in the FY 25 budget. He highlighted that more than half of the total was for K-12 additional foundation funding, which had been designated as a one-time item outside the formula. The governor submitted quite a few new Department of Education and Early Development (DEED) programs as permanent items [in the FY 24 budget] and the legislature's budget had switched them to one-time items to review them again in the current budget process. He highlighted a \$5 million increment for the Alyeska Reading Academy as an example. The items had been designated as one-time increments to come out in the base and the governor was asking for most of the items to come back in the FY 25 budget. He noted the items appeared as a change to the adjusted base, but it was really making a one-time item from FY 24 permanent in FY 25. The slide also included items the legislature had added explicitly as one-time items such as the grant to the Alaska Travel Industry Association (ATIA), Alaska Gasline Development Corporation (AGDC), and Alaska Seafood Marketing Institute (ASMI). The items all came out in the adjusted base to create a clean starting point.

[2:31:11 PM](#)

Representative Galvin looked at the \$7.5 million increment for childcare benefits on slide 17. She had not seen it in information provided by OMB. She was grateful to see the increment and asked for details.

Mr. Painter replied that in the FY 24 budget, the legislature had included a one-time increment of \$7.5 million in UGF and federal funding for childcare benefits to enhance declining federal funds as COVID-19 funding was eliminated. He explained that recommendations from the governor's Childcare Taskforce had not yet been finalized and there may be some items from the taskforce included in the governor's forthcoming amended budget. He stated that those funds would be different than the \$7.5 million designated as a one-time item. He reiterated that the items were one-time and would reflect a policy difference if they were included in the governor's amended budget.

Representative Galvin stated her understanding that because the [\$7.5 million] increment was included in FY 24, it was

included on the slide, but it may change depending on the work of the taskforce.

Mr. Painter clarified that the slide showed one-time items from the FY 24 budget that were backed out in the FY 25 adjusted base. He noted that the governor had included some of the items in his budget and may include others. He explained that to get to [the adjusted base] the [one-time FY 24] items were backed out.

Representative Hannan looked at the one-time increments of \$1.9 million for the Public Defender Agency and \$9.5 million for the Division of Public Assistance on slide 17. She believed the funds were for staffing increases and thought some of the funding was for permanent positions and some was for temporary one-year positions to catch up.

Mr. Painter answered that both of the items were multiyear appropriations that were effective across FY 24 and FY 25. He elaborated that the items counted as FY 24 costs, but they would be available over multiple years. The items were not counted against the FY 25 budget because they used previous year's revenue. The governor included additional related items in the proposed FY 25 budget, some of which added to the base.

Representative Josephson understood the purpose of backing the one-time items out to result in a clean view of the base budget. He asked if there was a simple way to show which items the governor had restored if the committee was interested in restoring the items [on slide 17].

Mr. Painter answered that LFD could follow up with the information.

[2:34:39 PM](#)

Mr. Painter advanced a table showing formula adjustments on slide 18 titled "FY25 Adjusted Base (cont.)." There was a reduction in the formula projected of \$30.1 million UGF for K-12 education. Part of the change was due to a shift to the Public School Trust Fund, which offset general funds. The state cost went down by \$27.2 million in the same statutory formula. He noted the reduction was due to a decrease in the state's share going to districts. He explained that basic need was calculated based on the Base Student Allocation (BSA) multiplied by the adjusted student

count and was paid by multiple parties including municipal governments. He elaborated that as property tax values increased in communities, the minimum required local effort increased because it was based on a mill rate of the communities' tax value. He explained that the situation essentially shifted the cost from the state to municipalities. Additionally, there was increased deductible federal impact aid, meaning the state could deduct more. He elaborated that the state paid less but it was not less money going districts; costs were shifted from the state to federal funding. There were student count changes resulting in a \$2.2 million decrease, which was offset by a \$3 million increase from Pre-K funds through the Alaska Reads Act. He remarked that although there appeared to be a decrease to K-12 funding, the amount to districts was almost the same because the change to student count offset by the additional Pre-K funding. There was a shift from state funding to other payers funding the formula.

Mr. Painter addressed a decrease of \$9.6 million to school bond debt reimbursement on slide 18. There was a moratorium on the issuance of new school bond debt from July 1, 2015, to July 1, 2025. Consequently, the amount owed by the state decreased each year. The Regional Educational Attendance Area (REAA) Fund also declined because the two items moved in tandem. The state's contribution to retirement increased by about \$46 million because of higher calculated liability to the funds based on the June 30, 2022 valuations. There was also a cost to the state as an employer (shown on the next slide), reflecting an increase in the state's share paid on behalf of school districts and local governments.

Mr. Painter turned to salary adjustments to the FY 25 adjusted base on slide 19. The first salary adjustment was a \$22.7 million increase (\$11 million UGF) for the state as an employer associated with Public Employees' Retirement System (PERS) and a slight decrease for the state as an employer with the Judicial Retirement System (JRS).

[2:38:55 PM](#)

Mr. Painter briefly highlighted the second row on slide 19 showing an increase in health insurance cost. The slide included a series of union cost of living adjustments from previously negotiated contracts from prior years showing next year costs. He noted the legislature had to approve

the money annually. He pointed out that the slide did not include any new contracts. There were three unions currently in the negotiation process that had until the 60th legislative day to provide the contracts. Additionally, when Representative Josephson's bill had passed several years ago that increased salaries for exempt employees, it had included language specifying that increases to the supervisory unit would go to exempt employees as well. He stated that future legislation would be needed to make that happen. The supervisory unit was currently in contract negotiations and the legislature may want to pass a bill that followed the supervisory unit. He pointed out that it required legislation and would be a future policy choice. He stated that it could be discussion for the legislature later in session, while currently it was merely an unknown cost.

Representative Hannan referred to the intent language in Representative Josephson's legislation about exempt employees following the supervisory unit. She asked if it was followed in one or two years. She stated her understanding it was not currently being followed.

Mr. Painter responded that the supervisory unit was in the middle of a contract that paid employees 3 percent, then 1 percent, then 1 percent. He explained that at the time, the 5 percent increase received by exempt employees was 1 percent more than the supervisory unit had received at the time. In FY 24, the two units had equalized when 1 percent went to the supervisory unit and no increase went to exempt employees. Going forward, to keep pace with one another, a bill would be required to increase the exempt salary schedule. He believed the two were currently roughly the same. He noted that while legislative employees were on 40-hour workweeks like the supervisory unit, not all exempt executive branch employees were on a 40-hour workweek; therefore, they may not be quite comparable in terms of their hours.

Representative Coulombe looked at slide 18 and asked how long the moratorium on school bond debt reimbursement would be needed to retire the debt owed.

Mr. Painter answered that because the debt could be refinanced, some had been refinanced beyond FY 33. He could follow up with the current end date. He added that if the debt continued to be refinanced the payments could be

extended farther into the future. He reasoned that because rates were not as favorable currently, refinancing may be less likely than it was several years back.

[2:43:29 PM](#)

Representative Josephson referenced the moratorium on school bond debt that would sunset in the near future. He assumed major maintenance increased because the state had been uninvolved in inviting districts to invest in new construction. He asked for verification that the governor's bill only covered a couple of schools on the major maintenance list.

Mr. Painter replied that the governor put forward one project from the school construction list and two from the major maintenance list in the capital budget. He would discuss the topic more when he reviewed the capital budget slide.

Mr. Painter turned to a fiscal summary on slide 20 titled "Governor's FY25 Budget." The top row of the table showed the revenue forecast [for FY 24 and FY 25]. He highlighted a decrease of about \$100 million in agency operations on the second row. He noted that due to numerous one-time items in FY 24, the FY 25 agency operations actually reflected an increase over the adjusted base. The big increase in the governor's budget was the PFD going from \$881 million in FY 24 to \$2.3 billion in FY 25. He noted the energy relief payment used FY 24 money for distribution to Alaskans in FY 25. As a result, the governor's FY 25 budget was \$1.175 billion higher than the FY 24 budget (an increase of 19 percent). There was \$292.7 million available in the FY 24 budget for future appropriation or lapse; the governor was currently spending \$17 million of the total. The LFD fiscal summary assumed any unspent surplus went into the CBR. He highlighted that the CBR numbers shown on the slide were higher than those in OMB's fiscal summary because LFD's analysis assumed any unspent funds would go to the CBR. Additionally, LFD's analysis assumed any remaining funds would not be spent without an appropriation, although some amount was likely to be spent.

Mr. Painter turned to slide 21 and highlighted a pre-transfer deficit of \$977 million [in FY 25] and a post-transfer deficit of \$982.3 million, which would deplete the SBR and draw just under \$1 billion from the CBR. The

largest increase was the statutory PFD payment. He relayed that appropriations were above the adjusted base; however, there were several areas where LFD expected the budget to be significantly higher by the time the budget was finished.

[2:46:28 PM](#)

Mr. Painter turned to a snoop graph comparing the FY 24 management plan budget to the governor's FY 25 budget (UGF only) on slide 22. The red bars reflected the FY 24 management plan and blue bars reflected the governor's FY 25 budget. The graph was broken out into type, with the PFD as the largest item in the governor's budget, followed by DEED and the Department of Health (DOH). He noted the PFD was third after DEED and DOH in FY 24. The graph helped show the relative size of various agencies and made it easier to see where big changes resided from year-to-year. He highlighted that the PFD stood out and education was lower, much of which was due to a one-time increment of \$87.4 million in FY 24. He noted significant increases in the Department of Corrections (DOC), the Department of Public Safety (DPS), and the Department of Transportation and Public Facilities (DOT).

Mr. Painter addressed agency operations items in the governor's FY 25 budget on slide 23. There was a \$20.8 million UGF decrease due to the sunset of the Senior Benefits program. He noted an extension of the program would require legislation. There were significant UGF increases to DOC and DOT with a mix of fund source changes and increments to both departments. There was \$17.3 million UGF over the adjusted base for DEED due to one-time FY 24 items the governor was proposing to make permanent in FY 25 (e.g., additional funding to the Alyeska Reading Academy and the Alaska Native Science and Engineering Program). The largest reduction (outside of one-time items) was \$6.2 million to DOH to stop funding for the tuberculosis and congenital syphilis elimination plans. The items were made temporary by the legislature and the governor did not include the funding in FY 25. He noted the funding had been set to end in FY 30.

[2:48:35 PM](#)

Mr. Painter addressed statewide items totaling \$365 million in the governor's budget on slide 24. The governor's budget

fully funded school debt reimbursement, the REAA Fund capitalization, state assistance to retirement, and community assistance at statutory levels. He noted that the governor had vetoed the community assistance funding in FY 24. He detailed that the distribution from the program was based on one-third of the balance of the fund. As a result of the veto, the distribution to communities in FY 25 would be \$20 million. He explained that \$20 million was enough to pay the communities' base payments but not the per capita payments, meaning the impact of the veto would be on high population areas. Funding the full statutory \$30 million would result in a fund balance of \$70 million at the end of FY 25, meaning the distribution in FY 26 would also be reduced but it would still be a bit above the bases.

Mr. Painter addressed other fund capitalizations in the governor's budget on the bottom of slide 24. There was \$5 million for the Disaster Relief Fund. He elaborated that the legislature appropriated \$50 million in the FY 22 supplemental to the fund to try to cover future disasters. No money had been appropriated to the fund in FY 23 or FY 24 due to the large balance. The governor's budget requested an additional \$3 million for the Alaska Liquid Natural Gas (AKLNG) project fund. The budget also included funding for the Alaska Clean Water and Drinking Water funds. The funding had been appropriated two years back, but the department had not yet been ready to move forward with the program at the time. The funding had lapsed, and the department was making the request again in the FY 25 budget.

Representative Stapp recalled that the finance committee had added money into the FY 24 budget for community assistance that had not been in the governor's proposed budget. He stated that the money had been vetoed and the governor had included it in his FY 25 budget. He thought it was strange the governor would veto funding and put it back in the next fiscal year.

Mr. Painter responded that the [statutory appropriation] was one-third the balance of the fund and the fund balance had been \$90 million at the end of FY 23; therefore, \$30 million went out in FY 24. The remaining balance was \$60 million and without a capitalization of the fund, one-third of the balance was \$20 million. He believed the decision to veto the funding in FY 24 and include it in the FY 25

budget was a policy choice by the governor. He could not answer the reason why.

2:51:38 PM

Representative Galvin looked at the swoop graph on slide 22, which she believed provided a clear picture of the state's big expenditures. She observed that spending on education was lower in FY 25. She highlighted that the statutory PFD exceeded \$2.3 [billion] and she thought Mr. Painter had stated the prior PFD was \$1,300. She noted that Mr. Painter had mentioned the budget was unbalanced. She remarked that the PFD had been \$881 million in FY 24. She asked how appropriating funding for a \$1,312 PFD for FY 25 would change the \$1 billion deficit outlook.

Co-Chair Johnson noted that it was very early in the budget process.

Representative Galvin agreed. She noted that many people were talking about whether or not there would be any revenue, what the state would do with it, and statutory versus not statutory funding. She remarked that the graph provided substantial information in terms of the larger budget picture. She asked what [reducing the PFD to the FY 24 number] would do to the overall budget deficit.

Mr. Painter responded that he did not have the number on hand that would result from a \$1,312 PFD. He relayed that if the PFD was 25 percent of the POMV draw (which was larger in FY 25 due to a larger POMV draw) and nothing else changed in the governor's budget, there would be a surplus of about \$400 million. Under the scenario, the total PFD appropriation would be about \$914 million. He noted the total would be larger than the \$1,312 and would also include the energy relief payment. He would have to calculate what the total would be at a particular dollar figure.

Representative Galvin noted that she was aware it was early to discuss the topic but appreciated the response.

Co-Chair Johnson pointed out that the presentation focused on the governor's proposed budget compared to the budget passed by the legislature the previous year. She believed there would be some significant changes during the budget process.

[2:55:04 PM](#)

Mr. Painter reviewed capital budget items in the governor's FY 25 budget on slide 25. There was a huge increase in federal funds, largely due to \$1 billion for the broadband program. There were several new items including funding for the Alaska Housing Finance Corporation (AHFC) Down Payment Assistance Program. He relayed that about half of the capital budget was for matching general funds to obtain federal funding.

Co-Chair Edgmon asked if there were more operating items being put in the capital budget over the past four years.

Mr. Painter answered it was a broader trend with quite a few examples in the FY 25 budget. He confirmed that a number of the projects were potentially more appropriate in the operating budget. For example, he thought the AHFC Down Payment Assistance program was likely an operating item and did not create a state asset. Part of the question was how operating and capital were defined. Another example was the project for the University of Alaska Fairbanks to achieve research tier 1 status. He explained that the university was not building a new campus to do the work, it was hiring faculty, which was an operating purpose. The drone program had started as an operating item and had moved to the capital budget and was now proposed as a capital item in FY 25. He elaborated that much of the increment seemed to be for ongoing cost for faculty and not just creating drones for state use that would be creating an asset.

Mr. Painter had noticed a few areas where a portion of a project was a capital item and the remainder was not. For example, DOT had projects that included capital expenses in addition to five years of maintenance costs for an aircraft. He explained it was an item that should be in the operating budget. He added it was probably underfunded in the operating budget and had been inserted in the capital budget. He stated that ultimately ongoing maintenance for aircraft should be included in the operating budget and not put forward as temporary capital budget funding.

[2:57:42 PM](#)

Co-Chair Edgmon stated that conversely the \$5 million included in the FY 24 budget for the Alyeska Reading

Academy went towards or was projected for brick and mortar spending.

Mr. Painter stated his understanding that FY 24 funds were for hiring several employees, leasing a space, and funding a training conference. He elaborated that the funding would go towards travel for around 100 teachers. He stated it was more of an operating purpose and he was uncertain of the long-term plan.

Co-Chair Edgmon remarked that he could dig into the issue more when the OMB director was back before the committee. He remarked that if an operating item went into the capital budget, the one-year timeframe for expenditure increased to five years.

Mr. Painter answered that the timeframe increased potentially beyond five years. He explained that capital budget increments allowed five years to start the work and as long as substantial work was made every five years the funding could continue for decades. He stated there were two problems with including operating items in the capital budget. The first was the potential to stretch things out that should be done more quickly. Additionally, including an ongoing cost reflected in the budget every year rather than every few years led to a more predictable and transparent budget. For example, if the goal was to take care of DPS airplanes, the money should be included in the budget annually rather than putting it in the budget in the current year and having to request the funding again in five years.

[2:59:56 PM](#)

Representative Ortiz thought the capital budget reflected a decrease of about 10 percent from the previous year. He asked if the size of the capital budget had been decreasing over the past five to six years in comparison to the overall budget.

Mr. Painter answered that in FY 22 and FY 23 there had been higher revenue forecasts and much larger capital budgets. He noted the capital budget had been \$700 million in one of those years. He elaborated that the capital budget level had been much lower from FY 16 through FY 21 at a total of \$100 million to \$200 million per year. He noted the governor's proposed FY 25 capital budget was a significant

increase from those past amounts. He explained that as a result of the federal infrastructure bill [Infrastructure Investment and Jobs Act (IIJA)] a capital budget of \$125 million would no longer match federal funds. There had been an increase in part because the amount needed to match federal funds had gone up. He added that the state was not necessarily getting more highway projects, but the costs had increased. He explained that the FY 25 capital budget would be much smaller when compared to capital budgets prior to FY 16. The proposed budget was much larger than the lean budgets from FY 16 to FY 21, but much smaller than the \$2 billion UGF capital budget around FY 13 or FY 14.

[3:02:09 PM](#)

Representative Ortiz noted the costs for construction projects were increasing not decreasing. He remarked that the proposed capital budget only covered two items out of around 25 on the school deferred maintenance list. He asked if declining to address the issue at present meant it would be more difficult to address the issue fiscally in the future.

Mr. Painter agreed and believed it was evident in the state's deferred maintenance backlog. He explained that during the years where \$100 million was being invested in deferred maintenance, the backlog was decreasing. He noted that in the past year the backlog had increased from year-to-year by somewhere between \$200 million to \$400 million because of the increase in costs. He remarked that if the state had invested in the projects five years back, it may have been able to prevent some of the increase. There was currently a very large deferred maintenance backlog including school major maintenance and in the Department of Environmental Conservation. He stated there were many costs that the state did not necessarily have an established funding mechanism to cover. He emphasized that \$30 million per year was going from the Capital Income Fund into deferred maintenance against a \$1.8 billion backlog, which would not get through the backlog quickly.

[3:04:01 PM](#)

Mr. Painter highlighted items that were not yet included in the budget on slide 26. He noted that every year the governor released the budget followed by amendments. Most years the amended budget tended to be higher. He remarked

that childcare was not included on the slide because he did not know what the cost could be. The governor's budget did not include a Base Student Allocation (BSA) increase or outside of the formula funding. There was \$87.4 million outside the formula in the FY 24 budget. He elaborated that a bill on the House floor [SB 140] had a \$220 million price tag. He stated that where the amount would end up was unknown, but it was unlikely to be a zero dollar increase. Additionally, there was a pending issue with the federal disparity test that could cause state costs to increase by \$89.1 million. He noted there may not be clarity on the issue for a number of months. He highlighted that the cost could end up being higher if the state failed the disparity test. He noted it was a possibility related to how some districts had funded themselves.

Co-Chair Johnson asked about the date of the disparity test ruling.

Mr. Painter replied that the state typically submitted its test to the federal government in February. He stated that if the department found a way to pass the test, the issue would not be a concern. However, if the department had to change its methodology or the federal government determined the state's information did not account for everything, the situation could drag on longer. He relayed that the state had failed its initial FY 21 disparity test, which resulted in a resubmittal. He reported that the process in FY 21 had taken about a year before the issue was cleared up. He stated that there was not a clear timeframe on how long it would take to completely resolve the issue. He concluded it may drag on for a while.

Co-Chair Johnson asked if the committee needed to anticipate the situation or just figure out a way to fund the cost if it arose.

Mr. Painter replied that they may have better information forthcoming as the department was working to compile the data. The department did not yet have all of the financial data from districts. Once the department had the data, the seriousness of the issue may be clearer.

Co-Chair Edgmon remarked there were a host of other items that could be added to the list on slide 26 including the Renewable Energy Grant Program, weatherization, ASMI, and ATIA. He pointed out that when factoring in all of the

additional items it represented real money. He thought the list on slide 26 was impressive on its own and there were other additional items not shown.

3:07:26 PM

Mr. Painter answered there were certainly things that could be added to the list on slide 26. The list used a minimum threshold of \$20 million. He confirmed that using a lower threshold would include many additional potential increases.

Mr. Painter continued reviewing the list on slide 26. The governor's budget did not include an increase to Medicaid funding because the projection prepared by DOH was too late to include. The projection indicated a need for an additional \$22.6 million UGF. He explained that the estimate would be refined for the governor's amended budget. The Senior Benefits Program was scheduled to sunset and was not included in the governor's budget. He noted that based on the number of pieces of legislation and the variety of sponsors it seemed likely the program would be extended at a cost of \$20.8 million. The Alaska Energy Authority (AEA) received a \$206.5 million federal grant to upgrade the electrical grid, which would require equal state matching funds. The state could potentially pay the amount over several years, but many of the funding mechanisms may still require some upfront investments. For example, it may be possible to repurpose some existing bond money, but it would require permission from bond holders. He elaborated that it may take time and if no funds were put forward, AEA may not be able to start work on the project in the upcoming summer. The agency was working on a funding package, but the need in the FY 25 budget was likely to be \$30 million to \$35 million.

Mr. Painter continued to review items not included in the governor's budget on slide 26 beginning with the Alaska Marine Highway System (AMHS). He relayed there could be a gap up to \$38 million or no gap between what AMHS was able to run in terms of vessel and crew availability and the amount of federal funding. In calendar year 2024, the state applied for \$66 million in federal funds, but only received \$38 million, resulting in a large gap. He explained that the [U.S.] secretary of transportation had significant flexibility in how to award the funds and he had awarded extra funds in 2023 and a bit less in 2024. He elaborated

that although Alaska was the only state that really qualified, the eligibility had been opened at the secretary's discretion and \$21 million had been awarded to American Samoa. The application process for 2025 had not yet started and the potential future gap was unknown. He expounded that if the situation was the same as the current year and there was no backstop funding, the gap could be as much as \$38 million; however, if AHMS received more grants, the gap could be much smaller. He stressed it was a huge unknown.

Mr. Painter addressed the last item on slide 26. There were three sizable unions currently negotiating contracts, which could result in increases. He noted the increase could be substantial based on recent inflation.

Co-Chair Edgmon referenced Mr. Painter's earlier discussion of disaster fund capitalization. He recognized that it was a policy call. He asked if LFD would potentially add the expense to the list for FY 25.

Mr. Painter answered, "Probably not." He explained that the department had been able to use funds from a \$50 million capitalization in FY 22. He elaborated that many of the state's disasters had been partially federally funded, which had substantially reduced the state's costs. He relayed that there was a fairly healthy balance of general funds still available in the fund. He did not recall the number but would follow up with the information. He was not particularly concerned about the current fund balance because of the large infusion in FY 22.

[3:12:34 PM](#)

Representative Ortiz referenced the potential \$38 million shortfall for AMHS. He asked if the toll credits funding source was at all related to the \$38 million.

Mr. Painter answered that the issue was unrelated and was on the capital side. He explained it was a choice on how the governor had opted to meet the state's matching requirement for the Tustumena. One of the options for meeting the matching requirement was to use other federal revenue as toll credits. He elaborated that because the state had used receipts collected in the Marine Highway Fund for maintenance in the past, it was eligible to use federal funds as toll credits to mach. He clarified that it

was not required, and the state could use the federal money for additional projects and match it with other sources. How to fund the items was a policy choice.

Mr. Painter turned to slide 27 titled "Long-Term Outlook and Governor's 10-Year Plan." The LFD modeling baseline assumed the FY 25 adjusted base grew with inflation including FY 25 and that all statewide items were funded to statutory levels (including the PFD). He noted that adding all of the items listed on slide 26 to the governor's budget would exceed the cost of inflation. He was not certain it was a realistic starting point, but it was an objective starting point that had been used in the past. He was happy to model other scenarios requested by the committee as the budget process moved further along and governor's amendments were received.

Mr. Painter relayed that with LFD's baseline assumptions, deficits started at \$1.1 billion in FY 25, increased to a peak of about \$1.9 billion in FY 31, and subsequently declined a bit. The governor's 10-year plan made several policy changes relative to the baseline that would reduce the deficit, but there would continue to be deficits each year. He emphasized that the legislature had not run the state off a cliff in the past six years; it had run relatively balanced budgets. He clarified that the purpose of the information was not to indicate the state was going to run off a cliff. The information was meant to indicate what would happen if the current statutes for the PFD and other items were followed at current revenue and budget levels. He clarified that he believed it was a very unlikely scenario.

[3:15:37 PM](#)

Mr. Painter moved to slide 28 titled "LFD Baseline Model, No ERA Overdraws." The top row on the slide reflected the surplus and deficit in millions, reflecting a surplus in FY 24 followed by deficits increasing from \$1.1 billion to \$1.9 billion over the years. The bar graph on the left showed the UGF budget and revenue. The blue portion of the bars reflected traditional oil and non-petroleum revenue (non-POMV revenue). The green portion of the bars reflected POMV revenue, and the gold portion of the bars represented draws from the CBR and SBR. The black solid line reflected the budget including the PFD. He explained that to balance, the budget line and the bars needed to meet, which was

accomplished in FY 25 and FY 26 by drawing from state savings accounts. Savings accounts would run dry by FY 27 and an unfilled deficit resulted. He explained that the legislature could choose to fill the deficit with the ERA, but it was not automatic (shown on the next slide). He believed showing the picture without the ERA draw first demonstrated the size of the problem without compounding effects.

Mr. Painter addressed a graph on the right of slide 28 showing the state's budget reserves. The yellow portion of the bars represented the CBR and SBR balance. He noted the model left \$500 million in the CBR for cashflow needs. The realized ERA balance shown in green was declining based on discussion earlier in the meeting. The bottom of the slide showed the effective POMV draw rate, which included overdrafts as part of the POMV draw. The bottom row on the slide showed the PFD per person under the statutory formula, which was \$3,654 estimated in FY 25.

Mr. Painter reviewed slide 29 titled "LFD Baseline Model with ERA Overdrafts." The graph on the left showed UGF revenue and budget. The red portion of the bars reflected the unplanned ERA draw, which would draw the ERA balance to zero by FY 33 and result in a gap beginning in FY 33. He elaborated that if the legislature chose to run large deficits and run out of money with no changes, the ERA would no longer be available by the end of FY 33. The bottom portion of the slide showed how the ERA overdrafts would impact the effective POMV draw. He noted the scenario reflected running the current statutes and budget up with inflation into the future with no policy changes.

Co-Chair Edgmon stated that annually they went through the projections with a statutory PFD when everyone knew it was unaffordable as much as some would like to have it. He thought the OMB director had recently told the committee that the governor was required to include a statutory PFD in the proposed budget. He stated that the governor could put anything in his budget and was not required to include any statutory item. He believed it was the previous year that LFD did a 25/75 and 50/50 analysis [of the POMV draw split]. He thought including the statutory PFD was misleading for the public because it did not reflect the reality. He found it to be an annoyance. He reiterated that a governor was not required to include numbers in the budget because there was a statutory formula. He emphasized

the governor could put whatever they wanted in their proposed budget.

Mr. Painter confirmed that the governor could put forward any number. There were a number of statutes that were not followed year-to-year that the governor did not follow in his 10-year plan. He stated it was a policy choice. He relayed that LFD started its modeling with current statute and was happy to model proposals to do something different. He explained that as a nonpartisan agency, LFD did not want to pick scenarios or its favorite formula. He stated it was up to legislators as policy makers to pick what scenarios they wanted to see.

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Mr. Painter turned to slide 30 titled "Long-Term Outlook and Governor's 10-Year Plan (Cont.)." The governor's 10-year plan made a couple of policy changes. Agency operations and the capital budget grew at 1.5 percent instead of inflation, which LFD assumed to be 2.5 percent. The governor's budget did not fund community assistance with UGF after FY 25. He highlighted assumption differences in the LFD model that were not included in the governor's 10-year plan. There was a longstanding difference where the governor's plan assumed lapsing appropriations and supplementals canceled out, whereas LFD included a supplemental placeholder of \$50 million, which was based on the pre-pandemic average of the difference between supplementals and lapsing appropriations. He relayed that since the pandemic both of the numbers had been much higher, and it was more difficult to make a fair comparison. He noted the figure was merely a placeholder and he could not empirically justify any particular number because of the extreme volatility of the supplemental and lapsing funds over the past several years.

Mr. Painter continued to highlight assumption differences in the LFD model compared to the governor's 10-year plan. The LFD model included a placeholder based on historical numbers for new school debt after the moratorium was set to end in 2025. He relayed it was possible there would be increased school debt due to a backlog of projects or that districts may not want to use the program because of a lack of annual funding. He explained that because of the uncertainty, the LFD assumption used the historical number. Additionally, there was a timing difference between LFD

assumptions and the governor's 10-year plan. He detailed that the fall Revenue Sources Book and the governor's 10-year plan used a preliminary number from APFC that did not really reflect the final scenario. He explained the number was not public and could not be used by LFD. The LFD modeling used figures from APFC's November history and projections report because it had come out around the release of the governor's budget. The LFD model showed a bit higher POMV numbers and slightly lower PFD numbers than the governor's 10-year plan. He reiterated that it was a timing difference related to which forecasts had been used.

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Co-Chair Johnson asked Mr. Painter to provide the most important pieces between LFD's analysis and the governor's 10-year plan on the last slides. She stated they could look at the governor's 10-year plan all they wanted but she recognized it led the state down a path that it was unlikely to take. She asked for the key takeaways.

Mr. Painter moved to slide 31 with a comparison of the LFD baseline to the governor's 10-year plan. He found the big takeaway to be that inflation was very powerful and compound interest was a powerful force. He explained that a 1 percent change in the difference between 1.5 percent growth [in the governor's 10 year plan] and 2.5 percent growth [in the LFD model] started out small but amounted to a lot of money by the end of a 10-year period. He highlighted there was a sizeable difference between the baselines despite it merely being a difference in inflation assumptions. There was a difference of nearly \$700 million just because of inflation by FY 33.

Mr. Painter turned to slide 32 titled "Governor's 10-Year Plan in LFD Model, No ERA Overdraws." He stated the numbers were very similar to the 10-year plan. He highlighted that the governor's 10-year plan statute specified that the governor was supposed to balance expenditures and revenue and available fund sources; however, the governor's 10-year plan ran the CBR to -\$10 billion. He noted that it did not reflect balanced fund sources. He stated that the governor's 10-year plan did not reflect a full fiscal plan; it was not possible to follow the plan and get out of the fiscal woods. He noted that in past years the governor's plan had included a placeholder for \$900 million in new revenue and one year the governor had included five

different plans to look at, while he had provided one plan in the current year that did not balance. He agreed there was likely not a lot of point to keep talking about it.

Co-Chair Johnson did not know there was a requirement to include all of the statutory pieces for the PFD and so on in the proposed budget. Additionally, the structural deficit had been discussed. She did not know there was much more that really needed to be added in terms of discussion.

Co-Chair Edgmon shared that he had been in the legislature when the 10-year plan statute was implemented in 2008 by former Representative Mike Hawker. He emphasized that what the 10-year plan had become was counter to or violated the spirit of the original legislation. He explained the 10-year plan was supposed to be a viable look into the future and not merely a document that any governor could use to include policy implications. He noted he had recently asked in committee whether the document was used by credit rating agencies. He thought it was the last thing they would want to be able to put forward because it was not realistic. He highlighted that carbon capture money that had been included the governor's plan the previous year and it had disappeared in the current plan. He thought it seemed there needed to be a retooling of what the 10-year plan was supposed to be. He stressed it had ceased to be an effective tool or even a believable representation of what was going forward in many respects. He did not know if it deserved any more discussion.

Co-Chair Johnson noted it meant the committee did not necessarily have a lot of guidance, but the House Finance Committee had a responsibility - without significant sideboards - to sort out. She knew all of the committee members were committed to making it happen. She asked if Mr. Painter had any concluding comments.

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Mr. Painter thanked the committee for the invitation to present. He noted that LFD was happy to model 10-year plan scenarios the committee felt were more realistic. He relayed that LFD typically started with the governor's budget and 10-year plan. He stated that if it was not a particularly meaningful starting point to the committee, the division was happy to start with something the committee found to be more reasonable.

Representative Tomaszewski thanked Mr. Painter for the information. He stated it made it clear that the legislature had balanced its budgets on the backs of the people of Alaska in its tax of the PFD. He remarked it was clearly shown to be the case where there had been a balanced budget. He stated the balanced budgets reflected a regressive tax on the most vulnerable people in the state. He appreciated some of the comments about how the legislature needed to be thoughtful in the way it conservatively looked at its budgets. He looked forward to the process and determining how to balance the budget without hurting the most vulnerable Alaskans.

Co-Chair Edgmon thanked Mr. Painter for a great presentation. He found Mr. Painter's knowledge of the intricacies to be impressive. He remarked that Mr. Painter's knowledge was balanced with his practical experience in the building in different capacities for a number of years. He suggested that perhaps Mr. Painter could present various scenarios to the committee that were perhaps truer to the committee's sense of the budget going forward. He thought it would be helpful to have information for a two to three-year timeline as well. He equated making predictions after a certain period of time when considering commodities and oil prices to throwing darts at the wall.

Co-Chair Johnson thanked Mr. Painter for the presentation. She reviewed the schedule for the following day.

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ADJOURNMENT

[3:31:24 PM](#)

The meeting was adjourned at 3:31 p.m.