

SENATE FINANCE COMMITTEE
January 24, 2024
9:02 a.m.

[9:02:17 AM](#)

CALL TO ORDER

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

MEMBERS PRESENT

Senator Lyman Hoffman, Co-Chair
Senator Donny Olson, Co-Chair
Senator Bert Stedman, Co-Chair
Senator Click Bishop
Senator Jesse Kiehl
Senator Kelly Merrick
Senator David Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Senator Cathy Giessel; Alexei Painter, Director, Legislative Finance Division.

SUMMARY

PRESENTATION: FY 25 BUDGET OVERVIEW - LEGISLATIVE FINANCE DIVISION

Co-Chair Stedman relayed that the committee would hear an overview of the governor's FY 25 budget, presented by the non-partisan Legislative Finance Division (LFD).

^PRESENTATION: FY 25 BUDGET OVERVIEW - LEGISLATIVE FINANCE DIVISION

[9:03:12 AM](#)

ALEXEI PAINTER, DIRECTOR, LEGISLATIVE FINANCE DIVISION, spoke to a presentation entitled "Overview of the Governor's FY25 Budget" (copy on file).

Mr. Painter looked at slide 2, "Outline":

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

Mr. Painter spoke to slide 3, "UGF Budget & Revenue, FY19-FY25 Governor's Budget," which showed a graph of the revenue and budget since FY 19. He started with FY 19, as it was the first year the state had a Percent of Market Value (POMV) draw from the Permanent Fund. He noted that the change was essentially when the state's current fiscal system started with the POMV draw as the largest revenue source for most years. He pointed out that the area of the graph in the background was revenue, while green was petroleum revenue. The orange was indicative of the non-petroleum revenue. The purple represented the POMV draw, the bars in the front represented budgets for each year, and the blue at the bottom was agency operations. Red denoted statewide operations, including items that did not fit into agency budgets such as state assistance to retirement and debt service. The grey signified the capital budget, and the light blue at the top was the Permanent Fund Dividends (PFDs), including energy relief payments.

Mr. Painter discussed notable items from slide 3. He thought since the POMV draw was started, the state had a relatively stable fiscal situation. The state had surpluses in FY 22 and FY 24, and had run deficits in FY 18 through FY 21 as well as in FY 23. The governor's FY 25 budget proposed a deficit. He considered savings account balances and thought the surpluses had somewhat made up for some of the deficits. There was about \$2.7 billion between the Constitutional Budget Reserve (CBR) and Statutory Budget Reserve (SBR) in FY 19, and the state had almost exactly the same value at the end of FY 23 based on preliminary numbers.

Mr. Painter summarized that the budget had been relatively stable despite ups and downs through the year. He discussed the concept of a structural deficit. He explained that the legislature had roughly balanced the budget year by year based on available revenue. He noted that the previous few years the legislature had not had access to the CBR when

the budget was originally prepared, and in FY 23 there was a supplemental vote to give CBR access. The legislature had not had the option to run a deficit the previous few years, as there was no savings to draw from to allow it, nor the votes to access. The past few years had resulted in a relatively stable fiscal situation, and the legislature had varied the size of the capital budget and PFD each year based on available funding.

Mr. Painter referenced slide 4, "Daily ANS Price, November 2021- January 2024," which showed oil prices starting in November 2021 through Friday of the previous week. He noted that oil prices were the most volatile part of the state's revenue and had not been stable. He referenced prices going from the \$70/bbl range to a peak of \$125/bbl. In the fall there were prices nearing \$100/bbl, which were now in the \$70/bbl range. He thought the volatility in oil prices had not fully translated to the state's budget. He referenced the legislature's response to oil price volatility through sliding scale mechanisms. He mentioned energy relief checks and funding to the Public Education Fund as examples of measures for additional revenue.

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Mr. Painter turned to slide 5, "Investments: History and Projections," which compared the performance of the Alaska Permanent Fund Corporation's (APFC) investments with the Treasury's investments. He cited that investment revenues had not been stable and had been incredibly volatile. The graph used Public Employees' Retirement System (PERS) as the largest asset to provide a clear comparison. He identified that historically the two were very close year to year, with the average for the Permanent Fund at 8.67 percent and the average for PERS at 8.53 percent. Going forward, PERS had a slightly higher projected return of 7.59 percent, versus the Permanent Fund's 7.20 percent from FY 25 and beyond. He commented that if the state budgeted based on returns there would be a lot of volatility, but it had built in a mechanism to smooth the volatility with the POMV draw.

Mr. Painter considered slide 6, "Percent of Market Value Draw from Permanent Fund," which showed how POMV draws were calculated. He noted that Co-Chair Hoffman had requested the information from the Department of Revenue (DOR) and so he had included the slide. He discussed calculation of the

POMV draw, which averaged five percent of the previous five years, excluding the fiscal year that just ended as well as some funds that did not qualify for the purpose of the draw. He noted that FY 21 had huge investment returns and a spike in the value of the fund. He explained that because of the averaging, the POMV had not commensurately spiked.

Mr. Painter pointed out that the FY 24 value of the POMV was not necessarily 5 percent of the present fund because of the trailing average and as long as there was a growing fund. The FY 24 POMV value was about 4.6 percent of the FY 22 value of the fund, rather than 5 percent of the average. In a couple of years, the effective POMV rate might not be lower due to no lower years in the average. The lower years were helping to keep the draw lower, but future years might see the real rate of the draw coming closer to 5 percent.

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Mr. Painter displayed slide 7, "Earnings Reserve Account (ERA) Sufficiency":

- APFC's Statutory Net Income projection for FY25+ is 6.65%, compared to inflation of 2.50% and a 5.00% POMV draw. This leads to a projected decline in the balance of the ERA balance.
- LFD's probabilistic modeling shows an 54% chance of having an insufficient ERA balance to make the full POMV draw over FY25 - FY33, assuming full inflation proofing. If inflation-proofing is suspended when the ERA balance drops below the following year's POMV draw, that drops to 39%.
- As of June 30, 2023, \$8.3 billion of the \$11.9 billion (70%) of the unrealized gains were in relatively illiquid assets (private equity, private income, and real estate).

Mr. Painter discussed the Permanent Fund's statutory net income projection, which was the amount realized each year and went into the ERA. The realized income was from selling assets, dividends, or interest. He discussed the projection that even with the forecast Permanent Fund returns, there would be a decline in the ERA balance. He spoke to the graph on the bottom of the slide, which was drawn from projections from APFC. He pointed out the blue bar on the bottom, which was next year's POMV draw. The red on the top was the balance of the rest of the realized ERA balance,

which was the spendable balance of the ERA. He pointed out that in FY 22, the total was close to \$14 billion, dropping to just over \$8 billion by FY 33 if inflation proofing happened each year.

Mr. Painter noted that in FY 24, the legislature capped the inflation proofing transfer at the 2.5 percent inflation level. The actual inflation for the U.S. Consumer Price Index (CPI) was about 3.5 percent. He estimated that capping the inflation proofing saved about \$1 billion in the ERA. He noted that LFD's probabilistic modeling showed a 54 percent chance of not having enough funds for a POMV draw in the ERA over the forecast period if there was inflation proofing each year. If the legislature decided to stop inflation proofing once the balance reached what was shown by the blue bar (showing the following year's POMV), then the likelihood would drop to 39 percent. He thought there was a large risk that the straight-line projections did not necessarily show.

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Mr. Painter pondered the question of why the state did not have more realized income. He thought much of the reason was due to the nature of APFC's portfolio, which had \$11.9 billion of unrealized gains as of the end of FY 23. He continued that 70 percent of the amount was in illiquid assets such as private equity, private income, and real estate. He discussed the challenges of realizing income and the potential exaggeration of unrealized gains.

Co-Chair Stedman commented that the previous year the committee was looking at the cash flow for the state, considering the Permanent Fund and oil and gas as a revenue stream. He referenced measures in the previous year's budget such as capping the inflation proofing. He noted that the APFC would be coming to committee to discuss historical inflation-proofing numbers since inception. He thought the committee recognized that there was a disconnect between what was going on in the legislative arena or the state's arena needing revenue from the Permanent Fund's asset allocation, and the structure did not take into account the cash needs of the state. He spoke to the ability to adjust inflation contributions during times of tight budgets. He mentioned forward funding the draw on the Permanent Fund.

Co-Chair Stedman relayed that the legislature had multiple tools, which it would discuss at length with APFC, and the legislature would make a decision related to inflation proofing at the end of the session. He thought there was a timing issue to consider, and considered whether the inflation proofing would be in the final budget or be considered the following winter. He thought the legislature could avoid the negative fiscal scenario on the slide if it did its job.

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Mr. Painter commented that raising the issue now was not to be "doom and gloom," but rather so that the legislature as policy-makers could take action. He thought the committee's action the previous year was an example.

Senator Bishop referenced lost opportunity cost of not fully inflation-proofing.

Co-Chair Stedman clarified that the committee did not want to erode the Permanent Fund's purchasing power over time. He mentioned the draw rate, asset allocations, and returns over time that would be topics of further discussion along with inflation proofing.

Co-Chair Hoffman asked if Mr. Painter could provide more information on what other large funds did regarding inflation-proofing.

Mr. Painter agreed to provide the information. He thought it was generally unusual to have a separation of the principal of the endowment and an income account. He thought the structure was common in the 1970s and when the fund was created, but was not common presently. He noted that the Public School Trust Fund was previously in the same structure, and then was collapsed in 2018 when the opportunity was provided through statute.

Co-Chair Hoffman relayed that he brought up the topic because individuals had investments all over the world and did not inflation proof.

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Mr. Painter highlighted slide 8, "Fall 2023 Revenue Forecast":

- DOR's Fall 2023 Forecast shows higher oil prices in FY24 and FY25, but lower oil production, higher lease expenditures, and higher transportation costs.
- The result is an increase in projected revenue, but by less than price alone would explain.

Mr. Painter thought the forecast was interesting. He thought DOR and the Department of Natural Resources (DNR) had both indicated the state was moving into a new era regarding oil revenue and where it came from. He directed attention to the chart on the top of the slide and noted that revenue in FY 24 was up by \$221 million and in FY 25 was up by \$79 million. However, the price was up in FY 24 by \$9.39/bbl and \$6/bbl in FY 25. The previous year the budget showed that each marginal dollar of additional oil price would yield about \$70 million. Production was down in both FY 24 and FY 25, and lease expenditures were up significantly. In FY 24, lease expenditures were up \$755 million, and in FY 25 the expenditures were up \$1.6 billion over the previous forecast. The lease expenditures were normally deductions against the production tax and reduced production tax liability. Much of the difference was around the increased certainty of Willow and Pikka projects and they moved forward. He summarized that the big picture was that while prices were going up, there was a large shift under the surface and less revenue for the price.

Mr. Painter looked at slide 9, "Fall 2023 Revenue Forecast (cont.)":

- Fall 2023 forecast shows lower production in FY24-26 than the previous forecast, but higher production in FY29-32. Lease expenditures are higher in all years in the Fall 2023 forecast.
- Since lease expenditures are deductible from the production tax, higher lease expenditures generally mean less revenue. New production is also eligible for the Gross Value Reduction (GVR), which reduces production tax in the initial years of production.

Mr. Painter pointed out a graph on the right showing the fall 2022 forecast, which showed relatively flat production with a peak in 2027 to 2028. Fall 2023 showed lower production in the near term and higher production in the later term than previous forecasts. He pointed out that the lease expenditures showed higher fall forecasts in every

year, particularly in FY 27 through FY 29, which showed peak investments in the Willow field. Higher lease expenditures generally meant less revenue to the state, and would often bring a company down to the gross tax floor of 4 percent rather than paying based on profits. New production was also eligible for the Gross Value Reduction (GVR), which reduced tax in the initial years of production. As more new production was coming in, it did not necessarily signify more revenue right away, as there could be deductions from previous years or GVR eligibility.

[9:29:14 AM](#)

Senator Merrick asked if LFD concurred with DOR's estimate of \$1 change in oil price equating to \$45 million.

Mr. Painter answered "yes," based on the agency's forecast. He noted that DOR had changed how it treated volatility starting one year ago, in a way that he thought was more accurate.

Mr. Painter addressed slide 10, "Fall 2023 Revenue Forecast (cont.)," which showed a table comparing the production by unit in the Fall 2022 forecast to the Fall 2023 forecast. He noted that fields with a significant reduction in production were highlighted in red. In green were fields that had production increase. Prudhoe Bay was the state's largest legacy field, and the new forecast showed a significant reduction in the field's production. It had an outsized impact on the state's revenue because it was a legacy field with the lowest cost. There was an increase in Prudhoe Bay satellites, and the new fields were listed at the bottom of the slide. The new fields would make up for the production difference, but some of the new fields may not bring in quite as much revenue immediately.

Mr. Painter identified that Kuparuk, a legacy field, had lower production year by year but Kuparuk satellites had higher production throughout the forecast. He discussed the Natural Petroleum Reserve-Alaska (NPRA), which was comprised of the greater Moose's Tooth unit, where there was a new unit with lower-than-expected production. In the short term there was a big reduction in production in NPRA but in the long term there was the increasingly certain Willow project with increasing production. He cited that total production in FY 25 was down by 39.5 thousand barrels per day. The biggest impact of the reduction was in the

NPRA, for which the state did not receive royalties, so the state had less of a revenue impact. He noted that the changes were large but not necessarily in a consistent direction. He reiterated that the changes were masked by price. There was lower production in the legacy fields, and higher production in new fields in the out years, particularly with the Willow project coming online.

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Co-Chair Stedman discussed production and thought it would be nice to put the information in historical per-barrel production as well as forecasted barrels of production. He thought the information would provide a view on magnitude.

Mr. Painter agreed to provide the additional information.

Mr. Painter advanced to slide 11, "Fall 2023 Revenue Forecast (cont.)," which compared the last three fall revenue forecasts for Fall 2021 through Fall 2023. He thought the graph on the left showed a fairly big difference in oil prices in the forecasts in the short term, which diminished over time as the markets converged on what the long-term view of oil was. There was a very small band of revenue difference in the out years. He thought that while it looked like the oil price showed a great deal of revenue volatility, if one considered the long-term forecast, there was relatively little difference. For fiscal planning purposes long term, there was not a great deal of volatility despite short term variations.

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Mr. Painter looked at slide 12, "Fall 2023 Revenue Forecast (cont.)":

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 showed slide 13, "FY24 Budget Update":

- The enacted FY24 budget had an estimated \$293.2 million surplus based on the Spring forecast. It also had a provision that split the first \$636.4 million of UGF revenue received above the Spring forecast 50/50 between an energy relief payment (to be paid with the FY25 PFD) and the CBR.
- At the time, we estimated the energy relief payment would kick in above \$73 per barrel and max out (at about \$500 per person) at \$83 per barrel. With the updated revenue forecast, those trigger points have shifted to \$78 and \$90, respectively.
- Based on the Fall forecast, we estimate about \$110.6 million will go into each of the CBR and energy relief payment, paying about \$175 per person on top of the FY25 PFD.
- There is still a budget surplus based on the Fall forecast based on revenue received up to the Spring forecast, now estimated to be \$293.7 million. This is available for appropriation this session, or it will lapse to the CBR at the end of the fiscal year.

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Co-Chair Hoffman asked Mr. Painter to remind the committee how much the governor had vetoed from the FY 24 budget.

Mr. Painter estimated that the number was around \$200 million, and agreed to provide more detail at a later time.

Co-Chair Stedman referenced the third bullet on the slide and clarified that the year was still open for appropriation. He pondered the impact on the energy relief payment if the legislature decided to appropriate the funds elsewhere.

Mr. Painter relayed that the legislature could appropriate \$293 million without changing the trigger points, and it could also change the trigger points.

Co-Chair Stedman pondered if the legislature appropriated the \$220 million, and asked what impact it could have on the dividend portion.

Mr. Painter answered that there would be a conflict of appropriations since the funds had already been appropriated to the CBR and energy relief payment, which could result in a deficit. He recalled that there had been no successful vote to access the CBR in 2024.

Co-Chair Stedman brought up the topic because when the supplemental budget was being considered, it would have the added complexity of considering the trigger mechanism.

Co-Chair Hoffman brought up the supplemental budget for FY 24. He asked if Mr. Painter was indicating that the \$110 million would still go into the CBR regardless of how large the supplemental was.

Mr. Painter relayed that as long as the legislature spent \$292 million of UGF or less in the supplemental, there would be no impact on the transfer to the CBR or the energy relief payment. If more was spent, it could have an impact because there would be a deficit.

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Mr. Painter referenced slide 14, "FY24 Budget Update (cont.)," which showed a graphical version of what he had discussed earlier. The blue portion of the graph showed UGF revenue, which would go to the budget. If prices were below \$71/bbl, there was not a deficit-filling mechanism aside from \$20 million in the SBR, so there would be an unfilled deficit. If prices went down the next few months, a potential CBR-access vote would be needed to fill the deficit. The previous year required a CBR vote to access the funds to fund the budget. This year the "trigger point" number was \$71/bbl, and the forecast was for \$72/bbl. If revenue came in at the spring forecast or above, the state would have \$292 million in surplus, beyond which the funds would be split. He pointed out the orange line denoting the energy relief payment and the green denoting the CBR. The spendable surplus was shown by the yellow bar, and it did not change as the price went up, because the previous year's budget reserve appropriated all the funds above the amount.

Co-Chair Stedman understood that \$71/bbl was a break-even amount to balance the budget. He thought the three-quarters vote in the normal budget process would take place in May, and he pondered not having the votes to access the CBR by the end of the fiscal year in June.

Mr. Painter thought that if the legislature was in regular session, it could deal with a lack of CBR access through negative supplementals and reducing or shifting appropriations. If the legislature was not in session, the governor would have to try and take action by calling a special session or restricting expenditures on existing appropriations as needed to balance the budget. He thought it would take a pretty big swing in oil price to bring about the situation.

Mr. Painter turned to slide 15, "FY24 Budget Update (cont.)":

- The Governor's initial budget release included some supplemental requests, but more are expected on the 15th day of the legislative session.
- The Governor's FY24 supplemental requests total \$17.0 million UGF and \$19.7 million all funds, including:
 - o \$8.9 million (\$6.0 m UGF Match) for SNAP backlog
 - o \$5.0 million to Wrangell for dam safety and stabilization improvements
 - o \$3.0 million UGF for support of food banks and pantries
 - o \$2.5 million UGF for Ranked Choice Voting Media and Education
 - o The Governor's fiscal summary includes a placeholder of \$61.0 million for fire suppression, based on a preliminary estimate by the Department of Natural Resources.

Mr. Painter thought the full amount of \$61 million for fire suppression may not be needed, depending on how much federal money the state received. The estimate was from August, which he considered to be quite dated. He anticipated supplementals in the Department of Corrections and the Department of Health for Medicaid based on projections showing the state was a little short. He thought there could be additional supplemental the following week.

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Mr. Painter considered slide 16, "FY25 Adjusted Base":

- The starting point for the next year's budget is the Adjusted Base, which is the prior year's budget less one-time appropriations plus current statewide policy decisions (such as salary adjustments and formula changes) needed to maintain services at a status quo level.
- For FY25, LFD modified the Adjusted Base to include formula changes. Previously, it was difficult to distinguish policy changes from changes in formula amounts. Now, formula-driven adjustments (for items like the K-12 formula, debt service, or retirement payments) will be reflected in the Adjusted Base, making policy changes by the Governor easier to see.
- For formula items funded at a partial amount (such as the PFD), the Adjusted Base would be the same formula carried forward into the next year (25% of FY24's POMV draw in becomes 25% of FY25's POMV draw).
- The Adjusted Base now aligns with LFD's former "current policy"

Mr. Painter discussed changes in the adjusted base process. He discussed changes in funding that did not signify changes in policy from the previous year. The goal was to make it easier to identify the governor's policy changes by building more formula items into the adjusted base. He thought the new process would make the process easier and was a positive change that would reduce confusion. He noted that the Office of Management and Budget (OMB) had also agreed to use the adjusted base in its comparisons.

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Mr. Painter displayed slide 17, "FY25 Adjusted Base (cont.)":

- Largest One-Time Item removed in Adjusted Base is K-12 Additional Foundation Funding (\$87.4 million), accounting for over half of the total.
- The OTIs are a mix of items requested by the Governor as permanent items that were converted by the legislature to one-time funding, onetime legislative

additions, and multiyear appropriations that started in FY24 but will be spent over several years.

Mr. Painter relayed that he would walk through the changes made to the adjusted base. He used the example of Alaska Marine Highway System (AMHS) backstop funds, which had been a result of backstop language contingent upon federal funding. He pointed out the table on the top that showed the removal of \$165 million from the adjusted base.

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Mr. Painter highlighted slide 18, "FY25 Adjusted Base (cont.)," which showed the next series of changes:

- K-12 Formula reduced due to increased required local effort (-\$12.2m), increased deductible federal impact aid (-\$15.8m), and student count changes (-\$2.2m), increased by Pre-K funded in Alaska Reads Act (+\$3.0m).
- Retirement contributions up due to higher PERS and TRS past service costs based on June 30, 2022, valuations.
- School debt reimbursement continues to decline due to ongoing (FY16-26) moratorium on new debt.

Mr. Painter discussed the reductions to the K-12 formula. He noted a projected decrease in student count, which was partially offset by a higher number of special needs intensive students and higher number of correspondence students. There was a net \$27 million deduction of all state funds to the K-21 formula. There was an increase in the Public School Trust Fund amount, so the GF amount was down by \$30 million. The changes did not decrease funds to districts, but rather shifted to more funds from the federal government, more by local governments, and less by the state. He highlighted that because of the decreased student count, pupil transportation was to go down \$2 million. The moratorium on new school debt since 2015 was scheduled to end the following year. Starting in July 2025, districts were able to start bonding again and adding debt, which could turn the formula around.

Mr. Painter noted that other debt service was up in other funds, but down in UGF. State contributions to retirement were up nearly \$46 million in GF, and the amount on the slide only indicated the amount paid by the state on behalf

of other employers. There was an additional amount that would be shown on a subsequent slide. He explained that the amount went up due to a higher unfunded liability amount. The Regional Education Attendance Area (REAA) Fund capitalization was down slightly, which was a function of school debt going down as the two were tied together.

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Senator Merrick asked how districts could start bonding again in 2025 if the moratorium ended in 2026.

Mr. Painter explained that the moratorium was through FY 26, and the moratorium ended July 1, 2025. Depending upon municipal elections were, bonds could go out fall 2025. The state would not incur costs right away, because the bonds would not be reimbursed right away, but the state could see some added costs as early as FY 27.

Senator Merrick asked if there was a way to calculate how many years of moratorium would be needed to totally exhaust the debt.

Mr. Painter answered affirmatively and needed to examine the debt schedule. He offered to get back to the committee with the information.

Co-Chair Stedman thought at some point there would be a presentation of the entire debt schedule for the state, including schools.

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Mr. Painter looked at slide 19, "FY25 Adjusted Base (cont.)":

- Three unions are currently negotiating: the Supervisory Unit, the Alaska Correctional Officers Association, and the Labor, Trades and Crafts Unit. All may have additional amendments for salary adjustments.
- Previous legislative intent was for exempt employees to follow changes in the Supervisory Unit, but that would take legislation once that agreement is in place.

Mr. Painter explained that the state as an employer paid the new rates of salary adjustments each year. The increase was due to higher retirement rates in the current year. There were increases in health insurance, and from several unions for past year's contracts that were already authorized. So far there had not been any new agreements, but there were three unions negotiating that could result in future adjustments. He noted that the legislature had to authorize the funding each year. There was a total of \$44.5 million in UGF salary adjustments, and \$97 million in all funds. The majority of the number was from past due salary adjustments. The number would go up and could come in after the governor's amended budget was submitted. He noted that the last time the legislature increased salaries for exempt employees, there was a provision that said future increases to the supervisory union would be extended to the exempt employees. The provision needed an additional statutory change to happen through a bill rather than just through the budget. He noted that the supervisory unit was currently in negotiation.

Co-Chair Stedman recalled a presentation from the OMB director the previous day that showed vacancies across agencies. He had asked for more information on the fiscal impact linked to a more standardized rate of vacancies to understand the impact on the budget. He noted that there was a difference between authorized positions and funded positions. He thought Mr. Painter could work with OMB to provide the committee with information. He pondered going up to a 5 percent vacancy or 8 percent vacancy and thought the change would make a significant change in overall budget numbers.

Mr. Painter agreed to work with OMB on the matter. He noted that the following day he would provide a few more slides that addressed the topic.

[10:03:46 AM](#)

Mr. Painter addressed slide 20, "Governor's FY25 Budget," which showed a table depicting the UGF comparison of the governor's budget from FY 24 to FY 25. He pointed out that the revenue forecast overall was a reduction of \$177 million due to a lower [oil] price. For agency operations, the governor's budget was \$100 million below FY 24. There were \$165 million in one-time items, so a lot of the reduction was that one-time items were not being repeated.

Statewide items were up by \$18.2 million, and the capital budget was down \$54.6 million. The largest increase in the governor's budget was going from the 25 percent POMV dividend the previous year to the statutory dividend estimated to be \$3 billion. The energy relief payment was not repeated and was a reduction. Overall, the governor's budget, before considering supplementals, was up \$1.175 billion or 19.2 percent, largely due to the proposed increase in the PFD level.

Mr. Painter identified that in FY 24, before transfers, there would be a \$416.6 million surplus, and after transfers there would be \$292.7 million surplus in FY 24 available for appropriation. So far, the governor had spent \$17 million of the amount, leaving \$275.7 million in surplus. In FY 25, the post-transfer deficit was \$982.3 million based on the governor's budget. The governor proposed to meet the nearly \$1 billion budget by using the CBR and SBR. He noted that there were a few numbers that were different than OMB's fiscal summary, partly because OMB was not incorporating estimates for items such as the energy relief payment and the CBR yet, since the numbers were fluid. He noted that LFD included the numbers in order to demonstrate how much funding was available for appropriation. Additionally, LFD assumed that any surplus would go to the CBR, which was reflected in a higher CBR balance in the scenarios.

Mr. Painter advanced to slide 21, "Governor's FY25 Budget (Cont.)":

- The Governor's FY25 budget request has a pretransfer (fiscal) deficit of \$977.0 million, which would be drawn from the SBR balance and the CBR.
- The largest increase is the statutory PFD payment of \$2.3 billion compared to FY24's payment of \$881.5 million.
- Non-PFD UGF appropriations are up \$53.9 million (0.4%) from the Adjusted Base. However, there are several areas where we expect the budget to increase before the end of the legislative session.

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Mr. Painter looked at slide 22, "Governor's FY25 Budget (Cont.)," which showed a swoop graph comparing the FY 24 management plan with the FY 25 governor's proposals

including the PFD and capital budget. The slide had been requested by Co-Chair Stedman and was sorted by the largest expenditures to the smallest in FY 25. He identified that the largest item in the budget was the PFD followed by the Department of Education and Early Development (DEED), then the Department of Health (DOH). The previous year, the PFD was the third largest item after DEED and DOH. There were significant increases in a few agencies including DOC, the Department of Family and Community Services (DFCS), and Department of Public Safety (DPS); while there were significant decreases to DEED, DOH, and the capital budget.

Mr. Painter spoke to slide 23, "Governor's FY25 Budget (Cont.)":

- Agency Operations total \$4.3 billion UGF, \$94.9 million UGF (2.3%) above the Adjusted Base:
 - (\$20.8) million UGF reduction due to sunset of Senior Benefits program (will require legislation to extend)
 - \$31.8 million UGF increase to Department of Corrections (\$12.5 million in fund changes and the remainder in increments)
 - \$17.3 million UGF for multiple Department of Education items requested by the Governor in FY24 as permanent items for which the legislature gave one-time funding (such as the Alyeska Reading Academy)
 - (\$6.2) million UGF reduction in DOH to stop funding for the tuberculosis and congenital syphilis elimination plans
 - \$19.2 million UGF for various increases in the DOT's Highways and Aviation (such as expiration of federal COVID funds, reduced federal support for the Whittier Tunnel, and an increment for statewide contracted snow removal)

[10:11:38 AM](#)

Mr. Painter referenced slide 24, "Governor's FY25 Budget (Cont.)":

- Statewide Items total \$365.0 million UGF, \$13.6 million (3.9%) above the Adjusted Base:
 - School Debt Reimbursement, REAA Fund Capitalization, State Assistance to Retirement funded at statutory levels (reflected in Adjusted Base).

- Statutory appropriation for Community Assistance (\$30.0 million total, \$2.2 million UGF and \$27.8 million PCE Fund).
 - This funding was vetoed in FY24, so the distribution to communities in FY25 would be \$20.0 million without a supplemental appropriation.
- \$11.4 million for other fund capitalizations:
 - \$5.0 million for Disaster Relief Fund
 - \$3.1 million for AKLNG project fund
 - \$3.4 million for Alaska Clean Water and Drinking Water funds

Mr. Painter noted that because of the veto in FY 24, the distribution to communities was one-third of the balance as of the end of the fiscal year. In FY 25, with no supplemental, \$20 million would go out to communities. The amount would be enough for the base payments but no per capita payments, which would require a supplemental appropriation to get back to \$30 million. Putting in \$30 million in the current year would still result in reduced amounts going to communities in FY 26 and beyond unless there was a "catch-up" appropriation. He noted that the legislature put \$50 million into the Disaster Relief Fund in FY 22 as a supplemental appropriation, so it was not funded in FY 23 or FY 24. There was still money left and the governor wanted to keep building up the fund. He noted that the \$3.4 million had been put in the budget for the Alaska Clean Water and Drinking Water funds was put in the budget two years previously but was not spent because the department was not ready to do the projects as it was currently.

Mr. Painter turned to slide 25, "Governor's FY25 Budget (Cont.)":

- Capital Budget totals \$305.2 million UGF, \$3.5 billion all funds:
 - o \$1.0 billion federal for Broadband Equity Access and Deployment Program
 - o \$25.0 million for a new AHFC Down Payment Assistance program
 - o \$22.8 million UGF to DPS for seven projects, including:
 - \$9.5 million to replace the patrol vessel Enforcer
 - \$6.2 million to acquire a Pilatus aircraft

- o \$18.2 million UGF, \$47.7 million all funds for University of Alaska projects, including:
 - \$10.0 million UGF (and \$10.0 million UA Receipts) for UAF to Achieve Research Tier 1 Status, contingent on UAF awarding 70 doctoral degrees in the 2024-25 academic year
 - \$5 million UGF (and \$5.0 million UA Receipts) for year 3 of the drone program
- o \$4.3 million UGF for School Major Maintenance grants and \$4.0 million for School Construction grants
- o \$7.5 million to replace an ADF&G research vessel for the Gulf and Bering Sea

Mr. Painter noted that about half of the UGF in the governor's capital budget was for matching federal funds. The largest new item was \$1 billion in federal funds for the broadband program, which was the full five years of funding all at once. He commented that several of the items listed were more appropriate for the operating budget.

[10:15:34 AM](#)

Mr. Painter considered slide 26, "Governor's FY25 Budget (Cont.)":

- Also notable is what is not yet in the budget:
- o Education - no outside the formula funds or BSA increase (there was \$87.4 million outside the formula in FY24). There is also a pending issue with the federal disparity test that could cause State costs to increase by \$89.1 million.
 - o Medicaid - the Governor's budget does not contain an increase to Medicaid funding, but the Department of Health stated that the projection will be trued up in a future amendment. Preliminary projections indicate a need for an additional \$22.6 million UGF.
 - o Senior Benefits - the Senior Benefits program will sunset on June 30, 2024, without legislative action. If it is extended, it would cost \$20.8 million.
 - o Alaska Energy Authority Electrical Grid Grant - the Alaska Energy Authority (AEA) received a \$206.5 million federal grant to upgrade the Alaska Railbelt electrical grid that requires equal matching funds. The funds may be spread over several years, but securing the grant will require a significant

investment of general funds. AEA is considering multiple funding options, but the need this legislative session is likely to be \$30-35 million.

- o Alaska Marine Highway - the Governor's budget request does not change funding levels or sources from the Calendar Year (CY) 24 enacted budget, but it does not include any backstop funding if federal funding is insufficient. If a similar amount of federal grants are awarded in CY25 as the State expects in CY24, there will be a \$38.0 million shortfall in the CY25 budget.

- o Ongoing Employee Bargaining Negotiations - three unions (Alaska Correctional Officers Association, Alaska Public Employees Association Supervisory Unity, and Labor, Trades and Crafts) are currently negotiating new contracts to begin in FY25.

Mr. Painter noted that there were amendments to the governor's budget coming on the 30th day, as well as supplemental items coming the following week. He mentioned ensuring the state did not end up with an unfunded deficit due to the pending disparity test issue. He mentioned that there was a high level of uncertainty on the number for the Medicaid item as it went through the redetermination process.

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Mr. Painter continued to address slide 26. He discussed AMHS funding and noted that the budgeted level for FY 25 could be more than what was possible depending upon unknown funding factors. He mentioned policy considerations such as what schedule to fund to. He mentioned a childcare task force and its recommendations, which were not currently being funded. He summarized that the governor's budget, with its deficit, was likely a low starting point for where it would end up at the end of session.

[10:23:34 AM](#)

Co-Chair Stedman recalled the committee had spent some time on AMHS funding the previous year to ensure that there was sufficient resources to absorb unknown federal appropriation amounts. He expressed concern and the desire to do the legislature's portion of funding for AMHS. He thought there would be ample support for funding the system.

Co-Chair Stedman addressed education and the potential deficit related to no funding outside the formula and the potential disparity test issue. He asked if Mr. Painter planned on coming forward with a more refined numeric after the supplemental items were released.

Mr. Painter affirmed that some of the items would be refined after the submission of the governor's amended budget. He thought Medicaid and other items would be built in, but there would be ongoing uncertainty with some items such as the disparity test issue.

Co-Chair Stedman understood that if the state did not fund Medicaid, people received services anyway and the state received the bill.

Mr. Painter agreed that if the state did not fund the full amount, the payments to providers would be delayed till the following year.

Mr. Painter displayed slide 27, "Long-Term Outlook and Governor's 10- Year Plan":

- LFD modeling baseline assumes the FY25 Adjusted Base grows with inflation (including in FY25) and all statewide items are funded to statutory levels (including the PFD).
- With the baseline assumptions, deficits increase from \$1.1 billion in FY25 to a peak of \$1.9 billion in FY31.
- The Governor's 10-Year Plan makes several policy changes relative to the baseline that reduce the deficit, but still shows deficits each year that would drain the CBR in FY27.

[10:27:12 AM](#)

Mr. Painter highlighted slide 28, "LFD Baseline Model, No ERA Overdraws," which showed two bar graphs and a table, which depicted LFD's budget baseline model with no overdraws from the ERA. The first line on the slide showed the surplus and deficit, with a surplus for FY 24, and a deficit for FY 25 and FY 33. The left-hand side had a graph depicting revenue and the budget, and he pointed out the gap between the revenue and budget. The first couple years the gap was made up by draws from savings, which ran out in

FY 27 under the scenario. He pointed out the gap of the unfilled deficit. The right-hand graph showed budget reserves, including the CBR and SBR, and the realized ERA balance.

Mr. Painter pointed out that the realized ERA balance was declining in the baseline model and was the baseline assumption. The APFC modeling showed decline even without withdrawals. The model assumed leaving \$500 million in the ERA for cash flow, which was an assumption for the past several years. The effective POMV draw rate was shown at the bottom. The version of the model showed the statutory 5 percent level. The scenario included the PFD per person, with \$1,312 the previous year, and the estimates for statutory PFD's going forward at \$3,600 the current year to peak at about \$4,350 in FY 33.

Mr. Painter looked at slide 29, "LFD Baseline Model with ERA Overdraws," which showed the same baseline model graphs if the legislature filled the deficits from the ERA. He noted that the budget could not have unfilled deficits, and based on the baseline the savings were not enough to get through FY 33. He made note of additional overdraws leading to higher effective POMV draws in later years due to overdrawing the ERA. He noted that the scenarios were based on the assumption of the legislature doing nothing. He noted that the legislature had not run the budget in the manner of the model and had varied elements such as the PFD and the capital budget to ensure the state was not running big deficits. The scenario illustrated what would happen if the budget followed current statutes.

[10:30:39 AM](#)

Mr. Painter addressed slide 30, "Long-Term Outlook and Governor's 10-Year Plan (Cont.)":

- Policy changes in Governor's 10-Year Plan:
 - Agency operations and capital budget grow at 1.5%
 - Does not fund Community Assistance with UGF after FY25
- Assumption Differences in LFD Model:
 - Governor assumes supplementals and lapse cancel out after FY24, LFD includes \$50.0 million placeholder
 - LFD includes a placeholder for new school debt after the moratorium ends in 2025, Governor does not

- DOR's Fall Revenue Sources Book used preliminary POMV/PFD estimates from APFC; LFD uses the figures from APFC's November History and Projections report

Mr. Painter explained that the \$50 million placeholder for the supplemental was based on a pre-Covid average. He discussed LFD's assumption of \$7.8 million of new state obligations each year based on school debt before the moratorium. He thought it was possible that the number could be higher or that some school districts might be less interested in the debt reimbursement program. He noted that the result of LFD using different POMV and PFD estimates was higher POMV numbers by about \$100 million per year.

Co-Chair Stedman noted that the committee members had seen the budget base model for many years. The models would be considered again after the governor's budget amendments and adjustments.

Mr. Painter advanced to slide 31, "Long-Term Outlook and Governor's 10-Year Plan (Cont.)," which compared the governor's 10-year plan to the LFD baseline. He noted that the biggest difference was the rate of budget growth, with rates of 2.5 percent versus 1.5 percent. He mentioned the powerful force of compound interest. He noted that the difference grew over time, with a nearly \$700 million difference by FY 33.

Co-Chair Stedman reminded that the committee would be focusing much narrower than ten years forward because of the substantial deficit and would be reining in some of the analyses to look forward two to three years.

[10:35:30 AM](#)

Mr. Painter reviewed slide 32, "Governor's 10-Year Plan in LFD Model, No ERA Overdraws," which showed two bar graphs and a table. He explained that LFD's model showed similar numbers to the governor's because the assumption differences balanced out. There was a deficit of about \$1 million in FY 25, shrinking slightly then growing to a peak of \$1.5 billion. The governor's plan was submitted and showed the CBR being drawn to negative \$10 billion by FY 33. The statutory requirement in the ten-year plan was to balance the sources of revenues and expenditures and fund balances. He continued that the governor's 10-year plan did not provide a full fiscal solution, and just funded the CBR

negatively. He noted that LFD's model did not run the CBR negative but showed an unfilled deficit. He noted that the deficits were smaller than in the baseline model because of the governor's proposed policy changes.

Mr. Painter spoke to slide 33, "Governor's 10-Year Plan in LFD Model with ERA Overdraws," which showed if the legislature chose to fill the deficits out of the ERA rather than leaving them unfilled, it would draw the ERA down for a combined ERA/CBR balance of about \$2.5 billion by FY 33. He thought it was unlikely that the legislature would do so, but the slide showed what the ten-year plan would result in.

Co-Chair Stedman suggested that the data include the Permanent Fund Market value.

Mr. Painter showed slide 34, "Questions?":

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Co-Chair Stedman explained that the slides had shown preliminary data and future presentations would reflect updated numerics from the governor over the next several weeks.

Co-Chair Stedman discussed the agenda for the afternoon meeting.

ADJOURNMENT
[10:38:44 AM](#)

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