HJR

39

Berrier
1/17/84

DRAFT

IN THE HOUSE BY THE STATE AFFAIRS COMMITTEE

CS FOR HOUSE JOINT RESOLUTION NO. 39 (State Affairs)

IN THE LEGISLATURE OF THE STATE OF ALASKA

THIRTEENTH LEGISLATURE - SECOND SESSION

Proposing amendments to the Constitution of the State of Alaska creating an appropriation reserve fund and limiting increases in appropriations.

BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. Article IX, sec. 16, Constitution of the State of Alaska, is repealed and reenacted to read:

SECTION 16. APPROPRIATION LIMITATIONS. Except for appropriations to the Alaska permanent fund and appropriations required to pay the principal and interest on general obligation bonds, appropriations from the treasury during a fiscal year may not exceed the lesser of 95 percent of the unrestricted revenue of the state for the previous calendar year or the amount appropriated in the year this section takes effect adjusted for the cumulative inflation and population growth or decline as defined by law. An appropriation in excess of this limit may not be made unless a state of emergency is declared by the governor as provided by law.

4, etc.

Amend #1

* Sec. 2. Article IX, Constitution of the State of Alaska, is amended by adding a new section to read:

SECTION 17. APPROPRIATION RESERVE FUND. An appropriation reserve fund is established. Appropriations may not be made from the appropriation reserve fund except for the purpose of repelling invasion, suppressing insurrection, defending the state in war, meeting natural disasters, or ~~redeeming indebtedness of the state outstanding at the time this section becomes effective.~~ appropriations required to pay the principal & interest on GO debt After June 30 of the year

attach

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~~in which the balance of the appropriation reserve fund exceeds the total unrestricted revenue of the state for the preceding 18 months, the balance of the appropriation reserve fund shall lapse into the treasury~~. The balance of the appropriation reserve fund shall be invested at competitive national market rates. All earning of the fund shall become part of the principal of the fund.

* Sec. 3. Article XV, Constitution of the State of Alaska, is amended by adding a new section to read:

SECTION 29. APPROPRIATION RESERVE FUND. Beginning July 31, 1985, and continuing until June 30 of the year in which the balance of the appropriation reserve fund ~~exceeds the total unrestricted revenues of the state for the preceding 18 months~~, an amount equal to 8.8 percent of the unrestricted revenue for each month, as determined in accordance with this section, shall be transferred from the treasury to the appropriation reserve fund. Any balance transferred to the appropriation reserve fund under section 30 of article XV shall reduce by the balance transferred the amount required to be transferred in a year by the provisions of this section but no excess amount transferred may be carried forward to reduce the amount required to be transferred in another fiscal year.

* Sec. 4. Article XV, Constitution of the State of Alaska, is amended by adding a new section to read:

SECTION 30. APPROPRIATION LIMITATIONS. After June 30, 1986, and until June 30 of the year in which the balance of the appropriation reserve fund exceeds the total unrestricted revenue of the state for the preceding 18 months, except for appropriations to the Alaska permanent fund and appropriations required to pay the principal and interest on general obligation bonds, appropriations from the treasury during a fiscal year may not exceed the amount appropriated in the

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prior fiscal year by more than the cumulative inflation and population growth or decline as prescribed by law. An appropriation in excess of this limit may not be made unless a state of emergency is declared by the governor as provided by law. No less than 25 percent of that portion of the unrestricted revenue of the state which has not been appropriated as allowed by this section shall be transferred from the general fund to the appropriation reserve fund. on the 1st of each fiscal year

* Sec. 5. Section 1 of this amendment takes effect on July 1 of the year in which the balance in the appropriation reserve fund established in sec. 2 of this amendment exceeds the total of the unrestricted revenue of the state for the preceding 18 months.

* Sec. 6. The amendments proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

A M E N D M E N T

Offered in the HOUSE By Abood

TO: HJR 39

Page 1, lines 25 and 26:

Delete: "the legislature shall annually appropriate"

Insert: "there shall be transferred"

SUGGESTED AMENDMENTS TO HJR 39 FOR HOUSE STATE AFFAIRS COMMITTEE, 2/8/84

Amend #1

1. PAGE 1, LINE 16, LANGUAGE SHOULD READ, FOR CLARIFICATION, "LESSER OF THE AMOUNT APPROPRIATED IN THE YEAR THIS SECTION TAKES EFFECT ADJUSTED FOR THE CUMULATIVE INFLATION AND POPULATION GROWTH AS DEFINED BY LAW OR 95 PERCENT OF THE UNRESTRICTED REVENUE OF THE STATE FOR THE PREVIOUS CALENDAR YEAR."

Amend #2 see bill

2. PAGE 1, LINE 28, LANGUAGE SHOULD READ, TO PREVENT A RUN ON THE RESERVE FOR THE PURPOSE OF RETIRING ALL OUTSTANDING INDEBTEDNESS, "NATURAL DISASTERS, OR AS REQUIRED FOR REDEEMING INDEBTEDNESS OF THE STATE OUTSTANDING"

3. PAGE 2, LINE 1, SHOULD READ, TO OBVIATE THE POSSIBLE EFFECT OF A WIDE SWING IN REVENUES IN ANY ONE YEAR, "IN WHICH THE BALANCE OF THE APPROPRIATION RESERVE FUND EQUALS 1.5 TIMES THE APPROPRIATIONS OF ~~GENERAL FUND~~ UNRESTRICTED REVENUES FOR THE PRECEDING FISCAL YEAR." THIS CHANGE SHOULD ALSO BE REFLECTED IN PAGE 2; LINE 11: PAGE 2; LINE 24: PAGE 3; LINE 10.

4. PAGE 3, LINE 1, IN ORDER TO OBVIATE THE EFFECTS OF A LOW REVENUE YEAR DURING THE REVENUE PERIOD, SHOULD READ, "YEAR IN WHICH THIS SECTION BECOMES EFFECTIVE BY MORE THAN THE CUMULATIVE POPULATION AND INFLATION"

5. PAGE 3, LINE 7, SENTENCE SHOULD CONTINUE "ON THE FIRST DAY OF EACH FISCAL YEAR", SINCE NO TIME FOR DEPOSIT IS SPECIFIED IN PRESENT LANGUAGE.

6. PAGE 2, LINE 15, LANGUAGE SHOULD READ "TO THE APPROPRIATION RESERVE FUND AT THE BEGINNING OF EACH MONTH." THIS CLARIFIES LANGUAGE WHICH MIGHT OTHERWISE ALLOW TREASURY TO MAKE DEPOSITS ANNUALLY.

ALASKA STATE LEGISLATURE
HOUSE OF REPRESENTATIVES
RESEARCH AGENCY

Pouch Y, State Capitol
Juneau, Alaska 99811
(907) 465-3991

February 7, 1984

MEMORANDUM

TO: Neil Phelps-Munson
Professional Assistant

FROM: Alexander Hoke
David Teal
Legislative Analysts

Alexander Hoke
Teal

RE: Comments on CS HJR 39

As you requested, we have reviewed the House State Affairs Committee work draft of CS HJR 39. We offer the following comments:

Page 1; Line 16. As discussed on an earlier occasion, limiting appropriations to "95 percent of the unrestricted revenue of the state for the previous calendar year...." leaves a residual of 5 percent in the general fund each year. While the interest earnings on this 5 percent residual can be appropriated in future years, the principal will remain in the general fund. This means that the general fund will grow perpetually, potentially raising the general fund balance to $20 billion by the year 2010.

Also, the wording in this section is somewhat ambiguous in that the 95 percent limitation seems to apply to both limiting mechanisms. This ambiguity can be cleared up by reversing the order of the two limiting mechanisms in this paragraph.

Page 1; Line 28. During the period when contributions are being made to the CBB reserve fund, provisions in this section prohibit appropriations from the fund except for the purpose of "redeeming indebtedness of the state outstanding at the time this section becomes effective." Our concern is that with this language, the CBB reserve could conceivably be raided to pay off the State's total indebtedness outstanding which is currently estimated to be about $518 million.

Page 2; Line 2. After carefully considering the mechanism for triggering the automatic start-up of cash-based budgeting, two suggestions come to mind. First, instead of setting the CBB reserve target equal to "total unrestricted revenue of the state for the preceeding 18 months," it might prove useful to set the target equal to "1.5 times the appropriations of general fund unrestricted revenue for the preceeding fiscal year." This procedure ties future appropriation levels to past appropriation levels regardless of what total revenues may have been for the prior year.

Secondly, since the effective level of appropriations (during the years when contributions to the CBB reserve are being made) is diminished by the amount of annual contributions to the reserve fund, the CBB reserve target might be tied to the effective level of appropriation also. This can be achieved with the following language:

"After June 30 of the year in which the balance of the appropriation reserve fund exceeds 1.5 times the appropriations of general fund unrestricted revenue for the preceeding fiscal year less any appropriations to the appropriation reserve fund,..."

The trigger mechanism described above would lower the target amount needed to start cash-based budgeting by the amount of the final year contributions to the CBB reserve. As a consequence, cash-based budgeting could begin one year earlier, or the annual contribution percentages could be lowered as described later.

Any changes to the definition of the automatic CBB start-up mechanism should also be made in the following locations:

Page 2; Line 11
Page 2; Line 24
Page 3; Line 10

Page 2; Line 12. The percentage for contributions of general fund unrestricted revenue is set at 8.8 percent in the work draft. With the new automatic start-up language stated above, other percentages may be in order. A 10.3 percent monthly contribution of general fund unrestricted revenues would be sufficient to trigger an automatic start of cash-based budgeting in FY 94 according to a 30th percentile revenue forecast. In order to begin cash-based budgeting by FY 93, the monthly general fund contribution percentage should be set at 11 percent, and a front-end contribution of $325 million would have to be made during the current session.

Page 2; Line 29 - Page 3; Line 2. Section 30 sets an appropriation limitation that will be effective during the period of time when contributions are being made to the CBB reserve fund. This provision limits annual appropriations to the previous year's appropriations adjusted for changes in population and inflation. This limitation mechanism may present a problem if there is a single unexpectedly low revenue year during the CBB reserve contribution period. With a single low year, the appropriation limit for all subsequent years would be tied to the lowest level in the period, whether or not revenues rebound to higher levels.

An alternative is to limit annual appropriations to the amount of the appropriations in the year that this section becomes effective, with adjustments for inflation and population change (as was done in Section 16; Page 1; Line 17).

Page 3; Lines 4-7. There is no provision in this section which sets the timing of contributions from the year-end unappropriated general fund balance. We suggest that language be added to the end of this section which states that this contribution occurs once each year, preferably at the start of the year.

AH/DT

Introduced: 3/18/83
Referred: State Affairs and
Finance

BY HAYES, ABOOD, BARNES,
BETTISWORTH, COWDERY, FLOOD,
LISKA, MARTIN, RINGSTAD,
UEHLING, WARD, LINDAUER
AND BUSSELL

IN THE HOUSE

HOUSE JOINT RESOLUTION NO. 39

IN THE LEGISLATURE OF THE STATE OF ALASKA

THIRTEENTH LEGISLATURE - FIRST SESSION

Proposing amendments to the Constitution of the State of Alaska creating an appropriation reserve fund.

BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. Article IX, Constitution of the State of Alaska, is amended by adding a new section to read:

SECTION 17. APPROPRIATION RESERVE FUND. An appropriation reserve fund is established. After July 1, 1992, no money in excess of the balance of the appropriation reserve fund at the close of the preceding fiscal year shall be withdrawn from the treasury except for the purpose of repelling invasion, suppressing insurrection, defending the State in war, meeting natural disasters, or redeeming indebtedness outstanding at the time this section becomes effective. After July 1, 1992, all revenue of the State shall be placed in the appropriation reserve fund and the balance of the appropriation reserve fund shall lapse into the treasury at the close of each succeeding fiscal year.

* Sec. 2. Article XV, Constitution of the State of Alaska, is amended by adding a new section to read:

SECTION 26. APPROPRIATION RESERVE FUND. Beginning with the First Session of the Fourteenth Legislature and continuing through the First Session of the Seventeenth Legislature, the legislature shall annually appropriate from the general fund to the appropriation reserve fund an amount equal to 15 percent of the average gross receipts of the general fund, as determined in accordance with this section. For the purposes of this section, "average gross receipts of the general fund" is determined by dividing the total amount of money deposited in the general fund and in special accounts within the general fund (other than the appropriation reserve fund) from all sources during the four fiscal years immediately preceding the current fiscal year by four.

* Sec. 3. The amendments proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

Introduced: 3/18/83
Referred: State Affairs and
Finance

BY HAYES, ABOOD, BARNES,
BETTISWORTH, COWDERY, FLOOD,
LISKA, MARTIN, RINGSTAD,
UEHLING, WARD, LINDAUER
AND BUSSELL

IN THE HOUSE

HOUSE JOINT RESOLUTION NO. 39

IN THE LEGISLATURE OF THE STATE OF ALASKA

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* Sec. 2. Article XV, Constitution of the State of Alaska, is amended by adding a new section to read:

SECTION 26. APPROPRIATION RESERVE FUND. Beginning with the First Session of the Fourteenth Legislature and continuing through the First Session of the Seventeenth Legislature, there shall be transferred ~~the legislature shall~~ annually ~~appropriate~~ from the general fund to the appropriation reserve fund an amount equal to 15 percent of the average gross receipts of the general fund, as determined in accordance with this section. For the purposes of this section, "average gross receipts of the general fund" is determined by dividing the total amount of money deposited in the general fund and in special accounts within the general fund (other than the appropriation reserve fund) from all sources during the four fiscal years immediately preceding the current fiscal year by four.

* Sec. 3. The amendments proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

STATE OF ALASKA
FISCAL NOTE

Revision Date , 1983

I. REQUEST

Bill/Resolution No: HJR 39
Title: Amendments to Constitution to Create Appropriation Reserve Fund
Sponsor: Hayes
Requestor: State Affairs Committee

II. FISCAL DETAIL

Agency Affected: Revenue
Program Category Affected:
BRU, Program of Subprogram(s) Affected:

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 83	FY 84	FY 85	FY 86	FY 87	FY 8
OPERATING						
100 PERSONAL SERVICES	-	-	-	-	-	
200 TRAVEL	-	-	-	-	-	
300 CONTRACTUAL	-	-	-	-	-	
400 COMMODITIES	-	-	-	-	-	
500 EQUIPMENT	-	-	-	-	-	
600 LANDS & STRUCTURES	-	-	-	-	-	
700 GRANTS, CLAIMS, ETC.	-	-	-	-	-	
TOTAL OPERATING	-	-	-	-	-	
CAPITAL	-	-	-	-	-	
REVENUE	-	-	-	-	-	

FUNDING: (Thousands of Dollars)

	FY 83	FY 84	FY 85	FY 86	FY 87	FY 8
GENERAL FUND	-	-	-	(545,900)	(475,800)	(433, (433,200)
FEDERAL FUNDS	-	-	-	-	-	
OTHER (Specify Source)	-	-	-	-	-	
Appropriation Reserve Fund	-	-	-	524,900	488,150	475,3 475,351

POSITIONS:

FULL-TIME	-	-	-	-	-	
PART-TIME	-	-	-	-	-	
TEMPORARY	-	-	-	-	-	
	-	-	-	-	-	

III. SOURCE OF FUNDS TO OFFSET FISCAL IMPACT OF BILL:

IV. ANALYSIS: Attach a separate page for any Analysis.

Prepared By: Vincent D. Wright VW
Division: Revenue - Research
Phone: 465-2173
Date: 4/13/83

Approved by Commissioner: [signature]
Department: Revenue
Date: 4/18/83

Distribution:
- Original to Legislative Finance
- Copy to Office of Management and Budget (for Legislature introduced bills)
- Copy to Department (for Governor introduced bills)
- Copy to Sponsor
- Copy to Requestor (if different from Sponsor)

IV. Analysis of HJR 39

The effect of these proposed constitutional amendments is to create an appropriation reserve fund (ARF). For each fiscal year from 1986 through 1992 the Legislature would be required to appropriate from the general fund (GF) to the ARF an amount equal to 15 percent of the average gross receipts of the GF excluding the appropriation to the ARF for the four preceding fiscal years. Thus the appropriation to the ARF in fiscal year 1986 would be 15 percent of the total gross receipts of the GF for fiscal years 1982 through 1985 divided by four and so on. Beginning with fiscal year 1993 the entire receipts of the state would be placed in the ARF and only the balance in the ARF at the close of the preceding fiscal year would be put in the GF and made available for appropriations. Thus the amount accumulated in the ARF from fiscal years 1986 through 1992 could be spent in fiscal year 1993 and the receipts from fiscal year 1993 could be spent in fiscal year 1994 and so on.

The amounts shown on the accompanying fiscal note as a reduction in GF revenues represent both the estimated appropriation to the ARF and the resulting reduction in GF investment earnings for the respective fiscal years. The amounts shown as an increase in ARF revenues represent both the estimated appropriation to the ARF for the respective fiscal year and the estimated earnings on the ARF balance from the preceding fiscal year.

Tax Exempt Home Mortgage Bonds (supporting legislation)

HOUSE JOINT RESOLUTION NO. 37, by Reps. Uehling, Barnes, Bussell, Cowdery, Furnace, Lindauer, Liska, Martin, Pestinger, and Ward. Supports passage of H.R. 1176 and S. 137 in the U.S. Congress, amending the Internal Revenue Code to allow certain home mortgage bonds to continue to be tax-exempt. States that the tax-exempt mortgage revenue bond program under 26 U.S.C.103A (P.L. 96-499 Mortgage Subsidy Bond Act of 1980) ends on December 31, 1983, and states that its termination would work a hardship on consumers who are eligible for loans under the Alaska Housing Finance Corporation tax-exempt bond program and similar programs in other states. Resolves that the Alaska Legislature supports passage of H.R. 1176 and S. 137 in Congress to allow continuation of the tax-exempt mortgage revenue bond program. (Identical to SJR 20, page 310.)

Introduced March 16 and referred to the House Special Committee on State Loans, Finance.

Natural Gas (transporting & marketing)

HOUSE JOINT RESOLUTION NO. 38, by Reps. Cowdery, Abood, Barnes, Bettisworth, Bussell, Cato, Glood, Fritz, Fuller, Furnace, Grussendorf, Hurlbert, Koponen, Lacher, Larson, Lindauer, Liska, Martin, M.W. Miller, Pestinger, Phillips, Ringstad, Shultz, Tischer, Uehling, Ward, Wendte and Hayes. Resolves that the state of Alaska fully supports the efforts of all owners of the gas and other parties to secure sales commitments for North Slope gas in any market, including within the state. States that citizens of Japan, Korea, and other trading partners of Alaska, are strongly urged to consider and take advantage of the secure, long-term trading relationship with Alaska and the U.S. that purchase of Alaska's North Slope gas would offer. States that the Legislature calls upon the other owners of the gas, Alaska's delegation in Congress and all other parties with an interest in the gas to explore every means to privately finance and construct a transportation system for the gas.

Resolves that the State of Alaska immeadiately enter into negotiations for the sale of its royalty interest in North Slope gas to in-state users in order that they and the state serve as a catalyst for the construction of a transportation system for Alaska's natural gas. Resolves that the federal government is urged to explore the prospect of making development of gas transportation facilities a National Interst Project of nations on both sides of the Pacific for its long term benefits to this nation and its potential trading partners.

Introduced March 18 and referred to Resources.

* Appropriation Reserve Fund (creation of)

HOUSE JOINT RESOLUTION NO. 39, by Reps. Hayes, Abood, Barnes, Bettisworth, Cowdery, Flood, Liska, Martin, Ringstad, Uehling, Ward, Lindauer, and Bussell. Proposes amendment to the state constitution creating an appropriation reserve fund. Amends article 9 (Finance and Taxation) to provide that after July 1, 1992, no money in excess of the balance of the appropriation reserve fund at the close of the preceding fiscal year shall be withdrawn from the treasury except for wars, natural disasters, or redeeming indebtedness outstanding at the time section becomes

HJR 39 (cont'd)

effective. After July 1, 1992 all state revenue shall be placed in the fund and the balance of the fund shall lapse into the treasury at the close of each succeeding fiscal year.

Amends article 15 (Schedule of Transitional Measures) to provide that beginning with the first session of the 14th Legislature and continuing throu the first session of the 17th Legislature, the legislature shall annually appropriate from the general fund to the appropriation reserve fund an amount equal to 15% of the average gross receipts of the general fund. The average gross receipts are determined by dividing the total amount of money deposited in the general fund and in special accounts within the general fund from all sources during the four fiscal years immediately preceding the current fiscal year by four.

Provides amendments proposed by resolution be placed before the voters at the next general election.

Introduced March 18 and referred to State Affairs, Finance.

Public School Foundation Program (est. Joint Committee on)

HOUSE CONCURRENT RESOLUTION NO. 23, by Reps. Koponen, Clocksin, Davis, Duncan, Goll, Larson, McBride, M. M. Miller, Szymanski, Vaska, Wendte, Zharoff and Malone. Would establish a Joint Committee on the public school foundation program. Provides the President of the Senate appoint three members and the Speaker of the House appoint three members and the President and Speaker jointly appoint one chairperson to study and make recommendations for improving the public school foundation program.

The committee is to report the scope of its intended research to the legislature no later than May 31, 1983 and make a final report by February 1, 1984. The committee shall have the power to call witnesses, hold hearings, and hire staff. The committee is encouraged to hear witnesses from the Alaska School Board Association, the Office of Management and Budget, the Department of Education, the State Board of Education, the Alaska Council of School Administrators, and other concerned groups. The committee terminates February 1, 1984.

Introduced March 14 and referred to Health, Education & Social Services, Finance.

Public School Foundation Program (state funding)

HOUSE CONCURRENT RESOLUTION NO. 24, by Reps. Koponen, Clocksin, Davis, Duncan, Goll, Larson, McBride, M. M. Miller, Vaska, Wendte, Zharoff and Malone. States that school districts in the state are required by law to prepare local school district budgets by April 1, 1983 and preparation of these budgets requires calculation of the amount to be contributed by the state under the public school foundation program. Resolves that the Alaska State Legislature pledges to appropriate 100 percent of its share of funding under the program so that local districts may have a firm figure on which to base their budget estimates.

Introduced March 14 and referred to Health, Education and Social

CASH-BASED BUDGETING:
A Response To Revenue Uncertainty

EXECUTIVE SUMMARY

House Research Agency
Alaska State Legislature
January 1984

House Research Agency Report 83-A

CASH BASED BUDGETING: A RESPONSE TO REVENUE UNCERTAINTY

EXECUTIVE SUMMARY

Cash-based budgeting (CBB) has been proposed as a means of eliminating the budgeting problems created by uncertain and fluctuating State revenues. Cash-based budgeting (also known as "forward funding") would reduce or eliminate uncertainty by tying the State budget for a given year to the amount of revenues already received and deposited in the treasury during a prior year. Before enacting or signing the budget, the legislature and governor would know exactly how much money was actually available to spend.

Conventional budgeting practices in most states (including Alaska) involve forecasting revenues for the coming fiscal year. Appropriations included in the budget are limited to the anticipated revenues for that year. With approximately 85 percent of Alaska's total revenues dependent on oil taxes and royalties, an error in projecting the price of oil or production level for the coming year can result in substantial miscalculations of total available revenues.

In response to the risk associated with any forecast of future revenues for the State of Alaska, the Department of Revenue began issuing a "risk adjusted" forecast for the FY 84 budget year. The so called "30th percentile" forecast implies that actual revenues are likely to fall short of the projected amount only 30 percent of the time. This means that there is a 70 percent probability that actual revenues will equal or exceed the forecast for that year.

"Revenue Uncertainty" And The Design Of A CBB Program

Given that the objective of the cash-based budgeting proposal is to resolve the "revenue uncertainty" problem, it is important that the concept of revenue uncertainty be fully understood.[1] Revenue certainty relates to the likelihood that incoming revenues will be sufficient to cover budgeted appropriations. If "reasonable certainty" is sufficient for budgeting purposes, one might choose to limit appropriations to the 30th percentile revenue projection (which gives a 70 percent assurance that actual revenues will equal or exceed budgeted appropriations).

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[1] It is important to recognize that the "revenue uncertainty" addressed by cash-based budgeting relates to a 12 or 18-month time period. The revenue uncertainty associated with a projected long-term revenue decline is not the specific target of cash-based budgeting.

Only when a 100 percent probability exists that revenues will be sufficient to offset budgeted appropriations for the next fiscal year can one say that "revenue uncertainty" has been eliminated. This means that the legislature and governor must know that there is "cash in the bank" sufficient to meet expenditures budgeted for the next year.

The major requirement of a cash-based budgeting program is the creation of a cash reserve from which appropriations can be made.[2] A cash reserve equal to 18-months of expenditures is required if the legislature wishes to begin each session with absolute certainty that there is sufficient cash to meet expenditures budgeted for the next fiscal year. For absolute certainty on July 1 (the start of the budget year), only 12-months of revenues are required in the reserve. Funding of the CBB reserve fund can be structured in two basic ways:

- a single very large deposit would allow for a near-term implementation of cash-based budgeting, or

- smaller annual deposits over a period of years would provide for a delayed start of this budgeting system.

Based on the assumption that the current State government expenditure policy of appropriating total projected revenues applies for the year in which cash-based budgeting begins, an 18-month CBB reserve must contain $4.836 billion to start cash-based budgeting in FY 86, or $5.173 billion for a delayed start in FY 94.

Deferred Implementation of Cash-Based Budgeting

During the current session, legislative attention on cash-based budgeting has focused on a long-term payment plan (CS HJR 39) for developing the CBB reserve fund. There are essentially three sources of funding the CBB reserve for deferred implementation of cash-based budgeting: the General Fund, Permanent Fund earnings, and new or higher taxes. Over a period of years, contributions to the CBB reserve would come from one or a combination of these sources (CS HJR 39 targets general fund unrestricted revenues). A significant feature of CS HJR 39 (and the computer model used in this report) is the automatic start-up of cash-based budgeting once the reserve fund exceeds the total expenditures in the preceding 18 months.

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[2] A Constitutional amendment is the generally preferred means of creating the reserve fund and defining its use for budgetary purposes. The Constitution would serve to insulate the cash-based budgeting reserve fund from the political process much as is the case with the Permanent Fund.

The General Fund. In this report, General Fund unrestricted revenues identified as potentially available for contribution to a CBB reserve fund are those revenues "in excess" of the projected operating costs of government. For this purpose, no real growth in the Operating Budget above the FY 84 level ($2.057 billion) is assumed.

Three mechanisms for obtaining contributions to the CBB reserve fund are considered in this report:

- A percentage of unrestricted revenues deposited into the CBB reserve fund monthly;

- A "grubstake" contribution to the CBB reserve fund appropriated in the 1984 legislative session to become effective contingent on voter approval of the CBB program during the 1984 general election.

- A percentage of the balance of unobligated (unappropriated) revenues remaining in the General Fund at the end of each year.

Assuming that actual revenues match the 30th percentile revenue forecast, annual contributions of 11.6 percent of total unrestricted revenues would enable the CBB reserve fund to attain the 18-month reserve requirement of $5.173 billion by FY 94. An FY 94 cash-based budgeting start-up could also be achieved with an annual General Fund contribution of 10 percent if a front-end (grubstake) contribution of $325 million were made during the current session. Under these options, annual contributions to the CBB reserve fund would range between $325 million and $472 million. General Fund "excess revenues" would be sufficient to meet CBB contribution requirements in every year except FY 92 and FY 93.

Permanent Fund Earnings. Permanent Fund earnings are another potential source of funds for a CBB reserve account. This report assumes the Permanent Fund is restructured to allow annual contributions to the CBB reserve fund. In addition, the Undistributed Income Account balance of the Permanent Fund (estimated at $535.6 million for FY 85) is assumed to be deposited into the CBB reserve fund as a grubstake contribution.

Under this set of assumptions, Permanent Fund earnings contributed to the CBB reserve fund are projected to increase from $208 million in FY 86 to $457 million in FY 93. Given the earnings potential of the CBB reserve fund, cash-based budgeting could be started in FY 95 with Permanent Fund earnings as a source of contributions.

New or Higher Taxes. A third alternative for funding cash-based budgeting is through new or higher taxes. However, this approach is less promising than the General Fund or Permanent Fund earnings options for the following reasons:

- The political feasibility of raising petroleum taxes is a matter of considerable conjecture, especially in light of the Congressional debate over the need to limit the ability of petroleum producing states to increase oil production taxes.

- Given the January, 1984 estimate of all nonpetroleum tax revenue of $131 million, tax rates would have to be three to four times higher than existing rates in order to meet CBB reserve contribution requirements of between $300 to $450 million per year.

- A reinstituted Alaska individual income tax could potentially raise revenues of around $225 million per year. This potential source of funds for cash-based budgeting is of a sufficient magnitude to fund a CBB reserve by the late 1990s, but may also be useful as a supplementary source of funds under other implementation options.

Near-Term Implementation of Cash-Based Budgeting

Two methods by which cash-based budgeting could conceivably be implemented soon after voter approval in 1984 are by a loan from the Permanent Fund and by bonding. Both options would require adoption of a constitutional amendment allowing the State to incur debt for purposes other than for capital construction projects. Assuming cash-based budgeting could begin in FY 86, both the permanent fund loan and bonding methods would involve a lump sum deposit into the CBB reserve fund of $4.836 billion.

Permanent Fund Loan. The plan for repayment of the Permanent Fund loan depends on the interest rate and repayment period assumed. Given a 7-year repayment period and an annual interest rate of ten percent, $479 million per year (in addition to interest earnings on the balance) would be diverted from the General Fund to repay the loan.

The Permanent Fund loan approach to funding the CBB reserve presents difficulties for the following reasons:

- The loan repayment plan stated above assumes perfect liquidity of Permanent Fund investments. In actuality, some Permanent Fund investments are not readily retrievable for contribution into the CBB reserve fund. Consequently, the start-up date for cash-based budgeting may be delayed from 2 to 3 years, and the annual repayment amounts would be increased since the CBB reserve fund target grows in proportion to revenue projections through FY 90.

- A serious drawback of the Permanent Fund loan concept is the precedent that such a use of the permanent fund principal would set.

- A Permanent Fund loan would likely be viewed by the bond market as no different than any other general obligation debt of the State. Consequently, this very large outstanding debt might cause the State's AA bond rating to drop to A or A-, making further bond sales for any State agency more expensive while the loan was being repaid. Furthermore, a debt of the magnitude of $4.8 billion would eliminate any further debt capacity for the State until this loan is repaid.

Bonding. An alternative near-term cash-based budgeting funding source is bonded debt. If $4.836 billion in bonds could be sold by the State, cash-based budgeting could be started in the near term with a repayment schedule much like that which would occur under the Permanent Fund loan option. The following potential problems are associated with the bonding alternative:

- According to a recent report of State debt capacity, an additional $1.2 billion in debt could potentially be incurred by the State through FY 90 only by doubling its current debt service to revenue ratio. This report recommends against such an increase in the debt service/revenue ratio since the State's AA bond rating would be in jeopardy.[3]

- The Internal Revenue Service (IRS) forbids financial arbitrage with regard to revenues raised by sale of tax exempt bonds. This means the State would be prohibited from investing revenues raised by bond sales at interest rates higher than those pertaining to the sale of the bonds. This factor would effectively raise the overall cost of the bonding alternative for funding cash-based budgeting by the amount of foregone interest earnings of CBB reserve fund investments.

The Fiscal Benefits and Limitations of Cash-Based Budgeting

The intent of legislation proposing cash-based budgeting is to create a budgeting system which will allow legislators to know precisely how much money can be appropriated in the budgets that they will prepare. However, cash-based budgeting is more than simply a mechanism for making revenues more certain.

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[3] A Review of Debt Capacity and Debt Management for the State of Alaska; August 1983, prepared by Government Finance Research Center-Municipal Finance Officers Association, Washington D.C.

Fiscal Restraint. The implementation of cash-based budgeting would provide for a constitutional prohibition against deficit spending by requiring that appropriations for a given fiscal year may not exceed total revenues already in hand from the prior calendar year. In addition, about $400 million per year would be diverted from the revenue stream to the CBB reserve fund during the period of reserve fund growth. In those years, less revenues would be available for appropriation for other purposes.

Bringing Certainty To The Budgeting Process. Knowing exactly how much money is available for appropriation each year is different from the task of allocating available funds. Even though the size of the pie will be known under cash-based budgeting, the problems of dividing up the pie will still require difficult political decisions. For local governments and school districts, who rely on State appropriations to finalize their budgets, uncertainty over revenues would remain until the legislative allocation process is complete. This source of revenue uncertainty will become an increasing problem for local jurisdictions during a period of declining revenues as a consequence of increasingly intense competition among contenders for a piece of the budget pie.

In addition, cash-based budgeting resolves the "revenue uncertainty" problem for budgeting purposes on a year-to-year basis, it does not eliminate the considerable uncertainty concerning how the State will budget "within its means" during a period of projected declining revenues.

Revenue Stability - Smoothing. With the start of cash-based budgeting, an element of revenue stability would be introduced to the extent that revenues needed to cover future appropriations will be "in the bank." However, cash-based budgeting would do nothing to smoooth out an eratic revenue stream (including both sharp increases and dramatic drops) since revenues would presumably be appropriated at the same level at which they were received 18-months earlier.

Cash-Based Budgeting As An Expenditure Limitation. As a limit on expenditures, cash-based budgeting differs from conventional expenditure limitations which are tied to growth in demand for governmental services (population growth) and changes in the costs of goods and services. Instead, cash-based budgeting is simply bound to increases or declines in total State revenues which are predominately determined by changes in the price and production level of petroleum.

Flow Charts Showing the Implementation of Cash-Based Budgeting

Figures 1 and 2 illustrate the transition to cash-based budgeting under the deferred implementation option. Figure 1 shows the timing of the flow of funds and Figure 2 shows the anticipated impact of CBB on State expenditures. Information provided by the graphs is summarized below.

Figure 1 shows that:

- the current practice of preparing the annual budget during the preceding fiscal year is retained under CBB;
- the current practice of spending revenues during the period in which they are collected continues during the transition period (1986 through 1993);
- a portion of annual revenues is diverted to the CBB Reserve Fund during the transition period;
- the CBB Reserve Fund is transferred to the General Fund in 1994 and is the source of money spent during FY 94;
- revenues collected during the first half of FY 94 are held for expenditure in FY 95;
- the CBB Reserve Fund is the source of the remainder of the money spent during FY 95; and
- beginning in 1996, expenditures during the fiscal year are limited to the amount of revenue collected in the preceding calendar year.

Figure 2 shows that:

- contributions to the CBB Reserve Fund begin in 1986 and continue through 1993;
- annual contributions to the CBB Reserve Fund reduce the level of expenditure because they divert revenue which would otherwise go to the General Fund;[4]

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[4]This conclusion is based on the assumption that expenditures will equal revenues in each year. If the amount budgeted without cash-based budgeting is less than revenues, the reduction in spending under cash-based budgeting would be less than shown in the graph.

- the CBB Reserve Fund grows to over $5 billion in 8 years, including $1.8 billion in interest earnings;
- contributions stop when the balance of the CBB Reserve Fund exceeds total revenues for the preceding 18 months;
- when the balance of the CBB Reserve Fund is transferred to the General Fund in 1994, expenditures can exceed the level of expenditure that could have occurred without CBB;
- future interest earnings from the large General Fund balance permit higher annual levels of expenditures than could occur without those interest earnings;
- although CBB permits a higher level of future expenditures, the level of expenditures follows the same trend as expenditures without CBB; and
- CBB does not reduce annual fluctuations in the permissible level of expenditures.

Figure 1

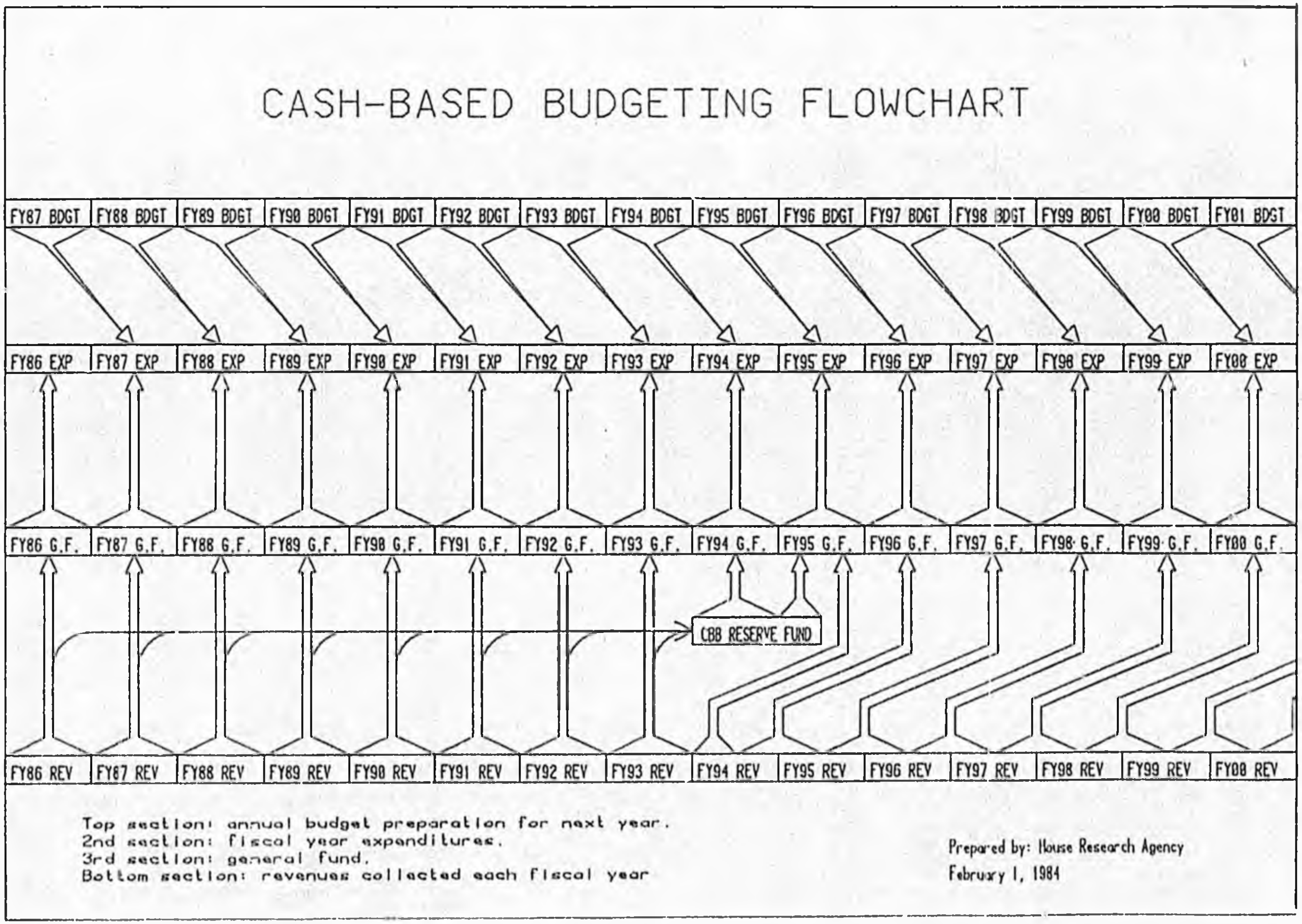
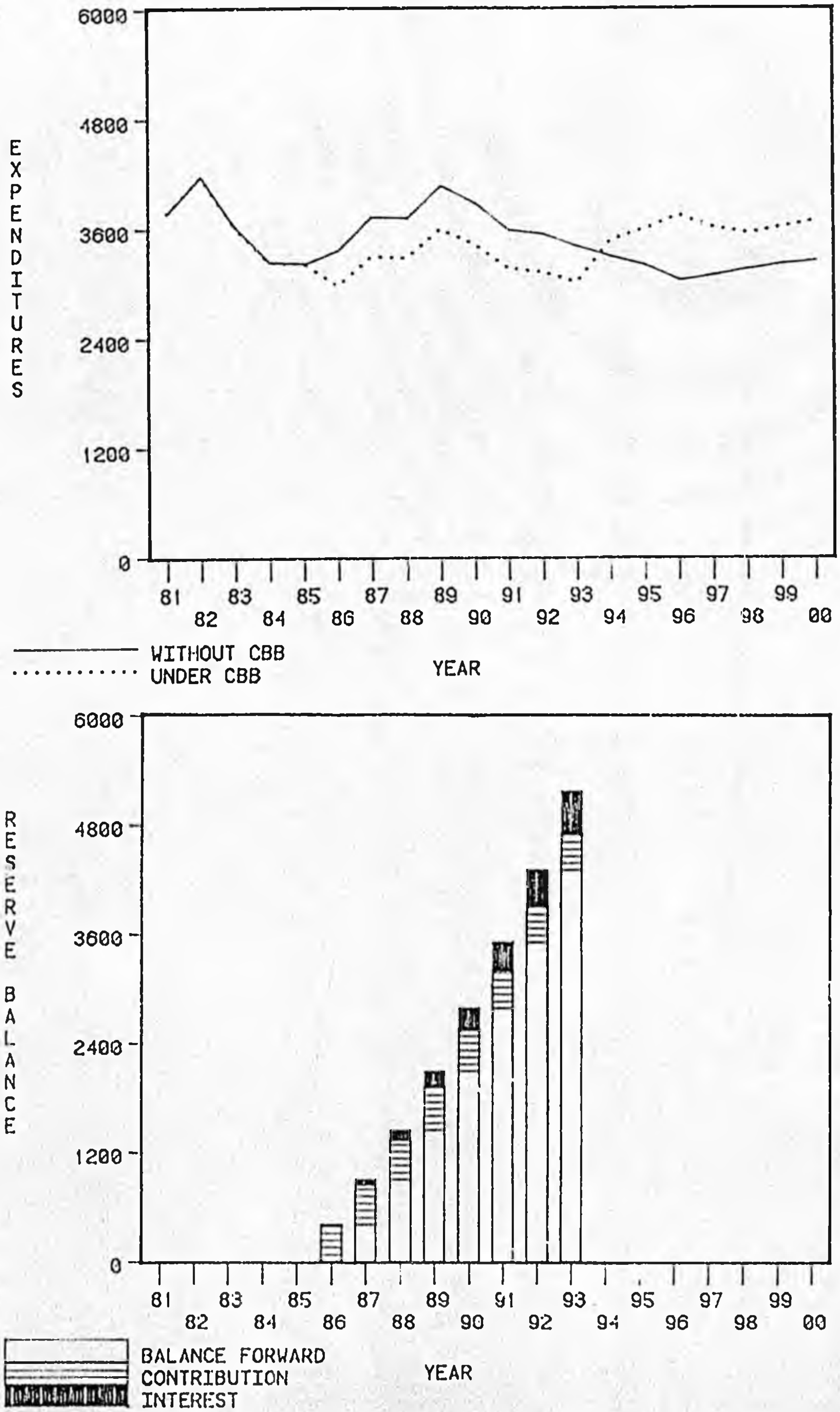

CASH-BASED BUDGETING FLOWCHART
FY87 BDGT
FY88 BDGT
FY89 BDGT
FY90 BDGT
FY91 BDGT
FY92 BDGT
FY93 BDGT
FY94 BDGT
FY95 BDGT
FY96 BDGT
FY97 BDGT
FY98 BDGT
FY99 BDGT
FY00 BDGT
FY01 BDGT
FY86 EXP
FY87 EXP
FY88 EXP
FY89 EXP
FY90 EXP
FY91 EXP
FY92 EXP
FY93 EXP
FY94 EXP
FY95 EXP
FY96 EXP
FY97 EXP
FY98 EXP
FY99 EXP
FY00 EXP
FY86 G.F.
FY87 G.F.
FY88 G.F.
FY89 G.F.
FY90 G.F.
FY91 G.F.
FY92 G.F.
FY93 G.F.
FY94 G.F.
FY95 G.F.
FY96 G.F.
FY97 G.F.
FY98 G.F.
FY99 G.F.
FY00 G.F.
CBB RESERVE FUND
FY86 REV
FY87 REV
FY88 REV
FY89 REV
FY90 REV
FY91 REV
FY92 REV
FY93 REV
FY94 REV
FY95 REV
FY96 REV
FY97 REV
FY98 REV
FY99 REV
FY00 REV
Top section: annual budget preparation for next year.
2nd section: fiscal year expenditures.
3rd section: general fund.
Bottom section: revenues collected each fiscal year
Prepared by: House Research Agency
February 1, 1984

Figure 2

EXPENDITURES AND RESERVES UNDER CASH BASED BUDGETING

(IN MILLIONS OF $)



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TITLE PAGE ONLY HAS BEEN FILMED.

State Budget Policy Under Uncertain Revenue Forecasts

Options for Legislative Action

House Research Agency
Alaska State Legislature
January 1983

House Research Agency Report 82-B

THE PURPOSE OF THIS LEGISLATION, ORIGINALLY INTRODUCED IN A SLIGHTLY DIFFERENT FORM IN APRIL OF 1979 WITH A BI-PARTISAN LIST OF 24 SPONSORS, IS TO STABILIZE BUDGETING IN ALASKA. AT THE PRESENT ALASKA, LIKE EVERY OTHER STATE, BUDGETS MONEY "ON THE COME", THAT IS, WE MAKE OUR VERY BEST EFFORTS TO CALCULATE PROBABLE INCOME FOR THE NEXT FISCAL YEAR, AND THEN ATTEMPT TO BUDGET UP TO THAT FIGURE, HOPING THAT WE HAVE NEITHER OVERSPENT AND CAUSED LEGAL PROBLEMS, OR LEFT TOO MUCH ON THE TABLE AND CONSEQUENTLY DISAPPOINTED LARGE NUMBERS OF VOTERS.

BY THE SIMPLE EXPEDIENT OF SETTING ASIDE, IN A CONSTITUTIONALLY-PROTECTED ACCOUNT, 15 PERCENT OF AN AVERAGE YEAR'S INCOME FOR A PERIOD OF SEVEN YEARS, WE WILL HAVE A TOTAL OF 105 PERCENT OF AN AVERAGE YEAR'S INCOME IN THE ACCOUNT. BEGINNING IN THE EIGHTH YEAR, ALL BUDGETING WOULD BE DONE FROM THAT FUND OF <u>KNOWN CASH RESERVES</u>, AND ALL INCOME FROM THAT TIME ON WOULD GO INTO THE RESERVE FUND.

A POTENTIAL EXISTS OF LEGAL CHALLENGE AS TO WHETHER APPROPRIATIONS TO THE FUND WOULD RUN AFOUL OF THE SPENDING LIMITATION WHICH WAS APPROVED BY THE VOTERS LAST FALL. A TOP-OF-THE HEAD OPINION FROM THE LEGAL DIVISION IS THAT IT WOULD NOT, BUT WE ARE HAVING IT RESEARCHED IN MORE DEPTH, AND MIGHT HAVE TO INTRODUCE AMENDMENTS ACCORDINGLY.

THE MAIN THRUST OF THE AMENDMENT IS THAT IT WOULD:

1. PLACE THE ENTIRE BUDGETING PROCESS ON THE BASIS OF <u>KNOWN</u> FISCAL RESERVES.
2. SHORTEN LEGISLATIVE SESSIONS BY ELIMINATING THE NECESSITY OF JUGGLING INCOME PROJECTIONS.
3. ENABLE INTERIM BODIES AND INDIVIDUALS TO WORK ON THE BUDGETARY PROCESS THROUGHOUT THE YEAR.
4. ELIMINATE THE DANGEROUS PROBABILITY OF OVER-BUDGETING.
5. SIMPLIFY ANSWERING CONSTITUENT DEMANDS FOR FUNDING OF MANY PROJECTS AND PROGRAMS.
6. ENSURE FULL FUNDING OF PROJECTS AND PROGRAMS APPROVED BY THE LEGISLATURE.

OBJECTIONS WILL BE THAT WE CANNOT AFFORD THE SETASIDE AND THAT WE WOULD BE IDLING LARGE AMOUNTS OF MONEY FOR AN ENTIRE YEAR. TO THE FIRST OF THOSE WE ANSWER THAT WE PROBABLY CANNOT AFFORD, GIVEN THE RADICAL CHANGES IN INCOME WHICH WE EXPERIENCE, <u>NOT</u> TO INSTALL SOME SORT OF STABILIZING DEVICE. TO THE SECOND THAT THE MONEY WILL BE AT WORK, EARNING INCOME, FOR THE ENTIRE PERIOD DURING WHICH IT IS IN THE LIMBO OF THE RESERVE ACCOUNT <u>AND</u> EVEN AFTER IT IS BUDGETED WILL CONTINUE TO BE AT WORK UNTIL ACTUALLY EXPENDED.