

ALASKA LEGISLATURE

1884

HOUSE and SENATE FINANCE COMMITTEE FILES, 1999 - 2000

Intergenerational Equity

- Ability to purchase for future beneficiaries what the endowment can purchase for today's beneficiaries (inflation-proofing)

Total Return - Economics Perspective

- Investing for maximum return
- No distinction between capital appreciation and current income
- No distinction between realized and unrealized earnings

Total Return - Management Perspective

- Disconnects investment decisions from short-term spending considerations
- Spending provision becomes part of long-term investment strategy rather than tactical response to market cycles

Endowment Management

Conflicting Objectives - Trade-offs

- Preserve purchasing power of endowment
- Maximize distributions (current and future)
- Predictable payouts

Strategic Questions

- How much is needed for distribution to the beneficiary (spending)?
- How much is needed to preserve purchasing power (inflation-proofing)?
- Time horizon for major distributions?

Strategic Issues

- Expected or needed rate of return
- Risk tolerance
- Asset class preference

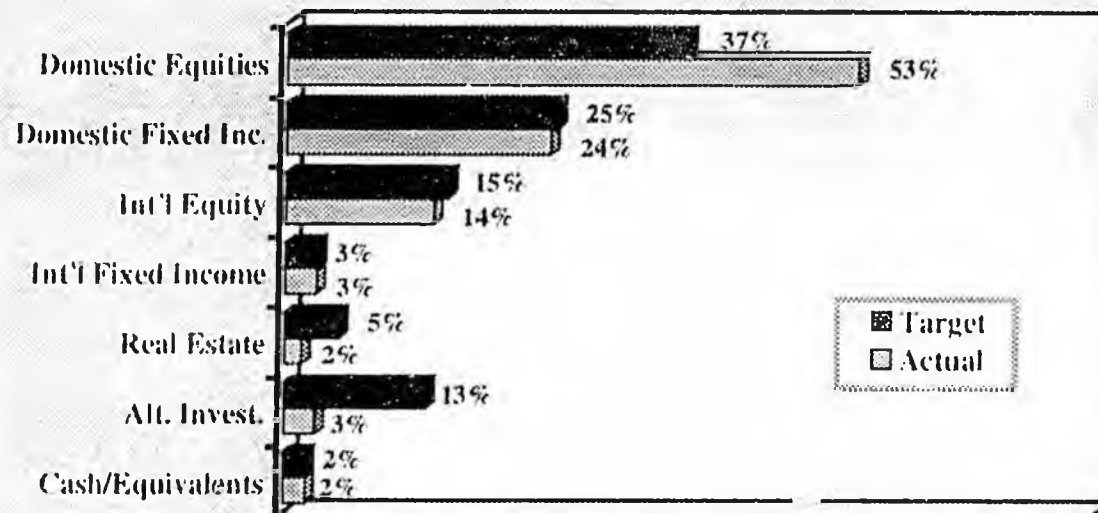
Strategic Outcomes

- Portfolio asset allocation

- Spending Methodology

Asset Allocation

Consolidated Fund
Asset Allocation Target v. Actual December 31, 1998

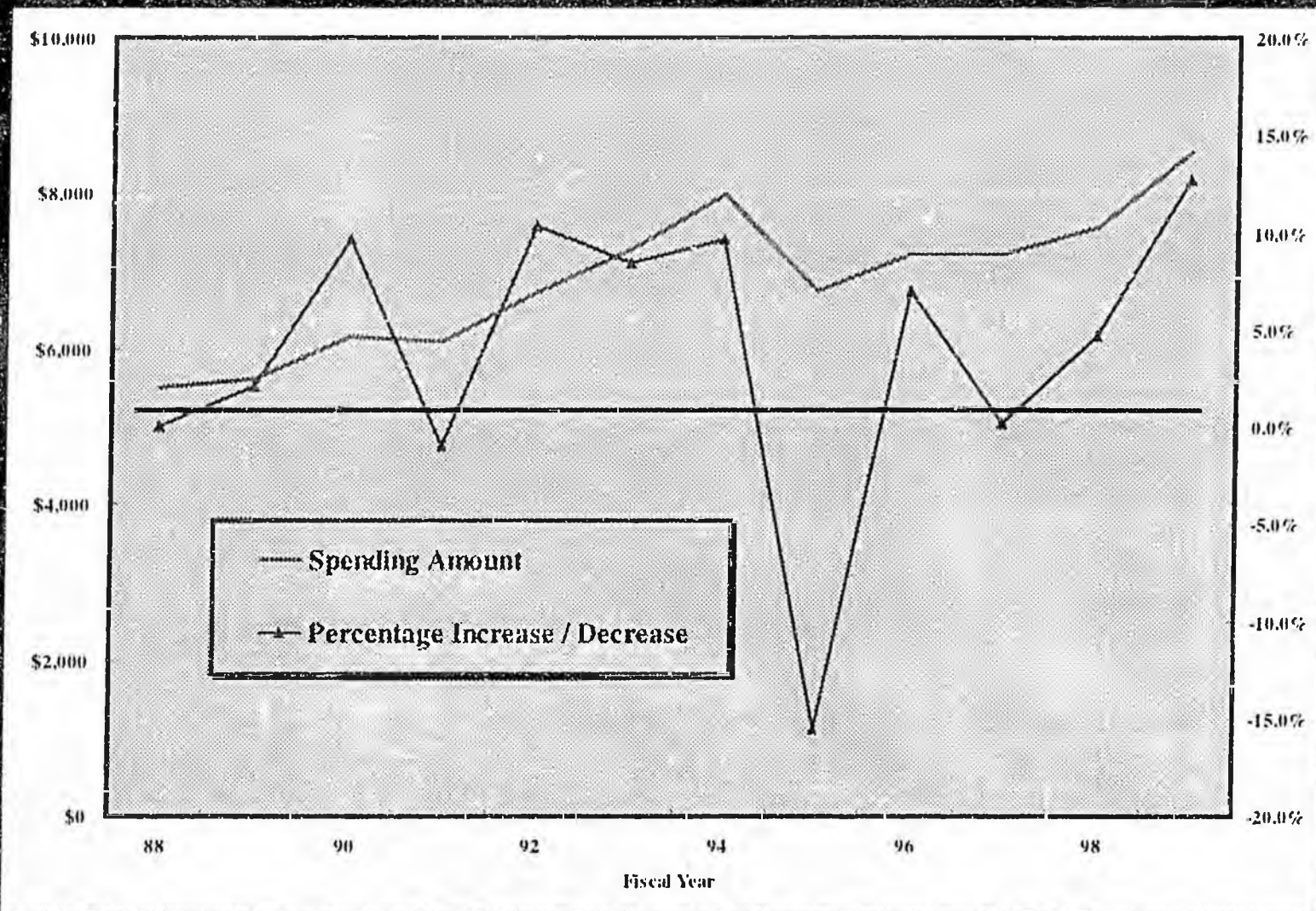


Spending Methodologies

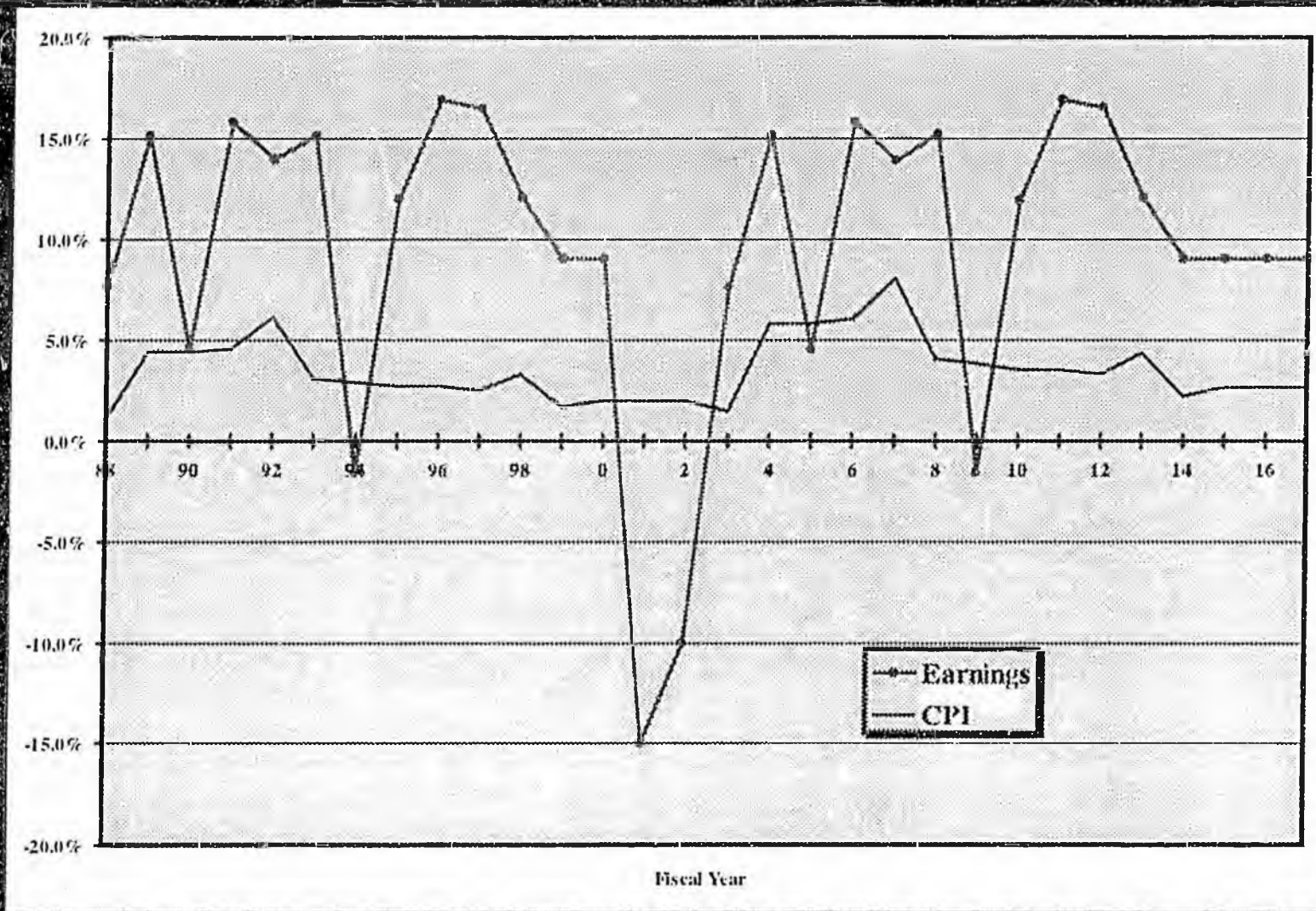
	<u>Utilization</u>
Spend all current income	4%
Spend X% of current income	2%
Spend X% of beginning market value	5%
Spend X% of moving avg. of mkt. values	70%
Increase prior year spending by X%	6%
Decide each year	5%
Other	9%
Total (506 respondents)	100%

(Source: NACUBO Endowment Survey, 1998)

Theoretical Fund Spending Allowance History



Theoretical Fund Earnings Rate and Inflation Assumptions

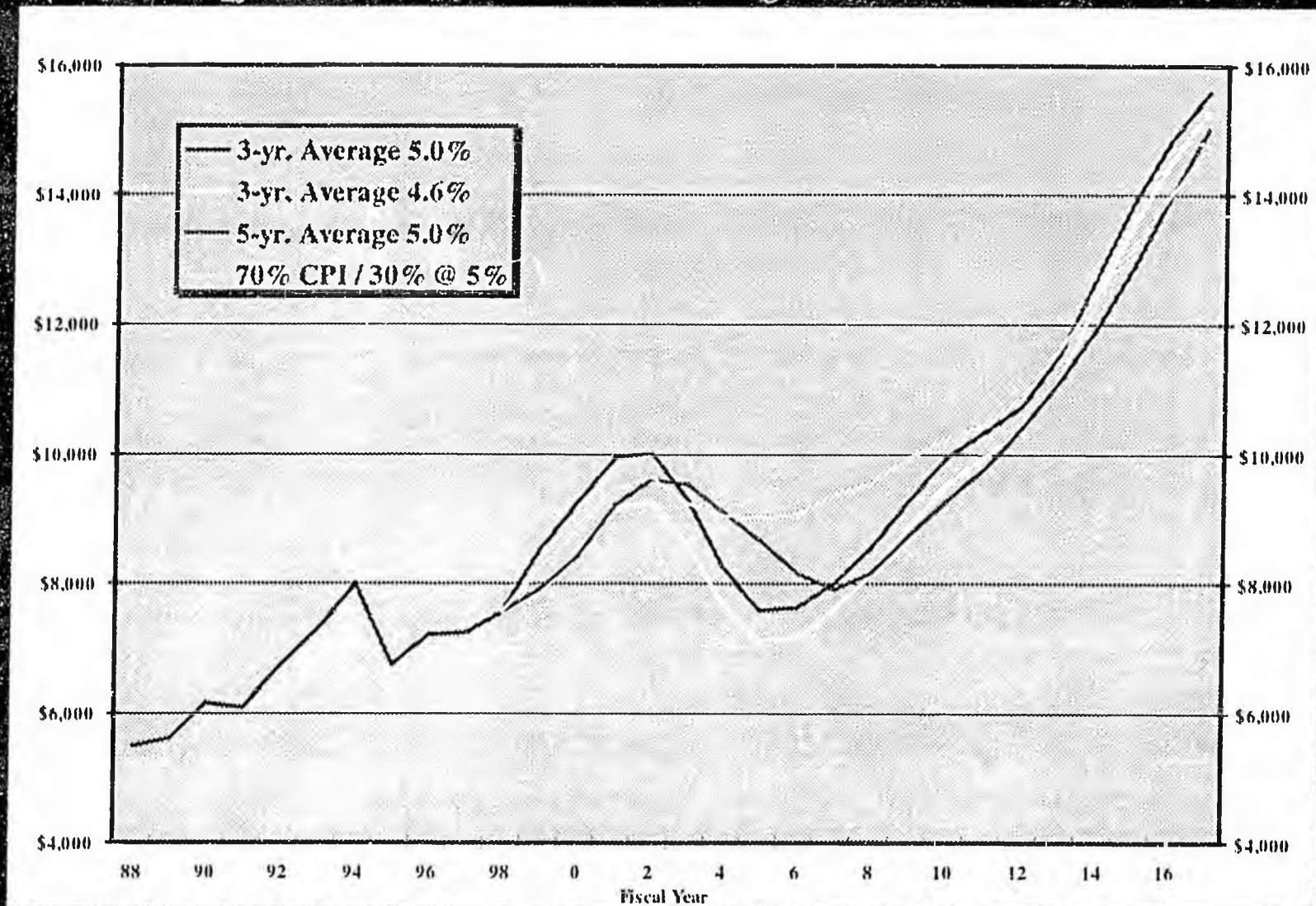


Spending Alternatives Analyzed

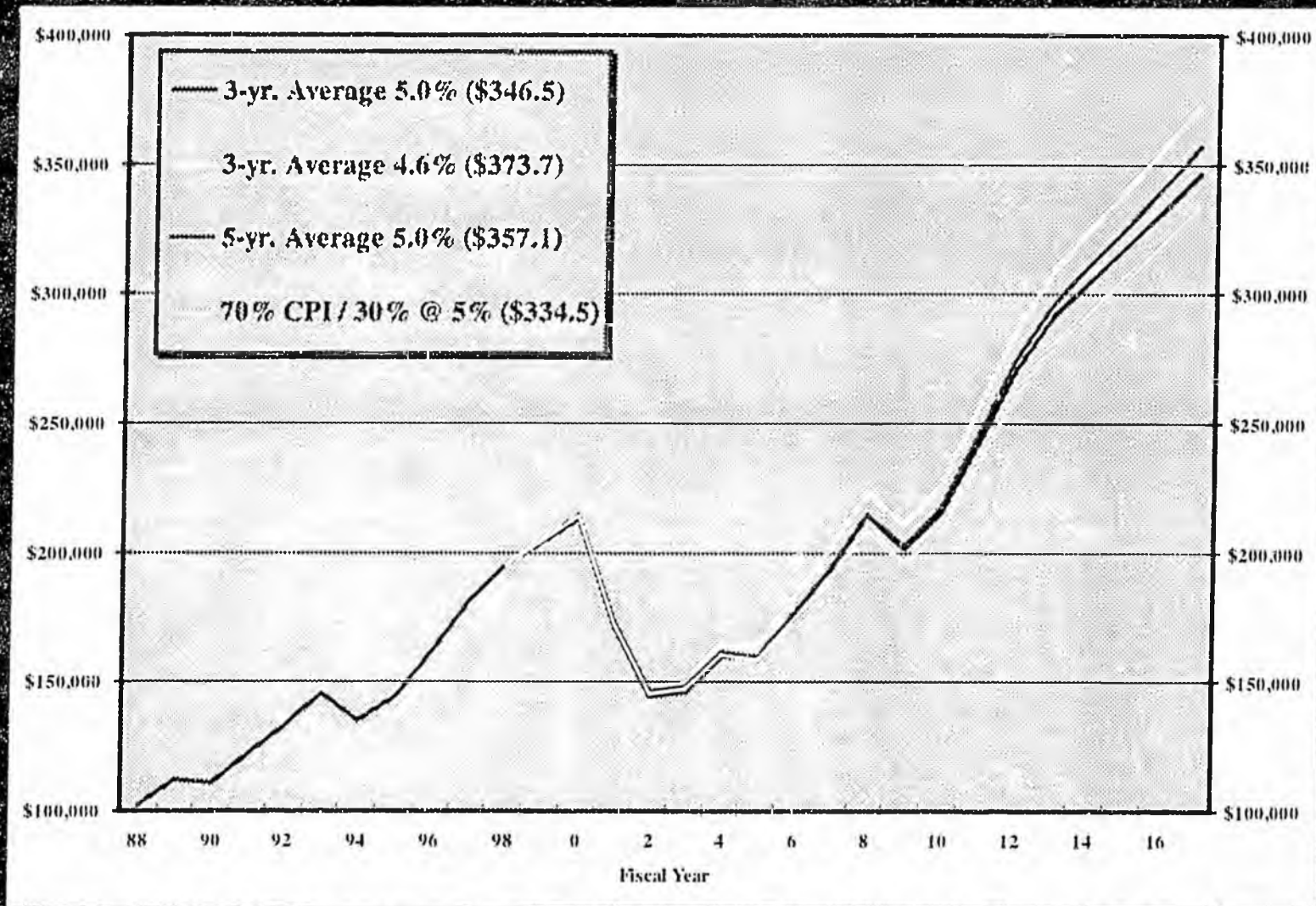
- 3-Year Average Market Value X 5.0%
- 3-Year Average Market Value X 4.6%
- 5-Year Average Market Value X 5.0%
- Yale Methodology - (70% Prior Year Spending adj. for inflation) + (30% of Market Value X 5.0%)

Theoretical Fund Spending Allowance Alternatives

Annual Distribution Amounts



Theoretical Fund Spending Alternatives Endowment Principal Balances





Anchorage *Star of the North*
Chamber of Commerce

Recommendations to Secure Alaska's Fiscal Future

We recommend these steps be taken to bridge the gap between state spending and recurring revenues, and the tools be used in the following order:

1. **Take action on a long-term plan this legislative session.**
2. **Reduce state spending.**
 - *Establish a periodic process to identify and review essential and appropriate services. Through this process:*
 - Identify spending priorities that reflect a government's traditional responsibilities.
 - Promote state programs that encourage development of Alaska's economy, with special emphasis on development that generates a positive return to the economy and state treasury.
 - *Incorporate performance measures by which state services are evaluated on whether they are effective in meeting intended missions and efficient in the use of public dollars. Use this information to make spending reductions and investments.*
 - *Implement alternate ways to deliver state services such as privatization and contracting with the private sector.*
3. **Use earnings from financial investments and other instruments.**
 - *Use Permanent Fund earnings.*
 - Inflation-proof the Fund first.
 - Remainder of earnings is available for dividends and to support government services.
 - *Use the constitutional budget reserve fund or a similar fund as a "shock absorber" against oil price fluctuations.*
 - *Use general obligation debt, as appropriate, to finance the state's infrastructure needs on a long-term basis.*
4. **Implement broad-based taxes and implement/or increase consumption taxes.**
 - *Taxes should meet a standard of fairness and equity.*

Ralph Samuel, Chair

April Jensen, President



Comments by
Cheryl Frasca
before the Senate Finance Committee
March 24, 1999

Criteria to Evaluate Fiscal Plans

Purpose

Advance identification of a financial plan that closes the state's fiscal gap and fosters the long-term prosperity of the Alaskan economy and its people.

Principles for a plan

1. Stability
2. Sustainability
3. Fairness
4. Simplicity
5. Complete and full disclosure

Evaluation Criteria

1. **Stability**
 - a) Stable and predictable annual flow of revenues
 - b) Predictable tax regime
 - c) Stable spending
 - d) Ability to adjust to changing needs
 - e) Can be implemented

2. **Sustainability**
 - a) Protects and grows the Permanent Fund
 - b) Maintains revenue generating capacity of other financial assets
 - c) Advances financial investment policies that achieve maximum financial return

3. **Fairness**
 - a) Trade-offs between taxes, dividends, and public services are balanced across all Alaskan households, businesses, and communities
 - b) Links economic activity and a return to the state treasury
 - c) Connects Alaskans to financial decisions
 - d) Provides a smooth transition between any change in the size of dividends, taxes, or public services



4. Simplicity

- a) Disposition of revenues and financial earnings is understandable
- b) Clear definition of each element's composition and purpose
- c) Consistent presentation of plan

5. Complete and full disclosure

- a) Uses reasonable assumptions for revenue generating capacity of natural resources and financial assets
- b) Uses reasonable assumptions for population growth and composition change, and inflation
- c) Balances revenues and spending for at least twenty years
- d) Clearly accounts for all revenues, current spending and future financial commitments

CORRECTION

THE FOLLOWING DOCUMENT(S)
HAVE BEEN REFILMED TO
ASSURE LEGIBILITY OR PAGINATION



Rev. 6/98

Central Microfilm Services
Department of Education & Early Development
State of Alaska



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3/24/99



THE ALLIANCE

... for responsible development of Alaska's Oil, Gas & Mineral Resources

Alliance Testimony – State Fiscal Gap

March 24, 1999

by Karen Cowart, General Manager

I am Karen Cowart, General Manager of the Alaska Support Industry Alliance (The Alliance). Thank for the opportunity to provide comment and perspective as you begin making important decisions on the state's budget.

The Alliance is a statewide trade organization formed 20 years ago to provide a collective voice for companies that provide goods and services in support of oil and gas exploration, development and production. Although The Alliance does not include all support businesses in the state, most of the major players are members. Like most trade organizations, we believe our membership reflects the industry as a whole.

The Alliance has 300-plus member businesses, organizations and individuals that operate and work all across the state, from the North Slope to the Kenai Peninsula. Collectively, our membership employs about 25,000 Alaskan residents. While The Alliance is headquartered in Anchorage, we have active chapters and committees in Fairbanks, Kenai and Prudhoe Bay.

The Alaska oil and gas support industry is suffering difficult times in these days of low oil prices. We estimate at least 4,000 people have lost their jobs within our membership during the last quarter of 1998 and the first quarter of 1999. For the next 18 to 36 months, we expect downsizing and layoffs to continue. According to industry experts, despite the recent upward fluctuation, overall low oil prices will likely go on for another one to two years, perhaps longer.

As business people, we understand that oil companies, our clients, must slow production, delay development and suspend exploration in times of low profits. These are necessary measures if investors are to maintain presence in the state until oil prices warrant an increase in activity.

In the meantime, it is critical that we *do not lose sight of the future*, when the economic climate changes and opportunities re-emerge. The most important thing that state government can do *right now* is to ensure that Alaska is poised to encourage and take advantage of future resource development. And that means balancing the budget, *this year*.

I think it is important to note that The Alliance has advocated a balanced state budget virtually since its inception in 1979. Closing the state's fiscal gap *remains as our top priority* this year. Why? Because the financial status of state government will dictate our members' livelihood by either encouraging future petroleum investments, or by chasing investors away.

Unchecked, the rising fiscal gap between state revenues and expenditures projects an image of an unstable, irresponsible government. It generates uncertainty among potential and existing industry investors. It is critical that oil companies view Alaska as a *stable place to invest* in when oil prices rise in the future.

For this reason, The Alliance is heartened to see *bipartisan efforts* to address the state's most serious problem, the budget. We *applaud the governor* for coming to the table with a proposal. It is a starting point, serving as the catalyst for meaningful dialogue. We also deeply appreciate the legislature's ongoing commitment to a 5-year budget-balancing plan. In the days ahead, lawmakers can build on this foundation.

I'd like to emphasize that The Alliance has always supported efforts to reduce government spending as the *first and foremost* method of balancing the budget. We still do, but we also realize spending cuts alone will not close the billion-dollar-plus gap. The time has come to consider all options.

The fact is that no one wants to pay more for products and services with a sales tax. No one wants to see less of their paycheck with a state income tax. And no one wants to receive a smaller Permanent Fund dividend. But no one can sensibly "just say no" to *everything* anymore. *Alaskans need to say "yes"* to a fiscally stable government and a sustainable economy.

We understand the legislature and the administration is looking to the people of Alaska to determine realistic ways to address the fiscal gap. We would like to give you the support industry's point of view. The Alliance polled its membership in mid-March to discover which tools are most palatable. This is what we found:

State Government Spending Reductions

The vast majority - 98% - of Alliance members *support continued cuts* in government spending. They believe that there are many more efficiencies to be gained in government, whether it be by results-based budgeting, consolidation of government programs, elimination of non-essential services, use of a two-year budget cycle, and/or privatization of some government functions.

About three-fourths (76%) picked spending cuts as the *top choice* of methods to balance the budget. Most agreed that *spending reductions should occur before any other revenue sources are established*.

Permanent Fund Unrealized earnings and Dividend

Using some portion of the Permanent Fund's unrealized earnings to fund government is acceptable to *eight out of 10* members. Two-thirds (64%) supported use of some, but not all of the fund's unrealized earnings, while 16% said use it all, if necessary.

About half - 45% - picked use of unrealized earnings as their *second choice* of methods to balance the budget. About a quarter (23%) picked this tool as their third choice.

Permanent Fund Dividend

Limiting (or eliminating) the Permanent Fund Dividend, and using the remaining earnings to fund government services, was acceptable to *seven out of 10* of responding Alliance members. About 42% ranked this method as their third choice; while 23% said it would be their second choice.

State Income Tax

Alliance members *overwhelmingly oppose a state income tax*. Eighty-one percent said they “do not support” or “strongly oppose” using this tool to balance the budget. Six out of 10 (61%) ranked an income tax as the tool they prefer least.

State Sales Tax

While taxes of any type were the least popular budget-balancing tools to Alliance members, a sales tax appeared to be the most palatable taxation. About half – 52% - said they would support a state sales tax, *provided it would be levied statewide and on a fair and equitable basis*.

Four out of 10 said they did not support a state sales tax. About 46% ranked sales tax as the fourth choice among methods to balance the budget, 16% said it was their number three choice, and 17% ranked it last.

Conclusion

We hope this input is valuable as the legislature develops and modifies its own specific budget proposals. We are willing to review and provide feedback on these proposals at your request. As plans are put forth, however, The Alliance does ask that they are presented to the people *with all the cards on the table*. We urge you to devise a simple way to show the full budget - *all revenues and expenses* - whether they flow through the general fund or not. This will allow us to see how much we are really paying for government services, in what form, and then come to our own conclusions on programs we feel are essential to the state and its residents.

In closing, I would like to leave you with this thought. The Alaska oil and gas support industry IS in crisis. Businesses are taking *immediate measures* to survive in the long term. They are realigning budgets to reflect losses in project revenues and reducing expenditures accordingly.

It is imperative that the state does the same. Time IS of the essence. The time for talk is long over. The state MUST take action now. We encourage you to continue budget dialogue with the intent to resolve the problem this year. Our sector of the economy, and commerce across the state, is counting on you.

Again, thank you for the opportunity to provide testimony on this important issue.



THE ALLIANCE

4220 'B' Street, Suite 200 • Anchorage, AK 99503-5911 • Phone: (907) 563-2226 • Fax: 561-8870

RESULTS OF ALLIANCE MEMBERSHIP "BUDGET" SURVEY

The Alliance surveyed its over 300 members in mid-March regarding the state's \$1 billion fiscal gap, and various proposed tools to close it. Response was excellent, and the oil and gas support industry's trade organization now has a clear picture of how the majority of members feel. Below is a summary of tabulated results. A copy of the original survey is attached for reference.

1. State Government Spending

Recommendation: Cut Deeply: 42% Cut Moderate: 56% Don't Cut: 2% Increase Spending: 0%
Ranking: Number 1: 76% Number 2: 12% Number 3: 7% Number 4: 2% Number 5: 1%

Continued cuts in government spending are overwhelmingly (98%) supported by the majority of Alliance members. About three-fourths (76%) picked spending cuts as their top choice of methods to balance the budget.

2. Permanent Fund Unrealized Earnings

Recommendation: Use All: 17% Use Some: 64% Don't Use: 11% Never Use: 7%
Ranking: Number 1: 10% Number 2: 45% Number 3: 23% Number 4: 12% Number 5: 5%

Use of some, but not all, of the Permanent Fund's unrealized earnings is supported by two-thirds (65%) of Alliance members. About half (45%) picked use of unrealized earnings as their second choice of methods to balance the budget; while about a quarter (23%) said this is their third choice.

3. Permanent Fund Dividend

Recommendation: Eliminate: 9% Limit: 61% Leave Alone: 16% Never Touch: 12%
Ranking: Number 1: 1% Number 2: 22% Number 3: 41% Number 4: 11% Number 5: 13%

Limiting (or eliminating) the Permanent Fund Dividend, and using the remaining earnings to fund government services, was acceptable to nearly three-quarters (72%) of Alliance members responding. About 42% ranked this method as their third choice; while 23% said it would be their second choice.

4. State Income Tax

Recommendation: All Alaskans: 18% Upper Income Only: 1% Do Not Support: 33% Strongly Oppose: 47%
Ranking: Number 1: 2% Number 2: 4% Number 3: 9% Number 4: 21% Number 5: 60%

There is overwhelming opposition (81% "do not support" or strongly oppose) to a state income tax on the part of Alliance members. Six out of 10 (61%) ranked an income tax as the least preferable choice among methods to balance the budget.

5. State Sales Tax

Recommendation: Statewide: 52% Except Where Local: 7% Do Not Support: 23% Strongly Oppose: 16%
Ranking: Number 1: 3% Number 2: 13% Number 3: 16% Number 4: 45% Number 5: 17%

While taxes of any type were the least popular budget-balancing tools among Alliance members, a sales tax appeared to be the most palatable taxation, provided it would be applied on a statewide basis. About 46% ranked sales tax as the fourth choice among methods to balance the budget.



THE ALLIANCE

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FAX-BACK STATE BUDGET SURVEY – by March 16

First, check how you feel each budget-balancing tool should be used, if at all. Then rank the methods by placing a "1" next to your top choice, "2" next to your second choice, "3" next to your third choice, "4" next to your fourth choice, and "5" next to the tool you prefer least.

RANK

_____ State government spending Cut deeply Cut moderately Don't cut Increase Spending

Comments: _____

_____ Permanent Fund unrealized earnings. Use all Use some Don't use Never use

Comments: _____

_____ Permanent Fund dividend. Eliminate dividend Limit dividend Leave it alone Never touch

Comments: _____

_____ State income tax. On all Alaskans Upper income only Do not support Strongly oppose

Comments: _____

_____ Establish a state sales tax. Statewide Except where local tax Do not support Strongly oppose

Comments: _____

Company: _____

Voting Member or Representative: _____

Thank you for your input!

Please fax back to The Alliance at (907) 561-8870 by Tuesday, March 16.

Responses will be tabulated by March 19.

ALL RESPONSES WILL BE KEPT CONFIDENTIAL

3/24/99

A.G.C.

HELLO MY NAME IS ROXANNA HORSCHER.... I OWN A SMALL CONTRACTING BUSINESS AND I AM HERE TODAY REPRESENTING THE ASSOCIATED GENERAL CONTRACTORS ASSOCIATION OF ALASKA..

THE ASSOCIATION HAS CLOSE TO 600 MEMBERS FROM ANCHORAGE, FAIRBANKS, KENAI AND S.E. AREAS OF THE STATE. THE MEMBERSHIP IS MADE UP OF BUILDING, HIGHWAY, AND SPECIALTY CONTRACTORS AS WELL AS MATERIAL SUPPLIERS AND SERVICE RELATED COMPANIES.

BECAUSE THE AGC OF ALASKA IS QUITE CONCERNED OVER THE FISCAL GAP WE ARE PLEASED TO HAVE THIS OPPORTUNITY TO SHARE OUR POSITION, AND PRESENT THE FOLLOWING IDEAS FOR YOUR CONSIDERATION.

1. MAXIMIZE THE USE OF FEDERAL MATCH FUNDS FOR CAPITOL WORK.
THE ASSOCIATION FEELS VERY STRONGLY THAT NO FEDERAL OFFERINGS SHOULD BE LOST BECAUSE OF THE LACK OF STATE FUNDING FOR MATCHING DOLLARS.
2. MAINTAIN A STRUCTURED APPROACH TO A CAPITOL PROGRAM. AS SET OUT IN THE STATE CONSTITUTION ARTICLE IX, SECTION 16 WHICH STATES IN PART THAT EXCEPT FOR A FEW SPECIFIC BOND APPROPRIATIONS, THE APPROPRIATIONS FROM THE STATE TREASURY SHALL NOT EXCEED 2.5 BILLION DOLLARS PER YEAR BY MORE THAN THE GROWTH IN POPULATION OR INFLATION SINCE JULY 1, 1981..... AND GOES ON TO STATE .."WITHIN THIS LIMIT AT LEAST ONE THIRD SHALL BE RESERVED FOR CAPITOL PROJECTS AND LOAN APPROPRIATIONS".
3. REDUCE STATE GOVERNMENT FUNCTION IN ACCORDANCE WITH ARTICLES III THRU X OF THE ALASKA CONSTITUTION. OTHER STATES OPERATIONS COULD SERVE AS A GUIDELINE TO DEFINE THE BASIC FUNCTIONS.
ALSO STATE EMPLOYEES SHOULD MORE RESEMBLE PRIVATE SECTOR EMPLOYEES IN SIMILAR WORK. MANY CONTRACTORS COMPLAIN THEY CAN NOT COMPETE WITH WAGES, AND BENEFITS PAID BY THE DEEP POCKETS OF STATE GOVERNMENT.
4. LOWER STATE EXPENDITURES THROUGH INCREASED PRIVATIZATION OF SERVICES.
5. USE SOME OF THE NON DESIGNATED PERMANENT FUND EARNINGS TO BALANCE THE BUDGET.

6. BONDS FOR CAPITOL PROGRAMS SHOULD BE USED TO BRIDGE SHORT TERM FISCAL GAPS.

7 WE SUPPORT AN INCREASE TO THE STATE MOTOR FUEL TAX PROVIDED THE REVENUES ARE USED FOR ADDITIONAL MAINTENANCE OF OUR TRANSPORTATION INFRASTRUCTURE AND DISTRIBUTED THROUGH A DESIGNATED FUND..

The AGC feels if all these points were implemented a State income tax would not even need to be considered.

WE THANK YOU FOR THE ATTENTION YOU HAVE GIVEN US. IN CLOSING I WISH TO SAY THAT WE ALL RECOGNIZE THE DIFFICULT DECISIONS YOU MUST DEAL WITH THIS YEAR AND WE ENCOURAGE YOU TO ACT IN THE BEST LONG TERM INTEREST OF THE STATE OF ALASKA , WITH THAT WE PROMISE OUR SUPPORT AND DEFINITELY OUR RESPECT.

3/24/99

Dain LaBolle

**Alaska State Chamber of Commerce
Recommendations on a Fiscal Plan for Alaska**

The ASCC supports a long-range budget plan that will bring state spending in line with revenues. Our recommendations are as follows:

1. Develop and enact a long-term fiscal plan this session. Establish the process for achieving a balanced budget, including a time frame, schedule, and spending/revenue targets.
2. Determine the appropriate role of state government, and through streamlining, consolidation, and privatization, reduce the size of state government. We believe an achievable target for reducing costs in this manner is at least 30%.
3. Utilize earnings from investments. After the Permanent Fund has been inflation-proofed, the remaining earnings should be used for dividends and to fund government services. General obligation debt should be used, as appropriate, to finance infrastructure needs on a long-term basis. We believe a reasonable funding target from investment earnings is approximately 50-55%.
4. The remaining 15% of the funding would come from broad-based taxes, fairly and equitably applied to all Alaskans.

Looking Out For Business...

A Report from the Alaska State Chamber of Commerce - the Voice of Alaska Business



About sixty members of the Alaska State Chamber of Commerce (ASCC) were in Juneau recently to meet with Governor Knowles and the Legislature on behalf of business, commerce, jobs, and economic development. The primary topic of discussion was the \$1.2 billion budget deficit and what to do about it.

The Governor received praise for his leadership in opening the debate by putting his budget plan on the table. And, although the Legislature had yet to put forth its version of a plan for discussion, it was obvious that a lot of work was going on behind the scenes - sorting ideas and developing options for a plan that a majority of them could commit themselves to. The position presented by the Chamber was that a plan is needed this year - a plan for state government that emphasizes efficiency, consolidation, streamlining, and privatization.

"Any ideas on how this should be done?" was a question asked by many Legislators. Well, maybe this is a good time to look back in Alaska's history and see how another governor and another set of Alaska business leaders tackled a similar task - an assignment to reduce state costs by streamlining various government operations.

Finding efficiencies was the goal when Gov. Jay Hammond asked the State Chamber to assemble a team to make an in-depth study of the way things were done in state government - and to come up with recommendations for how to do things better and at less cost.

At the time, Alaska's general fund expenditures were running about \$700 million a year, and total state spending - including federal dollars coming in to support various programs - was just a little more than \$1 billion. Now, more than \$6 billion is pumping through the state's cash drawers, including \$2.3 billion in general fund spending.

But the crisis was much the same back in November 1975, when Hammond asked for help in controlling spending. The Chamber's response was to make a major commitment to the job.

Two leading Anchorage businessmen, banker Jim Curley and restaurateur Bill Pargeter, signed on as chairman and vice-chairman, respectively. Three others volunteered to serve on the committee's executive committee, and businesses in Anchorage and elsewhere loaned 14 of their top executives to the task on a full-time basis. Twenty-eight others signed up as part-time team members, many of them serving as many as 12 weeks at a time on assignment in Juneau. Others were aboard for briefer periods - and in all, 55 individuals took part in the work.

That work took two full years. On Nov. 1, 1978, Hammond issued a report to the people of Alaska on the results of the "Governor's Management & Efficiency Review."

Implementation of the recommendations over the two-year period resulted in annual savings of more than \$44 million and one-time benefits of more than \$6 million. At the time of the report, 247 of the study's 362 recommendations had been implemented, and others were in the works.

Reading it today, we see that some recommendations never implemented are still applicable. This would be a good place for the Commission on Privatization and the Delivery of Government Services to begin its work. Senate Bill 33, now under consideration by the Legislature, would create such a commission, made up of business and government leaders, to review and evaluate state procedures and services and provide recommendations for consolidating, privatizing, and streamlining state government.

It has been 24 years since state government was looked at with an eye for its overall shape and performance. It has grown considerably since then. Every gardener knows that pruning is necessary to keep a rose bush healthy, growing strong, and producing at its best. It's time for another look at the shape of state government.

"The State Chamber is united in the position that we need to get the budget problem behind us now, so that we can concentrate all our energies on building Alaska for the future."

Pete Leathard, Chairman, ASCC

Cost of State Government – Then and Now

1978

Alaska's population – 403,099
State Budget - \$1 billion

1998

Alaska's population – 621,400
State Budget - \$6.2 billion

Accounting for inflation (at an estimated rate of 3.5% compounded over 20 years) today's budget is \$5.2 billion in 1978 dollars.

In today's budget, \$1.2 billion is paid in Permanent Fund dividends and is spent to inflation-proof the fund. Subtracting that reduces today's budget, in 1978 dollars, to \$3.9 billion.

The 1978 per capita cost of government was \$2,408.78. The 1998 per capita cost is \$6,276.15. This represents a 40% increase in per capita government spending in 20 years.

Alaska's population has increased 54%, while state spending has increased 290%.

In real dollars, if per capita spending had been maintained at the 1978 rate, today's budget would be \$3.06 billion, less than half of what it is.



Resource Development Council

for Alaska, Inc.

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State Fiscal Gap - Potential Tools

Comments of Ken Freeman
Executive Director
Resource Development Council

Before the Senate Finance Committee, March 24, 1999

Good morning, for the record my name is Ken Freeman, I serve as executive director of the Resource Development Council. I appreciate the opportunity to present comments on our number one public policy issue this session -- implementation of a long-term fiscal plan for the State of Alaska.

As many of you know, RDC is a non-profit, economic development organization with a broad statewide base and focus. Our members range from individuals to leading companies throughout Alaska's basic resource sectors, including oil and gas, mining, timber, tourism and fishing. Also included in our ranks are Native corporations, construction, labor and a number of local communities. All of these interests come together under RDC to work on common issues --issues which transcend all resource and economic sectors.

RDC is represented statewide by a 78-member Board of Directors and a 22-member Executive Committee. The later of which formulates policy and provides direction to a staff of four.

With the fiscal gap as our number one public policy issue this session, RDC helped coordinate the economic summit held last month in Juneau and our President testified on the fiscal gap before the Anchorage Caucus in late February.

What many of you heard at the economic forum was an assessment of business in Alaska. From the development sectors you heard that low oil prices and a slumping Asian economy have hit Alaska hard. You also heard that the timber and fishing industries are in the tank, both hit hard by weak Asian markets. Timber production is down by 70 percent or more, budgets have been drastically cut and industry employment has fallen to all-time lows. Meanwhile, the mining industry, which has shown record growth and production over the last several years, is now struggling to cope with low commodity prices.

RDC is here today to express our support and encouragement of the Legislature in finding a long-term solution to the state's fiscal dilemma and to offer suggestions on specific tools to develop such a solution.

I would like to applaud the Legislature and the Administration for making the budget issue the top priority this session - and in particular to the Senate and House Finance Committees which are working to evaluate the tools necessary to bridge the fiscal gap and create a long-term answer.

This issue is of extreme importance to our members and we are strongly advocating definitive action this session. RDC President Allen Bingham testified before the Anchorage Caucus in late February and said that RDC prefers all the tools available to close the fiscal gap be considered in the early deliberations of formulating a plan. He also said we have the tools to fix the problem before us but it will take cooperation and hard work - watching the session unfold we have seen both and it has encouraged us to come before the Legislature again to lend our support.

We appreciate the non-partisan and cooperative attitude expressed by both the Legislature and Administration to address the state's fiscal problems.

Over the course of many years, an assortment of ideas have been considered to close the fiscal gap. There are many good ideas out there and we look forward to providing input as appropriate. The state is fortunate that it has a very unique opportunity to identify and implement tools to close the fiscal gap before the Constitutional Budget Reserve is drained.

In terms of some specifics, RDC supports the use of the following tools presented in order of priority.

I. First, continue the Legislature's and Administration's reductions in state spending.

We appreciate the steps taken over the past few years to cut state spending. Without that leadership to bring spending more in line with recurring revenues, we would be in a much more serious situation.

We suggest that additional reductions could be achieved by establishing a periodic process to identify and review essential and appropriate services and recommend the establishment of priorities that reflect a government's traditional responsibilities to its citizens, i.e. public safety, transportation, education, and resource management.

The state must continue to promote programs that encourage development of Alaska's economy. Special emphasis must be directed to development that generates a positive return to both the local economy and state treasury.

Next, incorporate performance standards by which state agencies are evaluated as to their effectiveness in meeting intended missions and efficiency at the use of public dollars, -- results -- based budgeting.

And finally, evaluate and implement alternate ways to deliver state services such as privatization and contracting with the private sector.

RDC believes that additional budget cuts and increases in state efficiencies are achievable and will help, however, we all agree there is no way the state can realistically cut \$1 billion from the current budget.

Having said this, however, RDC believes any long-term fiscal plan should first establish spending priorities before addressing how those priorities will be funded.

II. Secondly, RDC further advocates for diversifying and stabilizing state revenues through the expanded use of the Permanent Fund earnings. Our Executive Committee believes the fund earnings should be used to fund appropriate state services, in addition to the traditional inflation proofing and dividend payment.

By using the permanent fund earnings to fund certain state government services, public interest in how and where their money is being spent will grow. Such a climate will hopefully generate more efficient state government.

There is an assortment of ideas that this committee may evaluate in terms of utilizing the Permanent Fund earnings to pay for state government services. We are not advocating one plan over another, but merely offering our support that using the earnings is a realistic and necessary measure that must be considered. On the revenue side, this is probably the most important tool that needs to be part of a long-term plan to fund state government. Members of our Executive Committee strongly believe this was the original intent of the fund and now is the time to begin to use some of those earnings to bring stability to public budgeting.

We believe further budget cuts and use of the Permanent Fund earnings will close the gap.

III. In the event these tools are not enough, RDC would entertain, as a final step, the implementation of a broad-based tax. Our members would have some comfort with a tax increase - such as the possible implementation of a sales tax. There is little support for an income tax.

New or increased taxes on industry are not the answer as such an action would shake the confidence of investors and harm a business climate already severely disturbed by global economic events. In fact, the fiscal gap itself is a significant hurdle in attracting investment capital here. Nervous investors may think twice about Alaska if they believe there is a serious risk of higher corporate taxes as a consequence of a continuing gap between recurring revenues and state spending.

RDC believes the solution can be found in using a combination of tools to solve the problem. No one tool — budget cuts, use of Permanent Fund earnings or a tax— solves the problem entirely.

Alaska is looking into the hour-glass, but RDC is confident the Legislature and the Administration will come to grips with this problem and do what is in the best interest of our state. Action is needed now while we have options rather than waiting until we are faced with a tougher dilemma down the road. Thank you for this opportunity to present our thoughts on this issue. I would be glad to try and answer any questions you may have.

3/24/99

(incorporated into record)

**Comments of Ralph Samuels,
Anchorage Chamber of Commerce**

Good morning, my name is Ralph Samuels, and I am the Chairman of the Board of Directors at the Anchorage Chamber of Commerce. I appreciate the opportunity to share with you some of the thoughts and concerns of the Anchorage business community.

The Anchorage chamber is an organization of over 1300 members. A vast majority of our members are small businesses. In addition to the large corporations that you are all familiar with, we represent small restaurants, gift shops, hotels, transportation companies, service companies and a myriad of other businesses in the Anchorage area.

For the past several years, the chamber has made the implementation of a long term fiscal strategy for the State its number one priority. We feel that in order for businesses to have the confidence to invest, expand and plan for their future, they must know that the State is going to have a stable fiscal policy. We are very much pleased that the Legislature has been active on this topic this session, and that the Administration is working in conjunction with the Legislature in order to get our fiscal house in order.

The Anchorage chamber board has spoken on the issue of long term fiscal planning with the following recommendations, to be used in the following order.

1. Take action to implement a plan this legislative session. If we wait until next year, the process will become embroiled in election year politics, and we will have spent one more years worth of reserves. Without a doubt, the time to act is now. The longer we wait the harder the decision will be.

March 24, 1999

2. Reduce State Spending- Using a model of Government based on results, eliminate programs which do not achieve the desired, measurable results. Every dollar the State spends should be considered an investment that has a measurable return.

Privatization and contractual agreements with the private sector should be examined at every turn to more efficiently deliver State services which are determined to be essential. In the private sector, if we have a drop in revenues or even cash flow problems, we examine every employee, every expense, every purchase, every facet of the way we do business in order to make sure we are getting the most for our money. Although the State cannot operate entirely like a business, this business-like attitude must be pervasive in every department, and in every budget in State Government. If the State does not gain the confidence of the Alaskan people that we are getting the most return for our State dollars as possible, the path towards fiscal certainty will be even more difficult to travel than it already is. We must have the courage to declare that some programs do not work, and to eliminate them, or substantially change them. The Chamber realizes that this is not an easy task. We also realize that most, if not all, of the department heads will tell you that their programs are cost-effective, and that THEIR programs are doing exactly what they were intended to do, and if they had just a little bit more money, they would really get into the swing of things, and save the State a whole bunch of money. In short, we know that your job is not an easy one. However, it is not easy in the private sector to make cuts either. The recent oil industry layoffs were not easy for the oil companies, or the oil field service companies either, but they did what they had to do for the long-term health of their organizations. We are asking you to do the same.

When it comes to public sector vs. private sector employees, I will only make one comment. The wages and BENEFITS should be comparable between the two sectors for similar jobs. Anything other than this simply defies common sense.

3. After the paring of the budget, the revenue side of the equation must be examined. The first tool on the revenue side to be used should be the use of earnings from investments, including earnings from the Permanent Fund.

The Chamber feels that we should inflation proof the fund first, and that the rest of the earnings should be made available for dividends and to support vital State services. This means that PF dividends should compete for funds against other State expenditures.

We should still use the Constitutional Budget Reserve, or a similar fund, as a "shock absorber" against oil price fluctuations.

The use of general obligation debt should be carefully considered to keep a stable, sustainable capital budget to keep up with the States infrastructure needs on a long-term basis.

4. After all of these steps have been taking, and only then, the State must consider a broad-based tax, or increase consumption taxes. Any tax plan that is even to be considered must be fair and broad-based. The business community is concerned that increasing taxes will decrease the take-home pay of their most valuable employees, forcing the businesses to increase wages to keep the employees that contribute the most to the company. This,

combined with an already tight market for a productive work force, will have a detrimental effect on the business community.

In our past, Alaskans have done many things we can be proud of...we created the Permanent Fund, we created the Constitutional Budget Reserve. It is time to act now to do something else that we can be proud of, plan for the future for all of us. The Chamber feels that by following the priorities we have touched on here...

1. Handle the problem this session.
2. Identify appropriate budget reductions and take actions to implement a budgeting plan for all departments based on goals and results. We care not only about what we spend...we are very concerned about what we get for the money we do spend.
3. Use a revenue stream using investment earnings to cover budget shortfalls.
4. Then, and only then, implement a broad-based tax that is fair to all Alaskans.

By following these steps, Alaska's long term fiscal future will be far more secure than waiting too long to act.

I appreciate the time you have given the Chamber to voice our concerns, and we know that both the Legislature and the Administration are moving forward to solve our collective problem. Thank you.



Analysis of Alaska's Budget Deficit

March 24, 1999

Senate Finance

1

3/24/99



Presentation Objectives

- Identify potential goals and guidelines to be used to assess any long term financial plan

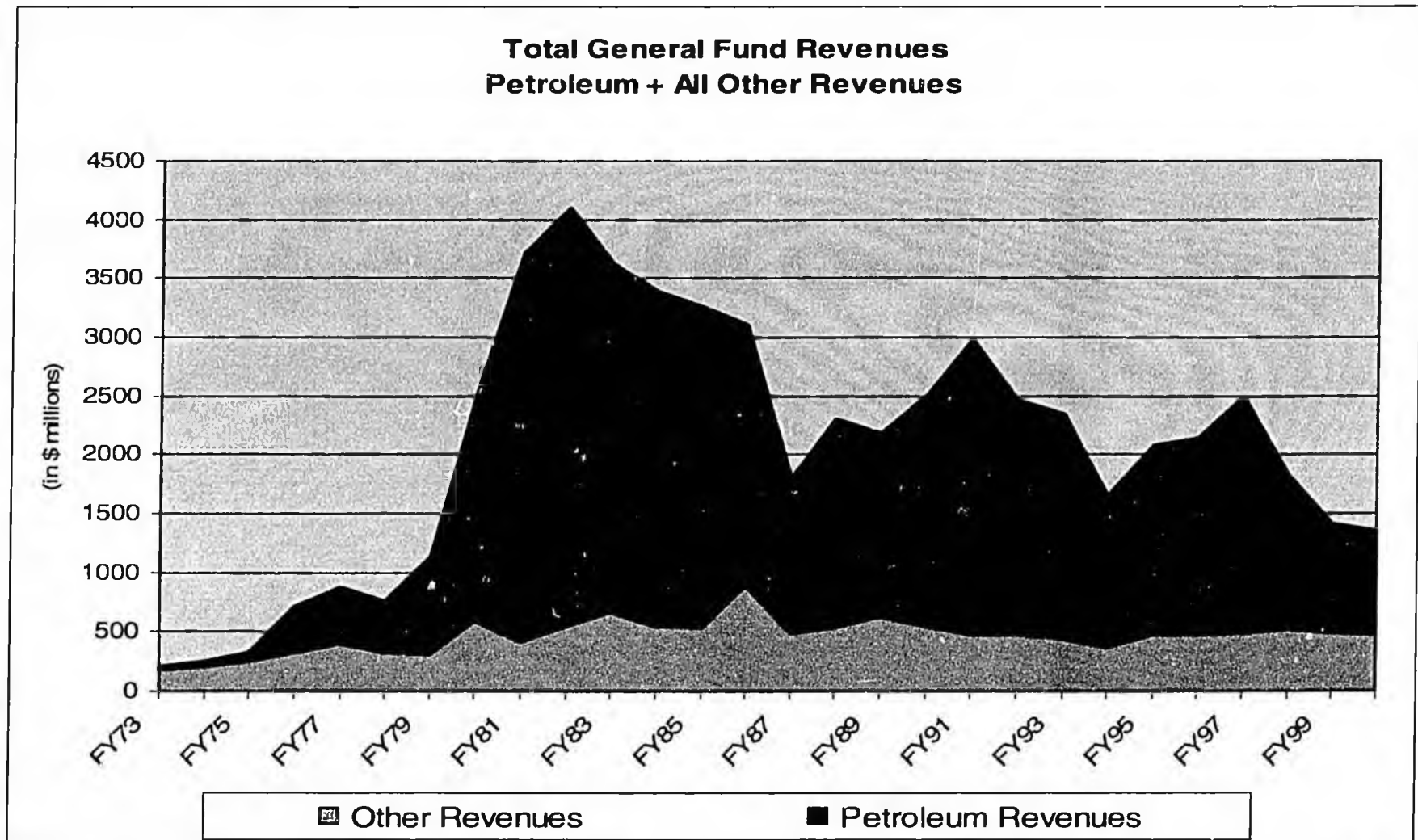
How To Begin The Analysis?

■ Current Situation

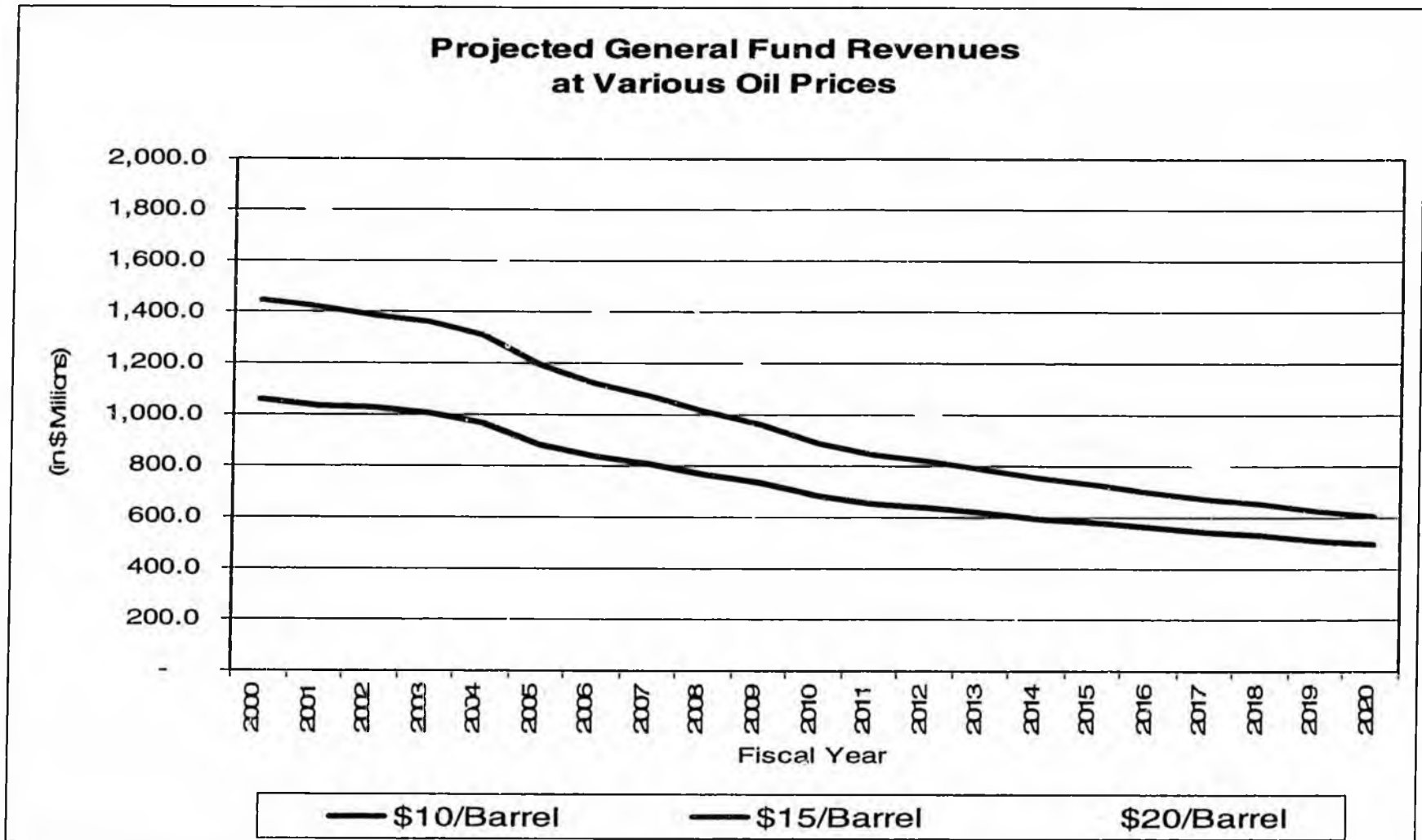
- ◆ Understand the magnitude of the problem
- ◆ Understand the model

■ Current Situation with High Oil Prices

Historical State Revenues



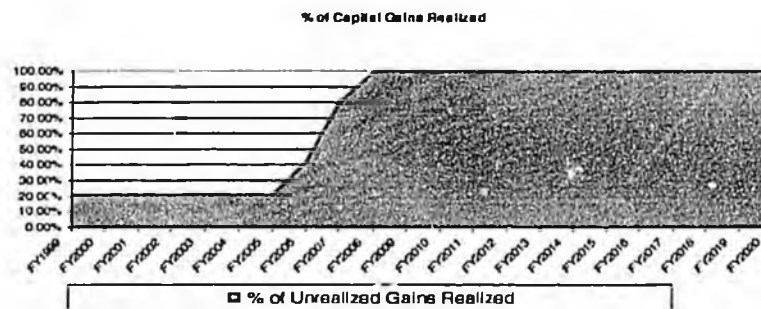
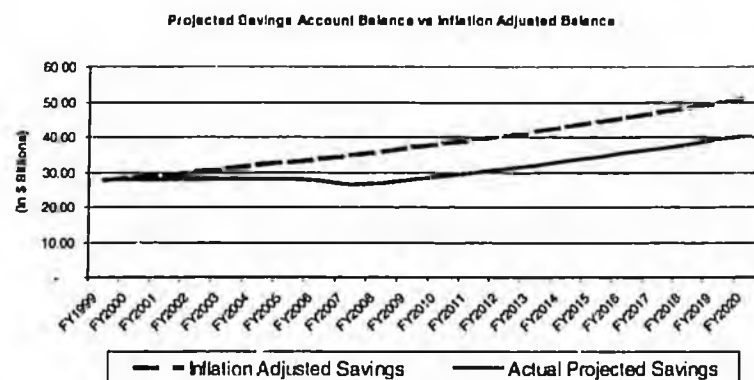
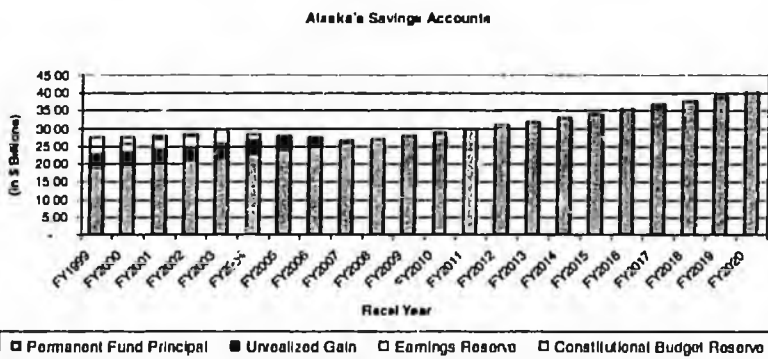
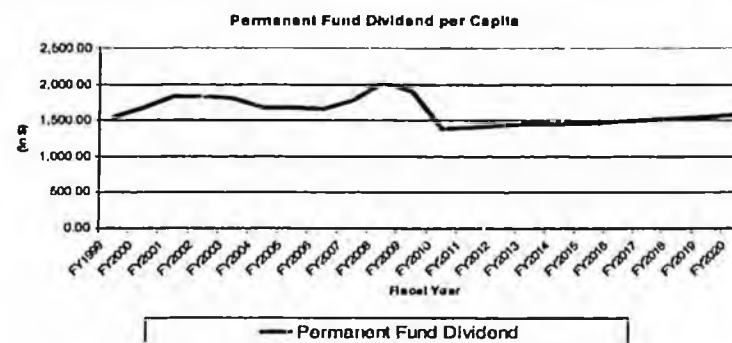
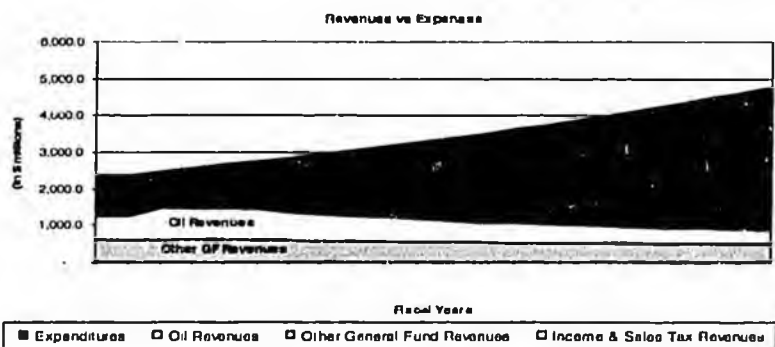
Projected Revenues



Current Situation - Assumptions

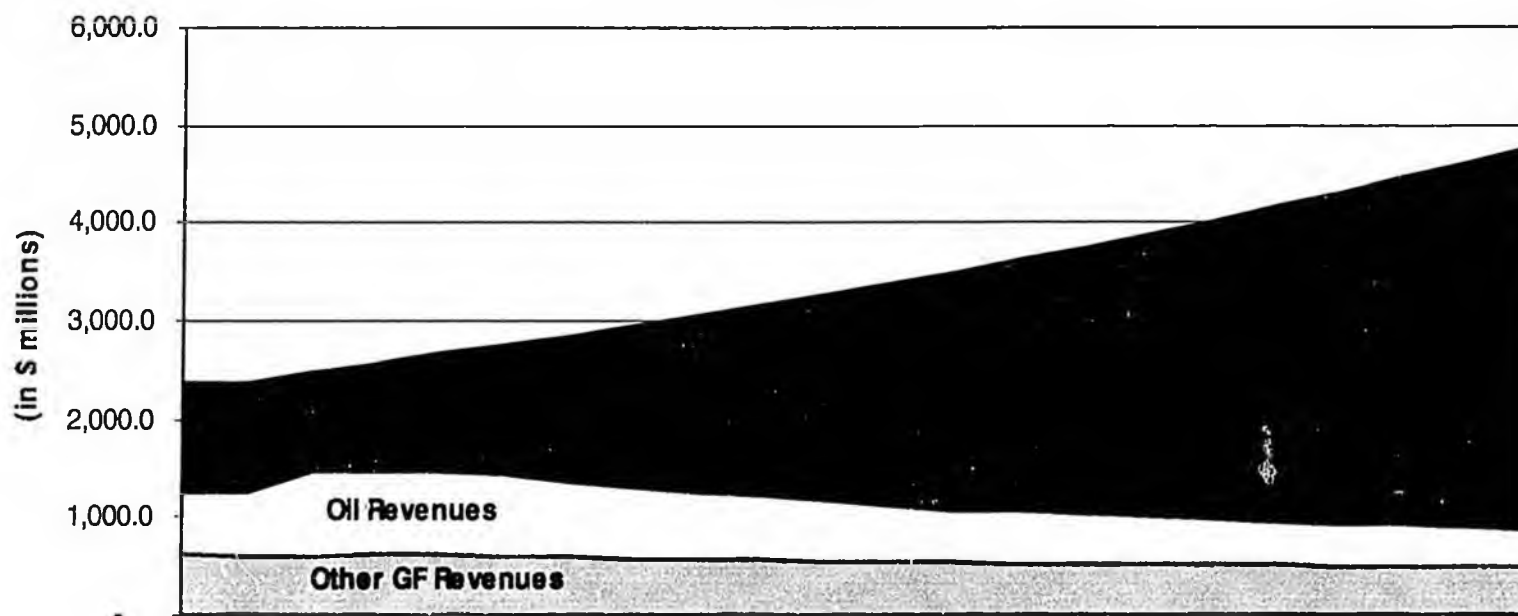
- 3.0% Inflation
- 1.5% Population Growth in K-12 Education
Formula Population
- 2% Population Growth for Dividend ONLY!
- No Growth in Population for all other Formula or
Agency Expenditures
- Permanent Fund Total Return of 7.75%
- CBR Total Return of 5.5% if less than \$3B and
8.1% if greater than \$3B

Current Situation

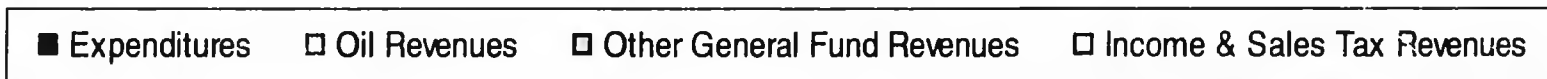


Current Situation - Revenues & Expenditures

Revenues vs Expenses

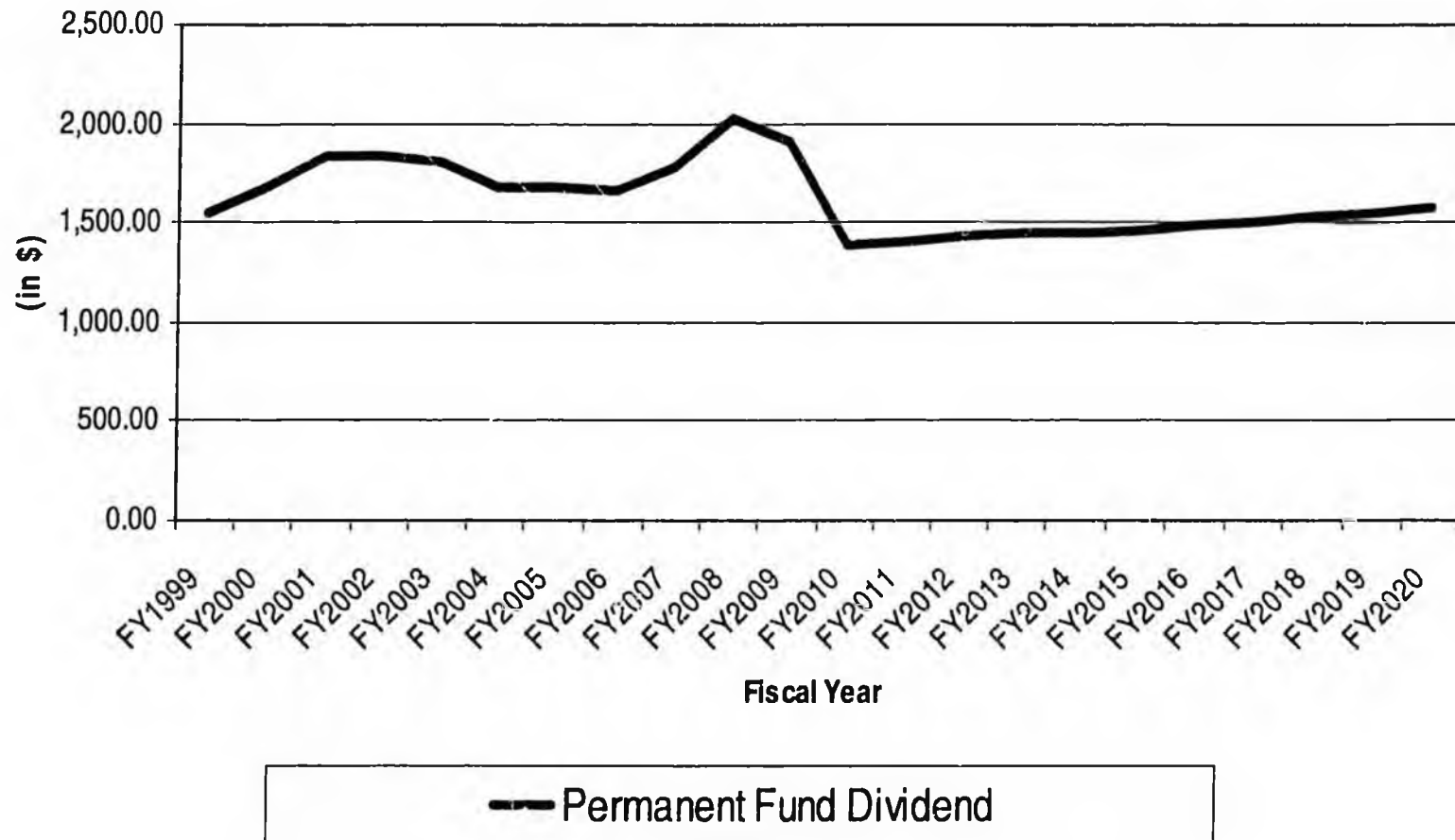


Fiscal Years



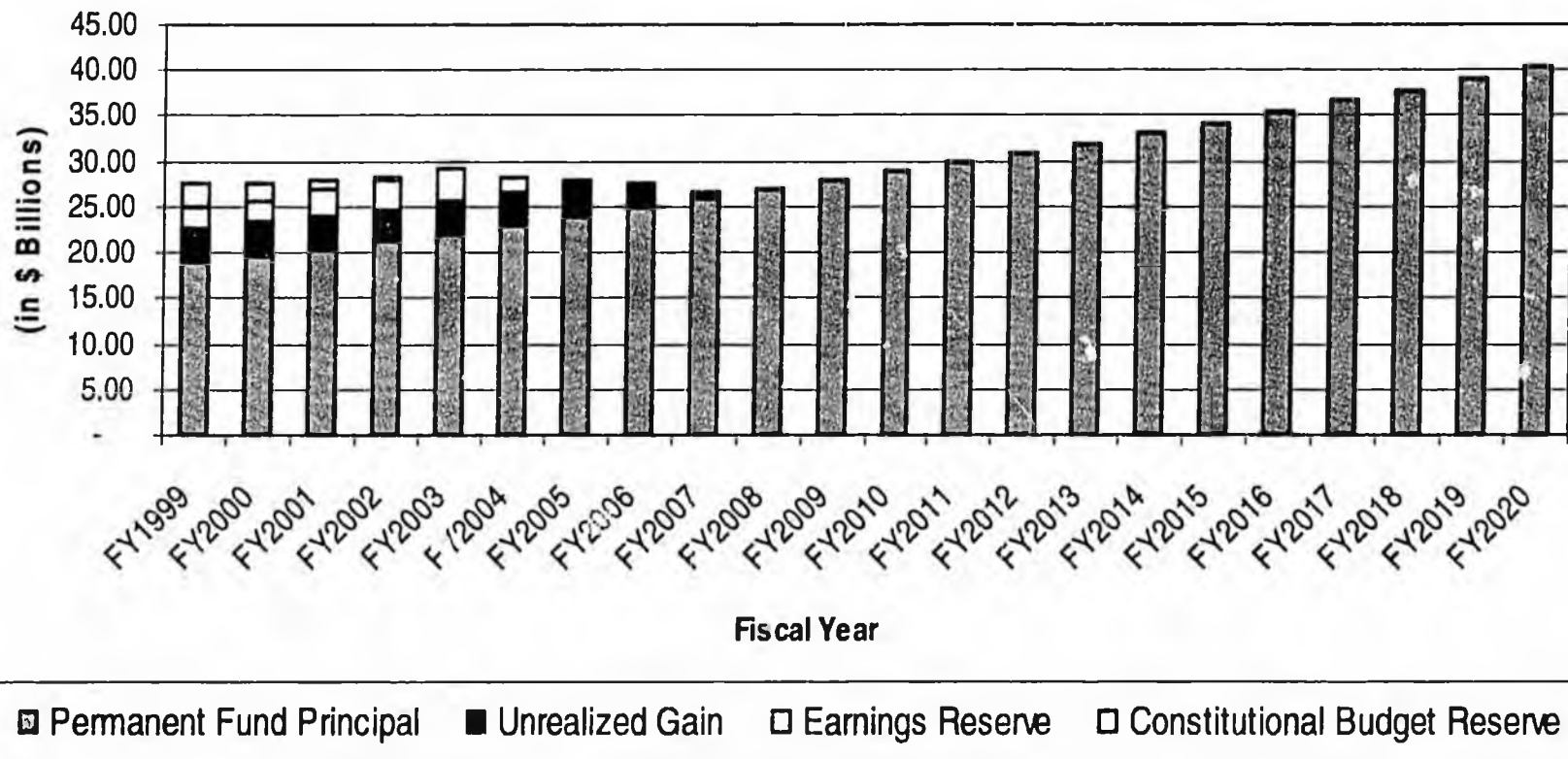
Current Situation - Permanent Fund Dividends

Permanent Fund Dividend per Capita



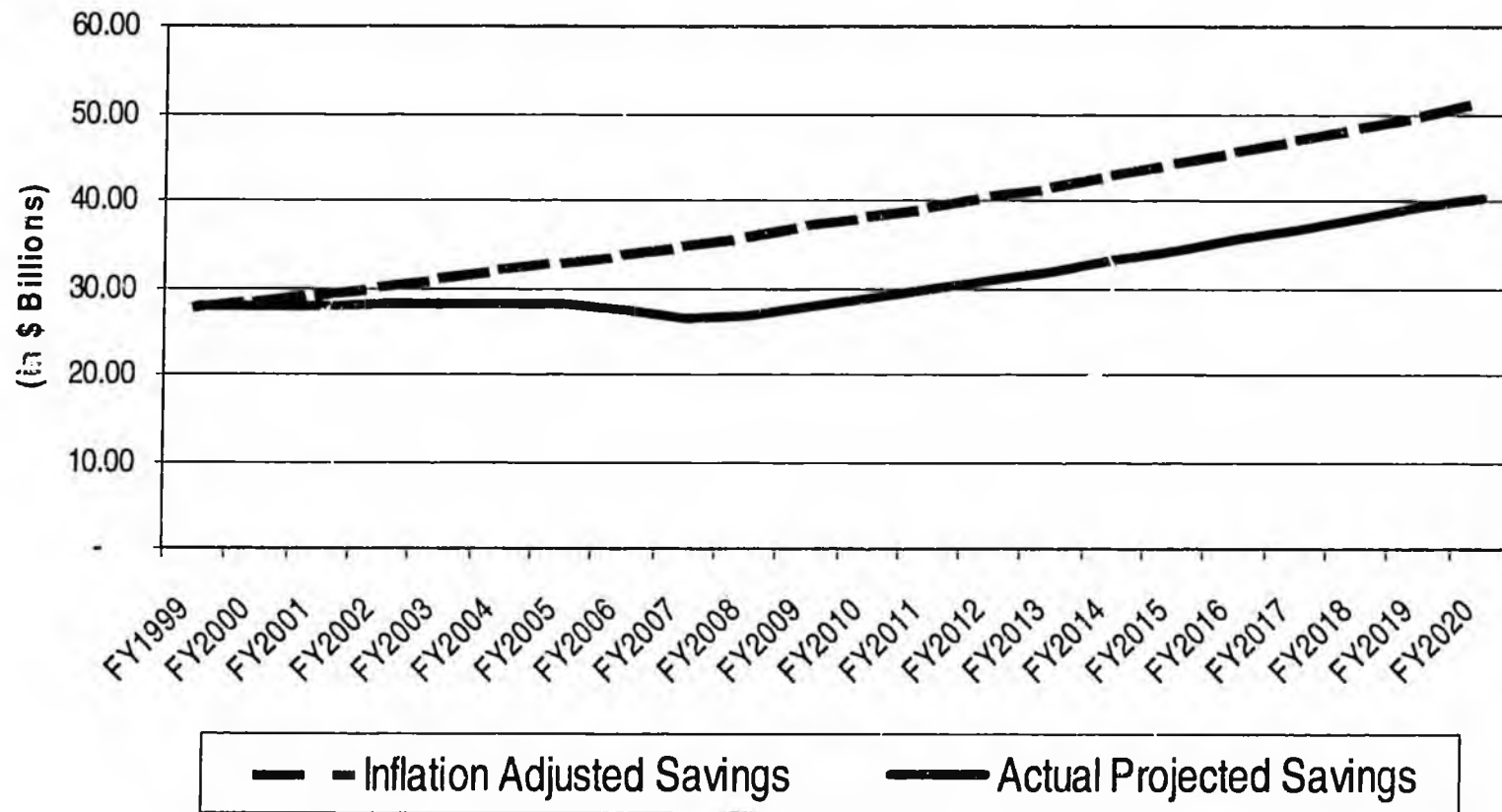
Current Situation - Alaska's Savings Accounts

Alaska's Savings Accounts



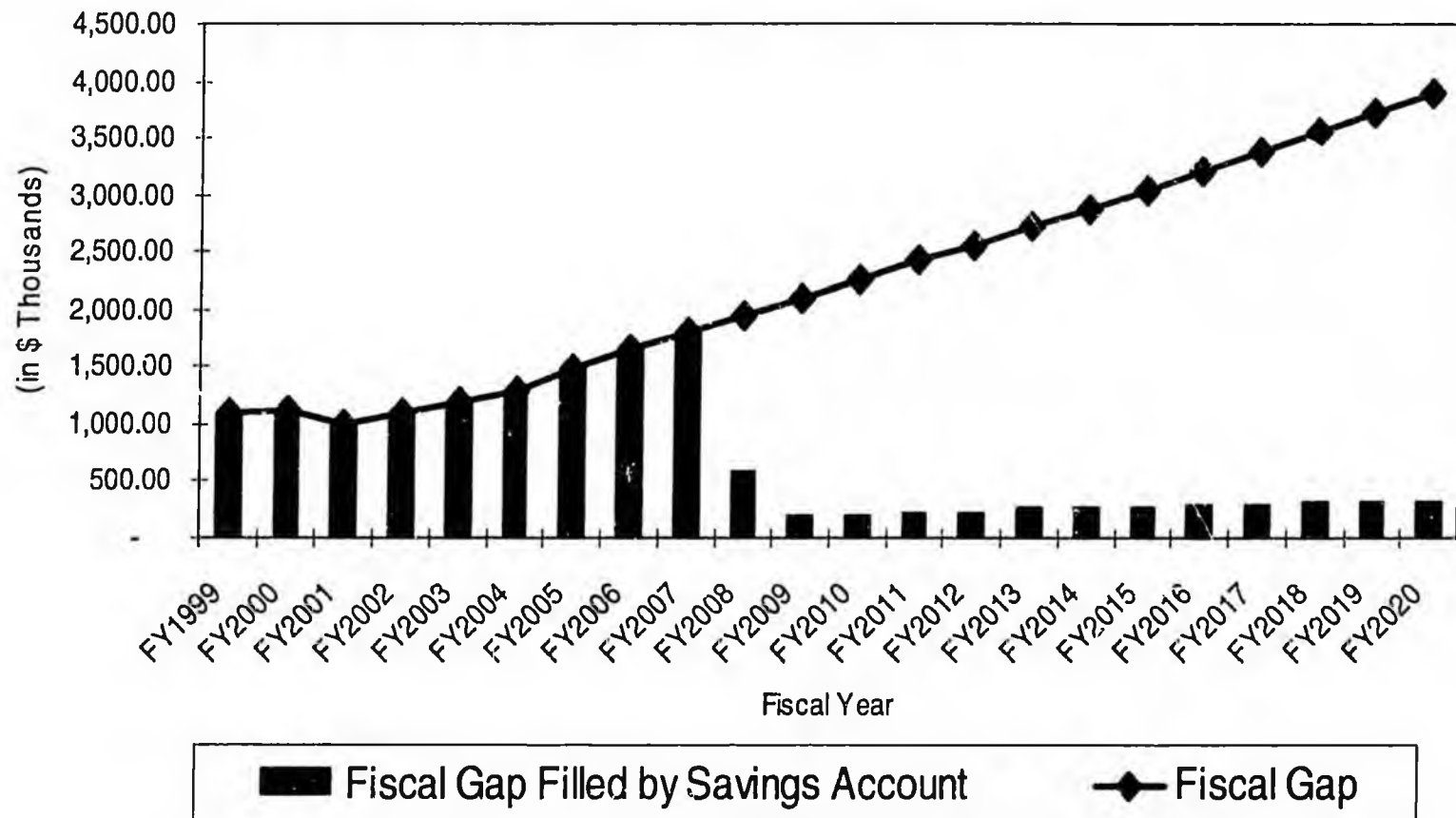
Current Situation - Savings Account Analysis

Projected Savings Account Balance vs Inflation Adjusted Balance



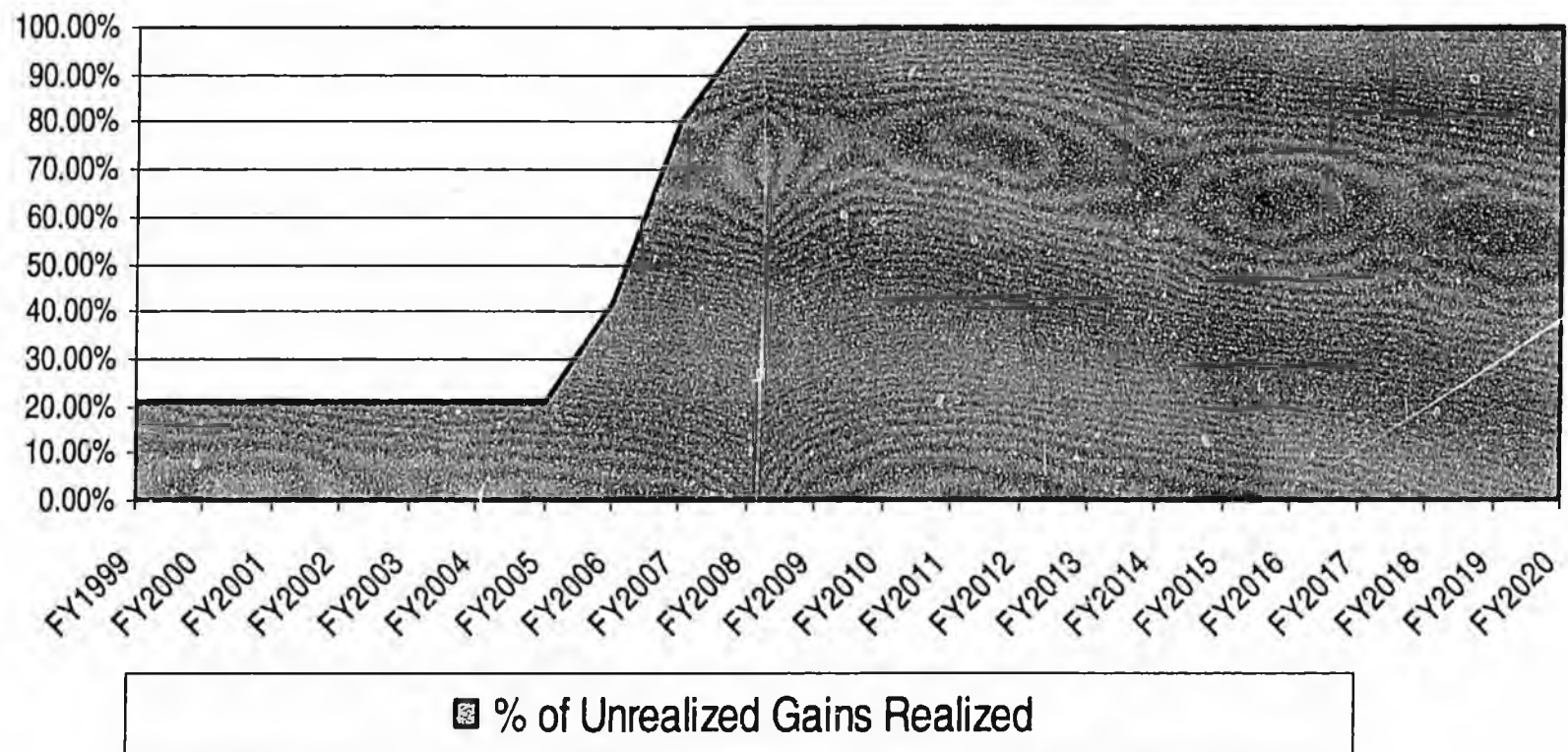
Current Situation - Budget Deficit

Fiscal Gap vs Savings Account Earnings Used to Fill Fiscal Gap



Current Situation - % of Capital Gains Realized

% of Capital Gains Realized

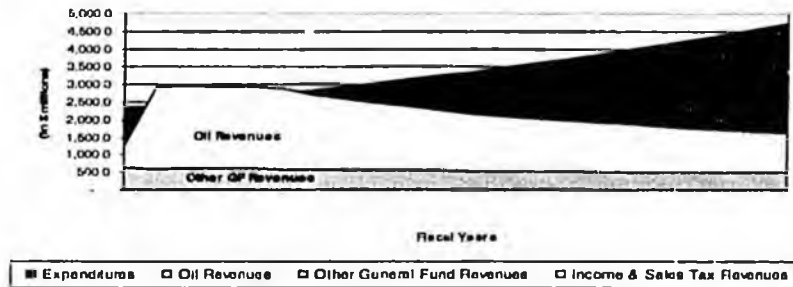


\$34/bbl Oil Assumptions

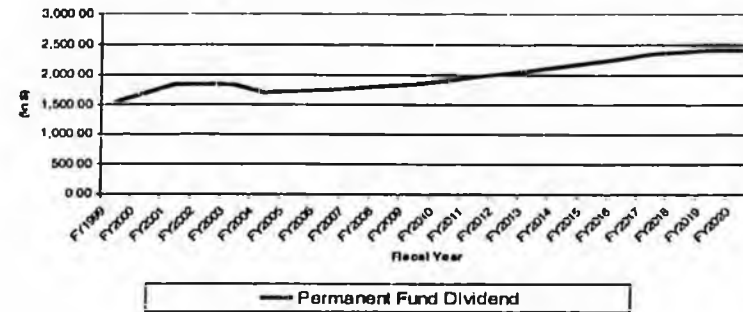
- Same as Current Scenario
- Except:
 - ◆ Oil goes to \$34/bbl in FY2000
 - ◆ Oil never goes down from \$34/bbl
 - ◆ In fact it rises every year at the inflation rate of 3% (In FY2020 Oil = \$61.41/bbl)
- Why \$34/bbl?
 - ◆ That is what it would take to create a sustainable budget until 2020 with no cuts and no taxes...But there are concerns.

Current Scenario with \$34/bbl Oil

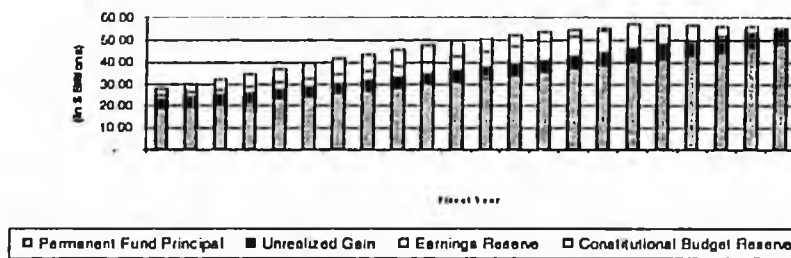
Revenues vs Expenses



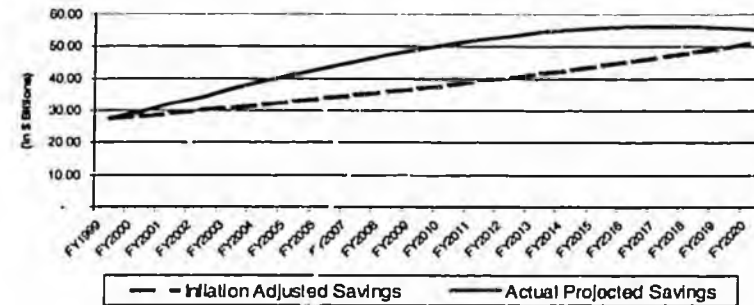
Permanent Fund Dividend per Capita



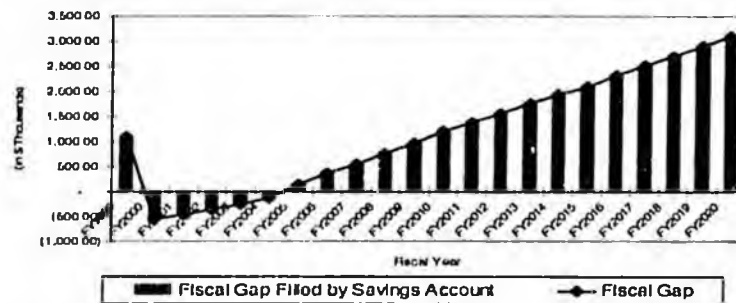
Alaska's Savings Accounts



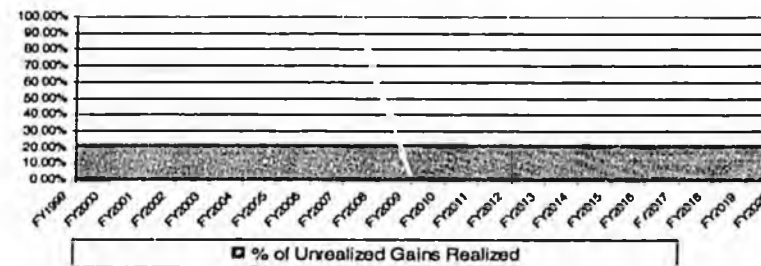
Projected Savings Account Balance vs Inflation Adjusted Balance



Fiscal Gap vs Savings Account Earnings Used to Fill Fiscal Gap

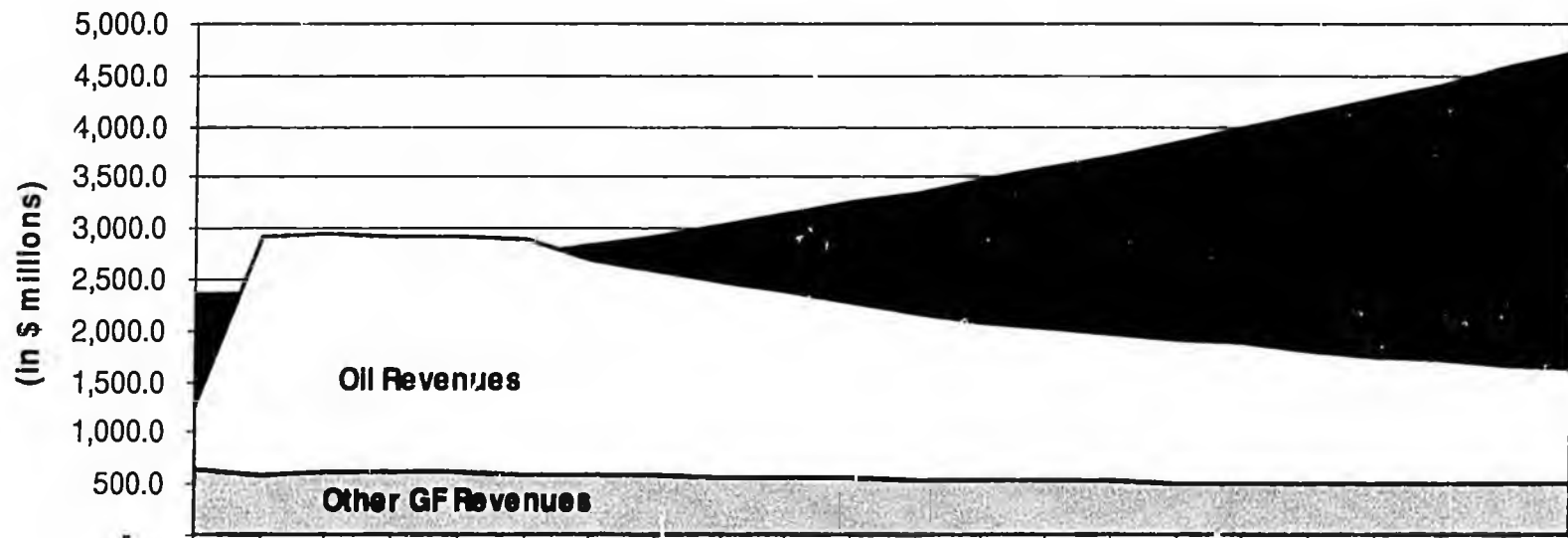


% of Capital Gains Realized

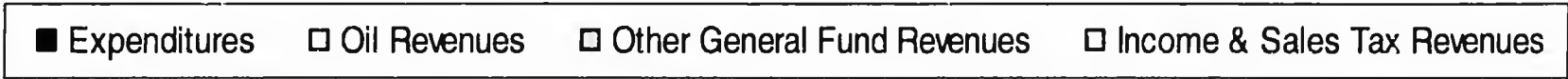


Current Scenario with \$34/bbl Oil

Revenues vs Expenses

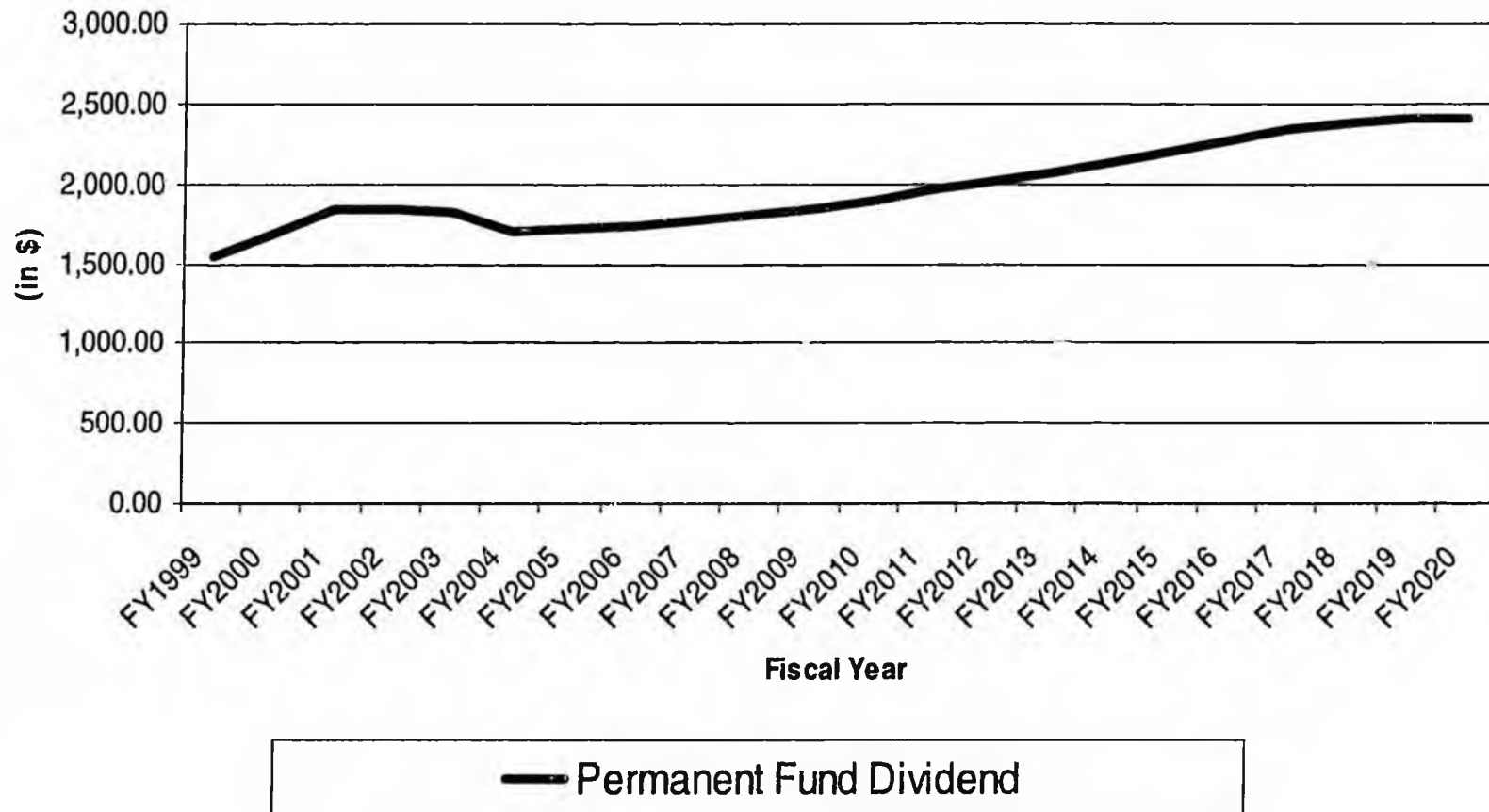


Fiscal Years



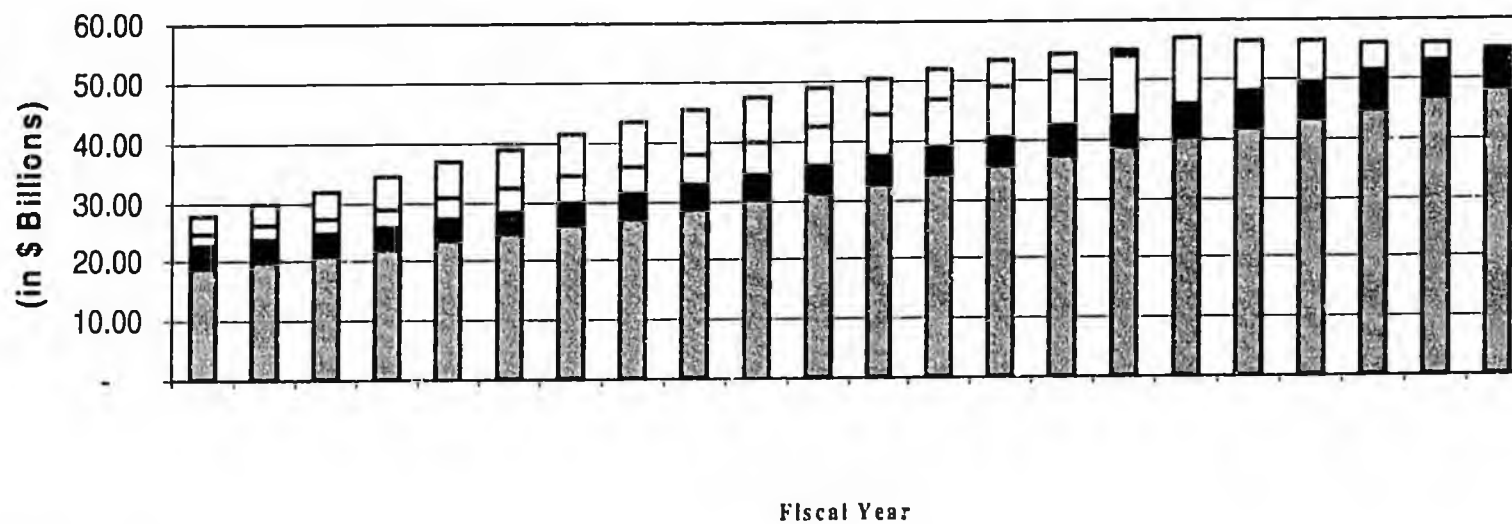
Current Scenario with \$34/bbl Oil

Permanent Fund Dividend per Capita



Current Scenario with \$34/bbl Oil

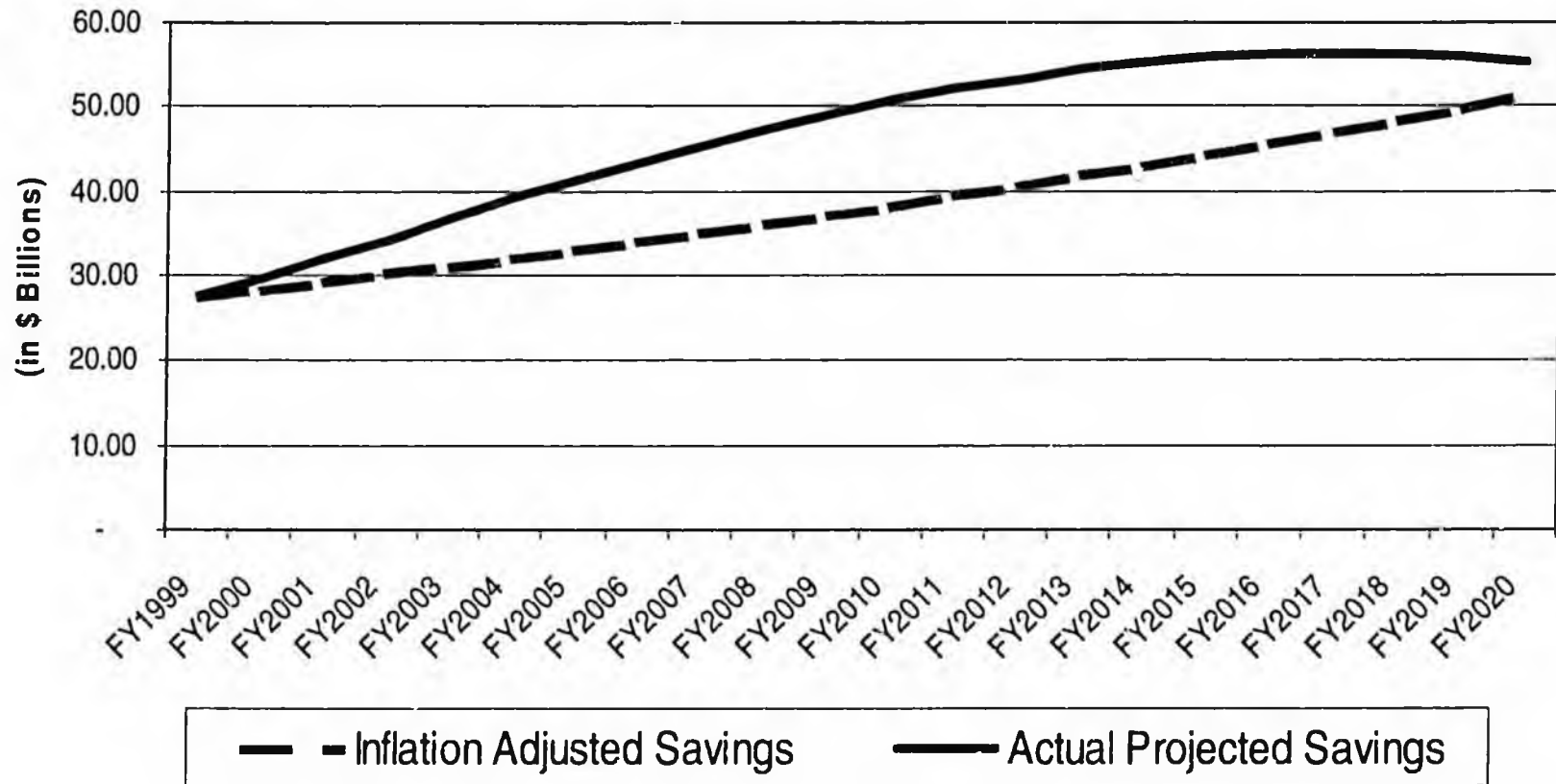
Alaska's Savings Accounts



Permanent Fund Principal
 Unrealized Gain
 Earnings Reserve
 Constitutional Budget Reserve

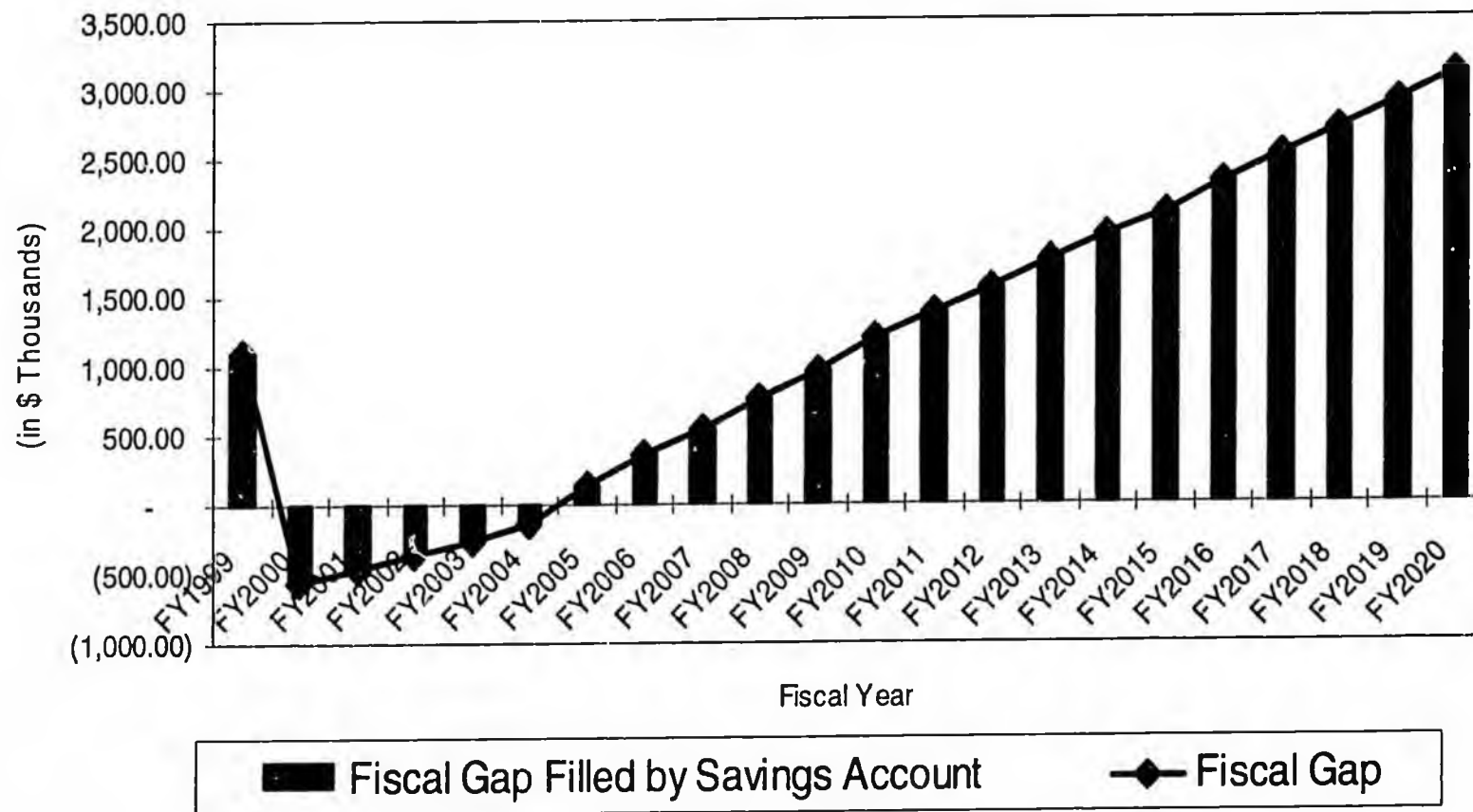
Current Scenario with \$34/bbl Oil

Projected Savings Account Balance vs Inflation Adjusted Balance



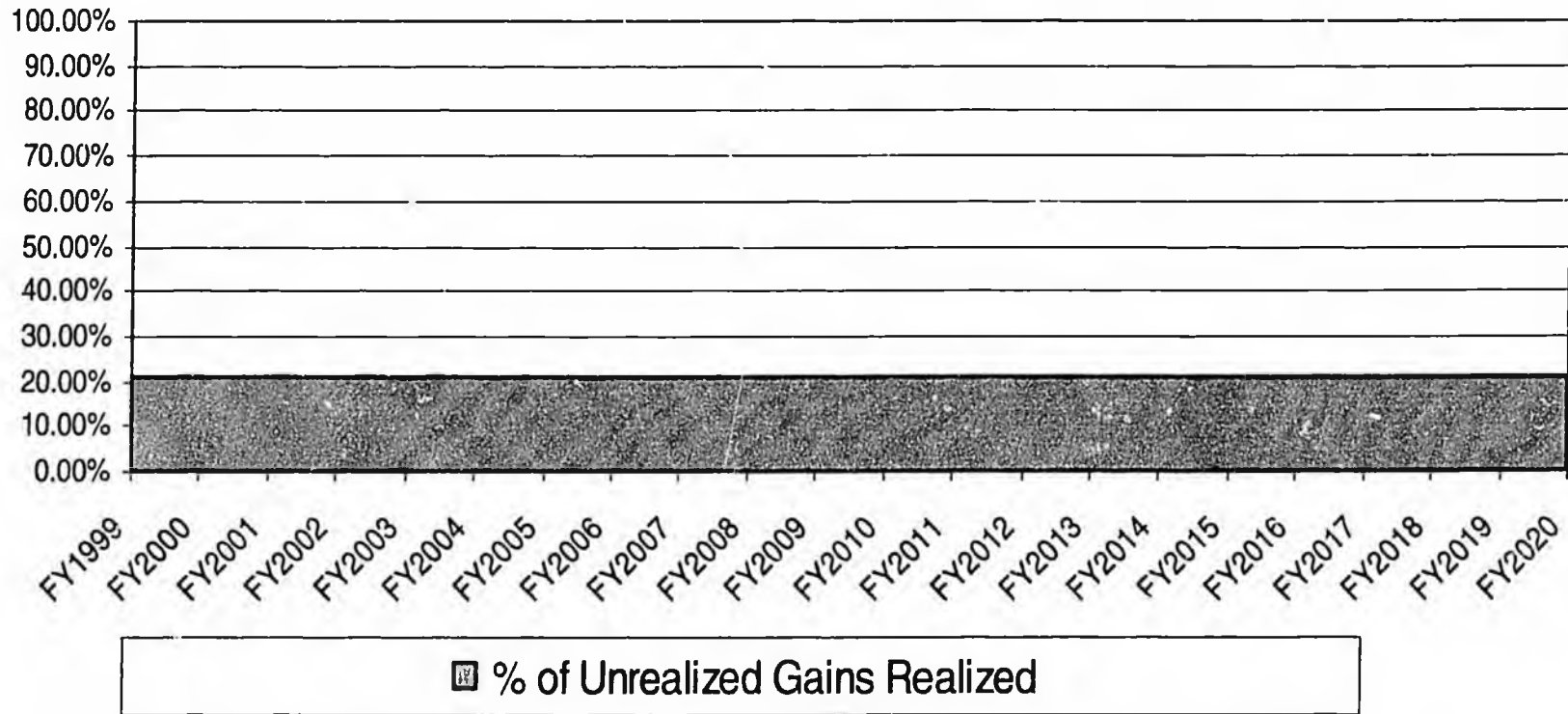
Current Scenario with \$34/bbl Oil

Fiscal Gap vs Savings Account Earnings Used to Fill Fiscal Gap



Current Scenario with \$34/bbl Oil

% of Capital Gains Realized



What Does this all mean?

- The model shows that the problem is not a cyclical problem, but rather it is a structural problem.
- Structural Problems cannot be overcome by riding it out.



Issues Facing the Legislature

- Pivotal moment in Alaska's History
- Not a short term/cyclical problem, but rather a long term/structural problem



Choices

- Cut Costs
- Raise Revenues
- Begin to systematically use the State's Savings Accounts
- A Combination of the above

Potential Measurable Goals of a Long Range Plan

- Sustainability
 - ◆ Intergenerational Equity
- Stability
- Predictability
- Ability to fund Permanent Fund Dividends
- Ability to fund the Deficit

Sustainability

- Protect the Principal (Traditional)
- Inflation Proofing
- Is the goal to protect the purchasing power of the Alaska's Savings Accounts?
- What time horizon is appropriate?



Intergenerational Equity

- Closely related to Sustainability
- All generations are held equal.



Stability

- Plan's ability to weather worst case scenarios
- Plan's ability to reduce the State's revenue volatility.

Predictability

- What level of predictability do we want to assume for:
 - ◆ Revenue Assumptions
 - ◆ Expenditure Assumptions
 - ◆ Market Assumptions

- Implications for Risk & Asset Allocation

Presentation order for the Private Sector - Testimony
Wednesday March 24, 1999

to Jerry Lee
FROM
DeB


Fiscal Policy Council - Cheryl Frasca

Ak State Chamber - Pam LaBolle

Resource Development Council - Ken Freeman

Anchorage Chamber of Commerce - chairman Ralph Samuels

Ak Support Industry Alliance -General Mgr. Karen Cowart

Associated General Contractors- Roxanna Horschel

LOCATION: ANCHORAGE

BALANCED BUDGE

BALANCED BUDGE

CHARLES

ROGER

MCKEE

CREMO

TESTIFY

TESTIFY

03/24/99
09:03:29

LEGISLATIVE TELECONFERENCE NETWORK SYSTEM
PARTICIPANT LIST (ALL PARTICIPANTS)
TCN:90429 SCHEDULED FOR:03/24/99 09:00 TO 11:00
PUBLIC HEARING SENATE FINANCE

LTN1150
BY:ANC
FOR:ANC

LOCATION: ANCHORAGE
BALANCED BUDGE

VINCENT

O'REILLY

TESTIFY