Big-Picture Truths Regarding Alaska's Fiscal Challenge

by ACG Chair Cliff Groh written for the Alaska Bar Rag on page 7 of the April-June 2016 edition.

Let's look past the legislative impasse as of this writing (May 10) to review some enduring truths about Alaska's circumstances. At the end of this piece, there's an invitation to a free event to help you learn even more.

The long-term decline in Alaska oil production and **the deep slump in world oil prices over the past two years** have combined to create major and continuing challenges for both Alaska's government and Alaska's economy.

The State of Alaska's oil revenues have fallen more than 90 percent in the last four years (Fiscal Year 2012 to Fiscal Year 2016, which ends June 30, 2016). That large reduction in oil revenues is a big problem given that oil revenues provided an average of 90 percent of Unrestricted General Fund revenues for the period of Fiscal Year 2005 through Fiscal Year 2014.

This sharp drop in revenues has contributed to **big structural deficits both this year and in the future**. The deficit is approximately $4 billion this year (FY2016), and that number is equal to about ¾ of the budget (as conventionally defined as Unrestricted General Fund spending).

The State of Alaska's ability to finance deficits using the Constitutional Budget Reserve Fund—the savings account traditionally used to fill the gap—is going away fast. **The Constitutional Budget Reserve Fund (CBR) will fall to zero in less than two years at the current burn rate.**

Although still probably the highest per capita among the states, **Alaska's state budget has fallen and continues to**

fall. Adjusted for inflation and population, the operating budget is the lowest it has been in 10 years.

The State of Alaska's top three General Fund expenditures are for K-12 education, health and social services, and refundable oil tax credits. Refundable oil tax credits—which represent only a subset of all oil tax credits offered by the State of Alaska—cost $500 million this fiscal year (FY2016). As of this writing, refundable oil tax credits are projected under current law to cost $775 million in Fiscal Year 2017 (July 1, 2016-June 30, 2017), which works out to more than $1,000 per Alaskan.

Alaskans are the lowest-taxed people in the U.S. Alaska is the only state with no form of state income tax and no form of statewide general sales tax.

The restructuring of the Permanent Fund earnings system under the most frequently discussed proposals will still likely leave Alaska with a substantial deficit.

The existence of the Permanent Fund—and even more the Permanent Fund Dividend—make fiscal politics in Alaska more difficult and complex than in other states.

The Permanent Fund and the Permanent Fund Dividend raise unusual questions of equity, both among classes and among generations.

Critical questions relevant to the fiscal challenge include "What is the Permanent Fund for?" and "How long do you intend to live in Alaska?"

Alaska perhaps faces a future of battles in court over levels of government funding.

Resolving Alaska's fiscal challenge is a question of values as well as a question of numbers.

Alaska's challenge is psychological and cultural as well as fiscal and political. Alaska needs to move from imagining easy prosperity to find fiscal sustainability in an era likely to feature increasing scarcity.

Alaska’s legislators face a particular challenge. The Big Oil era in Alaska has made it relatively easy for lawmakers in Alaska to accommodate a lot of requests and desires for spending. Now the sharp decline in oil revenues is forcing legislators to transition to a new reality of picking winners and losers (or at least relative winners and losers).

The transition is not going well so far. One or more of the following impulses seem to be driving a number of legislators: hope; expedience; desire to inflict pain; and blame-shifting.

The hope is for higher oil prices. Oil prices have increased in the last few months, but—as always—it is critical to focus on scale. World oil prices would have to more than double and—given the forecasted continued declines in oil production—keep going up in real terms to solve Alaska’s fiscal problem through price increases alone.

The expedience comes in with the wish of a number of lawmakers to put off big decisions until after the general election in November. Although there is a benefit to delay if that passage of time allows Alaskans to better understand the actual facts and options, the major cost is that the longer Alaskans wait to address the fiscal challenge, the lousier their options become.

The desire to inflict pain comes from the expressed belief of some legislators that big and difficult decisions need to come after their constituents feel the hurt of more cutbacks.

The blame-shifting part arises because a number of legislators feel a need to blame any unpopular decisions on somebody else or on some external event. One risk for Alaskans is that this external event might be a recession exacerbated by the Legislature’s actions and omissions this year.

You can join other Alaskans—including probably some legislators—in learning more about the continuing fiscal and economic challenges at an event **Saturday, October 1, at the Wendy Williamson Auditorium on the University of Alaska Anchorage campus.** This event is free, open to all, and sponsored by Alaska Common Ground. Attending it will allow you to get more information about the facts and options as Alaska confronts the reality of paying for public services and maintaining a good economy in a new environment.

Cliff Groh is a lifelong Alaskan, a lawyer, and a writer. He is also Chair of Alaska Common Ground, a non-partisan and non-profit public policy organization focused on helping Alaskans seek consensus on the major issues facing the state. He worked on oil tax legislation while serving as Special Assistant to the Alaska Commissioner of Revenue in 1987-1990 and was the principal legislative assistant on the legislation creating the Permanent Fund Dividend in 1982.