Not Your Ordinary Fiscal Crisis

Janet McCabe : Opinion Piece Anchorage Daily News : March 22, 2020

In the shadow of the COVID-19 pandemic and a consequent worldwide recession, Alaska legislators have self-isolated in Juneau, communicating with the public remotely. This is an abnormal and worrisome time. We want them to complete the essential work of the session and be able to go home.

But they should not quit until they agree on an affordable amount for the Permanent Fund dividend and give the dividend a dependable and stable future so it will grow as the Permanent Fund does.

Using the 40-year-old statutory formula to calculate the amount of the dividend, the Legislative Finance Division has projected that the state's budget deficit for the upcoming fiscal year will exceed $1.5 billion. Many of us have trouble visualizing a number that large. As a current example, take the governor's proposal to raise $100 million from a state lottery. It would take 15 lotteries in a single year to raise $1.5 billion and close the fiscal gap.

Without action this session, $1.5 billion will be drained from the Constitutional Budget Reserve (CBR). That's the state's emergency rescue account, separate from the Permanent Fund. Budget analysts say the CBR should always be at least $2 billion. But unless legislators cure the fiscal crisis this session, the CBR will be reduced to $500,000, one quarter of the needed amount.

What if COVID-19 does strike with a vengeance, or climate change increases food insecurity in villages, or next summer. the forest fires we saw last year become overwhelming? Life is far too uncertain for the state to drain its emergency rescue account.

Recently, in recognition of the urgency of the fiscal crisis, the Trustees of the Alaska Permanent Fund Corporation, normally an apolitical group, added their voices to a growing chorus (Resolution 20-01). On March 5, Craig Richards, chairman of the Trustees, announced that payments from the Permanent Fund earnings are endangered. He recommended “that the State put in place a structure that minimizes that risk before a series of bad market events result in payment shortfalls.”

That warning was on March 5. Since then, the stock market has tumbled and a worldwide recession is looming.

The root of the problem as set forth by the Trustees is the conflict between (1) the statute that set the amount of the dividend 40 years ago, and (2) the percent-of-market-value statute adopted in 2018 to provide the state with sustainable annual revenue from the Permanent Fund Earnings Reserve Account. If the market falls repeatedly, Permanent Fund earnings would be reduced to the point where “we couldn’t fund the government and we couldn’t fund people’s dividends.”

The Trustees’ warning came with some useful advice, offering the legislature realistic solutions. The first of which was: “Transform by constitutional or statutory amendment, the Alaska Permanent Fund and the (Permanent Fund) Earnings Reserve Account into a single fund and limit the annual draw to the fund’s long term real return.”

House Joint Resolution No. 31 would do just that, using a constitutional amendment to combine the two parts of the Permanent Fund. Annual payments to the general fund follow the system adopted by the legislature in 2018 by passing SB 26. That bill established a percent of market value (POMV) system putting annual draws from the Permanent Fund on a sustainable system like that used by many institutions to manage large endowments.

Senate Bill 26 was just in time. Oil revenues dropped to $2 billion in 2018, but the POMV draw from the Permanent Fund (Earnings Reserve account) provided $2.9 billion, reversing a long decline in total state revenue.

Now, in implementing the Trustees’ proposal, the Legislature should pick up a piece of unfinished business from 2018. In developing SB 26, the 30th Legislature had intended to include language establishing a percentage for the dividend so it would be a stable ongoing amount of the POMV draw. But they had bogged down because, at that time, a few legislators still supported the traditional formula.

Now that the state is facing an immediate fiscal crisis specifically caused by a supersized dividend that would drain our emergency rescue account; now that the Trustees of the Alaska Permanent Fund Corporation have warned the legislature about effects of a “series of bad market events”; now that the size of the traditional dividend threatens the future of the dividend itself – now is surely the time to give the dividend a stable and affordable place in Alaska’s fiscal future. The dividend should grow as the Permanent Fund grows. This can be done by statutorily resetting the amount of the dividend, so it is a percentage the annual POMV payment.

Last December at Commonwealth North’s traditional pre-session luncheon, House Speaker Bryce Edgmon and Senate President Cathy Giessel both emphasized their wish to “communicate, collaborate and compromise.” Giessel quoted from President John F. Kennedy’s first inaugural address. Even more memorably, she quoted former U.S. Sen. Ted Stevens: “To hell with politics. Let’s do what’s right for Alaska.”

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Read the piece in the ADN here.

What Kind of Alaska do we

want?

A packed crowd gathered at the 49th State Brewing Company on December 10, 2019 for Alaska Common Ground's fiscal forum entitled **What kind of Alaska do we want? How do we get there?** The discussion featured Senator Natasha von Imhof, Co-chair of the Senate Finance Committee; Anchorage Mayor Ethan Berkowitz; CIRI Government Relations Vice President, Greg Razo; Institute of Social and Economic Research economist, Mouhcine Guettabi; and Atwood Chair at the UAA Department of Journalism, Larry Persily. Thea Agnew Bemben of Agnew::Beck moderated. The goal of the event was to increase public knowledge and understanding of the realities of Alaska's financial situation, and of potential measures to achieve a positive fiscal future.

Senator von Imhof launched the forum with a well-illustrated dose of reality (see her presentation slides here). "We are at a crossroads!" she said. Alaska cannot stay solvent if the state continues to pay dividends at, or even close to, the current statutory amount. She wants the legislature to find middle ground for all spending and establish a spending cap. Though she believes there are still government inefficiencies to be corrected, she noted that "It takes time and focus and energy to find more efficiencies…large cuts have to be walked back."

She and other panelists highlighted the fact that Alaska's primary source of revenue for government spending is now through management of the Permanent Fund as an endowment under Senate Bill 26. State revenue from this source now exceeds revenue from petroleum production, and, based on current projections, will continue to do so. The statute established 5.5% as the percentage of the market value available from the Permanent Fund this year. Next year it will be 5%. Other endowment systems were studied, and percentages were carefully gaged and set to protect the principle of the fund.

Greg Razo noted that Alaska's public spending must recognize the food insecurity in villages where part of the economy is subsistence hunting, fishing, and gathering. Climate change is threatening this ancient and traditional part of Alaska's economy.

Mayor Berkowitz described how once generous state assistance to Anchorage has been reduced over the years to a pittance. Now the state does not even clear sidewalks on state roads within the municipality. He sees great potential to build the earnings of the Permanent Fund by investing more money in it. The Mayor advocated dividing the growing "percent of market value" earnings three ways to establish an ongoing percent for municipalities, for state services, and for dividends.

Mouhcine Guettabi and Larry Persily took the lead in emphasizing the economic value of quality of life and the fact that attracting people and economic development to Alaska depends greatly on having good state educational systems, transportation, and other public services. Persily concluded by telling people to look at the math, face reality, and find the revenues to build the secure and prosperous state that we want. All speakers noted that establishing ongoing fiscal predictability and stability would be an economic stimulant. The need for new revenue sources, such as taxes, was mentioned frequently in describing a positive fiscal future for our state.

The event was audio recorded by Alaska Public Media, livestreamed on Facebook, and video recorded by Jenson Hall Creative. You can watch the video here. Co-chairs of the planning committee for this forum were Janet McCabe and Cliff Groh. Cliff Groh has written a series of articles for the Anchorage Press on Alaska's fiscal issues. You can read one here. If you want to read them all, search for Cliff Groh at anchoragepress.com.

We shouldn't waste the time before the budget wars begin again

Larry Persily, Published October 21, 2019, Anchorage Daily News

As the chances of a special legislative session this fall diminish, Alaskans have some extra time to think about how to fix the state's fiscal future next year.

The Legislature will convene in regular session in less than 90 days and no doubt the budget, public services and long-term finances will dominate the debates — as they should. We've confronted — and at the same time avoided — the problems since the 1990s. The indecision is hurting our communities and Alaska's economic future.

We've put off the decisions in election years for fear of punishment at the polls, and have been unable to solve them in non-election years because too many players are looking ahead to the next campaign.

All the while, the big-number options for balancing spending and revenues are unchanged despite years of arguing, spreadsheets and town halls: Cut state spending on public services; collect taxes from individual Alaskans, non-resident workers and/or visitors; increase taxes on oil production; use Permanent Fund earnings and adjust the calculation for the annual Permanent Fund dividend.

People can talk all they want about railroads to Canada, roads to remote Alaska mining districts, mythical North Slope natural gas pipelines and hypothetical benefits of being "open for business" (whatever that overused slogan means), but the mathematical reality is that none of the above politically inflated legends could ever produce enough state revenue to avoid the hard decisions on public services, taxes and the size of the PFD.

Our decisions should be based on reality, not dreams.

Those decisions on public services, taxes and the PFD are uncomfortable, even painful to many, and all are politically dangerous, maybe even politically deadly. But waiting any longer isn't going to make some new option appear out of nowhere or make the problems go away, just like the broccoli isn’t going to disappear from the 12-year-old’s plate no matter how long he avoids it.

The solution is all of the above (minus the broccoli). Everyone benefits in the long term if everyone contributes. The odds of political success are better if everyone jumps together.

In the 1969 film, “Butch Cassidy and the Sundance Kid,” Robert Redford and Paul Newman survived when they jumped off the cliff together. Sure, they were being chased by a posse for robbing a train — unlike Alaska, which is being chased by fiscal reality — but the solution is the same: Take the leap together.

Which means legislators and the governor — and the public — need to work next year toward a comprehensive plan for a healthy, stable long-term fiscal future for Alaska.

Which means permanently restructuring the dividend formula to an affordable level that can pay Alaskans for decades.

It means spending enough on public services to protect and educate Alaskans, while building for the future, but resisting spending on programs and special projects that are beyond the role of government.

It means looking at a broad-based tax on individuals, so that all Alaskans, and the guests who enjoy and prosper during their time in the state, contribute.

And it means the oil industry should not be excused from the collective answer.

That doesn’t mean expecting the oil industry to solve all our problems with one big check, like the backers of the oil tax initiative promote. The industry knows it will always be a deep pocket in Alaska. What worries the decision-makers in corporate offices is the 40-year history that they are the only pocket we reach into. That attitude among many Alaskans, and the resulting fear among the industry, is destructive of future investment.

Our best hope is that the higher-oil-taxes-solve-everything lobby, the don’t-touch-my-PFD lobby, the no-new-taxes lobby, and the cut-

spending lobby
will put down their signs, stifle their campaign rhetoric, stop their Facebook
attacks and find an all-of-the-above compromise.

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It's Probably Worse than you Think

By Cliff Groh, Nov 4, 2019, Anchorage Press

Alaska's fiscal outlook is bad due to factors
such as drooping oil prices, long-falling Alaska oil production, and an absence
of broad-based taxes. The non-partisan Alaska Legislative Finance Division
projects that starting next year, the State faces annual deficits exceeding $1
billion under current law and the most likely assumptions.

But that gloomy scenario probably understates our fiscal squeeze. Numerous other factors either threaten future revenues or create pressures for spending to increase.

Let’s start by looking at some of those upward pressures on the budget: the unfunded liabilities of the state government’s pension systems; the capital budget; and refundable oil tax credits.

The State of Alaska is paying off the unfunded liabilities previously built up in the Public Employees’ Retirement System (PERS) and the Teachers’ Retirement System (TRS) under an officially adopted payoff plan that runs at least until Fiscal 2039. Actuaries project that the annual installments under that plan will increase every year but one, and also project that those installments will total more than $8 billion over the decades. Changing demographics and shifts in financial markets, however, could increase that total price tag over the next two decades.

The capital budget was probably too large in some years of high oil revenues. That spending for buildings and other infrastructure has fallen substantially in the last half-dozen years, however, and this year it is less than $150 million in

General Fund spending. Experts see that number as too low. The Office of Management and Budget estimated in 2018 that the State of Alaska has needs for deferred maintenance totaling $1.87 billion. One observer’s calculation is that the annual capital budget should be at a minimum tripled to start catching up on that backlog.

Then there’s refundable oil tax credits, an obligation which the Alaska Department of Revenue estimated at $700 million in June of 2019. The State has proposed to pay off the credits through a bond program now in litigation while paying zero for the credits in the current year’s budget. The obligation to pay the oil tax credits is much weaker legally than the obligation to pay in full the pension system benefits, which are explicitly protected in the Alaska Constitution.

Now let’s turn to the revenue side of the equation. Climate change poses a systemic fiscal danger to our state.

The evidence of this global phenomenon is all around us. Humans are changing their behavior in reaction to the changing physical world. The use of electric cars may blow past gasoline-powered vehicles by 2040. Oil companies are changing their names to shed their oil-only images and are focusing increasingly on wind, solar, and other renewable sources. Carbon taxes are likely to further reduce the demand for oil worldwide. At least one major energy producer—Norway-based Elsinor (formerly Statoil)—has projected that oil demand could start to decline by 2030, as Alaska Public Media’s Elizabeth Harball noted in 2018.

Climate change already appears to be reducing oil production from Alaska’s North Slope, as long-time oil industry observer Tim Bradner has pointed out. The Arctic is warming at rates twice as fast as regions further south, and those higher temperatures thaw permafrost and reduce the efficiency of oil-producing facilities.

The climate change news will probably get substantially worse for Alaska. Energy companies recognize that there is a growing possibility that the warming planet will lead to significant amounts of oil now ticketed to be produced to end up in the ground unburned. Some of that oil stranded by climate change is likely to be on the North Slope, in part because that region is expensive to work in and high-cost provinces are most likely to be the home of stranded oil.

Over the next year—and over the next 10 years or so—the downside risks for Alaska on the fiscal front appear to exceed the upside potential. Alaskans should prepare accordingly.

Cliff Groh is an Anchorage lawyer and writer as well as the legislative assistant who worked the most on the bill in 1982 that created the Permanent Fund Dividend we have today. He also designed a course he taught at the University of Alaska called "Navigating Alaska's Fiscal and Economic Challenges." This is the ninth installment of a continuing series on the Permanent Fund Dividend and Alaska's fiscal system.