The Most Important Things to Understand About Alaska's Fiscal Situation

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The presentation will be posted on ISER's website at:
www.iser.uaa.alaska.edu

The fall in oil prices has led to growing concern among Alaskans about the state's fiscal situation.

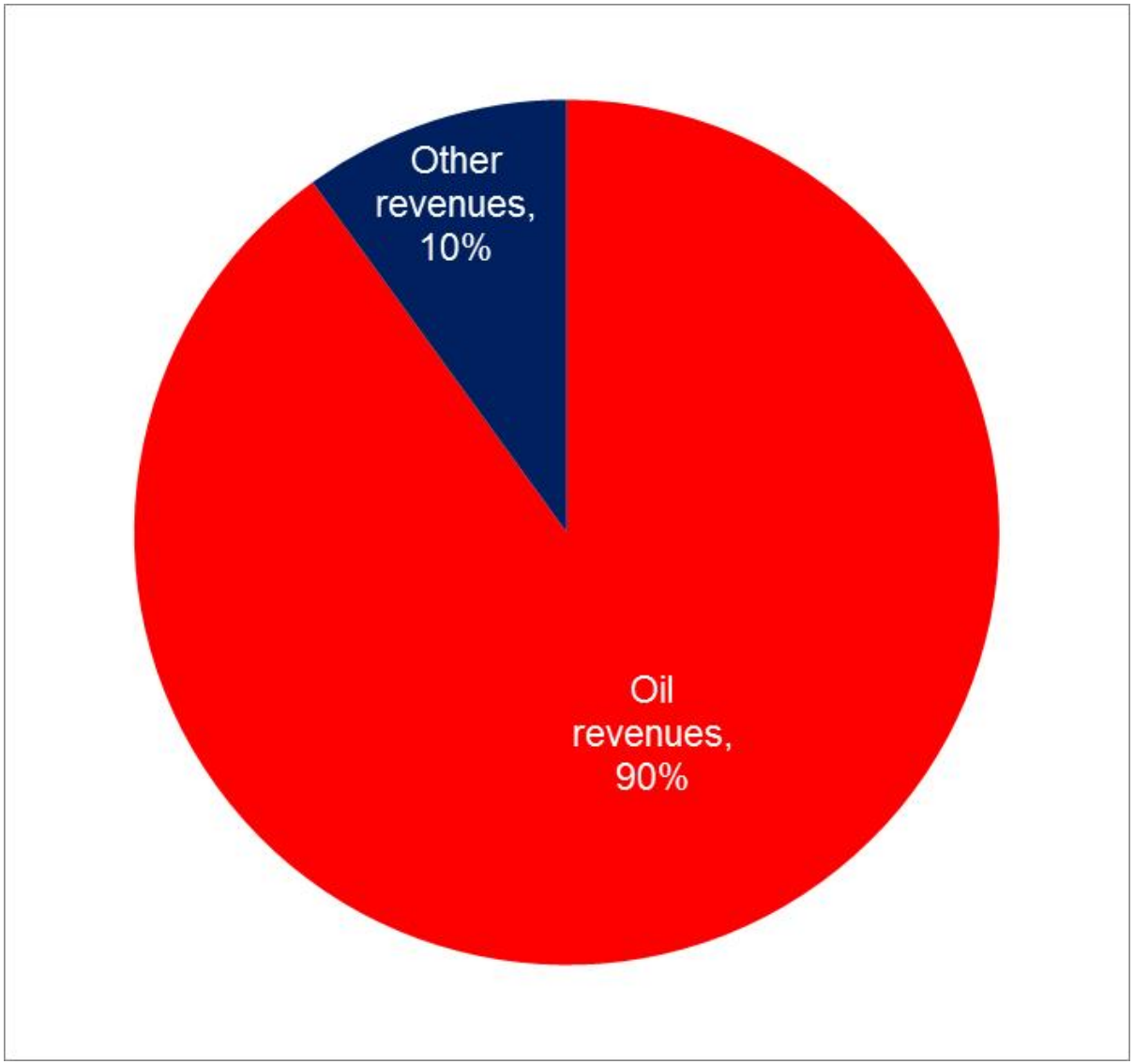
This presentation summarizes some of the most important things to understand about our fiscal situation.

This is a short introduction to a complicated topic.
I've focused on the "big picture."
I've used some simplified terms,
and I've left out many important details.

At the end of the presentation I've listed the sources for the data shown in the presentation.

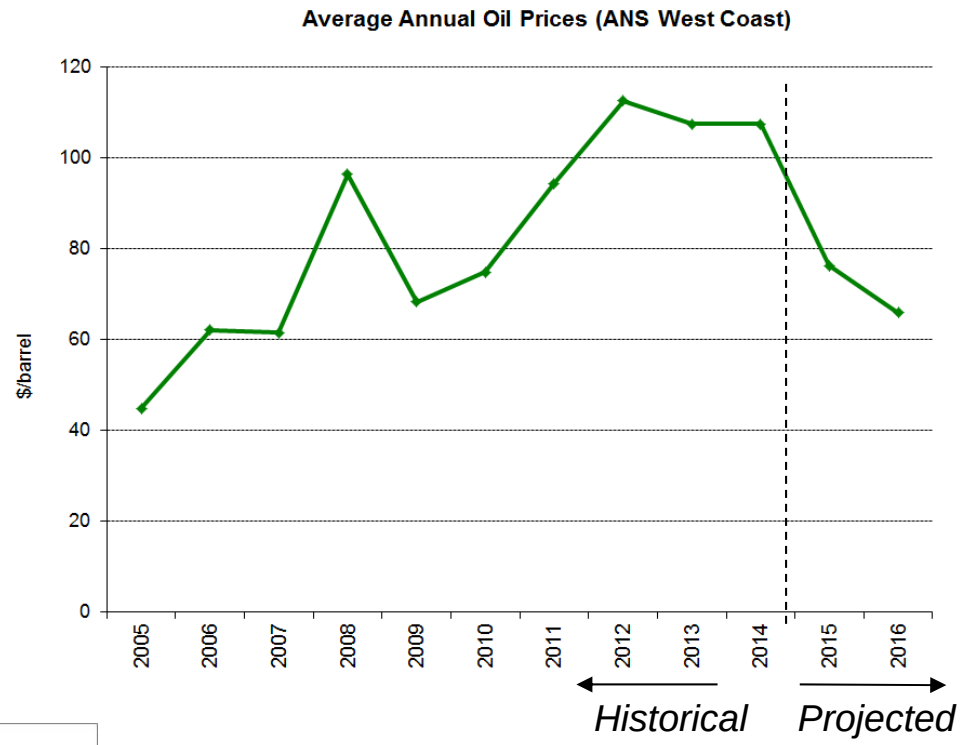
1. Alaska is extremely dependent on oil revenues to fund state government.

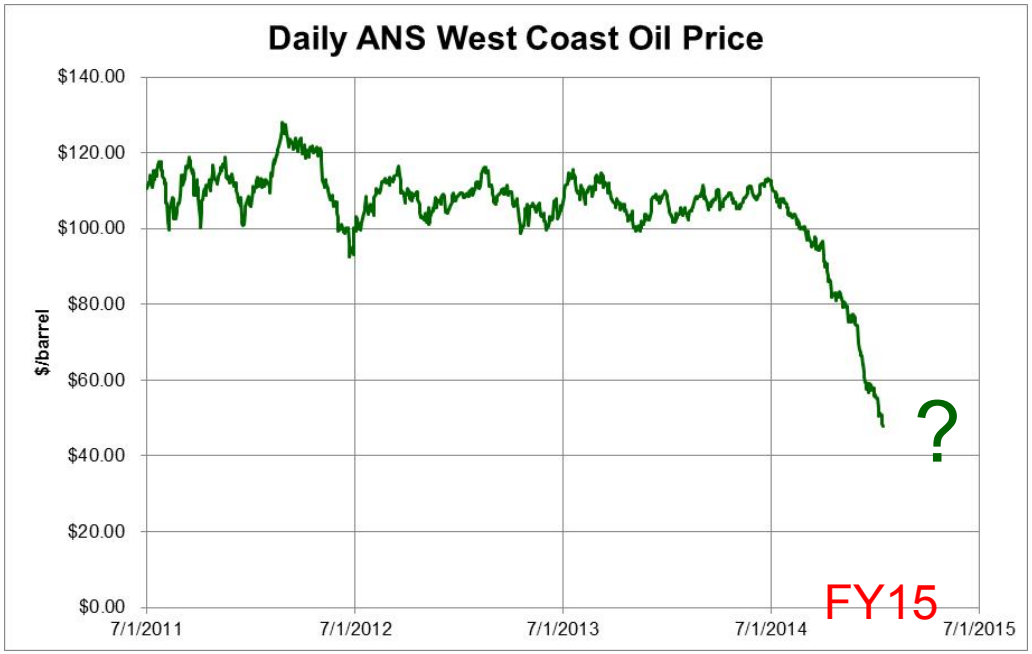
From 2005 to 2014, oil revenues averaged 90% of Alaska's unrestricted general fund revenues



2. After rising dramatically for many years, over the past three years oil prices and oil revenues have fallen drastically.

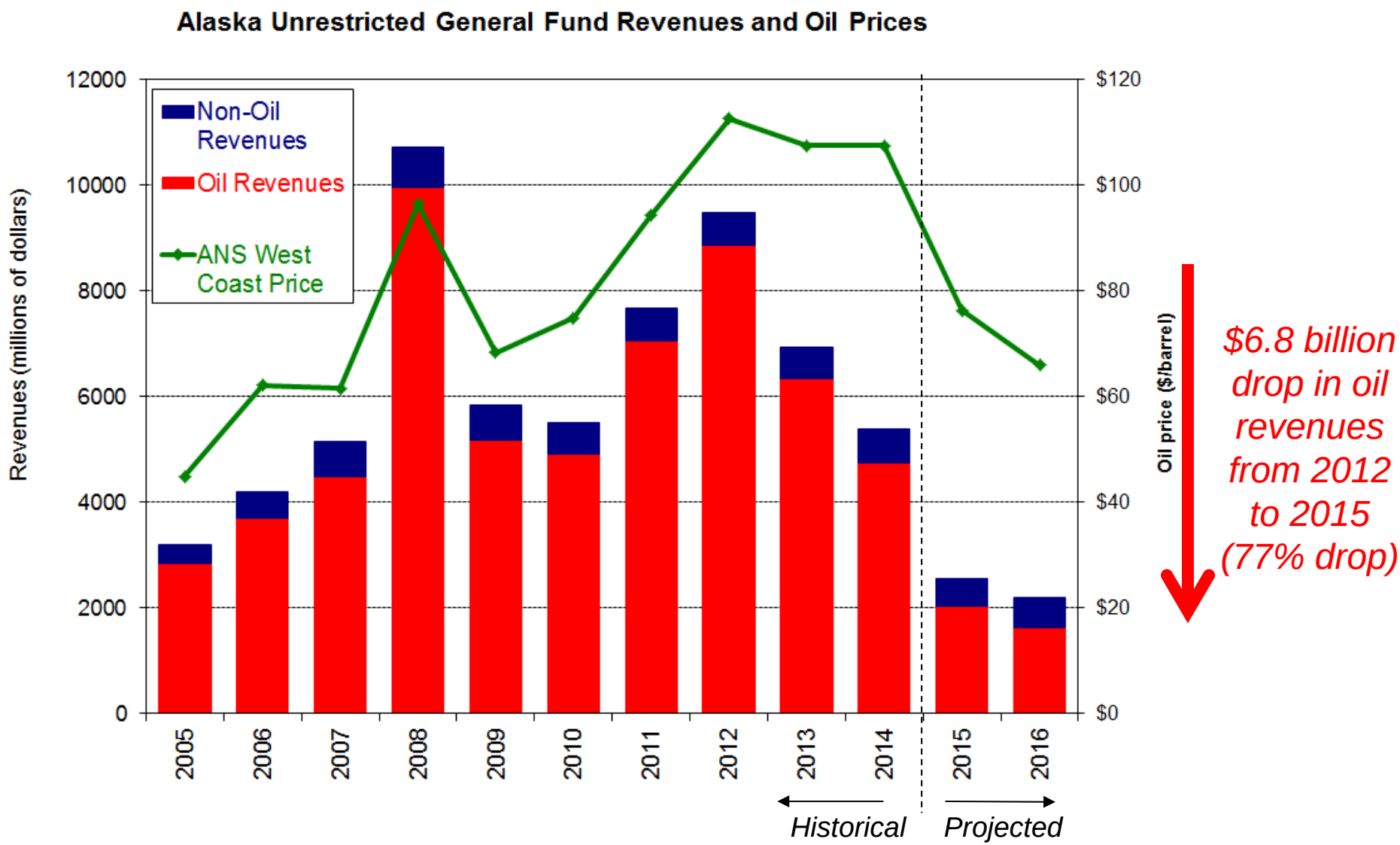
Average <u>annual</u> prices since 2005. . .





<u>Daily</u> prices since 2011. . .

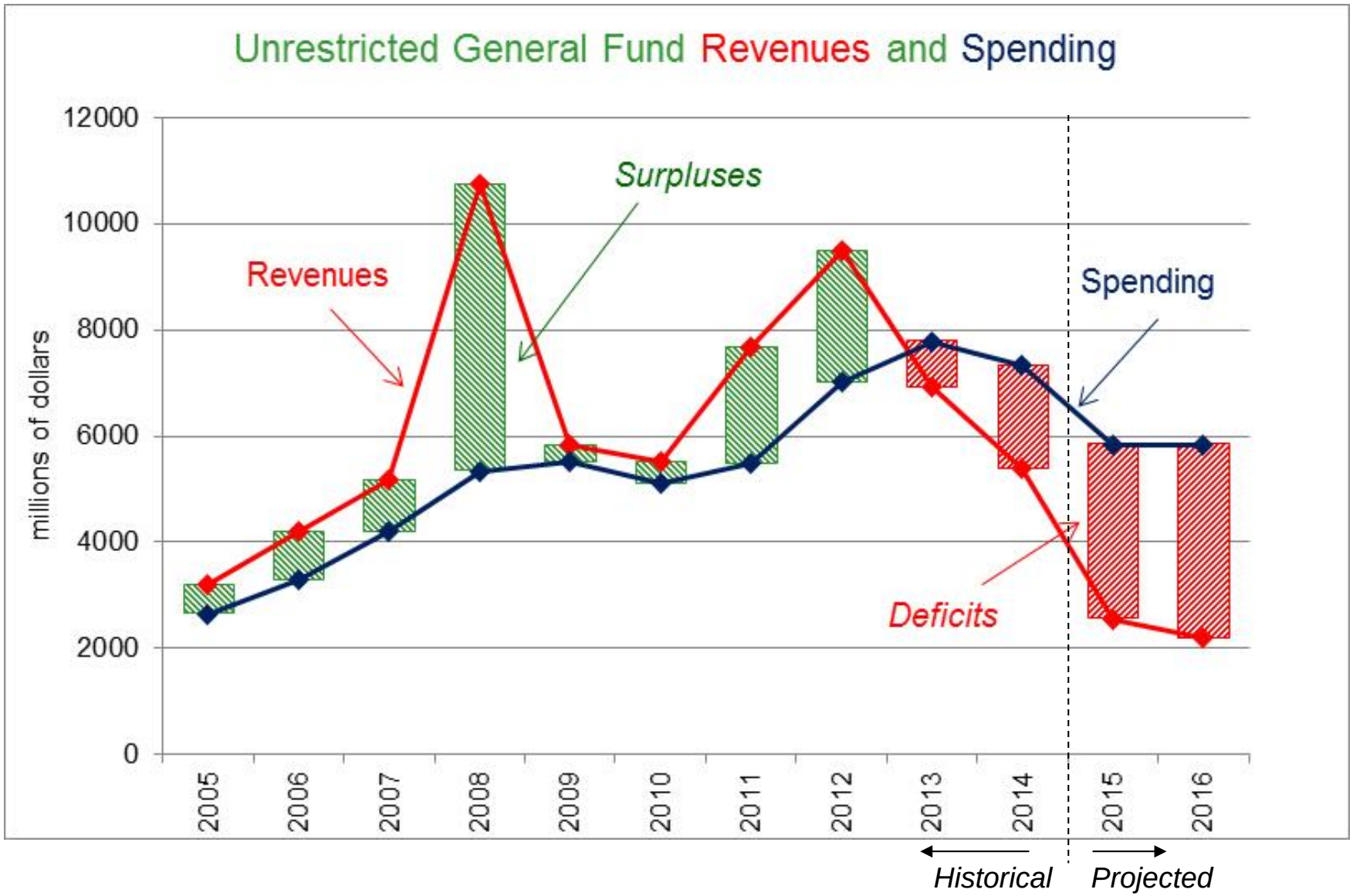
As oil prices have fallen, oil revenues have fallen drastically.



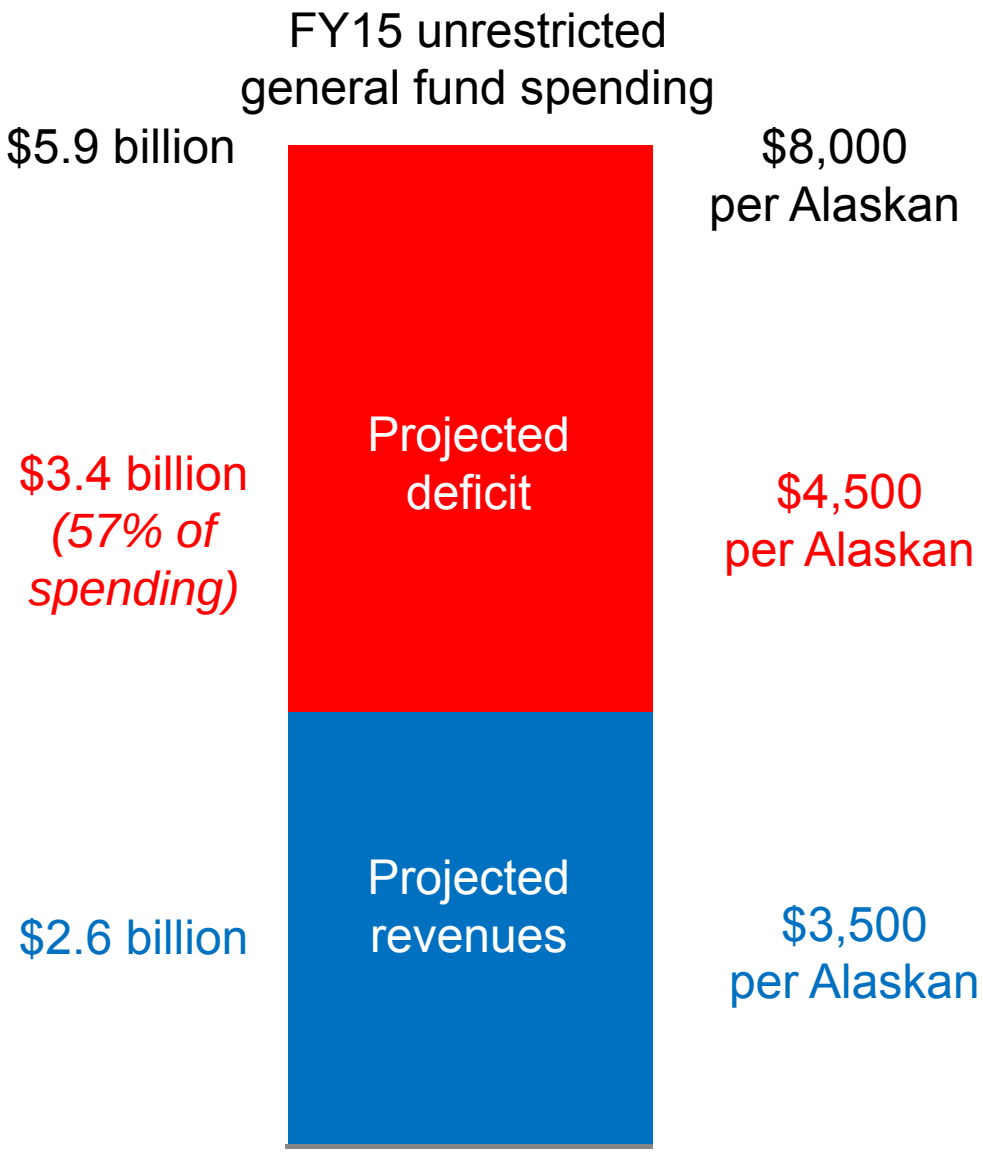
3. Spending has also fallen since 2013
—but not as fast as revenues.

We have gone from
large surpluses to large deficits.

We ran big **surpluses** from 2005 to 2012.
Since 2013 we have been running big **deficits**.

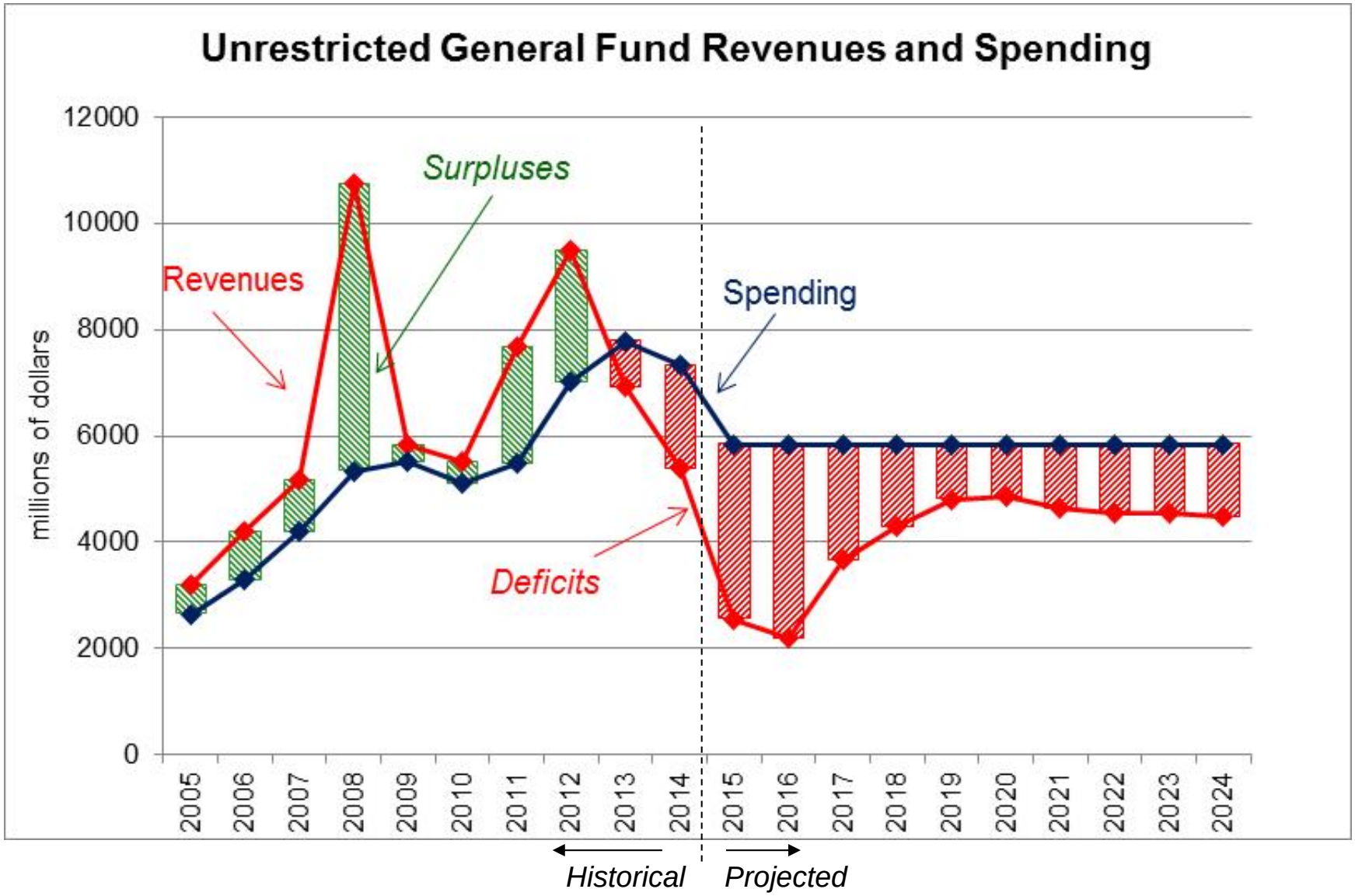


This year's projected deficit is huge.



4. At current spending and projected revenues, we would continue to run large deficits.

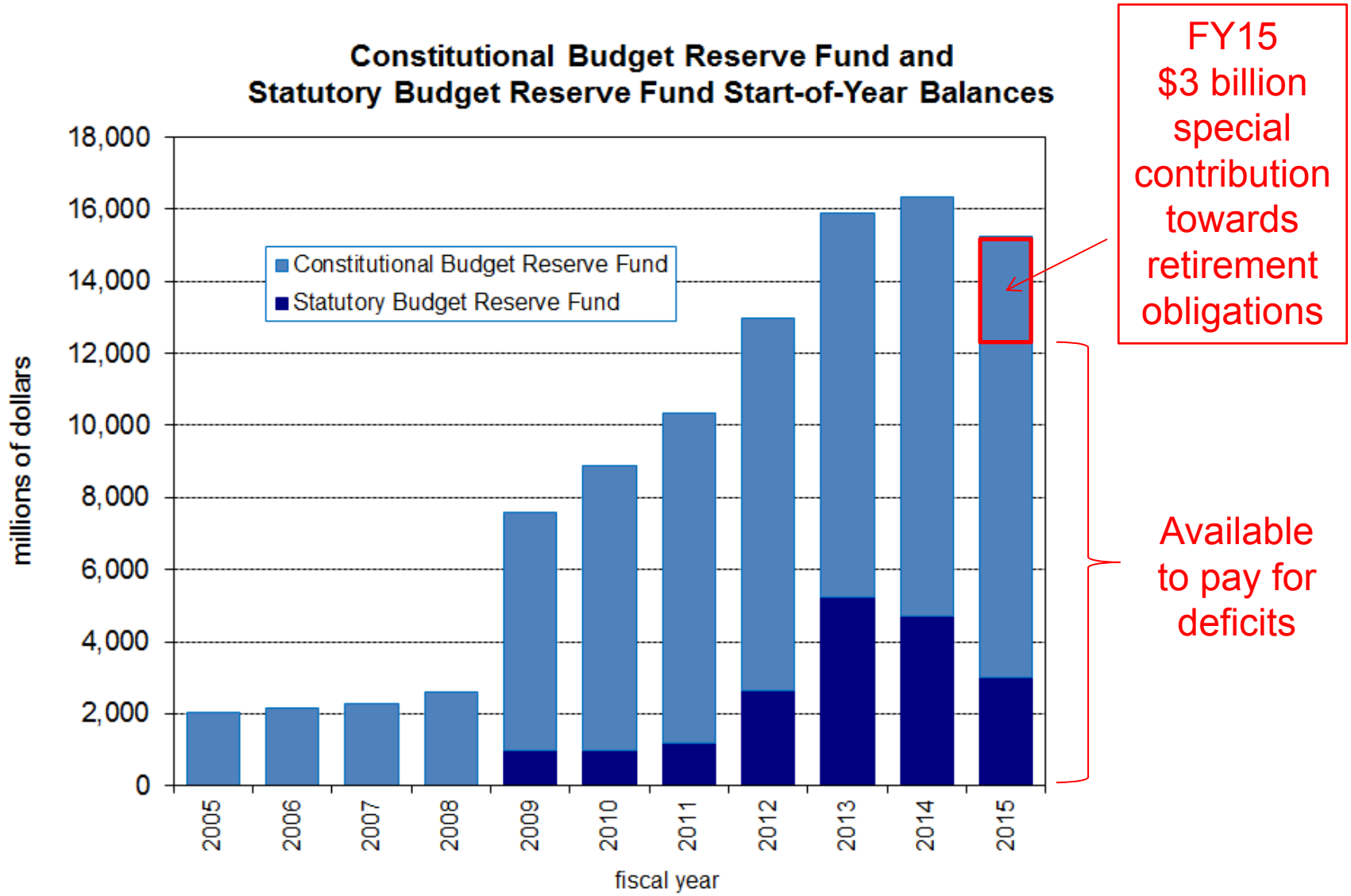
Even though revenues are projected to rise beginning in 2017, at current spending deficits would remain very large.



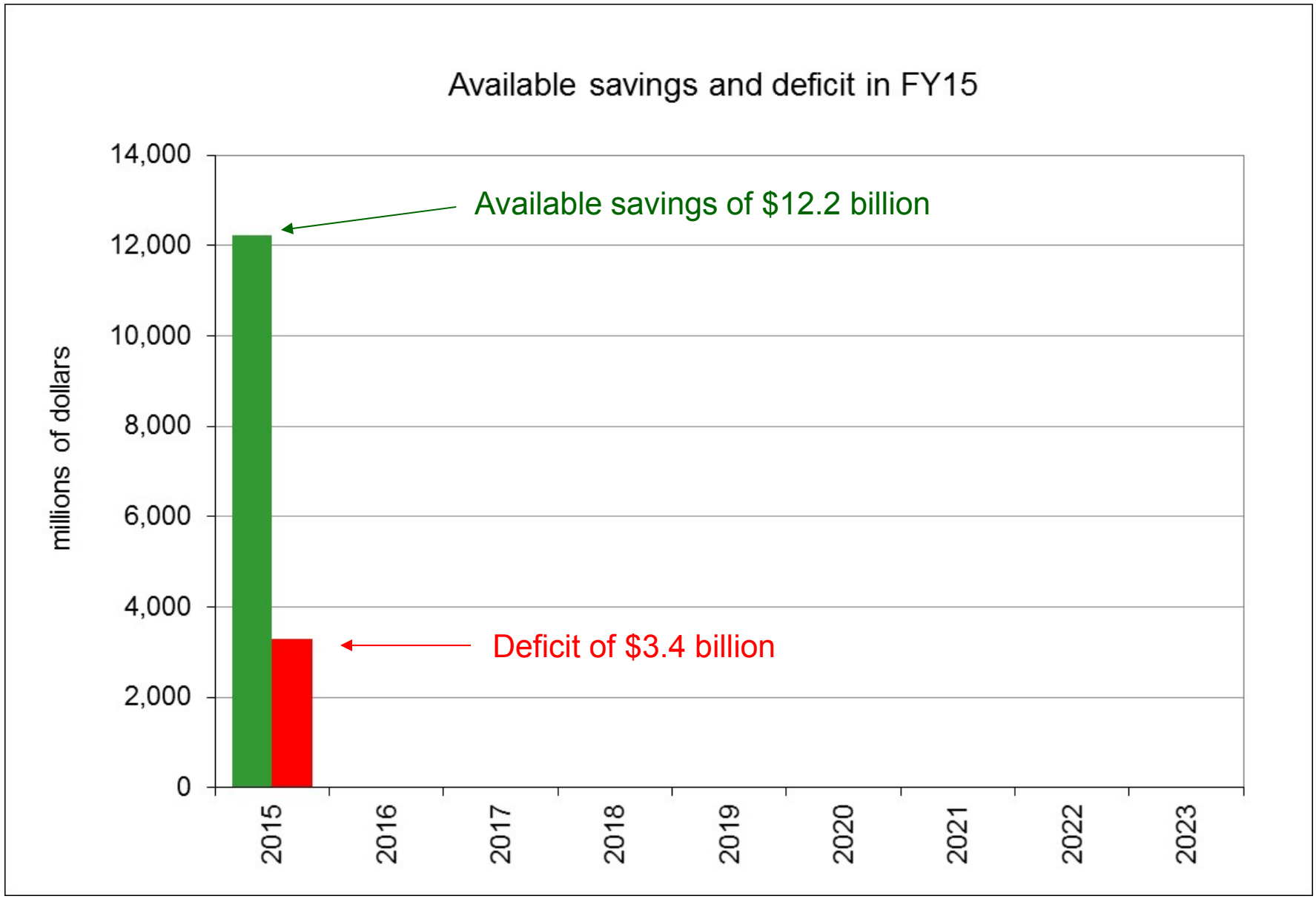
5. When we were running surpluses we built up big savings which are now paying for deficits.

At current spending and projected revenues, projected deficits would drain our savings in about seven years.

We used the surpluses between 2005 and 2012 to build up our savings in two reserve funds.

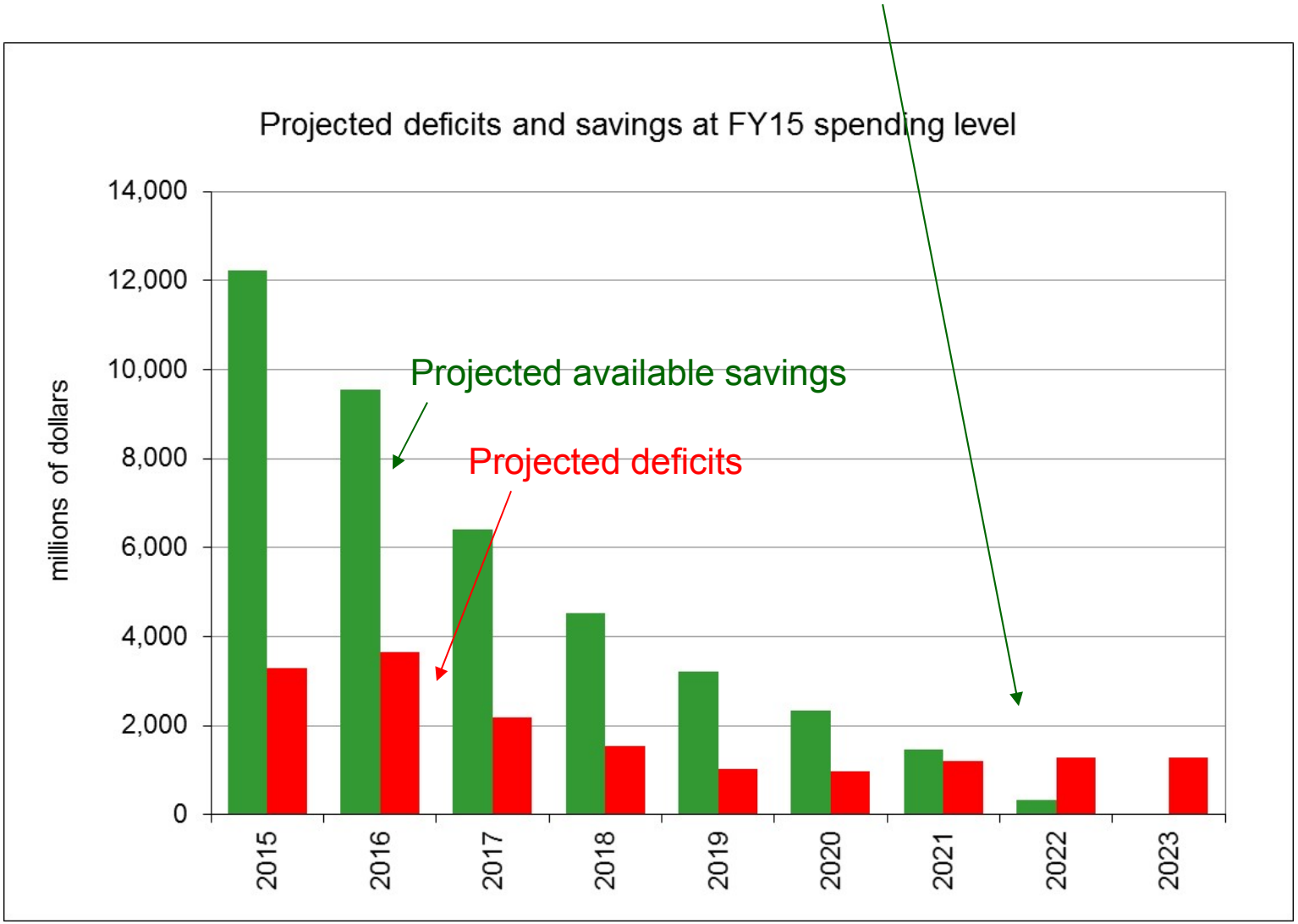


At the start of FY15, we had $12.2 billion in savings available to pay for deficits.



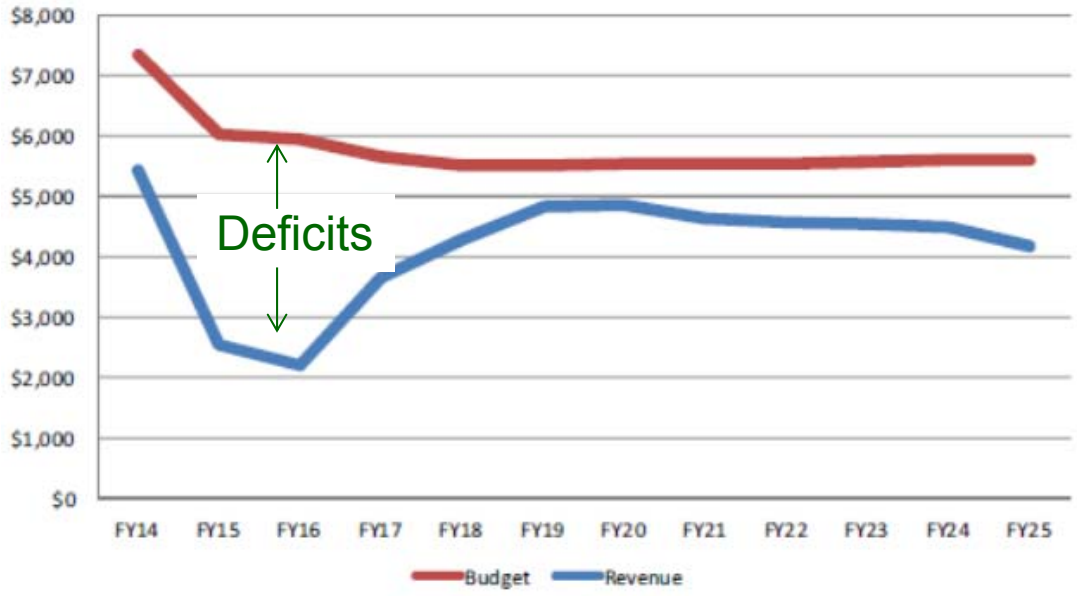
My estimates. . .

At this year's spending level and projected future revenues, we would drain our savings in 7 years



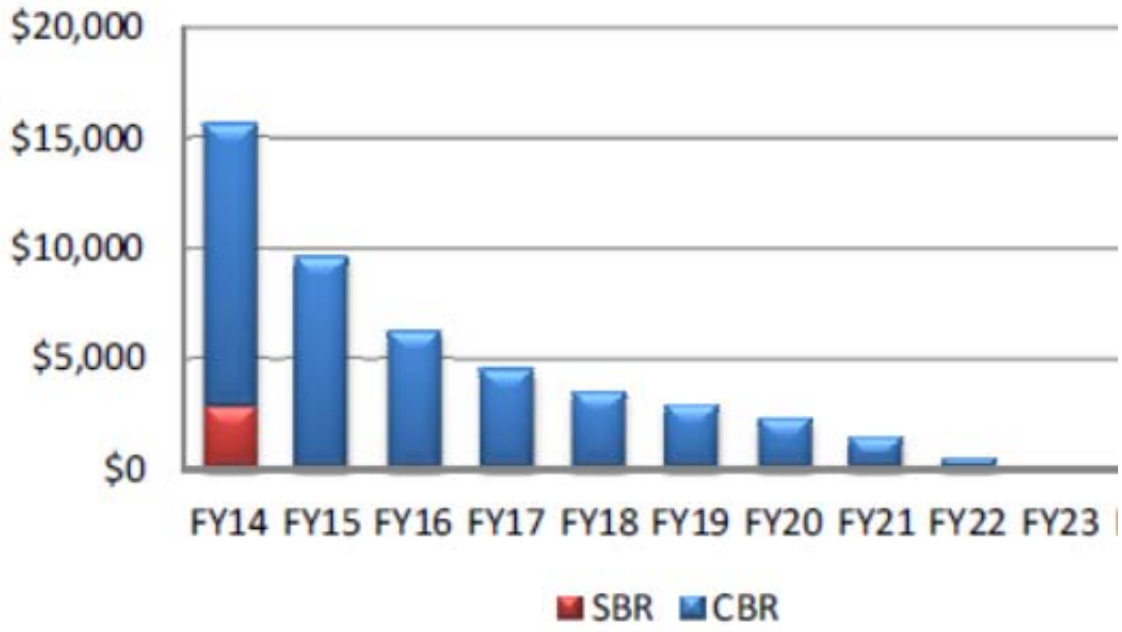
Legislative Finance Division estimates, January 19, 2015

Budget, revenues & deficits



Projections if we continue spending at current levels

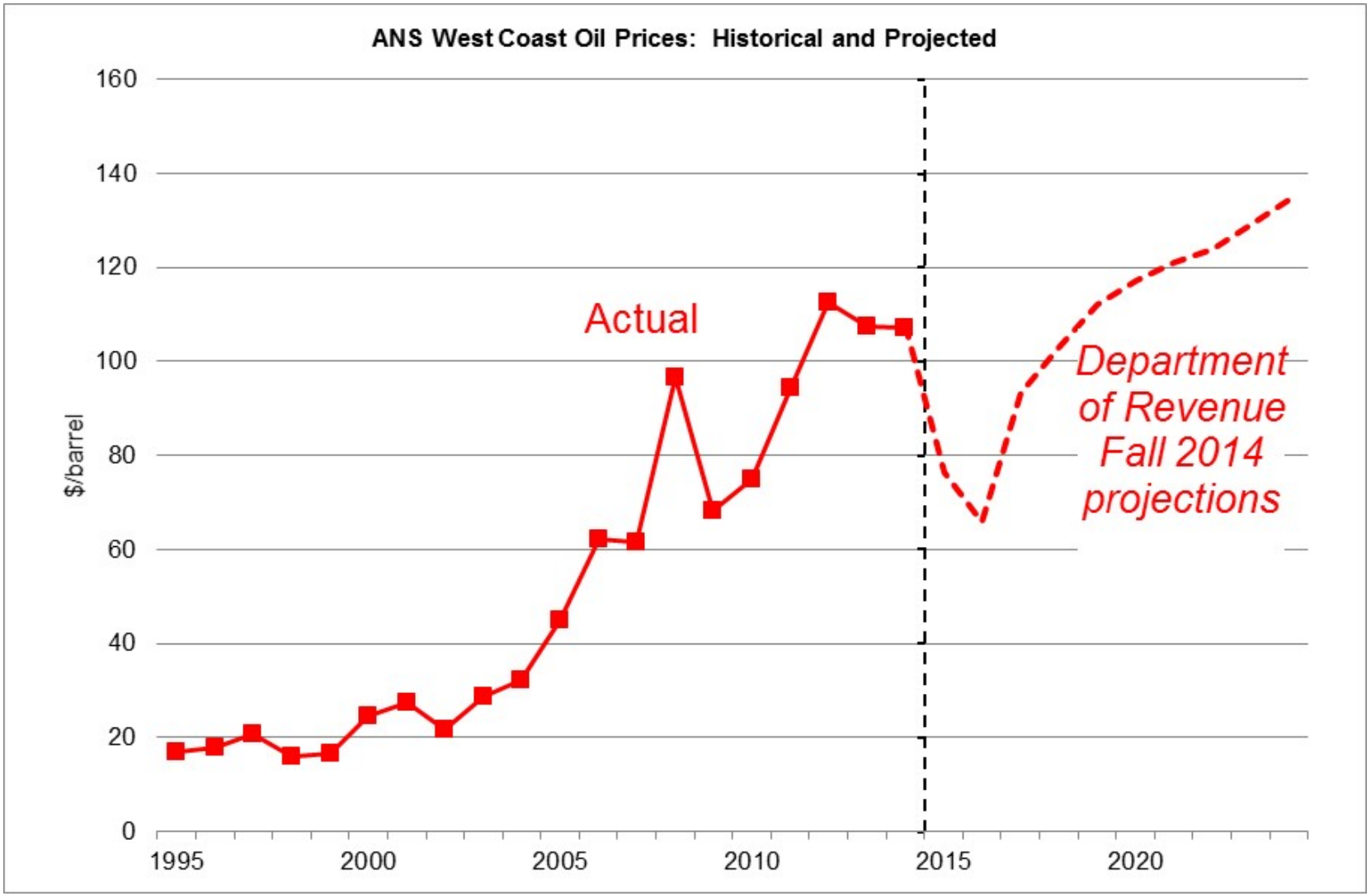
End-of-year savings



6. Future oil prices are highly uncertain.

They might be significantly lower than the Department of Revenue assumed for their revenue projections.

The revenue projections assume oil prices will rebound after 2016



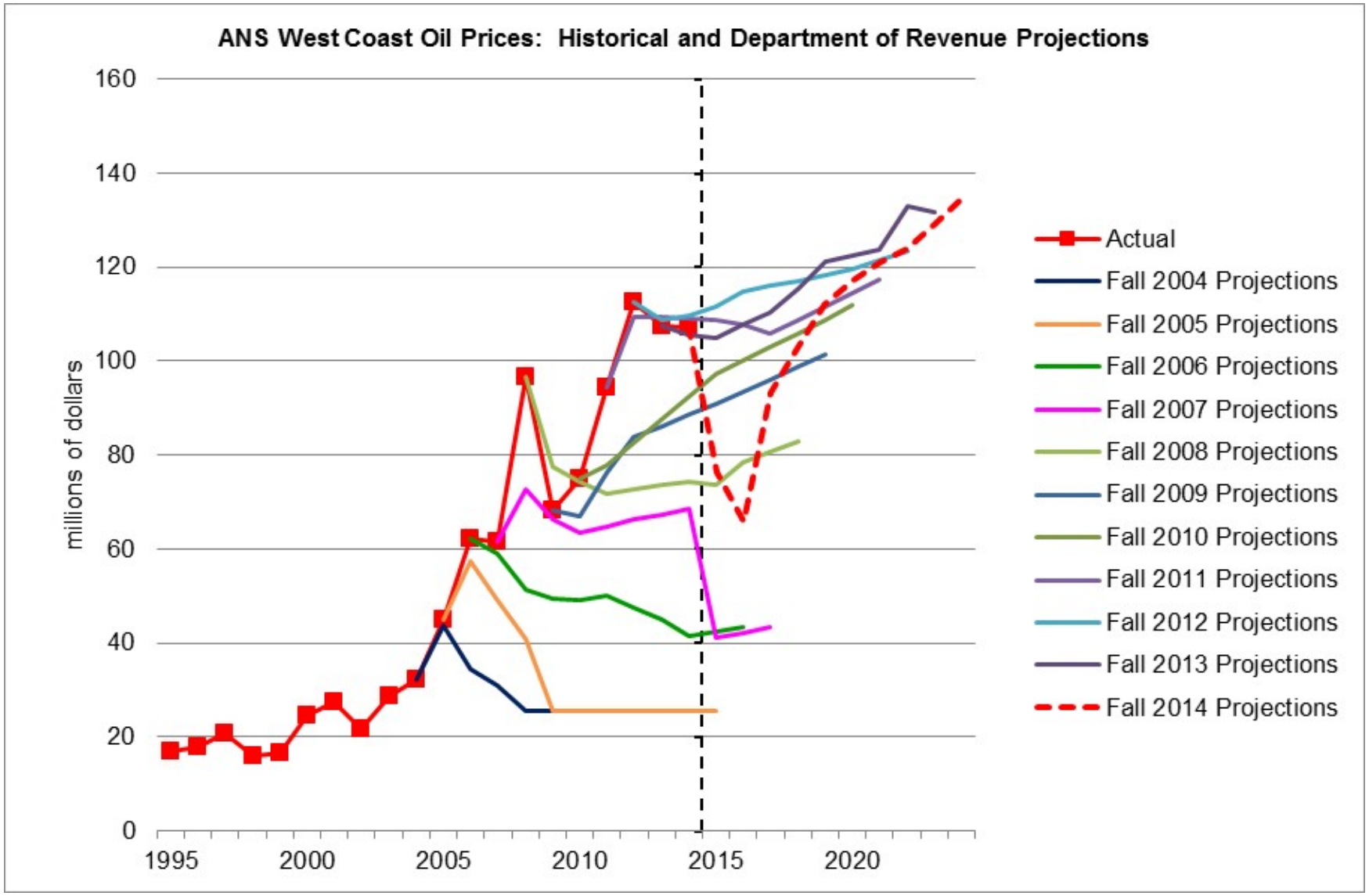
Most “experts” think:

- Prices fell because world oil production exceeded demand
- Falling prices will reduce production
- When production equals demand prices will stop falling
- Prices will rise again as demand grows

BUT

- So far production hasn’t fallen much
- Slowing economic growth is reducing demand
- Future price growth may be limited by rebounding production

What will actually happen to oil prices is highly uncertain.
We can't assume that the Department of Revenue projections will be correct.

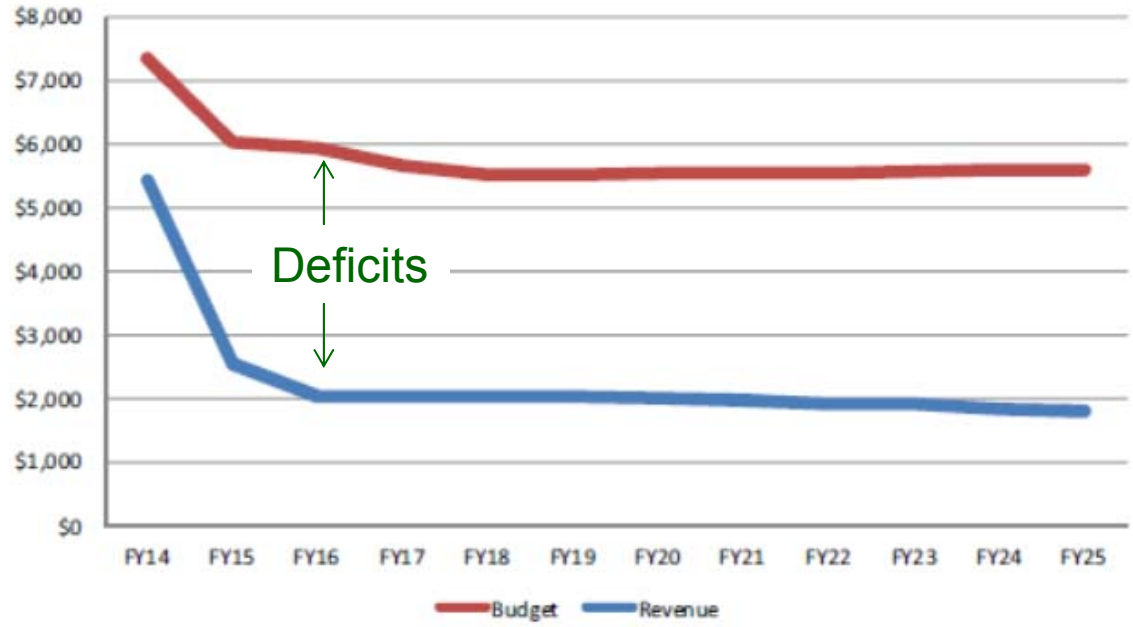


7. How long our savings might last depends critically on oil prices.

If oil prices are lower than projected, we could drain our savings much sooner.

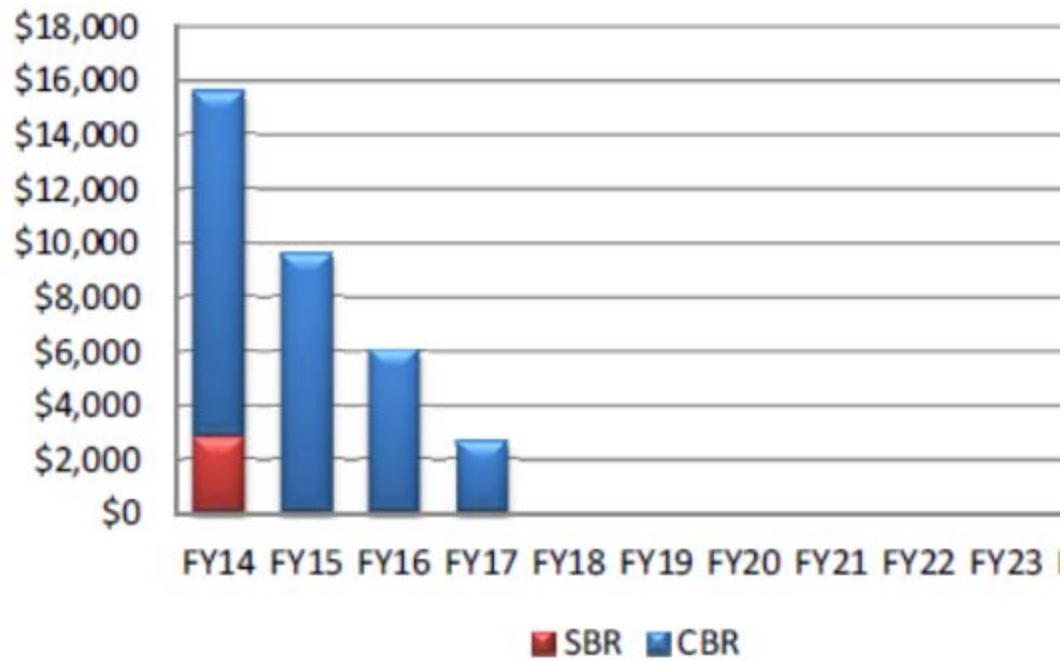
Legislative Finance Division estimates, January 19, 2015

Budget, revenues & deficits



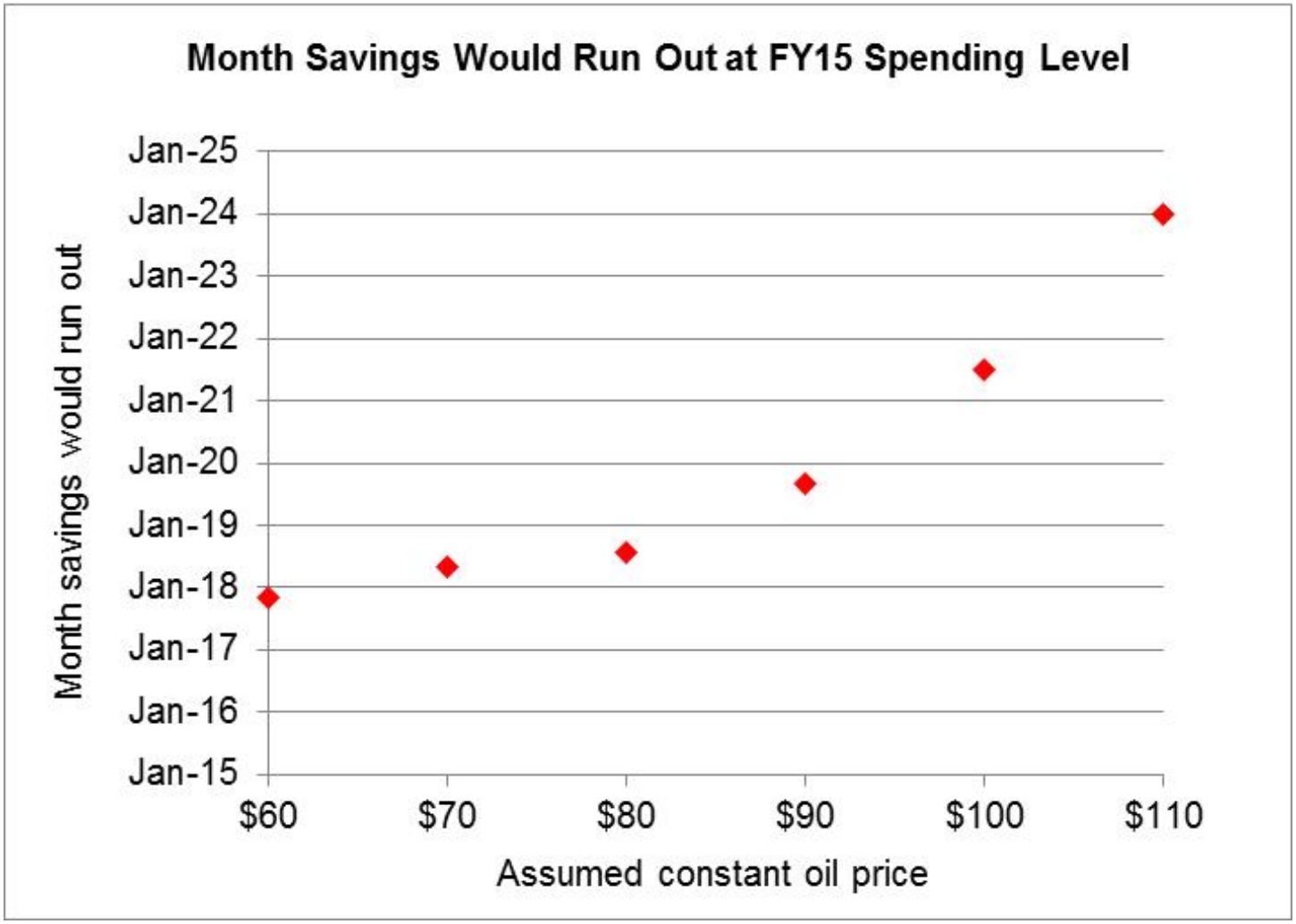
Projections if oil prices average $60/barrel

End-of-year savings



Department of Revenue estimates,
Fall 2014 Revenue Sources Book

Projected month in which savings would run out under different constant oil price assumptions



Source: Department of Revenue Fall Revenue Sources Book, page 61

8. We can’t run deficits without savings to pay for them.

Unless oil prices rise dramatically
within a few years we will <u>have</u> to make
big changes to our spending or revenues.

9. Unless oil prices rise dramatically, we face two big choices:

How to adjust?

- Spend less?

- Find new revenues?

- Both?

When to adjust?

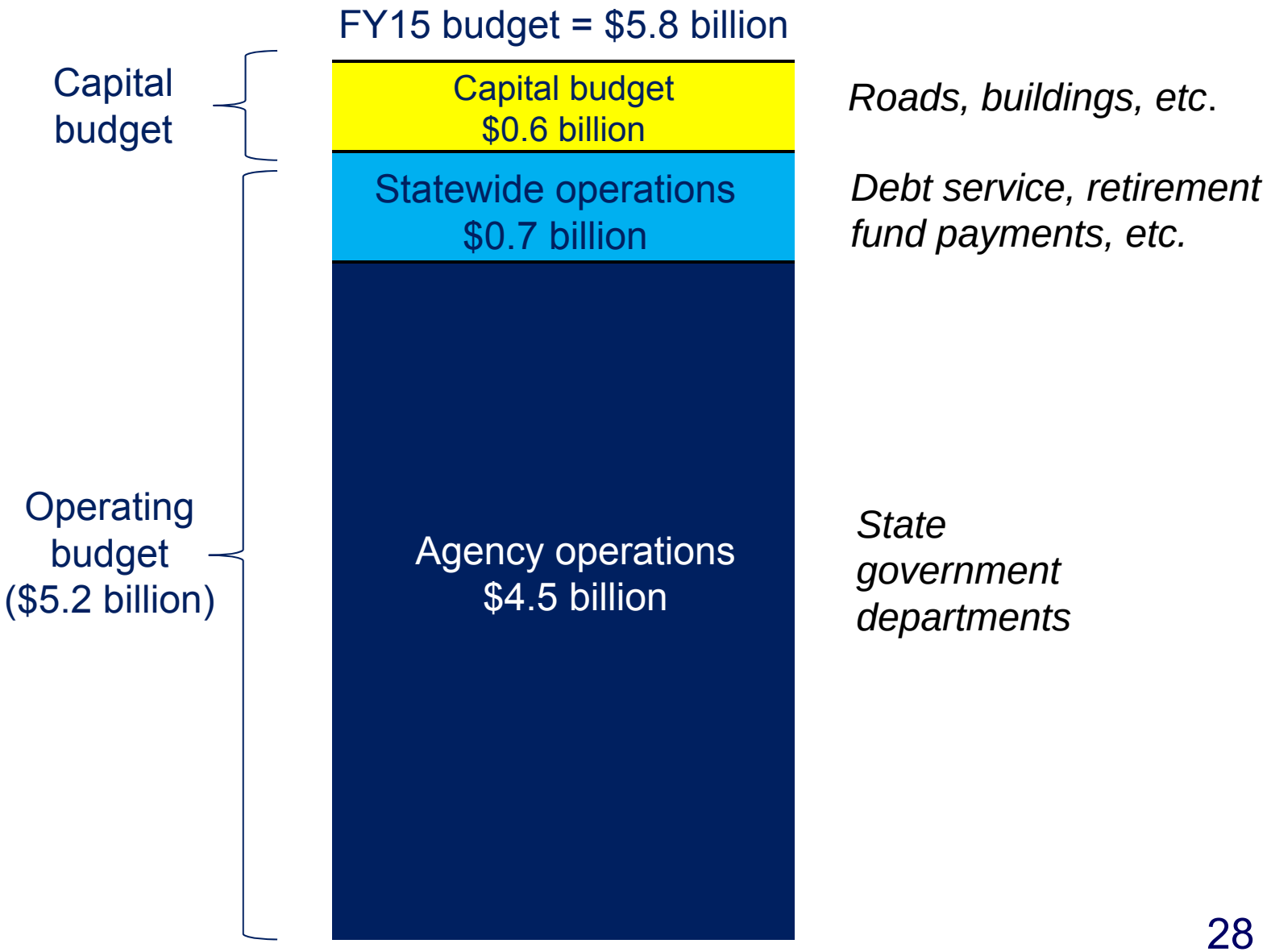
- Now?

- Gradually?

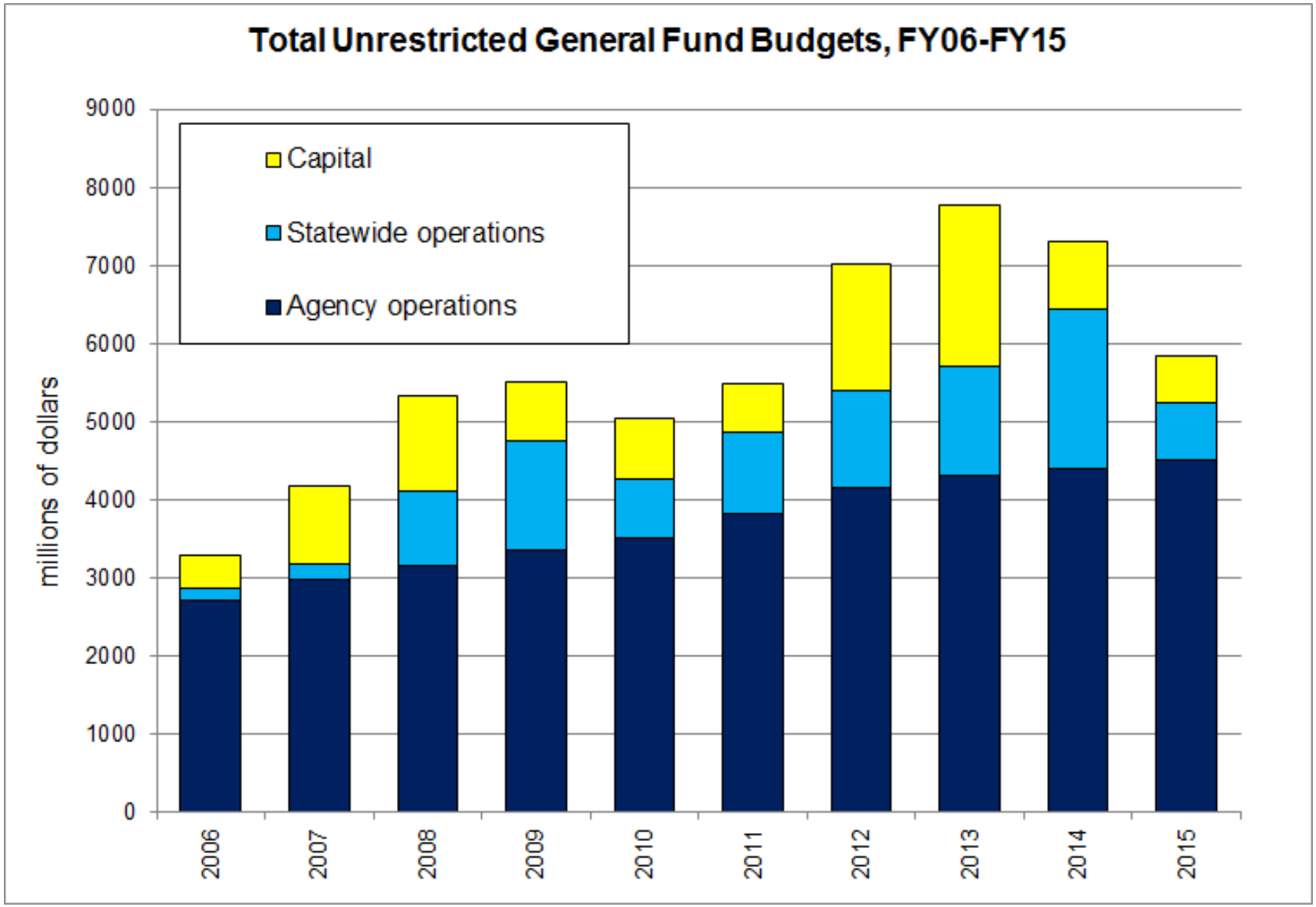
- When our savings run out?

10. It is not obvious how to cut spending enough to make up for the deficits we face.

Most of the state budget is in agency operations.

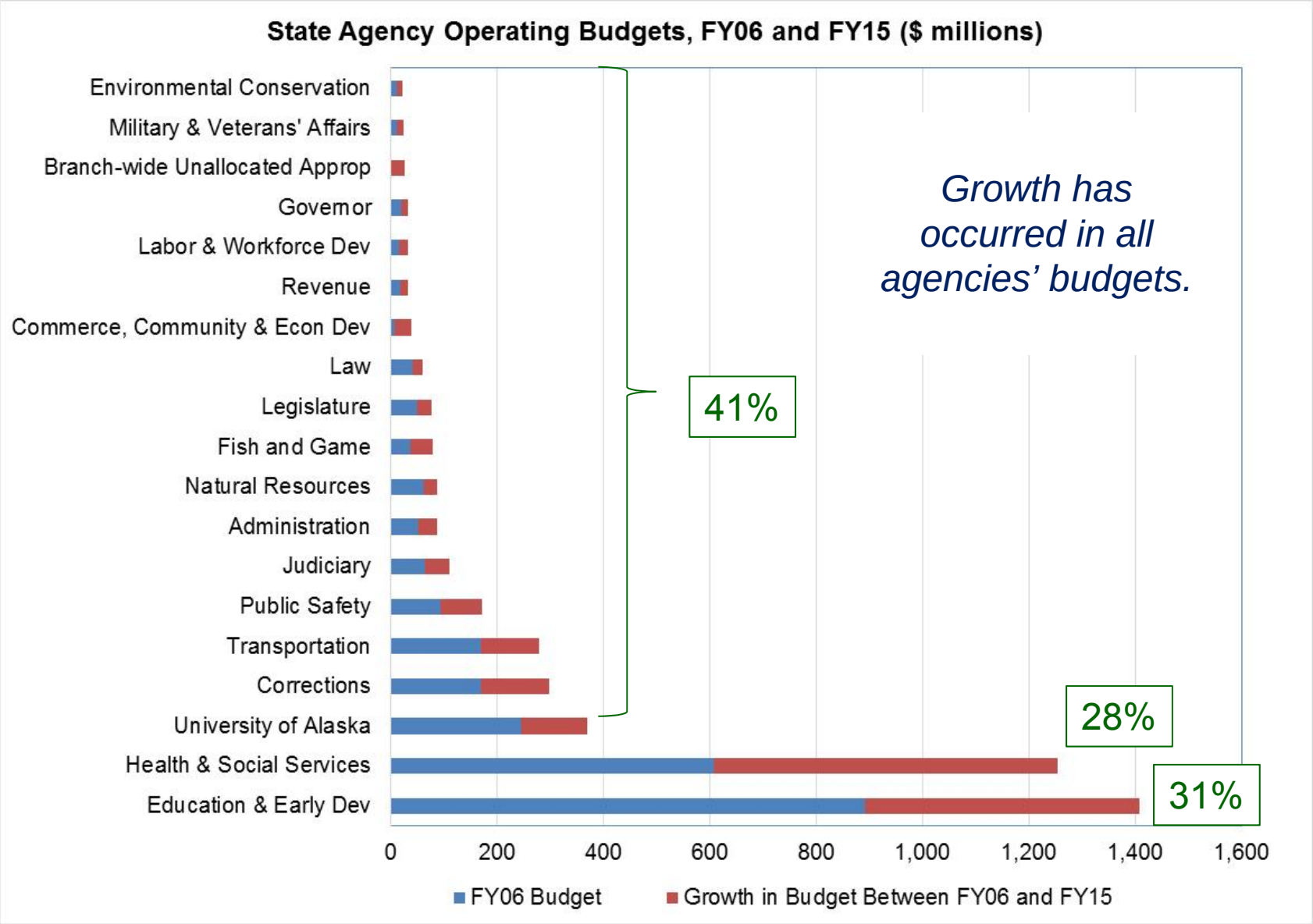


We have reduced the capital and agency operations budgets —but the agency operations budget has kept growing.



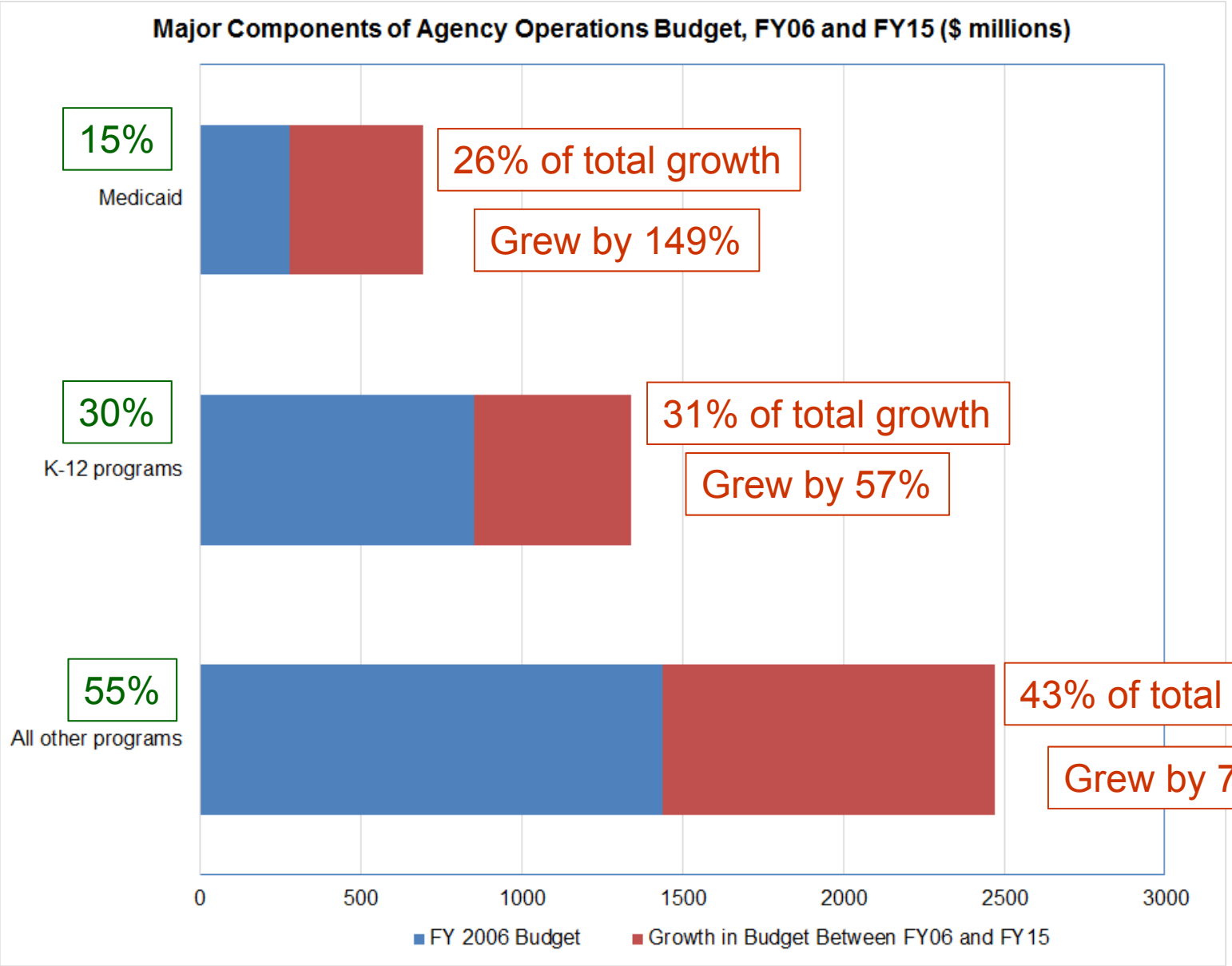
Source: Legislative Finance Division

Education and Early Development & Health and Social Services account for 59% of the FY15 agency operations budget



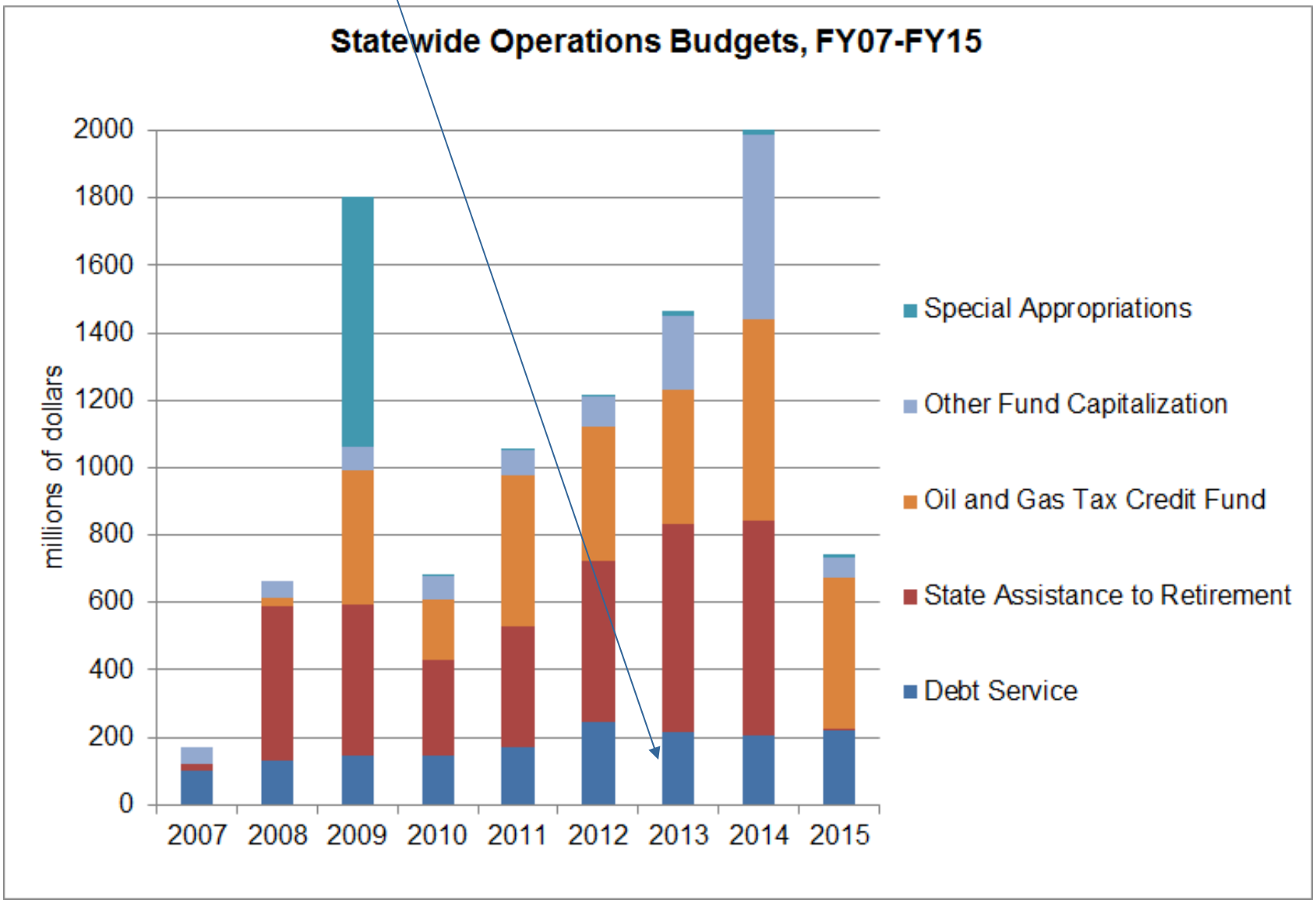
Source: Legislative Finance Division

K-12 and Medicaid Programs account for 45% of the FY15 Agency Operations budget



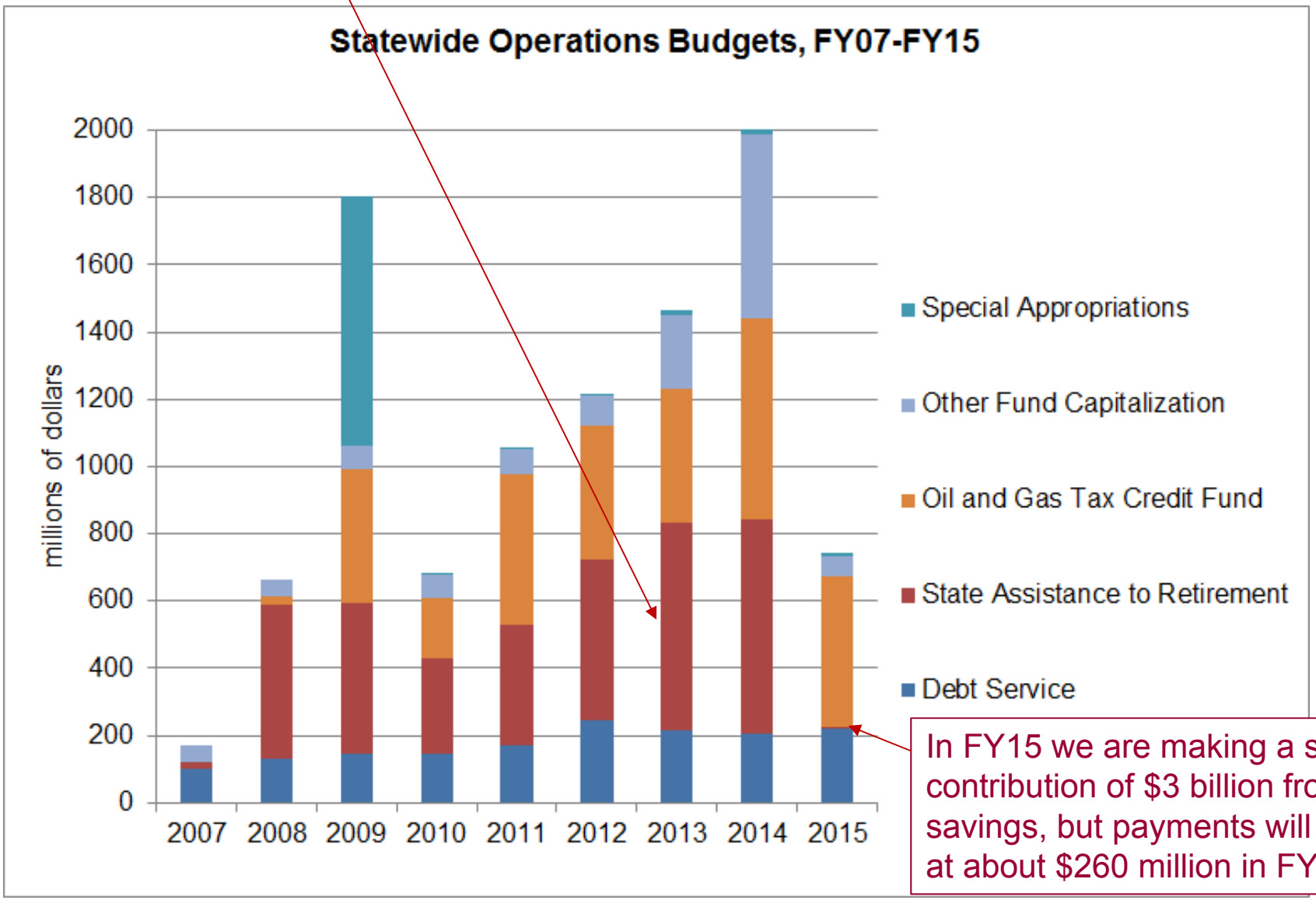
Source: Legislative Finance Division

Debt service obligations can't be cut.



Source: Legislative Finance Division

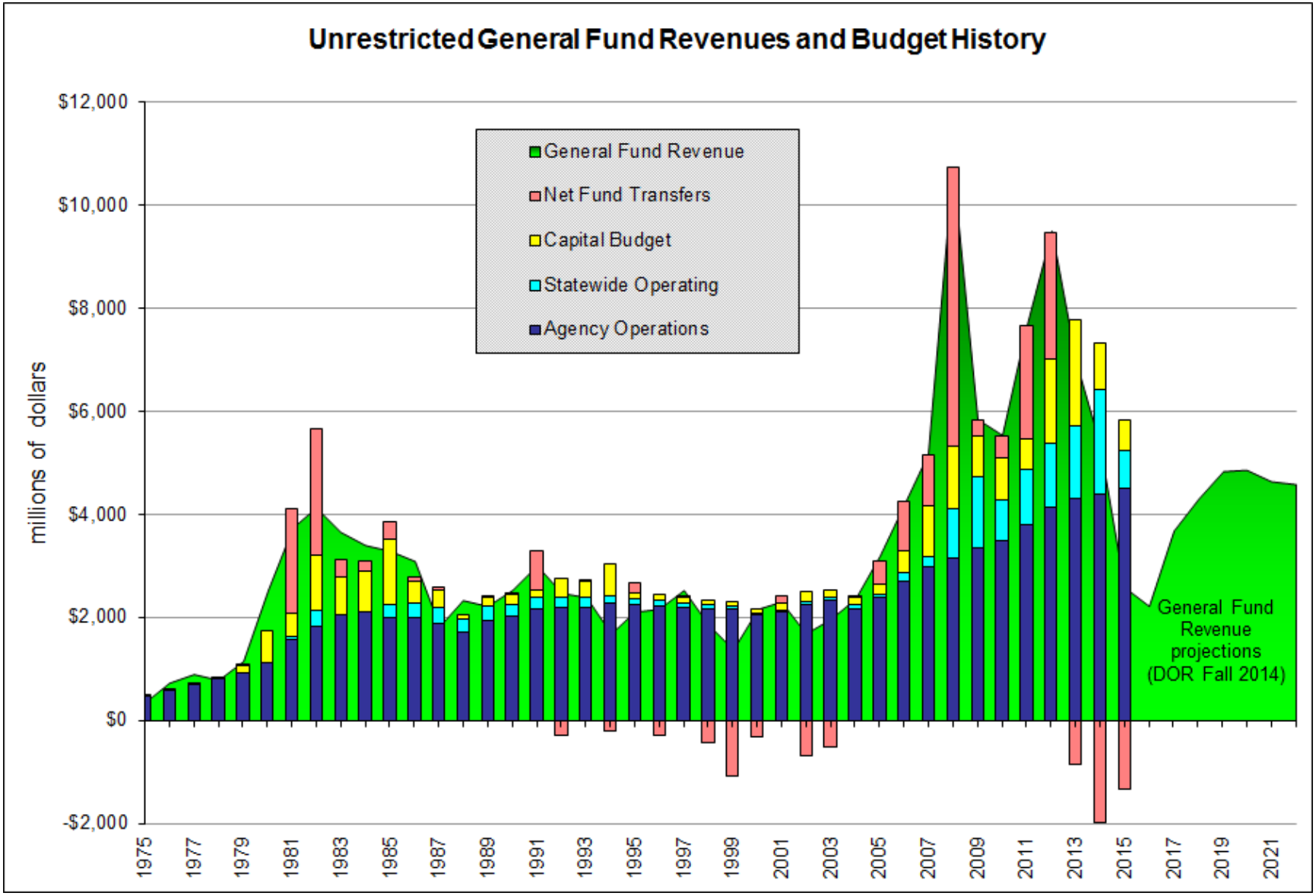
State assistance to retirement would be difficult to cut.



In FY15 we are making a special contribution of $3 billion from our savings, but payments will resume at about $260 million in FY16.

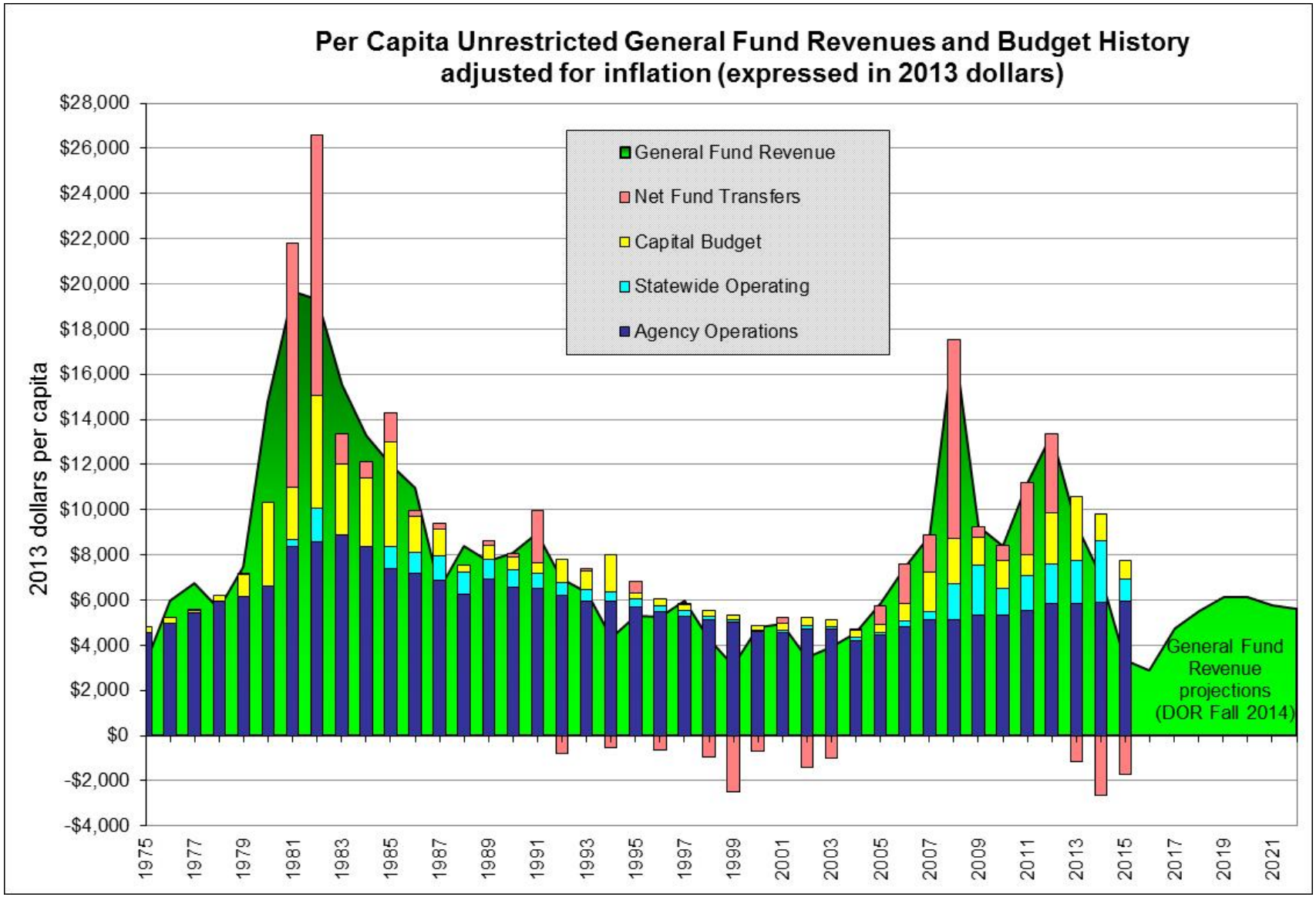
Source: Legislative Finance Division

From a long-term perspective, the growth in spending since 2005 looks dramatic, expressed in total dollars.



Source: Legislative Finance Division

Adjusted for inflation, the growth in spending *per Alaskan* since 2005 seems less dramatic, particularly for agency operations.



Source: Legislative Finance Division

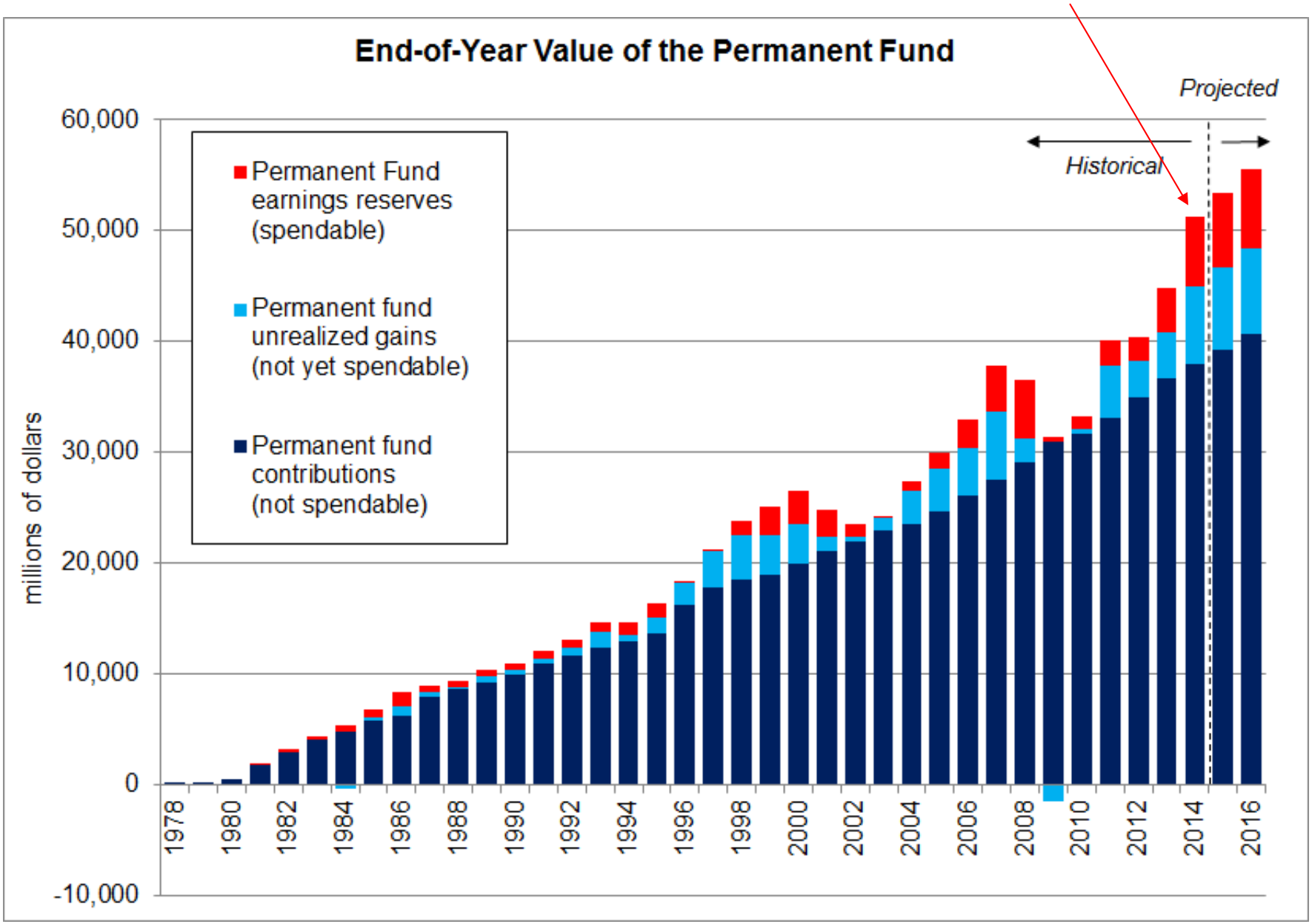
11. Many Alaskans think the Permanent Fund should be “off the table” in how we respond to our fiscal situation.

But:

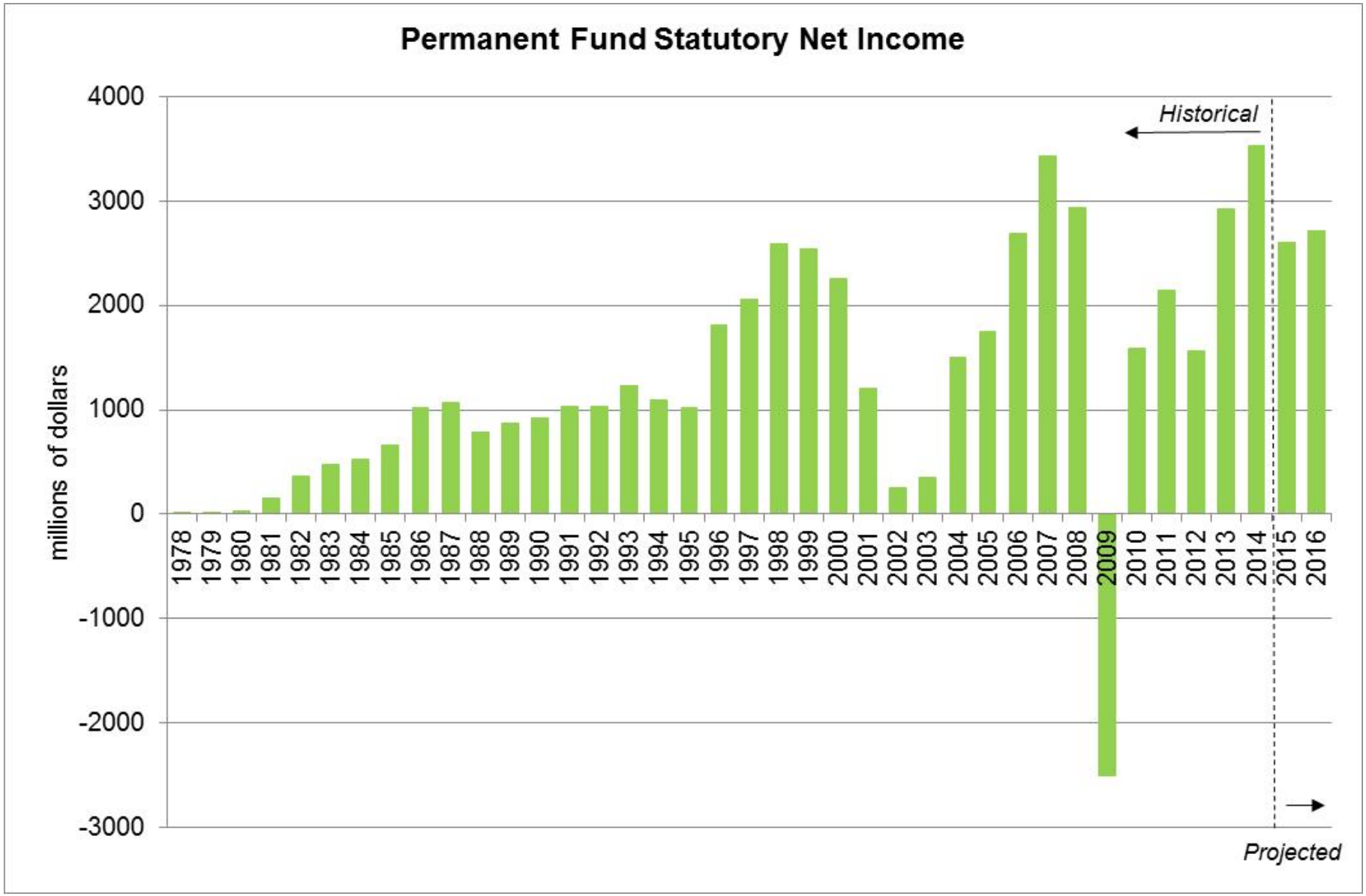
The Permanent Fund accounts for a growing share of state savings and revenues.

Permanent Fund dividends account for a growing share of state spending.

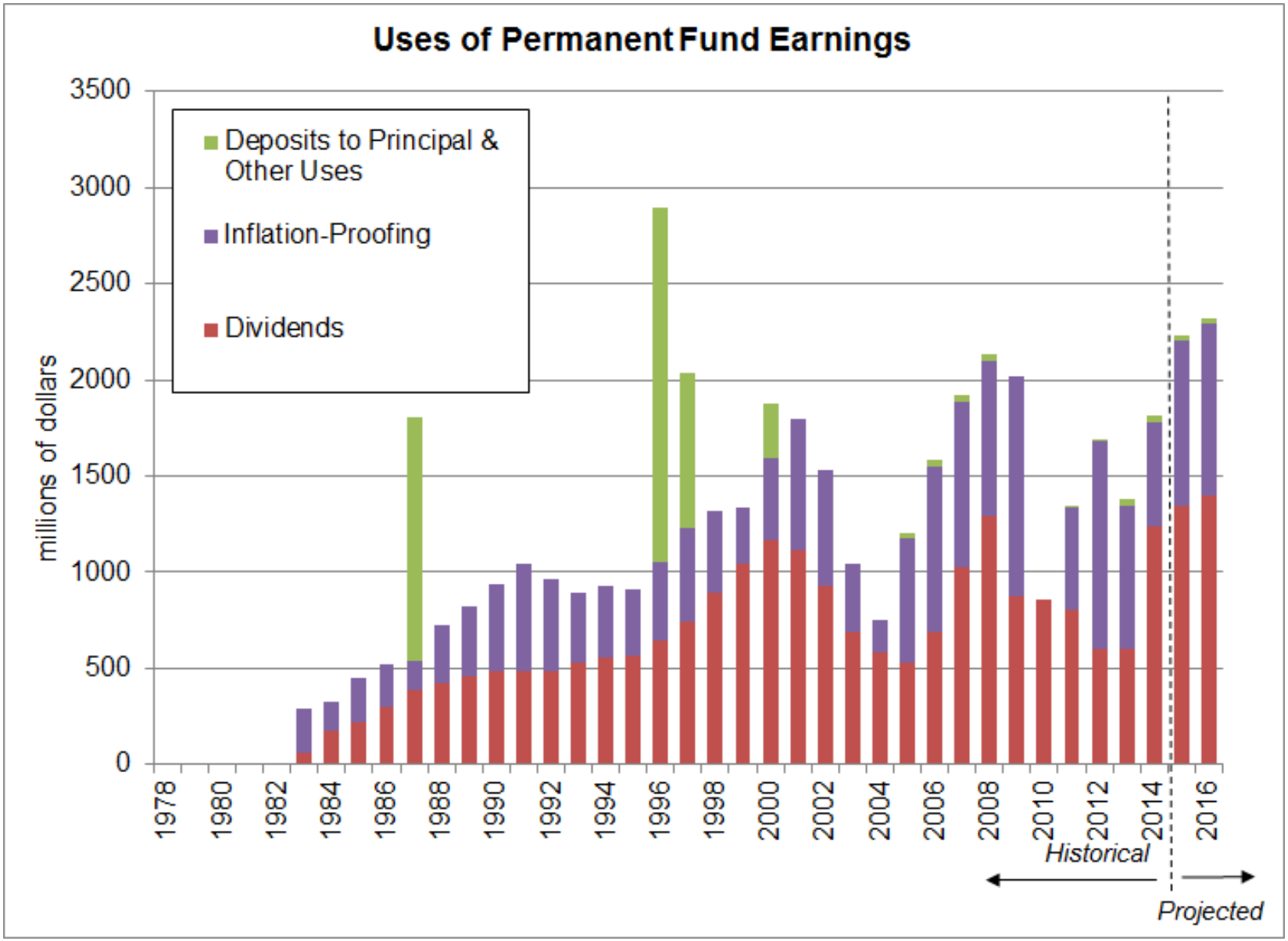
This Permanent Fund is worth more than $50 billion.
We can only spend the "realized earnings" in the "earnings reserve."



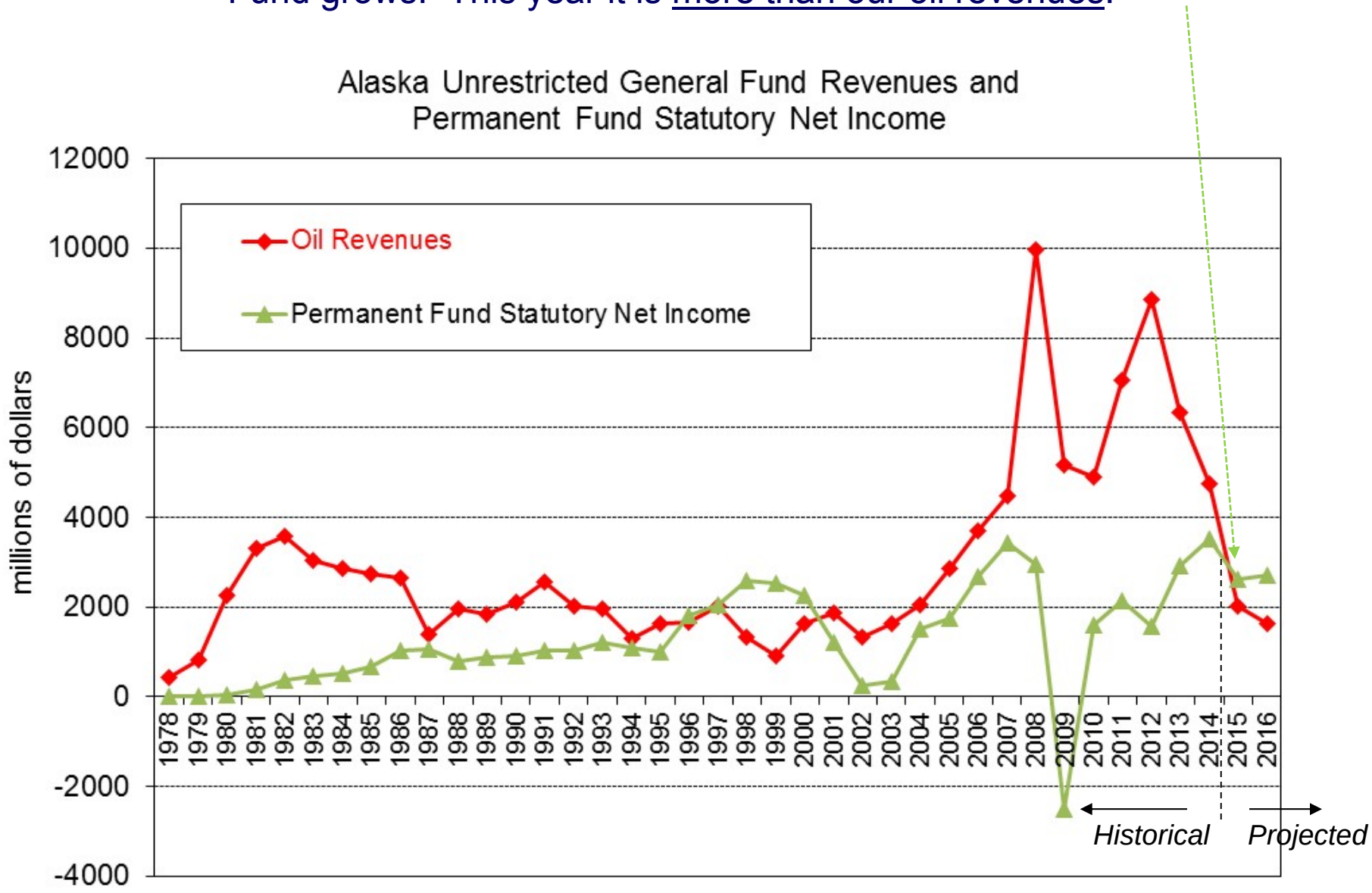
Each year the statutory net income of the Permanent Fund gets added to the earnings reserve.



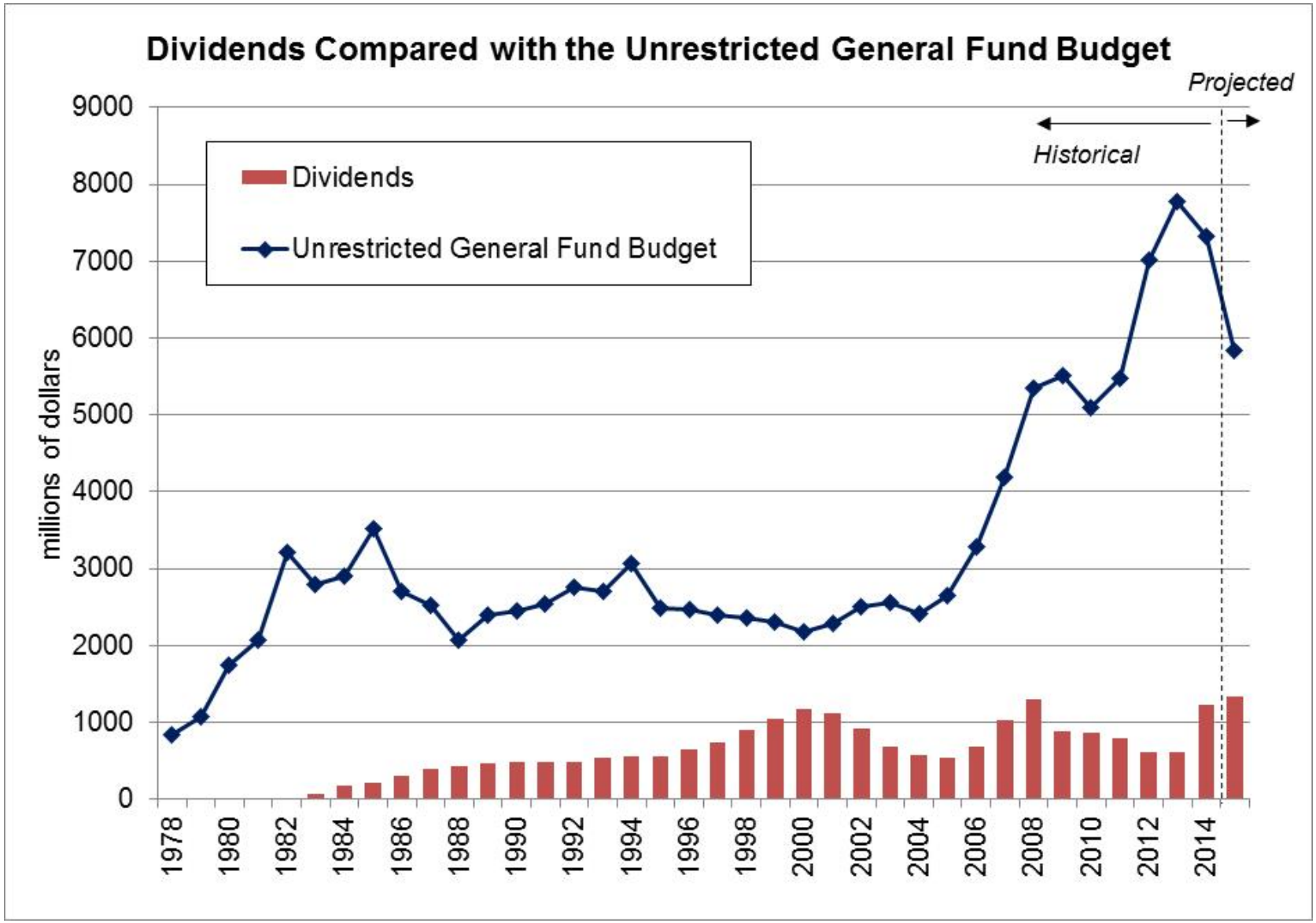
Each year we draw from the earnings reserve to pay for dividends and inflation proofing.



Permanent Fund statutory net income is highly variable but it has been growing as the Fund grows. This year it is more than our oil revenues.



Dividends are significant compared with other state spending.

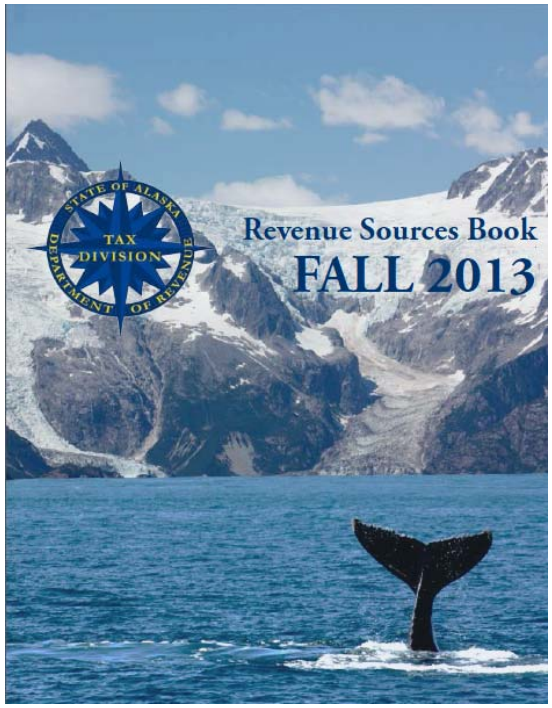


Overview of Data Sources for this Presentation

Data for historical and projected state revenues in this presentation are from Fall *Revenue Sources Books* prepared by the Alaska Department of Revenue's Tax Division. These clearly-written reports provide detailed information about the many different sources of state revenue. They are available at:

http://www.tax.alaska.gov/programs/sourcebook/index.aspx

Most of the revenue data are from *the Fall 2014 Revenue Sources Book*. Some data are from earlier revenue sources books.



Most of the state spending data in this presentation were provided by the Legislative Finance Division. Very detailed information about state budgets is provided on the Division's website:

http://www.legfin.state.ak.us/

The Division regularly prepares two-page fiscal summarizes of major budget categories by fund type. These are very useful as a summary of budgets by major fund type. They are posted at.

http://www.legfin.state.ak.us/FisSum/DisplayReports.php

Most of the spending data in this presentation are for fiscal year final budgets. Data for the FY14 and FY15 budgets are from the state of Alaska fiscal summary published August 29, 2014, which is shown on the next two slides.

Much more detailed budget information is provided in the annual Summary of Appropriations documents, which are posted at:

http://www.legfin.state.ak.us/Summary/DisplayReports.php

The Legislative Finance Division puts out two-page *Fiscal Summaries* which summarize major items in the state's budget and how they are funded.

State of Alaska Fiscal Summary--FY14 and FY15 (Part 1)

($ millions)

		FY14 BUDGET						FY15 BUDGET						Change in UGF	
		Unrestricted General Funds	Designated General Funds	Total General Funds	Other State Funds	Federal Receipts	All Funds	Unrestricted General Funds	Designated General Funds	Total General Funds	Other State Funds	Federal Receipts	All Funds	$	%
1	**REVENUE** (Excludes Permanent Fund Earnings) (1)	5,338.9	977.7	6,316.6	589.5	2,971.1	9,877.3	4,522.9	959.6	5,482.5	638.6	3,137.8	9,258.9	(816.0)	-15.3%
2	Unrestricted General Fund Revenue (Spring 2014) (2)	5,304.0	-	5,304.0	-	-	5,304.0	4,522.9	-	4,522.9	-	-	4,522.9		
3	Carryforward (3)	34.9	-	34.9	-	1.6	36.5	-	-	-	-	-	-		
4	Designated General Fund Revenue (4)	-	977.7	977.7	-	-	977.7	-	959.6	959.6	-	-	959.6		
5	Other State Funds and Federal Receipts	-	-	-	589.5	2,969.5	3,559.0	-	-	-	638.6	3,137.8	3,776.4		
	APPROPRIATIONS														
6	**TOTAL OPERATING APPROPRIATIONS**	6,438.8	743.8	7,182.6	550.8	2,042.1	9,775.5	5,244.5	772.4	6,016.9	3,573.5	2,019.5	11,609.9	(1,194.3)	-18.5%
7	**Agency Operations**	4,394.2	721.8	5,116.0	466.2	2,001.4	7,583.6	4,512.9	751.5	5,264.4	517.6	1,991.8	7,773.9	118.7	2.7%
8	Current Fiscal Year Appropriations (Includes Fiscal Notes)	4,386.2	721.7	5,107.8	466.2	2,001.4	7,575.4	4,492.9	751.5	5,244.4	517.6	1,991.8	7,753.9	106.8	2.4%
9	Agency Operations (Non-Formula)	2,297.0	647.8	2,944.8	463.2	914.8	4,322.8	2,246.3	642.9	2,889.2	514.7	903.8	4,307.7	(50.6)	-2.2%
10	K-12 Formula and Pupil Transportation	1,216.2	10.5	1,226.7	-	20.8	1,247.5	1,200.6	10.0	1,210.6	-	20.8	1,231.4	(15.6)	-1.3%
11	Other Formula Programs	873.0	63.4	936.3	2.8	1,063.9	2,003.0	877.7	74.9	952.5	2.8	1,067.2	2,022.5	4.7	0.5%
12	Revised Programs Legislatively Approved	-	-	-	0.2	1.9	2.1	-	-	-	-	-	-		
13	Fiscal Notes (FY14 notes are included in Management Plan)	-	-	-	-	-	-	168.3	23.8	192.1	0.1	0.1	192.2		
14	*Vetoes (non-additive)*	*(1.4)*	-	*(1.4)*	*(0.1)*	*(0.3)*	*(1.8)*	-	-	-	-	-	-		
15	*Duplicated Authorization (non-additive) (5)*	-	-	-	*734.7*	-	*734.7*	-	-	-	*736.4*	-	*736.4*		
16	Supplemental Operating Appropriations	8.0	0.1	8.2	0.0	(0.0)	8.2	20.0	0.0	20.0	0.0	0.0	20.0	11.8	144.6%
17	**Statewide Operations**	2,044.6	22.0	2,066.6	84.6	40.8	2,191.9	731.6	20.9	752.4	3,055.9	27.7	3,836.1	(1,313.0)	-64.2%
18	Current Fiscal Year Appropriations	2,004.2	22.0	2,026.2	61.6	40.8	2,128.5	731.6	20.9	752.4	3,055.9	27.7	3,836.1	(1,272.6)	-63.5%
19	Debt Service	207.4	20.8	228.2	54.5	17.5	300.1	218.8	19.3	238.1	50.3	5.2	293.7	11.5	5.5%
20	Fund Capitalization	1,146.0	1.2	1,147.2	7.1	23.3	1,177.5	507.5	1.6	509.1	5.6	22.5	537.1	(638.5)	-55.7%
21	Local Government Support	60.0	-	60.0	-	-	60.0	52.0	-	52.0	-	-	52.0	(8.0)	-13.3%
22	Oil & Gas Investment Tax Credits	600.0	-	600.0	-	-	600.0	450.0	-	450.0	-	-	450.0	(150.0)	-25.0%
23	AIDEA Capitalization (Fiscal Note)	125.0	-	125.0	-	-	125.0	-	-	-	-	-	-	(125.0)	-100.0%
24	In-State Pipeline Fund	355.0	-	355.0	-	-	355.0	-	-	-	-	-	-	(355.0)	-100.0%
25	Other Fund Capitalization	6.0	1.2	7.2	7.1	23.3	37.5	5.5	1.6	7.1	5.6	22.5	35.1	(0.5)	-7.0%
26	Retirement Costs: Actuarial Recommendation	633.8	-	633.8	-	-	633.8	5.2	-	5.2	-	-	5.2	(628.5)	-99.2%
27	Retirement Costs: Additional Contributions	-	-	-	-	-	-	-	-	-	3,000.0	-	3,000.0		
28	Special Appropriations	17.1	-	17.1	-	-	17.1	-	-	-	-	-	-		
29	*Duplicated Authorization (non-additive) (5)*	-	-	-	*42.0*	-	*42.0*	-	-	-	*12.1*	-	*12.1*		
30	Supplemental Statewide Appropriations	40.4	-	40.4	23.0	(0.0)	63.4	-	-	-	-	-	-	(40.4)	-100.0%
31	Debt Service	(15.4)	-	(15.4)	23.0	(0.0)	7.6	-	-	-	-	-	-		
32	Other Fund Capitalization	52.3	-	52.3	-	-	52.3	-	-	-	-	-	-		
33	Judgments, Claims and Settlements	3.5	-	3.5	-	-	3.5	-	-	-	-	-	-		
34	*Duplicated Authorization (non-additive) (5)*	-	-	-	*(22.9)*	-	*(22.9)*	-	-	-	-	-	-		
35	**TOTAL CAPITAL APPROPRIATIONS**	880.4	219.5	1,099.9	36.8	929.0	2,065.7	594.9	164.5	759.4	65.1	1,118.2	1,942.7	(285.5)	-32.4%
36	Current Fiscal Year Appropriations	796.2	212.8	1,008.9	34.8	929.0	1,972.7	594.9	164.5	759.4	65.1	1,118.2	1,942.7	(201.3)	-25.3%
37	Project Appropriations & RPLs (Revised Programs)	769.2	212.8	981.9	34.8	929.0	1,945.7	594.9	164.5	759.4	65.1	1,118.2	1,942.7	(174.3)	-22.7%
38	Fund Capitalization	27.0	-	27.0	-	-	27.0	-	-	-	-	-	-	(27.0)	-100.0%
39	*Projects Funded with Other Debt Proceeds (non-additive)*	-	-	-	*35.0*	-	*35.0*	-	-	-	*172.5*	-	*172.5*		
40	*Duplicated Authorization (non-additive) (5)*	-	-	-	*58.3*	-	*58.3*	-	-	-	*200.9*	-	*200.9*		
41	Supplemental Appropriations	84.2	6.8	91.0	2.0	0.0	93.0	0.0	0.0	0.0	0.0	0.0	0.0	(91.0)	-100.0%
42	Capital Projects (net of Duplication)	84.2	6.8	91.0	2.0	-	93.0	-	-	-	-	-	-		
43	*Duplicated Authorization (non-additive) (5)*	-	-	-	-	-	-	-	-	-	-	-	-		
44	*Money on the Street (includes all fund sources) (6)*	*880.4*	*219.5*	*1,099.9*	*95.1*	*929.0*	*2,124.0*	*594.9*	*164.5*	*759.4*	*265.9*	*1,118.2*	*2,143.5*	*(285.5)*	*-32.4%*
45	**Pre-Transfers Authorization** (unduplicated)	7,319.2	963.3	8,282.5	587.6	2,971.1	11,841.2	5,839.4	936.8	6,776.2	3,638.6	3,137.8	13,552.6	(1,479.8)	-20.2%
46	*Pre-Transfers Surplus/(Deficit)*	*(1,980.3)*	*-37.1%*	*of UGF Revenue*				*(1,316.5)*	*-29.1%*	*of UGF Revenue*					

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Source: http://www.legfin.akleg.gov/FisSum/DisplayReports.php

Legislative Finance Division *Fiscal Summary* (page 2)

State of Alaska Fiscal Summary--FY14 and FY15 (Part 1)

($ millions)

		FY14 BUDGET						FY15 BUDGET						Change in UGF	
		Unrestricted General Funds	Designated General Funds	Total General Funds	Other State Funds	Federal Receipts	All Funds	Unrestricted General Funds	Designated General Funds	Total General Funds	Other State Funds	Federal Receipts	All Funds	$	%
47	**Transfers (7)**	**(266.3)**	**14.4**	**(251.8)**	**1.9**	**-**	**(249.9)**	**67.7**	**22.8**	**90.5**	**(3,000.0)**	**-**	**(2,909.5)**	**334.0**	**-125.4%**
48	**Current Fiscal Year Transfers**	(292.1)	14.4	(277.7)	1.9	0.0	(275.7)	67.7	22.8	90.5	(3,000.0)	0.0	(2,909.5)	359.9	-123.2%
49	Loan Funds	10.0	-	10.0	-	-	10.0	-	-	-	-	-	-	(10.0)	-100.0%
50	Designated Reserves (Public Education Fund)	1.3	-	1.3	-	-	1.3	58.4	-	58.4	-	-	58.4	57.1	4400.7%
51	Undesignated Reserves (Alaska Housing Capital Corp)	(374.1)	-	(374.1)	-	-	(374.1)	(63.1)	-	(63.1)	-	-	(63.1)	311.0	-83.1%
52	Oil & Hazardous Substance Fund	8.7	13.6	22.3	-	-	22.3	8.4	3.4	11.8	-	-	11.8	(0.3)	-3.4%
53	REAA School Fund	36.2	-	36.2	-	-	36.2	40.0	-	40.0	-	-	40.0	3.8	10.6%
54	AMHS Fund	0.8	-	0.8	-	-	0.8	0.1	-	0.1	-	-	0.1	(0.7)	-88.9%
55	Renewable Energy Fund	25.0	-	25.0	-	-	25.0	20.0	-	20.0	-	-	20.0	(5.0)	-20.0%
56	Other Funds	-	0.8	0.8	1.9	-	2.8	4.0	19.4	23.4	(3,000.0)	-	(2,976.6)		
57	**Supplemental Transfers**	25.9	0.0	25.9	0.0	0.0	25.9	0.0	0.0	0.0	0.0	0.0	0.0	(25.9)	-100.0%
58	Undesignated Reserves (Alaska Housing Capital Corp)	(37.5)	-	(37.5)	-	-	(37.5)	-	-	-	-	-	-		
59	AMHS Fund	2.5	-	2.5	-	-	2.5	-	-	-	-	-	-		
60	AMHS Vessel Replacement Fund	8.4	-	8.4	-	-	8.4	-	-	-	-	-	-		
61	Permanent Fund Transfers	52.5	-	52.5	-	-	52.5	-	-	-	-	-	-		
62	**Post-Transfers Authorization (unduplicated)**	**7,052.9**	**977.7**	**8,030.7**	**589.5**	**2,971.1**	**11,591.3**	**5,907.1**	**959.6**	**6,866.8**	**638.6**	**3,137.8**	**10,643.1**	**(1,145.8)**	**-16.2%**
63	*Post-Transfer Balance to/(from) the SBR (8)*	*(1,714.1)*	*-32.1%*	*of UGF Revenue*				*(1,384.2)*	*-30.6%*	*of UGF Revenue*					
64	**Permanent Fund**	-	2,062.6	2,062.6	7.2	-	2,069.8	-	2,173.0	2,173.0	8.5	-	2,181.5		
65	Permanent Fund Dividends	-	1,070.0	1,070.0	-	-	1,070.0	-	1,150.0	1,150.0	-	-	1,150.0		
66	Deposits to Principal	-	934.0	934.0	-	-	934.0	-	965.0	965.0	-	-	965.0		
67	Alaska Capital Income Fund	-	20.0	20.0	-	-	20.0	-	22.0	22.0	-	-	22.0		
68	*Other Uses of Earnings (included in op or cap budget) (9)*	-	*38.6*	*38.6*	*7.2*	-	*45.8*	-	*36.0*	*36.0*	*8.5*	-	*44.5*		
69	**Total Authorization (unduplicated)**	**7,052.9**	**3,001.7**	**10,054.7**	**589.5**	**2,971.1**	**13,615.3**	**5,907.1**	**3,096.6**	**9,003.8**	**638.6**	**3,137.8**	**12,780.1**	**(1,145.8)**	**-16.2%**
	FISCAL YEAR SUMMARY	7,319.2	2,987.3	10,306.5	587.6	2,971.1	13,865.2	5,839.4	3,073.8	8,913.2	3,638.6	3,137.8	15,689.6	(1,479.8)	-20.2%
	Agency Operations	4,394.2	721.8	5,116.0	466.2	2,001.4	7,583.6	4,512.9	751.5	5,264.4	517.6	1,991.8	7,773.9	118.7	2.7%
	Statewide Operations	2,044.6	22.0	2,066.6	84.6	40.8	2,191.9	731.6	20.9	752.4	3,055.9	27.7	3,836.1	(1,313.0)	-64.2%
	Total Operating	**6,438.8**	**743.8**	**7,182.6**	**550.8**	**2,042.1**	**9,775.5**	**5,244.5**	**772.4**	**6,016.9**	**3,573.5**	**2,019.5**	**11,609.9**	**(1,194.3)**	**-18.5%**
	Capital	**880.4**	**219.5**	**1,099.9**	**36.8**	**929.0**	**2,065.7**	**594.9**	**164.5**	**759.4**	**65.1**	**1,118.2**	**1,942.7**	**(285.5)**	**-32.4%**
	Unduplicated Appropriation of Permanent Fund Earnings	0.0	2,024.0	2,024.0	0.0	0.0	2,024.0	0.0	2,137.0	2,137.0	0.0	0.0	2,137.0		
	Transfers (non-additive)	*(266.3)*	*14.4*	*(251.8)*	*1.9*	-	*(249.9)*	*67.7*	*22.8*	*90.5*	*(3,000.0)*	-	*(2,909.5)*	*334.0*	*-125.4%*

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Notes:

(1) **Although Permanent Fund earnings may be appropriated for any purpose, the legislature traditionally excludes them from the definition of available revenue. Appropriations of Permanent Fund earnings are reported in lines 64-67 of the summary. Permanent Fund earnings and balance information is reported in part 2 of the Fiscal Summary.**

(2) The Department of Revenue's Spring 2014 oil forecast for FY14 is 0.522 mbd at $106.61 per barrel; the FY15 forecast is 0.498 mbd at $105.06 per barrel.

(3) Carryforward is money that was appropriated in a prior year that is made available for spending in a later year via multiyear appropriations or reappropriations. Total carryforward into FY15 will be unknown until the close of FY14.

(4) Designated general funds include 1) program receipts that are restricted to the program that generates the receipts and 2) revenue that is statutorily designated for a specific purpose.

(5) Duplicated authorization is in the budget twice, such as when funds flow in and out of a holding account or one agency pays another for services provided. Duplicated authorization also includes the expenditure of bond proceeds when debt service on bonds (which includes repayment of principal) will be reflected in future operating budgets.

(6) Including duplicated fund sources in the amount of capital spending provides a valuable measure of "money on the street" because it includes projects funded with bond proceeds and other duplicated fund sources.

(7) "Transfers" refer to appropriations that move money from one fund to another within the Treasury. Although transfers are not true expenditures, they reduce the amount of money available for other purposes so must be included in the calculation of the surplus/deficit. For reserve accounts, a positive number indicates a deposit and a negative number indicates a withdrawal. When money is withdrawn and spent, the expenditure is included in the operating or capital budget, as appropriate.

(8) The post-transfer withdrawal necessary to balance the budget is anticipated to be $1.7 billion in FY14 and $1.4 billion in FY15.

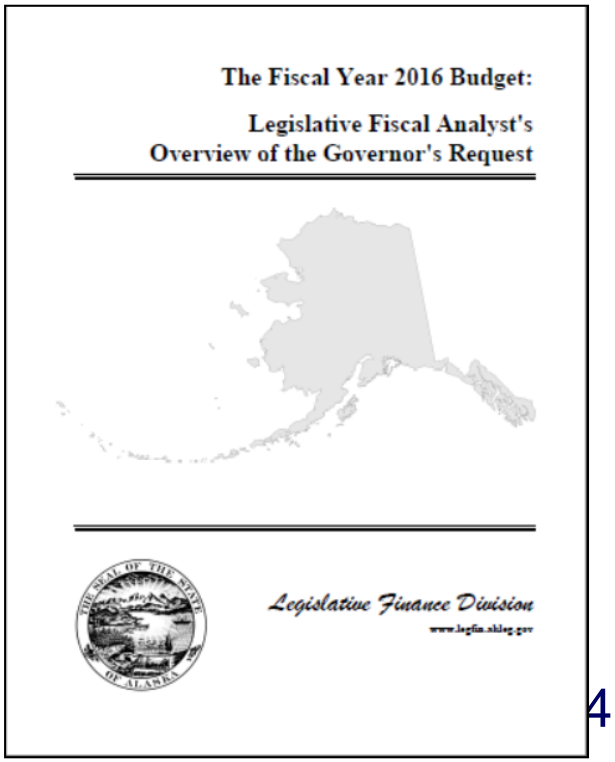
(9) Amounts shown on line 68 can be considered duplicated appropriations--they are included in the operating or capital budgets above. The Designated General Fund column include amounts associated with the dividend program. Amounts in the Other column reflect gross earnings of the Permanent Fund spent for purposes other than operation of the corporation.

Approximate start-of-year and end-of-year balances of reserves in state funds can be found near the front of the Summary of Appropriations documents in part 2 of the Fiscal Summary.

Most of the historical budget data in the presentation for years prior to FY14 was provided to me by the Legislative Finance Division as Excel spreadsheets by special request.

In mid-January 2015, the Legislative Finance Division prepared a report entitled The Fiscal Year 2016 Budget: Legislative Fiscal Analyst's Overview of the Governor's Request. The 8-page introduction to this report provides a very useful summary of the state's budget situation as of January 2015.

http://www.legfin.state.ak.us/Overview/Overview2016.pdf


The Fiscal Year 2016 Budget:

Legislative Fiscal Analyst's
Overview of the Governor's Request

Legislative Finance Division

Detailed current and historical data about the Permanent Fund can be found in the monthly and annual reports posted on the Alaska Permanent Fund Corporation website at:

http://www.apfc.org/home/Content/publications/reportArchive.cfm