Sustainable Budget Proposal

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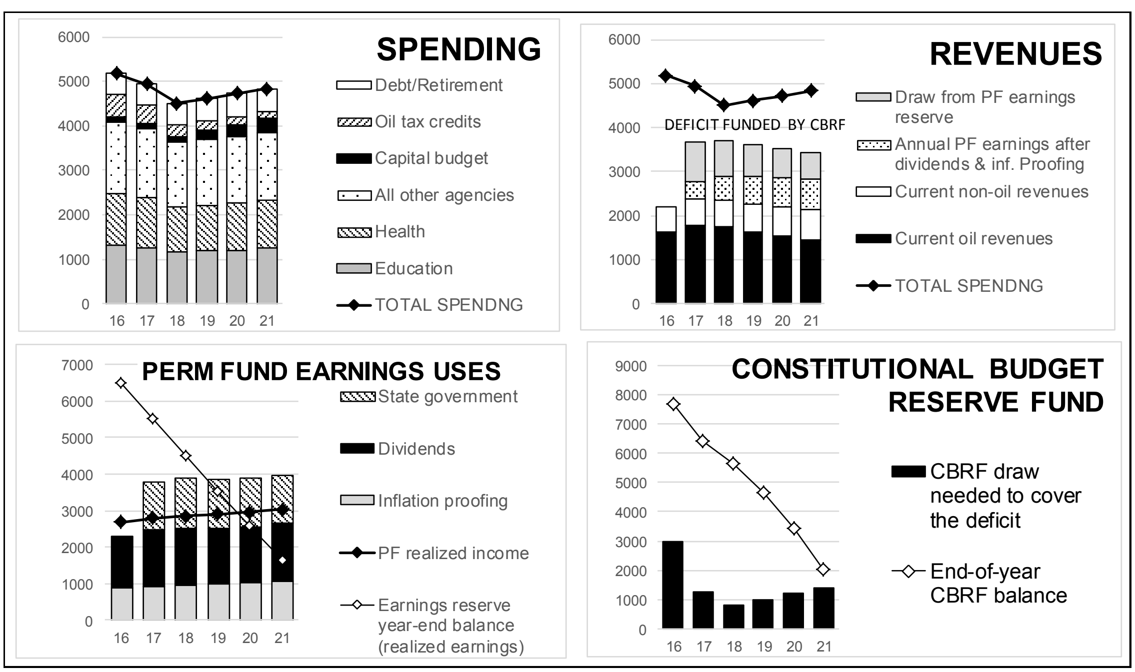
My proposal is built around Scott Goldsmith's sustainable budget model. That approach takes a long-term view, treats all generations equitably by providing both current and future generations with the same share of the state's resources, and offers Alaskans significant predictability. (The model and a series of papers are available at www.iser.uaa.alaska.edu.)

Based on the assumptions in the model's supplemental sheet, the long-term sustainable spending number is in the range of $4.5 billion annually, adjusted thereafter for inflation and population growth. Consistent with the intent of the founders of the Permanent Fund, the sustainable budget approach includes as part of government revenues the income earned from the Permanent Fund remaining after deductions for paying Permanent Fund dividends and inflation-proofing the principal of the fund. If any of the significant assumptions fail to materialize, the sustainable number is less.

This proposal reduces spending to $4.5 billion by FY 2018. All spending is affected, but the largest share of reductions (36% of the total) falls on reimbursable oil tax credits, which are reduced and capped at the levels projected in fall 2014. Once reduced to $4.5 billion, all spending categories adjust with inflation beginning in FY 2019, except that additional funds are shifted from oil tax credits to capital spending, in significant part to help pay state costs for the planned LNG project.

Consistent with the sustainable budget approach, this proposal pays for current spending by combining oil revenues with income earned from the Permanent Fund in excess of the amounts required for the PFD and inflation proofing, supplemented by borrowings from the Constitutional Budget Reserve and accumulated past excess earnings from the Permanent Fund (held in the earnings reserve). Draws from the CBR and earnings reserve are repaid beginning in 2025, when revenues exceed the sustainable spending level because of LNG and growing financial earnings. Because long-term revenues are sufficient to fund spending, the proposal does not cap or reduce the PFD or rely on broad-based taxes.

A key to the proposal is continued monitoring and fiscal discipline. If any of the long-range assumptions change—for example, if the LNG project no longer appears likely, oil prices don't achieve anticipated levels, or financial returns are less than projected—then spending must be reduced further or supplemental revenues enacted. For the present, however, this approach responsibly reflects what we see ahead.



Graphs prepared by Gunnar Knapp to compare state finances for FY16 (this year)
with projections under this proposal for FY17-FY21, if oil prices average $70/barrel.