



Alaska Fiscal Challenges and Choices



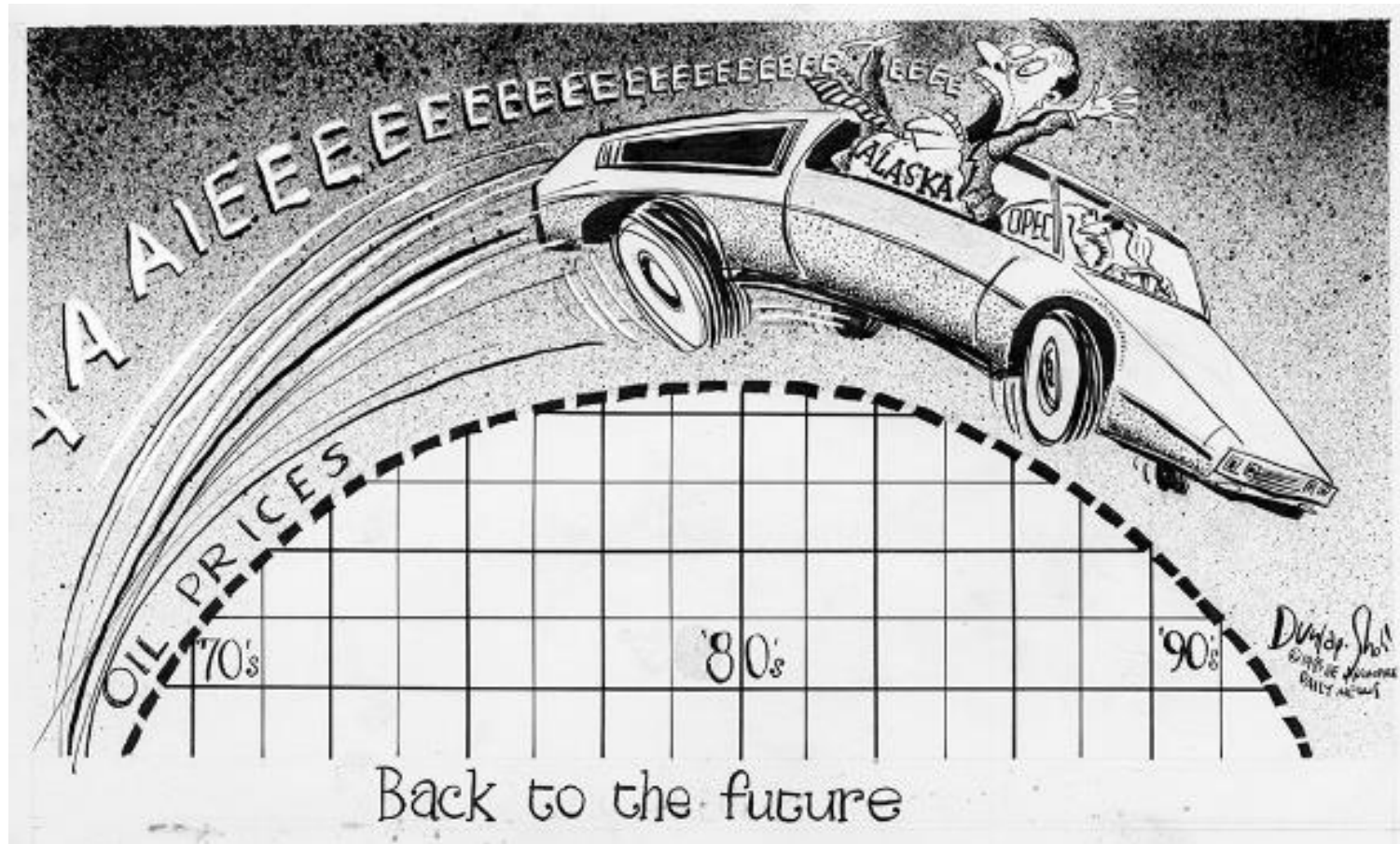
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oleanchorage.org



Including selected historical political cartoons of
Peter Dunlap-Shohl,
long-time wonderful editorial cartoonist for the
Anchorage Daily News



Alaska's finances are very complex.

- Many different kinds of revenues, spending and savings.
- Accounting for state finances is
 - Complex
 - Confusing
 - Inconsistent
 - Incomplete
 - Not up-to-date
 - Frustrating
- Politicians use many accounting tricks to try to look better
- State finances are very hard to understand
 - Including for legislators
 - Including for me

Don't believe anyone who tells you the issues are simple.

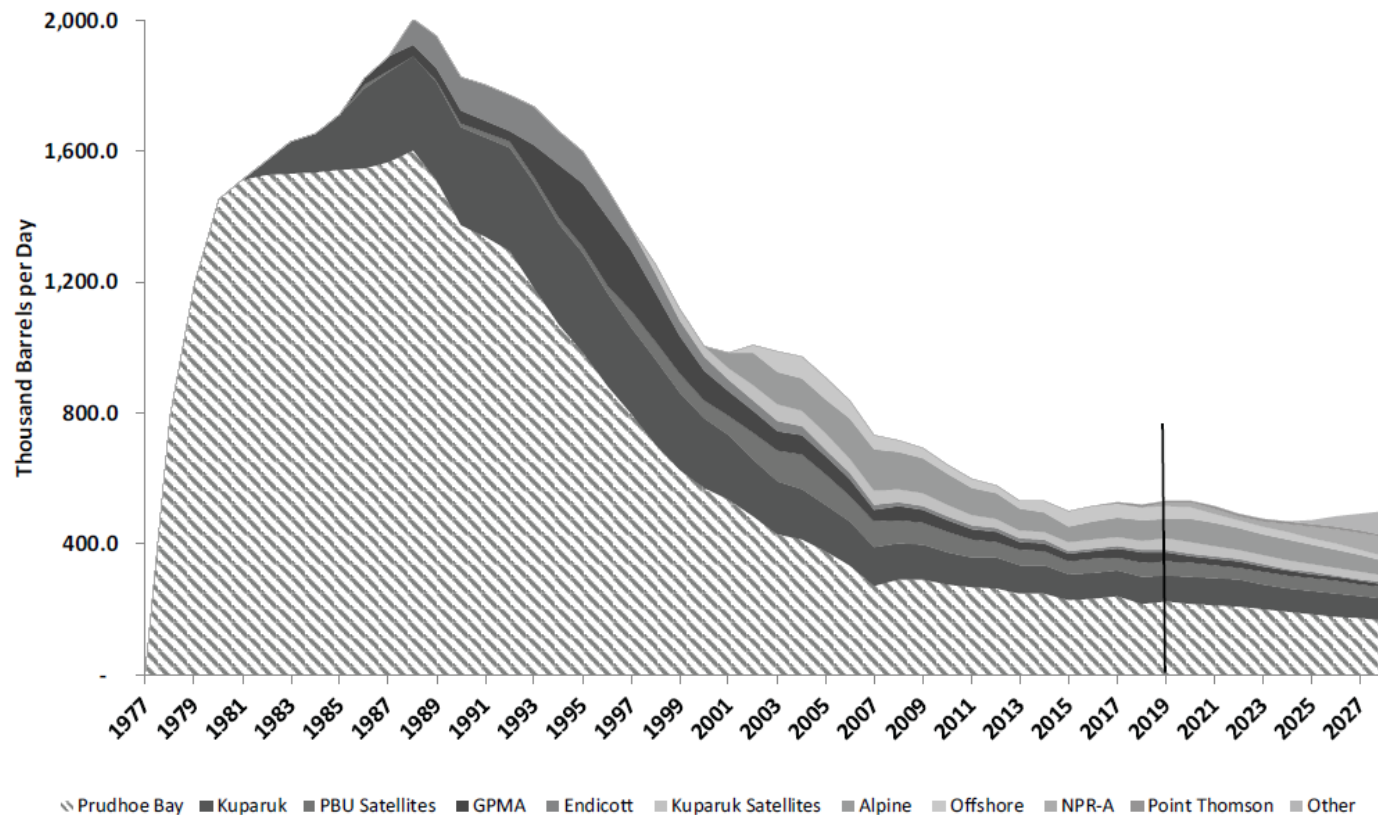
Uses of Alaska Revenues: Traditional and New

	Traditional (before FY19)	New (after FY19)
Oil revenues	Government	Government
Other traditional revenues		
PF earnings	Dividends Total distribution = 1/2 of average earnings for the past 5 years	Government & Dividends Total distribution = 5% of average value over the past 5 years

Oil has driven Alaska's economy and state finances
for as long as most Alaskans remember.

But oil production has fallen by almost 75% since peaking in 1988.
In recent years production has leveled off.
Production may increase but probably not substantially.

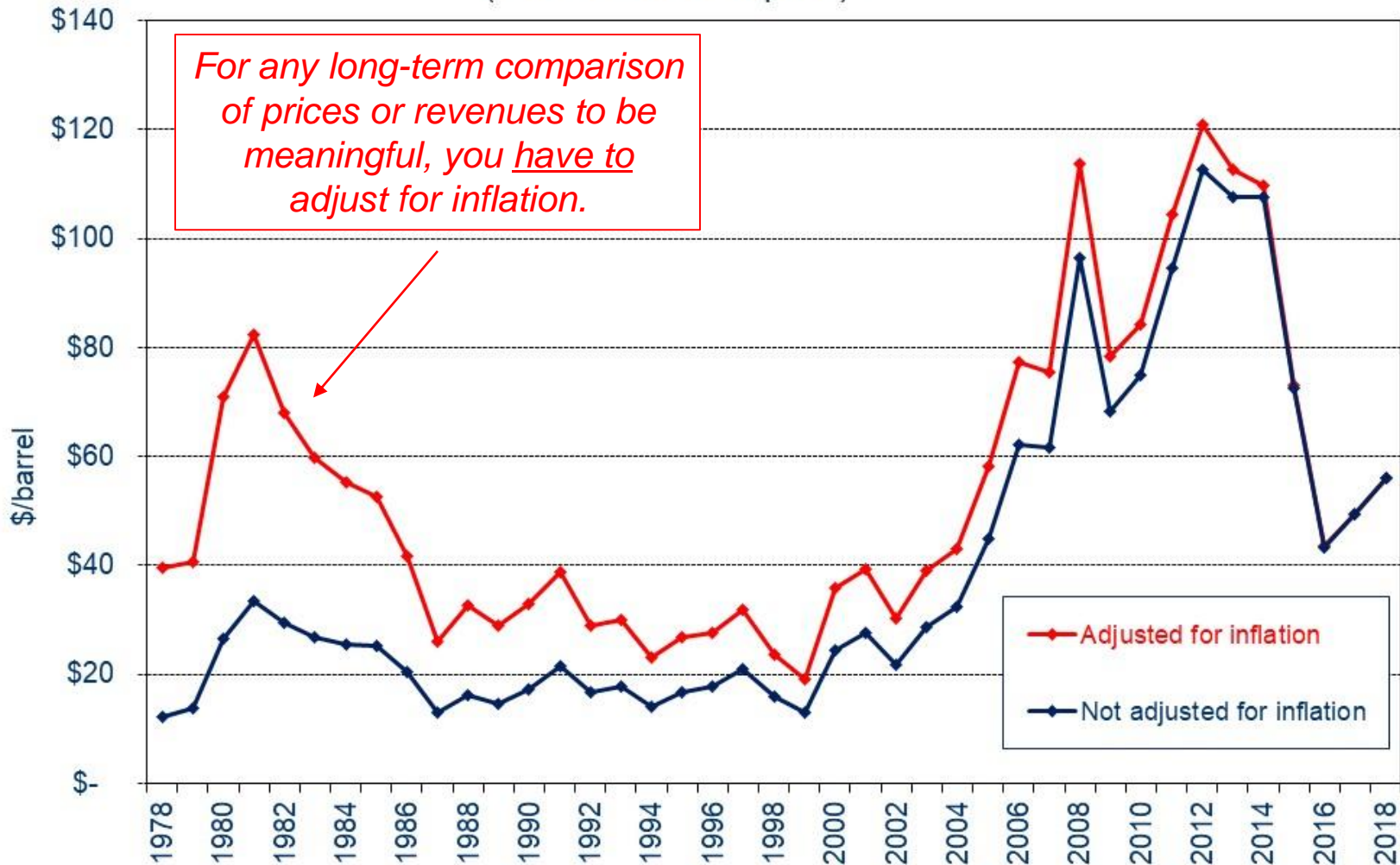
Alaska North Slope Oil Production: Historical and Projected



Source: Alaska Department of Revenue, Tax Division, *Revenues Sources Book*, Fall 2018, page 59.

Oil prices have fluctuated drastically since North Slope oil production began.

Average Price of Alaska North Slope Oil
(ANS West Coast price)



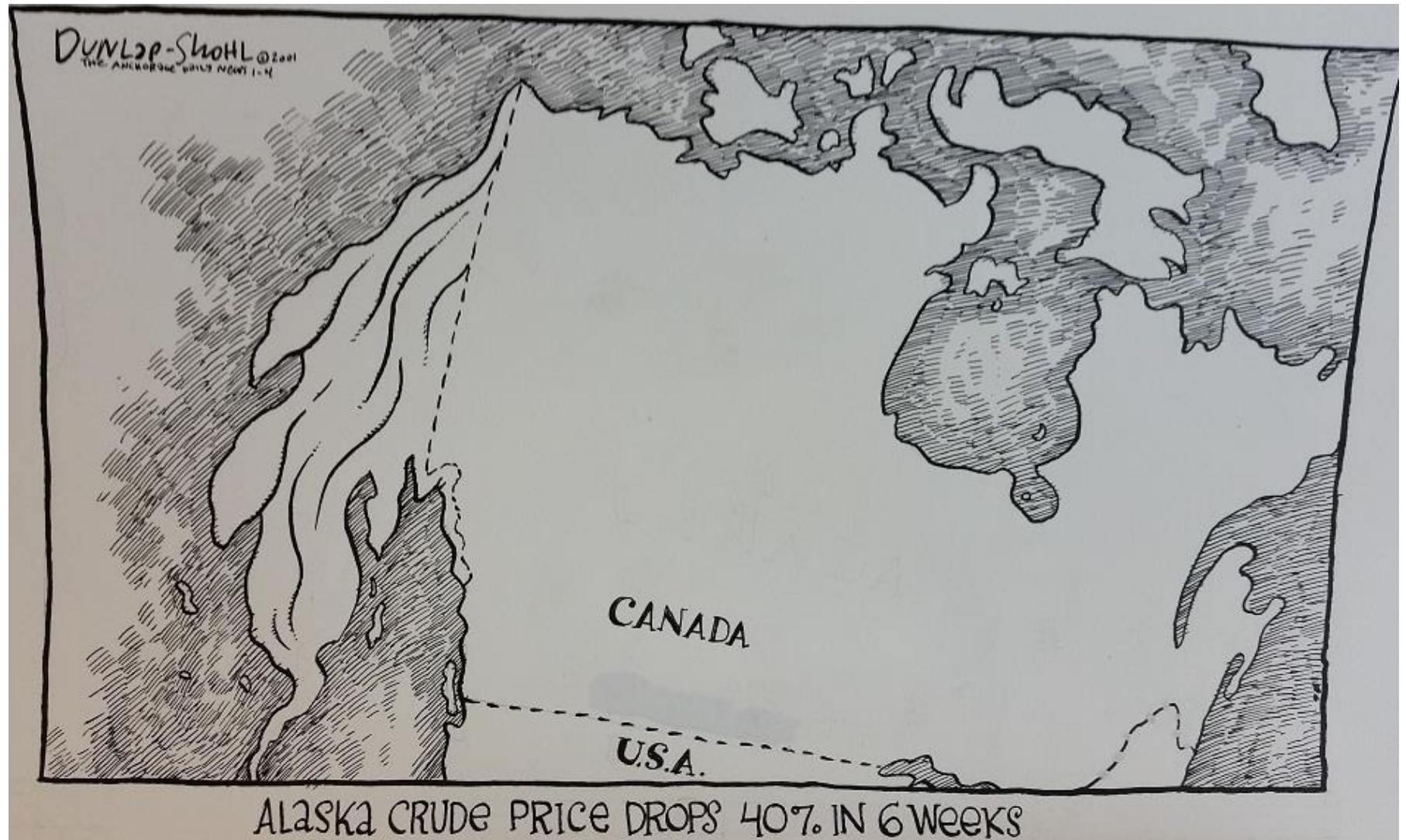
2018
average
price is
DOR Fall
2017
projection.

THE GOOD NEWS: DOES ZERO to SIXTY IN NOTHING FLAT

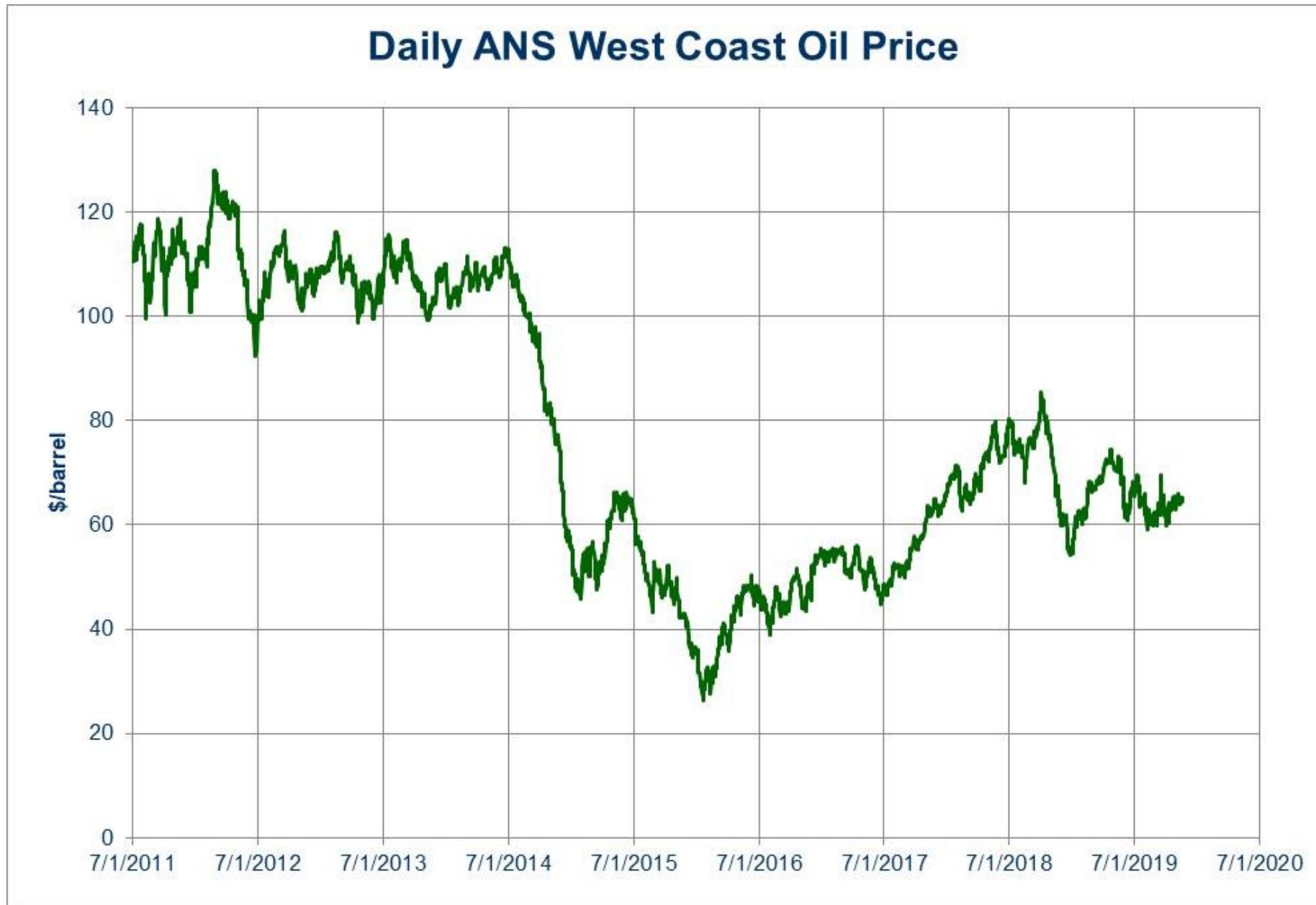


THE BAD NEWS: SURPRISE! JUST as SPEEDY WHEN
IT UNEXPECTEDLY SHIFTS INTO REVERSE.

In 2001, oil prices dropped 40% in 6 weeks . . .

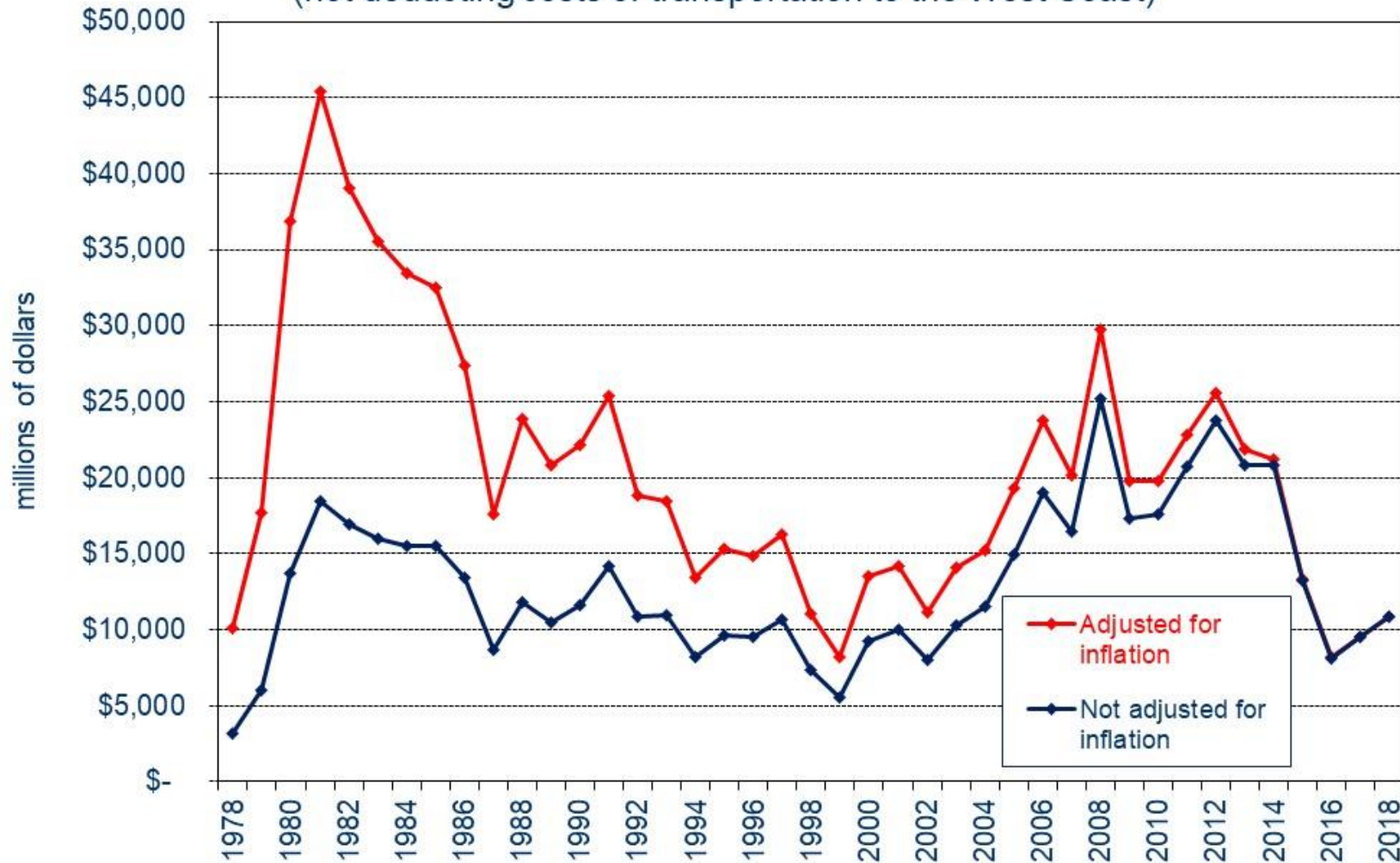


Oil prices dropped drastically five years ago and seem unlikely to recover.



The combined effect of fluctuations in oil production and prices has been drastic fluctuations in the value of Alaska oil production.

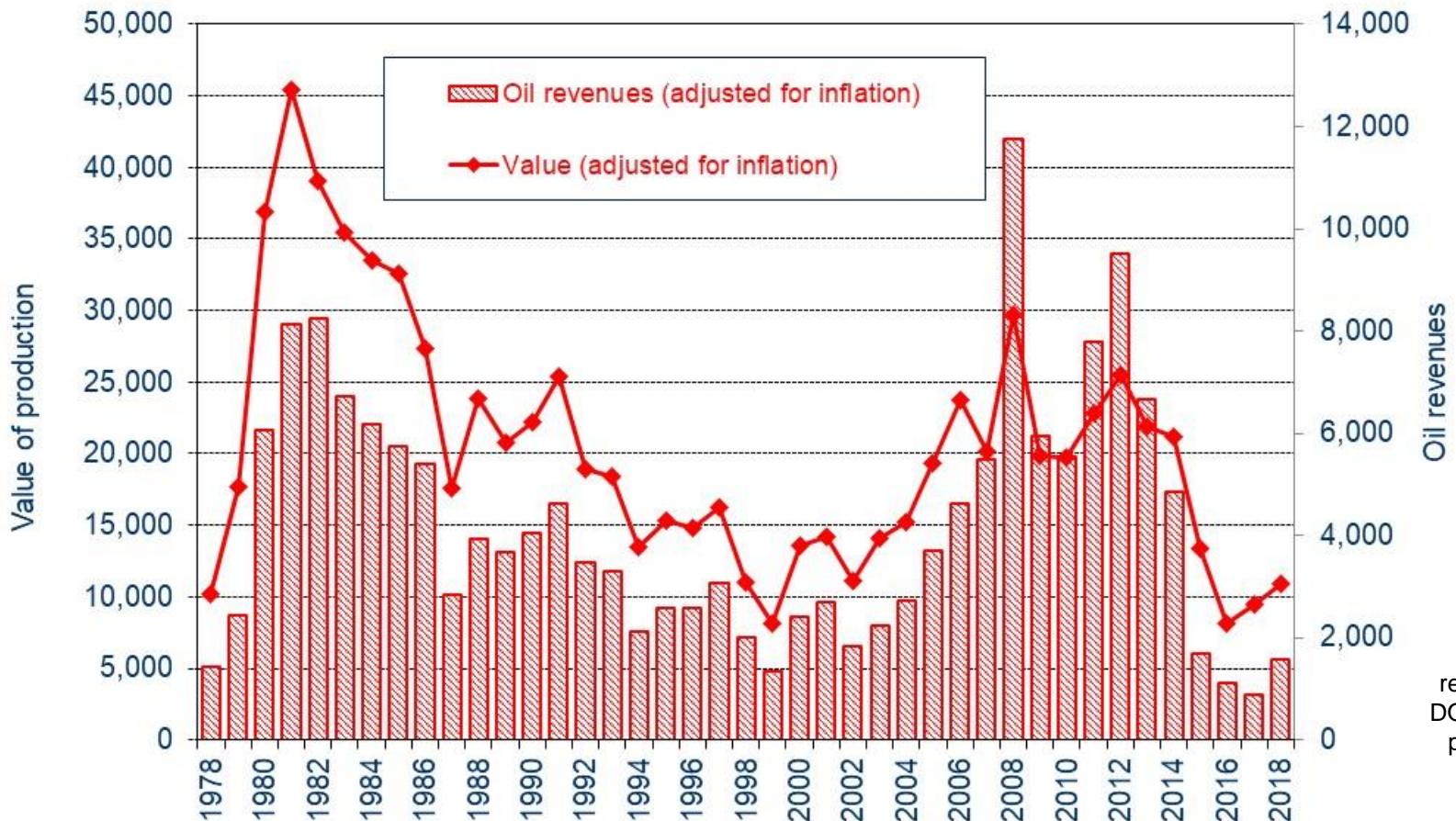
Total West Coast Value of Alaska North Slope Oil Production
(not deducting costs of transportation to the West Coast)



2018 average price value is based on DOR Fall 2017 projected production & price.

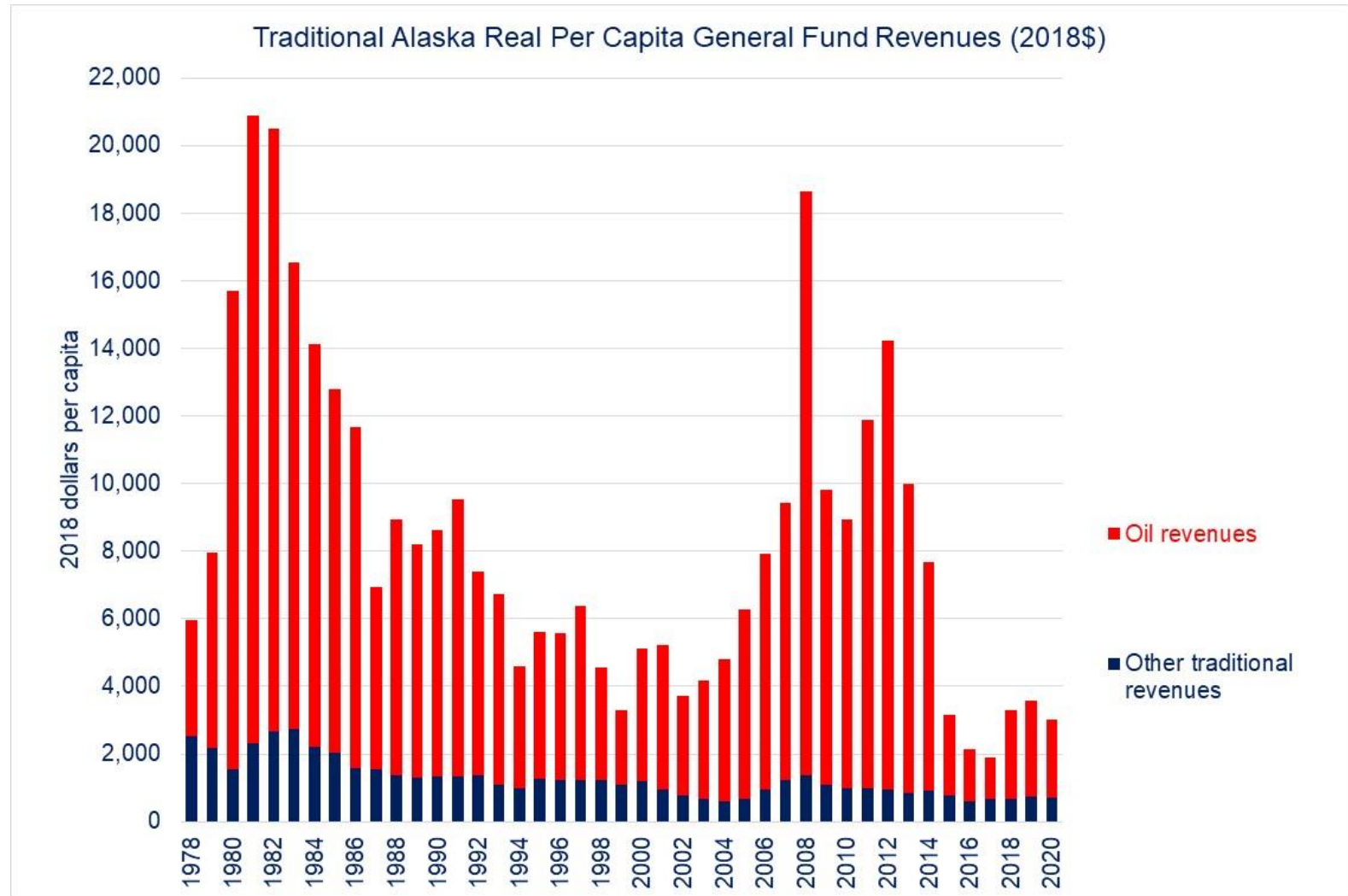
Drastic fluctuations in the value of Alaska oil production were reflected in drastic fluctuations in Alaska oil revenues.
(Other factors, such as changes in oil taxes and costs, also affected oil revenues.)

Value of Alaska North Slope Oil Production and Alaska UGF Oil Revenues)
(millions of 2017 dollars)



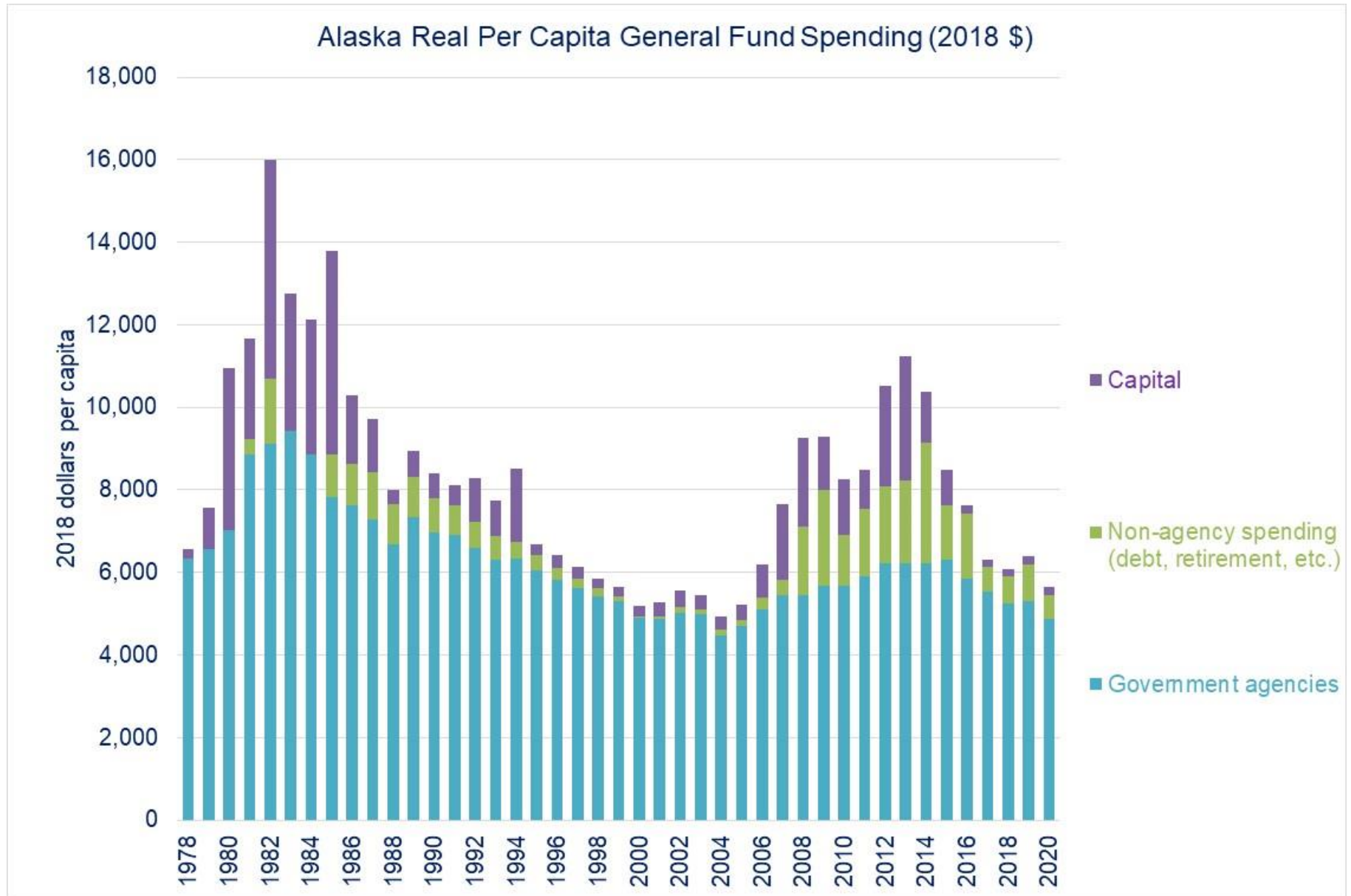
2018 oil revenues are DOR Fall 2017 projections.

Although oil revenues fluctuated dramatically, they provided most of state revenues for more than three decades. Oil accounted for 86% of total UGF revenues between 1980 and 2014.



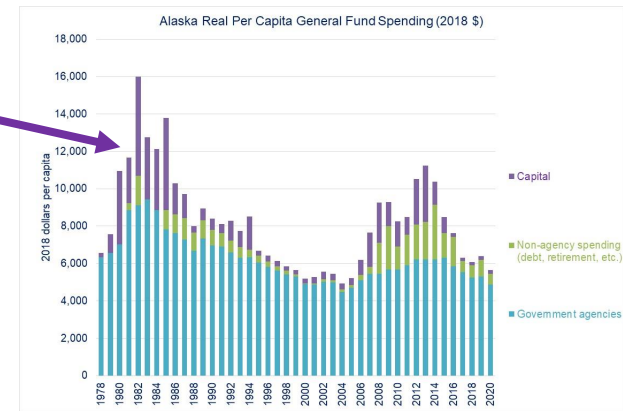
Note: Graph shows per capita revenues and spending adjusted for inflation to 2018 dollars per person. For any long-term comparison of spending to be meaningful, you have to adjust for inflation and population change.

As our traditional revenues went up and down, so did our spending.



When we were rich,
we built stuff!

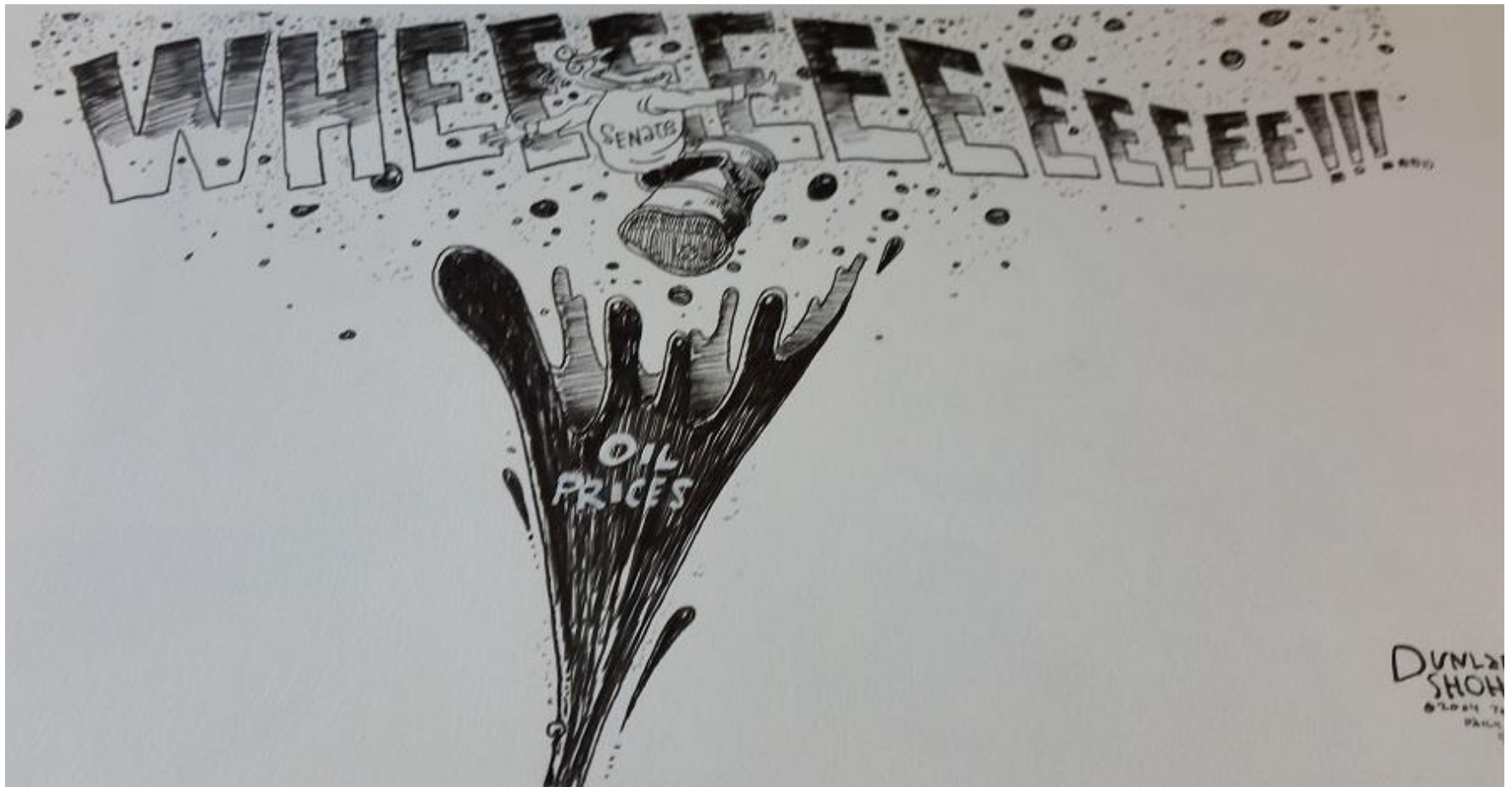
1984



When we were poor, we cut spending.
In 1987, oil prices crashed, and our economy crashed . . .



But after each time prices and revenues fell,
they came back up—and we spent more!

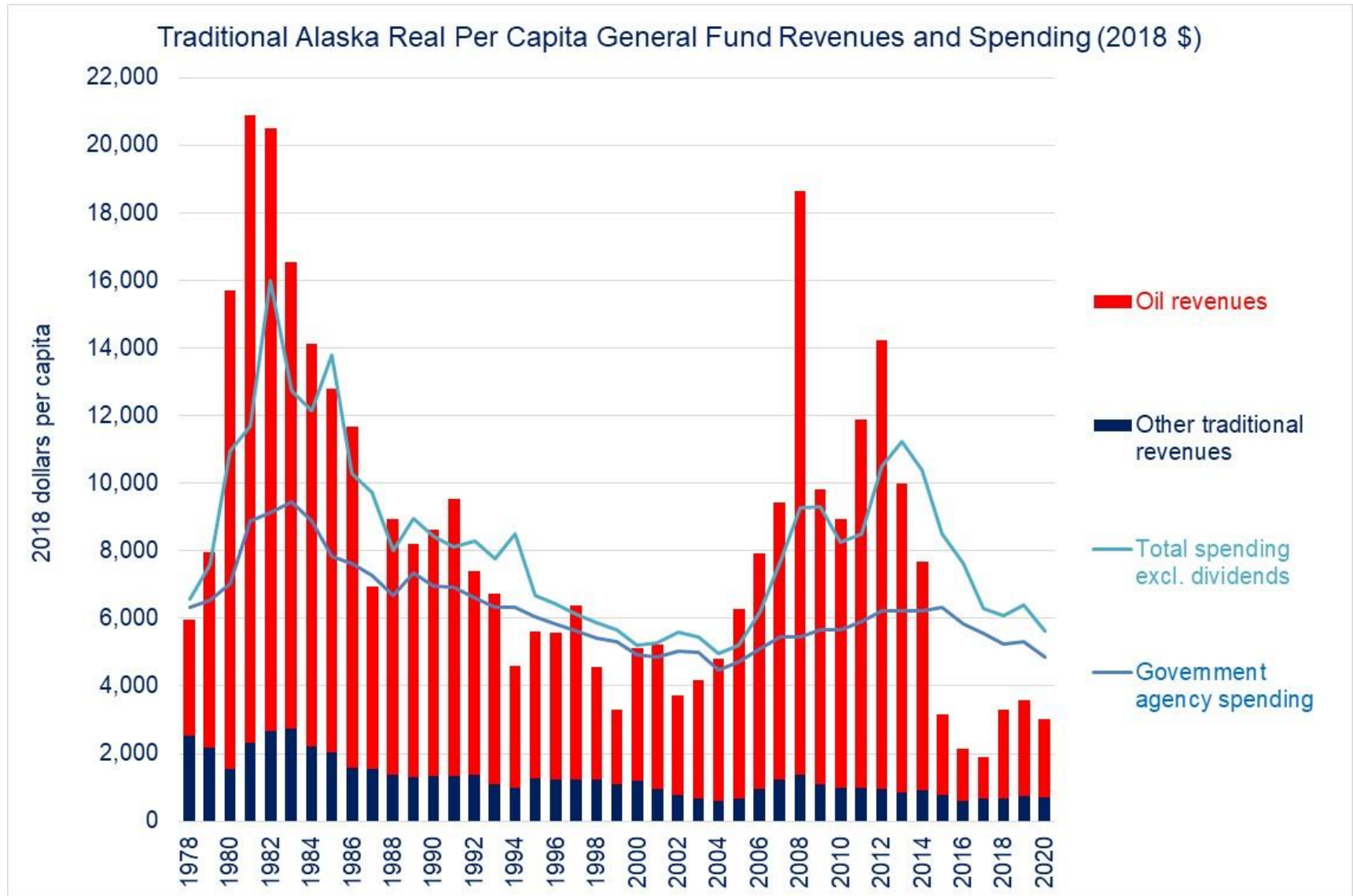


Multiple times we were “saved” when oil prices rose again . . .



THE ALASKA FISCAL PLAN, AS WE KNOW IT.

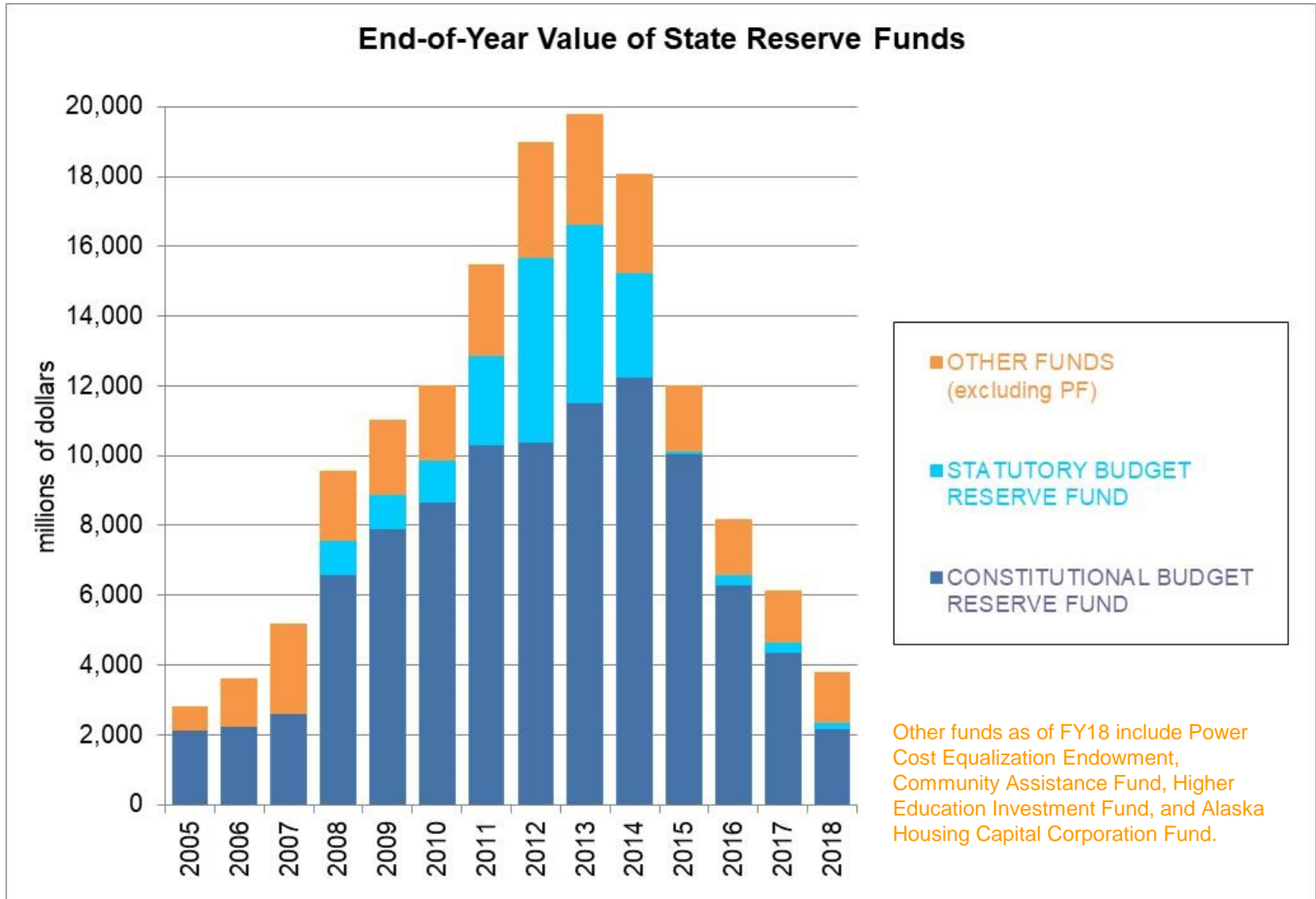
When we had lots of oil money, we ran surpluses—and built up savings.
When we had less oil money, we ran deficits—and drew down savings.



Note: Graph shows per capita revenues and spending.

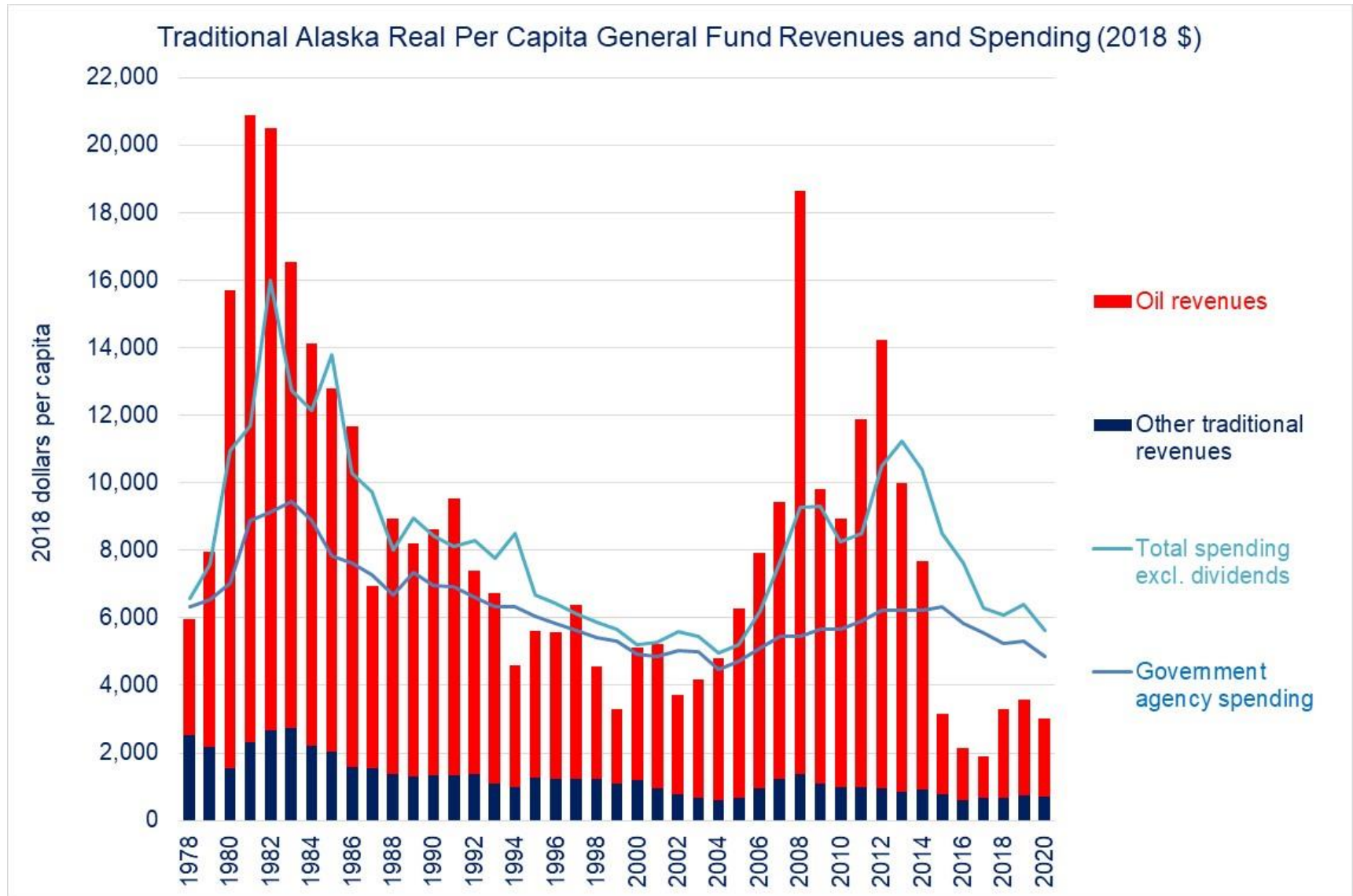
For any long-term comparison of spending to be meaningful, you have to adjust for inflation and population change.

Before 2013 we used surpluses prior to build up our savings reserves funds.
After 2013 we drew down these funds to pay for deficits.

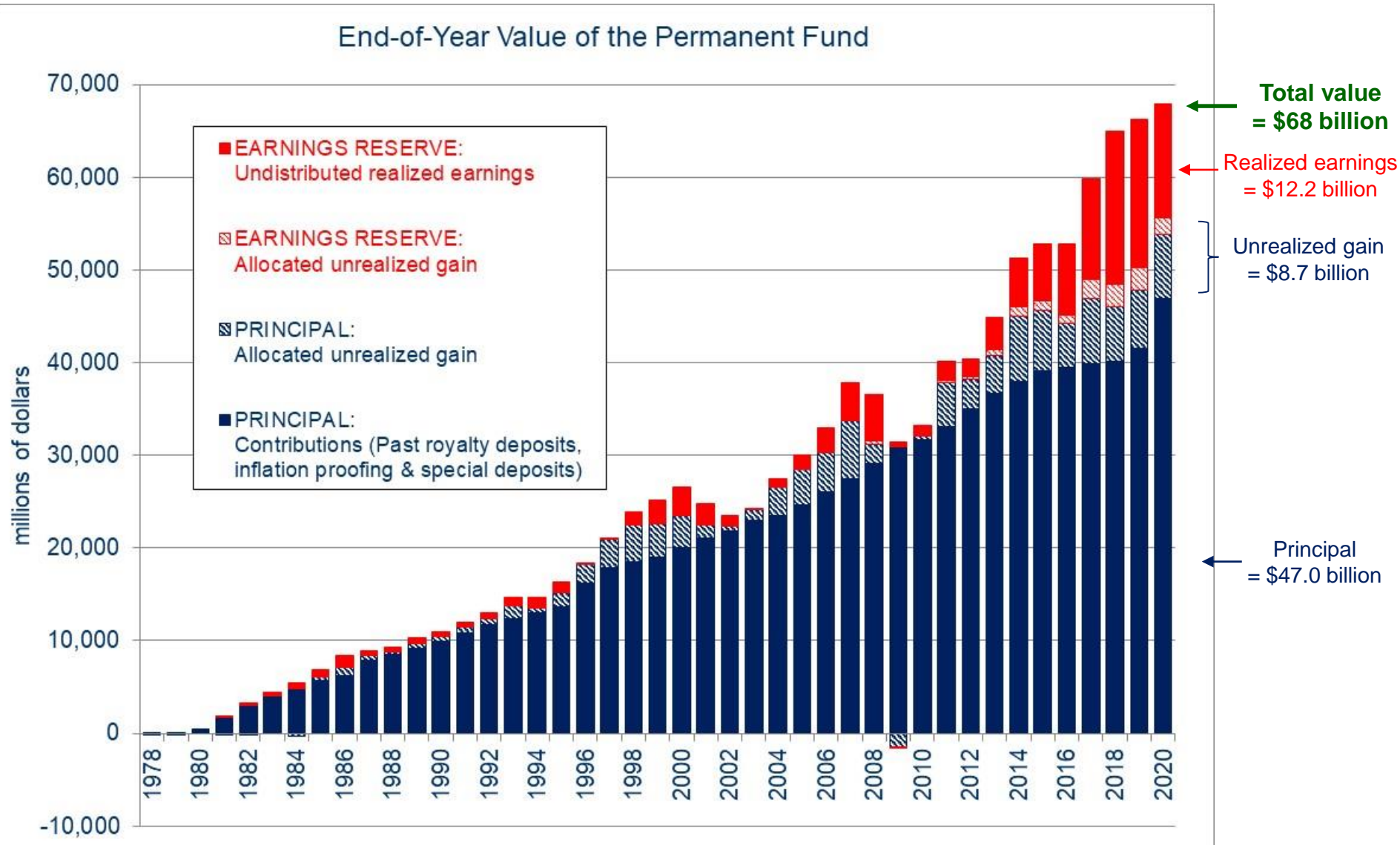


Note: 2018 data are Legislative Finance Division projections.

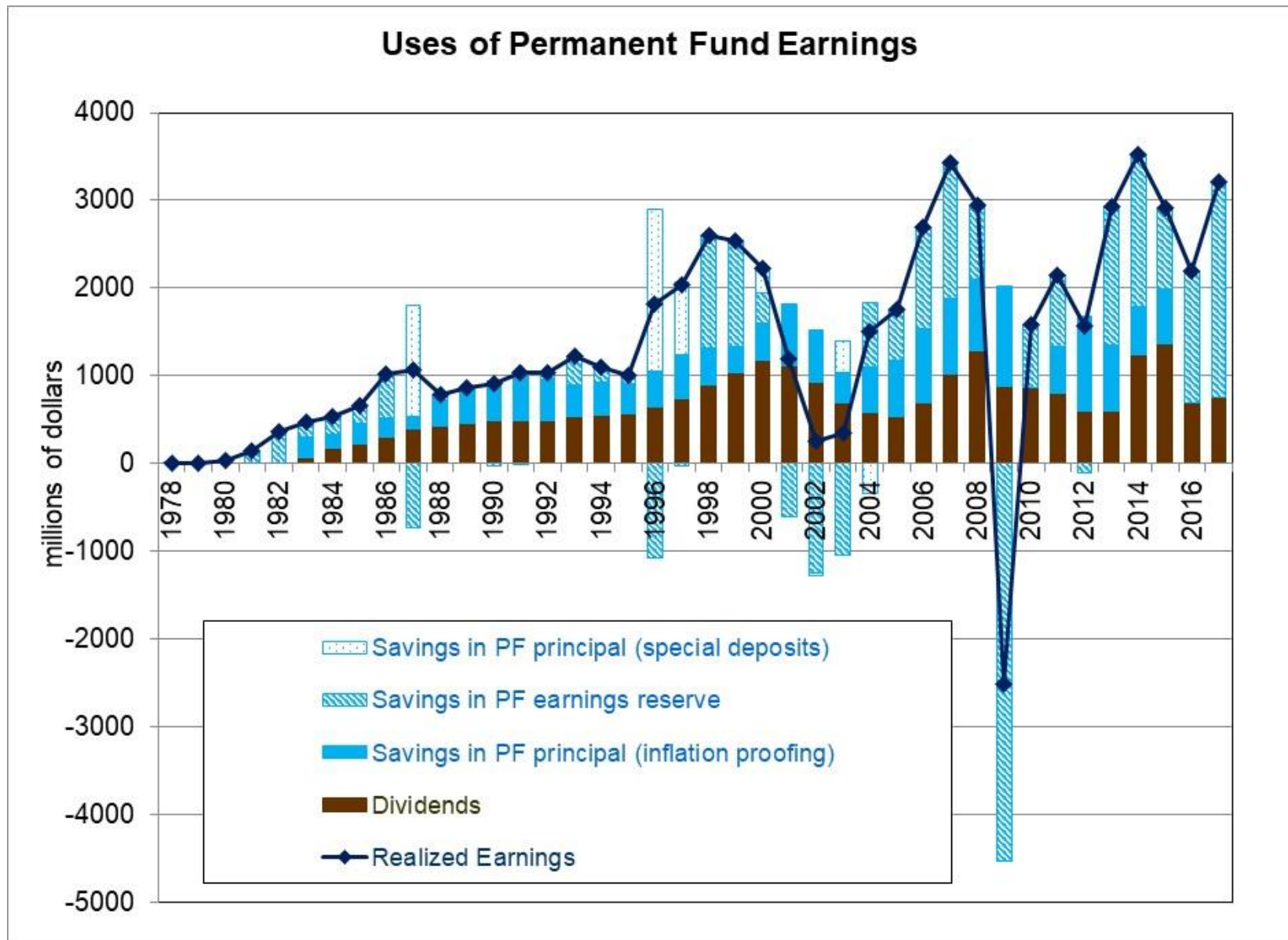
We can no longer pay for state government from our traditional revenue sources.
Oil revenues have fallen too much. And we can't or won't cut spending enough.



Luckily we saved a lot of money in our Permanent Fund, which had grown to a total value of \$68 billion on June 30, 2019. The principal may not be spent but **the realized earnings may be spent.**

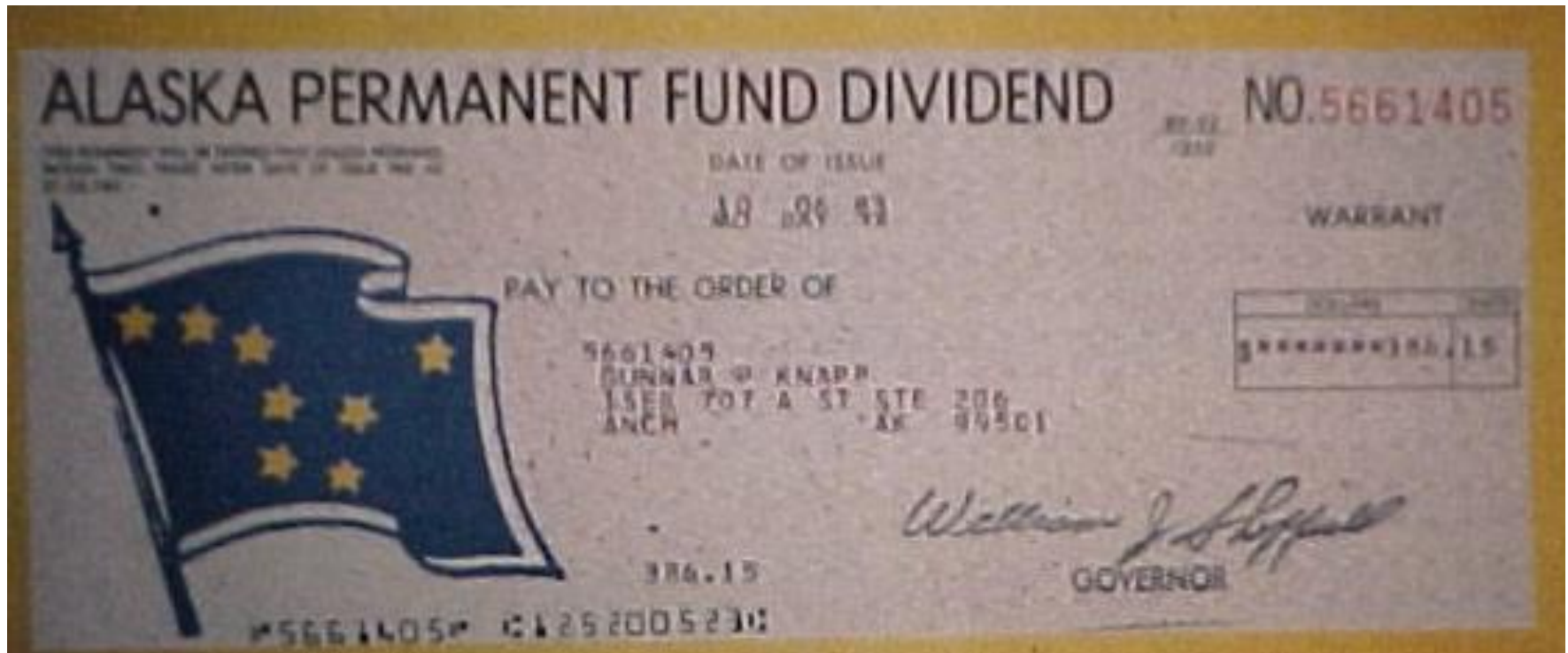


Until FY 2017, we used approximately half of the earnings for dividends and saved the other half.



My 1983 Permanent Fund Dividend check, for \$386.16

(The first check paid under the “half of average PF earnings for the past five years” rule)

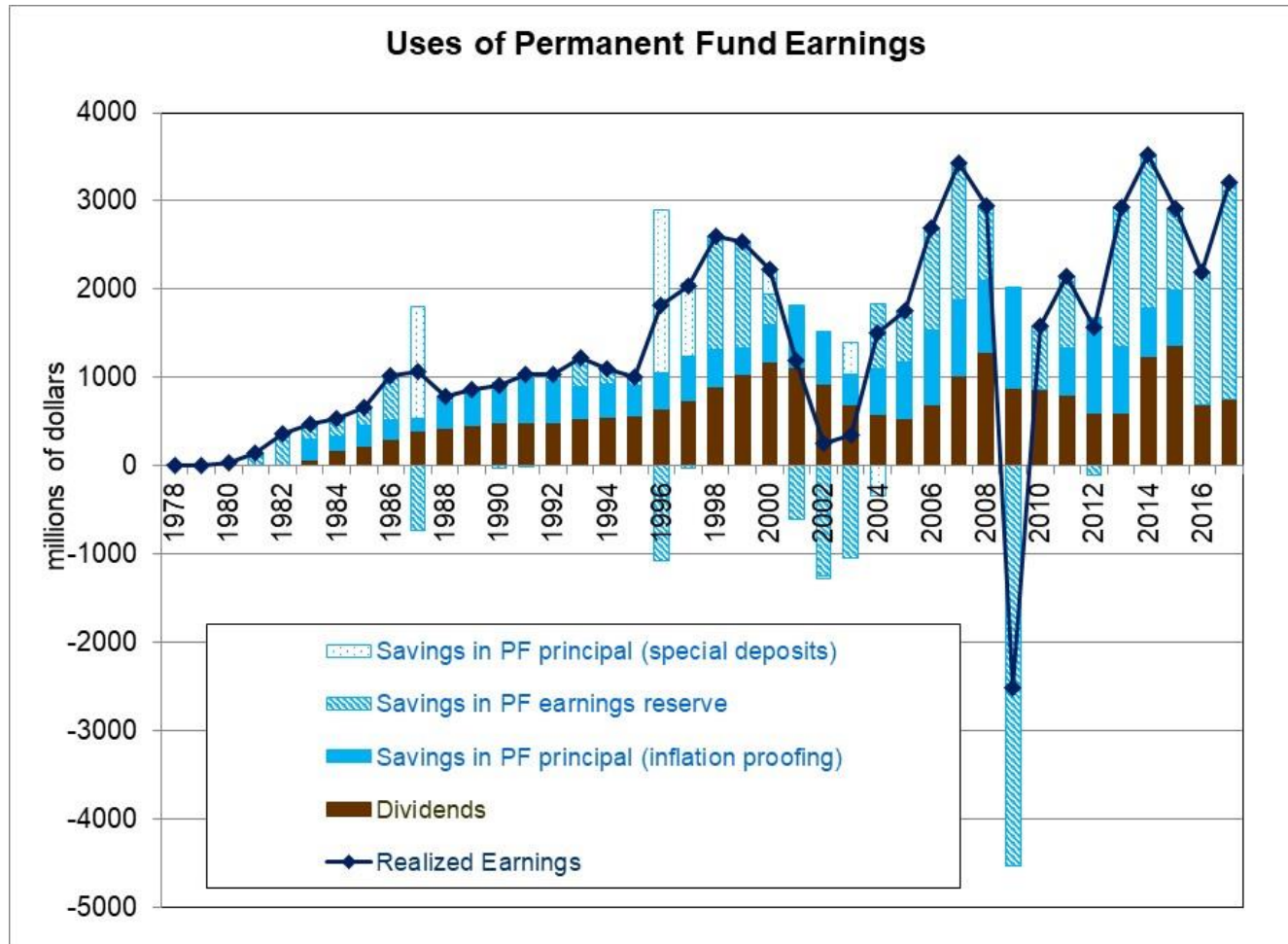


Key fiscal issues which arose as deficits continued:

Should we begin to use PF earnings to help pay for state government?

How much should we use for government?

How much should we use for dividends?



Last year the legislature passed a bill (SB26) which provides for an annual “Percent of Market Value” (POMV) distribution of Permanent Fund Earnings which the legislature may spend for government or dividends.

Uses of Alaska Revenues: Traditional and New

	Traditional (before FY19)	New (after FY19)
Oil revenues	Government	Government
Other traditional revenues		
PF earnings	Dividends Total distribution = 1/2 of average earnings for the past 5 years	Government & Dividends Total distribution = 5% of average value over the past 5 years

Every year the Legislative Finance Division prepares a very complicated “Fiscal Summary” to summarize state spending and revenues.

State of Alaska Fiscal Summary--FY19 and FY20 (Part 1)

(\$ millions)

	FY19 Budget						FY20 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	\$	%
REVENUE	5,421.7	1,045.8	6,467.5	746.4	3,995.8	11,209.6	5,308.0	921.5	6,229.5	798.4	3,741.1	10,769.0	(113.7)	-2.1%
Unrestricted General Fund Revenue (Spr. 19 Forecast) (1)	2,683.4	-	2,683.4	-	-	2,683.4	2,303.6	-	2,303.6	-	-	2,303.6	-	-
Royalties Beyond 25% Constitutional Dedication (2)	-	-	-	-	-	-	71.3	-	71.3	-	-	71.3	-	-
POMIV Payout from ERA for Public Services (3)	1,699.5	-	1,699.5	-	-	1,699.5	2,036.6	-	2,036.6	-	-	2,036.6	-	-
POMIV Payout from ERA for Dividends (3)	1,023.5	-	1,023.5	-	-	1,023.5	896.5	-	896.5	-	-	896.5	-	-
Carryforward, Repeals, and Reappropriations (4)	15.3	30.4	45.7	2.0	0.5	48.2	-	-	-	-	-	-	-	-
Restricted Revenue (5)	-	1,015.4	1,015.4	744.4	3,995.2	5,755.0	-	921.5	921.5	798.4	3,741.1	5,461.0	-	-
APPROPRIATIONS														
TOTAL OPERATING APPROPRIATIONS	4,643.0	893.9	5,536.9	666.5	2,797.3	9,000.6	4,180.3	880.7	5,061.0	726.9	2,718.9	8,506.8	(462.7)	-10.0%
Agency Operations	3,985.9	822.0	4,807.9	612.9	2,732.3	8,153.1	3,727.9	817.6	4,545.4	621.0	2,682.5	7,849.0	(258.1)	-6.5%
Current Fiscal Year Appropriations	3,955.1	822.6	4,777.8	612.3	2,645.2	8,035.3	3,727.9	817.6	4,545.4	621.0	2,682.5	7,849.0	(227.3)	-5.7%
Agency Operations (Non-Formula)	1,870.0	771.5	2,641.6	580.8	929.9	4,152.2	1,787.8	748.1	2,535.9	590.3	967.6	4,093.9	(82.3)	-4.4%
K-12 Foundation and Pupil Transportation (Formula) (6)	1,269.9	-	1,269.9	23.7	20.8	1,314.4	1,279.8	-	1,279.8	22.0	20.8	1,322.6	9.9	0.8%
Medicaid Services (Formula)	661.2	0.9	662.1	7.3	1,591.1	2,260.4	516.3	0.9	517.2	7.9	1,594.3	2,119.4	(144.9)	-21.9%
Other Formula Programs	154.0	50.2	204.2	-	101.5	305.7	144.0	50.2	194.2	-	99.7	293.9	(10.0)	-6.5%
Revised Programs Legislatively Approved (RPLs)	-	-	-	0.6	1.9	2.6	-	-	-	-	-	-	-	-
Fiscal Notes (FY19 notes are included in MP)	-	-	-	-	-	-	(0.1)	18.3	18.3	0.8	-	19.1	(0.1)	-
Vetoes (non-additive) (7)	-	-	-	-	-	-	(98.1)	(7.1)	(105.2)	(10.8)	(1.8)	(117.9)	(98.1)	-
Duplicated Authorization (non-additive) (8)	-	-	-	778.9	-	778.9	-	-	-	893.8	-	893.8	-	-
Supplemental Appropriations (Agency Operations)	30.8	(0.6)	30.2	0.5	87.1	117.8	-	-	-	-	-	-	(30.8)	-
Statewide Items	657.1	71.9	729.0	53.6	64.9	847.5	452.4	63.1	515.5	105.8	36.5	657.8	(204.7)	-31.1%
Current Fiscal Year Appropriations	614.8	71.9	686.7	53.6	27.9	768.3	452.4	63.1	515.5	105.8	36.5	657.8	(162.4)	-26.4%
Debt Service	200.0	39.8	239.8	47.2	5.2	292.3	122.8	16.5	139.3	40.2	5.2	184.8	(77.2)	-38.6%
Fund Capitalizations	143.7	32.1	175.8	6.4	22.7	204.9	21.7	0.2	21.9	31.4	31.2	84.5	(122.0)	-84.9%
Community Assistance	4.0	30.0	34.0	-	-	34.0	-	-	-	-	-	-	(4.0)	-100.0%
Oil & Gas Production Tax Credits	100.0	-	100.0	-	-	100.0	-	-	-	-	-	-	(100.0)	-100.0%
REAA School Fund	39.7	-	39.7	-	-	39.7	19.7	-	19.7	-	-	19.7	(20.0)	-50.3%
Other Fund Capitalization	0.05	2.1	2.1	6.4	22.7	31.2	2.0	0.2	2.2	31.4	31.2	64.8	2.0	4129.2%
State Payments to Retirement Systems	271.1	-	271.1	-	-	271.1	307.9	-	307.9	-	-	307.9	36.8	13.6%
Shared Taxes	-	-	-	-	-	-	-	33.9	33.9	34.2	-	68.1	-	-
Fiscal Notes (FY19 notes are included in MP)	-	-	-	-	-	-	-	12.5	12.5	-	-	12.5	(101.9)	-
Vetoes (non-additive) (7)	-	-	-	-	-	-	(101.9)	-	(101.9)	-	-	730.8	-	-
Duplicated Authorization (non-additive) (8)	-	-	-	752.7	-	752.7	-	-	-	-	-	-	(42.3)	-
Supplemental Appropriations (Statewide Items)	42.3	-	42.3	-	37.0	79.3	-	-	-	-	-	-	(41.9)	-
Disaster Relief Fund	41.9	-	41.9	-	37.0	78.9	-	-	-	-	-	-	(0.4)	-
Judgments, Claims and Settlements	0.4	-	0.4	-	-	0.4	-	-	-	-	-	-	-	-
TOTAL CAPITAL APPROPRIATIONS	168.0	124.4	292.4	77.9	1,198.5	1,568.8	144.3	37.9	182.2	71.3	1,022.1	1,275.7	(23.7)	-14.1%
Current Fiscal Year Appropriations	147.8	112.8	260.6	76.8	1,109.6	1,447.0	144.3	37.9	182.2	71.3	1,022.1	1,275.7	(3.5)	-2.4%
Project Appropriations & RPLs	147.8	112.8	260.6	76.8	1,109.6	1,447.0	1.5	37.9	39.4	71.3	1,022.1	1,132.9	(146.3)	-99.0%
Direct Appropriations from the Constitutional Budget Reserve (9)	-	-	-	-	-	-	142.8	-	142.8	-	-	142.8	-	-
Capital Vetoes (non-additive) (7)	-	-	-	-	-	-	(31.4)	(2.2)	(33.6)	(6.6)	-	(40.2)	(31.4)	-
Duplicated Authorization (non-additive) (8)	-	-	-	37.4	-	37.4	-	-	-	20.5	-	20.5	-	-
Supplemental Appropriations (Capital)	20.1	11.6	31.8	1.1	88.9	121.8	-	-	-	-	-	-	(20.1)	-
Money on the Street (includes all fund sources) (10)	168.0	124.4	292.4	115.3	1,198.5	1,606.2	144.3	37.9	182.2	71.3	1,022.1	1,296.2	(23.7)	-14.1%
Pre-Permanent Fund Authorization (unduplicated)	4,810.9	1,018.4	5,829.3	744.4	3,995.8	10,569.4	4,324.6	918.6	5,243.2	798.2	3,741.1	9,782.4	(486.4)	-10.1%
Permanent Fund Appropriations	1,023.5	-	1,023.5	-	-	1,023.5	1,140.2	-	1,140.2	-	-	1,140.2	116.7	11.4%
Permanent Fund Dividends from GF	1,023.5	-	1,023.5	-	-	1,023.5	896.5	-	896.5	-	-	896.5	(127.0)	-12.4%
Permanent Fund Dividends from SBR	-	-	-	-	-	-	172.4	-	172.4	-	-	172.4	-	-
Inflation Proofing Deposits to Principal	(942.0)	-	(942.0)	-	-	(942.0)	(943.0)	-	(943.0)	-	-	(943.0)	-	-
Inflation Proofing Deposits from ERA	942.0	-	942.0	-	-	942.0	943.0	-	943.0	-	-	943.0	-	-
Other Deposits to Principal	-	-	-	-	-	-	(4,000.0)	-	(4,000.0)	-	-	(4,000.0)	-	-
Other Deposits from ERA and Royalties	-	-	-	-	-	-	4,071.3	-	4,071.3	-	-	4,071.3	-	-
Pre-Transfers Authorization (unduplicated)	5,834.4	1,018.4	6,852.8	744.4	3,995.8	11,592.9	5,464.7	918.6	6,383.3	798.2	3,741.1	10,922.6	(369.7)	-6.3%
Pre-Transfer Balance to/(from) the CBR (11)	(412.7)	Revenue Covers	92.9%	of Appropriations	(156.7)	Revenue Covers	97.1%	of Appropriations						

For FY17 the fiscal summary included only “traditional” revenue sources as unrestricted general funds used to pay for state government.

	Unrestricted General Funds
REVENUE	1,186.5
Unrestricted General Fund Revenue (Spring 2016) (1)	1,246.4
Carryforward and Repeals (2)	-
Adjustments and Fiscal Notes (3)	(59.9)
Designated General Fund Revenue (4)	-
Other State Funds and Federal Receipts	-

For this fiscal year (FY20) the fiscal summary added “POMV payouts” as unrestricted general funds used to pay for state government.

	Unrestricted General Funds
REVENUE	5,308.0
Unrestricted General Fund Revenue (Spr. 19 Forecast) (1)	2,303.6
Royalties Beyond 25% Constitutional Dedication (2)	71.3
POMV Payout from ERA for Public Services (3)	2,036.6
POMV Payout from ERA for Dividends (3)	896.5
Carryforward, Repeals, and Reappropriations (4)	-
Restricted Revenue (5)	-

This year's total POMV payout is \$2.9 billion:
more than oil and all other traditional revenues combined.

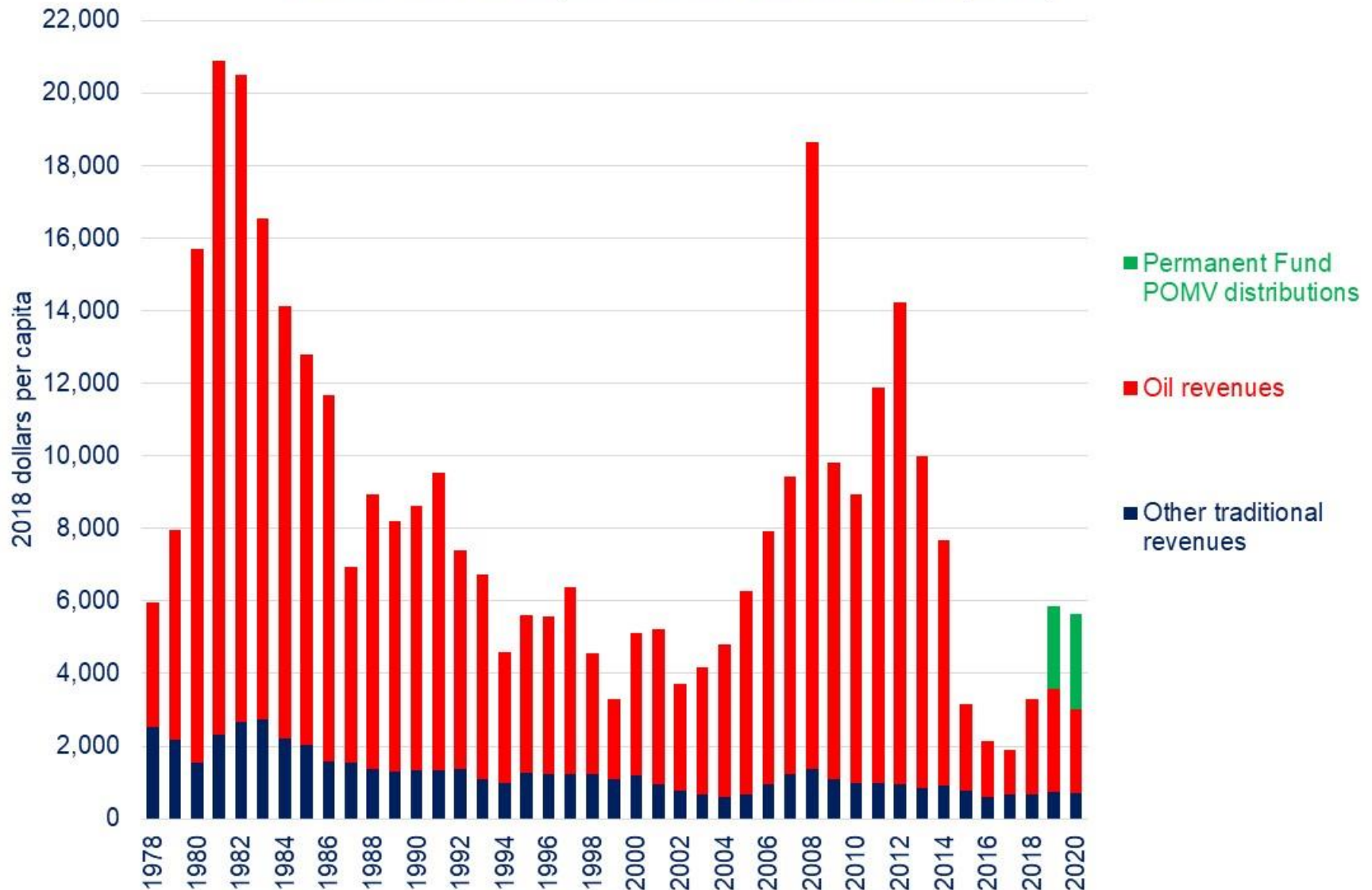
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Carryforward, Repeals, and Reappropriations (4)	-
Restricted Revenue (5)	-

POMV payout:

\$2,303.6 million for government services
+ \$896.5 million for a \$1600 dividend
= \$2,933.1 million total

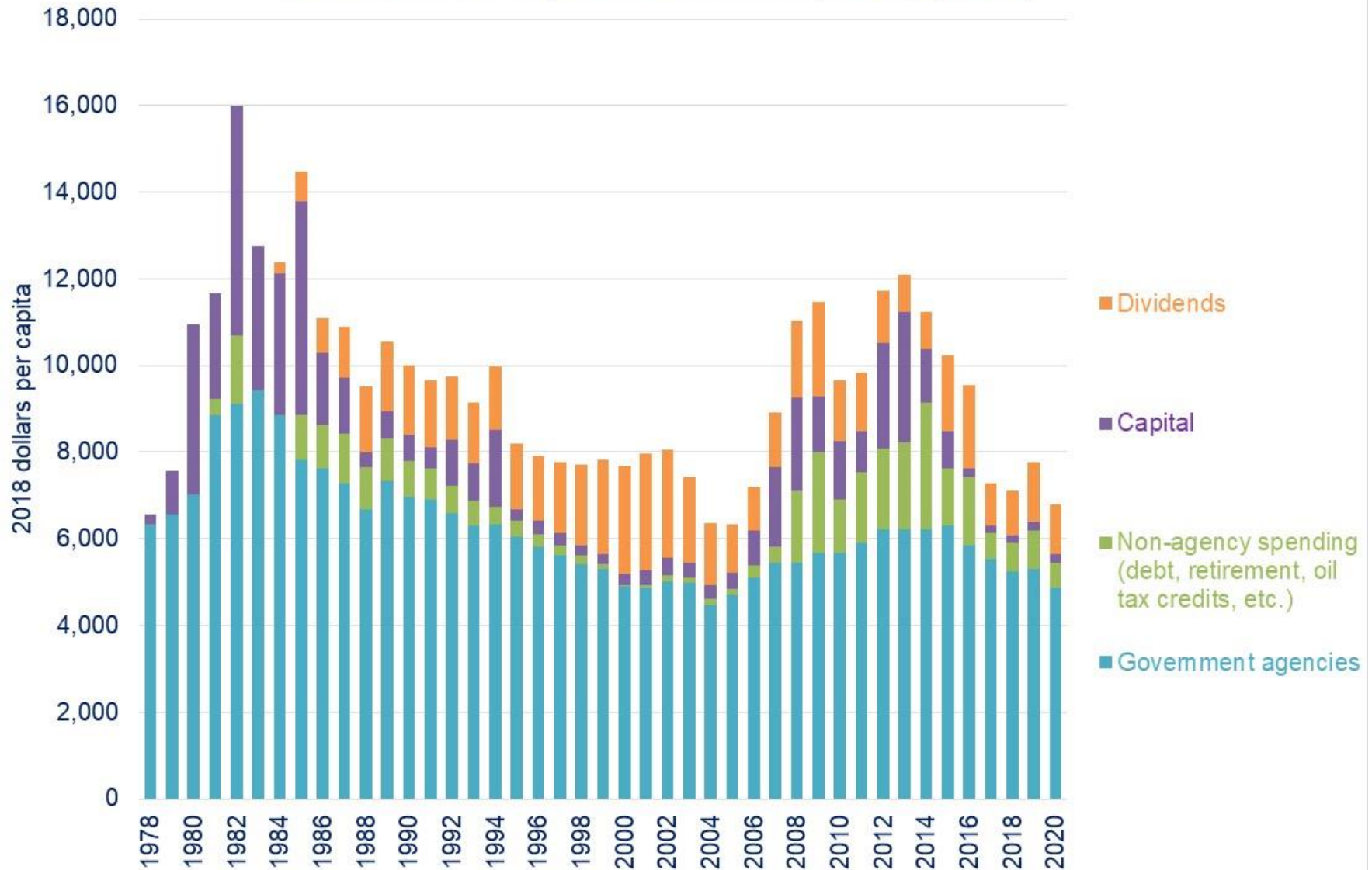
The “new” way of thinking about state revenues —including Permanent Fund POMV distributions.

Alaska Real Per Capita General Fund Revenues (2018\$)



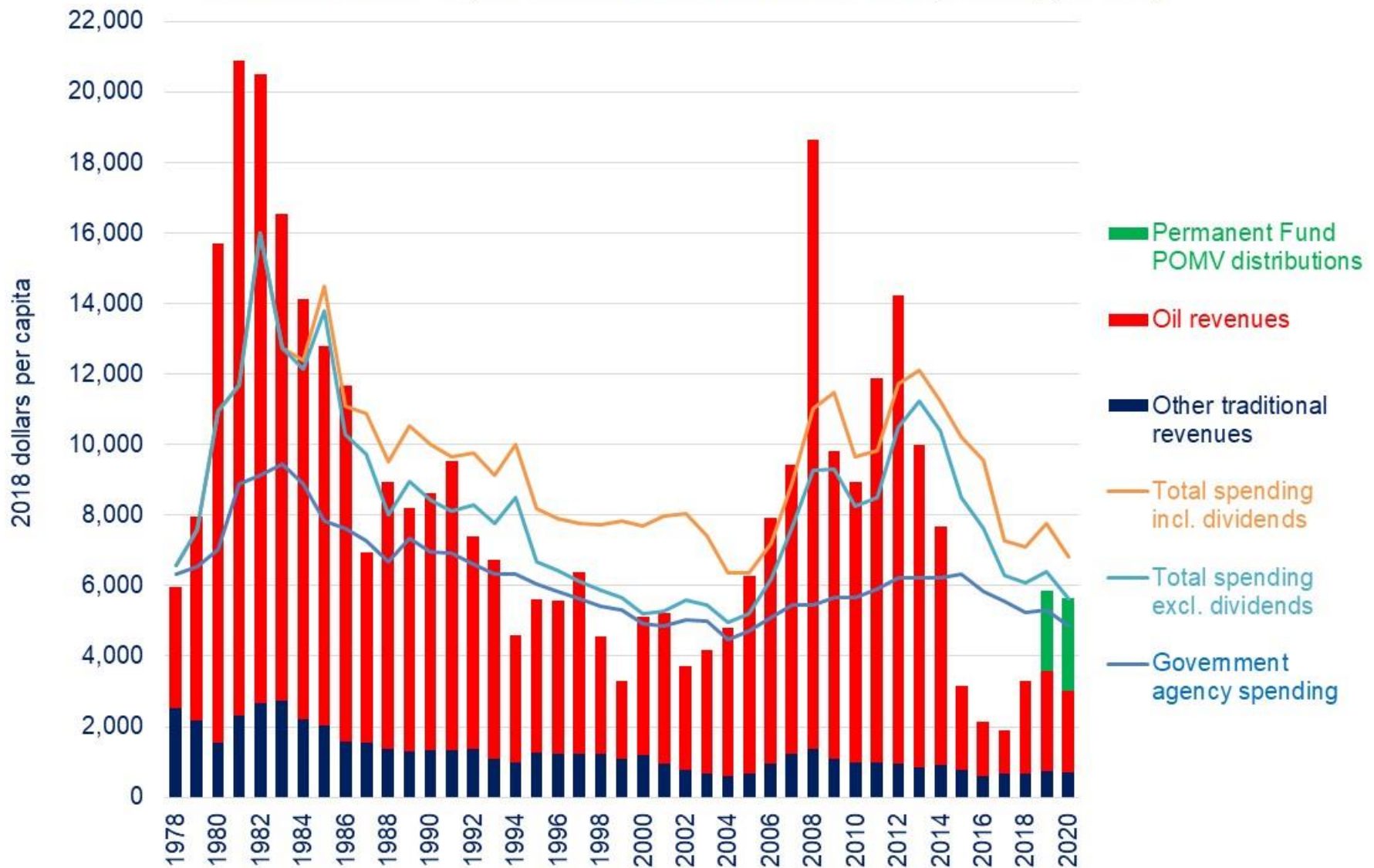
The “new” way of thinking about state spending —including Permanent Fund dividends.

Alaska Real Per Capita General Fund Spending (2018 \$)



Comparing our total revenues (including PF distributions) with our total spending (including dividends)

Alaska Real Per Capita General Fund Revenues and Spending (2018 \$)

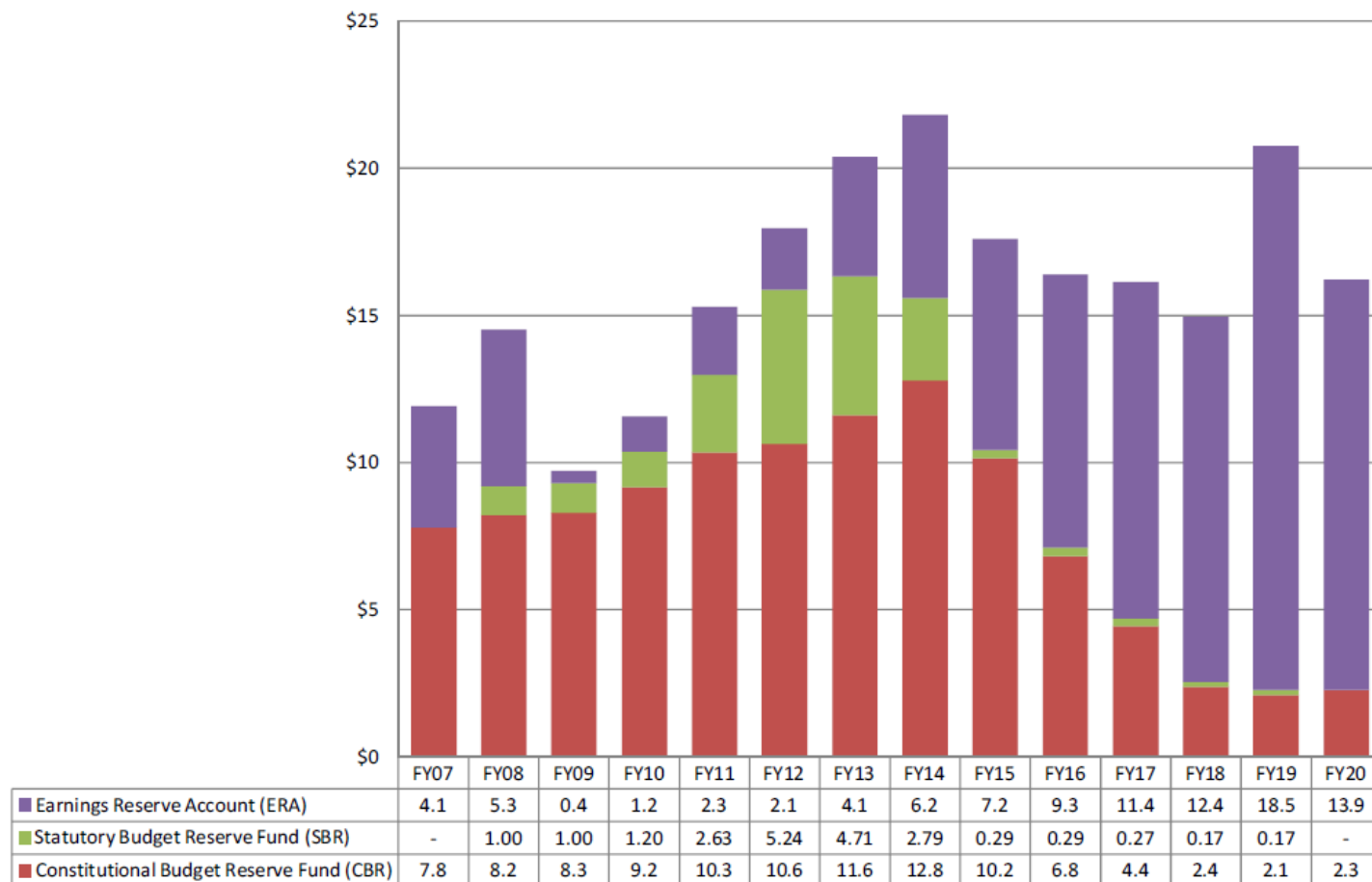


We will still run a deficit this year, even though . . .

- We are using Permanent Fund earnings to help pay for government
- We made significant cuts to government spending
- We paid a much smaller dividend (about \$1600) than the “full” dividend (about \$3000) as calculated by the traditional formula

The good news is that the Permanent Fund earnings have been high enough that our total savings are staying steady. . .

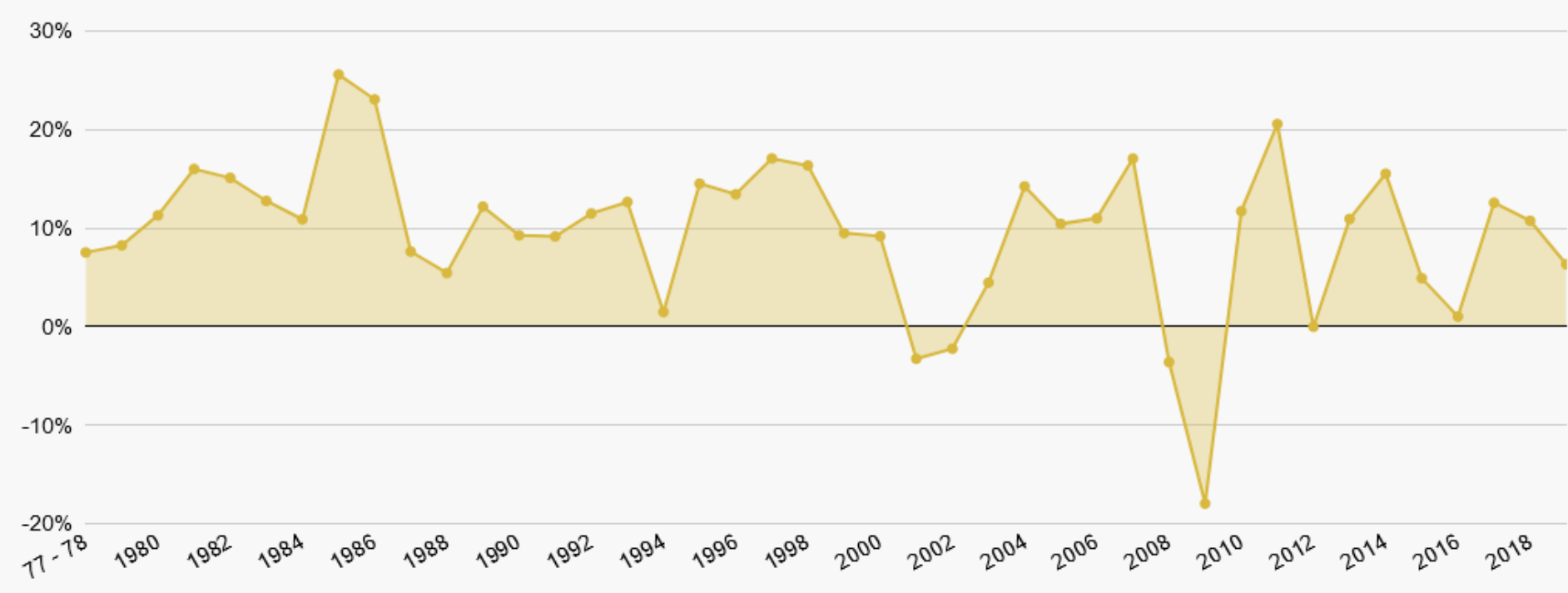
End-of-Year Balances of State Savings Funds and the Permanent Fund Earnings Reserve Account (\$ billions)



But Permanent Fund rates of return and earnings
won't necessarily stay high.

Historically they have been highly variable.

PERMANENT FUND RETURN



Alaska's continuing fiscal challenge:

**If we continue to spend more than our sustainable revenues
we will run out of savings we can use to pay for deficits.**

We face direct tradeoffs between:

- Reducing state spending
- Reducing dividends
- Increasing revenues from broad-based taxes
 - income taxes, sales taxes, etc.
- Increasing revenues from resource taxes
 - oil taxes, fish taxes, etc.

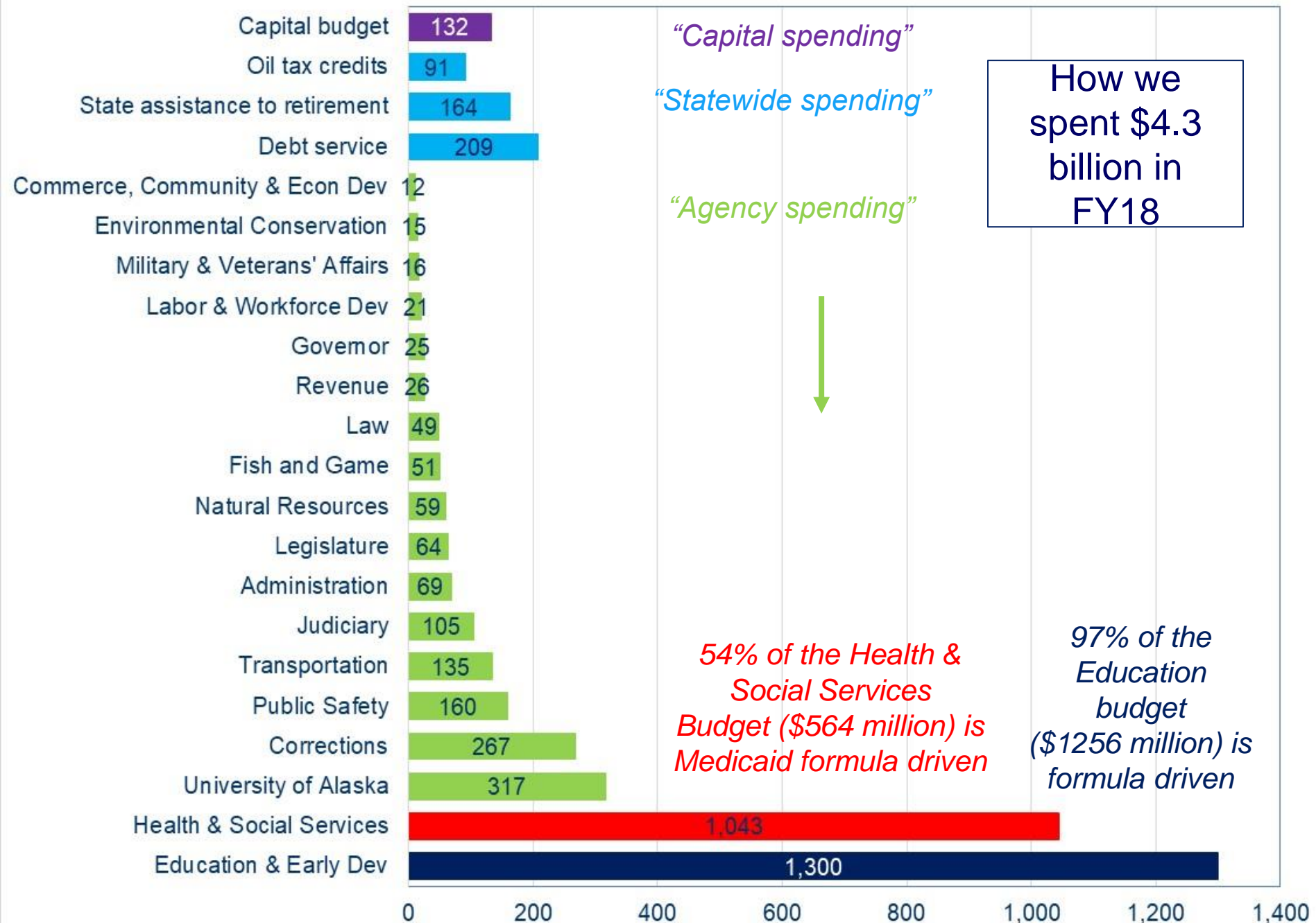
Fiscal option #1 . . .

Reducing state spending . . .

Further reductions to state spending will be difficult because:

- Some kinds of spending can't be cut
 - Debt repayment
 - Retirement obligations
- The easiest cuts have already have been made
 - Capital spending
- There is strong public resistance to further cuts
 - Many Alaskans say “government spending should be cut!”
 - But there is strong resistance to *specific* cuts
- Some kinds of spending will need to increase
 - Retirement obligations
 - Capital spending for deferred maintenance
 - Investments in economic development
- Inflation will increase future costs

Unrestricted General Fund Budget, FY18 (\$ millions)



The first reaction to every revenue crisis:
Cut the budget!



Fiscal option #1 . . .

Reducing state spending . . .

- Cuts aren't real unless
 - You can identify them
 - The legislature can make them
- All of us can point to specific examples of “wasteful spending”
 - That don't mean vastly larger spending cuts are feasible
 - We don't all agree about what is “wasteful”

Fiscal option #2 . . .

Reducing dividends . . .

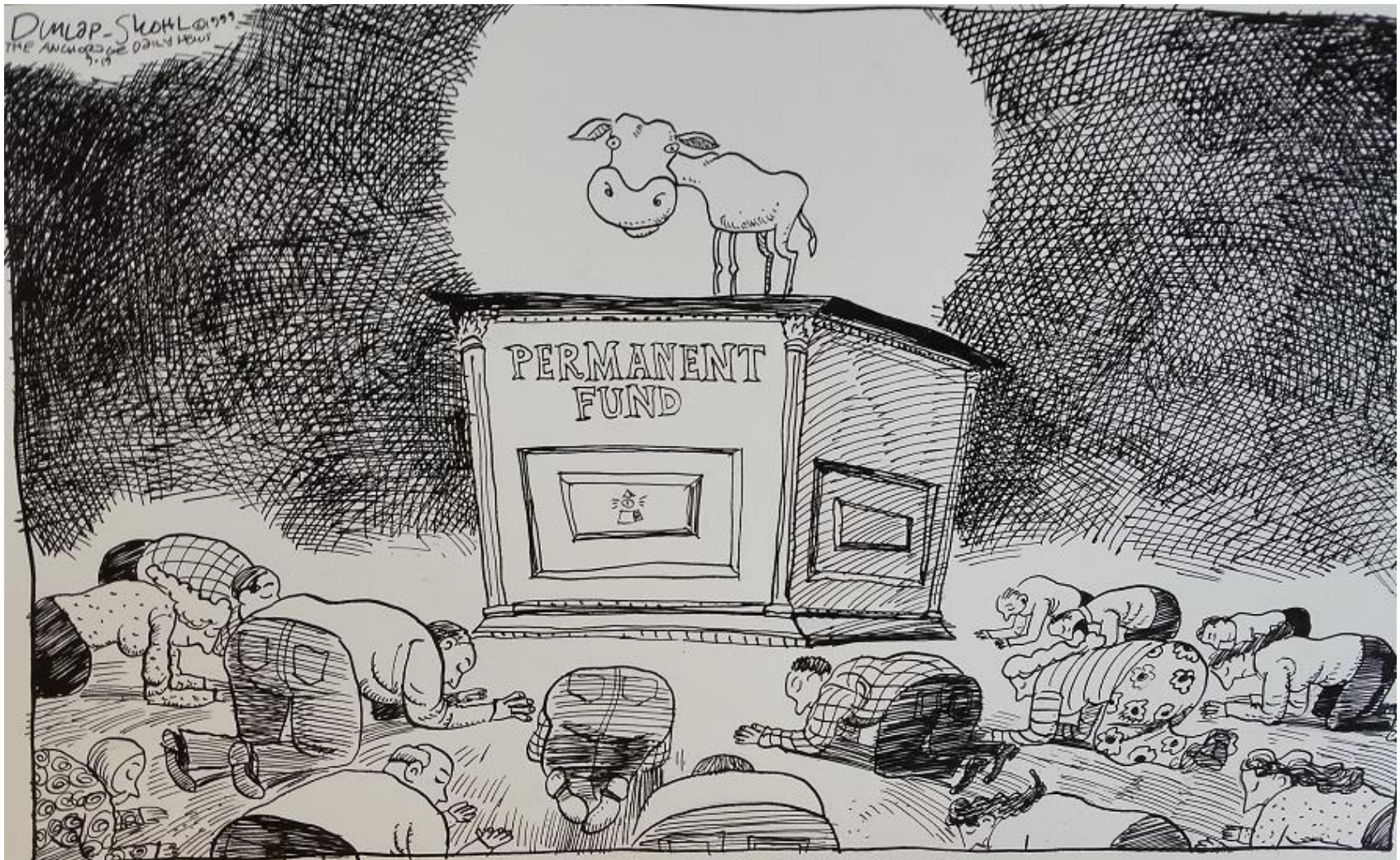
Until recently, it was taboo to talk about cutting dividends . . .



Fiscal option #2 . . .

Reducing dividends . . .

Until recently, it was taboo to talk about cutting dividends . . .



FROM GOLDEN GOOSE TO GOLDEN CALF

Fiscal option #2 . . .

Reducing dividends . . .

Alaskans have widely varying perspectives about dividends—
with widely varying implications for fiscal policy.

- **Dividends are the people's money—not a gift from government**
- Cutting dividends to pay for government spending is not an option
- If we need to pay for spending, we should raise it in other ways
- Dividends give every Alaskan a stake in Alaska's wealth
- Dividends protect the fund from bad investments and “raids”
- Dividends promote a more equitable society
- **Dividends are the government's money and a form of spending**
- The Permanent Fund was not created to pay dividends
- The benefits of dividends have to be balanced against
 - The benefits of other kinds of spending
 - The costs of raising revenues in other ways
- We can't afford to keep paying the same dividends we did when we had more money

Fiscal option #2 . . .

Reducing dividends . . .

Different perspectives have different implications for fiscal policy.

- **Dividends are the people's money—not a gift from government**
- **Cutting dividends to pay for government spending is not an option**
- **Dividends are the government's money and a form of spending**
- **We should reduce dividends to help pay for government**

Implies

- *we have to accept some combination of significantly:*
 - *Lower government spending*
 - *Higher taxes*
 - *Higher drain on our savings*

Implies

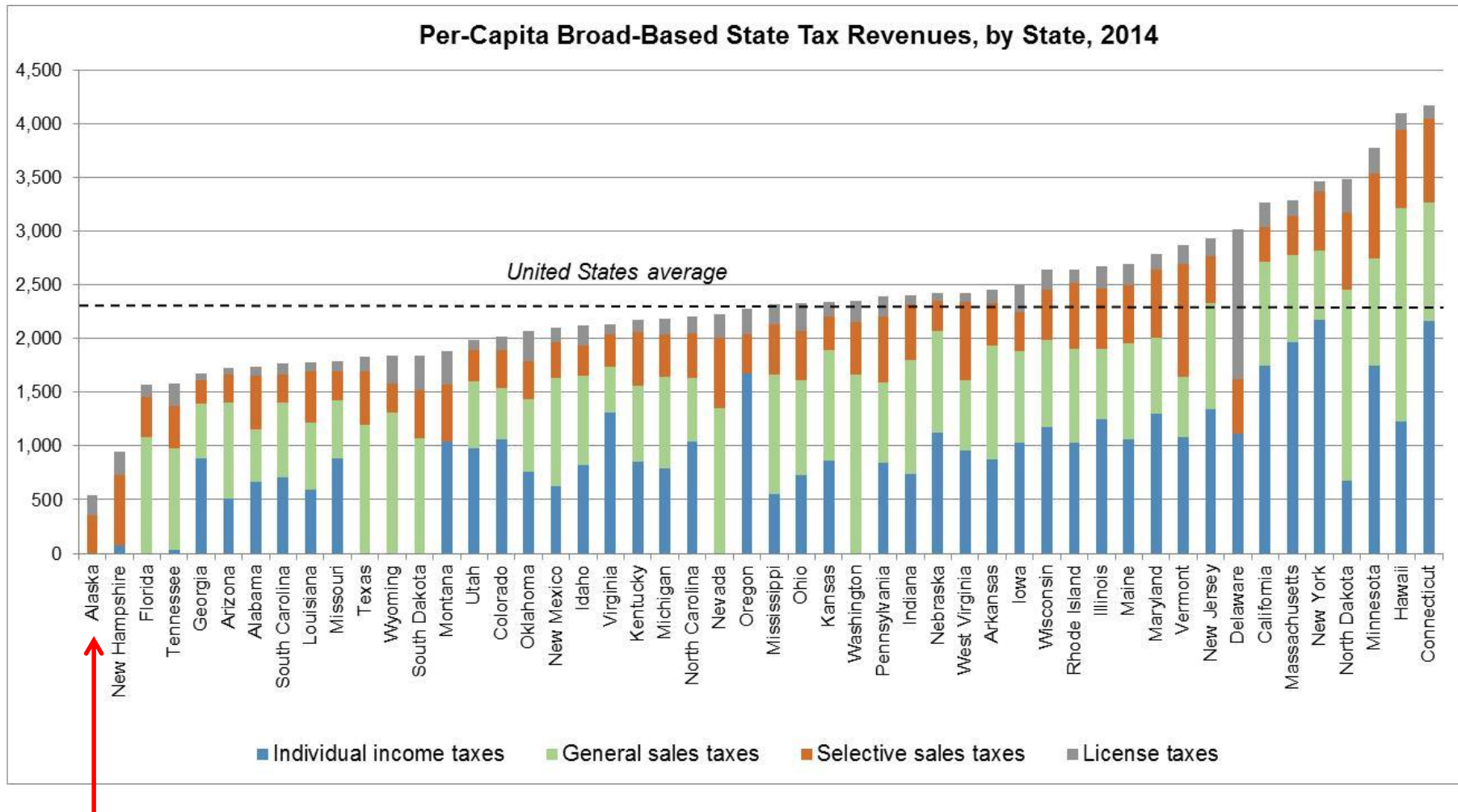
- *We are asking the poorest child to give up as much as the richest millionaire to pay for government—unless we also impose other more progressive taxes*

Fiscal option #3 . . .

Increasing revenues from broad-based taxes . . .

- New broad-based taxes would help to diversify and stabilize our revenues
- Paying income or sales taxes wouldn't kill us
 - Economies function in the other 49 states
 - Reasonable taxes which support important public services help economies
 - We need to get beyond the rhetoric that taxes destroy jobs
- Taxes require careful thought and take time to implement
 - If we think we *might* need new revenues, we should be talking about them now
- People pay more attention to spending when they pay taxes
- It's not economically healthy for government and citizens to help pay for services they receive
 - It creates dependency
 - Growth doesn't pay for itself

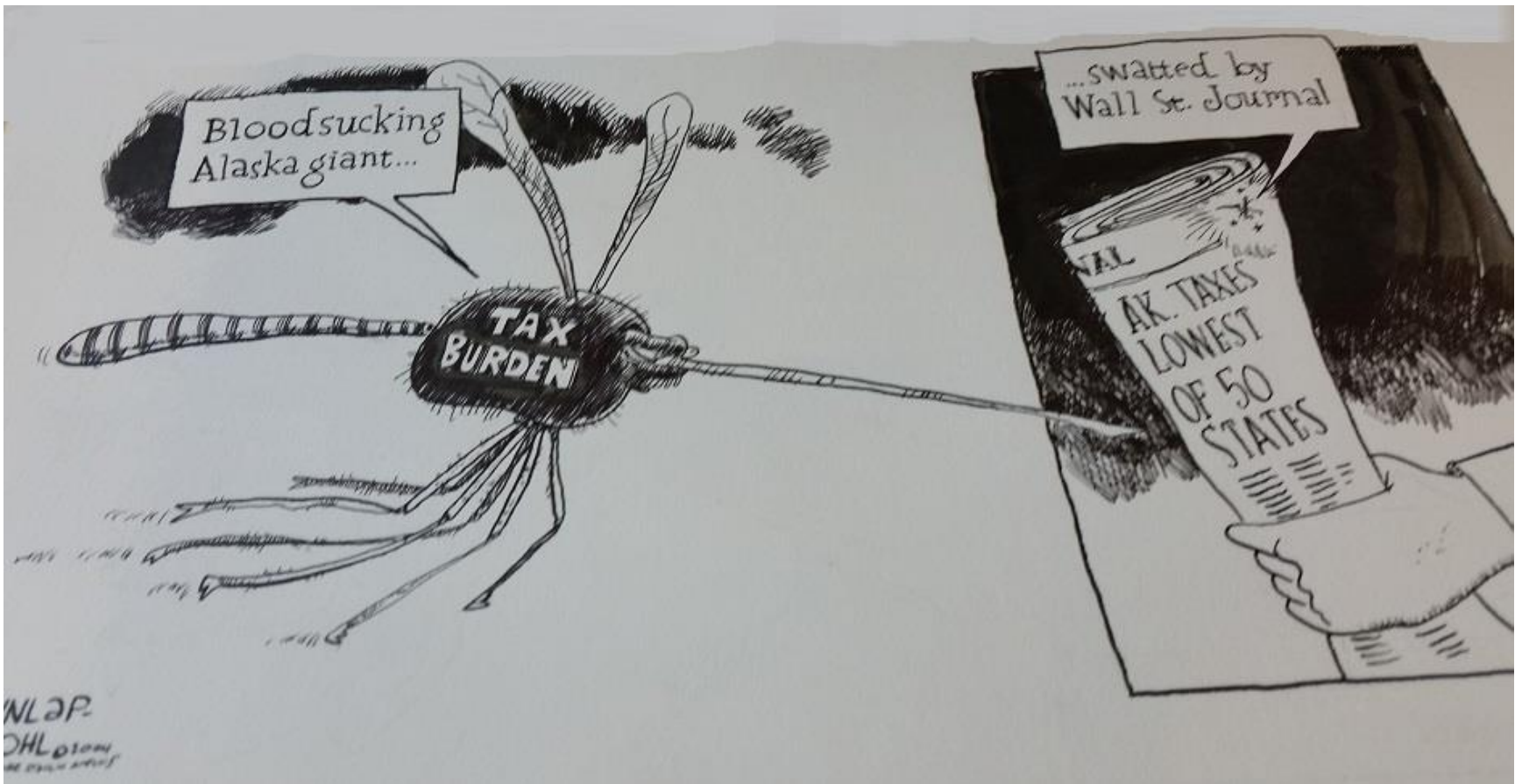
Alaskans pay much lower broad-based state taxes than residents of any other state.



Alaska

Other people don't think we're overtaxed . . .

2004



The “Alaska Disconnect”

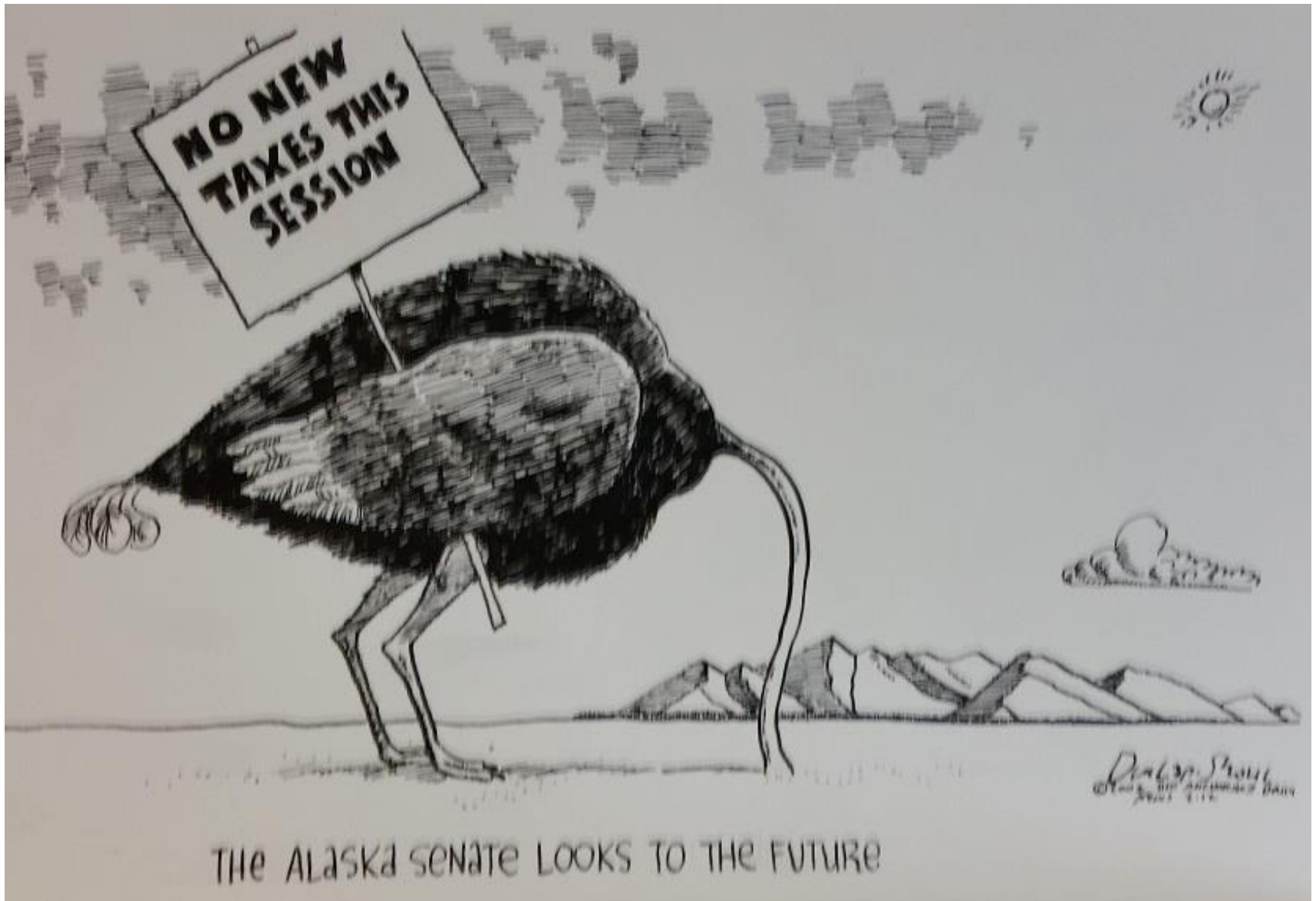
Alaska’s fiscal structure—specifically the fact that Alaskans do not pay any significant broad-based taxes—leads to a problem which has become known as the “Alaska Disconnect.”

If economic developments creates more jobs, Alaska’s population grows. As the population grows, Alaskans need more schools and teachers for their children and the other services that state and local governments provide.

Although the new Alaskans pay local sales and property taxes which support local services, they don’t pay broad-based state taxes to cover the cost of state-funded services such as education and roads.

The new jobs create new costs for the state but not corresponding new revenues. As a result, except for oil development (which pays high state taxes), many kinds of economic growth make the state’s financial situation more rather than less difficult.

But so far, we have not been willing to tax ourselves.



Fiscal option #4 . . .

Increasing revenues from resource taxes . . . (particularly oil)

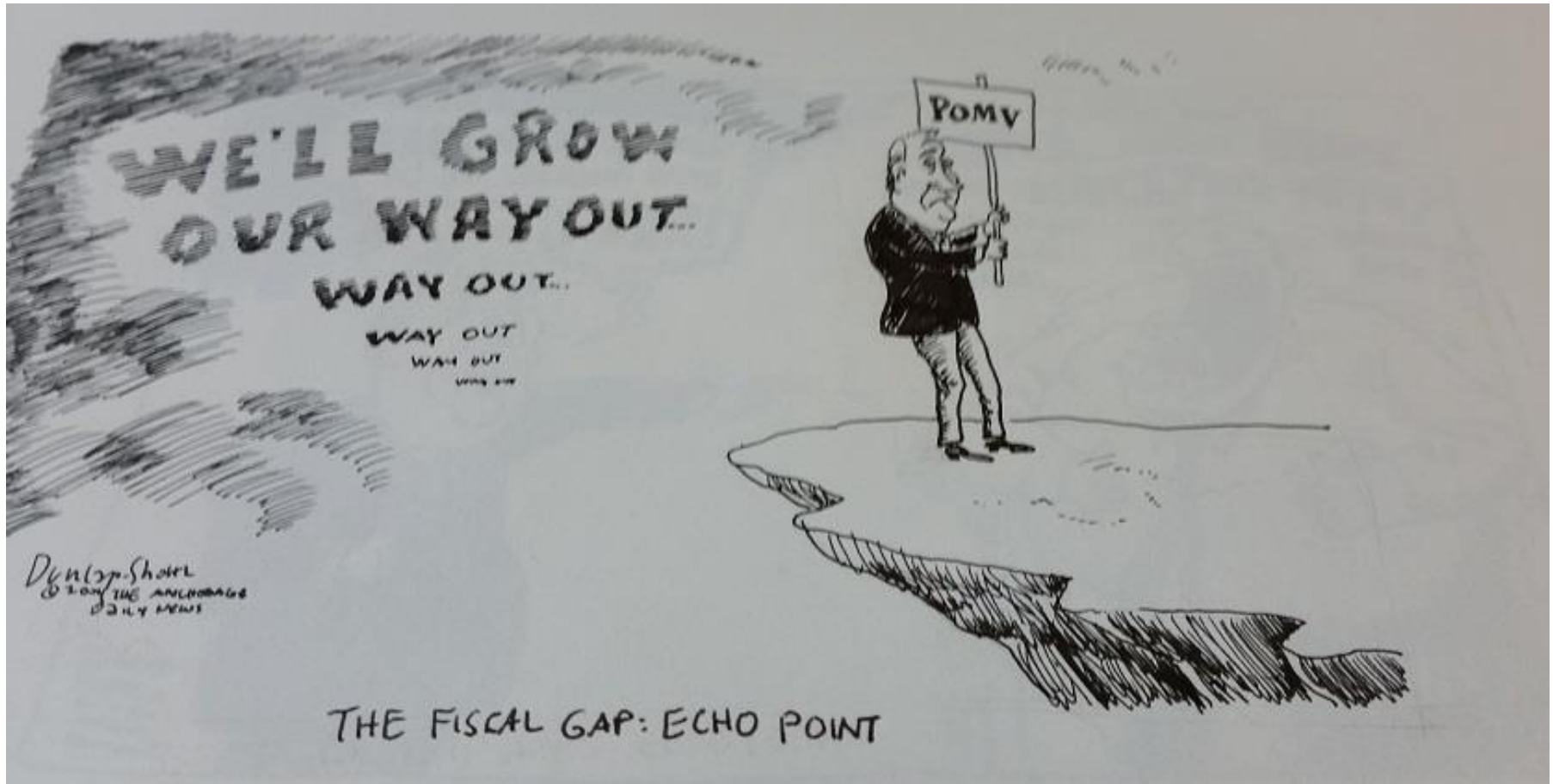
WE COULD:

- Many argue that we aren't getting our "fair share"

BUT THERE ARE RISKS:

- The devil is in complex details of how resources are taxed
- Profitability of Alaska resources is unclear
- Would reduce competitiveness of Alaska for resource investment
- Would increase uncertainty about Alaska development costs

Always popular:
The magic solutions



Be skeptical of “simple” solutions to our fiscal challenge.

We shouldn't take any advocates of any fiscal choices seriously unless they can present a full fiscal plan

- *Based on prudent assumptions about:*
 - future oil revenues
 - future investment revenues
- *With clearly defined choices about:*
 - government spending
 - dividend spending
 - new revenues
 - changes in our total savings
- *Which:*
 - Add up mathematically
 - Are politically feasible

Roles of state and local governments . . .

- A credible fiscal plan has to work not only for state government but also for local governments.
- Our state government pays for many of the services local governments pay for in other states.
- We could cut state government spending by making local governments responsible for more government services and cutting support for local government.
 - But that would drive up local government costs and taxes

Economic impacts of our fiscal choices: what matters?

- What are their short-term economic impacts?
- How fair are they in how they affect different Alaskans today?
- What are their long-term economic impacts?
- How might they influence how Alaskans engage with government?

Fundamentally, our fiscal choices are about
what kind of state we want
and what kind of future we want for Alaska.

2001

Addressing our fiscal challenge will require leadership.

