

**Alaska's Operating Budget:
Critical Crossroads, Choices, and
Opportunities**

Commonwealth North

February 25, 2015

Why Just Study the Operating Budget?

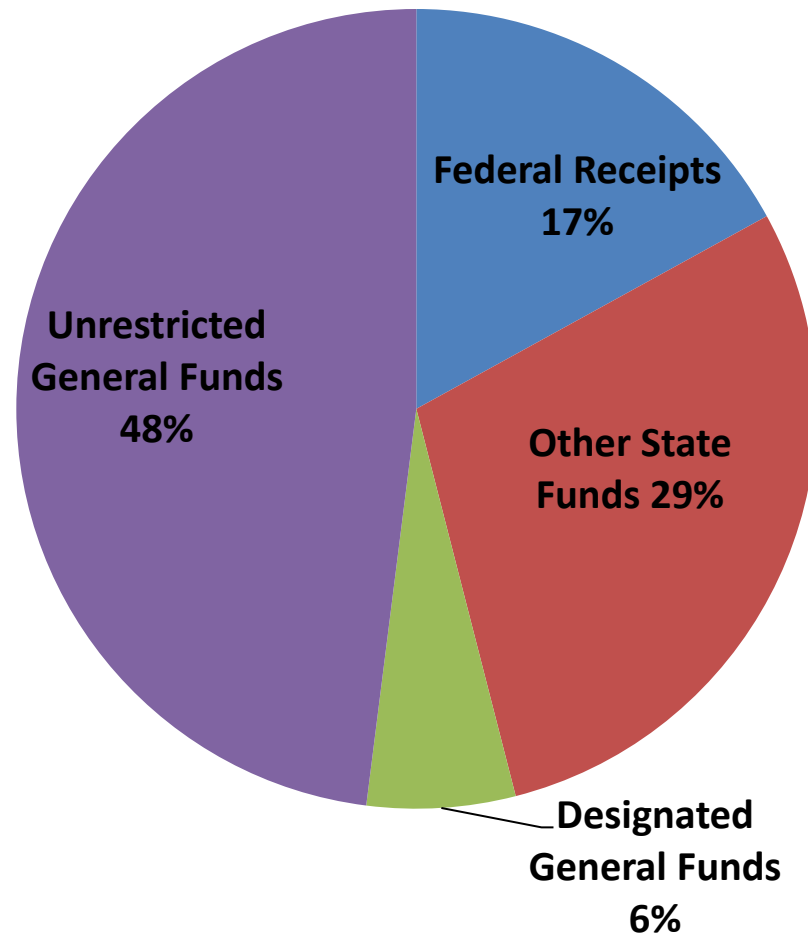
- Recurring obligations
- Increased 105% over 10 years
 - Inflation increased 30%
 - Population increased 11%
- Strong spending lobby that protects spending
- Limited public scrutiny beyond bottom line numbers

Bottom Line Recommendations

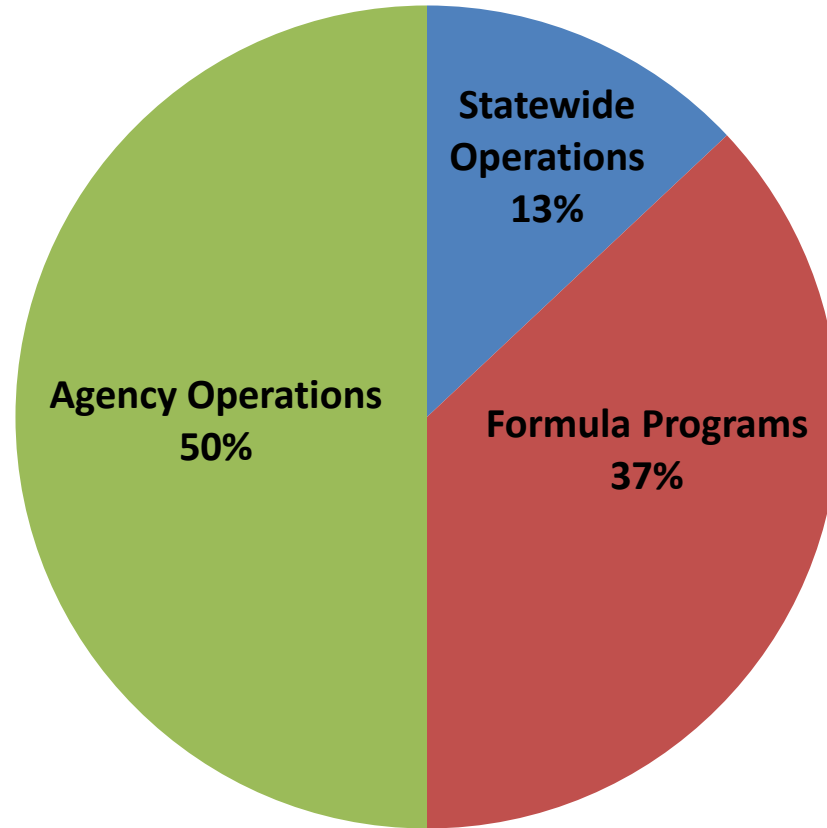
- #1. All programs/spending must be examined
- #2. All current revenue needs to be available to ensure priority services are funded
- #3. Reform budget practices that inhibit achieving #1 and #2

FY 15 Revenue Sources

\$11.6 Billion



FY 15 Operating Budget **\$6 Billion GF**



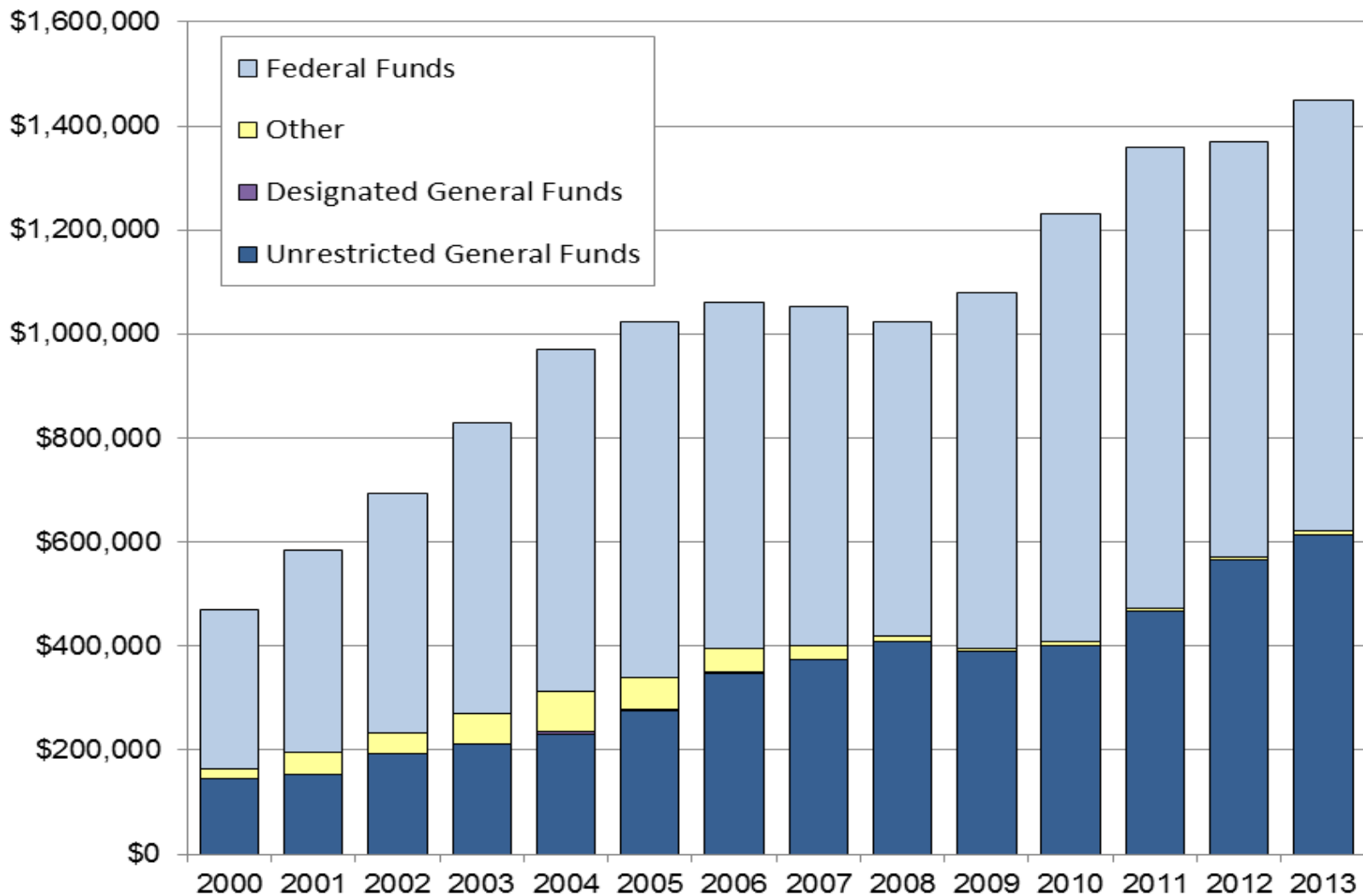
Examine All Spending – Including Formula Programs

Department	State Funds	Federal
DHSS	\$905 million	\$1.1 billion
Education	\$1.3 billion	\$21 million
Commerce	\$45 million	\$11 million
Administration	\$2.1 million	
DMVA	\$0.6 million	
Total	\$2.3 billion	\$1.1 billion

Cost Driver: Medicaid

- Serves low-income, elderly, disabled population
- State provides all optional services
 - Mandatory Services \$933 million
 - Optional Services \$481 million
- Unlike other states, Alaska has not implemented substantial reforms
- Reform is vital for services to continue

Historical Medicaid Expenditure by Fund Source (in thousands)



Recommendations

Immediately get Medicaid reforms underway to ensure the state can continue to provide services to those most in need.

All formula-driven programs must be reviewed in terms of policy goals, results being achieved, and cost effectiveness.

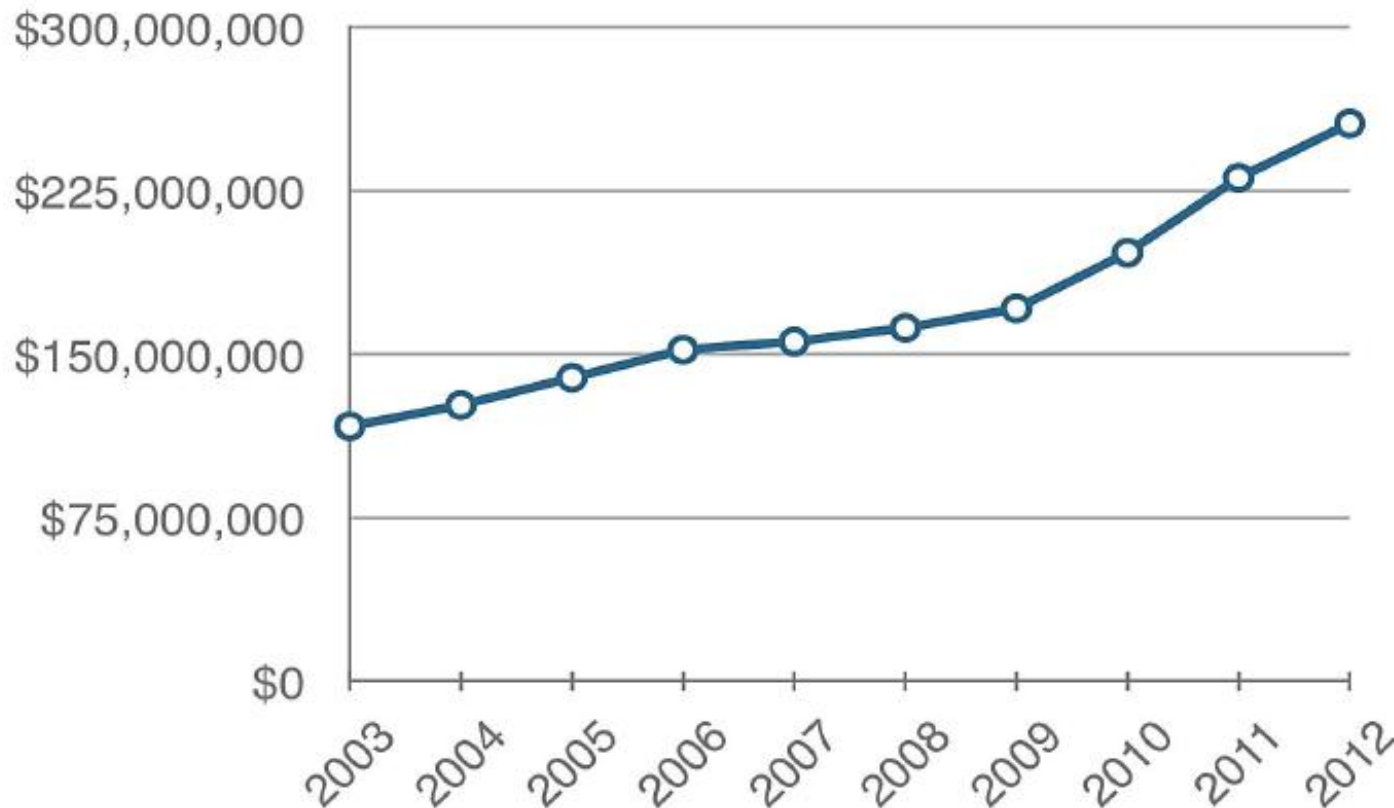
Challenge of High Health Care Costs in Alaska

- Alaska's costs are among the highest:
 - Commercial health care premiums are about 30% higher than the average
 - Commercial hospital reimbursement is about 37% higher
 - Average hospital costs are about 38% higher
 - Physician reimbursement is about 50% higher; for commercial payers this increase is about 69%.

Budget Cost Driver: Agency Health Care Costs

- Agency Operations - \$935 million in FY 15
 - Retirees \$492 million
 - Active employees \$372 million
 - Inmates \$44 million
 - Workers Comp \$27 million

STATE COSTS FOR ACTIVE EMPLOYEE HEALTH INSURANCE

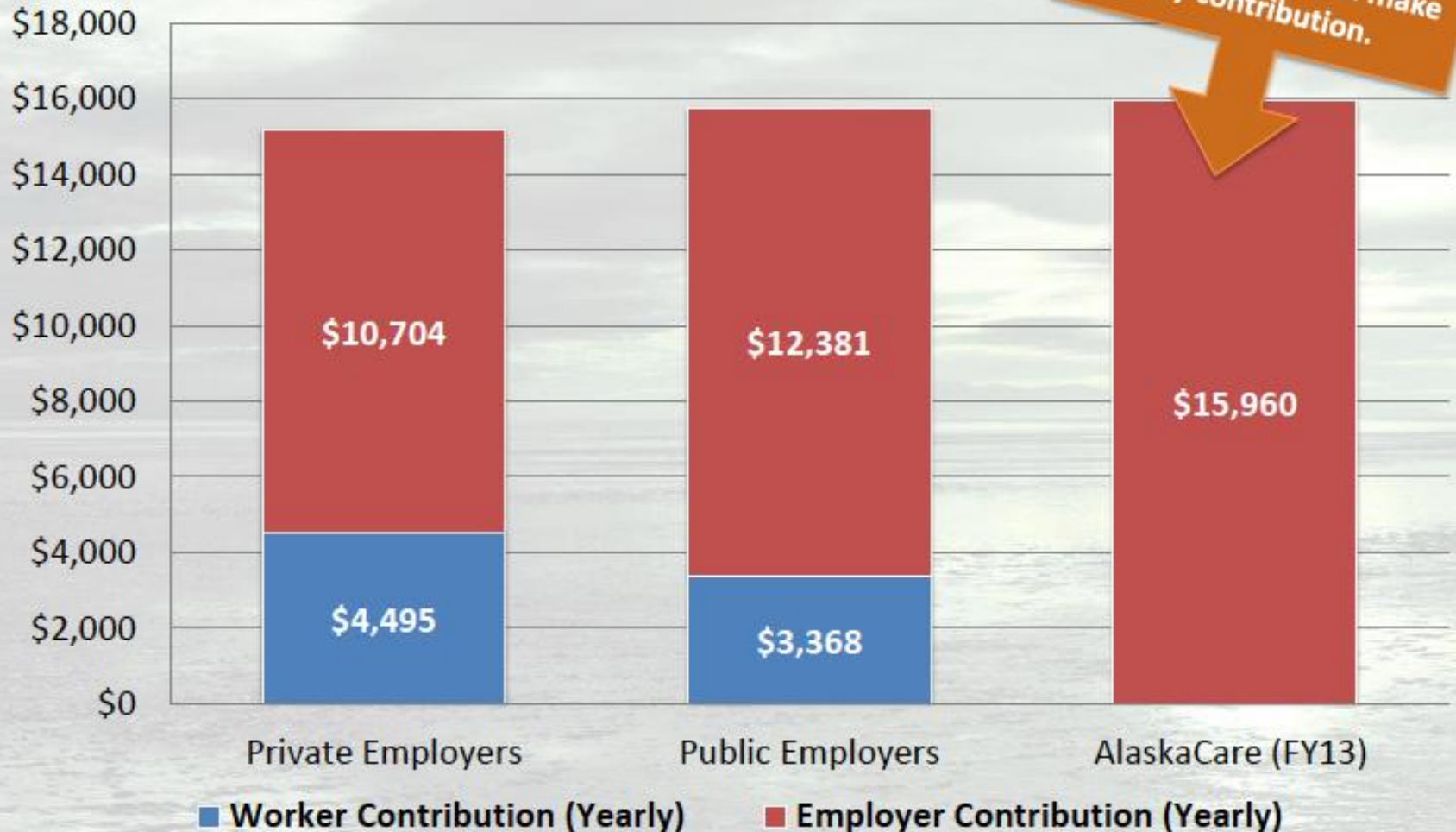


- State employee health insurance costs have more than doubled in the past decade, from \$117mm in 2003 to \$256mm in 2012.
- The population-adjusted increase is approximately 7%/year.

US EMPLOYER & EMPLOYEE CONTRIBUTIONS

Worker and Employer Premium Contributions for Family Coverage / Economy Plans (2012)

Participants in the economy plan don't make any contribution.



Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 2012.

Cost Driver: Employee Annual Salary Increases

- Cost of salary increases
 - \$53 million in current year
 - 1% COLA (contractual) \$25 million
 - Merit Increases (statute) \$28 million
- Next Year
 - COLA is 2.5% for largest unions
 - Merit increases continue unless statute change

Recommendation

Administration, unions re-open negotiations to identify short and long-term savings in personnel and benefit costs

Revenue: “Earmarks” Alaska Style

- Alaska’s Constitution prohibits dedicated funds
- Instead, Alaska has designated funds
 - Fund sources
 - Reserves

Earmarks: Designated Fund Sources

- Certain revenue placed in separate buckets
 - “Designated GF” bucket - \$770 million
 - “Other State Funds” bucket - \$3.1 billion
- By practice budgeters focus on pure general fund spending that results in:
 - Less scrutiny of programs funded by earmarked revenue
 - Earmarked revenues are unavailable to fund highest state responsibilities

Earmarks: Designated Reserves

Designated Reserves	FY 15 Projected Year End Balance
Alaska Capital Income Fund	\$13.1
AK Higher Education Investment Fund	\$443.8
Public Education Fund	\$1,261.1
Revenue Sharing Fund	\$172.0
PCE Endowment	\$902.2
Total	\$2,792.2

(in million\$)

Recommendation

Ensure all current revenue is
available to fund highest priorities
by placing all state revenue in the general fund
unless external legal restrictions

Spending: Ensure Value for Dollars Spent

- Shift focus from incremental changes to identification of appropriate and effective services
 - Constitutional requirement?
 - If so, how effective is the program—what are the results?
 - What’s the cost to deliver those results?
 - Is the State the only entity that can provide the services?

Recommendation

Undertake in-depth review of programs that examines effectiveness and appropriateness and engage citizens in these reviews

Report results to citizens and use data to inform budget decision-making

Management Review

- Governors Hammond and Hickel initiated reviews to identify organizational and management efficiencies

Recommendation

Governor establish citizen-led commission to undertake such a review

Implementation Hurdles

- Recognize powerful spending lobby protects every dollar

Recommendation

Establish a process similar to BRAC to implement package of recommendations that will be necessary to re-size state programs

Engage Alaskans

- Important that Alaskans understand the problem before they will be willing to accept solutions
- Engage Alaskans through dialogue
 - Very different from customary 3-minute Town Hall testimony
 - Way to advance understanding of the challenges
 - Citizens identify choices they would make
 - Serves as input to decision makers

Recommendation

Governor and Legislature co-sponsor series of dialogues in which citizens better understand the challenge and through which they provide input on the choices they believe should be made.

Budget Practices & Process

Recommendations - Governor

- Governor's Budget Development
 - Citizen panels provide input into Governor's proposed budget
 - Governor moves up budget submission to Nov. 15
 - Provide Legislature more time

Budget Practices & Process

Recommendations - Legislature

- Revenue Limit
 - Establish limit on savings used in any one year
 - Provides additional pressure for spending reductions
 - Prolongs availability of savings
- Deposit all savings in statutory budget reserve
 - Removes $\frac{3}{4}$ vote requirement to access Constitutional Budget Reserve

Budget Practices & Process

Recommendations - Legislature

- Create Joint Ways & Means Committee
 - Establish revenue limit by defining, through resolution, amount of savings and other revenues available to fund next budget
 - Review revenue forecasting for reliability

Budget Practices & Process

Recommendations - Legislature

- Increase time for budget work
 - Return to Constitution's 120-day session
 - Increase interim work on budget
 - Special session(s) devoted to budget work if necessary
- Implement contingency plan for mid-year savings when significant drop in revenue

In the Meantime, Buy Some Time . . .

- Legislature strategically uses its power of appropriation
 - “Short fund” next year’s budget by approving 7 months of funding at a substantially reduced level
 - Provides time for further review of programs
 - Statewide dialogue with Alaskans about choices
 - Next session Legislature evaluates program changes and approves funding
 - Decisions are informed by program evaluation work and citizen input
 - Provides management flexibility through appropriation structure

Then There's Politics . . .

- Each recommendation hits up against some political obstacle
- This time really is different
 - Dramatically higher recurring obligations
 - Lowest oil production
 - Sizeable savings
- Requires deliberative, thoughtful actions to ensure economic stability and appropriate services continue at a level Alaska can afford

Thank You

Study group participants who endured
five months on this subject

Presenters who shared their knowledge,
understanding, and ideas

To Jim and Aaron, CWN Staff

Northrim Bank