Alaska Revenue and Expenditures—FY07-FY17

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Alaska is in the midst of the gravest fiscal crisis in state history: FY16 and FY17 revenue is expected to cover less than 30% of annual expenditures, leaving fiscal gaps that are too large to fill with sustainable draws from reserves. Many citizens believe—thanks in part to information provided by some legislators and various advocacy groups—that government expenditures have ballooned even as revenue has fallen. This paper provides a set of facts that is intended to enlighten the debate about the magnitude and causes of the fiscal crisis.

Figure 1 shows that FY17 expenditures ($4.3 billion) are approximately the same level as in FY07. This comparison—which is not adjusted for inflation or population growth—should moderate claims of out-of-control spending. Perhaps the persistence of the claim is due to belief that the budget growth of FY07 through FY13 continued even after revenue could no longer support that growth.

High oil prices supported rapid expenditure growth from FY07 through FY12; there were budget surpluses in each of those years. The FY13 budget was formulated based on FY12 revenue—remember that the budget for a year is set before the year begins and is based on projected revenue—and did not anticipate a revenue decline. The FY13 deficit was about $900 million.

The FY14 capital budget was cut in response to the FY13 decline in revenue (that some believed would be brief/temporary), but the operating budget continued to grow. Revenue declined far more than the $500 million reduction in spending in FY14, and the resulting deficit of $1.9 billion was sufficient to reverse the rising trend in reserve balances shown in Figure 2.[1]

Again in FY15, a large ($3.1 billion) decline in revenue far exceeded the $1.3 billion reduction in spending. The result was a $3.7 billion deficit, with revenue covering only 38% of expenditures. As shown in Figure 2, the $16.3 billion peak balance of budget reserve funds (in FY13) had fallen to $10.4 billion by the end of FY15. FY15 revenue ($2.3 billion) was less than a quarter of the $10.7 billion peak in FY08.

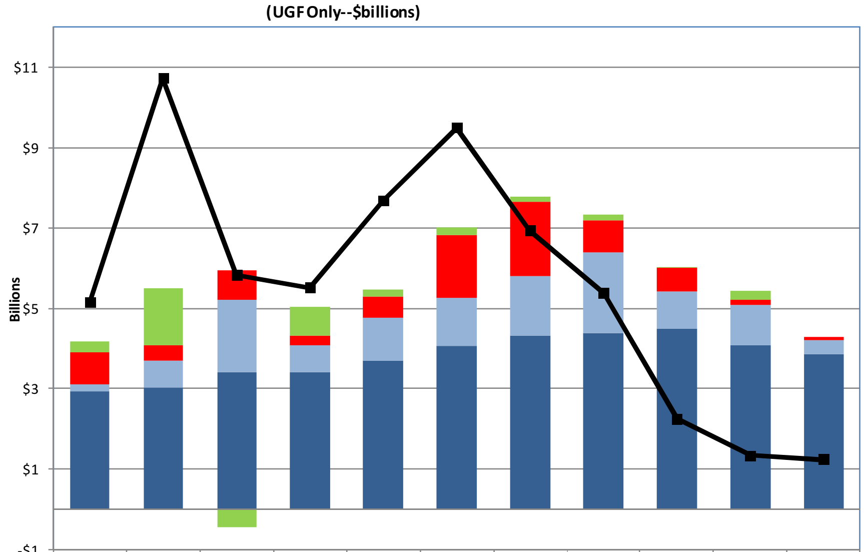
Despite $600 million in expenditure reductions in FY16, the deficit grew to $4.1 billion as revenue declined again (this year by $1 billion to a level of $1.3 billion). Filling the deficit required about one-third of budget reserves. Projections showed that all budget reserves would be consumed in FY18 if annual deficits continued to exceed $3.2 billion. The Governor began a campaign to convince Alaskans that "falling off a budget cliff" in the near future could be avoided only by a combination of further expenditure reductions, increased non-oil revenue, and use of earnings of the permanent fund.

The FY17 budget is about $1.1 billion lower than in FY16, bringing expenditures down to the FY07 level of $4.3 billion. This is $3.5 billion less the $7.8 billion spent in FY13. Despite the series of expenditure

[1] In this case, "reserve balances" refers to the sum of the constitutional and statutory reserve funds (the CBR and SBR, respectively). The earnings reserve account (ERA) is a part of the permanent fund and has not been used to support general fund expenditures.

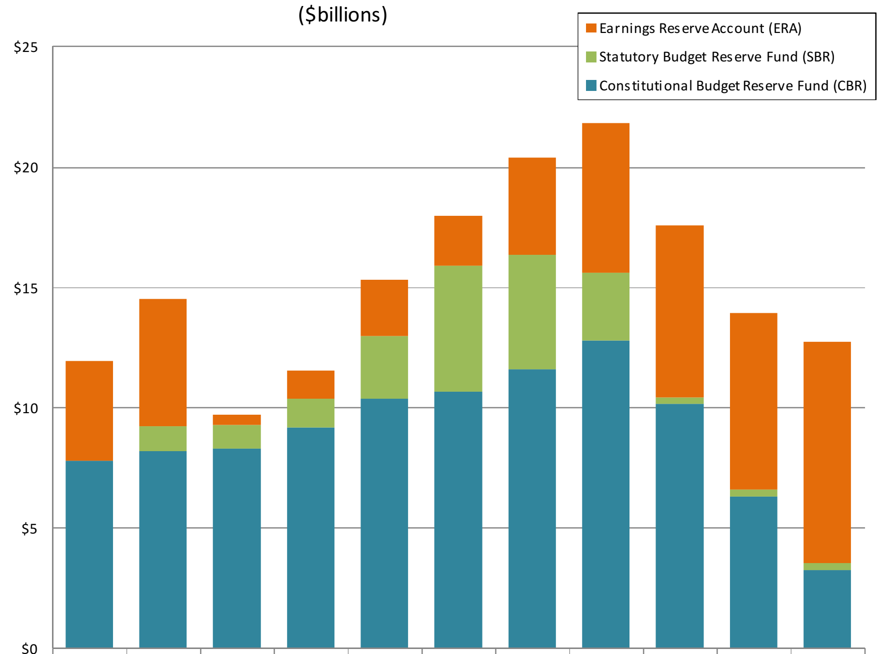
reductions, the FY17 deficit is expected to be about $3.1 billion. As shown in Figure 2, budget reserves are expected to total about $3.5 billion at the end of FY17.

Figure 1: Total Agency Operating Budgets, Statewide Items and Capital Budget Compared to Revenue
(UGF Only--$billions)



	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Supplementals	0.3	1.4	(0.5)	0.7	0.2	0.2	0.1	0.1	0.0	0.2	-
Capital	0.8	0.4	0.7	0.2	0.5	1.6	1.9	0.8	0.6	0.1	0.1
Statewide Items	0.2	0.7	1.8	0.7	1.1	1.2	1.5	2.0	0.9	1.0	0.3
Agency Operations	3.0	3.0	3.4	3.4	3.7	4.1	4.3	4.4	4.5	4.1	3.9
TOTAL BUDGET	4.2	5.5	5.5	5.0	5.5	7.0	7.8	7.3	6.0	5.4	4.3
UGF Revenue	5.2	10.7	5.8	5.5	7.7	9.5	6.9	5.4	2.3	1.3	1.2
Revenue Covers % of Expenditures	123%	195%	106%	110%	140%	135%	89%	74%	38%	25%	29%

Figure 2: End-of-Year Reserve Balances, FY07-FY17
($billions)



	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Earnings Reserve Account (ERA)	4.1	5.3	0.4	1.2	2.3	2.1	4.1	6.2	7.2	7.3	9.2
Statutory Budget Reserve Fund (SBR)	-	1.0	1.0	1.2	2.6	5.2	4.7	2.8	0.3	0.3	0.3
Constitutional Budget Reserve Fund (CBR)	7.8	8.2	8.3	9.2	10.3	10.6	11.6	12.8	10.2	6.3	3.3

The facts are clear:

1. Expenditures have been cut by 44% ($3.5 billion) since FY13 and are at the same level as in FY07 (when there was a surplus of $900 million). Ballooning expenditures are not driving the fiscal crisis.
2. FY17 revenue is about 16% of the average revenue available in FY07 through FY13; revenue covers less than 30% of FY17 expenditures.
3. Without some combination of higher oil prices, further expenditure reductions, revenue enhancements or use of permanent fund earnings, budget reserves will be insufficient to last through FY19.

What numbers were used to produce Figures 1 and 2?

Revenues and expenditures include only unrestricted general funds (UGF). While some may argue that including other state funds and federal funds would provide a more appropriate analysis, that argument is based on measuring the "footprint of government" rather than on measuring the health of the treasury. The purpose of this paper is to present facts about the deficit and the condition of budget reserves. By definition, expenditures of federal and other state funds equal revenue for each category, so that UGF is the only type of funds that directly affect the deficit or reserves.

Reported expenditures reflect appropriation/authorization levels rather than actual expenditure levels. Although using actual expenditures may seem to provide a more accurate historical picture, there are sound reasons to use appropriation levels:

1. There is a two-year lag in reporting actual expenditures, so FY16 and FY17 would not have numbers comparable to earlier years.
2. Actual expenditures may not be reported completely or accurately, and reported amounts have no documented historical ties across fiscal years that would allow auditing the reported numbers.

Should the ERA be excluded from budget reserves?

The earnings reserve account (ERA) has been used to pay dividends and to increase (via transfers) the value of the permanent fund itself. It has not been used for general government support.

The Governor's fiscal plan envisions using permanent fund earnings to support general government. That implies that the ERA could be classified as a budget reserve fund. But Alaskans should be wary of viewing the ERA as a budget reserve account even if the Governor's fiscal plan is adopted.

The ERA balance is—and will continue to be—highly volatile. All budget reserves can be expected to respond to both financial returns and to surplus/deficit conditions, making balances somewhat volatile and unpredictable. The volatility of the ERA is much greater than the balances of CBR and SBR because financial returns to the ERA are highly leveraged.

As an example, assume the CBR and ERA have a balance of $5 billion each, that they are invested identically, and that the total balance of the permanent fund is $50 billion. Now assume a 10% realized loss on investments. The CBR will fall 10% to $4.5 billion. The ERA will accumulate the losses of the entire $50 billion permanent fund, so the ERA balance will fall to zero.

This situation is not a hypothetical example with a remote probability of occurrence. Note in Figure 2 that the ERA balance fell nearly $5 billion in FY09 due to poor financial returns on permanent fund investments. In summary:

- the ERA is a far less reliable source of reserves than the CBR and SBR and
- those concerned with fiscal stability/security should argue for multi-billion dollar reserve balances outside the ERA and/or for excluding the ERA from the definition of budget reserves.