Alaska State Fiscal Policy Agenda

Scott Goldsmith 5/27/10

State government spending exceeds the sustainable level, creating future fiscal and economic problems. However the current high oil price and general fund surplus make it politically impossible to diversify our tax revenue base or rein in spending.

The state has enjoyed 3 previous episodes of extremely high revenues—the 1968 North Slope lease sale, the high oil price regime from 1979 to 1985, and the period of settlement of tax and royalty disputes during the early 1990s. These coincided with the creation of the 3 institutions that define state fiscal policy--the Permanent Fund, the Constitutional Spending Limit and the Constitutional Budget Reserve. The current environment represents another opportunity.

In this environment, state government should work toward implementation of the following policies to put our fiscal house in order.

1) **New Endowment Fund**—Current mechanisms for saving—the Permanent Fund and the Constitutional Budget Reserve-- do not provide a sustainable source of revenue to fund government. A new fund should be established that would be managed as an endowment and from which only the earnings could be spent on government programs. This fund could be bankrolled in a number of ways--most obviously thru a periodic sweep of excess general fund balances.
2) **Mechanisms to Control Operating Budget Growth**—Fiscal stability requires control over growth in the operating budget. The ceiling in the existing Constitutional Spending Limit is set too high to work. A new mechanism, or set of procedures needs to be established to cap operating budget growth (methods from other states can be considered). Related to this is the need for greater transparency in the budget making process.
3) **Explicit Criteria to Enforce Discipline into Capital Spending**--When revenues are high there is inescapable pressure to expand the capital budget with hard-to-justify projects. Discipline could be incorporated into the process (and cover for legislators to say no) with the establishment of an explicit application procedure and specific project criteria such as a financial contribution for local projects, review of past performance, etc.
4) **Enhanced Capacity to Analyze Economic Impacts of Petroleum Revenue Regime**—We are unable to determine the impact that the current tax regime has had on petroleum industry investments and consequently future revenues and employment opportunities. Since petroleum accounts for 85% of general fund revenues, the establishment and maintenance of this capacity within state government is critical.
5) **Fiscal Projections and Public Education**—Although OMB is now required to produce a 10 year budget projection, the exercise needs to cover a longer time period to account for the uncertainty of natural gas revenues, it needs to show the impact of different revenue and expenditure assumptions, and it needs to identify how current account deficits would be addressed thru new revenues or budget reductions. The annual presentation of this projection should be the focal point for a discussion of progress in the effort to create long term fiscal stability and economic growth. Quantitative measures should be created to monitor progress.
6) **POMV—**Management of the Permanent Fund as an endowment should be implemented without altering the formula for calculating the Dividend.
7) **Triggers**—Mechanisms that automatically introduce and increase or decrease taxes and /or spending under predetermined conditions (for example, a drop in the CBR below a target level) can be put in place today in a non crisis environment.