

off the record

a legislative
update from
Senator Kim Elton

a bi-weekly way to stay in touch

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Capitol Undercurrents

It bears repeating—George Orwell's 1946 essay on *Politics and the English Language* reminds us that vagueness and euphemism and abstraction abet muddled thinking. That is especially true as elections draw near. It's tough to say "taxes" and easier to say "revenue enhancements". It's easier to say "efficiencies" than it is to say "cuts".

Orwellian advice taken—The executive director of the Resource Development Council, one of Alaska's most outspoken development groups, noted—in blunt language that would have pleased George Orwell—that economic development creates a burden on state government resources. In the RDC newsletter he wrote: "Every new job adds to the state's responsibility in terms of schools, roads, and dividend checks. Meanwhile, residents in Alaska pay nothing, outside of modest user fees and sin taxes, into state coffers. Visitors and non-resident workers also pay nothing to the state. Alaska is the only state in the union with this unique set of circumstances." He adds: "Failure to make real progress (on the fiscal gap) in the short run risks creating an Alaska that has neither the ability to provide for its citizens, nor the strength to compete in the world market."



(continued on pg. 2)

Permanent fund can be more permanent

This week, Alaska Permanent Fund Trustees announced the size of the dividend for this year. A PFD of \$1,540 plus for every Alaskan this year should not lull us into a world of comfortable illusion—there are challenges aplenty for the permanent fund trustees, the new governor, and the new legislature.



The challenges include:

1. In the last two years, the permanent fund's earnings reserve (used to pay dividends and inflation-proof the corpus) went from \$8.6 billion to negative territory in July (it has come into the black, slightly, since then).
2. Over 40 percent of that precipitous decline is due to market losses, less than 40 percent was for dividend payouts, and about 20 percent was for inflation-proofing the corpus of the fund.
3. *The Alaska Budget Report* notes that if (economist Gregg Erickson, publisher of the report, notes it is a big "if") steep declines in the market continue the earnings reserve won't be able to pay dividends and inflation proof the corpus.
4. The legislature has not approved an endowment approach suggested by permanent fund trustees that limit annual appropriations to 5 percent of the fund's market value—some legislators may want to preserve the option of appropriating more given the state's growing fiscal gap.
5. There is a political vertigo issue. The continuing lack of a fiscal policy that balances state spending with state revenues makes it easier for elected officials to balance the budget with permanent fund earnings (if there are any) instead of implementing new taxes. As one trustee put it, he's afraid the state will "default" to the earnings reserve when the Constitutional Budget Reserve (our savings piggy bank) is exhausted in the next couple of years.

The last two points are issues that elected Alaska officials actually have control over. Fed Chairman Alan Greenspan is better equipped to cure the financial ague infecting the stock market than is the Alaska legislature. An up tick in the national economy is needed to boost permanent fund earnings that will replenish the earnings reserve.

But legislators must focus on the last two issues. We can't, as Mark Twain once suggested, "Put off until tomorrow what we can do the day after tomorrow." We've already done that. Technically, we've now delayed difficult fiscal solutions from one millennium to the next.

(continued on pg. 2)

Permanent fund...

We've put off any real debate on the endowment concept suggested by the permanent fund trustees. Their concept provides sustained yield over the years and is similar to endowments established by universities and other entities. Technically known as the "percent of market value" approach, the trustees suggest that 5 percent of the earnings averaged over the last five years be available for spending (including the spending on dividends).

The second quarter, 2002, permanent fund report notes that this sustained yield approach is the same concept used by scientists managing our fisheries to ensure future seafood harvests in the out years. It's pretty basic. Because the fund since its inception has average earnings of 8 percent, a 5 percent payout allows for ample inflation proofing of the permanent fund while ensuring a stream of money for dividends or other use.

If the legislature had adopted this endowment approach when first proposed, *The Alaska Budget Report* suggests, lack of money in the earnings reserve this July "would have been largely a non-issue."

One of the real beauties of this percent of market value approach is that it does provide a long-term, ironclad solution to protecting the permanent fund from inflation (the first chair of the Board of Trustees, Elmer Rasmuson, noted that "inflation is like a thief in the night"). Right now, we statutorily inflation proof the fund. That's okay, but future legislators can easily change statutes.

But under the trustees' endowment proposal, a constitutional amendment (that is first approved by the legislature and then by the voters on a statewide ballot) more securely inflation proofs the permanent fund. A constitutional amendment makes it more difficult for future political meddlers.

And that is particularly important given the fiscal gap. As the spending/revenue conundrum continues to flummox elected leaders, I'm concerned that the simple, though highly unpopular, solution when we hit the wall of financial reality will be to use permanent fund earnings to pay exclusively for government. That means two things happen: the dividend, now financed from earnings, goes away; and, as one trustee notes, the permanent fund board may have to adopt a shorter investment horizon to maximize short-term gains.

Over the last couple of years, the budget gap has been the fiscal carbuncle we've been unwilling to treat. That unwillingness makes defaulting to the earnings reserve of the permanent fund more likely. There are three solutions out there: use the earnings of the permanent fund; more taxes; draconian cuts.

One of the solutions doesn't work. We can't continue to cut our way out of this financial mess. We've already cut the budget by a quarter billion dollars in the last decade (Alaska is the only state spending less now than ten years ago). A \$250 million cut is not an insubstantial amount given the fact that our general fund budget this year is \$2.5 billion. The notion we can cut another \$750 million each year is absurd.

But the bad news is, even with deep cuts already taken, almost a third of this year's general fund budget is financed out of our savings, the Constitutional Budget Reserve. And that CBR will be gone in a couple of years.

It's time for tough choices. The easiest and best first step is to protect the permanent fund corpus by taking the financially responsible percent of market value approach favored by the permanent fund board and enshrining it in our constitution. We need to do it now.

Undercurrents continued...

Do I sense an Orwell theme here—

Rep. Andrew Halcro, the retiring Anchorage GOP gadfly who never pussy-footed around an issue with the vagueness or abstraction or euphemism criticized by Orwell, was approached by the Republican Moderate Party to see if he would run for governor on their ticket. A vacancy was created at the top of the Moderate ballot when the nominated candidate withdrew. Andrew declined, but not until after he tweaked his former legislative aide by calling him and asking what he thought of the idea.

Southeast Conference constraint—

One of the first people I saw at the Southeast Conference in Craig was Dick Burton—a long-time state trooper who capped his law enforcement career as commissioner of the Department of Public Safety. He's now a member of the Ketchikan Gateway Borough Assembly. I first met Dick when I was a callow high school youth attending a mid-60s S.E. high school basketball championship in Ketchikan. At the time, he was commander of the First City's trooper detachment and had offered his home to house some of the invading students. I was one of the lucky ones to be housed with him. Despite my first away-from-home high school adventure, I really, really watched what I said and did and obeyed the curfew to the minute. As soon as I saw him in Craig, I kind of felt like I should also mind my Ps and Qs at the conference.

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