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Alaska; Appropriations; General Obligation; Moral Obligation; Note

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Credit Profile		
US$151.18 mil GO bnds ser 2016A due 08/01/2035		
Long Term Rating	AA+/Negative	New
Alaska GO		
Long Term Rating	AA+/Negative	Affirmed
Alaska GO		
Long Term Rating	AA+/Negative	Affirmed
Alaska GO		
Unenhanced Rating	AA+(SPUR)/Negative	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'AA+' rating to Alaska's $151.2 million in general obligation (GO) bonds, series 2016 A. We also affirmed our 'AA+' rating on Alaska's previously issued GO bonds. The outlook on all debt ratings is negative.

Proceeds from the series 2016A GO bonds will be used to retire on March 18 the state's GO bond anticipation notes, issued on March 19, 2015.

The GO bonds are backed by the state's full faith, credit, and resources. Although the state is in the midst of grappling with large general fund operating deficits, we continue to view Alaska as having very strong credit quality. This reflects our view that the state benefits from several favorable features, including:

- Budget reserves that, despite not representing a permanent solution to the state's unrestricted general fund deficit problem, remain large, equal to 298% of annual appropriations (as of February 2016);
- The potential to resolve much of the general fund gap by overhauling the flow and customary treatment of various legally unrestricted state revenues; and
- Its moderate debt burden and closed defined-benefit retirement system that should benefit actuarially from a recent large asset infusion.

Alaska's legislature is currently in negotiations over Governor Bill Walker's fiscal 2017 budget proposal and -- more broadly -- his recommendation to reform state finances. As it is, the state's general fund is mired in a large operating deficit, estimated at $3.6 billion, equal to 69% of total fiscal 2016 appropriations. The current imbalance, as with much about Alaska's recent economic and fiscal experience, is summed up by collapsing oil prices on the global markets and declining production on Alaska's North Slope. Reflecting its linkage to the commodity markets, Alaska's economy has begun to contract and is out of step with the U.S. economy, which continues to expand. For much of the past 40 years, taxes and royalties on oil production have been sufficient to pay for a majority of the state's general fund expenses. For instance, in fiscal 2012, when Alaska North Slope (ANS) west coast spot prices averaged $112.65 per barrel, the state brought in nearly $9.5 billion in total unrestricted revenue. But by the spring of 2015, the state's ANS oil price forecast -- $66.03 per barrel in fiscal 2016 -- was projected to produce just $2.2 billion in unrestricted general fund revenue. Consequently, despite having cut spending by 16% relative to the prior year -- and 38% since fiscal 2013 -- the state's fiscal 2016 budgeted appropriations still exceeded anticipated revenues by $2.7 billion, a shortfall equal to 54% of budgeted expenditures. Lawmakers covered the gap in the budget by authorizing a transfer from the state's Constitutional Budget Reserve (CBR), albeit only after first getting hung up in the negotiating process.

Even this would prove optimistic, however, and as the year progressed, the slump in oil prices persisted. In its fall revenue forecast update, the state revised its fiscal 2016 ANS average spot price forecast lower, to $49.58 per barrel, translating to a downward revenue adjustment of about $600 million. This translates to roughly $1.6 billion in unrestricted revenue for the year, leading the already large fiscal gap to balloon to the more recent $3.6 billion estimate.

Our rating partly reflects that a broader view of state revenues -- including those currently treated as restricted, but subject to appropriation -- shows a smaller fiscal gap. In fiscal 2016, for example, there is approximately $3.8 billion in revenue that is subject to appropriation. If the legislature repurposed all of this revenue to the general fund, it could eliminate the deficit. Of the additional revenue subject to appropriation, $3.4 billion is from realized earnings on the permanent fund. Of this, however, $1.4 billion was used to fund dividend payments to state residents while another $892 million was redirected back to inflation-proof the permanent fund. Therefore, even if there are not legal constraints on appropriating this revenue, we believe there are practical and political ones. Nevertheless, although the policy choices involved are difficult, we view the state's potential fiscal capacity as greater than its unrestricted petroleum-related revenue alone suggests.

Furthermore, Alaska's still sizable budget reserves enable it to endure large operating deficits for several years. Ultimately, however, and particularly if lawmakers are unwilling to repurpose the restricted revenues, the fiscal trajectory sketched out above is unsustainable. Apart from the effect of falling commodity prices, declining oil production is putting a strain on state finances. ANS oil production peaked in 1988 at 2 million barrels per day, but has been in gradual decline since. The state anticipates 504,900 barrels of production in fiscal 2017, falling to fewer than 400,000 barrels per day by 2022. Following a months-long campaign to highlight these facts, Governor Bill Walker put forward a plan to overhaul, or "re-plumb," state finances as part of his fiscal 2017 budget proposal.

Governor's proposal to reform state finances

The main thrust of the governor's financial reform proposal involves Alaska's transitioning away from relying on volatile oil revenues to fund state government. Under the governor's plan, Alaska would instead finance most of its general fund expenditures from investment earnings on its asset holdings, in a variant of what state officials refer to as the sovereign wealth fund model. The state estimates that, in order to sustainably support both general fund and the permanent fund dividend program at present levels, roughly $100 billion in total assets is necessary. However, the value of Alaska's combined assets -- prodigious as they are -- falls short of this, at about $56 billion. The governor's proposal represents, therefore, a partial sovereign wealth fund model, supplemented by several other more conventional fiscal reforms that result in additional revenue and lower spending.

In our view, the governor's various reform proposals fall into one of the following three categories:

- 1. Adopt a partial sovereign wealth fund model highlighted by two fundamental changes to the design of Alaska's finances:
- --a. Redirect all oil production tax revenue and 50% of oil royalty revenue away from the general fund to the state's permanent fund earnings reserve (PFER). The oil-related revenues make up $946 million of $1.8 billion in total projected unrestricted revenue for fiscal 2017. The remaining $851 million in nonpetroleum-related unrestricted revenues would continue flowing into the general fund as it does now;
- --b. Establish an annual draw from the PFER to the general fund, used to pay for a majority of governmental operations. The draw amount (proposed at $3.3 billion for fiscal 2017) would be set according to formula and designed to preserve the real value of Alaska's invested assets.
- 2. Implement an additional $169 million (4.1%) in cuts to state agency operations, following $400 million in reductions in fiscal 2016. Additional future spending reductions would come from the governor's proposal to transform its oil and gas tax credit program into a loan program intended to spur development activity while lowering expenses.
- 3. Generate additional tax revenue from a new personal income tax, as well as increases to the state's mining, fishing, motor vehicle, alcohol, and tobacco taxes. New revenue from these changes would sum to a projected $350 million in fiscal 2017, but increase to $460 million in future fiscal years once annualized.

Governor's proposal would link permanent fund dividends to Alaska's natural resources

Central to the governor's reform proposal is the capacity of the state's financial assets to sustainably support an annual transfer of investment earnings to the state's general fund. Traditionally, the state has used half of the investment earnings from the Alaska permanent fund to pay an annual dividend to state residents. As part of repurposing these revenues, the governor has recommended changing the method for funding the annual dividend program, tying it to the state's receipt of oil royalties rather than to investment returns. This adjustment -- which is integral to the sovereign wealth fund model -- would reduce the cost of the dividend program to about $700 million in fiscal 2017 from $1.4 billion in fiscal 2016. While there is a philosophical consistency to the governor's approach in that the dividend program was meant to recognize Alaskans as resident-owners of its natural resources more than beneficiaries of its investment gains, the bottom-line result is a smaller dividend check.

Legislative members have put forward measures that would similarly shift the general fund's reliance on the permanent fund as its primary source of funding. The competing proposals would differ, however, in that rather than withdrawing for deposit to the general fund a consistent amount of revenue, they would transfer a fixed percentage of market value (POMV) of the permanent fund to the general fund.

Assessing the financial reform proposal from a credit perspective

The governor's proposal illustrates how it's possible that Alaska's fiscal flexibility could extend well beyond that which is provided by its traditional definition of unrestricted general fund revenue. By redirecting oil-related revenue to its PFER, future windfall-like revenues from oil price spikes would be retained in the permanent fund, allowing the state's asset base to grow. Conversely, when oil prices fall to low levels, the resulting decline in oil-related revenue would be absorbed by the state's permanent fund rather than its general fund. Insofar as the sovereign wealth fund model would transfer the volatility of the oil-related revenue away from the general fund to the state's permanent fund, it could have a stabilizing effect on the state's budget performance. It could help lawmakers be less inclined to engage in yo-yo budgeting. We have observed that lawmakers in Alaska have a history of allowing appropriations to swell during years when oil prices are high, only to be forced to make steep cutbacks when they fall.

In contrast, the POMV approach would result in larger transfers -- and thus potentially larger general fund budgets -- in years when the permanent fund value increases. Because the permanent fund value would increase most in years when oil prices are high, the state's fiscal linkages to conditions in the commodities markets would likely be greater under the POMV funding model.

Stabilizing the state budget in the manner proposed by the governor involves a wholesale redesign of the state's financial architecture, however. Not surprisingly, some of the individual components of the proposal have already been met with resistance by some members of the legislature and other stakeholders. And if the politics of enacting a fiscal overhaul prove too politically difficult, resulting in inaction this year, the state's options will narrow. On a combined basis, Alaska's various budget reserves currently total about $15.5 billion (PFER, CBR, and statutory budget reserve fund, or SBRF). While reserves at that level remain comparatively strong, it's unlikely they can be sustained, considering the state is operating with a $3.6 billion structural deficit this year.

Even assuming no budget reform and an unrestricted general fund structural deficit of about $3 billion, the projected date-to-depletion of the state's reserves is unclear. That's because a significant share of permanent fund investment earnings are retained and allowed to accumulate in the PFER. In fiscal 2017, for example, the state forecasts investment earnings of $3.4 billion, approximately $1.4 billion of which would be spent on dividends under the existing methodology. The remaining $2 billion in investment earnings would bolster and extend the life of the state's budget reserves even if they were simultaneously being drawn upon to fund the budget gap.

Nevertheless, Alaska's lawmakers confront a relatively urgent situation if they hope to move the state away from its budgetary dependence on the volatile oil-related revenues. In order for the annual draw from state savings to be sustainable, officials estimate that Alaska's invested assets need to generate a 6.5% average annual rate of return. According to the governor's proposal, the state's asset base currently could sustainably support a $3.2 billion transfer to the general fund. But if lawmakers defer taking action, allowing PFER balances to be drawn down, the assets would support only a smaller annual transfer.

In our view, Alaska has sufficient financial resources to stabilize general fund operations if it can assemble the necessary political will to adopt the necessary changes. We expect this will require asking residents to accept reduced state spending, higher taxes, and, if it is to use investment earnings, a reconstituted -- and lower -- dividend payment. Although from a constitutional and statutory standpoint, the investment earnings are unrestricted revenues, using them to fund general fund expenses represents a politically difficult tradeoff. Given that lawmakers have yet to coalesce around either the governor's proposal or some alternative, we therefore continue to evaluate the state's creditworthiness largely according to its existing budgetary framework. Through this lens, and in light of the unrelenting oil price declines, the state's fiscal structure is deeply misaligned and its reserves, while still significant, are declining at a fast rate.

The stakes are high for the state to enact a package of fiscal reforms that would help stabilize the state's credit quality at a high rating level. Part of the administration's medium-term fiscal strategy involves using pension obligation bonds in an effort to drive down the budgetary cost of funding actuarially sound annual contributions. On the economic development front over the longer term, we understand the state is interested in seeing its estimated 30 trillion cubic feet in natural gas reserves get developed. And lacking a mechanism for delivering the gas to market, state officials are contemplating partially debt-financing a natural gas pipeline. Both propositions make less economic sense, however, in a scenario where the state's credit rating is significantly lower and its cost of capital materially higher.

Based on the analytic factors we evaluate for states, on a four-point scale in which '1' is the strongest, Standard & Poor's has assigned a composite score of '1.7' to Alaska.

Composite scores ranging from 1.6 to 1.8 correspond with a 'AA+' rating under our criteria. Although previously we have employed a one-notch upward adjustment as allowed under our criteria to account for what we viewed as uncommonly high budget reserve levels, we view the current trajectory of the reserves and fiscal condition as no longer warranting this adjustment.

Outlook

The negative outlook reflects the large structural budget deficit in Alaska's unrestricted general fund. Currently, the state is able to finance its operating deficits by withdrawing funds from its budgetary reserves. Alaska had built up large budget reserves that thus far have shielded the state's credit quality from the degradation that the large deficits would inflict on most states' credit quality. But the magnitude of the fiscal deficits makes the arrangement unsustainable and, unless corrected, inconsistent with the current rating. Therefore, we will likely again lower the state's rating -- possibly by more than one notch -- if state lawmakers do not enact measures to begin correcting the state's fiscal imbalance during its 2016 legislative session.

The typical lag that exists between the enactment of fiscal policy adjustments and when they yield results implies the need for lawmakers to act soon. Therefore, even with its reserve balances at still-strong levels, we would likely lower the state's rating even within the next year if lawmakers defer enacting corrective fiscal policy adjustments.

In the event policymakers continued to take no action, the current initial rating change most likely represents the first step in a downward migration that would likely accelerate as the state's reserve balances approached depletion. If lawmakers succeed in putting the state on what we view as a glide path to a sustainable fiscal structure, with its strong reserve balances still intact, we could revise the outlook to stable.

Governmental Framework

The Alaska constitution requires the governor to submit a balanced budget proposal to the state legislature by Dec. 15 for each fiscal year, which begins on July 1. The governor is required to submit three budgets -- an annual operating budget, a mental health budget, and a six-year capital budget. The governor can line-item veto legislatively approved budget bills. An enacted state budget is not required to stay in balance during the course of the fiscal year after budget adoption, but the governor can hold back expenditures when revenue is below budget.

Although the governor has proposed one, currently the state does not have an individual income tax or sales tax but has occasionally adjusted its formula for oil production and other mining-related tax rates. The state legislature can impose new taxes by majority vote, but a qualifying referendum petition could be filed to challenge new tax legislation. Alaska has the legal authority to re-impose an income tax (which it had in place before 1978) or to impose a sales tax if it so chooses.

Alaska's constitution provides that proceeds of state taxes or licenses "shall not be dedicated to any special purpose" except for restricted federal revenue, money dedicated before statehood, and money required to be placed in the state's permanent fund. As a result, most revenue is placed in Alaska's general fund although the state has created numerous subaccounts within the general fund.

The state's permanent fund was established as the result of a constitutional amendment in 1977, which requires that at least 25% of all mineral lease rentals, royalties, royalty sale proceeds, and federal mineral-sharing revenue and bonuses be placed in the fund. An additional 25% is currently deposited to the fund per state statute. Investment income and annual constitutional and statutory deposits into the fund are reflected in the state's audited financial statements as restricted revenue. According to existing statute, investment income is used to fund the state's annual dividend program and inflation-proof the permanent fund with any remaining income held in savings. The portion of investment income held in savings is retained in the PFER and is available for appropriation by the legislature.

A component of the governor's fiscal reform proposal is the Alaska Permanent Fund Protection Act (APFPA). Under the APFPA, the dividend payments would be funded from 50% of any mineral royalties. The balance of mineral royalties, plus 100% of production taxes and investment income, would flow directly into the permanent fund. Within the permanent fund, 25% of royalty revenue would continue to flow to the corpus of the fund, pursuant to the constitution. Other mineral royalty revenue would flow to the PFER, with the objective of building a balance equal to 400% of the prior year's transfer to the general fund. In effect, investment income would be the primary source of funding for the PFER. The additional revenue from mineral royalties, taxes, and investment income beyond what is required for the targeted balance would flow to the permanent fund corpus.

The state's Constitutional Budget Reserve Fund (CBRF) was created as a constitutional amendment, in 1990, that requires all money received by the state after July 1, 1990, through resolution of disputes about the amount of certain mineral-related income must be deposited here. Investment income, as well as any current-year resolution dispute revenue, deposited into the fund is reflected as restricted revenue. In most cases, appropriation from the fund requires a three-fourths majority vote of the legislature and approval of the governor.

Alaska has wide legal latitude to cut disbursements as it chooses. It has an appropriation limit and reserves one-third of the amount within the limit for capital projects and loan appropriations. Because state appropriations have never significantly approached the limit, Alaska does not believe the reservation has constrained state operations. The appropriation limit does not apply to the permanent fund.

Voter initiatives may be placed on the ballot upon collection of enough petition signatures to equal 10% of the votes cast at the latest general election. However, successful voter initiatives only have the effect of statutory law and can be overridden or repealed by the legislature after two years. Voter initiatives may not amend the state constitution. In Standard & Poor's opinion, voter initiative activity has not historically affected or hindered state operations.

The state issues GO debt, lease-secured debt secured by annual appropriations, moral obligation debt, and dedicated tax revenue bonds. Due to the state's practice of annually appropriating reserve replenishment in its budget, we rate its Alaska Municipal Bond Bank (AMBB) debt, which also carries the moral obligation backing of the state, under our appropriation-backed criteria. GO bond authorization requires a simple majority voter approval. GO bonds may be issued only for capital purposes except for veterans' mortgage guaranteed bonds. The state has issued moral obligation debt for its Bond Bank, for the Alaska Energy Authority, and for the Alaska Student Loan Corp. The state can also legally issue cash flow notes but has not done so in the past 35 years because of its historically strong cash position.

The Alaska constitution does not specify a priority of payment for GO debt service compared with other expenditures, but annual GO debt service, as constitutionally authorized debt, could be paid in absence of a specific annual budget appropriation. Generally, the state has appropriated both GO and lease-secured debt service under a separate line-item appropriation.

The state provides assistance to school districts, including discretionary payments since 1970 to subsidize pre-qualified local school district debt service but also can cut funding if it deems doing so necessary, as long as cuts are distributed so as to preserve equitable per-pupil funding across the state. The state has provided 60% to 100% reimbursement depending on different factors.

On a four-point scale in which '1' is the strongest, Standard & Poor's has assigned a '1.5 ' to the state's governmental framework.

Economy

Alaska's economy is largely dependent on the oil extraction and mining industry, but the fishing, timber, and tourism industries are also present. Alaska's high cost of living and dispersed population can serve to restrain growth in non-oil-and-gas-related industries. Employment sectors differ from those of the nation as a whole in some key respects. Most notably, construction and mining together account for about 11.0% of state employment versus 5.0% for the nation, according to IHS Connect estimates. Alaska's manufacturing employment is 4.2% of total employment compared with 8.7% for the nation; its business and professional services are 8.8% compared with the nation's 13.7%, and its governmental employment is 24.4% compared with 16.0% for the nation. This introduces potential exposure to employment losses from federal fiscal consolidation efforts.

Although the state's population has been increasing faster than that of the U.S. as a whole, this fluctuates from year to year. For example, Alaska's population increased 11.73% in from 2004 to 2014 versus 8.9% for the U.S., but the state's population dipped 0.07% in 2014. The state's age dependency ratio -- the ratio of dependent population to total population -- is 53.5% compared with the nation's rate of 60.2%.

Because of the state's sizable rural population, its unemployment rate has historically been higher than that of the nation, but in recent years, as national unemployment has increased and the state's unemployment rate has held steady, its seasonally adjusted unemployment rate has fallen below national rates. Alaska's unemployment rate in 2015 was 6.5% compared with 5.3% for the nation. The most recent monthly seasonally adjusted unemployment rate, for December 2015, was 6.6% compared with the national rate of 4.9%.

As the state's economy has gradually matured, the composition of its employment base has shifted. In recent years, new jobs in health care, construction, and government have offset job losses in timber and seafood processing. With that said, seafood processing employment for the first nine months of 2013 was well ahead of where it was in 2012, suggesting that is likely to show growth in 2013 once the numbers are final. In addition to oil, gold, metal ore mining, and the possible construction of a major natural gas line could also prove promising for new jobs.

Notwithstanding recent declines, the value of mineral production resulted in Alaska's real gross state product (GSP) per capita equaling 142% of the U.S. level, although this is down from 154% in 2012. Whereas U.S. GDP (real) grew at 2.4% in 2014, Alaska saw a 1.3% contraction. Still, over a longer term, the state's economy has track record of growing faster than the nation. Alaska's 10-year average annual GDP growth rate through 2014 of 1.9% exceeds that of the nation (1.4%). The federal Bureau of Economic Analysis' 2014 estimate of Alaska's per capita personal income is $54,012, or 117% of the nation.

Relative to other states, Alaska's income figures are more prone to volatility because of the economic linkages to oil prices, which tend to fluctuate in response to global economic and geopolitical forces. Alaska suffered a severe recession in the mid-1980s following a collapse in oil prices, and we believe it is now at risk of entering recession as a consequence of the collapse in oil prices.

Alaska continues to exploit its potential for natural resources production aggressively, in our view. The state is exploring the possibility of developing a natural gas pipeline to derive economic benefit from an estimated 35 trillion cubic feet of natural gas reserves located on Alaska's North Slope. The current market and price differential between North American and Asian markets is such that exporting natural gas in the form of liquefied natural gas may offer more benefit than an overland pipeline.

On a four-point scale, in which '1' is the strongest, Standard & Poor's has assigned a score of '1.5' to Alaska's economic structure.

Financial Management

Financial management assessment: Good

We consider Alaska's formal management practices good under our financial management assessment (FMA) methodology. An FMA of good indicates our view that the state maintains many best practices deemed as critical to supporting credit quality, particularly within the finance department. These practices, however, may not be institutionalized or formalized in policy, may lack detail or long-term elements, or may have little recognition by decision makers outside of the finance department.

The state has a statutory budget reserve within its general fund that, although not always funded, is available to provide liquidity. In addition, the state has also established the CBRF, which voters approved. Funds may be appropriated for certain purposes by a vote of three-fourths of each house of the legislature, but money can be used for interfund borrowing for general fund expenditures. All appropriations from the fund are recorded as a general fund liability.

Until recently, the state's forecast of its leading predictor of state revenue, the price per barrel of oil, has tended to err on the low side. (This changed in fiscal in fiscal 2015 following the unanticipated collapse in global commodity prices.)

The state also forecasts production and has recently enhanced its methodology on this front. Budget amendments can occur throughout the year.

Alaska produces detailed revenue forecasts, with the focus being the price of oil, which -- unless the governor's reform package is adopted -- remains the leading determinant of general fund revenue. Other revenue sources are also included in the revenue source book, which is released twice each year. The tax division of the Alaska Department of Revenue (DOR) prepares the book, using numerous outside sources of information to help predict the price of oil.

In addition to the revenue forecast, the Office of Management and Budget maintains a 10-year fiscal forecast, which is updated annually. Expenditure projections are less detailed although the state accounts for some inflationary and caseload pressures on spending levels.

The state's debt management policy is updated annually with the public debt report and debt affordability analysis as required by statute. The debt report describes the different types of debt that Alaska issues, mainly certificates of participation and GO bonds. For general-fund-supported bonds, the state has a debt capacity that it determines, by policy, to be 8% of unrestricted revenue.

Investment management is also covered by the investment policy statement, and the performance of the state's investment portfolio is monitored daily. Each year the fund undergoes a fiduciary audit, which includes a review of legal and administrative constraints for each invested fund. The audit policy's stated goal is to keep Alaska's investment process intact during periods of market upheaval.

Alaska enacts an annual capital budget. Expenditure assumptions for the state's operating budget are adjusted as appropriate when capital projects begin. A transportation agency capital plan provides an annually prioritized plan detailing three years of projects and funding sources.

Budget management framework

The DOR issues formal revenue forecasts twice a year, in the spring and fall. The forecast is based on consultation with an engineering firm and the state department of natural resources. As noted above, the methodology for forecasting oil production has been revised to incorporate the greater variability associated with production forecasts from some oil fields that are still under development or are in the evaluation phase of development. The net effect of these changes has been to increase the long-term rate of production decline. The revenue forecast has historically been used as presented for budget adoption and not adjusted during the budget-adoption process.

Historically, Alaska has used existing high fund balances to carry deficits and is not legally required to make midyear budget adjustments in the event a midyear gap develops. The governor has the discretion to hold back spending in the middle of the fiscal year if a budget gap appears to be developing. Such adjustments were last made in fiscal 2009, during oil price fluctuations. The governor can unilaterally prioritize such holdbacks, but the holdbacks have no formal requirement or schedule.

On a four-point scale in which '1' is the strongest, Standard & Poor's has assigned a '2.0' to Alaska's financial management.

Budgetary Performance

The state has no legal requirement to fund reserves at any specified level. However, historically it has held total general fund balances we consider very high. With its exceptionally strong cash liquidity, the state's intrayear cash flows are positive, averting the need for it to borrow for cash flow purposes. On an audited basis, the general fund held a $14.8 billion cash and investment position at fiscal year-end 2014, equal to 113% of general fund expenditures. Although the state has no legal minimum budget reserve requirement, it has created a CBRF that holds money received by the state as a result of legal settlement, administrative proceedings, or litigation of mineral-related revenue. For liquidity purposes in the past, the state has used the CBRF for temporary borrowing within the year or to balance the budget at the end of the year. The CBRF is also available for general expenditures with a three-fourths vote of the legislature and approval of the governor. In fiscal 2015, the state transferred $3 billion from the CBRF to its two pension systems.

In 1990, when state revenues began to outpace its expenditures in a given year, the legislature began to appropriate the surplus to the SBRF. And while the state has no explicit policy to maintain a particular balance in the SBRF, to the extent that one is available, the state first draws upon the SBRF for liquidity purposes before borrowing from the CBRF. Transfers from the SBRF to the general fund require consent from a majority of the legislature. At this time, the SBRF balances have been depleted.

According to generally accepted accounting principles (GAAP), the direction of change from year to year in Alaska's net asset position on a government wide basis is not always dictated solely by its general fund operating performance. The state generates considerable investment income from its invested assets -- primarily the Alaska Permanent Fund. In fiscal 2015, for example, the $45.6 billion permanent fund had income of $3.1 billion from rents and royalties ($597 million) and interest and investment income ($2.5 billion), on a GAAP basis. In some years, the state can run an operating deficit in the general fund but see its net asset position grow due to the income earned by the permanent fund. For example, permanent fund income in fiscal 2014 of $7.7 billion was more than enough to offset the general fund deficit of $1.3 billion. Largely as a result of this, the state's overall net asset position increased $6 billion despite the general fund deficit. In fiscal 2015, the state's net asset position declined by $10.2 billion, however, driven in large part by the state having implemented governmental accounting standards board statement (GASB) 68, wherein the state added its net pension liabilities to its balance sheet.

Despite the recent large structural deficit, the general fund remains solvent, with a fiscal 2015 year-end committed and unassigned general fund balance of $15.5 billion, or 118% of expenditures on a GAAP basis, which we consider very high. The state has had either an unreserved or unrestricted general fund balance higher than annual expenditures since fiscal 2008, when it produced a record $7 billion financial windfall from high oil prices and a new tax structure that effectively increased tax rates on oil companies.

On a four-point scale in which '1' is the strongest, Standard & Poor's has assigned a '1.7' to Alaska's budgetary performance.

Debt And Liability Profile

As of fiscal 2015, we calculate Alaska's tax-supported debt per capita at $1,396 (based on 2014 population), which we view as moderate. At June 30, 2015, the state had about $810.7 million of GO debt, but about $56.9 million of this is considered self-supporting veterans' mortgage revenue-secured debt, leaving about $753.8 million net tax-supported GO debt. At the end of fiscal 2015, Alaska also had about $274.8 million of annual appropriation-supported debt. Tax-supported debt (GO and appropriation) to personal income is 2.89%, which we view as moderate. Tax-supported debt to GSP, now at 1.8%, is low. Tax-supported debt service as a percentage of general fund spending was low, at about 0.8%, in fiscal 2015 and remains low, at 1.6%, when including the local municipal school and capital-reimbursement-related debt paid by the state on behalf of local jurisdictions. About 47% of combined GO and lease debt matures in the next 10 years. The governor's fiscal 2017 budget proposal includes approximately $185 million in unrestricted state funds for capital funding, down from the fiscal 2015 budget, which included about $600 million in state funding for capital projects.

Pension and OPEB liabilities

In 2006, Alaska moved all new employees to a defined-contribution retirement plan from a defined-benefit plan, but employees hired before that continue under the state's defined-benefit pension plan. In addition, unlike most other states, Alaska's other post-employment benefits (OPEB) are constitutionally protected. Also unlike most states, however, the state has an OPEB trust fund and a track record of funding the liability on an actuarial basis. Thanks to a large, extraordinary $3 billion contribution from the state's CBRF to its pension systems, its funded ratios -- for both its defined benefit pension and OPEB liabilities -- improved markedly in fiscal 2015. The contribution was split between the Alaska Public Employee Retirement System, or PERS ($1 billion), and the Teachers' Retirement System, or TRS ($2 billion).

Following implementation of GASB 68 and as of fiscal 2015, the PERS multiemployer plan had a 64% pension-funded ratio. We estimate that, as of fiscal 2015, the state's proportionate net pension liability (NPL) related to PERS was $3.8 billion. The separate TRS had a 74% pension-funded ratio as of fiscal 2015, up from a 56% ratio in fiscal 2014. Improvement to the TRS funded ratio was more pronounced than that for PERS because of the disproportionate contribution to that system. Both PERS and TRS employ an 8.0% assumed rate of return on invested assets.

Combined with the liabilities associated with much smaller pension systems judicial officials, and retired national guard and naval militia members, the total PERS and TRS NPL was $3.4 billion as of June 30, 2015. As of fiscal 2015 and after incorporation of the extraordinary contribution that year, the combined pension-funded ratio stands at 80.3%, which is above average, in our view. However, the NPL remains high, in our view, at $4,665 per capita and 8.6% of total state personal income.

Annual contributions to PERS and TRS have been set according to percentage of salaries. However, on July 1 of each year or as soon as funds are available thereafter, the state is required by statute to contribute sufficient additional funds to bring the total pension contribution for the prior fiscal year to the actuarially determined level, which we view favorably.

Favorable health care cost trends combined with the effect of the large contribution to the PERS and TRS systems, the state has achieved virtual full funding (99% based on fiscal 2015 estimates). The OPEB liability also includes those of other participating local governments. The state is required by statute to fund the annual contributions to the pension system at the actuarially recommended level.

In addition to the state's direct debt, since 1970 Alaska has supported the bonds issued by pre-qualified school districts, with the legislature able to reimburse municipalities for 60% to 100% of debt service costs. The actual program funding depends on annual legislative appropriations, and although not contractually obligated to do so, the state has done so in recent years. Alaska has made the payments. In fiscal 2015, the budget includes an appropriation of $125 million for the municipal school debt reimbursement program on total local school district obligations of approximately $895.4 million. In 2015, the legislature placed a five-year moratorium beginning that year on additional bond authorizations in the program.

The state also has about $1.2 billion of self-supporting state moral obligation debt issued by the AMBB, the Alaska Energy Authority, and the Alaska Student Loan Corp. Our rating of the AMBB debt recognizes features we view as strengthening related to its 2005 resolution requiring an annual open-ended appropriation to backfill the reserve, if necessary.

On a four-point scale on which '1' is the strongest, Standard & Poor's has assigned a score of '1.9' to Alaska's debt and liability profile.

Related Criteria And Research

Related Criteria

- USPF Criteria: State Ratings Methodology, Jan. 3, 2011
- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007
- USPF Criteria: Bond Anticipation Note Rating Methodology, Aug. 31, 2011
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- USPF Criteria: Moral Obligation Bonds, June 27, 2006

Ratings Detail (As Of March 1, 2016)		
Alaska APPROP		
Long Term Rating	AA/Negative	Current
Alaska NOTE		
Short Term Rating	SP-1+	Current
Alaska Energy Auth, Alaska		
Alaska		
Alaska Energy Auth (Alaska) pwr rev (Bradley Lake Hydroelectric Proj)		
Long Term Rating	A+/Negative	Current
Alaska Mun Bnd Bank, Alaska		
Alaska		

Ratings Detail (As Of March 1, 2016) (cont.)		
Alaska Mun Bnd Bank (Alaska) GO moral oblig (MBIA) (National)		
Unenhanced Rating	AA(SPUR)/Negative	Current
Alaska Mun Bnd Bank (Alaska) GO (Moral Ob)		
Long Term Rating	AA/Negative	Current
Alaska Mun Bnd Bank (Alaska) MORALOBLIG		
Long Term Rating	AA/Negative	Current
Alaska Mun Bnd Bank (Alaska) MORALOBLIG		
Long Term Rating	AA/Negative	Current
Alaska Mun Bnd Bank (Alaska) MORALOBLIG		
Long Term Rating	AA/Negative	Current
Alaska Mun Bnd Bank GO		
Unenhanced Rating	AA(SPUR)/Negative	Current
Alaska Mun Bnd Bank (Alaska) GO		
Unenhanced Rating	AA(SPUR)/Negative	Current
Matanuska-Susitna Boro, Alaska		
Alaska		
Matanuska-Susitna Boro (Alaska) lse rev rfdg bnds (Alaska) (Goose Creek Correctional Ctr Proj)		
Long Term Rating	AA/Negative	Current
	NR(prelim)	
Matanuska-Susitna Boro (Alaska) lse rev (Goose Creek Correctional Facs) (ASSURED GTY)		
Unenhanced Rating	AA(SPUR)/Negative	Current

Many issues are enhanced by bond insurance.