THE STATE of ALASKA
GOVERNOR MIKE DUNLEAVY

Department of Revenue
COMMISSIONER'S OFFICE

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November 2, 2020

The Honorable Neal Foster

Co-Chair, House Finance Committee
State Capitol Room 505
Juneau, AK 99801

The Honorable Jennifer Johnston

Co-Chair, House Finance Committee
State Capitol Room 511
Juneau, AK 99801

Dear Co-Chairs Foster and Johnston:

The purpose of this letter is to provide you with responses to the questions asked of the Department of Revenue (DOR) regarding the presentation to the House Finance Committee on October 2, 2020. Please see the questions in italics and our responses immediately below the questions.

1. ***What would the amortization on the oil and gas tax credit bonds be, had the Supreme Court ruled the other way? What is the delta between a successful HB331 scenario and an unsuccessful HB331 scenario?***

In May of 2018, a payment schedule was anticipated based on an August 2018 bond issuance. Assumptions included a 10-year amortization with an interest rate of 3.62%, and a discount rate of 5.12% for all of the credits. The following table shows estimated tax credits for each fiscal year based on the estimated statutory appropriation under the Spring 2018 forecast, and their discounted value.

Fiscal Year	Tax Credits Due	Discounted Value
	$ Millions	
2019	$184.00	$184.00
2020	$168.00	$159.82
2021	$168.00	$152.03
2022	$167.00	$143.77
2023	$120.00	$98.27
Total	**$807.00**	**$737.89**

Total financial benefit achieved by issuing bonds through the Alaska Tax Credit Certificate Bond Corporation to pay discounted prices for tax credits at that time were projected at $122.69

million. The discount off the tax credit's face value would have been $69.11 million plus an additional benefit achieved by reducing or eliminating spending in the state budget and theoretically retaining funds in investments that amounts to approximately $53.58 million.

If we were to update the analysis of the Alaska Tax Credit Bond Corporation to October 1, 2020, assumptions would be a lower 3% interest rate of today and correspondingly lower discount rate of 4.5%. The following table shows estimated tax credits for each fiscal year based on the estimated statutory appropriation under the Spring 2020 forecast, and their discounted value.

Fiscal Year	Tax Credits Due	Discounted Value
	$ Millions	
2022	$40.00	$38.28
2023	$42.00	$38.46
2024	$44.00	$38.56
2025	$47.00	$39.41
2026	$45.00	$36.11
2027	$48.00	$36.86
2028	$61.00	$44.82
2029	$78.00	$54.85
2030	$106.00	$71.33
2031	$113.00	$72.76
2032	$115.00	$70.86
2033	$4.00	$2.36
Total	**$743.00**	**$544.66**

Total financial benefit achieved if the state could issue bonds through the Alaska Tax Credit Certificate Bond Corporation to pay discounted prices for tax credits at the current time would be projected at $263.30 million. The discount off the tax credit's face value would be $198.34 million plus an additional benefit achieved by reducing or eliminating spending in the state budget and theoretically retaining funds in investments that amounts to approximately $64.97 million.

2. ***The Alaska Permanent Fund Corporation (APFC) reports that the Permanent Fund Earnings Reserve Account has a balance of ~$10.3 billion as of July 31, 2020. APFC anticipates a withdrawal of ~$3.1 billion for the FY 2022 POMV and considers ~$1.7 billion of the account as unrealized earnings. Based on these figures, if the state were to pay the retroactive dividends totaling ~$4.6 billion that would leave ~$1 billion uncommitted in the Earnings Reserve Account as of July 31, 2020. Under this scenario does the department think the Fund's earnings will be enough to maintain the POMV?***

Forecasts for Permanent Fund growth are based on a "most likely" rate of return, which is one possible level of investment returns with a wide range of uncertainty around those forecasts. Based on the most current fund value from APFC, expected returns from Callan Associates, and Economic Research Group (ERG) modeling, the answer to this question is yes, the state could pay retroactive dividends and still maintain the POMV. However, such an action would increase the possibility of an insufficient earnings reserve balance to fund future POMVs, should investment returns not perform as expected.

Practically speaking, a reasonable scenario which we use for this analysis is for retroactive dividend payments to be included in the FY 2022 budget, though a supplemental FY 2021 appropriation would also be a possibility. Based on the August 2020 "History and Projections" from APFC, the POMV withdrawal for FY 2022 is fixed at $3,069 million and the expected ending value of the earnings reserve account is $13.1 billion (including $11.6 billion of realized earnings). Assuming that funds for retroactive dividends were withdrawn at the end of FY 2022, the expected ending value of the earnings reserve account would be $8.0 billion (including $7.0 billion of realized earnings). ERG modeling suggests that if the Permanent Fund achieves the forecasted 6.75% annual return, then a POMV of at least $3.2 billion could be maintained going forward after FY 2022. However, future investment returns are uncertain and changes to investment returns or outlook could impact this projection: lower earnings reserve balances necessarily increase the state's exposure to future investment volatility.

3. ***Please provide a table similar to slide 16 that shows producer take under current oil tax law (SB21) and under BM1.***

The BM1 initiative contains several provisions that require interpretation and clarification. This analysis represents one possible interpretation of the initiative and does not represent a final decision on these provisions and should be used accordingly. The Department of Revenue is in the process of reviewing and updating the data on which this analysis is based. As a result, future analyses could have different results.

The following chart provides the information from slide 16, with SB21 comparisons included for all price points.

This analysis provides estimates of how profits from oil production are shared between the different stakeholders at different prices. This analysis is based on Spring forecast assumptions for FY 2022 for the oil production impacted by BM1. Based on Revenue's understanding of Ballot Measure 1 as described by the sponsors, this analysis assumes that the qualifying production is from Prudhoe Bay, Kuparuk River, and Colville River.

	Current Law (SB21)					Impacts of Ballot Measure 1				
Price/BBL	$35/bbl	$45/bbl	$55/bbl	$65/bbl	$75/bbl	$35/bbl	$45/bbl	$55/bbl	$65/bbl	$75/bbl
State Take - Taxes	19%	12%	11%	11%	16%	47%	24%	28%	30%	31%
State Take - Royalty	66%	30%	23%	20%	18%	66%	30%	23%	20%	18%
State / Muni Take - Property Tax	27%	9%	5%	4%	3%	27%	9%	5%	4%	3%
Total State / Muni Take	112%	50%	38%	35%	37%	140%	62%	56%	53%	52%
Federal Take	0%	10%	13%	14%	13%	0%	8%	9%	10%	10%
Producer Take	-12%	39%	49%	52%	50%	-40%	30%	35%	37%	38%

Note: Numbers may not add due to rounding.

4. Is the producer take under current oil tax law (SB21) competitive with other tax regimes?

The State of Alaska has not undertaken recent analysis comparing Alaska to other fiscal regimes and has not been directly involved with any third parties who have done so. Therefore, the state cannot verify the data that may have gone into any comparison. However, since it is publicly available, the following is a link to a presentation by IHS Markit consultants, who were engaged by the American Petroleum Institute to conduct an independent competitiveness study that attempts to document how Alaskan oil fields would compete for investments in the domestic and international markets both under current law and if Ballot Measure 1 were enacted:. https://www.commonwealthnorth.org/wp-content/uploads/2020/09/CWN-Forum-090220-Irena-Agalliu-1.pdf

Our statement in the hearing that Alaska is generally competitive with other jurisdictions under current law was based on this and other analysis showing that Alaska's government take is within the range of other jurisdictions in its peer group.

I hope you find this information to be useful. Please do not hesitate to contact me if you have further questions.

Sincerely,

lucinda mahoney

Lucinda Mahoney
Commissioner,
Department of Revenue