

HOUSE FINANCE COMMITTEE
March 16, 2022
9:05 a.m.

9:05:10 AM

CALL TO ORDER

Co-Chair Foster called the House Finance Committee meeting to order at 9:05 a.m.

MEMBERS PRESENT

Representative Neal Foster, Co-Chair
Representative Kelly Merrick, Co-Chair
Representative Dan Ortiz, Vice-Chair
Representative Ben Carpenter
Representative Bryce Edgmon
Representative DeLena Johnson
Representative Andy Josephson
Representative Bart LeBon
Representative Sara Rasmussen
Representative Steve Thompson
Representative Adam Wool

MEMBERS ABSENT

None

ALSO PRESENT

Dan Stickel, Chief Economist, Economic Research Group, Tax Division, Department of Revenue; Brian Fechter, Deputy Commissioner, Department of Revenue.

SUMMARY

HB 281 APPROP: OPERATING BUDGET/LOANS/FUNDS

HB 281 was HEARD and HELD in committee for further consideration.

HB 282 APPROP: MENTAL HEALTH BUDGET

HB 282 was HEARD and HELD in committee for further consideration.

PRESENTATION: SPRING FORECAST BY THE DEPARTMENT OF REVENUE

Co-Chair Foster reviewed the meeting agenda.

#hb281

#hb282

HOUSE BILL NO. 281

"An Act making appropriations for the operating and loan program expenses of state government and for certain programs; capitalizing funds; amending appropriations; making reappropriations; making supplemental appropriations; making appropriations under art. IX, sec. 17(c), Constitution of the State of Alaska, from the constitutional budget reserve fund; and providing for an effective date."

HOUSE BILL NO. 282

"An Act making appropriations for the operating and capital expenses of the state's integrated comprehensive mental health program; making capital appropriations and supplemental appropriations; and providing for an effective date."

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^PRESENTATION: SPRING FORECAST BY THE DEPARTMENT OF REVENUE

[9:06:16 AM](#)

DAN STICKEL, CHIEF ECONOMIST, ECONOMIC RESEARCH GROUP, TAX DIVISION, DEPARTMENT OF REVENUE, provided a PowerPoint presentation titled "Spring 2022 Forecast Presentation: House Finance Committee," dated March 16, 2022 (copy on file). He reviewed Slides 2 and 4. Slide 2 was titled "Agenda:"

1. Forecast Background, Economic Indicators, and Key Assumptions
2. Spring 2022 Revenue Forecast
 - Total State Revenue
 - Unrestricted Revenue
3. Petroleum Forecast Assumptions Detail
 - Oil Price

- Oil Production
- Oil and Gas Lease Expenditures
- Oil and Gas Transportation Costs
- Oil and Gas Credits

Mr. Stickel addressed Slide 4 titled "'Background: Spring Revenue Forecast:"

- 1.Historical, current, and estimated future state revenue
- 2.Updates key data from Fall Revenue Sources Book
- 3.Official revenue forecast used for final budget process
- 4.Located at tax.alaska.gov

Mr. Stickel informed the committee that the spring forecast updated the Fall Revenue Sources Book that was only published once a year.

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Mr. Stickel moved to slide 5 titled "Key Alaska Economic Indicators." He reported that although the focus of the Department of Revenue (DOR) was on state revenue, they analyzed the broader Alaskan economy. He discussed the table on the slide representing Alaska's economic indicators that was updated on March 14, 2022. He noted that the state Gross Domestic Product (GDP) slightly increased in the third quarter of 2021. He elaborated that since the end of 2020, GDP was flat and was down 6 percent when compared to the same period in 2019. The data indicated that the value of the economy was holding steady, but it was not fully recovered from the pandemic. He added that the fourth quarter data would begin to reflect the higher oil prices and would be available on March 31.

Representative Wool cited the real GDP of \$53 million in 2019 compared to \$50 million in 2020 and noted DOR's expected increase in the next quarter. He asked what percentage of oil comprised GDP. Mr. Stickel answered that he did not have the number on hand. He elaborated that typically oil was the significant contributor to the state economy and GDP through its production and associated benefits to other industries. The industry breakdown was available in the GDP data, and he offered to provide it to the committee. Representative Wool pointed to the 2021 third quarter and noted the significantly lower GDP. He

inquired whether it reflected the calendar year and what the price of oil was in the third quarter of 2021. Mr. Stickel referenced a chart later in the presentation and estimated the price of oil had been about \$70 at the time and had steadily increased as well as a broader opening of the economy and possible increases due to tourism.

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Mr. Stickel continued to review slide 5. He relayed that employment had increased by 2.7 percent or 8,000 jobs but remained lower than the 12,000 jobs in the same quarter of 2019. The state had rebounded to an increase of 24,000 jobs since the lows of the pandemic recession and was still down by over 53 thousand jobs compared to July 2019. He noted that transportation, oil and gas, and hospitality sectors were the largest contributors to the lower job numbers. He commented that wages and salaries had recovered from the pandemic lows. He ascribed it to a combination of some job increases and strong wage increases due to the tight labor market. He indicated that bankruptcies and foreclosures were both lower than in pre-pandemic levels. He attributed the decrease to government and industry programs that helped people pay their bills and remain in their homes. He offered that housing starts increased from 2020 to 2021 and ended the year at pre-pandemic levels. He reported that mortgage delinquency rates continued to decline due to the strong labor market, robust growth in housing prices, and programs by lenders that offered borrowers payment flexibility.

Representative Carpenter asked how Mr. Stickel would characterize GDP and real wages in relation to inflation in 2021. Mr. Stickel answered that the total wages were in nominal terms and were increasing therefore, the cost of employing people was increasing. He observed that the GDP was flat indicating income and cost growth in nominal terms but in real terms the economic activity was flat.

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Mr. Stickel spoke to Slide 6 titled "Spring Forecast Assumptions:"

The economic impacts of COVID-19 and geopolitical events are uncertain; DOR has developed a plausible scenario to forecast these impacts.

•Key Assumptions:

Investments: Stable growth in investment markets, 5.86% for FY 2022 and 6.20% for FY 2023+.

Federal: The forecast incorporates stimulus funding as of March 1, 2022, includes updated estimates of IIJA funding.

Petroleum: Alaska North Slope oil price of \$91.68 per barrel for FY 2022 and \$101.00 per barrel for FY 2023.

Non-Petroleum: Continued economic growth. 75% of capacity assumption for 2022 cruise season, minerals prices based on futures markets.

Mr. Stickel characterized the slide as demonstrating uncertainty. He related that COVID-19 was still a source of uncertainty and another major uncertainty pertained to geopolitical events and the war in Eastern Europe. He communicated that DOR was not predicting a recession. The division estimated 1.5 million cruise ship passengers as the long term annual capacity and predicted continued growth. He noted that mining activity revenues had increased slightly.

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Representative Johnson referred to slide 6 and asked how the investment projection had been calculated. Mr. Stickel answered that the estimates were prepared by Callan Associates that were contracted by the Alaska Permanent Fund Corporation (APFC). The department worked with APFC to generate the investment returns data.

Representative Wool cited the FY 22 average price of oil. He asked what the price need to be for the remainder of the year to maintain the average. Mr. Stickel replied that the monthly outlook was over \$100 per barrel of oil. Representative Wool asked if he had the exact number. Mr. Stickel responded that he did not have the detailed monthly breakout but offered to provide it to the committee. Representative Wool guessed that a number had been generated and assumed that Mr. Stickel had forgotten the numbers. Mr. Stickel replied that the estimate was calculated using real prices through the end of February

2022 and estimated the prices for the remaining four months. He recalled that Slide 18 did portray the monthly data. Representative Wool pointed out that oil prices had been \$140 per barrel, and it was now below \$100 per barrel. Mr. Stickel maintained that the forecast addressed uncertainty.

Co-Chair Foster referenced Mr. Stickel's statement that the price would need to be over \$100 per barrel to maintain the forecasted price of \$91.68. He relayed that he had heard the price would need to be \$115 per barrel. Mr. Stickel answered that the number was in the realm of accuracy.

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Representative Edgmon asked if they did any standard deviation analysis. He conveyed that in looking at a stock market analysis, statistical modeling was performed to ascertain the probability of the prediction actually happening versus offering a flat number. He voiced that the legislature had to build a budget around the number. He noted that some analysts thought the price was going to increase and others did not. He noted the uncertainty of oil prices and its relation to current world events. He wondered what the probability of the predicted price of oil maintained at \$101 per barrel was. Mr. Stickel replied that the department paid attention to volatility and the range of potential outcomes. He could share some slides related to price volatility he prepared for another committee. He expounded that one of the slides examined the implied range of oil prices from the options market and based on that demonstrated a range of potential oil prices. He also could provide a straight sensitivity analysis that examined a range of oil prices from \$10 per barrel to \$150 per barrel and the amount of revenue for each level.

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Mr. Stickel turned to Slide 7 titled "Relative Contributions to Total State Revenue: FY 2021." He reported that total state revenue was \$29.8 billion in FY 21. He noted that investment earnings provided the largest share of revenue at 65.8 percent. He detailed that the number was driven by some unusually high returns for the Alaska Permanent Fund (PF) at 30 percent combined with robust federal revenue due to the stimulus packages.

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Mr. Stickel moved to slide 8 titled "Relative Contributions to Total State Revenue: FY 2023." He pointed out that the total state revenue was expected to change [\$16.4 billion] and oil and gas, federal revenue and investment earnings were the largest and equal sources [Approximately 30 percent each]. He noted that oil and gas was predicted to be the largest source of income at 31.4 percent.

Representative Wool looked at federal revenue of 31.2 percent. He asked if it included the Infrastructure Investment and Jobs Act (IIJA) funding and COVID stimulus money. Mr. Stickel responded that the division worked with the Office of Management and Budget (OMB) on the number and confirmed that it included the last of the COVID stimulus funding and the IIJA money.

Representative Edgmon remarked that the petroleum and revenue ratios were like those in 2013 and 2014 and the investment earnings were minimal. He asked for a comparison to prior years. Mr. Stickel referenced a figure from the Fall Revenue Sources Book (Figure 2-B) that depicted a graphic of the 10-year comparison to the slide's numbers. He confirmed that petroleum revenue was the largest share and investment revenue could be volatile where it was high in 2021 and modest in 2015. Representative Edgmon pointed out that the price of oil had dropped precipitously in 2016 to \$26 per barrel and the state had a \$4 billion deficit.

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Vice-Chair Ortiz referenced federal revenue at 31.2 percent. He wondered how the current percentage compared to historical averages. Mr. Stickel replied that federal revenue had been a stable revenue source. He delineated that it typically was around one-third of state revenue, and the current number was on par with historical averages.

Mr. Stickel moved to slide 10 Titled "Unrestricted Revenue Forecast: FY 2021 and Changes to Two-Year Outlook." He offered that the slide compared the key changes in unrestricted revenue, forecast for the current and next fiscal year. He related that the oil price had significantly increased by \$15.96 in FY 22 and by \$30 in FY 23. He expounded that the increases were attributed to a continued recovery in the oil market based on the futures

market and the Russian invasion of Ukraine had caused prices to spike rapidly. The PF transfer did not change and the entire change in unrestricted revenue was ascribed to the increased price of oil. He remarked that the forecast was increased by \$1.2 billion in FY 22 and \$2.4 billion in FY 23. The slide did not show Alaska North Slope (ANS) oil production - it was essentially unchanged from the fall forecast.

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Co-Chair Foster noted Representative Rasmussen had joined the meeting.

Representative Carpenter inquired what impact the current instability in Eastern Europe had on the price of oil and if there were some other events that had impacted the price of oil even more.

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Mr. Stickel responded that broadly speaking since the middle of 2020 the oil demand had rebounded strongly since the lows of the COVID recession and production had been slower to catch up therefore, demand had been increasing faster than supply leading to higher prices. The instability was layered on top of an already tight oil market.

Vice-Chair Ortiz asked if the FY 23 oil price forecast of \$101 per barrel was derived using a variety of national forecasting models or was there a specific model. Mr. Stickel answered that a future slide had detailed data. He indicated that the division used future's market data for Brent Crude Oil and based it on the median 5 day futures ending on March 9, 2022. Vice-Chair Ortiz inquired whether it was the historical method. Mr. Stickel responded that DOR used oil futures in projections for the last several forecasts.

Representative Wool referenced the five-day window and thought it was narrow. He asked if they used a model based on a broader view. He speculated that 5 days seemed inadequate. Mr. Stickel replied in the affirmative. He delineated that the division used several other sources and had more detail in a future slide. He explained that the goal of the 5 - day window was to offer a current forecast

and not based on a month ago or longer. He added that if there had been a particular day where oil prices spiked or dropped significantly due to a transient event it was filtered out of the forecast. He exemplified an attack on oil infrastructure in Saudi Arabia in a prior year that substantially increased prices for only one day.

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Representative Wool argued that the price of oil recently dropped from \$140 per barrel to \$100 per barrel "in a couple days," and would considerably affect the forecast if it was near that time. Mr. Stickel agreed with the statement and spoke to the environment of high volatility in the oil market.

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Mr. Stickel moved to slide 11 titled "Total Revenue Forecast: FY 2021 to FY 2023 Totals." He discussed that in the forecasted budget revenues were categorized into 4 types: Unrestricted General Funds (UGF) that were available for any purpose; Designated General Funds (DGF) were customarily appropriated for specific purpose such as alcohol taxes used for treatment and prevention; Other Restricted Revenue appropriations were dedicated to a specific use and were not available for general use like the Constitutionally dedicated portion of royalties that were deposited into the PF. Lastly, federal revenue was considered restricted and were subject to the provisions of the federal government. He relayed that in total the state received \$29.8 billion in revenue in FY 21 and was expected to be \$15.8 billion in FY 22 and \$16.4 in FY 23.

Representative Edgmon shared that the average rate of return for the PF was 11.37 percent over the last 5 years, the year to date was 3.9 percent, and lost \$2 billion in value. He advised that it was an important source of revenue to focus on.

Representative Carpenter cited the non-petroleum revenue in the DGF category and noted the decline in non-petroleum revenue between FY 22 and FY 23 compared to increases in

other categories. He wondered why the portion of revenue was decreasing. Mr. Stickel did not have the detail on hand. He recounted that the non-petroleum revenue in the DGF category included corporate income tax and mining license tax. He was unable to answer regarding the other categories and would follow up.

Representative Carpenter wanted to focus on non-petroleum revenue and deduced that it reflected jobs in oil versus non-oil and how money was flowing into the state. He believed that it was a focus of the majority of Alaskans and how they live and work. He thought that was a recognition of the state's economy growing. He requested data aimed at the number of people working in non-petroleum jobs.

Representative Edgmon remarked that the state was significantly tied to oil. He guessed that it had to reflect at least one-third of the state's revenue. He ascertained that as the state transformed to an endowment driven budget where the Permanent Fund Percent of Market Value (POMV) provided 50 percent of UGF income, Alaska was still largely tethered to the oil industry.

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Representative Josephson referenced the \$16 billion in investment revenue. He asked where the money would be reflected. He asked if it would come into the Earnings Reserve Account (ERA) over time as unrealized became realized earnings. Mr. Stickel explained that the approximately \$16.3 billion in FY 21 represented earnings of the PF beyond the 5.25 POMV transfer (\$3.1 billion in FY 21) to the PF and represented a nearly 30 percent return on investments. The investment earnings were included in "other restricted revenue" and the earnings would be in either unrealized or realized earnings. He offered that some of the earnings were unrealized. Representative Josephson asked if everything that was unrealized eventually became realized. Mr. Stickel replied by saying, "not necessarily." He indicated that a gain in an investment that declined would not be realized. Stable returns and stable gains would eventually become realized gains.

Representative Wool asked whether the investment earnings could be considered revenue. He maintained that it was an

increase in value, not all was realized, and therefore, was not really revenue. Mr. Stickel answered that unrealized gains of the PF were considered revenue in accordance with the Governmental Accounting Standards Board (GASB) principles. However, the gains were not available to spend, which was why it was designated as other restricted revenue versus UGF revenue.

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Mr. Stickel turned to slide 12 titled "Unrestricted Revenue Forecast: FY 2021 to FY 2023 Totals." He shared that investment revenue was one of the largest sources of unrestricted revenue. He noted that the largest source of revenue in FY 22 and FY 23 was expected to come from petroleum revenue. He noted that in FY 23 investment revenue was expected to total \$3.4 billion. He added that petroleum revenue was anticipated at \$4.4 billion and about \$500 million of non - petroleum revenue for a total revenue of \$8.3 billion and just under \$7 billion in FY 22.

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Mr. Stickel discussed slide 13 titled "Unrestricted Investment Revenue: FY 2021 to FY 2023." The chart depicted total UGF. He pointed out that the POMV transfer accounted for 40 percent and 62 percent of unrestricted revenue over the 10-year forecast. He delineated that DOR anticipated investment earnings increasing and oil prices moderating. He pointed to the small portion of investment revenue from the general fund that was forecasted at -\$4.7 million for FY 22 but expected it to return positive in FY 23.

Representative Rasmussen asked for the predicted rate of return over the next 10 years for the PF. Mr. Stickel answered they were expecting a 5.86 percent rate of return for FY 22 and a 6.2 percent for FY 23 and beyond based on Callan and Associates projections.

Representative Edgmon mentioned the \$1.5 billion of federal money for broadband as well as other large infusions of federal dollars. He asked whether any of the modeling included the federal funding.

Mr. Stickel responded that to the extent federal revenues flowed through the state it was included in the revenue forecast. He detailed that all the federal revenues were

considered restricted. The department forecasted the infrastructure funding from FY 23 through FY 27 and was included in the restricted portion of revenue.

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Representative Edgmon understood that there was no way to forecast the total amount of federal funding coming to Alaska. He deemed that the federal funding was a supplement to the current revenue forecast, but also unknowable and could be significant.

Mr. Stickel looked at Slide 14 titled "Unrestricted Investment Revenue: Percent of Market Value (POMV) Transfer Forecast:"

- Permanent Fund total return for FY 2021 of 29.7%.
- The statutory POMV rate changed to 5% beginning FY 2022.
- For FY 2019 -FY 2021 this rate was 5.25%.
- Forecast assumes Permanent Fund's long-term total return expectation of 6.20% for FY 2023+; 5.86% for FY 2022.
- Differing Permanent Fund returns, and petroleum deposits could significantly alter actual POMV amounts.

Mr. Stickel delineated that the graph portrayed the POMV transfer to the general fund over the next 10 years, expected to be over \$3 billion every year, growing to \$4.7 billion by FY 2032. He reported that the fiscal year to date return, as of the end of January was 3.95 percent. The PF was a stable source of income for the state based on the trailing market average calculation used for the POMV transfer that filtered out year to year volatility in the value of the fund. The baseline was based on the POMV draw and did not account for any ad hoc draw or potential contributions beyond the mandated royalty contributions.

Co-Chair Foster relayed the meeting would recess until 1:30 p.m.

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Co-Chair Foster called the meeting back to order.

Mr. Stickel continued with slide 14 to address questions from earlier in the meeting. He addressed a question regarding slide 5 and the percentage of GDP from oil revenue. He communicated that in calendar year 2020, the most recent full year of data, about 21 percent of total GDP was derived from the oil and gas industry and it was 26 percent if excluding government. The transportation and warehousing industry comprised 10 percent of GDP and 13 percent if excluding government and mostly represented pipeline transportation.

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Representative Wool asked what the GDP percentage of oil and gas industry was comprised of. Mr. Stickel had stated that the amount represented the value of the oil itself and not the taxes paid.

Mr. Stickel responded to an earlier question raised concerning slide 5. He voiced that the price of oil in the third quarter of 2021 was \$73 per barrel of oil.

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Mr. Stickel addressed a question regarding slide 6 and the average price of oil necessary in the remainder of FY 22 to hit the forecasted price. He divulged that the average price necessary was \$114.57 per barrel of oil and broke down the average price by remaining months as follows: \$113.80 for March, \$113.32 for April, \$117.24 for May, and \$113.91 for June.

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Mr. Stickel answered a question about volatility assumptions on slide 6 and shared some statistics. He reported that for FY 22 the department used a 10 percent and 90 percent probability ranging from \$80.76 bbl. to \$110.26 in FY 22 and in FY 23 the range was \$62.50 bbl. up to \$163.43 bbl.

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Mr. Stickel moved to slide 11 to answer the question concerning why non-petroleum DGF was decreasing. He

responded that it had to do with two one-time impacts in the FY 21 and FY 22 numbers. He explained that in FY 21 a larger than usual transfer was taken from the Alaska Capital Income Fund that was invested concurrently with the PF and reflected the strong PF earnings in FY 21. The FY 22 budget included some one-time revenue from refinancing the Tobacco Securitization Fund and reflected a return to normal rather than a decrease.

Representative Josephson asked if the petroleum revenue on slide 11 reflected a 50 percent royalty or 25 percent royalty to the corpus of the PF. Mr. Stickel responded that the 25 percent Constitutionally required deposit to the PF was included in "other restricted revenue." The other 25 percent for certain leases issued in 1980 and beyond was included in DGF. He furthered that there were 2 elements of royalties deposited into the PF, the constitutionally required 25 percent denoted as other restricted revenue and an additional 25 percent deposited via statute signified as DGF.

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Mr. Stickel moved to slide 15 titled "Unrestricted Petroleum Revenue: FY 2021 to FY 2023 Totals." The chart detailed the unrestricted general fund petroleum revenue. He noted the four main sources of unrestricted petroleum revenue: Petroleum Property Tax; Petroleum Corporate Income Tax; Oil and Gas Production Tax; and Royalties. He elaborated that property tax was levied on all oil and gas production property in the state and was a stable source generation over \$1 million each year. He elucidated that in addition to the state share a municipal share generated over \$400 million. The state levied a corporate income tax and applied to the profits of almost all the oil producers. In FY 21, the state paid out \$19 million in refunds due to losses caused by COVID 19. In FY 22, oil revenue was expected to increase to \$190 million and \$340 million in FY 23. Included in the estimates was a federal provision from the Coronavirus Aid, Relief, and Economic Security (CARES) Act that allowed the oil companies to carry back losses from calendar year 2018 to 2020 and receive refunds. The estimated impact was \$2.4 million for FY 21 and \$79.4 million in FY 22, which was included in the forecast. The production tax on oil and gas was anticipated to significantly increase due to the forecasted higher prices at \$1.9 billion in FY 22 and \$2.5 billion in FY 23.

Finally, royalties from the production of oil and gas on state land was no longer the largest source of petroleum revenue but remained a significant source of revenue forecast at \$1.3 billion in FY 22 and \$1.15 billion in FY 23.

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Mr. Stickel continued to slide 16 titled "Unrestricted Non-Petroleum Revenue: FY 2021 to FY 2023." He explained that non-petroleum taxes represented the largest share. The non-petroleum corporate income taxes generated \$102 million in revenue in FY 21 and was impacted by the COVID related loss carry forwards that refunded \$6.7 million in FY 21 and was estimated at just under \$80 million in FY 22, which was the reason for the decline in non-petroleum revenue. He elucidated that other significant taxes included mining license taxes, insurance premium taxes, fisheries taxes, and excise taxes. He pointed to mining licenses taxes and expected significant increases in FY 22 and FY 23 due to higher prices. In total, non-petroleum taxes would generate roughly \$220 million and \$370 million in FY 23. He noted that the "Other" Unrestricted Non-Petroleum Revenue category included: Charges for Services, Fines and Forfeitures, Licenses and Permits, Rents and Royalties, and Miscellaneous Revenue and Transfers.

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Mr. Stickel announced that the last section of the presentation addressed the petroleum forecast assumptions in detail. He began with slide 18 titled "Petroleum Detail: Changes to Long-Term Price Forecast." The graph portrayed how the Fall 2021 forecast increased in the Spring 2022 forecast. He indicated that the department changed its methodology in the fall of 2021 and began employing oil futures markets predicted through 2029. He delineated that the shift was from a prior methodology that used the first two years of futures predictions and then assumed a constant real price. The change was made to provide a more useful revenue forecast for long range fiscal planning. He reiterated that for the spring forecast they used the median futures outlook for the 5 trading days ending March 9, 2022, which resulted in a price increase of roughly \$16 per barrel for FY 22, \$30 bbl. for FY 23, and an estimated \$8 to \$9 per barrel increase through 2029.

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Mr. Stickel moved to slide 19 titled "Petroleum Detail: Nominal Brent Forecasts Comparison as of March 14, 2022" that showed a comparison to other forecasts. He noted that the graph was updated on March 14, 2022. The graph depicted a comparison of DOR's revenue forecast to the Futures Market as of March 14, 2022, as well as the Analysts Forecast, and the U.S. Energy Information Administration (EIA) forecast from their March 2022 Short-Term Energy Outlook (STEO). He observed that DOR's forecast was higher than the other forecast due to the timing of March 9, 2022, prior to the decline over the last week. Even with the decline in price, the forecast remained within the general range of the other forecasts.

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Representative Carpenter thought it was interesting to see like minds coming up with the same trends. He asked if the other entities were making the same predictions or assessments regarding the effects of the war between Russia and Ukraine. He wondered if there was an agreement on the outcome of the war and whether it was reflected in the predictions. Mr. Stickel suggested that the oil market impact was concentrated on the short-term and the EIA STEO Forecast relied heavily on the Futures Market for its outlook. In terms of analyst predictions, he considered it a median "consensus forecast;" some analysts had much different outlooks.

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Representative Wool commented that the state was currently using the futures market forecast. He wondered if the state's predictions were higher because of basing it on the earlier week in March when prices were higher. Mr. Stickel responded in the affirmative. He noted that the data on Slide 19 was pulled from closing future prices on March 14, 2022 and demonstrated a shift in the futures market since the state's forecast.

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Representative Wool guessed the difference in a couple of days "played out for years." He referenced that earlier Mr. Stickel mentioned that the spike in oil was due to the war

in the Ukraine and a shortage due to COVID. He inquired whether the refineries and production facilities would catch up to the demand and offset the spike increase. Mr. Stickel thought the world was in a period of undersupply trying to catchup to demand. He elaborated that high prices would impact future supply and demand. As prices remained high, companies would look to increase production while consumers would reduce demand. The prediction was that the process would play out in future years resulting in the longer term price of approximately \$70 per barrel range.

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Mr. Stickel continued to slide 20 titled Petroleum Detail: UGF Relative to Price per Barrel (without POMV): FY 2023." He referenced the discussion regarding volatility and uncertainty and felt that it was an important slide which showed how unrestricted revenue in FY 23 would change with different levels of oil prices. The graph depicted the \$101 bbl. forecast generating \$5 billion in unrestricted revenue. He qualified that the data did not include the POMV transfer from the PF. He reported that near the forecasted ANS price, a \$1 increase or decrease in price led to an approximately \$80 to \$85 million change in UGF revenue.

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Mr. Stickel moved to slide 21 titled "Petroleum Detail: North Slope Petroleum Production Forecast." He shared that the production forecast was developed in collaboration with the Department of Natural Resources (DNR). He conveyed that production would decrease in FY 22 followed by modest increases over the next several years with oil production averaging 535 thousand barrels per day by 2030. The stable to slightly increasing production was due to a couple of factors, including resumption in drilling from the COVID period. There was also the anticipation of additional new production. He noted that the high and low predictions represented the uncertainty in the forecast.

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Mr. Stickel presented slide 22 titled "Petroleum Detail: Changes to North Slope Petroleum Production Forecast" that showed the changes from the Fall FY 21 forecast to the

Spring 22 forecast. There were not significant changes in the production forecast.

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Mr. Stickel advanced to slide 23 titled "Petroleum Detail: North Slope Allowable Lease Expenditures." He indicated that the graph showed how the North Slope allowable lease expenditures changed over the prior decade and forecasted the next 10 years. In addition, historical data regarding oil and gas employment was included to show the correlation between spending and jobs. He reported that in FY 21, North Slope capital expenditures were \$1.5 billion and had \$2.4 billion in operating expenditures with significant cutbacks due to the COVID pandemic. The state was anticipating some slight increases in spending in FY 22 and significant increases in FY 23 to FY 25. There was a possibility that final investment decisions would be made in the current year leading to higher capital spending.

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Representative Wool brought up operating expenditures. He asked if the payroll stayed higher than the number of employees and deduced that capital expenditures tracked the number of employees more than operating expenditures. He asked whether he was correct. Mr. Stickel responded that the ongoing cost of employees in the field was reflected in operating expenses. The larger driver for employment was capital spending. He detailed that many of the fields had become automated, but a certain baseline number of employees was required. Certain activities related to drilling and building a pad were labor intensive. The projection for increased capital costs in FY 23 and beyond for development of new fields was the potential driver for increased employment. Representative Wool understood that capital expenses tracked employment better than operating expenses in the oil industry. Mr. Stickel indicated that he was correct.

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Representative Josephson asked if the qualified expenses would meet the requirements for credits against profits under the carry forward lease expenditure program of HB 111 [- Oil & Gas Production Tax; Payments; Credits / CHAPTER 3 SSSLA 17/ 07/27/2017]. He argued that the state had a hand

in paying for some of the industry expenses. Mr. Stickel replied in the affirmative. He purported that the allowable lease expenditures were "important" because they indicated industry activity and were deductible against production tax. To the extent that a company had production and available gross value, the expenses were subtracted against the gross value of oil or gas to determine the production tax value similar to the net profit value. He furthered that if a company lacked sufficient gross value or was in the development stage, the expenses turned into carry forward lease expenditures and once the company came into production the expenses could be applied towards future tax liability.

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Mr. Stickel advanced to slide 24 titled "Petroleum Detail: North Slope Transportation Costs." The slide reviewed the transportation costs of getting the oil to market per barrel of oil. The costs were based on tanker costs, Trans Alaska Pipeline (TAPS) tariffs, and other costs. He relayed that in FY 21, the average transportation cost was \$9.19 bbl. The department forecasted \$9.71 bbl. in FY 22, and \$9.40 bbl. in FY 23. The expectation was that transportation costs would stay under \$10 per barrel in the 10-year forecast due to stable and slightly increased production.

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Representative Johnson asked Mr. Stickel to remind her generally how the transportation costs were calculated. She recalled that they did not fluctuate as much as oil prices. She deduced that a direct correlation between transportation costs and the price of oil did not exist. Mr. Stickel spoke to the drivers of the transportation costs. He explained that marine or tanker costs were partly related to the price of oil; increased oil prices increased fuel costs and increased the cost of operating the tankers. It was one of the reasons for the increase in transportation costs on slide 24. Pipeline costs and tariff costs were based on the costs of pipeline operations plus an allowable return to the pipeline operator. The costs were divided by the number of barrels of oil transiting the pipeline. The more barrels transiting TAPS the per barrel cost decreased due to its fixed operating costs.

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Representative Carpenter asked if the reason why there were decreased transportation costs on slide 24 was due to the predicted increase in production. Mr. Stickel responded that TAPS costs and other costs were driven by the increased production forecast. The marine transportation costs were driven by lower oil prices that reduced the operating costs for the tankers. Representative Carpenter asked what the expectation of inflation was. Mr. Stickel indicated the revenue forecast included a 2.4 percent assumption for inflation.

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Representative Josephson thought it was good to be more conservative even with the forecasted increase in the price of oil. He returned to slide 19 and referred to the \$1 bbl. change reflecting \$85 million and relying on data on March 9, 2022. He asked what differential the state would see if they based the forecast on March 16, 2022. Mr. Stickel deduced that looking at the futures market in the present day the forecasted price would be about \$90 per barrel in FY 23.

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Representative LeBon was trying to understand the 5 day window in which prices were based. The student base allocation (BSA) number was based on a 30-day period. He asked why the forecast would not use a 30-day count. Mr. Stickel responded that using a 5-day window was to offer the timeliest forecast using the most recent outlook while still employing a mechanism to filter out any one specific day with a large price swing. Representative LeBon suggested that a 30-day average would have more of a smoothing effect. He thought a 30-day average was more conservative. He assumed that the spring and fall forecasts, based on a 6-month forecast, might be self-correcting.

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Representative Johnson cited the drop reflected on slide 19 of the analysts' prediction. She wondered what the reason was for the decline.

Mr. Stickel replied that there were a few different possibilities and it depended on the specific analyst. He speculated that the longer-term prices might not reflect some of the more recent market activity. Representative Johnson asked Mr. Stickel if he was more comfortable with the curve of the graph rather than the numbers on the graph. Mr. Stickel noted that in the last month or so there had been a significant amount of volatility in near term oil prices. The long-term prices had remained in the mid \$60's bbl. to mid-\$70's bbl. He ascertained that the anchoring of a long-term price was more reliable. Much of the volatility was around the short-term price.

Representative Wool referenced slide 19 and asked if the futures market line used a 5 day window and whether it was a different 5 day window. Mr. Stickel replied that the futures number reflected only 1 day - March 14, 2022. Representative Wool noted that on the DOR forecast line the price remained around \$100 bbl. for 2023 and if the 5 day window was based on today at \$98 bbl. the entire graph would look much different, and the curve would be below the futures market. He asked if he was accurate.

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Mr. Stickel replied that if the graph was updated in the current day, the chart would be similar to the futures market price listed. He emphasized that the department was releasing monthly revenue updates based on the prevailing prices.

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Representative Josephson suggested that if the calculation was made in the present day and the DOR forecast line was the same as the futures market line the difference would be multiple hundreds of millions of dollars. Mr. Stickel reiterated the "rule of thumb" that for FY 23; each \$1 change equated to about \$80 million to \$85 million in UGF revenue.

Vice-Chair Ortiz offered that the committee was tasked with budgeting for FY 23 and the oil price forecast was \$101 bbl. He asked that if the goal was to be protective and conservative in the appropriations process. He wondered if basing the budget on \$85 bbl. oil prices take a more conservative approach. Mr. Stickel responded that \$85 would

be conservative based on the current forecast and relative to the markets. He voiced that it was a policy decision.

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Representative Carpenter favored a conservative approach. He brought up the current war in Eastern Europe. He deduced that the forecast suggested that the effect of the war would not result in a high price of oil in the future. He guessed that many forecasters believed that the situation would resolve itself and did not include an escalation resulting in higher oil prices. However, regarding inflation, it was estimated to only increase by 2.5 percent. He opined that a more conservative approach would use a higher inflation assumption based on the oncoming influx of federal stimulus money. He favored the conservative approach to forecasting the price of oil but was lacking in consideration of rising costs and inflation.

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Representative Edgmon asked about DOR's monthly forecast. He wondered if it had ever been done. Mr. Stickel responded that it had been done internally for years. However, in February 2022, the department decided to publish the monthly forecast if there was greater than a 10 percent difference from the official forecasts. Representative Edgmon did not understand why the forecast would be done monthly because of the volatility in prices. Mr. Stickel deferred the answer.

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BRIAN FECHTER, DEPUTY COMMISSIONER, DEPARTMENT OF REVENUE, answered that the department was acknowledging volatility and was attempting to provide policy makers the most up to date information. Representative Edgmon was skeptical about the motivation by the department. He suggested it was about policy to justify paying a higher Permanent Fund Dividend (PFD). He stated that he did not see the utility in monthly updates given a spring and fall forecast. He noted the spring forecasts had been the guidepost in developing the budget and the fall acted as course correction. He thought the intent of making the information public was a motivation to influence policy makers regarding the PFD. He voiced that he was not "comfortable" with the decision to issue monthly updates. Mr. Fechter responded that the

Alaska Permanent Fund Corporation (APFC) provided monthly projections and posted it on their website. He furthered that the monthly update would be released if a 10 percent change occurred in either direction. The intent was to provide the most up-to-date information in any direction. Representative Edgmon remarked that it was a departure from the way the legislature previously received the information. He argued that the APFC did not depend on oil production, and it had a diversified portfolio. He reiterated his skepticism.

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Co-Chair Foster shared Representative Edgmon's concerns. He was also concerned with the low estimate of inflation and wondered how that would affect the budget in the future.

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Representative LeBon asked if Mr. Fechter would agree that a 30-day projection would be a more conservative approach when calculating the futures price. Mr. Fechter responded that it would depend on the market conditions at the time. He could think of plenty of periods of time when oil prices were very volatile in a 30 day period. He surmised that it depended on present market conditions.

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Representative LeBon asked Mr. Stickel if it would be easy to do a 30-day look back and provide the information to the committee. Mr. Stickel replied in the affirmative.

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Representative Wool asked about the monthly projection. He expressed confusion regarding what information would be included and asked for clarification. Mr. Stickel responded that the information would be provided if either the projection for the current or next fiscal year UGF revenue was more than 10 percent above or below the official forecast. The document was released on its website, and anyone could be added to a distribution list. The document provided an updated outlook for oil prices and UGF revenue for FY 22 and FY 23.

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Representative Wool wondered whether the update was based on a 5-day or 30 day window. Mr. Stickel responded that the past few updates were based on a single day futures market outlook. Representative Wool asked if it was based on a predictable day. Mr. Stickel replied that typically it was based on or around the 15th of the month.

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Mr. Stickel continued to the final slide of his presentation; Slide 25 titled "Petroleum Detail: Tax Credits for Purchase Detail." He explained that the graph depicted the various tax credits available prior to 2016 that were applied to a tax liability or turned into a tax credit certificate for the state to purchase. In 2016 and 2017 the legislature sunset the program and all credits eligible for state purchase were completely phased out. However, there was an outstanding credit balance of approximately \$532 million. Based on the statutory formula, which was either 10 percent or 15 percent of production tax levied, he estimated a statutory appropriation of \$349 million for FY 23 and a final statutory payment in 2024; the payments retired the statutory obligation.

Representative Josephson asked if the operating budget would include the statutory appropriation of \$349 million. Mr. Stickel replied in the affirmative. Representative Josephson asked if the administration took a position on whether to retire all the credits in the current fiscal year. Mr. Fechter responded that the administration did not have an official position. He suggested that the position was to refund the entire statutory amount through to retirement of the credits.

Mr. Stickel concluded his presentation.

Co-Chair Foster thanked the presenters.

ADJOURNMENT

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The meeting was adjourned at 2:31 p.m.