

SENATE FINANCE COMMITTEE
February 6, 2024
9:02 a.m.

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CALL TO ORDER

Co-Chair Stedman called the Senate Finance Committee meeting to order at 9:02 a.m.

MEMBERS PRESENT

Senator Lyman Hoffman, Co-Chair
Senator Donny Olson, Co-Chair
Senator Bert Stedman, Co-Chair
Senator Click Bishop
Senator Jesse Kiehl
Senator Kelly Merrick
Senator David Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Fadil Limani, Deputy Commissioner, Department of Revenue;
Ryan Williams, State Debt Manager, Department of Revenue;
Senator Cathy Giessel; Dan Stickel, Chief Economist,
Department of Revenue.

SUMMARY

PRESENTATION: STATE DEBT UPDATE

ADMINISTRATION RESPONSE TO PRIOR MEETINGS: DEPARTMENT OF REVENUE

Co-Chair Stedman commented that the committee would review state debt and related issues, and then hear the Department of Revenue's (DOR) response to previous questions raised by the committee.

^PRESENTATION: STATE DEBT UPDATE

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FADIL LIMANI, DEPUTY COMMISSIONER, DEPARTMENT OF REVENUE, introduced himself.

RYAN WILLIAMS, STATE DEBT MANAGER, DEPARTMENT OF REVENUE, introduced.

Mr. Limani discussed a presentation entitled "State of Alaska - Credit Rating Outlook and Debt Summary - February 6, 2023," (copy on file).

Mr. Limani looked at slide 2, "Introduction":

Fadil Limani

Deputy Commissioner, DOR

- Appointed Deputy Commissioner of the DOR in January 2023
- North Slope Borough School District - CFO - 3 years
- North Slope Borough - Deputy Director of Finance - 7 years
- KPMG LLP - 5 years

Ryan Williams

Debt Manager, DOR

- Alaska Department of Revenue - 14 years
- Alaska Department of Revenue - State Debt Manager - 1 year
- Alaska Municipal Bond Bank Authority - Executive Director - 1 year

Mr. Limani spoke to slide 3, "Framework":

- State's Bond Rating Overview
- Recent Bond Rating Meetings
- Credit Rating and Market Feedback
- Current Municipal Market Update
- State's Debt Profile
- State's Debt Capacity

Mr. Limani referenced slide 4, "State's Bond Rating Overview - Bond Rating General Information":

- A bond rating is a way to measure the creditworthiness of a bond, which corresponds to the cost of borrowing for an issuer. These

ratings typically assign a letter grade to bonds that indicates their credit quality.

- Bond ratings are provided by third-party independent rating agencies such as:
 - Standard & Poor's Global Ratings
 - Moody's Investors Service
 - Fitch Ratings Inc.
 - Kroll Bond Rating Agency
- Rating Agencies conduct a thorough financial analysis of the issuer based on their published Public Finance Criteria that generally focus on different but similar primary credit factors
 - Government Framework
 - Financial Management
 - Economy
 - Budgetary Performance
 - Debt and Liability profile
- Bond ratings are critical to alerting investors to the quality and stability of the bonds and the issuer
 - Higher rated bonds "investment grade" provide lower risk and lower borrowing cost
 - Lower rated bonds "non-investment grade" provide for higher risk and higher borrowing cost

Mr. Limani recounted that it was not until the Credit Rating Agency Reform Act of 2006 that the Securities and Exchange Commission (SEC) started regulating rating agencies for criteria and requirements. He discussed the importance of bond ratings.

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Mr. Limani turned to slide 5, "State's Bond Rating Overview":

Importance of Credit Ratings to State of Alaska

- Cost of Borrowing on Capital Improvement Projects
- State Bond Rating Benefits and or Impacts the Alaska Municipal Bond Bank and underlying issuers
- Positive Bond Rating attract national and global investors to the State

Mr. Limani pointed out that the state had not done a new bond authorization in over a decade. He noted that there

were 34 participants that partook in the Alaska Municipal Bond Bank. The rating from the bond bank was generally a notch lower than the state. He mentioned the continuing disclosure requirements.

Mr. Limani considered slide 6, "State's Bond Rating Overview," which showed a table of the bond rating scale. He noted that the state had engaged a rating agency that had assigned an AA, which the state had to publicly disclose to the market. He continued that the investors looking at the data were able to see the uptick in the state's rating. He noted that a higher rating attracted investor groups to do business in the state.

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Co-Chair Hoffman asked which communities were eligible to borrow from the Alaska Municipal Bond Bank.

Mr. Willams noted that he was also the Executive Director of the Alaska Bond Bank. He explained that all political subdivisions of the state were eligible to borrow through the bond bank. Additionally, joint action agencies, joint insurance agencies, the University of Alaska, and regional health organizations were eligible to apply to the bond bank.

Mr. Limani looked at the bond rating scale example on slide 6. He relayed that Moody's had a different scale than the other agencies. He drew attention to the rating descriptions and noted that ratings above a BBB or AAA was considered "investment grade," or "prime grade" quality of credit. A BB and below was considered a low investment grade or "junk bonds."

Mr. Limani displayed slide 7, "State's Bond Rating Overview," which showed a table demonstrating the state's bond rating from the four different bond rating agencies. He highlighted historical ratings in the middle of the slide. He pointed out a rating of BBB in 1961, followed by a rating of A in 1971. Fitch ratings was engaged in 1994 and had assigned an AA rating. On July 20, 2023, the new Kroll Bond Rating Agency had assigned a stable outlook with an AA rating. There had been movements in the state's rating overall, attributed to the state's financial position. He pointed out recent changes with the state's credit profile at the bottom. The agencies other than Kroll

had changed the rating from "negative" to "stable," or "stable" to "positive."

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Mr. Limani highlighted slide 8, "State's Bond Rating Overview," which showed another depiction of the state's credit rating, but in comparison to other states. He noted that there was no ranking shown for the state compared to other states, but the department planned to work on a ranking in the near future.

Co-Chair Stedman observed that California had similar ratings as Alaska. He asked why the state was not rated better than California when Alaska had almost \$80 billion in the Permanent Fund. He asked how the fund interacted with the rating agencies.

Mr. Limani noted that rating agencies looked at different attributes, and Alaska had a unique credit profile. California had a diverse economy in comparison, including a statewide sales tax and income tax and more diverse industry. He noted that Alaska had much higher reserves on a per capita basis, which offset California's advantages somewhat.

Co-Chair Stedman asked if the rating agencies gave any recognition for the ability to implement an income tax if needed.

Mr. Limani relayed that the agencies looked at the volatile movement of the price of oil and considered revenue measures (such as tax initiatives) the state could implement in the case of a deficit.

Co-Chair Hoffman referenced SB 26, which gave the authority to implement the Percent of Market Value (POMV) draw from the Permanent Fund.

Mr. Limani thought that rating agencies were not sure how the POMV draw would work initially, but currently looked favorably on the transfer and considered how much would go towards dividends and how much would go towards the General Fund.

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Senator Bishop asked if rating agencies factored reserves in Prudhoe Bay into calculations.

Mr. Limani affirmed that rating agencies looked at the economic profile of the state, including proven reserves. He noted that upcoming slides would address the topic and particularly the Pikka and Willow projects.

Senator Bishop asked if Mr. Limani would agree that South Dakota looked [economically] healthy.

Mr. Limani agreed and noted that South Dakota had an AAA credit rating.

Senator Bishop pointed out that South Dakota had an income tax, sales tax, and a defined benefit retirement program.

Mr. Limani looked at slide 9, "Recent Bond Rating Meetings":

Bond Rating Upgrade

JUSTIFICATION

- Very Strong Financial Position
 - Ample Reserves: Constitutional Budget Reserve Fund (CBRF) \$2.7 billion, Perm Fund Balance \$76 billion

- Low Debt Load and No New Authorization
 - Well Funded Pension Obligations

- Fiscal Discipline and Budget Management
 - Budget Surplus for main operating fund

- Ample Oil and Gas Natural Resources
 - Estimated to have 52 billion barrels of technically recoverable oil and over 300 trillion cubic feet of undiscovered, technically-recoverable natural gas, plus heavy and viscous oil and shale oil and gas
 - Large Mineral Deposits
 - 12% of the world's coal
 - 33.5% of the world's zinc
 - 3.5 % of the world's gold
 - 2.0% of the world's lead
 - 1.8% of the world's silver and copper

Mr. Limani mentioned the goal of raising the state's credit rating, which he had shared with the DOR Commissioner Adam Crum. He thought some agency's evaluation criteria did not reflect the uniqueness of the state. He stressed the importance of being able to accurately articulate the data. He discussed the amortization of the state's GO bond debt. He commented that the state's pension was well-funded compared to other states.

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Co-Chair Stedman mentioned the debt load and asked the department to provide the committee with a summary sheet of debt owed by the state, ranked by magnitude. He acknowledged that the state had a very low GO obligation bond issuance in the \$600 million range. He noted that over the previous 13 years, the state had paid about \$6.3 billion in Public Employees' Retirement System (PERS) payments, and the liability had gone up about \$100 million. He contrasted that the Teachers' Retirement System (TRS) payments had dropped in liability by about \$1.5 billion. He commented on the magnitude of cash flow. He referenced the Alaska Public Debt book (copy on file) and suggested that the requested information include a table of debt for municipalities.

Mr. Limani agreed to provide the information, and to include the information in future presentations.

Co-Chair Stedman noted concern in the past several years that some of the councils and assemblies did not grasp refinancing of bonds and debt. He thought the department could counsel communities on paying off assets.

Senator Bishop referenced the large mineral deposits listed on slide 9, and asked if the items were known and technically recoverable.

Mr. Limani affirmed that the slide listed known deposits.

Co-Chair Stedman thought the point could address the state's oil resources as well.

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Mr. Limani addressed slide 10, "Recent Bond Rating Meetings-Continued":

Bond Rating Upgrade

JUSTIFICATION

- Prominent Resource Development Projects on the Horizon

- Willow Development Project - \$10 billion investment with projected revenues of \$6.3 billion to the State and more than \$5 billion to local municipality and impacted communities
- Pikka Development Project - \$4.6 billion in operating expenditures and \$4.3 billion in capital expenditures
- Alaska Liquefied Natural Gas (LNG) Project - \$41 billion initial investment, billions of dollars in projected State revenues
- Letters of intent currently in place for front-end development capital

- Other Economic Development Prospects

- Carbon Credits and Carbon Capture, Utilization, and Storage (CCUS)
- Alternative Energy Transition Projects Estimated Capital Outlay \$105-\$175 billion
- Grid Resilience and Innovation Project (GRIP) \$206 million Grant from US Department of Energy

- Commitment towards a sustainable and long-term comprehensive Fiscal Plan

- Diversification of State Revenues

- Only 24.7% of revenues is based on oil and gas
- 15.1% of revenues is based on diverse world-wide income

Mr. Limani discussed the carbon credit and utilization proposals. He mentioned that the state had a third-party do an assessment of the state's alternative energy transition picture for the following 30 years. He noted that the GRIP project listed on the slide required a 100 percent match. He noted that the POMV draw had helped diversify the state's revenue.

Senator Kiehl thought the POMV draw was materially more than 15 percent of state revenues.

Mr. Limani did not have the forecast numbers but thought the amount would be close to \$3.5 billion for the following few years.

Co-Chair Stedman clarified that Senator Kiehl was referring to the last bullet on the slide that indicated 15.1 percent of income was based on diverse world-wide income.

Mr. Limani explained that the figure was based on revenue forecast numbers from the economic research group that included oil and gas and investments.

Senator Kiehl thought there was a wide variety of outlook items on the slide, some of which were similar to a "vision board" rather than something that could be taken to a bank. He asked how bond raters and analysts looked at the more speculative items.

Mr. Limani relayed that ratings usually considered imminent projects on the books such as the Willow project. Rating agencies also liked to look forward to state actions related to the economy and diversification.

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Senator Bishop was curious as to the commitment from the administration regarding a long-term comprehensive fiscal plan. He wanted his question to be directed at the commissioner.

Mr. Limani deferred the question. He commented that the POMV had provided stability over the period it had been in effect. He continued that agencies wanted to see stability in oil and gas forecasts and budget policies.

Co-Chair Stedman asked Mr. Limani to discuss the volatility he mentioned.

Mr. Limani relayed that rating agencies understood that no one could predict the oil price with a high degree of certainty. However, he pondered what tools the state had to mitigate volatility. He mentioned the concept of using a smoothing effect for oil prices over a 5-year period.

Co-Chair Stedman understood that the department would be bringing the concept forward for consideration after further analysis.

Senator Wilson followed up on Senator Kiehl's question regarding projects on the horizon. He asked about the \$41 million spent on the Alaska's Liquid Natural Gas (AK LNG) Project. He thought it was disappointing to continue to see the potential project when it was not likely to happen.

Mr. Limani explained that the scope of the project had changed from considering geopolitics and the need and demand for natural gas, coupled with a loan guarantee program from the federal government. He thought there had been a lot of interest for the project to move forward, which was why the project was included on the slide and why it had been monitored by rating agencies.

Senator Wilson asked what project Mr. Limani was referring to specifically. He asked about support from the federal government.

Co-Chair Stedman relayed that the federal government had offered to back loans from default risk for the AK LNG Project.

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Co-Chair Hoffman had similarly grave concerns about the prospect of the AK LNG line going forward. He thought the project came forward every five or ten years. He referenced multiple governors that had backed the project and noted that the legislature had spent multiple months reviewing the project. He knew the world was looking at natural gas and thought the potential for the utilization of natural gas as a long-term energy solution was more plausible, but cautioned that in-state use would not mean billions of dollars in projected state revenues. He thought the project would resolve the question of energy for the Railbelt and could considerably lower energy costs for the state.

Co-Chair Hoffman thought it seemed as though the companies had done very little to bring the gas to market. He echoed Senator Wilson's concerns and thought the state needed to move in a different direction.

Senator Bishop suggested that the \$41 billion listed on the slide for the AK LNG Project be risk-adjusted for cost overruns.

Mr. Limani advanced to slide 11, "Credit Rating and Market Feedback":

Initial Rating Agency Feedback

- The transfer from the Permanent Fund has been defined through a Percent of Market Value statutory structure and has been in place since FY2019
- Recent budgetary surplus and deposits to state savings accounts, including the Constitutional Budget Reserve Fund
- Significant reduction in state general fund spending since 2013
- Improved oil price environment and significant available natural resources under development
- Well Funded Pension Obligations including low debt service outstanding
- Improved Alaska's Economic Demographics

Market Feedback on Recent Transaction

- Institutional investors "love" Alaskan paper, very high-quality credit, highly secured
- More frequency in the market and larger bond issuances

Mr. Limani mentioned the Willow and Pikka Projects in reference to projects under development that were viewed positively by rating agencies. He mentioned the POMV split and a comprehensive long-term fiscal plan for the state. He referenced a bond issuance for \$33.5 million and feedback from the institutional investors. He thought that the state was viewed favorably anytime it issued bonds.

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Co-Chair Hoffman asked how much weight was given to the fact that the governor, for the previous six years, had proposed a full Permanent Fund Dividend (PFD) that was in excess of \$2 billion. He asked if the proposal played a factor in the state's credit ratings.

Mr. Limani thought that rating agencies looked at proposed budgets and recognized that there was a deliberation process before the final budget was put forward. He thought

agencies considered historical trends of budget values. He commented on the budget growth since 2019, which had only been 8 percent to 9 percent.

Co-Chair Hoffman pondered concerns about the administration picking and choosing areas in which to follow the statutes. He mentioned the Community Assistance Program (CAP), which was not funded in the budget according to statute. He considered that the legislature had trimmed the amount for the PFD, but had included an additional \$30 million for the CAP. He did not think that the administration strictly followed the law.

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Senator Bishop referenced the APFC board having discussed the idea of collapsing the Earnings Reserve Account (ERA) into the corpus of the Permanent Fund. He asked if the rating agencies were aware of the topic and if the change would create a higher credit rating.

Mr. Limani noted that Commissioner Crum had spoken on the topic to the rating agencies the previous January. He thought it was difficult to get an assessment from rating agencies about hypothetical situations, but the agencies had indicated that the change would engender a favorable review.

Senator Kiehl asked Mr. Limani to address the bullet "Improved Alaska's Economic Demographics." He referenced population loss and migration.

Mr. Limani cited 2 percent job growth in the previous year, which was higher than the U.S. average of 1.9 percent. The state's unemployment rate was at 4.3 percent, which was just slightly higher than the national average. He noted that the state was tracking with the national average over the previous decade. He cited wage growth at 6.5 percent compared to 5.5 percent for the national average. There was growth in the state's GDP, 4.6 percent. He considered an increase in jobs of a little over 2.2 percent growth in the previous year. The state was returning to pre-pandemic numbers. He thought the economic numbers were making a compelling case, particularly for Moody's.

Senator Kiehl acknowledged that the numbers were positive. He pondered long-term debt obligations and the need for progress.

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Co-Chair Stedman thought there had been a difference in the governor's submitted budget and the budget that was supported and passed by the finance committees. He recalled that there had been some discomfort with many of the reductions. He considered that if the legislature had supported and adopted the submitted budgets, there would be a different conversation taking place and the state's finances would be illiquid. He expected the legislature would endeavor to pass a balanced budget, although with the expectation of some uncomfortable decisions. He pondered future options and going to the debt market to build infrastructure. He mentioned having the time and ability to respond to downward oil prices. He lauded the committee for its fiscal restraint over the years.

Senator Merrick referenced Mr. Limani's several mentions of credit agencies' concern with the POMV split between the PFD and state services. She asked what split the administration would support.

Mr. Limani deferred the question to the governor's office.

Co-Chair Stedman expressed understanding.

Mr. Limani wanted to comment about the budget from the rating agencies' perspective. He explained that rating agencies recognized the budget process and made rating decisions based on the final budget.

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Mr. Williams looked at slide 12, "Current Municipal Market Update," which provided a market snapshot of current interest rates. He noted that the slide data was from December 15, 2023. He highlighted the chart on the lower left of the slide, which showed the spread between different rated credits. He noted that the market rates were fairly compressed, but there was a difference of about 30 to 50 basis points between the different rating categories.

Mr. Williams showed slide 13, "State's Debt Profile":

Authorization Process

- All forms of State Debt are authorized first by law
 - May be a one-time issuance amount or a not-to-exceed issuance limit in statute
 - General obligation bonds must then also be approved by a majority of voters
 - o General obligation bonds are the only debt secured by full faith credit and taxing authority
- All State Debt must be structured and authorized by the State Bond Committee
 - Includes general obligation bonds, subject to appropriation issues, & state revenue bonds
- The State Bond Committee determines method and timing of debt issues to best utilize the state's credit and debt capacity while meeting the authorized project's cash flow needs
- The State has established other debt obligations
 - Reimbursement Programs
 - The School Debt Reimbursement Program (SDRP) or HB 528 reimbursement, administered by the Department of Education and the Department of Transportation, respectively
 - o SDRP: Not currently authorized for new debt and periodically funded (was most recently partially funded in 2017, 2020 and 2022, and no appropriation in 2021; however, supplemental budget appropriations offset prior year reductions)
 - Retirement Systems
 - Unfunded actuarially assumed liability (UAAL) for defined benefit employees is guaranteed by the Constitution
 - Annual payments on the UAAL of other employers is reflected as State debt in the ACFR
 - Some flexibility in how payments are made

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Senator Kiehl did not recall HB 528 and asked for more detail.

Mr. Williams believed that the bill was listed in the Alaska Public Debt book as the Capital Project

Reimbursement Program. He furthered that HB 528 became law in 2002 or 2003 and included six municipalities, the University, and one electric association. The program was administered by Department of Transportation and Public Facilities (DOT).

Co-Chair Stedman asked Mr. Williams to get back to the committee with further detail on the program.

Mr. Williams referenced slide 14, "State's Debt Profile":

Types of Alaska Public Debt

- State Debt
- State Guaranteed Debt
- State Supported Debt
- Unfunded Actuarial Accrued Liability (UAAL)
- State Supported Municipal Debt - Eligible for State Reimbursement
- State Moral Obligation Debt
- State and University Revenue Debt
- State Agency Debt
- State Agency Collateralized or Insured Debt
- Municipal Debt

Mr. Williams explained that if one were to look at the slide from a security profile, the items would go in order. He explained that the state guaranteed debt was the collateralized veteran's mortgage program bonds issued through AHFC with the state's guarantee as a backing. He noted that lease revenue debt and certificates of participation were examples of state supported debt. He noted that he would go over each item on the slide in greater detail throughout the presentation.

Mr. Williams turned to slide 15, "State's Debt Profile," and noted that he had isolated the direct state debt as a General Fund commitment, including GO bonds in the amount of \$577.24 million outstanding as of June 30. He cited that subject-to-appropriation debt was lease revenue including Goose Creek Prison and Certificates of Participation (COPs). Lease debt also included a parking garage. The total outstanding combined debt was \$741.2 million, which was a fairly aggressive paydown of state GO debt of about 77 percent over a ten-year period. The chart on the lower

right showed the principal and interest payments per year through final maturity.

Co-Chair Stedman asked COPS.

Mr. Williams defined that COP signified certificates of participation. In 2014 the state issued COPS for the housing facility and sky bridge co-located with the Alaska Native Medical Center to improve access for patients.

Co-Chair Stedman asked Mr. Williams to get back to the committee with more information about COPS.

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Mr. Williams considered slide 16, "State's Debt Profile," which listed different types of Alaska public debt. There was \$41.3 million in the collateralized Veteran's Mortgage Program bonds outstanding, which had an underlying state guarantee. He highlighted state supported debt in COPS and lease revenue bonds with state credit pledge and payment. He looked at state supported municipal debt and the school debt service program. Of the \$650 million outstanding, \$433.6 million was associated with the state share. The Capital project program had about \$13.6 million outstanding. The pension system had \$3.52 billion outstanding in actuarially accrued liability. State moral obligation debt included the Alaska Bond Bank with a little over \$1 billion outstanding and the Alaska Energy Authority with \$204 million for a total of \$1.22 billion. He cited \$237.7 million in outstanding debt for International Airports Revenue Bonds. He noted that three years previously there was a complete restructuring of the airport system, which increased the strength of the debt profile.

Co-Chair Stedman asked for Mr. Williams to get back to the committee with more details on the pension liability which he thought was about \$6.5 billion. He thought some of the items appeared different. He wanted the items on the slide ranked by monetary value.

Mr. Williams displayed slide 17, "State's Debt Profile," which showed a table that was a continuation of revenue debt. He pointed out that state University of Alaska debt was \$241.4 million, with a total of \$479 million in state revenue and University debt. He cited state agency debt,

which included AHFC, capital project bonds, Alaska Railroad, Alaska Bond Bank, and Tobacco Settlement Asset bonds outstanding. There was also state agency collateralized or insured debt, which was also AHFC's various mortgage revenue bonds.

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Mr. Williams highlighted slide 18, "State's Debt Profile":

- General Fund (GF) Payment peaked in 2018 at approximately \$229 million
- FY2023 GF Debt service payments include approximately \$95.9 million in State General Obligation (GO) and State Supported debt, and approximately \$81.2 million for State Supported municipal debt
- \$776.1 million in remaining debt service to maturity of outstanding GO debt (principal + interest)

Mr. Williams reiterated that the state was on a fairly aggressive payment schedule for GO bonds. The 2023 GF debt service commitment was about \$95.9 million for all state supported debt, while the 2024 figure was \$90.1 million. He pointed out the chart on the bottom of the slide, which compared GF supported debt to the statutory payment to PERS and TRS. He pointed out that the payment totally eclipsed the other forms of state debt payments.

Co-Chair Stedman noted that the committee had asked the department to provide more information regarding the amount of extra payments the state had to address the unfunded liability. The committee had not yet received the numerics, which were being calculated by the actuary. He pondered the amount of support under the 22 percent to communities.

Mr. Williams looked at slide 19, "State's Debt Capacity":

Debt Affordability Analysis

- Annual analysis required by AS 37.07.045 to be delivered by January 31
- Discusses credit ratings, current debt levels, history and projections
- Relies upon debt ratios, limit of 4% for directly paid state debt, and 7% when combined with municipal debt that the state supports

- Identifies currently authorized, but unissued debt
- Establishes refinancing parameters
- Determines a long-term debt capacity at current rating level
- Discusses, but doesn't define, a capacity for short-term debt
- The 2023-2024 analysis determined that the State had a debt capacity of \$1,400 million
 - Adjustments made to base analysis to account for recognition of a percent of market value split for PFDs vs state budget, special funding for PERS/TRS and future budget uncertainty and volatility in the State's revenue sources

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Co-Chair Stedman explained that the debt capacity of \$1.4 billion did not signify that the state could afford to spend a great deal more.

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Senator Wilson wondered if the administration planned to have a conversation related to issuing bonds.

Mr. Limani shared that there had been some conversation between DOR, the Office of Management and Budget (OMB), and the governor's office. The administration was looking at energy-related projects, but nothing had been specifically identified.

Co-Chair Stedman thought the obvious concern was that increasing the debt burdened the operating budget going forward.

Co-Chair Hoffman asked if the energy discussions Mr. Limani referenced were statewide.

Mr. Limani answered "yes."

Mr. Limani showed slide 20, " Questions?":

Contact:
 Fadil Limani, DOR Deputy Commissioner
 Fadil.Limani@alaska.gov
 Ryan Williams, DOR Debt Manager

Ryan.Williams@alaska.gov

Co-Chair Stedman commented that the committee would most likely invite the testifiers back before the end of the legislative session. He mentioned upward pressure on the state's bond rating. He referenced the smoothing concept mentioned earlier, and relayed that it was a topic of interest for the committee.

Co-Chair Stedman thanked Mr. Limani and Mr. Williams.

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RECONVENED

Co-Chair Stedman relayed that the committee would consider a presentation from the Chief Economist for the Department of Revenue.

^ADMINISTRATION RESPONSE TO PRIOR MEETINGS: DEPARTMENT OF REVENUE

[10:13:42 AM](#)

DAN STICKEL, CHIEF ECONOMIST, DEPARTMENT OF REVENUE, spoke to a presentation entitled "Senate Finance Responses to Follow Up Questions from January 18, 2024 Revenue Forecast Presentation," and noted that the slides would address six follow-up questions from the committee after the previous presentation on January 18. He noted that the department had provided a written response. He showed slide 2, which showed the first follow-up question:

1. Provide an analysis showing revenue sensitivity to oil prices over the next several years

Mr. Stickel showed slide 3, "Estimated Unrestricted Revenue at Various Oil Prices," and noted that he had provided a document with a range of oil prices from \$20/bbl up to \$150/bbl over the ten-year forecast period. The document looked at what the Unrestricted General Fund (UGF) revenue would be if everything else was held the same as the fall revenue forecast.

Co-Chair Stedman asked Mr. Stickel to discuss the effects of an oil price of \$60/bbl and the expectations for FY 25.

Mr. Stickel suggested moving on to slide 4 to address the question. He explained that slide 3 was a screenshot of the document that was provided to the committee. He noted that the public could see the entire document as well as a breakout of royalty and production tax revenue under a range of oil prices.

Mr. Stickel showed slide 4, "Petroleum Detail: UGF Relative to Price per Barrel (without POMV): FY 2025," which showed how UGF for FY 25 would change with different oil prices. He noted that the slide was a repeat of the slide that was in the January 18 presentation. He cited that starting with the forecast price of \$76/bbl, forecast revenue was \$2.65 billion of UGF before the POMV draw. He observed a bend in the curve around \$65/bbl, below which would have most companies paid at the minimum tax floor. Once above the \$65/bbl range, there was progressively more state revenue for each \$1 increase in oil price.

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Mr. Stickel showed slide 5:

2. Provide an updated version of slide 18 that contains correct dates

Mr. Stickel showed slide 6, "Petroleum Detail: Nominal Brent Forecasts Comparison as of January 17, 2024," which showed a corrected version of one of the slides shown in the previous presentation. He noted that there had been a typo in the slide. He clarified that the data in the slide was updated, but the header had listed an incorrect date. The correct date was shown on the current slide, which showed a line graph depicting different oil price forecasts over time. He commented that with updated data, the slide would look much the same. The forecast was very similar to what the futures market outlook would say.

Co-Chair Stedman explained that on roughly the 15th of February, the committee would receive an update on the oil price and revenue projections.

Mr. Stickel clarified that the department was targeting the 15th of March for the forecast update.

Mr. Stickel showed slide 7:

3. Provide a list of allowable capital expenditure deductions for purposes of the oil and gas production tax

Mr. Stickel showed slide 8, "Allowable Capital Expenditures":

- Alaska's oil and gas production tax for North Slope oil is based on a tax on production tax value (similar to net profits) with a minimum tax floor.
- All allowable expenditures may be deducted in calculating PTV in the year incurred. Excess lease expenditures may be carried forward.
 - In general, any direct costs of oil and gas exploration and production
 - Statutes specify exemptions/ exclusions - AS 43.55.165(e).
 - Regulations further define allowable - 15 AAC 55.250 and 15 AAC 55.260.
- Capital expenditures: represent investments into long term tangible assets
 - In general, Alaska follows IRS guidelines in determining what is considered a capital expenditure.
 - Examples: building facilities, buying equipment with an expected life over one year, geological or geophysical exploration, and some drilling costs.
- Operating expenditures: any allowable lease expenditures other than capital expenditures.

Mr. Stickel explained that the written response to the committee had more detail than the bullets shown on the slide.

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Mr. Stickel showed slide 9:

4. How much of the decline between the Spring 2023 and Fall 2023 production forecasts for FY 2024 and FY 2025 was attributable to Prudhoe Bay?

Mr. Stickel turned to slide 10, "Comparison of Forecast Production," which showed a table of ANS oil production forecasts compared by area. The table had taken the data in appendix C2 of the Revenue Sources Book (RSB) and compared the information between the fall forecast and previous spring forecast. He noted that the Prudhoe Bay portion of the table was included in the first three categories. He pointed out that the total decline in forecast production in the initial production area of Prudhoe Bay. The decline was partly offset by increases in the Prudhoe Bay satellites and Greater Point McIntyre Area (GPMA). Within the two units operated by Hilcorp, there was some ability to shift around drilling plans. He pointed out the total production decline from FY 24 to FY 25, while other large contributors were in the National Petroleum Reserve in Alaska (NPR-A) and the Point Thomson area. The primary reason for all of the declines, according to DNR, was a reevaluation of the expected productivity and decline trends for new and existing wells. He pondered new activity and DNR's evaluations for future drilling.

Co-Chair Stedman asked Mr. Stickel to elaborate on NPR-A and the drop from the spring forecast.

Mr. Stickel noted that he would defer the details to the experts at DNR that produced the forecast. He commented that the biggest part of the decline was the Greater Moose's Tooth (GMT) Unit, and thought production had not come in as strongly as previously predicted. He considered previous iterations of the forecast that showed strong performance on some wells and some of the production that had since fallen.

[10:24:29 AM](#)

Mr. Stickel showed slide 11, "Comparison of Forecast Production," which showed a table that took the information from slide 10 and summarized it by grouping different units together. He noted that for FY 25 the central group (including Prudhoe Bay) was a relatively small component of the change to the forecast. The bigger components of the change were in the West group, which included GMT, Colville River, and Point Thomson fields.

Mr. Stickel turned to slide 12:

5. How much did the State of Alaska pay out for purchase of tax credits over the life of the program?

Mr. Stickel noted that as mentioned in the January presentation, all outstanding tax credits for state purchase had now been retired. He had indicated he would come back with more information about the total credits purchased over the life of the program, which was shown on the following slide.

Mr. Stickel advanced to slide 13, "Total Oil and Gas Credits Purchased," which showed a table with credits purchased by the state for the North Slope and non-North Slope areas. The total credits purchased were just under \$4.1 billion over the life of the program. There was an estimated distribution of about \$2.5 billion for activity on the North Slope and about \$1.5 billion for non-North Slope activity, which was primarily Cook Inlet and a small part in Middle Earth.

Co-Chair Stedman asked if the slide covered all the credits or just purchased credits.

Mr. Stickel answered that the table included all the credits that were purchased by the state.

Co-Chair Stedman asked if there were other credits.

Mr. Stickel affirmed that there were also credits against liability, and there were some credits that were earned and transferred to other companies. The credits could have been available for purchase but were ultimately applied against a different company's tax liability.

Co-Chair Stedman observed that the credits listed were but a portion of the total credits.

Mr. Stickel agreed.

Mr. Stickel noted that the information on slide 13 came from Table 8.4 of the Revenue Sources Book (copy on file). He explained that it would not be an arduous task to create the same slide using data for the credits against liability if it would be helpful to the committee.

[10:27:37 AM](#)

Mr. Stickel showed slide 14:

6. Provide and estimated North Slope production eligible for Gross Value Reduction (GVR) and non-GVR production for each year in the 10-year forecast. Further, provide a breakout of that production by landowner and the associated state royalty revenue

Mr. Stickel spoke to slide 15, "ANS GVR and Non-GVR Production by Land Ownership," which showed a table. He explained that the Gross Value Reduction (GVR) was an element of the production tax that allowed for a tax benefit for new production and for the first three to seven years of production from the field (depending upon oil prices). He looked at the table and noted that the information was in a table in the RSB, but the slide broke down the information by land type. He noted that the federal land included both the NPR-A as well as other federal land including offshore production in the North Star field. Privately held leases on the North Slope were primarily Native corporation lands, whether in the NPR-A or the state's land.

Mr. Stickel observed that the general trend was that beginning in FY 25 and FY 26 one could see the GVR-eligible fields started to decline as some of the fields started to "graduate" after having three to seven years of benefit before starting to pay under the regular production tax. Towards the end of the 10-year time horizon, the GVR number picked up quite a bit with new fields coming online - in particular Pikka and Willow. The two major fields were reflected in all three land types.

[10:30:08 AM](#)

Senator Kiehl looked at the production ramping up on the GVR-eligible oil and observed that it was on federal land. He asked if the state was giving a bigger production tax benefit on federal land where the funds could not be recouped in royalty.

Co-Chair Stedman asked for Mr. Stickel to give a brief explanation of land ownership to provide more clarity to the public while addressing Senator Kiehl's question.

Mr. Stickel explained that the state had several ways to benefit from oil and gas. State production tax, corporate

tax, and property tax applied regardless of the landowner. For royalty on state land, the state received the full amount. For royalty on federal land, the state received a share. Within the NPR-A in particular, the state's royalty was 50 percent and was required to be used for the benefit of impacted communities. For private land, the state did not receive a royalty directly but levied a tax as part of the production tax in the amount of 5 percent of the royalty interest. He noted that there was a slide in the original presentation from January 18, which included royalty provisions for each land type.

Mr. Stickel explained that the GVR provisions (as part of the production tax) were the same regardless of whether the production came from state or federal land. He continued that as Senator Kiehl noted, the GVR-eligible oil predicted for federal land was the largest component towards the end of the ten-year forecast. The increase had to do with the large size of the Willow Project, which was the largest component.

Senator Kiehl thought if the state was going to provide a "sweetener," the state should benefit.

[10:33:19 AM](#)

Mr. Stickel showed slide 16, "ANS GVR and Non-GVR Production by Land Ownership," which showed a table that assigned revenue numbers to the streams of production presented in the previous slide. The royalty on state land, including UGF share as well as royalty that went to the Permanent Fund and School Fund. Federal land shared royalty was included, most of which was in the NPR-A and had restrictions related to providing the funds to impacted communities. There was a small portion which was unrestricted. For illustrative purposes, the table showed estimated revenue the state received from private royalties.

Co-Chair Stedman commented on the nuance and complexity of the state's oil and gas tax system.

Co-Chair Stedman discussed the agenda for the following day.

ADJOURNMENT

10:35:50 AM

The meeting was adjourned at 10:35 a.m.