

**TESTIMONY, SENATE FINANCE AND TAX COMMITTEE
MARCH 17, 2021
HOUSE BILL 1358**

**TIM PORTER – CHIEF FINANCIAL OFFICER
BANK OF NORTH DAKOTA**

Madam Chair and members of the Committee, for the record my name is Tim Porter, Chief Financial Officer at Bank of North Dakota. I am here today to offer our thoughts on House Bill 1358 regarding establishing a process for hedging oil prices. In addition, I will provide the committee with some of the results from the Hedge Study we conducted from October 2019 through September 2020.

First of all, BND supports the amendments as presented for House Bill 1358. These amendments will initiate an Oil Hedging Advisory Committee and create an Oil and Gas Tax Revenue Hedging Fund. Any monies within the fund are appropriated to the Office of Management and Budget (OMB). The Oil Hedging Advisory Committee, with the Director of OMB as chair, would review hedge strategies and have the authority to hire an outside consultant that specializes in developing oil hedge strategies. We think it's important that the oversight of this function rest with a committee that has representation across state government, including the legislative branch.

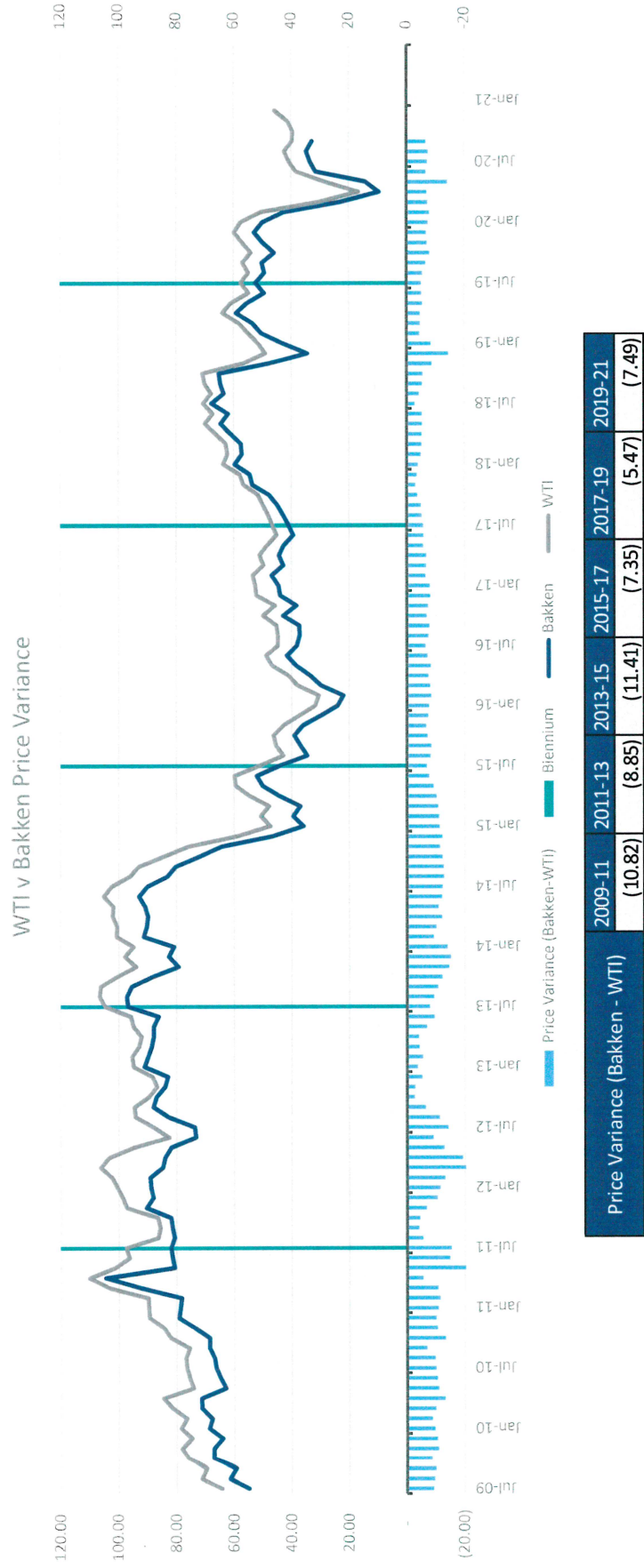
The amendment provides for an appropriation of \$20 million and a transfer each September from the Oil and Gas Tax Revenue Hedging Fund to the Strategic Investment and Improvement Fund (SIIF) of any amounts that exceed the original appropriation of \$20 million.

I've also included four pages from the hedge study completed by BND. These pages include historical perspectives of oil prices broken down by biennium and includes a look at the basis risk (WTI vs. Bakken price) as well as the biennial budget oil price versus the actual price for the past few biennium's. Page three describes the types of hedging instruments used in our study, and page four provides a monetary summary of the premiums we paid to purchase puts and the settlement values we realized when the oil price dropped below the floors established in our trades.

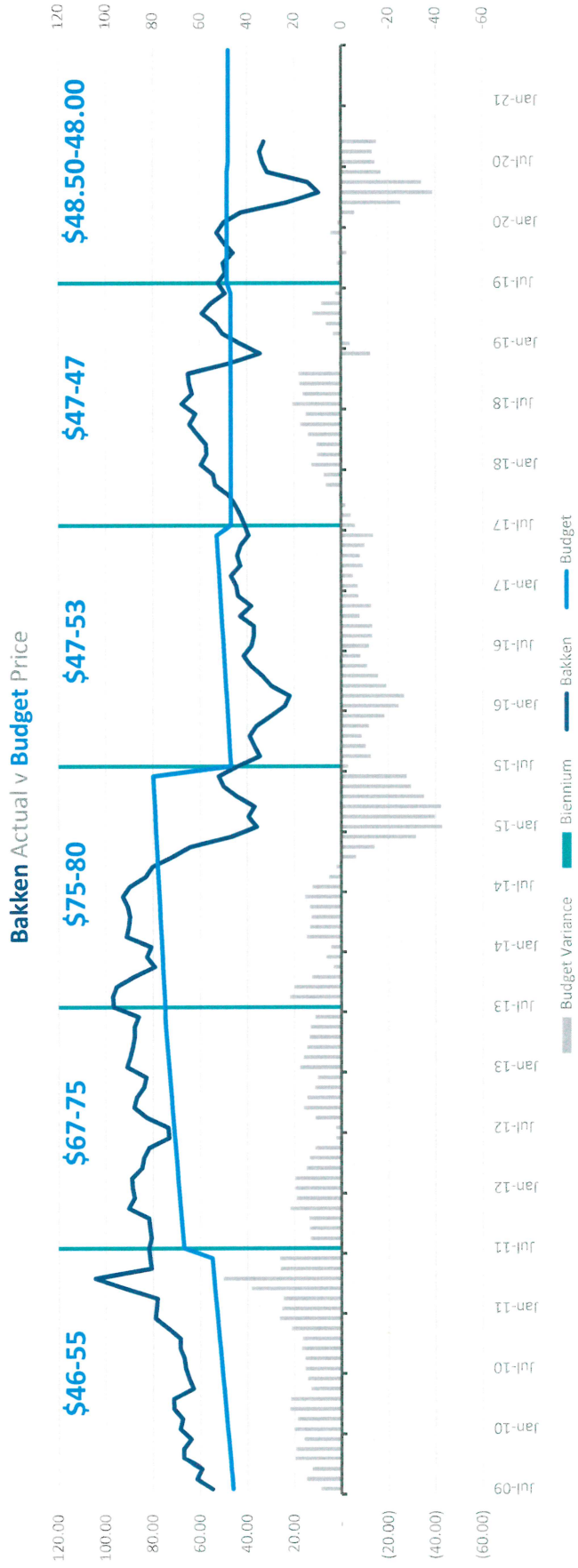
Overall, in cooperation and coordination with the Oil Hedging Advisory Committee, BND can play a role in establishing a strategy to reduce the risk of falling oil prices, but this risk needs to be on the state's balance sheet, not BND's. By establishing the Oil Hedging Advisory Committee and providing an appropriation, these amendments open an important dialogue for the legislature to debate whether its desire is to pay for the insurance to help protect a portion of the state's budget.

That concludes my testimony, Madam Chair and I would be happy to answer any questions.

Historical Price Perspective – WTI v Bakken



Historical Price Perspective – Biennial Budget Oil Price v Actual



2009-11	2011-13	2013-15	2015-17	2017-19	2019-21
21.09	13.80	(3.68)	(12.09)	7.21	(10.22)

Price Variance (Actual - Budget)

Hedging Instruments Primarily Used in Project

- **Put Option**
 - Pay a premium, and establish a floor
 - May not receive any payment if price does not reach floor
 - Minimize downside risk while still participating in upside
- **Costless Collar**
 - No upfront cost or premium
 - Lock in a ceiling and floor price
 - Minimizes downside risk and upside opportunity

Payment summary

The hedge portfolio has so far earned BND more than \$94 million in payouts

- The drop in oil prices led to significant payouts on hedges between April and September.
- In total, employing the hypothetical hedging program would have **netted ~\$80mm over 12 months**, mitigating the losses caused by declining oil prices.
- *If oil instead had a strong year, BND would not have recovered any of the \$14mm in premium payments, but this cost may be offset by increasing oil-related revenues.*
- In addition to payouts already received, the portfolio of remaining active trades has a value of **\$29.6 million**, with coverage extending to September 2022.

Date	Premiums	Settlements	Additional notes
Sep-19	-5,597,640	0	Purchased put option
Oct-19	0	0	
Nov-19	0	0	
Dec-19	-1,379,974	0	Purchased put option
Jan-20	0	0	
Feb-20	0	0	New costless collars (no premiums)
Mar-20	0	20,472,202	First payout following WTI collapse
Apr-20	0	33,910,944	
May-20	0	20,116,260	
Jun-20	-7,774,500	6,275,317	Purchased put option
Jul-20	0	4,686,728	
Aug-20	0	3,434,774	
Sep-20	0	5,425,305	
Total	-14,752,114	94,321,530	