



Representative Mike Hawker

Alaska State Legislature

Co-Chair Saddler and Co-Chair Feige,

Included are responses to questions posed by House Resources Committee members in hearings Feb. 4 and Feb. 6 on House Bill 4, In-State Gasline Development Corp. These responses are provided in part by my office and in part by the Alaska Gasline Development Corporation (AGDC).

Additionally, my office has provided via email to the committee co-chairs copies of the 2010 Alaska Natural Gas Development Authority audit, by the Division of Legislative Audit. That document and a summary are available online at <http://www.legaudit.state.ak.us/pages/digests/2010/30054dig.htm>

Thank you,

A handwritten signature in black ink, appearing to read "Mike Hawker", written over a light gray rectangular background.

Representative Mike Hawker

Question: Explain why the State Procurement Code is a problem and why AGDC should be exempt.

AGDC is already exempt from the procurement code; House Bill 369 in 2010 exempted an AHFC natural gas pipeline subsidiary. As HB 4 repositions AGDC as a stand-alone state corporation, HB 4 also moves the existing procurement code exemption from an AHFC subsidiary to AGDC. As requested by the committee, AGDC has prepared a comprehensive explanation for the need for a procurement code exemption; that explanation is attached at the end of this letter.

Question: Is it a violation of AGIA for a) the legislature to ask AGDC to or b) for AGDC to calculate the maximum technical capacity of the size and specification of pipe AGDC plans to use for the instate natural gas pipeline project designed to carry no more than 500 million cubic feet per day?

HB 4 sponsors have requested a Legislative Legal Services opinion on whether legislators, in making this request, could violate AGIA. The advisory opinion will be forwarded to the committee co-chair offices upon receipt, for distribution to the committee.

AGDC's legal counsel is still determining if this request could put AGDC at risk of violating AGIA.

Question: What would the \$400 per day board member compensation apply to; what is 'official board business?' What kind of work load should new board members anticipate? If AGDC's board meets on the same day as the members also meet as ANGDA's board, do board members get compensated for both meetings?

The \$400 per day applies to days that the board meets and other official business as required by the board; for example, attendance by a board member at some other related meeting, at the request of the board. If AGDC's board meets twice in a day, once as AGDC's board and once as a subsidiary corporation's board, they receive \$400 for each meeting. This is reasonable in considering the amount of time and effort required to prepare for a board meeting, and helps maintain the separation between a subsidiary and the parent corporation.

House Bill 4 allows for compensation for "official board business". This is identical to the allowances in Alaska Housing Finance Corporation and Alaska Industrial Development and Export Authority statutes (AS 18.56.030-AHFC, AS 44.80.050 -AIDEA). Both AIDEA and AHFC compensate board members for board meetings. Days spent outside of board meetings are not compensated when spent preparing for board meetings. Members of two related boards (AGDC and a subsidiary, such as ANGDA) receive compensation per meeting; if meetings for AGDC and for a subsidiary are on the same day, board members receive compensation for both meetings.

The sponsors intend that the compensation is for board meetings and other official, authorized board business, such as meetings a board member may be required to attend that are not board meetings. The sponsors further intend that board members receive compensation for each board meeting they attend, if serving as boards of multiple corporations; even if they meet twice in one day, once as AGDC's board and once as a subsidiary's board. Board compensation is to reflect the time and engagement required not only for the meeting, but for the off-hours time members must invest in preparing for meetings.

The learning curve for new board members is, as the committee suggested, likely to be high; that said, the appointment of board members with expertise in specialized, relevant areas should result in members relatively knowledgeable in the matters that will come before the board, as opposed to board members starting from scratch on complex issues. The sponsors acknowledge there will need to be, in part, a public service motivation for board members in accepting a board position.

Question: Provide more information comparing and contrasting AGDC and other public corporations of the state in regards to corporate authority and, specifically, applicability to the State Procurement Code; Administrative Procedure Act; State Personnel Act; Executive Budget Act; and legal counsel.

The sponsors continue working on this labor-intensive request. Initial review has compared the Alaska Railroad Corporation; Alaska Housing Finance Corporation; Alaska Permanent Fund Corporation; Alaska Student Loan Corporation; Alaska Aerospace Corporation; Alaska Industrial Development and Export Authority; and Alaska Energy Authority. Preliminarily:

- State Procurement Code: For all, at least some contracts are exempt; alternatively, some are exempt but are also required to develop procurement regulations substantially similar to the procurement code (AHFC, Aerospace, Railroad). AEA does not appear to be statutorily exempt.
- Administrative Procedures Act: AGDC would be exempt except for the Open Meetings Act under HB4. Also exempt except for the Open Meetings Act are Aerospace, AHFC, and AIDEA. The Permanent Fund and Alaska Railroad are partially exempt.
- State Personnel Act: All but AEA are exempt; AGDC would be exempt under HB4.
- Executive Budget Act: The Alaska Railroad is exempt; AGDC would be exempt under HB4. AHFC, AIDEA and ASLC are partially exempt; the operating budgets only are subject.
- Legal Counsel: Under HB4, AGDC will retain independent legal counsel. The Attorney General is by statute legal counsel for AIDEA and AHFC. Aerospace may hire legal counsel. The railroad must advise the Department of Law before initiating legal action.

House Bill 4 requires AGDC to retain legal counsel. The sponsors believe a deviation from the norm is appropriate for AGDC. The Attorney General is also legal counsel for the administration in regards to the Alaska Gasline Inducement Act and the contract between the commissioners of Natural Resources and Revenue, and licensee TransCanada.

Further, AGDC will engage with private sector partners; shippers; and financial institutions, and in doing so will require prompt, priority service from its legal counsel in order to retain a level relationship with these other entities. Subjecting AGDC to the potential for delays; sub-prioritization; and counsel dependent on state resources risks placing AGDC at a disadvantage in negotiations with these private sector entities. For these reasons, the sponsors believe it is appropriate to allow AGDC to retain its own legal counsel, other than the Attorney General.

Question: What constitutes ‘property’ in relation to ANGDA, AS 41.41.450?

HB4, Section 26, conforms ANGDA section 41.41.450, Property of the authority, to reflect the elimination of the term “project” from ANGDA’s definitions. With the change in HB4, ANGDA could still acquire property as described above, for the purposes of the corporation, but not for the purposes of financing a project. An example of property ANGDA may need to acquire is office space. Real property is physical land and the improvements attached to that land; personal property would be other property not attached (for example, an office is real property, and the office furniture is personal property).

ANGDA statute: Sec. 41.41.450. Property of the authority.

The authority may acquire, by purchase, lease, or gift, upon terms that it considers proper, land, structures, real or personal property rights, rights-of-way, franchises, easements, and other interests in land it considers necessary or convenient for the financing of the project or a part of the project.

House Bill 4, Section 26:

Sec. 41.41.450. Property of the authority. The authority may acquire, by purchase, lease, or gift, upon terms that it considers proper, land, structures, real or personal property

rights, rights-of-way, franchises, easements, and other interests in land it considers necessary or convenient for the purposes of the corporation [THE FINANCING OF THE PROJECT OR A PART OF THE PROJECT].

Question: HB 4, Section 3, 31.25.230, provides for refunding obligations. How will this work? Would any excess be returned to the general fund?

In general, a reduction in the cost of the debt or the pipeline operating costs would result in a lower tariff going forward. If the tariff was based upon the cost of the original financing, a later refinancing to lower cost debt would result in refunding/repaying the original bonds and a recalculation of new tariffs going forward at a lower rate. There would likely be little to no extra revenues to go back to the general fund.

Question: HB 4, Section 3, 31.25.260 exempts AGDC corporate property from state and local taxes. Would this apply to AGDC's partners? Does this give AGDC an advantage over the private sector?

AS 29.45 exempts state entities from state and local taxes. AGDC would be a state entity, and thus exempt per existing statute. AGDC's subsidiary corporations would likely also be tax exempt. AGDC's partners would not derive tax-exempt status from being partners with AGDC or any AGDC subsidiary.

The sponsors do not believe AGDC's tax-exempt status confers an advantage over private sector companies. First, AGDC would not be undertaking a gas pipeline if a private sector company was doing the project; without competition, there is little case for claiming an advantage. Further, AGDC's exemption does not affect the private sector's tax burden; the private sector would need to pay taxes whether AGDC was a partner or not. Finally, if a private company owned part of the pipeline, it would be subject to property taxes; but would also be ensured the opportunity to earn a regulated rate of return that would likely be of far greater value to the company than the cost of the property tax due. To that end, the sponsors find it unlikely that the private companies would forgo the benefits of pipeline ownership simply to enjoy a reprieve from property taxes.

AS 29.45.030. Required exemptions.

(a) The following property is exempt from general taxation:

(1) municipal property, including property held by a public corporation of a municipality, state property, property of the University of Alaska, or land that is in the trust established by the Alaska Mental Health Enabling Act of 1956, P.L. 84-830, 70 Stat. 709, except that

(A) a private leasehold, contract, or other interest in the property is taxable to the extent of the interest; however, an interest created by a nonexclusive use agreement between the Alaska Industrial Development and Export Authority and a user of an integrated transportation and port facility owned by the authority and initially placed in service before January 1, 1999, is taxable only to the extent of, and for the value associated with, those specific improvements used for lodging purposes

Question: HB 4, Section 34, exempts an AGDC-owned-or-financed project from paying state and local property taxes during construction. Can you estimate the amount of property taxes that the project would be subject to without this exemption?

AGDC has not done this calculation due to the high degree of uncertainty involved – where equipment and materials will be staged, for how long, etc. It is proposed mainly as a method for avoiding the tremendous accounting effort to track inventory and equipment movements during construction between different boroughs in the State. As such inventory and equipment is moved into a given borough, it becomes subject to property taxes in that borough, and ceases to be subject to property tax in the borough in which it was previously located.

Question: Provide detail on the types of information that could be held confidential under HB 4, and the types of confidentiality agreements AGDC could enter into.

HB 4 allows for certain information to be held confidential, and does not set time limits for that protection. In HB 4:

- AGDC can sign confidentiality agreements with private sector companies to protect information exchanged between the two. The information covered by these agreements will probably never be made public, as the agreements are the private sector's assurance that they may talk and negotiate freely with AGDC.
- AGDC can sign confidentiality agreements with a state entity and a third party to share information that the state is already holding confidential. As AGDC would be a 'third party' to existing confidentiality agreements or confidential information, AGDC would not disclose this information at any time (for example, taxpayer data that is protected by the state).
- AGDC can keep self-generated data and information confidential. This information includes results of field studies, technical data, and tariff models that are assets AGDC is developing for the state, using state money. While HB 4 does not restrict the confidentiality by time, this information may be of public benefit once a pipeline is operational.
- AGDC's open season negotiations are confidential, out of respect for the years of negotiations that generate first precedent agreements, then firm transportation agreements. However, HB 4 does require (as does FERC for an Alaska gas project) that certain information be released after a successful open season. After signing precedent agreements, AGDC is to release, for each successful bid, the name of the shipper; the amount of capacity contracted for, and the length of the commitments. This information is intended to assure Alaskans that, in an open season, AGDC has signed on enough credit-worthy shippers with long-term contracts that will be sufficient to support revenue bonds issued to pay for the pipeline.
- Also in HB 4, a contract carrier pipeline will need to provide precedent agreements to the Regulatory Commission of Alaska for review. While those contracts will be confidential, once the conditions on the agreements are resolved and the precedent agreements turn into firm transportation agreements (about the time of project sanction), the RCA will make the firm

agreements public. However, information that, if released, could cause commercial harm, can be held confidential if the RCA agrees the information should be privileged.

The primary information AGDC would hold confidential is the information obtained from other entities through confidentiality agreements. AGDC would keep that information confidential as long as required by the confidentiality agreements; a standard provision of confidentiality agreements is that the information becomes public to the extent AGDC uses it as part of a permit application process.

Question: Provide a list of pros and cons of making ANGDA a subsidiary corporation of AGDC.

Realizing that AGDC may need a gas aggregator/marketing subsidiary, the sponsors have ensured that HB 4 allows AGDC to create subsidiary corporations. Under HB 4, ANGDA becomes a subsidiary of AGDC. This reduces redundancies in state efforts developing natural gas. However, the sponsors are uncertain as to whether ANGDA will be used, as AGDC has the ability to create other subsidiaries as well; and the sponsors are uncertain as to whether a new role for ANGDA is sufficient to relieve concerns that ANGDA has exceeded its statutory authority, as identified in the 2010 legislative audit.

Question: Why does AGDC need a marketing subsidiary? How would a marketing subsidiary work? Does there need to be a firewall between AGDC and its marketing subsidiary? If so, why, and how? Does a marketing subsidiary have an advantage over other entities that want to ship gas through an AGDC line?

AGDC may need a subsidiary corporation to aggregate gas volumes on an AGDC pipeline. If an independent, private sector aggregator/marketer is involved in the AGDC project, AGDC would not need to create a subsidiary corporation for that purpose.

A gas marketing subsidiary would have the ability to acquire and transport gas in the ASAP pipeline. They could act as an aggregator for Alaska utilities or potential smaller customers who may not have the experience or wherewithal to do this on their own. A marketing subsidiary could also transport the state's royalty gas, if the DNR commissioner chooses to sell gas to customers through an AGDC pipeline.

In creating a marketing/aggregator subsidiary, AGDC can confer its statutory authorities to the subsidiary; for example, tax exemption. However, as AGDC would not need a marketing subsidiary if a private sector aggregator/marketer participates, it is unlikely that an AGDC subsidiary would have an advantage over other entities. Further, an AGDC marketing/aggregator subsidiary would have the same relationship with AGDC as other gas shippers; this is accomplished through a 'firewall' to prevent unfair information exchange or an inadvertent advantage.

The requirement that a shipper and a carrier who are affiliates have a strict "firewall" between them so neither one can unfairly benefit ensures the pipeline does not act anti-competitively by conferring an undue advantage on its affiliate. This is a standard business practice in the corporate world, and AGDC's potential partners and customers will expect a firewall to be in place. An example would be providing the marketing affiliate access to AGDC information while denying other marketing entities access to the

same information. The firewall ensures a fair and competitive process for all shippers without undue discrimination, regardless of affiliation.

Question: HB 4 limits judicial review of state permitting and other decisions. Does the Legislature have the authority to limit judicial review, including jurisdiction for complaints?

The sponsors have included with this response a memo from Legislative Legal Services addressing the committee's questions. The sponsors realize that the courts may ultimately decide whether or not the Legislature can limit their jurisdiction and powers; however, the sponsors also believe that the judicial review limitations in HB 4 are a reasonable balance between Alaskans' rights and a pipeline project in Alaskans' best interests. The sponsors encourage the committee to pose this question to the Department of Law, as well.

Question: HB 4 creates a new set of right-of-way lease covenants for a contract carrier. What are the implications for pipelines already operating on common carrier covenants in a state right-of-way lease?

Under HB 4, other pipelines would be able to apply to the state for a right-of-way lease as a contract carrier; further, HB 4 would not prohibit existing pipelines with a state right-of-way lease from requesting an amended lease agreement with the Department of Natural Resources to reflect contract carrier principles. DNR would best be able to discuss this question, including the lease amendment process and whether DNR anticipates other, existing pipelines seeking lease amendments.

AGDC Response to Procurement Code Exemption Question:

AGDC, as a subsidiary of AHFC, was granted exemption from the state procurement code by HB369. The primary reason for continuing relief from the State of Alaska procurement regulations for acquiring goods and services for the purpose of construction of an in-state natural gas pipeline is to expedite the contracting and purchasing process in light of the urgency to construct a viable method of transporting natural gas for the residents of the State of Alaska.

A project as large as the proposed gas line project will require an enormous effort to acquire necessary design contractors, construction contractors, temporary housing, transportation, equipment, materials, quality control, testing, and supplies to name just a few of the major components.

Given the time constraints for construction in terms of both the urgency and Alaska's limited "fair weather" construction season for certain tasks, a typical 60 to 90 day solicitation to advertise, review, and award contracts based on current procurement methods could translate to tens of millions of dollars in costs. (The cost of carrying \$8 billion dollars for three months is roughly \$50 million).

The state procurement code focuses primarily on the lowest price, while the magnitude of this project will best be served by availability or other qualities as circumstances dictate to complete the project as expediently as possible.

Relief from existing procurement regulations would reduce costs in the following ways:

1. Reduced administrative burden (time & expense) to prepare, advertise, review and award Invitations to Bid or Requests for Proposals. For instance, the procurement code mandates a public notice with a minimum 21-day advertising period, a 10-day protest period and if there is a protest a stay of award. The time and expense to ramp up/train a procurement organization large enough to exercise traditional state procurement regulations would be significant.
2. Eliminates costly delays due to simple clerical errors in solicitations that require addendums or extensions of the bidding/proposal time. Under the procurement code, if there is an error in the bid the party submitting the bid must be withdrawn. There is no allowance for corrections. This is unfortunate as even under the federal procurement process there is allowance to correct errors. A project of this magnitude will require extensive schedule preparation and analysis. Once the schedule is established, a "critical path" will be defined where any deviations from the "critical path" will result in delays along the entire path, resulting in an extended completion date.
3. Eliminates potential for bid protests that may not be germane to the project, yet have the potential to inflict significant schedule delays, or whose only purpose is to delay the contract award and project completion. Current regulations contain very generous opportunities to file bid protests that may be unrelated to the project, or may be based on minor technicalities that nonetheless must be addressed by a Contracting Officer in a time-consuming manner. Allowing time for bid protests and a statutory response time requires the attention and resources of the Contracting Officer at the expense of an expedited project completion date.
4. Reduce delays along the scheduled critical path by allowing poor performing contractors, vendors or suppliers to be quickly replaced when needed. Typically projects of this size will incorporate

some form of performance based contracting method that allows the performance of the contractors, vendors, suppliers, etc., to be evaluated, and if necessary replaced quickly in order to maintain the established schedule. A relatively minor hiccup in the project can cause a major disruption in the project completion schedule, if AGDC does not have the flexibility to replace that element as quickly as possible.

Use of contracting methods such as “Time & Materials” or “Cost-Plus”, are common in the private sector and government contracting as well. They can be done with full transparency and accountability. Third party estimators and other resources can be used to verify that costs are reasonable or within a range that is acceptable. Internal controls can be put in place to monitor and audit the procurement process at all phases of the project.

The US federal government recognizes the need for an alternate contracting and purchasing process for large projects and in 1994 the Federal Acquisition Streamlining Act was placed into United States law with the goal of lowering procurement barriers.

This Act enables simplified procurement procedures where the procurement is limited, facilitate reliance of commercial off-the-shelf technology, and promotes fixed-price performance based contracting. The law alters the United States government procurement strategy from lowest bid to best value. The Federal Acquisition Reform Act of 1996 removed the traditional oversight mechanisms that had been in place for decades and paved the way for a new method of awarding federal contracts.