

HOUSE FINANCE COMMITTEE
April 09, 2002
1:58 P.M.

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CALL TO ORDER

Co-Chair Williams called the House Finance Committee meeting to order at 1:58 P.M.

MEMBERS PRESENT

Representative Bill Williams, Co-Chair
Representative Eldon Mulder, Co-Chair
Representative Con Bunde, Vice-Chair
Representative Eric Croft
Representative John Davies
Representative John Harris
Representative Bill Hudson
Representative Ken Lancaster
Representative Carl Moses
Representative Jim Whitaker

MEMBERS ABSENT

Representative Richard Foster

ALSO PRESENT

Representative Pete Kott; Ed Flanagan, Commissioner, Department of Labor and Workforce Development; Neil Slotnick, Deputy Commissioner, Department of Revenue; Michael Hurley, Phillips Alaska, Anchorage; John Bitney, Legislative Liaison, Alaska Housing Finance Corporation, Department of Revenue; Joe Dubler, Director of Finance, Alaska Housing Finance Corporation, Department of Revenue; Linda Sylvester, Staff, Representative Pete Kott; Richard Mastriano, Director, Division of Labor Standards & Safety, Department of Labor; Michael Hurley, Phillips Alaska, Anchorage; Paul Fuhs, Yukon Pacific

PRESENT VIA TELECONFERENCE

Dan Fauske, Executive Director, Alaska Housing Finance Corporation, Department of Revenue, Washington D.C.; John Wagner, Tax Counsel, Omaha, Nebraska; Steve Kantor, Financial Advisor, New York; Howard Zucker, Tax/Bond Counsel, New York; Pat Gamble; Bill O'Leary; Stephanie Madsen; Jeff Brown, Goldman Sacks and Co.; Paul Bloom; E.

Wohlforth; Bill O'Leary, Vice President, Alaska Railroad Corporation, Anchorage

SUMMARY

HB 423 An Act relating to the Alaska Railroad; authorizing the Alaska Railroad Corporation to provide financing for the acquisition, construction, improvement, maintenance, equipping, or operation of facilities for the transportation of natural gas resources within and outside the state by others; authorizing the Alaska Railroad Corporation to issue bonds to finance such facilities; and providing for an effective date.

HB 423 was HEARD and HELD in Committee for further consideration.

HB 504 An Act relating to the wages of people working in the fisheries business.

HB 504 was HEARD and HELD in Committee for further consideration.

#HB504

HOUSE BILL NO. 504

An Act relating to the wages of people working in the fisheries business.

REPRESENTATIVE PETE KOTT explained that the bill would allow the remote processors the same opportunity as the non-remote processors in deducting from an employees wage, the cost of food and lodging.

Representative Kott noted that in 1959, the statute was enacted by the Legislature, which promulgated regulations, which exempted the remote processors. He stated that was over-stepping the boundary. HB 504 is an attempt to address concerns voiced by the remote processors.

Representative Kott referenced the committee substitute which would amend the Alaska Wage and Hour Act by adding a new section dealing with wages paid to employees in a fisheries business. An employer engaging in the fisheries business may deduct up to \$15 dollars each day from the applicable minimum wage paid to an employee for the combined cost of board and lodging provided to the employee. That deduction can be made only if it is based on a negotiated union agreement or a written agreement between employer and employee, entered into at the time of hire and that specifies the daily rate of deductions for room and board.

Representative Kott added that as defined in AS 43.75.290, a "fisheries business" means a person who engages in process fishery resource for sale by freezing, cooking, salting, or other methods and would includes but is not limited to canneries, cold storages, freezer ships and processing plants.

Co-Chair Mulder MOVED to ADOPT the work draft, #22-LS1595|P, Craver, 4/8/02, as the version of the legislation before the Committee. There being NO OBJECTION, it was adopted.

Vice-Chair Bunde asked if there were actual cost figures associated with the board and room.

Representative Kott replied that he had not yet acquired the exact amounts. According to the current federal regulations, the processors cannot charge over and beyond an amount that would bring them a profit.

Vice-Chair Bunde asked about the fiscal note and how many Alaskan processors would it apply to.

Representative Kott replied it would affect about thirty companies. He reiterated that \$15 dollars was a fair amount to pay for three meals a day and lodging.

Representative Lancaster asked if the legislation would be opening the door for remote construction sights.

Representative Kott commented that the "door would be opened for an industry that already has the door half opened". He stressed that the request was not for an exemption but rather parity for a quality of something that is already taking place. He agreed that another industry could be able to come in and pass similar legislation.

Representative Davies asked what the differences between the work draft and the original bill was.

Representative Kott explained the two changes which had been made:

- Adding the \$15 dollar price; and
- Placing into statute that there must be a written agreement.

Representative Davies noted that the stipulation that lodging would be "without profit" had not been included.

LINDA SYLVESTER, STAFF, REPRESENTATIVE PETE KOTT, explained that the original language of HB 504 comes directly from regulation. The regulations come directly from the federal code, which define the fair labor standards act. Those

standards are from federal legislation enacted in 1938. By using the terms "reasonable costs and without profit" will create built in protections for the employee that the charges will not be too excessive. The committee substitute proposes that in lieu of having a determination made by the Department of Labor for the reasonable costs, which would be further defined by non-profiting, new language would be substituted, indicating the \$15 dollar figure. She added that was a compromise given the assumption that the \$15 dollars is a "reasonable cost" for room and board.

Representative Hudson thought that the fiscal note was predicated upon the Department interpreting the reasonable costs without profit. By modifying that to the "P" version, it would be removed. He noted that the \$15 dollars was a set fee and would not indicate the actual costs. He understood that the fiscal note had been prepared to determine what the reasonable costs would be. He believed the fiscal note could be zeroed out.

Representative Kott agreed and recommended that the question be posed to Commissioner Flanagan from the Department of Labor.

Representative Harris advised that \$15 dollars a day would be charged for each day even if the employee was not working. He noted that would have to be agreed upon by the employee and employer before the work began. Representative Harris requested the bill's history.

Representative Kott explained that the minimum wage issue is looming over that industry. He pointed out that many of processing plants would be closing after this season. Closing the plants will not help these communities and their taxation concerns. In addition to the minimum wage change, there are additional cost driving factors.

Representative Kott stated his intent was to help the industry and that current regulations are "out of step" with the statutes.

Representative Harris inquired if this could be corrected through a regulation change rather than a statute change.

Representative Kott did not believe that it could be corrected through the regulation process. He noted that the Administration is "at a place" in which they could remove the regulation that stipulates alternative public housing must be available in that area. He wanted to see a statutory change.

Representative Croft asked if in the adopted work draft, language had been removed regarding a determination of the room or board price.

Representative Kott replied it had been and that \$15 dollars is a reasonable amount. He pointed out that testimony heard from the Department of Labor acknowledged that \$10 dollars a day was reasonable. The fiscal note was based on that.

Representative Croft asked if it was understood that \$15 dollars was both reasonable and fair and that the employer would not be making a profit at \$15 dollars a day.

Representative Kott agreed and that a profit could not be made according to the federal standards.

Representative Croft inquired if there was an appropriate distinction between a site that has an alternative and one that does not.

Ms. Sylvester pointed out that in the original language, the fair labor standards act, the act and the act of an employer counting the cost of room and board as a credit toward their wages has been upheld in federal court. The issue decided was if the employee needed to be consulted on that on a daily basis. The federal court upheld the statute and the determination that an employer could take a credit against the wages. The language in the original bill considered that the reasonable cost would be a profit for the adequate protection for the employee. The bill was further amended to include some requirements to the contract. That contract is signed at the beginning, with the employee's understanding of what the wage and limitations of that work site will be. She noted that through a compromise with the Finance Chair, rather than relying on the terms and definitions of the federal code, a \$15 dollar substitution would be made.

Representative Croft warned that someone might sign the agreement with little understanding of the conditions. He questioned what the limitations on the quality of the food and housing would be once the words like "reasonable" and "fair" were removed.

Ms. Sylvester acknowledged that the Department of Labor had registered those concerns. She added that a company could not take the proposed credit if there was an alternative. If an employee made a complaint, the Department of Labor would respond. If there were no value to the food or lodging, there would be no credit given. She reiterated that a decision had been made at the federal level.

Representative Croft asked if that was included in the language of the legislation.

Ms. Sylvester responded that would rest in the manner in which the Department of Labor addresses their complaints.

She noted that they previously testified regarding how they would address those situations. They do inspect and if there is a complaint, they respond.

Representative Kott mentioned the types of people who are attracted to the fish processor-type work. For the most part, they are students that come from out of State. He thought most of the workers would choose the lodging option. He pointed out that there are training and transportation costs associated with these services. The employers want to guarantee that the person being hired, understands what they are getting into. Often times, when going to remote sites, the employee opts for that knowing that they will not be distracted by places to spend their money. It is the intent of the employers to attract and retain their seasonal employees.

Representative Lancaster asked if the legislation would allow the employer to draw the \$15 dollars if they do not take the housing option.

Representative Kott responded that could be addressed during the contractual side of the agreement. He stated that the Legislature should not be dictating the terms of the contract. The terms should be left to each individual employer, however, the language should not be concrete. He commented that the market place would dictate a number between zero and \$15 dollars per day. He noted that the employee would investigate which employer would offer the best deal.

Representative Davies pointed out that if the fish were not running really well and the employee was only working eight hours a day, five days a week, that employee would be making \$1,000 dollars a month. If the legislation were in place, that same employee would be required to pay \$450 dollars a month for food and lodging.

Representative Kott admitted that there will be times when the fish are not running, regardless, it would still cost the employee something to live and eat where ever they were. He added that the last thing an employer wants is to have their employees not working. He added that the employee could be transferred to another remote site if there was no work. The employers attempt to keep all employees working most of the time.

Representative Davies commented that the employee could be "over the barrel" because of the transportation costs. He foresaw that circumstances could be unbearable for some individuals and they would then be really "stuck".

Representative Kott understood that during the hiring process, language is clarified that the transportation costs

would be paid out to the site and back, based on the fulfilling the contract. He interjected that there is "zero tolerance" for the use of drugs and/or alcohol at the site. If using, the employees would be sent back at their own expense.

Representative Davies reiterated his concern with those times there are no fish.

Representative Kott claimed that would be the last thing that a processor would want to happen.

Representative Moses questioned how a remote site is determined.

Ms. Sylvester replied that in the regulations, it is indicated that a remote site exists if there are no alternative places available to sleep and eat.

Representative Moses asked if the \$15 would be subject to a local sales tax.

Ms. Sylvester explained that the tax issue is an Internal Revenue Service (IRS) question. The IRS determined that it would not be included as income, because the facilities were on the premises of the employer. That is the way in which the employee gets out of paying taxes on the credit for wages paid. For purposes of the wage and hour act and the fair labor standards, that language does not consider room and lodging for the benefit of the employee, but rather the cost spent is for the benefit of the employer. She added that a person would not be charged a sales tax on that income.

Representative Whitaker noted that the language indicates that a maximum of \$15 dollars a day would be taken from the pay relative to the applicable minimum wage. He asked if there would be a sliding upward scale if the employee made more than minimum wage.

Representative Kott explained that was not the intention. The maximum is \$15 dollars per day. At present time, remote sites cannot pay below minimum wage.

Representative Whitaker asked if the intention was no more than \$15 dollars per day would be charged, regardless of the wage paid.

Representative Kott reiterated that \$15 dollars a day was the maximum, and noted it could be less.

Vice-Chair Bunde questioned the IRS impact.

Ms. Sylvester explained that under the IRS code, the \$15 credit is not considered part of the wage. However, if the employer paid the employee that \$15 dollars, the employee would then be taxed on that income.

Ms. Sylvester interjected that there is a floor and that "zero wages" was the term used for when more expenses are acquired than actual wages paid. According to the fair labor standards act, the employer cannot go below what the minimum wage was in January 1st, 1997. The Alaska wage and hour law takes precedence over federal law and is stricter. She reiterated that the State cannot fall below what federal law is.

Representative Davies asked if the State cannot go below the federal standard, how could they then deduct the \$15 dollars.

Ms. Sylvester responded that the people that work in the canneries make a lot of money and they cannot go below \$4.85 per hour level. If they did, they would be precluded because the employer cannot break federal law.

Discussion among Committee members followed regarding the minimum wage concerns and the minimum wage floor.

Co-Chair Williams noted that Alaska pays above the federal established minimum wage.

Representative Davies reiterated his concern of what happens when the employee is not getting the hours. Under that circumstance, almost half of the employee's income would be going to their deduction.

Representative Hudson asked if people coming to Alaska to work in the sport fishing lodges would be affected.

Ms. Sylvester advised that AS 23.10.085© applies and states that the regulations may permit deductions by employers paying minimum wage, applicable through the wage and hour act, to employees for the reasonable cost as determined by the director on an occupation basis for furnishing board and lodging. She stressed that it could apply to any situation of any remote sight; however, the only industry that this bill applies to is the fisheries business.

Representative Hudson recommended that there be equity in treatment. He questioned if the Department's regulations could manage the expense in a similar fashion.

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Ms. Sylvester noted that the Department of Labor regulations allows for that as long as there is alternative lodging available. The statutes clearly state it will be on an occupation basis. She noted that the Department could further discuss that.

Representative Kott interjected that the legislation can only happen on an occupational basis. He pointed out that there had been a misinterpretation of the statute regarding the difference between a remote and a non-remote processing plant. He maintained that there is no difference.

Representative Harris acknowledged that the bill only deals with the fisheries business, however, voiced concern that it could be "turned" to the North Slope construction business.

Representative Kott explained that the bill clarifies that the minimum wage earner could be penetrated. In the case of construction workers, they earn substantially more than minimum wage.

Representative Harris advised that he was thinking "down the road" and his concern when similar legislation occurs in the future to other industries.

Co-Chair Williams inquired if it would fall under the fair competition standards.

Ms. Sylvester interjected that the issue is regarding paying minimum wage. The most important issue is to allow the employer to deduct the room and board from the wages. Currently, regardless of how much an employee is making, the employer is prevented from recouping those costs from the employee. The amenities create a cost to the employer; urban employers are not asked to float these costs, but the remote employers are. The statute instructs the Department to make that determination on an occupational basis.

ED FLANAGAN, COMMISSIONER, DEPARTMENT OF LABOR AND WORKFORCE DEVELOPMENT, voiced strong opposition to the proposed bill. He stated that an inaccurate rendition of the regulatory history had been provided by the sponsor's office.

Commissioner Flanagan noted that the Alaska wage and hour act was written in 1959, with permissive language, which allows the Department to "may" promulgate regulations that would allow for deductions for room and board. He noted that was the same year that the minimum wage was established at fifty cents over the federal minimum of \$1 dollar an hour. Some of the issues raised at this time, placed that permissive language into the bill. No regulations were promulgated until 1985. He emphasized that the policy has been consistent through eight Administrations and three different political parties, and indicates that room and

board in remote locations is not charged to the workers. He pointed out that has been the custom of this country.

The 1985 regulations codified what the process was. At that time, the Department stated that there would be allowances made for reductions. He claimed that if the notion that room and board was being a "fringe" benefit was accepted, new and disturbing ground would be broken. The State would be well on its way to charging all other industries the same. He stressed that the Department has been consistent and that there has been no oversight on the interpretation.

Commissioner Flanagan identified the significance of the proposed change. There are some cannery workers that do make money, however, he pointed out that they usually work 80 hours a week. With that many hours, the person would be clearing \$565 dollars per week. Given the proposed wage increase, they would make \$775 dollars per week. He reminded members, that in those areas, there is no quality of life. Some of these employees do not work the rest of the year. These people cannot afford this legislation.

Commissioner Flanagan pointed out that the bill has an immediate effective date. It could be imposed before the minimum wage goes into effect. That would knock down their salaries to less than \$5 dollars an hour. That would be a shame.

Commissioner Flanagan asserted that the Legislature should be helping people "move over" the poverty level and minimum wage. He stressed that the ones who will benefit from the change are the employers. He pointed out that the percentage of actual Alaskan workers has risen in that industry from 24% ten years ago to currently about 40%.

Commissioner Flanagan emphasized that the proposed bill is "bad legislation". The medium age for a cannery worker in the State of Alaska is 34 years old. He disagreed with comments made by Representative Kott that usually college kids are hired. Commissioner Flanagan advised that there is only one plant that hires the old model "college kid", hoping to make a "bundle". Current day employees are "real" people trying to make a living.

Commissioner Flanagan urged that the Committee reconsider moving the bill.

Co-Chair Williams stated that the bill was attempting to help the processors. He understood that the logging industry used to pay room and board to loggers living in remote sites.

Commissioner Flanagan replied that if they were paying for room and board, they were not in compliance. He

acknowledged that the industry was having difficult times, but to change the method in aiding them and denying workers an increase in the minimum wage is bad policy. When times were better in fishing, the processors made money, the communities and fishermen made more money. The cannery workers only make minimum wage, regardless of the health of the industry. He reiterated that they do not make more money when times get better.

Co-Chair Williams reiterated that the legislation was an attempt to help the processors.

Commissioner Flanagan agreed that was the intent of the legislation, however, stated that was not a good remedy. Commissioner Flanagan disagreed with turning the State's back on 33 years of practice and now beginning to charge for room and board. He added that the action would affect all the other industries.

Co-Chair Williams stated that the fishing industry is "down on their knees" at this time. The Legislature is attempting to help that industry. He acknowledged that the fishing industry is changing.

Vice-Chair Bunde asked if there was a shortage of labor in the industry.

Commissioner Flanagan replied that there has been in recent years and that it moves up and down. There have been attempts to move people from one location to another attempting to follow the fish down.

Vice-Chair Bunde suggested that currently it is more of an employees rather than an employers market.

Commissioner Flanagan replied that was true two years ago, however, he was not sure about the circumstances at this time. He noted that there have been many closures, however, the processors have submitted more job orders than last year. Commissioner Flanagan reiterated that the work camps are a work, sleep, eat, environment. The cannery workers make very little for the amount of work they do.

Vice-Chair Bunde claimed that some people chose to work hard so that they can "take the rest of the year off".

Representative Davies commented that it would help the processors if the minimum wage were cut in half. He asked Commissioner Flanagan if the federal floor concerns had been addressed.

RICHARD MASTRIANO, DIRECTOR, DIVISION OF LABOR STANDARDS & SAFETY, DEPARTMENT OF LABOR, commented that he did not know what Ms. Sylvester was referring to. If someone came to the

Department with a contractual situation and if that employee agreed and voluntarily signed the contract, the employer could make those deductions. It could be below minimum wage.

Commissioner Flanagan interjected that there have been situations in which the employee ended up with a zero paycheck.

Mr. Mastriano added that that there have been times in which transportation and other costs were deducted from the employee wages, leaving the employee with no check. Those are the types of complaints that an investigator would look into.

Representative Kott asked if Mr. Mastriano had visited the processing plant in Petersburg.

Mr. Mastriano replied that was not located in his area and that he had not visited it.

Representative Kott asked if that plant was allowed to deduct their food and lodging costs. He noted that they were not a remote site.

Commissioner Flanagan replied that the Icicle plant in Petersburg pays their employees \$7 dollars per hour.

Representative Kott thought that with Icicle deducting those costs, they were penetrating the minimum wage.

Commissioner Flanagan explained that there are alternatives for food and lodging in Petersburg.

Representative Kott suspected that there would be only a few people living in the campgrounds and not taking advantage of the option offered by Icicle. He claimed that there are benefits to eating in the camp provided meal facility.

Commissioner Flanagan replied that there are other alternatives in Petersburg and that a person could probably subsist on a lot less than \$20 dollars per day. Deducting is illegal and that has been the law for over forty years. The legislation proposes to change the definition of room and board, which is a major departure from what the practice has been. He acknowledged that there are "tough" times for the fishing and processing industry but they should not be "helped out on the backs of workers".

Representative Kott pointed out that for some workers, the employer has dropped their pay below minimum wage. He stated that it should be made equitable and should be either rejected or repealed. He did not understand how the State

could distinguish between rural and urban in an occupational setting.

Commissioner Flanagan explained the area practices and the established situation in the State at that time, differentiates between urban and rural. The industry guaranteed that certain industries would be excluded when there was an alternative. In some locations such as Petersburg or Kodiak, there is a local work force that works in places. He noted that a formal campground could be an option in Petersburg and Kodiak.

Representative Kott claimed that the regulation has been discriminatory based on "remoteness".

Co-Chair Williams characterized that the bill as helping the industry.

Representative Harris acknowledged that HB 504 was intended to help the industry. He inquired if there had been an effort with the Administration to work out the differences to make the legislation "more appealing".

Representative Kott replied that there has not been much dialogue with the Administration. He claimed that it was a "cut and dry" issue.

Representative Croft claimed that there is a fundamental difference between having a choice and not having a choice. When a non-remote processor offers sub-standard housing for the crew, they can go somewhere else. He asked the Department's authority to monitor or change the condition of the provided housing and food.

Commissioner Flanagan responded that the authority for worker housing is listed under the Occupational Safety and Health Administration (OSHA). He did not know how they would deal with a complaint regarding the quantity and/or quality of the food.

Representative Croft asked what would happen if there was an allegation that the worker was not getting their \$15 dollars worth of food and bed.

Mr. Mastriano responded that if someone were to complain to the Department about the reasonable costs charged, the Department goes by the federal guidelines and would perform a reasonable cost audit.

Representative Croft understood that the Department would not have the authority, under the proposed legislation, to define "reasonable".

Commissioner Flanagan stated that the fiscal note was based on the original bill. If lawfully adequate room and board were being provided, the cost would probably be over \$15 dollars. If there were complaints, the Department would have to investigate. The \$15 dollar amendment moves much of the fiscal note and there would probably not be more than forty or fifty audits a year.

Representative Davies and Co-Chair Williams argued over whether to discuss the bill further.

Co-Chair Mulder interjected that there was bond counsel on line to discuss HB 423. He noted that was costing the State \$150 dollars per hour for the legal advice. He pointed out that he had urged Co-Chair Williams to wrap up discussion on HB 504 more quickly. He apologized to the Committee.

Co-Chair Mulder digressed and asked if the ergonomics regulations were still in place.

Mr. Mastriano replied that the Department was in the process of rewriting those regulations.

Representative Croft asked the source of "reasonable and fair" with regard to the food and lodging and the context in which it was being used.

Mr. Mastriano replied that was a federal source reference. He added that the costs of actually operating the facility must be taken into account, and not for profit. If the facilities were similar, they would look at what the cost for utilities & depreciation would be. All those considerations take into account what a reasonable profit is.

Representative Croft asked how long that had that been a part of federal law.

Mr. Mastriano replied since 1938 and that whenever a reasonable cost is determined, profits are not included.

Co-Chair Williams stated that HB 504 would be HELD in Committee.

HB 504 was HELD in Committee for further consideration.

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#HB423

HOUSE BILL NO. 423

An Act relating to the Alaska Railroad; authorizing the Alaska Railroad Corporation to provide financing for

the acquisition, construction, improvement, maintenance, equipping, or operation of facilities for the transportation of natural gas resources within and outside the state by others; authorizing the Alaska Railroad Corporation to issue bonds to finance such facilities; and providing for an effective date.

NEIL SLOTNICK, DEPUTY COMMISSIONER, DEPARTMENT OF REVENUE, spoke in support of the legislation. He observed that the initial review indicated that public financing could not be used for private activity. There are some exceptions to that rule, with a private activity cap for \$225 million dollars, which the State does have access to. That cap is almost always fully subscribed to because Alaska Housing and Finance Corporation (AHFC) use it for some of THEIR housing finance needs. None of the exceptions fit into something as large as a gas pipeline. Mr. Slotnick pointed out that there was one other exception and that there could be a "special congressional" exception to the requirement.

Mr. Slotnick noted that is where is was left when some outside advisors, bond counsel and the investment bank, Goldman and Saks, came to the Department of Revenue and informed the State of a special State exception that already exists in federal law, the Railroad Transfer Act. He pointed out that a copy of that statute had been included in member's packets, USC Title 45, Chapter 21, the Railroad Transfer Act, Section 12.07.A6A. (Copy on File). The exception allows the railroad to borrow money on a tax-exempt basis for purposes, which would include the financing of a transportation project of a natural gas pipeline. In addition, the Railroad would not have to take ownership of the pipeline.

Mr. Slotnick explained that would be termed "conduit" financing. He referred to Page 4 of the handout and the financing of the marine terminal by the City of Valdez. That City, using its tax-exempt financing status, did the financing but Valdez did not have to undertake the ownership of the marine terminal. They did not have to use their own credit-at-risk to issue bonds. The bonds are guaranteed by the credit of the underlying companies. The State is using the same analogy to explain what can be done for the gas pipeline. The law in the Railroad Transfer Act is a unique, special exception that does not have the same limitations of other practices trying to do private activity financing.

Mr. Slotnick explained how the financing would move forward in the market. He referred to the Canadian gas pipeline. That project was 70% debt and 30% equity, which is about the most debt that the market would allow the State of Alaska to undertake. The market wants to guarantee that there is a principal behind the financing that has its own capital at

risk. Tax-exempt financing runs at about 20% - 25% less than taxable financing.

Mr. Slotnick referenced the "Alaska Gas Pipeline Financing Alternatives" handout. (Copy on File). He noted Page 12, "Taxable versus Tax-Exempt: Gross Interest Cost". He commented that the best way to determine the savings is by preparing a present value analysis. There would be approximately a \$1 billion dollar savings if the producers had access to tax exempt financing through the Railroad. He reviewed some of the assumptions used in preparing the analysis:

- The credit would be backed by companies through a ship or pay contract.
- If project financing was used, it was assumed that there would be approximately an 8.5% interest rate with 6.5% tax exempt;
- Four year construction period; and
- Twenty-five year bond issue.

Mr. Slotnick explained why the State legislation was necessary even with the federal authorization. The feds gave the authority, but when the State purchased the Railroad, it did not give authority to issue bonds for a gas pipeline transportation project. The legislation authorizes the sale of bonds in the market for a project that is backed by contracts with the producers.

JEFF BROWN, (TESTIFIED VIA TELECONFERENCE), GOLDMAN AND SACKS, spoke in support of the legislation. He observed that there would be a 20-year amortization on the debt. The Governor's number of \$1 billion dollars could be larger given more aggressive assumptions. He complimented the Alaska State Department of Revenue for their detailed work.

In response to a question by Vice-Chair Bunde, Mr. Slotnick noted that producers do not feel that there is enough incentive. The Department's assumptions were based on a \$17 billion dollar project and a \$3 barrel of gas would have led the State to the same conclusion.

Vice-Chair Bunde estimated that a substantial return on the investment would be needed.

Mr. Slotnick did not know what the hurdle rate would be for the producers.

Representative Davies observed that there are concerns regarding the application of the Railroad Act.

Mr. Slotnick noted that the IRS has not been consulted on the issue.

ERIC WOHLFORTH, (TESTIFIED VIA TELECONFERENCE), ECONOMIST, ANCHORAGE, explained that it was adequate and complete for the Railroad to undertake tax exempt financing of the gas line when the Legislature authorizes that project. The Railroad lacks the power to issue bonds; consequently, the bill is needed. Once the bill passes, the Railroad would be legally able to move forward with the pipeline-financing project.

Representative Davies asked about the issues around the IRS re-authorization.

Mr. Wohlforth explained that the federal authorization path cleared without conflicts or ambiguities. It was clarified that there could not be specific exemptions. There is no doubt that there is clear authority to undertake the project.

Representative Hudson asked about the problem between the Railroad and the pipeline and the restrictions upon the Railroad's use of the tax-free borrowing capacity.

Mr. Wohlforth advised that the financing of a gas pipeline is within the charter authority of the Railroad and the Railroad was authorized to undertake financing for that purpose. It would be used for transportation.

Representative Hudson asked who would own the \$1 billion dollar asset.

Mr. Wohlforth explained that the gas pipeline would remain within the ownership as if no public financing had taken place and would be a pass through, non-recourse financing. It would be a financing not involving the change of ownership. There would be legal support of the bonds, but it would not allow any transfer of ownership.

Representative Hudson asked clarification that the State would no longer have the asset value of \$1 billion dollars if the Railroad secures the tax-free funds.

Mr. Wohlforth agreed and added that the State would not have ownership in the gas pipeline were financed.

Representative Croft asked if it was assumed was that the producers would own it.

Mr. Wohlforth thought that question should be left to Department of Revenue.

Mr. Brown added that the shippers for the oil companies would own the pipeline and that they would be able to take

the depreciation benefits on the pipeline. He explained that was important because:

- The ownership is a huge economic issue; and
- The Governor's Pipeline Counsel recommended that the State not own the pipeline.

Representative Croft asked if the "shippers" were the people who own the right to the oil.

Mr. Brown commented that the shippers could either be those who own the oil or the "ultimate" customers.

Representative Croft understood that the more financially secure the entity, the less advantage they get from the status. He asked if it was correct that a corporation as solvent as Exxon, would receive less of a benefit than an independent pipeline company.

Mr. Brown agreed that was a "fair assumption". With most big projects, there is an advantage to the user of the pipeline in order for it to be project financed. That minimizes the expensive equity put in. Different companies will look at it differently. Initially, only a few companies were registered but as it became a success, twenty or thirty companies came on board. That is why companies appreciate doing their own balancing rather than using a project balance sheet.

Representative Croft asked the different models created between a company owned by an independent versus the producer.

Mr. Brown noted that if an AAA oil company were financing it long term and using relatively less debt, versus a BBB pipeline company, the benefit would be very different.

Representative Whitaker asked if the mid-point savings would be \$1 billion dollars over a twenty-year time period and if it would be weighted equally over the course of the twenty years.

Mr. Slotnick stated that was not accurate as that is not the manner in which the municipal bond market works. The full advantage of the tax exemption is not yet provided. Bondholders do not like to take long-term tax risk. The \$1 billion dollars value is the present value and in actuality, it would be more like \$5 billion dollars real terms.

Mr. Brown noted that the raw numbers amounted to nearly \$100 million dollars per year.

Representative Whitaker thought that the \$100 million present dollar per year value added to an expected return, by the State's assumption would not get the project "over the hurdle". He claimed that the producers were seeking another number.

Mr. Slotnick advised that the economists had plugged in various assumptions over the years. He did not know what was a reasonable projection.

Representative Whitaker referenced the \$163 million dollar FY05 fiscal note projection, a contractual expense to be paid by bond proceeds. He questioned what the \$163 million dollars would be used for.

Mr. Slotnick advised that would be used for the expense of issuing bonds. It would be paid to bond counsel, underwriters and financial advisors. The decision would be left up to the Railroad, as they would be the contracting entity. Mr. Slotnick suggested that future questioning be directed to the Railroad. He advised that he had spoken with the Railroad to help develop the procedures for going to market. The agencies involved are Alaska Housing Finance Corporation (AHFC), Alaska Industrial Export & Development Authority (AIDEA), and the Department of Revenue.

Vice-Chair Bunde asked who would pay the cost.

Mr. Slotnick explained that the cost would be paid by the Railroad and would be reimbursed through the proceeds of the bond sale. The eventual payer would be the owner of the pipeline.

Representative Whitaker commented that the cost would be reflected in the tariff. He assumed that the State of Alaska would essentially be paying the \$160 million dollar cost.

Mr. Slotnick acknowledged that the cost of issuance of the bonds would be reflected in the tariff, even if it were taxable through taxable bonds or through tax-exempt bonds.

DAN FAUSKE, (TESTIFIED VIA TELECONFERENCE), EXECUTIVE DIRECTOR, ALASKA HOUSING FINANCE CORPORATION, DEPARTMENT OF REVENUE, WASHINGTON D.C., stated that there are a lot of questions that need to be answered in reference to the IRS. He noted that those concerns are beyond the control of AHFC and the legislators. He commented that the proposed legislation was a very "do-able" deal. However, the IRS agents or U.S. Congress could question the deal. He stated that it is important that the State put itself in a position to act on the proposed deal. He believed that would send a strong message to Congress about Alaska's preparedness to undertake the deal. Additionally, it would send a message

to the oil and gas industry that the project is do-able and in the case of dollars, tax exempt financing would be a step in the right direction to make the project viable.

Mr. Fauske referenced the fiscal note and the underwriting costs. The costs are built in on how to price that bond. Mr. Fauske did not know how those costs would be paid.

JOHN BITNEY, LEGISLATIVE LIAISON, ALASKA HOUSING FINANCE CORPORATION, DEPARTMENT OF REVENUE, referenced the handout distributed, "Presentation to the House Finance Committee by Alaska Housing Finance Corporation, April 9, 2002". (Copy on File). He noted that the information in the handout is a replica of what AHFC provided to the Alaska Railroad for preparing the tax-exempt finance bond.

JOE DUBLER, CHIEF FINANCAL OFFICIER, ALASKA HOUSING FINANCE CORPORATION, DEPARTMENT OF REVENUE, introduced the team of participants with AHFC and financial advisors that were on line.

Mr. Dubler spoke to the assumed a 30-year term. He claimed that AHFC's proposed numbers were more aggressive. He referenced the booklet and the tax-exempt bond issuance:

- Selecting appropriate professionals such as the financial, tax, legal, and financing specific experts;
- Performing feasibility analysis such as tax, financial, and project analysis;
- Developing optimal finance structure such as coordination with users of project;
- Generating local support;
- Providing information to the public; and
- Responding to rating agency concerns and obtaining a rating.

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- Marketing the bonds with the institutional and the retail investors; and
- Providing continuing disclosure.

Representative Whitaker thought that there should be more than one approach to the bond issue.

Mr. Bitney explained that AHFC was hoping that based upon their experience in providing the "lion's share" of tax financing to the State, they would show the types of things that are necessary to undertake that type of financing. HB

423 would authorize the Alaska Railroad for the federal tax exemption. The passage of the bill would be financing under the auspicious of the Alaska Railroad. At that point, it would be the obligation of that agency to conduct the financing.

Representative Whitaker asked if there would be an opportunity for the State to gain some of that portion back.

Mr. Wohlforth explained that in 1974, the City of Valdez was part of the first financing. The City charged 1% and has continued to charge that fee for recent refinancing, extending the term to 2031. With the 1% increased aid fee the City has charged, they now have a permanent fund in the order of approximately \$55 million dollars. That could be a consideration for the Railroad.

Representative Whitaker questioned if the AHFC approach was different from the approach put forward by the Department of Revenue.

Mr. Bitney responded that there have been no decisions regarding the specific approach of how to address the concern. AHFC is providing a series of necessary steps in order that it can happen. The key rests with the selection of the people involved in structuring the financing.

Representative Whitaker asked if the State was on the correct financing course.

Mr. Bitney did not know of any problems at this point. It is a process that needs to be driven by the Railroad.

Representative Whitaker commented on the nature of the transaction and the value it could have for serving the State of Alaska. He suggested that if AHFC should become aware of something in the process that was "non-competitive", they would come forward and warn the Administration.

Mr. Dubler explained that to the extent that AHFC was involved in any transaction, they will take steps to insure the process.

Representative Whitaker asked who would insure that the process was procedurally competitive and in compliance with how the public process is conducted.

Mr. Bitney advised that at this point in the process, AHFC is not in charge of the financing, pointing out that right now, AHFC is only addressing the process needed to get the procedure started.

Mr. Dubler explained that the meeting presentation had been encouraged by Alaska Railroad and was not intended to be a secondary or alternate approach.

Representative Whitaker asked who is in charge.

Mr. Dubler explained that the Railroad is in charge.

Mr. Fauske noted that AHFC was asked to prepare advice based on their experience. There are a couple of agencies involved that have extensive experience in financing. These agencies stand on the position that offering assistance would help show the way for the transaction to happen. Alaska Railroad will be issuing the bonds and they have no experience in doing that. With a model in place, AFHC, AIDEA and the State would be the best and most effective tax models.

Mr. Fauske mentioned that with a "deal" this large, it is important to get as many outside firms as possible involved to help market it. It is imperative that the Alaska Railroad authority will reside with that entity and that the Railroad has absolute control over the financing. He advised that there have been no discussions other than how to approach the issue with the underwriters. Mr. Fauske urged that the idea move forward as it would mean a great deal for the State and to the Nation.

MICHAEL HURLEY, PHILLIPS ALASKA, ANCHORAGE, spoke in support of HB 423. He noted that Phillips Alaska has reviewed the concept embodied in the bill. Conduit financing does have the potential to benefit the gas pipeline project. Additional clarity in several areas will be needed. He added that Phillips Alaska is continuing to evaluate the impacts more fully. At this time, Phillips Alaska supports passage of the legislation, which would provide the authorization necessary if the project were to become a viable alternative.

Representative Whitaker asked who Mr. Hurley previously represented.

Mr. Hurley noted that in the past, he had represented three companies, Exxon Mobil, British Petroleum and Phillips Alaska.

JERRY MCCUTHEON, (TESTIFIED VIA TELECONFERENCE), ANCHORAGE, claimed that there will not be a gas pipeline out of Alaska in our lifetime. He spoke to concerns regarding the C2's and C3's. The project would need about five trains a day. He commented that it could be done, if the State was willing to pay for the track. Amtrak is requesting billions of dollars. Amtrak and the Alaska Railroad are the two eligible entities for those billions for which Amtrak

desperately needs. He said that the current system of putting the gas liquids in a hot oil line is wasteful.

Vice-Chair Bunde suggested that there should be opportunities for future legislators to "weigh-in" or review the procedures. He warned about the size of the project and the amount of oversight that it will need.

PAUL FUHS, YUKON PACIFIC CORPORATION, spoke in support of the proposed legislation. He noted that when it was first proposed, it could only be used for a pipeline through Canada. The Oil and Gas Committee did amend the bill to allow other options including the pipelines to tide water in Alaska.

Mr. Fuhs pointed out that the State is attempting to make an economic model of a project available to the Oil and Gas Committee in contrast to other projects. Mr. Fuhs noted that there have been rates of returns indicated in the range proposed by Vice-Chair Bunde. If the railroad model could improve the financing, those rates would improve more.

He claimed that there is a huge fight regarding who will get the value added for the project. At this time, there are 18 alternative proposals. He stated that he would make the handout about the alternative mean proposals available to the Committee. (Copy on File). Two tests need to be used to determine whether the project is feasible:

- The first is the economic amount being put forward and whether the market would be buying that gas; and
- Whether the bonds can be sold. People will need to believe in the economics of the project.

Co-Chair Williams noted that HB 423 would be HELD in Committee for further consideration.

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ADJOURNMENT

The meeting was adjourned at 4:45 P.M.