

**ALASKA STATE LEGISLATURE**  
**HOUSE SPECIAL COMMITTEE ON OIL AND GAS**

March 25, 2002

9:08 a.m.

**MEMBERS PRESENT**

Representative Hugh Fate, Vice Chair  
Representative Fred Dyson  
Representative Mike Chenault  
Representative Vic Kohring  
Representative Gretchen Guess  
Representative Reggie Joule

**MEMBERS ABSENT**

Representative Scott Ogan, Chair

**COMMITTEE CALENDAR**

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."

- MOVED CSHB 423(O&G) OUT OF COMMITTEE

SPONSOR SUBSTITUTE FOR HOUSE BILL NO. 190

"An Act levying and collecting a tax on certain North Slope natural gas in place if certain requirements relating to its sale and delivery are not met, and imposing a limit on the Department of Natural Resources that relates to the issuance or extension of oil and gas leases containing natural gas that is capable of production in paying quantities; and providing for an effective date."

- BILL HEARING POSTPONED

**PREVIOUS ACTION**

BILL: HB 423

SHORT TITLE:NATURAL GAS TRANSPORTATION BY ALASKA RR

SPONSOR(S): RLS BY REQUEST OF THE GOVERNOR

Jrn-Date	Jrn-Page	Action	
02/13/02	2244	(H)	READ THE FIRST TIME - REFERRALS
02/13/02	2244	(H)	O&G, FIN
02/13/02	2244	(H)	FN1: (CED)
02/13/02	2244	(H)	GOVERNOR'S TRANSMITTAL LETTER
02/13/02	2244	(H)	REFERRED TO OIL & GAS
03/14/02		(H)	O&G AT 10:00 AM CAPITOL 124
03/14/02		(H)	Heard & Held
03/14/02		(H)	MINUTE(O&G)
03/18/02		(H)	O&G AT 9:00 AM CAPITOL 124
03/18/02		(H)	-- Meeting Canceled --
03/25/02		(H)	O&G AT 9:00 AM CAPITOL 124

**WITNESS REGISTER**

NEIL SLOTNICK, Deputy Commissioner  
Office of the Commissioner  
Department of Revenue  
P.O. Box 110405  
Juneau, Alaska 99811-0405  
POSITION STATEMENT: Presented HB 423 and answered questions.

SENATOR JOHN TORGERSON  
Alaska State Legislature  
Capitol Building, Room 427  
Juneau, Alaska 99801  
POSITION STATEMENT: Provided information pertinent to HB 423.

PATRICK GAMBLE, President and CEO  
Alaska Railroad Corporation (ARRC)  
Department of Community & Economic Development  
P.O. Box 107500  
Anchorage, Alaska 99510-7500  
POSITION STATEMENT: Testified on the impacts HB 423 might have on the Alaska Railroad.

DANIEL R. FAUSKE, CEO/Executive Director  
Alaska Housing Finance Corporation (AHFC)  
Department of Revenue  
P.O. Box 101020  
Anchorage, Alaska 99510-1020  
POSITION STATEMENT: Testified in support of the concept of HB 423 and answered questions.

JOE DUBLER, Finance Director

Alaska Housing Finance Corporation (AHFC)  
Department of Revenue  
P.O. Box 101020  
Anchorage, Alaska 99510-1020  
POSITION STATEMENT: Answered questions relating to HB 423.

JOHN WAGNER, Senior Partner  
Kutak Rock LLP  
(Address not provided)  
POSITION STATEMENT: As tax counsel for AHFC, answered questions relating to HB 423.

MICHAEL J. HURLEY, Senior Commercialization Specialist  
ANS Gas Commercialization  
Phillips Alaska, Inc.  
P.O. Box 100360  
Anchorage, Alaska 99501  
POSITION STATEMENT: Testified in support of HB 423.

PAUL FUHS, Lobbyist  
for Yukon Pacific Corporation  
1635 Sitka, Number 301  
Anchorage, Alaska 99501  
POSITION STATEMENT: Testified in support of HB 423, but requested an amendment.

DAVE MacDOWELL, External Affairs Manager  
for Gas Activities in Alaska  
BP Exploration (Alaska) Inc.  
17600 Rosemont Drive  
Anchorage, Alaska 99516  
POSITION STATEMENT: Testified in support of HB 423.

PAM LaBOLLE, President  
Alaska State Chamber of Commerce  
217 2nd Street, Suite 201  
Juneau, Alaska 99801  
POSITION STATEMENT: Testified in support of HB 423.

ERIC WOHLFORTH, Attorney at Law  
Wohlforth, Vassar, Johnson & Brecht, APC  
900 West 5th Avenue, Suite 600  
Anchorage, Alaska 99501  
POSITION STATEMENT: As bond counsel, answered question regarding Section 5 of HB 423, saying there is no reason the definition couldn't be expanded.

**ACTION NARRATIVE**

TAPE 02-18, SIDE A  
Number 0001

VICE CHAIR FATE called the House Special Committee on Oil and Gas meeting to order at 9:08 a.m. Representatives Fate, Chenault, Kohring, Guess, and Joule were present at the call to order. Representative Dyson arrived as the meeting was in progress. [Representative Ogan was excused.]

HB 423-NATURAL GAS TRANSPORTATION BY ALASKA RR

Number 0066

VICE CHAIR FATE announced that the committee would hear 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."

VICE CHAIR FATE invited Mr. Slotnick to explain the bill [which was sponsored by the House Rules Standing Committee by request of the governor].

Number 0101

NEIL SLOTNICK, Deputy Commissioner, Office of the Commissioner, Department of Revenue, informed the committee that the department has been working extensively with outside consultants and the Alaska Railroad Corporation (ARRC), analyzing the concept in HB 423, which is using the ARRC's exemption to the "tax-exempt financing laws" in the Internal Revenue Code to finance development of a natural gas pipeline in Alaska.

Number 0176

MR. SLOTNICK brought attention to a written presentation in committee packets titled "Alaska Gas Pipeline Financing Alternatives: Use of Tax-Exempt Financing through the Alaska Railroad," dated February 7, 2002. Page 4, he pointed out, depicts what are called official statements relating to the offering in 1977 of some bonds issued by the City of Valdez for the marine terminal for the Trans-Alaska Pipeline System (TAPS).

He cited those as an example of what is being discussed today: conduit financing using a public corporation - in this case, the ARRC, which is similar to the City of Valdez, a municipal entity - to sell tax-exempt bonds to finance what is essentially a private-enterprise transportation facility.

Number 0380

MR. SLOTNICK explained that in 1977, offerings were made by the City of Valdez on the basis of the credit of the companies that would be building the marine terminal. The City of Valdez bonds, therefore, were backed by the credit of Exxon Corporation. Although able to use its tax-exempt status to issue the bonds, the city didn't bear any of the risk that the marine terminal would prove unprofitable or that bondholders could go against the City of Valdez.

MR. SLOTNICK noted that similarly, proposed here is that ARRC use its tax-exempt status to issue bonds to finance the building of a natural gas pipeline from Prudhoe Bay to markets in the Lower 48. As to why Valdez could do this in 1977 but the state must go through the ARRC, he explained that for one thing, the 1977 financing was only for the marine terminal. Valdez took advantage of the ports-and-harbors exception to the rules against using tax-exempt financing for private, for-profit projects and was able to sell these bonds, and yet the companies could retain ownership and back the project with their credit.

MR. SLOTNICK pointed out that "our" opportunities today to sell tax-exempt financing are limited to public projects such as schools, roads, or "other things that you'll typically see the state or municipalities selling bonds for."

Number 0480

MR. SLOTNICK referred to the limited exception used by Valdez in 1977 and reported that in the Tax Reform Act of 1986, Congress narrowed that exception further; if Valdez tried [today] to finance such a ports-and-harbors project, it would have to retain ownership.

MR. SLOTNICK specified that under discussion today is the model of ARRC selling bonds, but having the ownership and risk stay with the private companies, which are the producers or pipeline companies that actually build and own the line.

Number 0546

MR. SLOTNICK explained why the railroad has a special exemption. In the [Alaska] Railroad Transfer Act of [1982], when the federal government transferred ownership of the Alaska Railroad to the state, a last-minute provision was added that exempts the railroad from the requirements of what were then called industrial development bonds - now called private activity bonds.

MR. SLOTNICK read from the Alaska Railroad Transfer Act, "Obligation issued by such entity shall be deemed to be obligations of the state but not obligations within the meaning of section 103(b)(2) of the Internal Revenue Code." He indicated this gives the railroad an exemption to the rules that otherwise would require the entity selling the industrial development bonds as a conduit to retain ownership of the facilities.

MR. SLOTNICK reported that furthermore, there is no cap here on the amount of bonds that could be sold. Student loans can be sold by the state, for example, but are capped. He added, "I think the State of Alaska has a \$185 million cap, ... and that's always spoken for by AHFC [Alaska Housing Finance Corporation], by AIDEA [Alaska Industrial Development and Export Authority], and by Alaska Student Loan [Corporation], as well as by municipalities."

Number 0739

MR. SLOTNICK pointed out that despite the Alaska Railroad's unique exemption in the United States Code, it doesn't have authorization under state law to issue bonds. It has to come back to [the legislature] before issuing any bonds at all, and it doesn't have specific authorization to issue bonds for development of a natural gas pipeline. He therefore urged passage of HB 423.

MR. SLOTNICK suggested that bond counsel Eric Wohlforth of Wohlforth, Vassar, Johnson & Brecht, who was on teleconference, could offer expertise regarding both the Alaska Railroad Transfer Act and the financing that took place on the Valdez marine terminal, should there be technical questions.

Number 0851

MR. SLOTNICK turned attention to the financing modeling and why it might be something the producers would be interested in. He

said tax-exempt financing is always cheaper than taxable financing. People who buy the bonds don't have to pay taxes on the interest from the bonds; therefore, the bonds can be sold at a much cheaper interest rate. Generally, the market will price tax-exempt bonds 20-25 percent cheaper than taxable bonds.

MR. SLOTNICK estimated that if this were financed today on a "project-finance" basis, the spread in interest rates between a taxable and a tax-exempt project-finance bond would be roughly 2 percent. For example, if the market priced this project at about 8.5 percent taxable, he said, "we would think it would be about a 6.5 tax-exempt."

Number 0955

MR. SLOTNICK noted that the producers would have many financing options for this project. For instance, rather than having the bonds based on the project itself, they could be based on the balance sheet of the corporations, which would provide a cheaper rate because of the more solid guarantee. Tax-exempt bonds sold based on the corporate credit would be, again, roughly 20-25 percent cheaper than taxable bonds.

MR. SLOTNICK explained that because of the numerous options, presenting a model and figuring out the amount of savings was difficult; nonetheless, he was presenting a model that assumes a \$17 billion project that is 70 percent debt-financed and 30 percent equity-financed, which requires someone to come up with cash before the bonds are brought to market. The market doesn't want to see 100 percent debt financing, he explained, but wants someone taking risks other than the purchasers and investors in the bonds used to finance a project. He cited the Alliance Pipeline that transports natural gas from Alberta to Chicago as an example of a project with that [70-30] structure.

MR. SLOTNICK noted that using the foregoing assumptions, the model has \$14.25 billion in bonds issued in a tax-exempt scenario. "That's more than the 70 percent if you're doing the quick math in your head," he pointed out, "but that's because you also sell bonds to finance the interest payments during the period of construction." He said he would provide the figures for a taxable scenario for comparison.

Number 1128

MR. SLOTNICK continued with the model. He referred to the gross-interest difference referenced in the packet, but said it

is a meaningless figure because interest is tax-deductible. What should be compared is the after-tax difference in cost to the companies of tax-exempt versus taxable financing. To make it meaningful, he said, one needs to "present-value it" back to today's dollars. This is a 25-year project, he pointed out, and future dollars aren't worth as much as dollars in hand today; therefore, in this model it is "present-valued" back to the start of the project, with a resulting savings to the producers "in 2007 dollars" of more than \$1 billion for tax-exempt financing.

Number 1239

MR. SLOTNICK highlighted an important element of the model: the expectation that the producers would enter into ship-or-pay contracts. He explained:

That would be the basis of ... taking this credit to market. That's the way the Alliance Pipeline was done, is that the producers entered into ship-or-pay contracts, meaning that even if ... the project doesn't get built or is delayed, there is a requirement that the producers come up with the money that would be backing the bonds. That's why there ... would always be the credit of the producers behind such a project.

Number 1280

MR. SLOTNICK reported that [the Department of Revenue] had worked closely with an "investment banker" firm to do this modeling. Not only had the department's economist run models, but economists and analysts at the firm of Goldman Sachs had assisted and run some models as well. Mr. Slotnick said he wasn't sure whether the analyst from Goldman Sachs was on teleconference that day to answer questions, but if there was a question he himself couldn't answer, he could get back to the committee later with the answer.

Number 1336

MR. SLOTNICK explained [Section 2] of HB 423. He reiterated that the Alaska Railroad has a unique authorization in federal law that allows it to issue bonds to finance this project, but doesn't have that authority in Alaska law. [Section 2] therefore requests an amendment to AS 42.40.250, the enabling Act for the Alaska Railroad, to add a paragraph [(13)] to the

list that provides authority for the railroad to issue the financing "for the acquisition, construction, improvement, maintenance, equipping, and operation of facilities for the transportation of natural gas resources within and outside the state without regard to whether the facilities are [or] will be owned in whole or in part by the corporation or located on land owned by the corporation."

Number 1426

MR. SLOTNICK explained Section 3. He said AS 42.40.630 describes that the railroad can issue bonds with legislative authorization and can pay for those bonds through its own revenues or with state or federal grants. He remarked, "But here, of course, we're going to require that the railroad pay for these bonds through means of a contract entered into with the gas-producing entities. So we wanted to put that directly into the law, as well, for these bonds that would be sold under the previous authorization that I've just described."

MR. SLOTNICK noted that Section 4 just states clearly that these bonds are for a public purpose, which is a requirement to issue tax-exempt bonds. Section 5 gives the actual authorization for ARRC to sell these bonds.

Number 1485

MR. SLOTNICK brought attention to the fiscal note from ARRC, which describes ARRC's estimated contractual costs for issuance. He explained, "Those costs would be paid for by the bond proceeds, but nevertheless they would be a cost that would ... have to go through the railroad; so, therefore, we put in the fiscal note with that estimate in it."

MR. SLOTNICK turned attention to the fiscal note from the Department of Revenue, saying the department has put in a small fiscal note for this upcoming fiscal year. He explained:

The purpose of this money is to RSA [use a reimbursable services agreement] to the railroad so that the railroad can enter into contracts with a financing team. The railroad should have the same kind of access to the same kind of outside consultants that we at the Department of Revenue have whenever we go to the market to sell bonds.

Number 1580

MR. SLOTNICK continued with the department's fiscal note. He said all entities that sell bonds engage a financial advisor and bond counsel for these complicated transactions; there are lots of laws governing them and lots of financial considerations about structure and timing, for example, that require an expert's advice. Frequently, contracts with financial advisors or bond counsel are done on a "deal contingency" basis: "when the deal is done, that's when they collect their money." That is how the Department of Revenue pays its financial advisor and bond counsel, he noted.

MR. SLOTNICK cautioned, however, that although ARRC could probably procure outside consultants on this basis, he believes ARRC should avail itself of advisors whose pay isn't necessarily contingent on having a deal go forward. If, for some reason, the deal being discussed was not in the best interest of the state and the Alaska Railroad, it would be best if the advisor had no incentive to keep that information quiet.

Number 1644

MR. SLOTNICK continued with the fiscal note:

My suggestion here is that it's a small amount of money, \$50,000 for the next two years to RSA over to the railroad for it to obtain advisors that can work with the railroad on how best to structure this, how best to go forward to market. And if ... those advisors end up putting in more time than is covered by this, well, I'm not too worried about that. They'll be willing to do that. ...

If this goes forward at all, this is going to be a very big deal, and advisors and consultants are going to be willing to give the railroad all the help that [it] needs.

MR. SLOTNICK reiterated that he'd feel more comfortable "if the railroad's financing team was not out there with its pay contingent on the deal, that we had a contract in place to make clear that these advisors were working on behalf of the railroad." He continued:

I think the Department of Revenue is willing to RSA this money to the railroad. The railroad is not under the Executive Budget Act and didn't put in a fiscal

note itself for these advisors; we agreed to do that on their behalf, but we do think that is a step that should be taken. ... I've met with the railroad. I appeared before the railroad board last week. We've explained this fiscal note to them.

MR. SLOTNICK concluded by discussing suggestions made:

We've also suggested to the railroad that perhaps we should assemble a committee of the state entities that have a lot of experience in issuing tax-exempt bonds. Besides the Department of Revenue, that would include AIDEA, which has a history of doing conduit bonds like this, and it is an industrial development agency, ... and then Alaska Housing [Finance Corporation]; ... it's actually the biggest issuer of tax-exempt bonds in this state, so they have a lot of experience and a lot of good staff.

So my suggestion to the railroad was, as it's pushing forward with this and working on this project and this deal, that they consult with this committee. And I talked to Bob Poe [executive director of AIDEA]. I talked to Dan Fauske [chief executive officer (CEO) and executive director of AHFC]. We're all willing to provide whatever help the railroad needs. And so I made that suggestion to the railroad board last week.

Number 1781

VICE CHAIR FATE called upon Senator Torgerson, noting that he is the chair of both the Senate Resources Standing Committee and the Joint Committee on Natural Gas Pipelines.

Number 1810

SENATOR JOHN TORGERSON, Alaska State Legislature, came forward to testify. He told members:

I just mainly wanted to inform the committee that a lot of what you just heard about hiring outside counsel to look at this is something that we've already done. Legislative Council authorized a goodly sum of money to do this. I went out with an RFP [request for proposals], as the chairman of the joint committee on pipelines, and we selected a Washington, D.C., firm ... named Hogan & Hartson, the largest law

firm in Washington, a very reputable firm. They are going through and doing the first "due diligence" on ... whether or not the railroad actually has the authority.

It comes down to some fundamental questions, which I'll share with the committee, that I've asked them: Most generally, ... does the railroad have extraterritorial powers? Does the law that the federal government authorized, the [Alaska Railroad] Transfer Act, say that the railroad has powers to loan money anywhere in the state or in a foreign country?

I realize a lot of this would be done through ... an American firm, and Alaska-based, maybe, and what they do with their money after that is maybe no business of ours, as long as it has something to do with the pipeline. So ... it will, in fact, be building something in a foreign country, but it may be under the obligation of ... another entity. ...

The question really is, ... in the transfer Act - which was really clear on the property that was owned by the Alaska Railroad, and which was decided with legal descriptions and so forth, this was just ... one little paragraph in that transfer Act - did it mean that the railroad could do anything it wanted to outside of that area?

Number 1916

SENATOR TORGERSON highlighted five questions he'd asked [Hogan & Hartson] to respond to initially. First, can the Alaska Railroad provide tax-exempt financing for that portion of a pipeline within Alaska? Second, can it provide such financing for a portion of a pipeline outside of Alaska - in Canada, other states, the Far East, or Mexico? He noted that any incentive might "tip a few more projects over the edge as far as being economical."

SENATOR TORGERSON continued with the five questions. Third, could it provide such financing for that portion of a project that isn't a part of the pipeline, such as extraction plants in Alaska, Canada, or the Lower 48; "liquefaction" plants in Alaska; or "regassification" plants in the Far East or Mexico? Fourth, can it provide financing for more than one project? He mentioned the need for suggestions on how to do that.

Number 1979

SENATOR TORGERSON noted that the fifth question, one of the larger ones, is whether a letter ruling from the Internal Revenue Service (IRS) is needed. He added, "Once we get those done, then it'll be our job, and this committee's job, to look at the impacts this will have on our corporate tax structure, if any, the ad valorem taxes of our municipality - our 20 mills, which we share with local governments." He told members:

I want this to work, but this is a big question. This is a lot of money. And we need to make sure ... that we have all the information that we can. So I expect an initial ruling back from this law firm in about three weeks, which I'll be glad to share [with] the committee. And I'll make our consultant available to the committee. And I have no idea what you're going to do with the bill, but if anywhere we need to do it, I'll be glad to make ... this person available, plus we'll be having hearings through the Joint Committee on Natural Gas Pipelines.

Number 2054

VICE CHAIR FATE expressed hope that some of those questions will be answered by the time HB 423 gets to [the Senate Resources Standing Committee]. He thanked Senator Torgerson, noting that those questions were ones the committee had been going to ask.

Number 2088

PATRICK GAMBLE, President and CEO, Alaska Railroad Corporation (ARRC), Department of Community & Economic Development, testified via teleconference, noting that with him was Bill O'Leary, chief financial officer for ARRC. He told members:

At this early stage in the process, while everybody's getting the legal issues sorted out, the railroad and the executive staff for the railroad are ... intentionally maintaining a pretty low profile with regard to taking steps to move forward at the present time, steps that would include hiring advisors or structuring the organization in some way other than its current structure, in anticipation of this project.

And we do that deliberately because while there have been ... some great suggestions that have been made, such as Neil Slotnick's suggestion to have a committee with AIDEA and AHFC and [Mr. Slotnick] and his folks, together with the railroad, these are all probably good ways that we could evaluate to move forward when the time comes.

The bottom line is that the railroad really can't take any official steps until its board of directors authorizes us to sell the bonds. And that step, of course, has not been taken, and it's going to be awhile, probably, before it is taken, because the board is in the process of getting better educated on this whole issue itself.

At our last board meeting, as [Mr. Slotnick] mentioned, we had AHFC sort of gives us a "Bonds 101," a peak under the tent at what the corporation is in for, should ... the decision be made to move forward on this. And the board is in the business of preparing to authorize us to take the first steps. Their presentation was very helpful in ... helping us to determine what kind of organizational impact this overall project would have on the railroad.

Number 2198

MR. GAMBELL continued:

The railroad's position is, we've also got a railroad to run and ... run it safely, and that's first and foremost our consideration. And this would be a large addition to what we are currently very busy doing. So there are some significant impacts that would accrue to the railroad, and we're quietly doing our homework with regard to those kinds of things. But, formally, we are not out hiring anyone at the present time. We're sort of keeping our powder dry but getting a lot smarter, so that when the time comes, we can move forward in concert with those others that ... will support us and move with us and give us assistance.

And as you well know - and I've said this a couple of times before - the railroad has been instrumental in some of the key development moves in the state in the past, and this is simply a continuation ... of that

history, to be able to ... possibly do this again in the future in a very big way. And so we stand ready, willing, and able to step up to the plate ... and do that when the time comes.

Number 2284

VICE CHAIR FATE referred to Mr. Gamble's mention of the responsibility of the railroad and to previous mention by Senator Torgerson of multiple projects. He asked whether a bonding capacity of \$17 billion, if entirely utilized, would interfere with the operation of the railroad, and whether [ARRC] would be able to bond any other projects.

MR. GAMBLE said that is a legitimate question that needs to be developed more fully. He added:

I can tell you that there would be a considerable amount of additional business in actually moving the pipe, ... just plain railroad business. The capacity of the railroad to move those very heavy, long lengths of pipe, and the additional structure that it would take in terms of cars, so as not to compete with the current business that we ... have, including our passenger service in the summertime - you know, we don't want to kick them off the line - we would see the possibility ... of some improvements - in terms of our capacity to be able to handle all the additional work at the same time - as possibly being a precursor to ... actually moving the pipe.

And in that sense, there may be some project-kinds of improvements, to say the parts of the rail line that haven't been rebuilt as we've been rebuilding our infrastructure, maybe improvements to some of our bridges. As you know, those ... can be weak points when you're hauling very heavy items. And, of course, the maintenance of our line is directly proportional to the weight and frequency of heavy trains crossing that line, which would be significantly increased.

So ... the original idea of the bonds, when this was put into the transfer Act, was for railroad development. And we certainly would have to take a close look at what further development ... the railroad might need ... in order to make sure its infrastructure can provide the robustness that's

required for the safety and capacity that's going to be called for in this very large project.

Number 2438

DANIEL R. FAUSKE, CEO/Executive Director, Alaska Housing Finance Corporation, Department of Revenue, came forward accompanied by Joe Dubler. He noted that on teleconference should be Eric Wohlforth; Steven Kantor [President, Arimax Financial Advisors], financial advisor to the corporation; and John Wagner [Senior Partner, Kutak Rock], special tax counsel. He said these were the same individuals present before the railroad board a week ago, as Mr. Slotnick had referenced. He suggested that Mr. Wagner, in particular, could address questions posed by Senator Torgerson in regard to the ability to build pipelines in Alaska as well as Canada.

MR. FAUSKE brought attention to a handout in committee packets titled "Presentation to the House Special Committee on Oil and Gas by Alaska Housing Finance Corporation," dated March 25, 2002. He explained that as requested by the committee, it was the same packet [AHFC] had produced for the railroad except for the title page.

MR. FAUSKE referred to the page labeled "AHFC Team Participants." Besides people present and on teleconference, he noted, the team included others [Judith DeSpain, Deputy Executive Director, AHFC; Michael Buller, Chief Administrative Officer, AHFC; and Ken Vassar, Senior Partner, Wohlforth, Vassar, Johnson & Brecht].

MR. FAUSKE referred to the next page, "AHFC Team." He indicated AHFC averages \$500 million to \$900 million a year in various types of bond transactions. He said the assembled team had been together for some time, and "assists us in performing all this activity." [The Management and Finance team list included the AHFC executive staff, the AHFC finance department, and Arimax Financial Advisors. The Legal Team included Wohlforth, Vassar, Johnson & Brecht, "Leading Bond Counsel in Alaska"; Kutak Rock, "One of the nation's leading municipal bond tax firms"; and Hawkins Delafield & Wood, "The nation's largest law firm devoted exclusively to municipal bonds."]

Number 2545

MR. FAUSKE brought attention to the next page of the handout, "\$13.153 Billion in Bonds Issued by AHFC," noting that it

provides a brief history and details the amount of bond work it has done. He said [for tax-exempt bonds] there were 101 negotiated transactions and 25 competitive transactions, for a total of \$9.017 billion; there also were about \$4.136 billion in taxable bonds [from 70 negotiated transaction]. In addition, AHFC is involved in short-term debt issuance of "Euro commercial paper," although he said, "We no longer have the Euro commercial paper program; we brought all that onshore [in] ... '99." In addition, he noted, are [repurchase] agreements in varying amounts.

MR. FAUSKE turned attention to the next page, "Non-Housing Bonds Issued by AHFC." He noted that so-called tobacco settlement bonds were \$116 million in 2000 and \$126 million in 2001; university [dormitory] bonds were \$33 million [in 1997]; state capital project bonds under SB 360 totaled about \$300 million [\$196 million in 1999 and \$74 million in 2001]; and the Robert B. Atwood Building bought in downtown Anchorage [required bonds of \$40 million in 1999].

Number 2606

MR. FAUSKE discussed the next page, labeled "AHFC has issued more bonds than any other issuer in Alaska"; he pointed out that its graph relates to Mr. Slotnick's testimony and various issuers of bonds in Alaska. It shows that AHFC is certainly a key player [at 31.6 percent of tax-exempt debt in Alaska from 1992 to 2002], as are other entities. He noted the activity across Alaska by not only state institutions, but also by municipal governments, boroughs, the Alaska Student Loan Corporation, and others.

Number 2626

MR. FAUSKE referred to the cap mentioned by Mr. Slotnick that is imposed on tax-exempt bond financing; he informed members that the cap now has been raised to \$220 million. All those entities doing private-activity bonds compete against it. As for the issue addressed in HB 423, he said:

The beauty of this transaction is that it is not under that cap. So that would be a significant advantage, because for a deal of this size - I believe the bill states \$17 billion - that would tie up that private-activity bond cap for "pretty much ever." There would be no ability to do that project in an effective manner and also allow [AHFC], AIDEA, [Alaska] Student

Loan [Corporation], North Slope Borough, Kenai Borough, [or] any of the other entities that need to apply for pieces of that cap for their tax-exempt authorization.

So the ability for this bond transaction to be outside that is absolutely key to its success and its ability to function without undue harm being created to the other issuing entities across the state of Alaska.

Number 2675

MR. FAUSKE brought attention to the next page of the handout, "The Bond Issuance Process." Selection of the appropriate [professionals] is key to that process, he said, whether financial, tax, legal, or financing-specific experts. He again noted that Mr. Kantor, AHFC's financial advisor, was on teleconference to answer questions.

MR. FAUSKE recalled that WEFA [Wharton Economic Forecasting Associates, now combined into DRI-WEFA] had been brought on to analyze the legitimacy of the figures produced by the tobacco industry in relation to what the settlement payments to all the states would be. He indicated WEFA was an outside quantitative analyst that gave support to the states and eventually to AHFC in creation of the Northern Tobacco Securitization Corporation to issue the bonds, so that there would be verifiable data to take to the investors - in the process of putting a bond package together, to provide an indication of the payment schedules and of the validity and security for those payments - prior to purchase of the bonds.

MR. FAUSKE suggested this present case would be no different: experts would analyze the validity of the project and the financing structure, to offer additional security and comfort levels for those getting involved in the transaction. Certainly, he said, there would be special tax counsel; he again noted that on teleconference was a person whose services [AHFC] has used many times, Mr. Wagner of Kutak Rock, a well-known firm that does tax counsel work for Exxon[Mobil Corporation]. There also would be bond counsel, he said, which the firm of Wohlforth, Vassar, Johnson & Brecht provides for the corporation and other entities around the state. Furthermore, there would be disclosure counsel, engineering specialists, investment advisors, and other specialty consultants, to name a few.

Number 2850

MR. FAUSKE advised members that in developing an optimal financing structure, coordination with the users of the project is essential. As pointed out earlier, this is conduit financing; the absolute credit and ability to pay is "structured within the firms of the industry," and in this case, Exxon[Mobil], BP, and Phillips are the three primary players.

MR. FAUSKE recounted that while he was with the North Slope Borough, "we would issue bonds on behalf of the North Slope Borough." Although those were general obligation (GO) bonds, he also was involved in conduit financing to develop a solid-waste treatment facility. When he met with rating agencies and investment [firms], one of the first things he'd ask was what the underlying credit of BP and ARCO were; in those days, the North Slope Borough's tax structure was such that 94-95 percent of its tax revenue came from two or three major [oil] firms.

MR. FAUSKE said the first question to ask, therefore, is what the underlying credit is; in the instance of ARRC's issuing of the bonds on behalf of the producers, as contemplated in HB 423, the credit of the producers is what is [important]. He remarked that the three major oil companies are "large players" on an international scale.

Number 2898

JOE DUBLER, Finance Director, Alaska Housing Finance Corporation, Department of Revenue, addressed an earlier question about ARRC's issuing bonds for its own purposes. He explained that because the \$17 billion - or whatever the number ends up being - in bonds won't use the railroad's credit but will look to the oil companies for their credit ratings, the oil companies' ability to access the bond market shouldn't be affected at all.

Number 2920

MR. FAUSKE mentioned the type of structure and the numerous options, noting that Mr. Slotnick's model, to his belief, has a four-year construction schedule. He emphasized the need to have the oil companies involved because there would be interim short-term financing, in many cases, for construction costs. That could be accomplished in a number of ways. For instance, an "equity infusion" could be put in place by the industry; he noted that Mr. Slotnick's model uses 30 percent equity.

MR. FAUSKE said the individual financial structures of the issuing entities would need to be looked at regarding how they want to see the short-term financing. They might opt to have ARRC issue bond anticipation notes (BANs), which are short-term, low-interest-bearing credit used for interim financing, "which are then taken out longer term by bonds." Or some entity fairly heavy in cash might decide to use cash financing for its piece.

TAPE 02-18, SIDE B  
Number 2985

MR. FAUSKE explained that even though it's a big project, it will use the same financial strategy used in smaller deals. It relates to how firms and issuers maximize their abilities to enter the bond market in the most efficient manner so that the best cost savings are generated. Carefully matching construction financing with long-term financing ends up being critical to the overall success of the project. If one reason to go to the tax-exempt market is because of savings, it is critical to have a well-planned financing timetable so that money is available when needed to supply that efficiency.

Number 2937

VICE CHAIR FATE asked what the timeframe is to put the package together.

MR. FAUSKE answered that there are some legal parameters regarding authorization as to when to actually issue the bonds. Consulting with Mr. Dubler, he said it is 60 or 90 days, to his belief, regarding disclosure items and presentation of the official statements. "To put together documents, we generally allow 45 to 60 days," he added. He said the ability to get into the market is actually a fairly quick process if all members of the team are in place and know their roles; it could be a matter of weeks or months, "maybe a couple of months at the outset," to do the first phase. He remarked:

I would never advocate - and I don't think anyone here would - that you'd be out on the street selling \$17 billion worth of bonds at one sale. It'd be just too big. One thing, it would just inundate ... the U.S. market of tax-exempt [financing]; ... it'd be hard to ... disburse that number of bonds in an effective manner. And, also, it probably wouldn't match the construction cycle. You wouldn't need all that money upfront. So you'd want to stage yourself going out so

that you'd maximize the economies of scale when selling those [bonds].

Number 2857

VICE CHAIR FATE added that one must stay ahead of "the power curve in the permitting and the licensing procedures that are going to take place, which take a much longer period of time."

MR. FAUSKE agreed. He then addressed local support. Regarding selling bonds to build a trans-Alaska natural gas pipeline, he said it isn't something he would anticipate a great deal of "disharmony" about, although there could be some. He offered his perception, from what is in the papers and "on the street" that it would be viewed quite positively by the public. However, information to the public may be limited because the petroleum companies won't be required legally to reveal construction and drilling schedules, for example.

Number 2770

MR. FAUSKE turned attention to rating agencies. Long before issuing the first bonds, he said, "you" are going to be meeting with the three major rating analysts - Moody's, Standard & Poor's, and Fitch - to outline the proposals; discuss the bonds; and discuss the structure, even prior to the selection of underwriting firms. Prior to issuance, then, there will be a rating, by the rating agencies, on those bonds. That is critical because it establishes the level of risk, which [determines] the amount of interest paid on those coupons or bonds being issued.

Number 2725

JOHN WAGNER, Senior Partner, Kutak Rock LLP, testified via teleconference, noting that his law firm is special tax counsel to AHFC. In response to Vice Chair Fate's question about the timetable for getting into the market, he said the tax laws have restrictions regarding how quickly one must start using bond proceeds. He explained:

One of the rules is that you have to expect to use ... 85 percent of the proceeds within three years. Obviously, this is a very long-term project, so these bonds will have to be issued in trenches, based upon the engineers' expectations of the use of money. Our firm happened to be underwriters' counsel on the

Valdez financings many years ago, ... [which] occurred over a period of time for that very reason.

Number 2684

REPRESENTATIVE KOHRING thanked Mr. Fauske and Mr. Dubler for their work and for the staff's outstanding job over the years. He commended them for doing such an exemplary job at AHFC. He suggested the need to support elements of government that do a good job; he said AHFC certainly is one of those, being one that actually makes money for the State of Alaska, although the legislature has seen fit to take some of that money as a "reward" for doing a good job. He recommended that AHFC continue, along with ARRC, to advise the legislature regarding this bond-issuance process.

Number 2620

MR. FAUSKE addressed marketing of the bonds, which he said is critical. Selling a bond is selling a product, he explained. A deal of this size will involve a great many "large, institutional investors" such as insurance companies or pension trust funds. In addition, AHFC's schedules include a process it has initiated - going out to retail investors. "In other words, we have a special timeframe that we offer up, on our bond transactions, where Alaskans get a priority scheduling at a time where they buy bonds," he said, noting that on "the tobacco deal," 50 percent of the \$126 million was done under retail transactions. He added:

We've found it to be a good piece of business. [It] ... gives Alaskans an opportunity to ... be in that marketplace. And something with a credit rating that I would assume this is going to have is generally a pretty good investment. And it's back to that public support issue, as well as to give Alaskans an opportunity to make sure that they're purchasers.

Number 2547

MR. FAUSKE explained that the process doesn't end the day the last bond is sold. He said:

You've got disclosure and continuing disclosure on those bonds for years to come, absolutely out through the life of the bonds. And without knowing the structure of this - whether they're 10-year or 15- or

20-year bonds - you're certainly going to be in the marketplace, because you're going to be doing refinancings or refundings of bonds, potentially, depending on what interest rate markets do.

But also, ... any disclosure issues or any ... questions involving the bonds would come back to the issuing entity and its ... experts that it has on staff for disclosure items, to answer those questions to the purchasers of the bonds.

Number 2512

MR. FAUSKE asked Mr. Wagner to respond to Senator Torgerson's testimony about "the ability of financing outside the borders of Alaska."

MR. WAGNER responded:

Senator, I know it's one of the questions you asked of Hogan & Hartson, so I don't mean to, in any way, interfere in what they're going to look at for you. But there is ample evidence, in at least the Lower 48, of states or their local municipalities issuing bonds and using the proceeds to finance facilities that are located outside the state and, in some cases, even outside the territory of the United States, that is, in foreign countries, particularly in Canada, where this is done a lot by publicly owned utilities, not investor-owned, but ... actually political subdivisions themselves, and they finance portions of hydroelectric lines and ... such from Canada.

So, for what it's worth, there is ... ample precedent in the ... other states for the use of bonds to finance facilities that are located outside the territory of the state where the issuer is located.

Number 2441

VICE CHAIR FATE asked whether there is a general legal precedent.

MR. WAGNER answered:

I can think of two things offhand. One is, there's an actual case from, I believe, ... the supreme court of

the State of Michigan, where a county in Michigan issued tax-backed bonds and built a retirement facility in Florida. And they gave a preference to Michigan residents. But the supreme court in Michigan said that it was OK for a county in Michigan to build and own and operate a retirement home in Florida. ...

The others really involve utilities. Like I said, they're not privately owned utilities, but public utilities, which there are a lot of ... in the Midwest and the Seattle-Northwest area. And they routinely ... have issued bonds ... and used the bond proceeds to finance their participation interest in, particularly, transmission of electricity. And it's also in the case of natural gas pipelines. But those are not done pursuant to treaties; those are just done pursuant to their general authority.

Number 2364

VICE CHAIR FATE asked whether the natural gas pipelines are private pipelines.

MR. WAGNER replied that the pipelines are, in most cases, owned by a partnership. Or if they're owned by a private company, then the utility is actually financed in a "participation or a partial ownership in that pipeline."

VICE CHAIR FATE indicated he wanted to establish that it doesn't involve a public utility like the power lines do. "In other words, there's two separate things that you're dealing with there," he added.

MR. WAGNER said that's right.

Number 2317

MR. DUBLER referred back to Vice Chair Fate's question regarding scheduling. He clarified that there is no legal requirement to go to market within a certain number of days. He said what Mr. Fauske had referred to, however, was that there appear to be significant legal questions about what authorization the Alaska Railroad really has under the section Mr. Slotnick referred to earlier, and whether that sweeping language would authorize a pipeline or a project of this magnitude.

MR. DUBLER said "there's a pretty good feeling from ... everybody" that a \$100 million [issuance] would not be a problem; however, a \$17 billion tax-exempt issuance will draw attention at the federal level. He said the legal issue Mr. Fauske was referring to, to his belief, was that ARRC should ensure, before going any further towards financing this project, that all its legal opinions from tax counsel are "in line." He offered the good news that it won't take as long as it will take the engineers to come up with a way to build the pipe. He added that the financing will not hold this project up.

Number 2249

MR. FAUSKE offered his position on HB 423:

I speak out in support of the bill and the concept of the bill in getting all the pieces put in place. The main question that seems to be being asked is, "Well, what's the IRS going to do?" Well, nobody knows what the IRS is going to do. I've looked at this; I've listened to others that [have] more expertise in areas of law.

MR. FAUSKE said it seems the transfer Act is fairly simple but gives a lot of authority. He suggested the IRS will analyze it "from a variety of positions." He remarked that Congress appears to be coming out in support, as is the President. He mentioned "issues of national energy policy, coupled with issues of national security" and said:

So I think it's not a matter of simply the IRS, in my opinion, just saying, "Well, no, we can't do this because of ... the effect that it has on the tax-exempt bond market." My response to that was, "Well, how much money does it cost to send the Seventh Fleet someplace to go deal ....?" So when we're talking about the ability of Americans to issue tax-exempt bonds to fund projects, I think it has to be coupled with this area of national interest.

I think it's also imperative that we, as a state, put ourselves in a position to do something. Every year, AHFC comes before you and we get authorization to issue bonds going out into the future. Whether we issue them or not, we come to you and explain to you what the issues are, what the market's looking like, what the needs of Alaskans are, and we ask you to

please give us authorization up to the hundreds of millions of dollars, so that when it's time to go to market, we have the ability to do that.

I view this no differently. It's a ... large number, but there's a great step that the legislature can take in putting Alaska in a position to do something - because once this thing starts to go, I think it's going to be imperative, too, that the U.S. Congress understand that the state is supporting this and in ... position.

MR. FAUSKE reiterated that things can happen quickly. There is a need to be in a position to act, especially if trying to capture market conditions on a particular day. Acknowledging possible amendments, he concluded, "I think the basic principle is absolutely sound. And from a financing perspective, this is absolutely doable, and it'd be a wonderful thing to get involved in ... and watch the state go forward with this."

Number 2095

REPRESENTATIVE GUESS agreed, but noted that page 3, lines 22-28, specifies a route in the bonding [section], which seems counterintuitive to the legislation's whole purpose. She asked, "If we're going to let the market drive how we should build the pipeline - and, you said, things can change and move, and we should be able to capture market conditions - why, in financing, would we specify a route?"

MR. FAUSKE answered that he'd assume something in the language must say where the pipeline will be. He deferred, however, to Mr. Slotnick or someone else from the administration to deal with the specifics.

VICE CHAIR FATE expressed appreciation to Mr. Fauske for what the AHFC has done. He announced that he planned to move the bill that day. He agreed it is not only another tool, but also an indication that the State of Alaska wants to move forward with a gas pipeline project. He remarked that Representative Guess's point is a good one that might generate an amendment.

Number 1977

REPRESENTATIVE KOHRING clarified that although he appreciates the great work AHFC is doing, he isn't necessarily supporting the legislation.

Number 1941

MICHAEL J. HURLEY, Senior Commercialization Specialist, ANS Gas Commercialization, Phillips Alaska, Inc., came forward in support of HB 423. He offered the company's initial view that the ability to use conduit financing has the potential to benefit a natural gas pipeline. He cautioned, however, that additional clarity in several areas will be needed. "We are continuing with our own due diligence, in efforts to evaluate the impacts of the proposal more fully," he told members. "In the meantime, we support the passage of the legislation, which would provide the authorization necessary, should this become a viable alternative."

Number 1873

MR. HURLEY, in response to Representative Chenault's request that he elaborate on concerns, said a lot of the concerns had been brought up in earlier testimony; there are still outstanding questions about extraterritoriality and many other issues. He pointed out that many issues about the financing itself will need to be answered closer to when the actual financing occurs; many will be reactions to the bond market, he indicated, and will relate to how comfortable the people are who will be buying the bonds. He added:

As you know, we've been working over the last year, year and a half, now, but our focus has been very much on trying to create an economically viable project. We've looked - very cursory level - at financing. As Mr. Slotnick pointed out earlier, there are lots of different options available to companies of our size and breadth. How we're going to structure the financing on this is ... still very much up in the air, from a company standpoint.

We believe this [bill] is helpful. We believe that it has the potential to be of benefit. But right now, we're concentrating on trying to get a project that is actually economically viable, because we may have bonding authority, but if we don't have a viable project, it won't do us much good.

Number 1745

PAUL FUHS, Lobbyist for Yukon Pacific Corporation (YPC), came forward to express support for HB 423 and request an amendment. He called attention to [page 3] lines 23-28, referenced earlier by Representative Guess, which says in part that [the proceeds of the bonds] shall only be used for a pipeline that "approximately follows the right of way of the Trans Alaska Pipeline System from Pump Station 1 on the North Slope to Delta Junction, and the Alaska Highway from Delta Junction to the Alaska/Yukon Territory border." He explained, "Once again, without any apparent justification, we're seeing legislation which limits Alaska's options for the way that it might develop its natural gas."

MR. FUHS provided a partially handwritten amendment containing three options, which read [original punctuation provided]:

1. Page 3 Line 23 to 28 Delete entire sentence starting with "the proceeds of the bonds etc.
2. OR: Line 25 that include "but are not limited to" a pipeline
3. OR Line 28 add "or a route to tidewater in Southcentral Alaska or for a spurline to Southcentral Alaska or other parts of Alaska".

Number 1633

MR. FUHS pointed out that without an amendment, there will be no opportunity to consider the developments which Senator Torgerson spoke of; to use this financing for a stand-alone "to tidewater" project in Alaska; to use it for a "Y" line, as has been discussed; or to use it for a spur line to Southcentral Alaska if, indeed, a trans-Canada pipeline is ever built. Regardless of any option's merits, he said, nobody has yet presented anything that says it is a "slam-dunk" to go one way or another.

MR. FUHS reminded members that two weeks ago, YPC presented information on a smaller project that YPC believes is economic. "Since that time," he reported, "we have not received any information from anyone saying that these numbers are wrong. We haven't seen anything on the trans-Canada pipeline, although I guess we're supposed to get that by March 31, was ... the latest information."

MR. FUHS returned attention specifically to HB 423 and said:

If you do amend it, then it would bring it in line more with the resolution which was passed two weeks ago out of this committee, where you said, "We also want to include the potential of LNG [liquefied natural gas] to the U.S. as one of the potential markets."

It would also bring it in line with [U.S.] Senator Murkowski's amendment that he got to the federal legislation, also saying that an Alaska project - an LNG project - would not be precluded by that legislation.

Number 1594

MR. FUHS discussed the three options in his proposed amendment [text provided previously]. He explained that the problem with the first approach, deleting the last sentence, is that the financing could be used for an "over-the-top" pipeline. The second option might do the same. The third option is more specific, perhaps addressing the concern voiced by Mr. Fauske that it should state what the financing is being used for.

Number 1550

REPRESENTATIVE JOULE pointed out that the third option says "or", whereas everything he has heard before has been "and/or". He added that the desire is to not "put ourselves in a straightjacket."

MR. FUHS said that would be fine, and that ["and/or"] is the intention.

Number 1515

REPRESENTATIVE GUESS inquired about the wording "or a route to tidewater or a route to Southcentral Alaska". She voiced concern about specifying it because certain people want certain routes. She asked, for a route to tidewater in Southcentral Alaska, whether [this third option] would prohibit it.

MR. FUHS answered that "tidewater" would mean Kenai or Valdez, so it is generic.

[Several members concurred that "tidewater" is generic.]

Number 1456

DAVE MacDOWELL, External Affairs Manager for Gas Activities in Alaska, BP, testified via teleconference. He told members:

We're supportive of this bill because there is a possibility that it could reduce financing costs for a gas pipeline, but even more generally because it's indicative of the creative thinking that must be done to help move a project forward.

An Alaska gas pipeline project is an immense challenge, as you all know - very expensive, very complex, very risky, and as of yet not commercially viable. We're encouraged, therefore, by all efforts to seek ways of addressing these challenges.

The proposal to use the Alaska Railroad Corporation as a vehicle to finance the pipeline with tax-exempt bonds is certainly a creative approach that, if possible, could help move towards lowering project costs. Now, given the creative nature of this approach, more work and assurance will likely be needed before bond investors would have sufficient confidence to invest in such bonds. However, if this confidence were achieved, lower financing costs could translate into lower pipeline tariffs. Lower tariffs, in turn, lead to higher netback prices and thus improved economics and more revenue for the state.

A cost-competitive transportation system, along with an efficient federal regulatory framework and a clear, predictable fiscal regime, are all necessary requirements for the creation of a commercially viable project.

BP Alaska is intrigued by the concepts outlined in this bill and is currently evaluating the potential benefits it may bring to a project. Meanwhile, we would ask this committee to support passage of this legislation.

Number 1306

PAM LaBOLLE, President, Alaska State Chamber of Commerce, came forward to testify in support of HB 423, which she characterized as another tool regarding possible opportunities for a gas pipeline. She added, "We're very encouraged that there is a lot

of thinking along this line, and we are in support of the legislation."

Number 1241

MR. SLOTNICK came forward again to respond to Representative Guess's question regarding why a route is specified in Section 5. He said:

To answer that question, I'd like to just draw your attention to the fact that Section 5 is part of the uncodified law. It's the actual authorization for the railroad to sell bonds. The codified law, the change that we gave in statute to the authority of the railroad, doesn't in any way constrain the discretion as to where the route would be - you know, what types of projects the railroad could sell bonds for.

But when you're taking the actual authorization to go to market, we considered this language and thought that it was perhaps more appropriate to constrain the railroad's discretion here to the project that ... at this time is under discussion with the producers. It's the project that we have modeled in-house; that's where we were able to come up with the numbers. We've run the numbers. We know what the financing looks like. We know what project we're specifying here. So, when we thought we'd come to the Alaska legislature for a part of the uncodified law specifying that you can go out and sell bonds, we thought it'd be better to say what project you can sell bonds for.

And we could ... ask Mr. Wohlforth - I believe this language came from ... his firm - whether he believes an open-ended authorization to sell bonds would have any repercussions with the market. I don't think it would, but I'd like to get his opinion on that, if that's what this committee's pleasure is.

But generally, when you're giving an authorization like that, you're going to do it for a project that you've been in discussions [about], that's been modeled, that's identified. And I would say that this authorization could be supplemented when someone else brings a project that meets those kind of criteria to you; it could be withdrawn if this project isn't the

project that goes forward. But the reason we wrote it this way is because this was the project we were considering.

VICE CHAIR FATE requested that Mr. Wohlforth respond.

Number 1068

ERIC WOHLFORTH, Attorney at Law, Wohlforth, Vassar, Johnson & Brecht, APC, testified via teleconference, saying, "There is no legal reason why the definition could not be expanded, if it was the committee's desire to do so."

Number 1053

VICE CHAIR FATE said this describes a "bullet" pipeline, which isn't the intent. He agreed with concerns expressed that if the language were adhered to, it may be not even allow a lateral [spur] or a valve or anything else. He said he was glad to hear Mr. Wohlforth's testimony that legally he could see no problem with a conceptual amendment to allow for other things to be built, whether a lateral line, a pipeline elsewhere, or a valve somewhere on the Yukon River, for example.

Number 0976

REPRESENTATIVE KOHRING requested elaboration regarding why the ARRC, if it is putting forth this bond issue, isn't incurring the risk, which is being incurred instead by the major companies.

MR. SLOTNICK answered:

The reason is that, by contract, the railroad will not assume any risk. And the bondholders are all made aware of that before the bonds are sold. It is stated in several places in what's called an official statement, which is the offering that goes out to the investors, to the bond holders, and becomes part of the contract with ... the investors. It will be stated in capital letters that there is no recourse to the railroad, to the State of Alaska, or to either or both of them as far as if there should be any default on the bond. The only place they can turn to would be the credit of the project or the credit of the corporations, depending on how this is structured.

Number 0864

REPRESENTATIVE KOHRING referred to the use of the proceeds of the bond sales and said he knows the intent is to make them available to the private sector, to use that money to finance the construction of a line. He asked whether those monies also could be used by the State of Alaska to build that line.

MR. SLOTNICK answered yes.

REPRESENTATIVE KOHRING remarked that one of his concerns is that if the bill passes without stricter parameters that would preclude the state from using those monies, "that might be the means with which the state could actually engage in a big capital project sponsored and funded and constructed by the government, which is something I philosophically disagree with, because it would be along the lines of the Seward grain terminal, the Delta barley project, things of that nature that have proven to be boondoggles." He said he might offer an amendment at some point that would add language to prohibit the state from using those proceeds.

Number 0757

VICE CHAIR FATE asked whether there were further questions of the testifiers, and then thanked Mr. Slotnick and Mr. Wohlforth. He asked whether there was further testimony; there was no response. He closed public testimony and returned attention to possible amendments.

Number 0711

REPRESENTATIVE JOULE reiterated the desire, other than what was written in Mr. Fuhs's proposed amendments, to say "and/or" and then address the issue of the route to tidewater or Southcentral Alaska or other parts of Alaska.

Number 0677

VICE CHAIR FATE suggested a conceptual amendment, on page 3, line 25, after "pipeline", to have it say "that is not limited to but approximately follows". The addition would be the phrase "that is not limited to [but]".

REPRESENTATIVE GUESS noted that it would be the second option in the proposed amendments provided by Mr. Fuhs. She acknowledged the desire to have flexibility, but said she believes this

legislature has made it clear that the flexibility wouldn't include "going north" [for an "over-the-top" pipeline route].

VICE CHAIR FATE remarked that there has been not only state legislation passed which prohibits that route, but also federal legislation; therefore, language already prohibits that northern route. That was his thinking in providing the conceptual language that didn't deal with the northern route, he explained.

Number 0523

REPRESENTATIVE JOULE remarked, "So long as that's covered." He pointed out, however, that the federal legislation is pending. He asked whether, for that reason, the amendment shouldn't be more specific.

Number 0464

VICE CHAIR FATE called an at-ease at 10:37 a.m. [End of Tape 02-18, Side B.]

TAPE 02-19, SIDE A  
Number 0001

VICE CHAIR FATE called the meeting back to order at 10:40 a.m.

Number 0026

VICE CHAIR FATE offered conceptual Amendment 1, on page 3, line 25, after the word "pipeline", to add "that is not limited to [but]". [Thus it would read, in part, "include a pipeline that is not limited to but approximately follows the right of way".] Vice Chair Fate asked whether there was any objection.

Number 0099

REPRESENTATIVE CHENAULT objected for discussion purposes, expressing concern that it still specifies a route.

VICE CHAIR FATE explained that the conceptual amendment says it isn't limited to a specified route.

REPRESENTATIVE CHENAULT withdrew his objection.

Number 0165

VICE CHAIR FATE announced that there being no further objection, conceptual Amendment 1 was adopted.

Number 0184

REPRESENTATIVE KOHRING began discussion of what he would offer as conceptual Amendment 2. He restated his concern about having the bond proceeds be used for the State of Alaska to build a pipeline on its own, rather than having private entities use those dollars to do so. He conveyed his belief that the process should be strictly market-based, and that the state shouldn't build a line just because of needing revenues from it; rather, the pipeline should be privately constructed, but only if the market demands and warrants it. He said he doesn't believe the state should be involved in the business of constructing major capital projects of this nature.

Number 0261

REPRESENTATIVE KOHRING therefore offered conceptual Amendment 2, to strike "Alaska Railroad Corporation" and substitute "State of Alaska" on page 3, line 25. He said it appears it is just excluding the Alaska Railroad Corporation, and he would like to expand that to include the State of Alaska.

Number 0316

VICE CHAIR FATE pointed out that it would change the intent because ARRC is the bonding entity. It states clearly that ARRC will not be the owner. He suggested that the conceptual amendment should retain the Alaska Railroad Corporation, therefore, with the State of Alaska as an addition.

REPRESENTATIVE KOHRING replied, "However we need to wordsmith that to accomplish my intent in the amendment, I'd be pleased to do that."

Number 0385

REPRESENTATIVE JOULE objected to conceptual Amendment 2.

REPRESENTATIVE GUESS indicated she objected as well.

REPRESENTATIVE JOULE requested that Mr. Slotnick and someone from the AHFC inform the committee about the ramifications.

Number 0416

MR. SLOTNICK suggested in order to accomplish Representative Kohring's goals, the words "Alaska Railroad Corporation" should remain, but the words "or the State of Alaska" should be added. That way, there would be ownership by entities other than the railroad or the state.

REPRESENTATIVE KOHRING thanked Mr. Slotnick for his clarification.

Number 0445

REPRESENTATIVE GUESS inquired whether that would preclude the state's being a partner in the pipeline. She added that she didn't believe so, from her reading, but just wanted to ask.

MR. SLOTNICK answered that it would require some thought. He read in part from page 3, beginning on line 24:

The proceeds of the bonds described in this section shall be used only for facilities that are owned by one or more entities other than the Alaska Railroad Corporation ...

He alluded to the fact that if conceptual Amendment 2 were adopted, it would be entities other than the state. If the state were a partner in any of those facilities, he said, it would seem to him that the proceeds of the bonds couldn't be used on those facilities. This would, therefore, remove the state from any ownership role of facilities financed by these bonds.

Number 0527

REPRESENTATIVE KOHRING said that is the intent of his amendment.

REPRESENTATIVE JOULE asked why Representative Kohring would want the state out of it, at this point.

REPRESENTATIVE KOHRING asked whether Representative Joule was referring to owning a facility to be constructed with the bond proceeds.

VICE CHAIR FATE rephrased the question, asking whether he would object to any equity interest in the pipeline, without outright ownership, which is what the proposed amendment implies.

Number 0582

REPRESENTATIVE KOHRING said no, but added that he doesn't believe the state should be constructing and in ownership of facilities, including a gas pipeline. The amendment is intended to prevent that from happening. He expanded on his answer:

I just see the state getting involved in another potential and very expensive boondoggle here, and we might feel more inclined to build this facility, whether we really need the facility or not - whether the market warrants it or not.

And if we end up spending billions of dollars to build this gas pipeline and we find out that ... the demand for our gas ... was not there, then we might look back, in hindsight, that it was a wasted investment, and it'll end up being as we've seen before with other state-funded projects like the Seward grain terminal, the Delta barley project, the agriculture operation out at Point MacKenzie in my area, and others. So, that's my concern.

Number 0682

REPRESENTATIVE GUESS explained that she objected to conceptual Amendment 2 not necessarily because of disagreement with Representative Kohring's concerns, but because she believes the question should still be on the table of whether it is in the state's best interest to have some equity interest in this pipeline, especially given the amount of revenue that can be generated from transportation "and the fact that we did not choose to do that in TAPS." Furthermore, she indicated, because of market forces she doesn't foresee the state's being able to "just go and build a pipeline on its own." She agreed with Representative Kohring's concern, but said she didn't believe this was the place to address it.

A roll call vote was taken. Representatives Kohring and Chenault voted to adopt conceptual Amendment 2. Representatives Guess, Joule, and Fate voted against it. [Representative Dyson was absent.] Therefore, conceptual Amendment 2 failed by a vote of 2-3.

Number 0823

REPRESENTATIVE GUESS moved to report HB 423, as amended, from committee with individual recommendations and the attached fiscal notes. There being no objection, CSHB 423(O&G) was moved out of the House Special Committee on Oil and Gas.

VICE CHAIR FATE thanked participants for the good discussion. He pointed out to Representative Kohring that other bills, not yet fully heard, deal with ownership of the pipeline; he suggested that discussion could be held when they are heard.

#### **ADJOURNMENT**

Number 0896

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 10:50 a.m.