

ALASKA STATE LEGISLATURE
SENATE TRANSPORTATION COMMITTEE

February 26, 2002
1:37 p.m.

MEMBERS PRESENT

Senator John Cowdery, Chair
Senator Gary Wilken
Senator Kim Elton

MEMBERS ABSENT

Senator Jerry Ward, Vice Chair
Senator Robin Taylor

COMMITTEE CALENDAR

SENATE BILL NO. 269

"An Act naming bridge number 1121, across the Knik River, the Sergeant James Bondsteel Bridge of Honor; and providing for an effective date."

MOVED SB 269 OUT OF COMMITTEE

SENATE BILL NO. 271

"An Act establishing the Alaska Marine and Rail Transportation Authority; establishing the marine and rail transportation fund; relating to ferries and ferry terminals; relating to the Alaska Railroad Corporation; and providing for an effective date."

HEARD AND HELD

SENATE JOINT RESOLUTION NO. 32

Proposing amendments to the Constitution of the State of Alaska relating to a marine and rail transportation fund.

HEARD AND HELD

PREVIOUS COMMITTEE ACTION

SB 269 - No previous action to record.

SB 271 - No previous action to record.

SJR 32 - No previous action to record.

WITNESS REGISTER

Ms. Carol Carroll
Department of Military and Veterans Affairs
PO Box 5800

Ft Richardson, AK 99505-0800

POSITION STATEMENT: Supported SB 269 and, as the representative of the Department of Natural Resources, opposed SB 271

Mr. Bill O'Leary
Vice President
Alaska Railroad Corporation
PO Box 107500
Anchorage, AK 99510-7500

POSITION STATEMENT: Opposed to SB 271

Mr. Bob Doll
Regional Director, Southeast Region
Department of Transportation &
Public Facilities
3132 Channel Dr.
Juneau, AK 99801-7898

POSITION STATEMENT: Took no position on SB 271

Captain George Capacci
General Manager, Marine Highway System
Department of Transportation &
Public Facilities
3132 Channel Dr.
Juneau, AK 99801-7898

POSITION STATEMENT: Answered questions pertaining to SB 271

Mr. Herb McDonald
Karloff Transportation
No address provided

POSITION STATEMENT: Opposed SB 271

ACTION NARRATIVE

TAPE 02-9, SIDE A

Number 001

CHAIRMAN JOHN COWDERY called the Senate Transportation Committee meeting to order at 1:37 p.m. Senators Wilken, Elton and Cowdery were present. The committee took up SB 269.

#SB 269

SB 269-NAMING BONDSTEEL BRIDGE OF HONOR

MR. LADDIE SHAW, State Director for Veterans Affairs, Department of Military and Veterans Affairs, asked members to support SB 269. The legislation honors an Alaska Medal of Honor recipient, James Bondsteel, who died on that bridge. He said that to honor a veteran in any way is appreciated, but for someone of Mr.

Bondsteel's stature, the honor is without question.

With no further questions or discussion, SENATOR WARD moved SB 269 from committee with individual recommendations.

CHAIRMAN COWDERY announced that with no opposition, SB 269 would move to its next committee of referral. He then informed members the committee would take up SB 271.

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#SB 271

SB 271-MARINE AND RAIL TRANSPORTATION AUTHORITY

SENATOR WARD, sponsor of SB 271, first asked Chairman Cowdery if the committee has received the requested warrants from the Alaska Railroad Corporation (ARRC).

CHAIRMAN COWDERY said ARRC has promised him that the warrants will be forthcoming and should be delivered in about one week.

SENATOR WARD expressed concern that the warrants are a very important part of the discussion about SB 271. He then made the following comments about SB 271.

The concept of an authority is not new, but in this time of streamlining and consolidating, an authority makes sense. SB 271 will create a transportation authority with two divisions: one for the ARRC and the other for the Alaska Marine Highway System (AMHS). When the state purchased the railroad from the federal government, part of the discussion was that the state would allow the real estate holdings to be transferred with it instead of separating them out and the land would be sold after five years. The purpose of the delayed sale was to provide time to see how the operation of the ARRC was going. That agreement has since changed and he believes for the better. He believes ARRC is a great state asset and that should be extended to Canada.

SENATOR WARD said he introduced SB 271 to provide a land base for the AMHS. Funding for the AMHS has been left to the will of a majority of legislators and the governor; the AMHS has been subject to appropriations. He noted that spoke to his constituents about the AMHS and found that funding for the AMHS will not get much support from his area because his constituents do not use it. He believes creating a transportation authority for the two entities and granting it an additional land base will be a good first step. He noted SB 271 was modeled after the Washington State authority, which has a land base. He crafted the legislation to enable the authority to grow and eventually add

dividends back to the state in the form of new transportation projects. Had a land base been given to the AMHS when the ARRC was purchased, he probably would not be introducing this bill. He feels SB 271 provides a long-term solution to funding the AMHS.

SENATOR WARD cautioned, as the Chair of the Senate Finance subcommittee on the Department of Transportation and Public Facilities, the state will be faced with choosing which types of transportation should be funded and he does not believe the AMHS and ARRC should be forced to compete against each other for general fund dollars when they can be given land bases. He estimated that Southeast Alaska contains around 500,000 acres of state land. He would favor giving the new authority all or any of that land to develop.

SENATOR WARD maintained that ARRC is working well because it has a land base but the AMHS is not. He held that both transportation entities fear this proposal because they fear losing authority over their own enterprises. He said the parties involved must set aside inherent fears over jurisdiction to come up with a workable plan. He then offered to answer questions.

1:45 p.m.

CHAIRMAN COWDERY recognized the presence of Senators Taylor and Ward. He then informed members that he did not support the purchase of the railroad years ago, and did not vote for it. He asked, for the record, how much land the AMHS owns at this time.

SENATOR WARD said it owns none.

SENATOR ELTON commented that the approach laid out in SB 271 gives the legislature an opportunity to discuss other things, such as how the AMHS is funded. He thanked Senator Ward for that opportunity. He stated that unlike a land-based highway system, 50 percent of the AMHS funds come from users. A few years ago, an idea similar to SB 271 was proposed. At that time he was told that to build a rural two-lane road in the Kenai Peninsula would cost \$1.3 million. Maintenance costs would be \$6,400 per year per mile for one lane. None of that money comes from the users, it comes from the general fund. He said the possibilities for transportation funding are intriguing. He suggested establishing a land base for the highway system and providing DOTPF with a corridor along the highway to leverage so that DOTPF could hopefully do as well on earnings as ARRC has done.

SENATOR ELTON said one of the good notions behind this approach is the acknowledgement that the state needs to invest in its

transportation systems. He said he is skeptical that an authority of this type will solve the problem as quickly as necessary. He indicated that if SB 271 passes, no benefits would be seen for five years.

SENATOR ELTON then asked several questions, the first being whether the transportation authority would fall under the Executive Budget Act or whether it would assume the position of ARRC, outside of the Executive Budget Act.

SENATOR WARD replied that it would fall under the Executive Budget Act. He maintained that Senator Elton hit on the problem, that being that the legislature and governor, if they wanted to develop some of the land along the roadway system to produce income to pay for transportation needs, could have done so but has not. A transportation authority, whose sole purpose is transportation, would develop that land before laying people off or stopping runs between towns. He said as the previous chairman of the Senate Transportation Committee, he heard from the port authority at Bellingham and others about their function and mission and land-based revenue systems. He said he agrees with Senator Elton about the cost of roads on the Kenai Peninsula but he sees this as a political problem. He noted that at a town meeting in Nikiski, and learned that if it comes down to a choice of fully funding a school in that district or funding the AMHS, the AMHS will be in trouble. He said he is trying to avoid that scenario.

SENATOR WARD said Alaska needs a statewide transportation plan of which a transportation authority would be a cornerstone. He indicated that he does not disagree with anything Senator Elton said about the AMHS, but the majority of Alaskans do not share the same view. He repeated that legislators need to take the funding argument off of the table and let a transportation authority deal with it.

SENATOR ELTON said his second question pertains to the two fiscal notes that add up to \$7 or \$8 million per year. He asked Senator Ward how much revenue from the land base is projected.

SENATOR TAYLOR referred to the second page of the ARRC fiscal note and read, "No revenue is assumed to be received from the lands to be transferred during the time of the fiscal note (FY 03-08). He said it does not shock him that the state could give to this authority 500,000 acres and the authority would not be able to make a dime off of it for five years.

SENATOR WARD added that when he spoke to people in Washington

about its authority, he could tell that every time the authority leased or sold land, it was completely focused on transportation needs. This half million acres is in existence today but is not helping the transportation needs of Alaska. He believes an authority will figure out a way to develop it. Otherwise, Alaska will run into very large transportation problems.

SENATOR ELTON asserted that one of the charges for 20 senators is to have a statewide outlook because most citizens would rather fund their local school than a transportation project in another region. He said that requesting funds for the AMHS from the legislature is no different than requesting funds for the rest of the highway system, the exception being that users pay 50 percent of the cost of the AMHS while the users of the highway system pay nothing.

CHAIRMAN COWDERY maintained that the trucking industry pays a fair share through fuel taxes. He then noted that Senator Elton's comparison of building costs of a two land road in Kenai with the AMHS is inaccurate because the AMHS does not have the same environmental requirements and restrictions.

SENATOR ELTON said that is true but the cost of a fast ferry would purchase a rural road system in the Kenai Peninsula. However, the road system would cost \$204,000 per year to maintain, which is much more than it will cost to maintain the ferry.

CHAIRMAN COWDERY maintained that at the last meeting, he asked DOTPF officials how many roads they had built. They had not built any so he does not know how they could be so certain of the cost.

SENATOR WARD responded:

The Marine Highway System's maintenance is absolutely being put at the back of the column. The ships and the people that work there - because they have contacted me - they feel like as if they're treated like a stepchild. All I'm trying to do is give them a land base so they don't have to be - eventually we'll end up just rusting a hole in these things and it's going to fall apart. We're talking hundreds of millions of dollars to replace it. We have to start just simple maintenance and we're talking about just enough money to keep them afloat let alone fixing it. We have to refocus this and if somebody's got a better plan than this, please bring it forward.

SENATOR ELTON agreed the AMHS has been treated like a stepchild.

SENATOR TAYLOR commented that he passed a bill that provided 250,000 acres over a 10-year period to be selected for the University of Alaska. This Administration vetoed that bill so a case is on its way to the Supreme Court. He stated he would love to see Alaska's 103 million acres of land finally provide some kind of economic base for schools and job opportunities. He questioned how Senator Ward intends to get this legislation passed if the Governor would not support a prior effort. He maintained that this Administration has not requested an increase in the AMHS budget for eight years except for a shortfall for the Kennecott. In addition, this Administration destroyed the AMHS trust fund because instead of asking for funds when they were needed, it [used the trust fund].

CHAIRMAN COWDERY then took public testimony.

MR. BILL O'LEARY, Vice President of Finance for ARRC, said he would provide a short background of ARRC and then discuss the ARRC's position on the bill in light of its history and structure.

The federally-owned railroad was transferred to the state 17 years ago, creating the Alaska Railroad Corporation. When legislators crafted the Alaska Railroad Corporation Act, they produced a well thought out document that positioned the new entity to thrive without operating subsidy from the state.

The Federal Transfer Act, an enabling state statute, provided the railroad with many tools to face the mandated challenges of being a self-sustaining economic driver for Alaska. Some of these tools included - similar to the Lower 48 railroads - significant land holdings were transferred to the corporation. The corporation was granted tax-exempt status.

The railroad was separated from the state budget and appropriation process so it could rapidly react to market demands. The corporation was also given legal tools to protect both itself and the state from liability. The railroad has used these tools to be successful in meeting its mission, a mission that requires it to act like a private business in many respects but with a responsibility to the public as it goes forward to promote economic development for the state. To accomplish this difficult mission, the railroad has required no state operating subsidy but

rather has operated profitably for the vast majority of the last 17 years. In fact we are projecting a \$4.2 million net earning figure for our fiscal 2002. Each year these earnings have been reinvested into the corporation's infrastructure in an effort to address the significant deferred maintenance problem the corporation inherited from its federal ownership days.

Let me be very clear about one thing - there are no surpluses at the Alaska Railroad. Every dollar earned is plowed back into the company and it is still not enough to meet the needs of a massive plant infrastructure that is required to run a railroad 24 hours a day, 7 days a week in the state of Alaska. Indeed the railroad's limited ability to generate sufficient internal capital funds has only recently been assisted by its eligibility for federal funding for certain of the corporation's capital needs.

So what has been the primary component of our earnings over these years? The corporation has historically relied upon its real estate activities for the majority of its earnings. For 2001, virtually all of the company's net earnings will be a result of real estate. Since transfer, real estate has played a key role for the corporation. Similar to the Lower 48 experience, Alaskan towns have grown up around the Railbelt. As these towns grew, rail land became more and more valuable. The railroad has capitalized on this phenomenon, leasing approximately 2500 acres of rail land currently and generating significant income from it.

In our opinion, this legislation would jeopardize all of this and further unravels the intent of the architects of the original Alaska Railroad Corporation Act. Although this bill proposes an innovative funding mechanism for the Marine Highway System, the Alaska Railroad Corporation cannot support SB 271. Simply put, we do not believe this bill and its companion constitutional amendment are financially workable.

As you know this bill creates an authority combining Marine Highways and the Railroad Corporation and permitting the authority to select 500,000 acres of certain state lands, presumably to be developed to provide sufficient income to bridge Marine Highways funding gap. Our initial analysis of the bill and its

financial impacts clearly indicates that it would spell disaster for the Railroad Corporation and the Alaskan companies and residents it serves.

Specific concerns we have with the bill include the following. First off, the legislation would make the Railroad Corporation's internal capital funding virtually non-existent. The bill requires all rail land not used for operations to be transferred to the authority. Without the revenue from its real estate, the deferred maintenance problem that we faced at transfer and have faced since then will manifest itself again quickly within a few years. Further, without internal funds to be used for required match money, federal funding will be jeopardized. In terms of industry standards, a railroad the size of the Alaska Railroad requires anywhere from \$15 to \$20 million per year annually to be invested into its rail line. Without real estate earnings, this will be an impossibility for the railroad.

CHAIRMAN COWDERY asked how much income is derived from the land each year and the amount of federal dollars needed for the railroad's operations per year.

MR. O'LEARY said ARRC's gross real estate income for 2001 was approximately \$10.5 million. He projected about \$60 million of federal funds for FY 2002 will be used entirely for capital projects. No federal funds are used for operating costs.

MR. LEARY then continued his overview.

The second point is this bill does not follow the successful model of the railroad. Railroad Corporation rail land is valuable due to its location and proximity to the tracks and the major cities that grew up around the tracks. Simply dedicating 500,000 acres of undeveloped land does not fit the successful model of the Railroad Corporation and its land development. There could be significant costs to bring this land to a state where it could be revenue producing. The timing of when this could occur may also be problematic.

The next point is that significant administrative and management cost increases would be a reality in our opinion. The bill appears to envision three divisions within the authority: Marine Highways, the Railroad and an authority system office. The cost of the system

office appears to be incremental cost. Along the same lines, we believe there would be very limited administrative efficiencies to be gained through consolidation - different locations, different benefit systems, different infrastructures, and different constituencies will not permit realization of such efficiencies in our opinion.

Next point is that placing the railroad under the Executive Budget Act would greatly inhibit the railroad from fulfilling its mission. The railroad's budget could become politicized under the Executive Budget Act. This, along with a loss in flexibility to react to market demands, could have a chilling effect on business confidence and the railroad's ability to deliver reliable service.

The bill, in our opinion, does not solve Marine Highway's problems. Transferring 500,000 acres of non-specific state land over a multiple year period will not address the fiscal problems faced by the Marine Highway System in our opinion. Depending on where this land is, millions of dollars may be required to transfer it and prepare it for any revenue generating use. That again may be years away.

As shown in the fiscal note submitted, we estimate the initial cost of implementing this bill at an increment of \$5.3 million for the first year from the state's general fund exclusive of what subsidy may be required by Marine Highways.

In summary, we believe this bill will not streamline government, nor reduce costs, nor wean Marine Highways off the general fund. It would rather create another layer of management, institute numerous costly administrative burdens, put a structure in place that would inhibit prompt reactivity to market changes and would have the bottom line impact of making two agencies dependent upon the state rather than one. We believe this is certainly not in the best interests of the railroad, its customers, nor the residents of the state of Alaska. The legislature, and this transportation committee in particular, is focused on economic development through enhancing and expanding the state's transportation network. We submit that this bill is not the appropriate vehicle by which to further this goal. Thank you again and for the opportunity to

testify and I stand ready to answer any questions the committee may have at this point.

SENATOR WARD said once the committee receives the warrants from ARRC, it can find out how much money there was and what it was spent on, however, a new railroad would not be able to survive without a land base. In the early 1980s, some argued that the railroad land would never be worth anything and would take forever to develop. He asked Mr. O'Leary why, if the concept of a land base works for the railroad, it would not work for the AMHS.

MR. O'LEARY said the ARRC believes that the specific model that has worked for the railroad has worked because of the specific land, which is located around the rail line. Because it is around the rail line, it became more valuable as the towns around the rail line grew. ARRC has a number of acres of land that are available for lease but cannot be leased because they are not in an area being developed.

SENATOR WARD again asked why, if the concept of a land base for a railroad is a good thing, that same concept would not be good for the AMHS.

MR. O'LEARY said, again, it depends on the land base and the costs of making that land revenue-producing. He repeated that most of the railroad's land is easily accessible and, in some ways, has grown up with the railroad.

SENATOR WARD concluded that the ARRC's problem with the bill is the possibility that the land granted to the AMHS will not be as good as the railroad's land.

MR. O'LEARY said ARRC has a number of concerns with the bill, one being ARRC's involvement in this bill at all. The choice of land transferred is also a concern.

SENATOR WARD indicated the railroad already has land that would become part of the authority so seed land is already being developed.

CHAIRMAN COWDERY asked if ARRC did site preparation when it leased its land or whether those expenses were paid by the lessees.

MR. O'LEARY said it is his understanding that the land has been developed in a combination of ways. In certain situations ARRC did the work and the cost was rolled into the lease rate, in other situations, the lessee did the work.

CHAIRMAN COWDERY said he prefers the later.

SENATOR TAYLOR asked whether ARRC has made more money from its land or the railroad operation over the last 18 years.

MR. O'LEARY replied it made more in gross income from real operations but the net income came down to real estate.

SENATOR TAYLOR said that when he looked at the balance sheet during the early years, the only thing ARRC made money on was land operations, which were subsidizing the railroad.

TAPE 02-09, SIDE B

SENATOR TAYLOR said that anytime the state considered selling the railroad, the responses it received said there isn't a railroad company in the United States wealthy enough to stand the losses long enough to buy it. He commented that he has reservations about this bill but his are centered on whether it can ever be enacted under this Legislature and Administration. He then asked Mr. O'Leary what recommendations ARRC can offer to expand the railroad south and to the McGrath area. He asked if giving ARRC alternate sections of land on either side of the right-of-way would be attractive to ARRC.

MR. O'LEARY said a strong Alaskan economy equates to profitable times for the railroad and that a lot of projects might occur that could change the face of the railroad, for example the gas line and extension to Canada. ARRC is supportive of anything that allows it to continue to be self-supporting. He offered to get back to the committee with more ideas.

SENATOR WILKEN asked if he has been invited by the Legislature to give a status report on the railroad this year.

MR. O'LEARY said he believes Mr. Gamble has given an overview to the House Finance Committee and is scheduled to give one to the Senate Finance Committee.

SENATOR WILKEN asked what percent of ARRC's net earnings are generated from its real estate holdings rather than the railroad.

MR. O'LEARY replied:

Senator Wilken, we're looking at between 10 1/2 and 11 million dollars worth of gross real estate income for 2002, with approximately between 3.5 and 4 million dollars of related expense, related to the real estate department, which is going to give us anywhere around 6 million dollars of net actually from our real estate department in 2002.

SENATOR WILKEN asked if the total earnings in 2001 were \$4.2 million.

MR. O'LEARY said ARRC is projecting \$4.2 million in 2002.

SENATOR WILKEN said:

Let me just tell you why I ask the question. My first year here we had a report to Finance and - I wasn't on Finance, I sat in - and I believe that the real estate versus the railroad operation was 90 real estate, 10 real estate. And then two years ago it was 52 percent real estate and 48 percent railroad operations. Obviously that's a big change so that's what I wondered, if you're continuing to be a real estate company or a railroad company and that's really what I wanted to know. So I'd appreciate you getting back to me sometime and let me know what those numbers - if they're correct and, if they are, where they are today.

MR. O'LEARY said for 2001 and 2002, virtually all of ARRC's net income will derive from real estate activities.

SENATOR WILKEN asked if ARRC is losing money on railroad operations but making money on real estate.

MR. O'LEARY said ARRC is in the process of taking a very hard look at its rail operations and trying to drive the operating ratio down so that the rail operation side will be more profitable. To this point, the rail operation side has been a break-even operation or has generated a small surplus. The 45 percent that Senator Wilken referred to most likely relates to 2000, when through a large federal reimbursement related to winter storms, ARRC had skewed net income figures. The average net income over those years was about \$6 million.

SENATOR WILKEN asked what the net worth of ARRC is.

MR. O'LEARY said the actual equity ARRC has is about \$140 million, which is the cumulative earnings since transfer. ARRC has \$350 million worth of assets in its financial statements at this time.

SENATOR WILKEN asked if the state sold everything and paid the debts it would get \$140 million.

MR. O'LEARY said ARRC has \$140 million of retained earnings and the state's investment of \$32 million so the total would amount to about \$172 million.

SENATOR WILKEN asked if the amount of money provided to ARRC by federal agencies would be jeopardized if ARRC and the AMHS are combined.

MR. O'LEARY said he believes so because a large part of the federal funding that ARRC receives comes with a 20 percent match requirement that ARRC would need to generate internally. Without its real estate income, ARRC would not be able to generate sufficient earnings to provide that match money.

SENATOR WILKEN asked what information the committee is waiting on from ARRC.

SENATOR WARD said he has requested copies of the checks written by ARRC last year. He was told it would take awhile to get that information together.

CHAIRMAN COWDERY added that ARRC had some legal issues it wants to look at first.

SENATOR WARD said nothing in this bill would take away any revenue from ARRC. An authority would oversee the operations. He assumes that the people appointed to the authority would do nothing to damage the ARRC any more than they would to damage the AMHS. He believes they would make decisions in the best interest of the state. He then asked whether hauling coal from Healy is profitable.

MR. O'LEARY said he is not comfortable discussing that question in this venue for proprietary reasons.

SENATOR WARD asked in what forum it would be appropriate to tell the legislators whether the railroad they own is making a profit from hauling that coal.

MR. O'LEARY said he would like to first speak to legal counsel to make sure that no information is disclosed in a public forum that would damage the railroad or one of its customers.

CHAIRMAN COWDERY offered that the information could be disclosed during an executive session.

MR. O'LEARY agreed.

2:38 p.m.

SENATOR ELTON thanked Mr. O'Leary for his straightforward testimony and then asked what percentage of the \$10.5 million gross income from real estate comes from ARRC's fiber optic leases.

MR. O'LEARY said a large part.

SENATOR WILKEN said from being around Fairbanks, the railroad and Healy coal, he would be shocked to find in executive session that the railroad made a nickel off of hauling the coal. Suneel (ph) drives a very hard bargain. It is his impression that the railroad has ponied up on numerous occasions to lower its costs to enable that mine to operate and ship half of its production to Korea.

SENATOR WARD thanked Mr. O'Leary for his testimony and said he understands the position ARRC is in. He believes ARRC has done an excellent job and is an asset to the state. However, he believes the AMHS is an equally good investment. He is trying to find a way for the AMHS to sit at this table and talk about its real estate holdings and ways to subsidize fares for citizens, like the railroad may be subsidizing Koreans to buy our coal. He noted he would like the elderly to ride free on the AMHS.

CHAIRMAN COWDERY asked about the transportation cost from Healy to Seward versus Healy to Anchorage. He asked if his information is correct that there is a large cost to split the trains to get over the Turnagain Pass.

MR. O'LEARY said there are a myriad of things that go into the cost structure of the railroad. ARRC looks at allocating fixed costs across the entire line and by line of business. The south end of the line from Anchorage to Seward does not have the traffic that the Anchorage to Fairbanks line has. Allocating costs can be done in a number of ways, he said, but certainly there is significant cost in taking coal from Anchorage over the pass. He does not know what the percentage split is.

CHAIRMAN COWDERY maintained that Alaska needs to be competitive when marketing its resources. He said:

You know we are by tidewater that's closer to get to Seward and it takes a long time to load the ships in Seward and I was just wondering if we could improve and make certain that this operation continues competitively. I understand - what is it Hyundai or somebody is shipping, they take care of the shipping and you do your negotiation through them. Anyway, [indisc.] with the Korean side of things.

SENATOR TAYLOR suggested dividing the issue so that instead of granting 500,000 acres to a joint authority, the AMHS and ARRC would each be given 250,000 acres. He asked Mr. O'Leary if his testimony would be different if that were to happen and whether the railroad could make money out of another 250,000 acres if it

was given to ARRC over the next 8 years.

MR. O'LEARY said the same questions apply regarding where the land is, what the access is, and what costs will be incurred to make it revenue producing but it is something the ARRC would take a serious look at.

SENATOR TAYLOR said it wouldn't be taxed so ARRC could do what the Knowles Administration does and let it just sit there. That's the way ARRC has been developing its lands anyway - it waits for someone to come along and ask to lease it. He stated that by dividing the question, the ARRC couldn't lose.

SENATOR WILKEN commented there has been a lot of noise and discussion around the Capitol lately about taking the money from working families of Alaska to fund government. He asked Mr. O'Leary what an appropriate franchise fee from the ARRC would be to help the people of Alaska fund their government.

MR. O'LEARY said there are a number of ways to view this but at this point, ARRC does not have enough to do what needs to be done to keep the railroad. Maintaining the infrastructure is a tremendous job. The federal money has been amazingly helpful but ARRC still needs every dollar of its internally generated funds to improve its operations. ARRC is continually striving to improve its operating ratio and profitability from rail operations so that it can generate more net income to plow back into the rail line. He said his initial response is that the ARRC cannot generate enough to take care of its own needs and hopes to do that before the legislature looks at any sort of dividend.

SENATOR WILKEN asked how many passengers the railroad will carry this year.

MR. O'LEARY answered around 480,000 to 500,000.

SENATOR WILKEN said if he could take \$10 from every passenger to keep his constituents from paying \$500,000 in income taxes, he would vote to tax those passengers. He advised Mr. O'Leary that the ARRC board may want to discuss the need to step up and help with the state's fiscal crisis because he believes that time is coming.

MR. BOB DOLL, Director of the Southeast Region of the Department of Transportation and Public Facilities (DOTPF), informed members he is responsible for the Marine Highway System as well as roads and airports in Southeast.

CHAIRMAN COWDERY asked if, given the opportunity to receive land for the AMHS, he would welcome that idea.

MR. DOLL said that is a very generous offer that DOTPF would have to seriously consider. He expressed skepticism, however, because ARRC makes money from the land that is contiguous to, or conveniently located to, the railroad, which it leases. It is not making money from the sale of property. Therefore, if the AMHS land is "over the mountain," he is not sure it will be beneficial.

CHAIRMAN COWDERY asked if it would be beneficial if it is in the right location.

SENATOR TAYLOR asked:

If you took your Marine Highway hat off for just a minute and I offered you 500,000 acres of Alaska lands that you could select, you'd worry about that and wonder where it was and whether or not you could make anything off of it or would you say I'll take it right now and I'll begin my selection tomorrow and I'll be making money off of it in six months?

MR. DOLL said that would be a likely reaction. However, he still has the problem of what to do next year and the year after that.

SENATOR TAYLOR asked if he is saying 500,000 acres would not be enough or that he would sell all of it in one year.

MR. DOLL said he believes identifying, assessing, and valuing it would be a process that is not likely to produce any real revenue for a considerable period of time.

SENATOR TAYLOR replied:

I wouldn't want to give it to you. I'd want to give it to somebody that would figure out how to develop it and make money off of it for a long, long time. In fact that's how we solved the Mental Health Trust problems because we gave them back their lands and they are generating significant income off of that land right now.

MR. DOLL said if that is a good model, the AMHS would hope to emulate it.

SENATOR TAYLOR said he would be shocked if the AMHS is opposed to having any additional asset base to help meet ongoing expenses.

CHAIRMAN COWDERY said that regarding selection of the land, small islands are in high demand for sale or lease. He said he agrees that giving the AMHS land in Tok Junction wouldn't be the most

desirable but land in Southeast would.

MR. DOLL said he is apprehensive that the designation of the land and the donation of it to the AMHS is anticipated to be the solution to a problem. He is not sure that it is but he is willing to consider it. He added if it doesn't rapidly produce revenue, it is not a solution.

CHAIRMAN COWDERY asked what "rapid" would be.

MR. DOLL replied two or three years would certainly be rapid.

SENATOR WARD asked if the AMHS is facing deferred maintenance costs and, if so, what the costs are.

MR. DOLL said there is deferred maintenance and asked Capt. Capacci for an exact figure.

CAPTAIN GEORGE CAPACCI, General Manager of the AMHS, said he does not have an exact figure for deferred maintenance projects but all ships have a certificate of inspection, Coast Guard inspections and American shipping inspections. He said a few years ago the amount of deferred maintenance was in the tens of millions of dollars.

SENATOR WARD remarked that if the AMHS meets all standards, no big projects need to be done right now.

CAPTAIN CAPACCI said that is correct.

MR. DOLL pointed out the legislature has been appropriating around \$4.5 to \$5 million every year for state-paid maintenance and for overhauls on the ships to bring the ships up to the condition Captain Capacci described.

SENATOR WARD asked what short term options the Administration has in mind to fund the AMHS in light of the lack of money in the marine highway fund.

MR. DOLL thanked Senator Ward for his concern about funding for the AMHS and for the thought that has gone into SB 271, but he said there are three aspects to what the Administration has in mind. The first has to do with the addition of shuttle ferries to the system, which will be less expensive to operate and which will address the problem of obsolescence of some of the mainliners. The second is a continuing examination of tariffs and an increase in revenue every two years. The third is to come to grips with the fact that some of the ships are now 40 years old. Whether they represent a worthwhile capital investment in the long term is a difficult question that will have to be faced. If the conclusion is that the costs of meeting their increasing

regulatory requirements is not worthwhile, taking them out of service will save money.

SENATOR WARD asked what will happen to the ferry schedule if the 40-year old ships are deemed too old to fix.

MR. DOLL said the system was originally designed to bring people in and out of Alaska and that design also provides transportation within Alaska. It does not do either job perfectly. The AMHS would like to improve the intrastate transportation system with a shuttle system and provide less of the interstate function. A good deal of the interstate function can be met with another shuttle system. He believes that by providing better transportation to people within the state at a lower cost, the long haul requirements can be met as well.

SENATOR WARD asked Mr. Doll if he plans to raise fees every two years.

MR. DOLL said that is correct.

3:02 p.m.

SENATOR WARD expressed disapproval and said he prefers the AMHS to use a land base to develop real estate instead of raising fees. He said it isn't right to subsidize coal for Koreans while charging his relatives more for travel. He stated he understands the turf issues involved in creating an authority but he can't justify raising fees. He said he is not opposed to splitting up the land for ARRC and the AMHS and that it is high time everyone has a discussion about what to do since the marine highway fund is out of money.

SENATOR ELTON asked if the transfer of land will include the transfer of subsurface mineral rights and whether the authority could select coal producing land.

SENATOR WARD said it is his intent that subsurface rights be transferred to the authority.

SENATOR TAYLOR asked if the state has subsurface rights on state-selected lands.

CHAIRMAN COWDERY was not sure.

SENATOR TAYLOR said the state is not allowed to convey those rights under the Statehood Act.

MS. CAROL CARROLL, Department of Natural Resources (DNR), said that is correct.

SENATOR ELTON said they can be transferred to another state agency.

SENATOR WARD said this authority is such an agency.

MR. DOLL stated that Senator Ward has raised some important philosophical questions and that DOTPF needs to give serious consideration to Senator Ward's question about how DOTPF should respond to the needs of the AMHS's financial needs.

SENATOR TAYLOR stated:

We've done the modest increases for several years now and we've modestly got ourselves up to the place where you're not begging for somebody to market you facilities so you can figure out how to get a rider back on them. It's just what Southeast needs right now for their economy - a couple more increases in ferry fares. Do you have toll road authority? I mean don't we charge a toll on Whittier? ...

MR. DOLL said he is not sure.

SENATOR TAYLOR said other states use them "like crazy."

MR. DOLL said he has never investigated the subject.

SENATOR TAYLOR said he co-sponsored a bill to get money for the Whittier Tunnel-Bradfield Toll Road bill. The money was appropriated based on the fact the Whittier road would be a toll road and the bonds would be repaid with toll charges. He wondered whether DOTPF has toll road authority because:

... if it does, I want a toll road put up on the Glen Highway and everyone of those rascals driving in and out of Wasilla and Palmer everyday going to work, they can pay one nickel and I guarantee it will fund your marine highway system forever, just off of that. And the nice thing to make them really appreciate the marine highway would be shut the blooming road down for about a week at a time like you do with all of my towns and we can let them all sit at home too [indisc.] then we could all feel the same way and be treated equally in this state. I don't know if you've got toll road authority and if you're looking at using it any place in the state.

MR. DOLL said he would be happy to research that question.

SENATOR TAYLOR asked Mr. Doll if DOTPF supports or opposes SB 271

and asked where the fiscal note is.

MR. DOLL said he has not discussed the subject beyond the Southeast region so he does not know what the department's position will be. He thought the Commissioner is on record as having said if a financing mechanism can be found, he would be happy to endorse it.

SENATOR TAYLOR said he thought that was the quintessential question of why Mr. Doll is here: whether DOTPF supports or opposes the bill.

SENATOR ELTON said he is hearing one entity say no and the other say maybe.

MR. DOLL said he did not come prepared to testify so he cannot answer the Senator's question but he will get an answer for the committee.

SENATOR TAYLOR asked if the committee failed to give DOTPF notification a week ago of this hearing.

CHAIRMAN COWDERY said DOTPF had notice.

SENATOR TAYLOR asked whether DOTPF submitted a fiscal note.

CHAIRMAN COWDERY said it did not. He then announced that he would hold the bill in committee until he has more information from the railroad.

MS. CAROL CARROLL, Department of Natural Resources (DNR), informed members that DNR has before the Finance Committee various revenue generating proposals. Those proposals might cost a little money but they use state lands.

CHAIRMAN COWDERY asked Ms. Carroll to provide in writing a list of all state owned islands with high commercial value in Southeast Alaska.

MS. CARROLL said she can provide information on the amount of state land in Southeast and whether that land is located on islands.

SENATOR ELTON said DNR has that information because it went through that exercise with the University lands trust bill.

SENATOR WARD said he requested from DNR a description of state land in Southeast and through the Rail belt, including buildings. He then asked about the total amount of state land in Southeast.

MS. CARROLL said she did not know and she does not know whether

500,000 acres of state land exists in Southeast.

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SENATOR TAYLOR said there is not; the federal government would not allow the state to select much land in Southeast. He noted that Native villages in Southeast only got one township (23,000 acres) while Native villages up North got four because of previous commitments made by the federal government on the Tongass and how much they would allow to be taken out of it.

MS. CARROLL informed members that DNR is most interested in Section 25 of this bill - the section that transfers 500,000 acres to the authority. That transfer will be a very difficult one. DNR will get into substantial controversy about which acreage to transfer. The process will be arduous and will be costly. The revenue generation from the undeveloped portions of the selected land would not occur for years into the future. Land that is already developed would have a lease sharing structure so that if the land is leased prior to selection, the state gets to retain the income. If it is leased after selection, that income goes to the authorities. The authority could select oil and gas properties as long as those properties are not on a five-year sale schedule. The authority could get the subsurface rights on the 500,000 acres.

SENATOR ELTON asked if intertidal lands could be selected.

MS. CARROLL said the bill does not say they cannot be selected. She added that DNR opposes this legislation.

SENATOR TAYLOR asked if DNR opposes the bill or was told to oppose it.

MS. CARROLL said DNR opposes SB 271.

SENATOR TAYLOR said he found the footnote on DNR's fiscal note to be absolutely fascinating. That footnote says it can be assumed that the Marine Rail Fund will select the most valuable parcels it can find with the effect of diverting a significant revenue stream out of the general fund where it would have been available for those public purposes the legislature deemed most important. He asked what the value of the significant revenue stream from 500,000 acres is under DOTPF's management today and how much DNR believes will come out of the future revenue stream of the state by diverting the 500,000 acres that DNR has done nothing with during the last 30 years of management.

MS. CARROLL replied DNR does not know the amount because it does not know what would be selected.

SENATOR TAYLOR said DNR could use the premise that the authority will take the most valuable acreage.

MS. CARROLL said she could provide an example of what happened under the University lands bill. The University wanted a parcel close to Denali Park. The University thought that parcel could be sold to the Park Service for a substantial amount of money. That land was undeveloped but it was worth a lot.

SENATOR TAYLOR said that was in the Wolf Townships and that the Governor was trying to find a way to protect the Toklat wolves "for his buddy up there." In the process, he wanted to force the University to take the land to sell to some "eco-group" who would gift it to the National Park Service to expand the Denali Park boundary north to make certain that no railroad ever came in from the northern end of the park. He alleged that had nothing to do with land value but instead had to do with politics on "the third floor." He asked Ms. Carroll if DNR has a piece of land with significant value in the marketplace that might be purchased rather than a piece that will be purchased for political purposes.

MS. CARROLL maintained that the piece of land he referred to was valuable to some people.

SENATOR TAYLOR said it would be very valuable to people in Kantishna or a person who might want to build a lodge out there but it is still in the ownership of DNR.

MS. CARROLL said it is.

SENATOR TAYLOR said, "Let's talk about some land if you know of any where a human being might be interested in using it for a business purpose, either harvesting timber or development."

MS. CARROLL informed members that DNR is selling agricultural land that brings a pretty good price. Most of the Point MacKenzie land has been sold. DNR is also holding annual land sales. The parcels that do not get sold during the initial offering get sold over the counter. She thought if an entity was interested in getting 500,000 acres, it would be looking at the things DNR is doing right now.

SENATOR TAYLOR said that was his assumption too. He asked how much DNR is bringing in off of state land sales today that would be lost if the 500,000 acres was given to the authority.

MS. CARROLL said she does not have that information right now. She estimated DNR has brought in about \$4 million from the sale of agricultural lands over the last couple of years. She offered to bring Senator Taylor a more accurate number.

SENATOR TAYLOR noted that if an authority took all of the most marketable lands that DNR has and started to sell them, the state would lose nothing. DNR would lose the money to the Department of Revenue and to the general fund. The legislature would no longer have to pay a subsidy to the AMHS and the ARRC would not have to subsidize its operations from its real estate operations.

MS. CARROLL said the land sale program in the department is funded from the sales that occur. If those lands were transferred out, DNR's land sale program would suffer. She offered to provide the committee with the types of acreage it might be interested in.

SENATOR TAYLOR pointed out that the notation on DNR's fiscal note claims this will deprive the state of a large income source the state has for its future. He asserted that DNR made \$3 million on lands it managed for 30 years while the University made \$43 million in the five years it managed them. He surmised that some other entity might be able to make more money off of managing land than DNR so he would not be opposed to giving it to someone with an incentive to make money from.

MS. CARROLL contended that DNR makes a lot of money on the land it manages.

SENATOR TAYLOR alleged that DNR does not make money: the private sector makes money and pays DNR for the permits to use that land. He said he is speaking to land sales and allowing people to develop land.

MS. CARROLL acknowledged that DNR has become better at managing land sales in the last two years when it when it began to have a revenue stream.

SENATOR TAYLOR said he prompted that to a good degree, in addition to DNR's timber sales. He said he is proud that incentive is working.

MS. CARROLL said the transfer of future oil and gas properties that aren't on the five-year schedule would amount to the loss of a substantial amount of money.

SENATOR TAYLOR agreed and said one small areawide lease might support the AMHS forever. He suggested giving THE AMHS something like Alpine or Kuparuk.

There being no further questions for Ms. Carroll, CHAIRMAN COWDERY called the next witness to testify.

MR. HERB MCDONALD, Karloff (ph) Transportation, made the

following statement.

Just here by accident but since Senator Elton said that highway users didn't pay I thought I'd better bring that up because we pay 32½ cents a gallon and \$550 per vehicle. But I think the real issue is controlling the subsidy. If it - whatever that is on highways, whatever it is on the marine highway, you as our representatives know what that subsidy is and you control it. With the railroad, you don't control that. I think the gentleman said they get 11½ million real estate and make about 6 million. I'm sure you could hire that out for about 500,000 - 5 or 10 percent and get that done. And if you throw the other 50, 60, 70 million a year in there, that's a pretty big subsidy that you guys don't control so that - to me that's the issue and I think putting land to subsidize an operation is a bad thing to do.

CHAIRMAN COWDERY asked Mr. McDonald how much his company pays per year in licensing fees and fuel or other taxes for use of the highway.

MR. MCDONALD estimated about \$400,000 to \$500,000.

SENATOR TAYLOR said he agrees with Mr. McDonald but said that unfortunately, with the way the railroad was created, it is not totally under the legislature's jurisdiction. He informed Mr. McDonald that DOTPF creates the Statewide Transportation Improvement Plan (STIP), which establishes the manner in which all highways will be constructed, and the legislature has no oversight other than whether to fund it.

MR. MCDONALD said he does not mean to be negative toward the railroad or the marine highway and actually believes the marine highway should be free to passengers because it is a highway. He felt the legislature should be making the decision about how much to subsidize.

SENATOR TAYLOR again said he agrees with Mr. McDonald and then said those trying to do business in Southeast Alaska not only pay the \$400,000 but also more than 50 percent of the cost of operating a ferry. Sometimes the ferry doesn't show up or three show up on the same day going in the same direction. He said if DOTPF would give Southeast one-half the cost per mile that is currently spent on roads up north, the marine highway's operating budget would increase by about 40 percent.

MR. MCDONALD said he is not qualified to argue that. He commented that when he puts a trailer on the ferry, he is not burning fuel and paying 32 cents per mile so maybe there is some

justification.

SENATOR TAYLOR said that is true but he is paying through the nose to put a trailer on the ferry and would not do so if there was any way to use a road.

MR. MCDONALD said if there is a road there shouldn't be a ferry.

SENATOR TAYLOR said roads run parallel to the ferries all over Southeast and there are roads to Valdez and Seward.

MR. MCDONALD said he believes the ferry should go from a large port to places like Kodiak and Cordova, where there are no roads.

SENATOR TAYLOR noted that the original mission statement of the AMHS said roads would be developed that would be interconnected to a shuttle ferry system. He stated, "It's only since these guys got here that they totally changed the mission statement of the marine highway system and they're still going to run every boat they can from Bellingham to Skagway and back."

CHAIRMAN COWDERY announced the committee would hold SB 271 and its companion bill, SJR 32, in committee until a later date. He then adjourned the meeting at 3:30 p.m.