

HOUSE FINANCE COMMITTEE

June 6, 2006

1:13 P.M.

CALL TO ORDER

Co-Chair Chenault called the House Finance Committee meeting to order at [1:13:50 PM](#).

MEMBERS PRESENT

Representative Mike Chenault, Co-Chair
Representative Bill Stoltze, Vice-Chair
Representative Jim Holm
Representative Reggie Joule
Representative Mike Kelly
Representative Beth Kerttula
Representative Carl Moses
Representative Bruce Weyhrauch

MEMBERS ABSENT

Representative Kevin Meyer, Co-Chair
Representative Richard Foster
Representative Mike Hawker

ALSO PRESENT

Denny DeWitt, Special Assistant, Office of the Governor;
Louisana W. Cutler, Attorney, Counsel, Preston, Gates,
Ellis, Anchorage

SUMMARY

#HB2003

HB 2003 An Act establishing the Alaska Natural Gas Pipeline Corporation to finance, own, and manage the state's interest in the Alaska North Slope natural gas pipeline project and relating to that corporation and to subsidiary entities of that corporation; relating to owner entities of the Alaska North Slope natural gas pipeline project, including provisions concerning Alaska North Slope natural gas pipeline project indemnities; establishing the gas pipeline project cash reserves fund in the corporation and establishing the Alaska natural gas pipeline construction loan

fund in the Department of Revenue; making conforming amendments; and providing for an effective date.

HB 2003 was HEARD and HELD in Committee for further consideration.

HOUSE BILL NO. 2003

An Act establishing the Alaska Natural Gas Pipeline Corporation to finance, own, and manage the state's interest in the Alaska North Slope natural gas pipeline project and relating to that corporation and to subsidiary entities of that corporation; relating to owner entities of the Alaska North Slope natural gas pipeline project, including provisions concerning Alaska North Slope natural gas pipeline project indemnities; establishing the gas pipeline project cash reserves fund in the corporation and establishing the Alaska natural gas pipeline construction loan fund in the Department of Revenue; making conforming amendments; and providing for an effective date.

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DENNY DEWITT, SPECIAL ASSISTANT, OFFICE OF THE GOVERNOR, noted that Ms. Cutler would provide a "walk-through" of the version of the bill before the Committee.

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LOUISIANA W. CUTLER, ATTORNEY, COUNSEL, PRESTON, GATES, ELLIS, ANCHORAGE, provided the bill's background.

Ms. Cutler explained that the role of the Alaska Natural Gas Pipeline Corporation [Alaska Pipe] has been misleading to date and offered to overview the Alaska Pipe. It will be a public corporation by which the Administration proposes, the State own the interest in the pipeline. It would be the mainline, limited-liability {LLC} entity, holding ownership interest in other segments of the projects. The mainline LLC would be the entity which would build the pipeline in Alaska; it is anticipated that the Alaska Pipe would spin-off subsidiaries to hold other aspects of the project, holding the interest in feeder lines on the slope. The details have not yet been defined.

The intent of the legislation would provide the necessary flexibility to complete the project.

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Ms. Cutler explained that the model used to develop the legislation was taken from successful corporations existing throughout the State such as the Permanent Fund Corporation, the Alaska Housing Finance Corporation (AHFC), & the Alaska Industrial Development Export Authority (AIDEA) statutes. The Alaska Pipe project would be a different magnitude from anything the State has ever been involved in.

Ms. Cutler highlighted the unique features of the legislation. The Alaska Pipe would be the entity through which the State would finance the venture. The legislation establishes the issuance of revenue bonds either with or without authorization. It would set-up the corporation as separate and independent, so that the liability and revenues would be closed-off from being connected to the State, which is important to protect the State's interest.

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Vice Chair Stoltze asked what the distinctions would be between the proposed entity and any existing corporations. Ms. Cutler replied she would address that later in the testimony, reiterating that this project would be the largest & most complicated partnership with the private sector. The structure would differ from other public corporations.

The Board would slightly differ from other boards and would have seven members:

- Two commissioners, one from the Department of Transportation & Public Facilities and one from the Department of Revenue
- Five for-cause public members, not serving at the pleasure of the Governor

She added Board members would need to be insulated from changes occurring in the political structure every four years. The idea is to create a stable board, making decisions over the long haul. The learning curve for the members will be big. The board members would serve a six-

year term. There would be no legislative confirmation, protecting political behavior, functioning independently.

Ms. Cutler highlighted other features including not required compliance with the Alaska Open Meetings Act. She foresaw many concerns, requiring quick decisions.

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Ms. Cutler said the State does not anticipate open meetings, however, realizes the importance for conveying public information.

Another feature regarding the Public Records Act includes language specifying exemptions. The Public Records Act contains a catch-all, subject to disclosure. The Courts have been reluctant to read the exemption broadly enough. She added trade secrets should not be subject to disclosure.

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Ms. Cutler highlighted provisions relating to the LLC so Alaska Pipe can accomplish what is important. In the context of other agreements, the Alaska Pipe would be located in the private sector. It is typical for parties to agree that if obligations are not met, certain rights are lost and the authority to do that would be in the statute, which would not be typical language.

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Ms. Cutler identified other features including the anti-indemnification exception, a specific provision in State law, making that approach illegal. Also, it would be exempt from compliance with the procurement code in order that the State can enter into projects, receiving required services. The Alaska Railroad Association is exempt from some codes including the procurement code. They are not required to comply with statutory or budgetary statutes; however, the Legislative Budget & Audit (LBA) Committee could audit that group.

Ms. Cutler commented on the ownership financing, provided through bonding authority & commercial loans. Alaska Pipe will have the authority to participate in financing. The Department of Revenue could carry the loan fund, anticipating that the Legislature would appropriate

directly into that fund. She commented on language establishing for-profit subsidiaries, similar to that in the tobacco litigation.

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Vice Chair Stoltze asked about the "conflict of interest" section. Ms. Cutler acknowledged that a conflict of interest section had been included & that members of the Board would be covered through the Ethics Act, indicating their conflicts.

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Ms. Cutler overviewed the House Judiciary Committee version/G of the bill, including the important "findings" section. She believed that the undertaking would be in the best interest for the State. The findings sections [(1) & (2)], deal with Article 8 of the Constitution.

Section 9, Pages 2 & 3, stipulate that it must be in the best interest for the State to acquire ownership and participate in financing construction of the project.

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Vice Chair Stoltze pointed out those findings sections are usually not supported by the House Finance Committee. Ms. Cutler understood and recognized that it was the choice of the Committee; however, given the magnitude of the project, it is important to include a finding section. Courts use the findings useful during challenges.

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Vice Chair Stoltze reiterated his concern with inclusion of that language.

Representative Holm voiced concern that HB 2003 had not been a legislative proposal, instead came through the Governor. He recommended that Ms. Cutler correct her terminology, indicating that the concept is only a "proposal before the Committee". He added his added concern with inclusion of the findings. Ms. Cutler apologized and stood corrected.

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Co-Chair Chenault pointed out that language on Page 3, Lines 16-31, discuss material previously mentioned. Ms. Cutler agreed.

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Ms. Cutler referenced Page 4, Section 2, Line 5, which addresses establishment of the corporation as a State separate instrument and is important language to include. Alaska Pipe should be established as a separate corporation with independence, yet separate from the Legislature and Governor and should be outside any normal State agency structure.

Representative Holm inquired if there had been discussion regarding resident status of the Board members.

Ms. Cutler said originally, no residency requirement had been proposed because of required expertise needed for that work. She pointed out language indicated on Lines 6-9 requiring certain experience. She emphasized that the project would be large and sophisticated. She understood that a majority of board members would be from Alaska.

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Vice Chair Stoltze requested names of the Alaska residents being considered. Ms. Cutler did not know.

Representative Joule added inquires regarding the make-up of the Board, asking if it would include a major oil company president. Ms. Cutler responded that current language does not provide for that; it was not the intent but instead getting people with oil and gas experience.

Representative Joule voiced concern including people from the oil & gas industry; he worried that the State of Alaska could become a minority member, negatively impacting Alaska's well-being.

Mr. DeWitt pointed out the language of the "conflict of interest" provision. There was discussion in the previous Committee regarding corporate versus non-corporate level person working for the company. That pool is large to avoid any conflict of interest. Ms. Cutler added that every partner would be a "minority-interest-holder"; no one would carry more than 50% ownership interest.

Ms. Cutler pointed out inclusion of the commissioners from both the Department of Revenue commissioner and the Department of Transportation & Public Facilities and language exception for those in the armed services.

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Ms. Cutler reiterated the need for extensive experience. Mr. DeWitt interjected that the criteria provides a small pool; the previous Committee {HJC} attempted to expand that pool, keeping sideboards. Ms. Cutler had mentioned an appointed designee, confusing HJC. The sentence was removed.

Vice Chair Stoltze advised that some boards and commissions address designees upon the death of a member. He was troubled that it would be okay to designate an unconfirmed deputy commissioner to make policy decisions. Ms. Cutler advised that both commissioners serve on many different boards and commissions, noting that the Permanent Fund has operated in the proposed manner for many years. She understood the concern, however, pointed out it could not be expected that those individuals would be able to make every meeting of the Alaska Pipe board. Mr. DeWitt agreed that it is a logistical problem; each commissioner would be involved but not always in attendance of all the meetings.

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Ms. Cutler reviewed provisions for board meetings.

- They would occur not less than once every three months;
- They would be subject to the call of the chair, allowing flexibility;
- They could occur through teleconference, standard procedure; and
- The Board would be exempt from the Open Meetings Act in order to do business quickly, discussing confidentially materials.

Ms. Cutler reviewed requirements for the minutes, the \$400 compensation and "removal for cause" clause of the board members. She pointed out that the board could delegate staff for day-to-day operations. The board requires that the executive director or other members of the staff be

delegated with authority to be board spokesperson at management level. The staff would serve at the pleasure of the executive director and could be removed at any time by the executive director without notice or cause.

Co-Chair Chenault asked if that was standard procedure. Ms. Cutler affirmed that anyone in exempt service is in that situation.

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Ms. Cutler reviewed the conflict of interest section, pointing that they would be covered by a financial disclosure statement. She observed that the Corporation could sell, lease, exchange, donate, convey, or encumber in any manner by mortgage, by creation of any other security interest or otherwise, real or personal property owned by it or in which, it has an interest, including any ownership interest in the project or in a subsidiary entity, when, in the judgment of the corporation, the action is in furtherance of its corporate purposes; to enter into and perform its obligations under contracts or agreements, including contracts or agreements to own, construct, manage, or operate the project, and do all things necessary or convenient to carry out its corporate purposes and exercise its powers.

Vice Chair Stoltze questioned if an upper threshold for the elective officials would need to be met. Ms. Cutler said that concern was addressed in:

(11) To enter into and perform its obligations under contracts or agreements, including contracts or agreements to own, construct, manage, or operate the project, and do all things necessary or convenient to carry out its corporate purposes and exercise its powers.

Ms. Cutler explained that the State might want to pay off its interest to another party. The corporation might want to sell off part of that ownership interest. The amount of interest should be discussed at the discretion of the Governor.

Representative Holm voiced concern with inclusion of the provision in Section 8, Page 9. He said it was not in the best interest for the program. Ms. Cutler and Mr. DeWitt agreed, noting it was added by the previous Committee, HJC.

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Representative Holm referenced item #6, Page 8, regarding operation of the project and asked about that "vision". Ms. Cutler explained that it was the intent of the corporation to take the ownership interest in the project, asking to design the corporation in a way that if the project takes a number of years to get going, could the Legislature see fit to establish it before the approval of a contract. Alaska Pipe could then move forward with the project. She thought that some State employees could be loaned to the operations.

Representative Kerttula observed that it would run similar to the Joint Pipeline Office, subsection (6) [power of the board to operate any project of any portion of the project]. Ms. Cutler observed that Alaska Pipe would not be building the pipeline itself, however, the intent is to give them all the necessary power.

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Vice Chair Stoltze inquired if names had been registered. Ms. Cutler said no. She highlighted the powers of the corporation & noted that the partners had voiced concern with the State's ability to meet the financial obligations under the contract. There was discussion regarding failure to do that could result in forfeiture:

(22) Except for a statutory change made by initiative or in response to a final nonappealable court order, to agree that, as part of an agreement to form an owner entity of the project, its voting rights and its access to confidential information otherwise provided for under the terms of the agreement may be restricted if this chapter is amended or another statute is enacted and that law has a material adverse effect on the corporation's ability to perform its obligations under that agreement; however, the corporation may not agree to any terms that attempt to limit the legislature's authority to exercise police powers of the state.

Ms. Cutler explained that Section 22 would provide Alaska Pipe authority to enter into an agreement that could have voting rights curtailed if it had an adverse effect on the corporation's ability to perform the obligation under that agreement.

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In response to Representative Kerttula, Ms. Cutler explained it is important that no action adverse impact Alaska Pipe's ability to meet obligations. The intent is to design the agreement so that it is in accordance with Delaware case-law, which addresses the material adverse effect upon standards. The fiscal contract would be Alaska law and the LLC would be Delaware law.

Representative Kerttula emphasized that the State would be giving up their ability to pass law, impacting it. She urged further discussion of what "material adverse effect" is & the differences between Alaskan and Delaware law regarding that.

Ms. Cutler highlighted Section [23] dealing with the power:

(23) In furtherance of the satisfaction of its obligations, including, without limitation, its project costs and financing obligations, to instruct any person making a payment or distribution to the corporation to make or the payment or distribution directly to any person specified by the corporation.

She explained the intent to assure that the Alaska Pipe has ability to pay debts directly. The LLC would be the major source of revenue for Alaska Pipe and the LLC would eventually 'spin off' revenue to all members through dividends. Section 22 allows the Alaska Pipe, through the LLC, to pay bond or loan holder's account, language recommended by the State financial advisors.

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Ms. Cutler referenced (24) (b):

(b) Notwithstanding (a) of this section and other provisions of law, the corporation or any subsidiary entity of the corporation may not sell, transfer, or otherwise dispose of an interest in the Alaska North Slope natural gas pipeline without the approval of the governor.

The above section provides language to allow subsidiaries to be established as proposed in the overview. The Alaska Pipe

would be in control of those subsidiaries. Canadian law could carry different requirements. Subsection (b) allows the subsidiaries to transfer assets to the subsidiary. The HJC did change Section (c), Lines 7-11, allowing for interlocking boards. In Canada, residency requirements exist; that language addresses those concerns.

Representative Joule asked about the Board's composition and if members could be other than U.S. citizens. Ms. Cutler said they could.

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Ms. Cutler briefly addressed Article 3, which covers all financing obligations & bonding provisions. Page 16, Lines 18-22, addresses moral obligations of revenue bonding.

Co-Chair Chenault asked if the bonding provisions would be the same in both the U.S. and Canada. Ms. Cutler explained the intent is to provide subsidiary power, issuing bonds if authority is provided. She offered to research that.

Ms. Cutler commented on Article 4, Page 19, Line 11, regarding establishment of the cash reserve fund, pulling money for the Alaska Pipe from the Legislature, using for the purpose of securing a credit line.

Co-Chair Chenault pointed out that would be only the initial investment. Ms. Cutler believed it would last for the life of the fund. Co-Chair Chenault assumed that could be identified in the fiscal note, indicating core receipts with no General Fund match. Initially, he thought it would be a General Fund match. Ms. Cutler said Mr. Porter indicated there were appropriations in the Capital Budget for that purpose. It would be up to the Legislature to determine how that would be paid. Ms. Cutler thought that the appropriation could come through the normal operating budget proceedings.

Representative Joule questioned the State's exposure. Ms. Cutler acknowledged that the corporation would be established as a separate and independent entity so that only those assets would be exposed. It is important to make sure that the liability is limited only to the assets of Alaska Pipe and set up as a separate public corporation. Representative Joule did not understand that; he wondered if there would be an 80% liability. Ms. Cutler replied the LLC

would be limited only to the assets of Alaska Pipe. Alaska Pipe will hold an ownership interest with three other partners. Those partners will hold a percentage of ownership, which means the financial obligations, would amount to 20% of equity and would include a debt percentage structure. As long as the corporation is the only entity undertaking the obligations, what is exposed would be the corporation, which may or may not be a 20% match. The General Fund would not be exposed. There is concern whether the Alaska Pipe would be "credit-worthy" enough and if there should be State involvement.

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Vice Chair Stoltze referenced Article 4 - the relationship to operations and questioned limiting the "political activity" language. Ms. Cutler explained there is a purpose to limit that language and the statement should be included for the appropriate tax-exempt ruling from the Internal Revenue Service (IRS). In discussion of those activities, it is assumed that the Alaska Pipe would not be able to go to Congress to participate in what the loan guarantee program would look like; hence, the language was narrowed.

Ms. Cutler pointed out Article 5, Page 20, the financial statements provided to the Governor and the Legislative Budget and Audit Committee (LBA), providing for audits of the books; a non-subsidiary entity could not be audited.

Section 41.42.510 was borrowed from the Permanent Fund statute and requires reports and publications including financial statements. It requires that the corporation establish a website for public access. She highlighted specific exemptions listed Lines 16-29, Page 21.

1. Information pertaining to the particulars of the business or affairs of an owner entity of the project, including, without limitation, tax returns, financial statements, and business plans;
2. Information containing a trade secret or other proprietary information of the corporation or of an owner entity of the project;
3. Information that is confidential or privileged under the laws of the state, whether at common law or by statute or court rule;
4. Information that is required to be kept confidential under an agreement with an owner entity of the project, or with other participants in an owner entity of the project;

5. Information that would affect the competitive position of the corporation or an owner entity of the project; and
6. Information of the corporation or an owner entity of the project that has commercial value that might be significantly diminished by public disclosure.

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Ms. Cutler added:

- Subparagraph (b) provides information in the possession of an owner entity of the project is confidential.
- Subsection © allows situations in which disclosure information is confidential, when it can be disclosed such as to lenders.

Representative Kerttula clarified that the information held by the LLC would not be public. She asked about the information coming from Alaska Pipe Co to the LLC. Ms. Cutler replied information to the LLC would not be covered by the Public Records Act and would not be subject to disclosure requirements associated with the Act.

Representative Kerttula asked if the LLC could control Alaska Pipe's behavior. Ms. Cutler compared any private company that has information; it does not apply to private sector entities.

Ms. Cutler noted that the definition section of the bill was contained in Article 6, Page 22, beginning Line 23.

- Alaska North Slope natural gas pipeline project
- Board
- Corporation
- Financing obligations
- Owner entity of the project
- Ownership interest in the project

Vice Chair Stoltze asked about the forestall spur-lines of the natural gas pipeline transportation system. Ms. Cutler hoped that would not happen and that the definition was intended to cover all aspects of the project.

Vice Chair Stoltze emphasized that the bill is about a pipeline in Alaska through Canada. He did not want to see something that would limit in-State options. Ms. Cutler

responded that the language deals with the main pipeline and the infrastructure needed to connect that pipeline. Mr. DeWitt agreed.

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Ms. Cutler pointed out that Sections 4 & 5 were technical amendments addressing the State entities buying stock. Section 6 establishes the loan fund within the Department of Revenue, providing options for financing the obligations, a typical loan fund with terms established by the Commissioner.

Ms. Cutler noted that Section 7, Page 25, Line 5, provides more technical amendments that place employees of the Alaska Pipe into an exempt service. Section 8, Page 26, Line 16, adds the Alaska Pipe staff to statute, requiring financial disclosure. Section 9, Page 27, Line 7, does the same thing for the Board. Section 10, Page 27, Line 9, adds a conforming amendment clarifying that the subsidiary board would not be governed by the Ethics Act because there would already be a Canadian Ethics Act in place.

Section 11, Page 27, Line 18, outlines a conforming amendment to the Public Records Act.

Sections 12 & 13, Pages 29-31, provides an indemnification provision to the effective date. There is a statute and common-law doctrine, which provides indemnification agreements in construction contracts. The language provides an exemption to the common-law doctrine, providing indemnification in construction projects.

Ms. Cutler explained that when building a pipeline project, it is common to indemnify the parties against mistakes and bad conduct. She understood that was done because it would be a large project. Sometimes mistakes result in liability and sometimes, worse conduct occurs, which brings about liability. In a project of this size, such potential must be managed and provides for many provisions of indemnification. That language could lower costs of the construction.

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Representative Kelly inquired if entering into a LLC would protect and adjust the corporate "veil". Ms. Cutler

understood, there would be mutual indemnifications. The statute largely governs the Alaska Pipe.

Representative Kelly asked if that could provide a "level playing field" or would it place the State in a vulnerable position. Ms. Cutler thought there would be cross indemnification authority. The language allows only the authority providing for the cross indemnifications. She could not guarantee that the agreement would accomplish that, however, that was what it was designed for.

Ms. Cutler added that the Administration would like to take the opportunity to respond to previous comments made by Mr. Gildan's memorandum contained in the member's file packet.

Representative Kerttula interjected that Representative Gara had presented an amendment regarding taxation to the State and asked if indemnification would extend to financial situations. Ms. Cutler responded that Representative Gara was concerned that the ability to indemnify the LLC construction of the project could be misinterpreted by the State against tax royalty owed. She understood the intent and that Mr. Gildan had testified that there might be a way to interpret it that way. The State of Alaska's position would like to reimburse the producer through a fiscal contract. HB 2003 is not the vehicle for the fiscal contract but rather the legislation, which would govern the establishment and hold member's interest in the LLC. The Administration would not support placing that language into HB 2003 because that is not their position to the contract.

Representative Kerttula asked if the language would include criminal behavior. Ms. Cutler said it would and that it is statutory authority.

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Representative Kerttula requested more information regarding that concern.

HB 2003 was HELD in Committee for further consideration.

#

ADJOURNMENT

The meeting was adjourned at 3:31 P.M.