

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

March 30, 2007

8:30 a.m.

MEMBERS PRESENT

Representative Vic Kohring, Chair
Representative Kurt Olson, Vice Chair
Representative Nancy Dahlstrom
Representative Ralph Samuels
Representative Mike Doogan
Representative Scott Kawasaki

MEMBERS ABSENT

Representative Jay Ramras

OTHER LEGISLATORS PRESENT

Representative John Coghill

COMMITTEE CALENDAR

HOUSE BILL NO. 177

"An Act relating to the Alaska Gasline Inducement Act; establishing the Alaska Gasline Inducement Act matching contribution fund; providing for an Alaska Gasline Inducement Act coordinator; making conforming amendments; and providing for an effective date."

- HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 177

SHORT TITLE: NATURAL GAS PIPELINE PROJECT

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

03/05/07	(H)	READ THE FIRST TIME - REFERRALS
03/05/07	(H)	O&G, RES, FIN
03/06/07	(H)	O&G AT 3:00 PM BARNES 124
03/06/07	(H)	-- MEETING CANCELED --
03/08/07	(H)	O&G AT 3:00 PM BARNES 124
03/08/07	(H)	-- MEETING CANCELED --
03/13/07	(H)	O&G AT 3:30 PM HOUSE FINANCE 519
03/13/07	(H)	Heard & Held

03/13/07	(H)	MINUTE(O&G)
03/15/07	(H)	O&G AT 3:00 PM BARNES 124
03/15/07	(H)	Heard & Held
03/15/07	(H)	MINUTE(O&G)
03/19/07	(H)	O&G AT 8:30 AM CAPITOL 106
03/19/07	(H)	Heard & Held
03/19/07	(H)	MINUTE(O&G)
03/20/07	(H)	O&G AT 3:00 PM BARNES 124
03/20/07	(H)	Heard & Held
03/20/07	(H)	MINUTE(O&G)
03/21/07	(H)	O&G AT 5:30 PM SENATE FINANCE 532
03/21/07	(H)	Heard & Held
03/21/07	(H)	MINUTE(O&G)
03/22/07	(H)	O&G AT 3:00 PM BARNES 124
03/22/07	(H)	Heard & Held
03/22/07	(H)	MINUTE(O&G)
03/23/07	(H)	O&G AT 8:30 AM CAPITOL 106
03/23/07	(H)	Heard & Held
03/23/07	(H)	MINUTE(O&G)
03/24/07	(H)	O&G AT 1:00 PM SENATE FINANCE 532
03/24/07	(H)	-- Public Testimony --
03/26/07	(H)	O&G AT 8:30 AM CAPITOL 106
03/26/07	(H)	Heard & Held
03/26/07	(H)	MINUTE(O&G)
03/27/07	(H)	O&G AT 3:00 PM BARNES 124
03/28/07	(H)	O&G AT 7:30 AM CAPITOL 106
03/28/07	(H)	Heard & Held
03/28/07	(H)	MINUTE(O&G)
03/28/07	(H)	O&G AT 8:30 AM CAPITOL 106
03/28/07	(H)	Heard & Held
03/28/07	(H)	MINUTE(O&G)
03/29/07	(H)	O&G AT 3:00 PM BARNES 124
03/29/07	(H)	Heard & Held
03/29/07	(H)	MINUTE(O&G)
03/30/07	(H)	O&G AT 8:30 AM CAPITOL 106

WITNESS REGISTER

PATRICK GALVIN, Commissioner
 Department of Revenue (DOR)
 Anchorage, Alaska

POSITION STATEMENT: Reviewed proposed amendments to HB 177 and responded to questions.

DON BULLOCK, Attorney
 Legislative Legal Counsel
 Legislative Legal and Research Services

Legislative Affairs Agency
Juneau, Alaska

POSITION STATEMENT: Spoke as the drafter of amendments to HB 177 and responded to questions.

ACTION NARRATIVE

CHAIR VIC KOHRING called the House Special Committee on Oil and Gas meeting to order at [8:30:57 AM](#). Representatives Samuels, Doogan, Kawasaki, and Kohring were present at the call to order. Representatives Olson and Dahlstrom arrived as the meeting was in progress.

HB 177-NATURAL GAS PIPELINE PROJECT

[8:31:08 AM](#)

CHAIR KOHRING announced that the sole order of business would be HOUSE BILL NO. 177, "An Act relating to the Alaska Gasline Inducement Act; establishing the Alaska Gasline Inducement Act matching contribution fund; providing for an Alaska Gasline Inducement Act coordinator; making conforming amendments; and providing for an effective date."

CHAIR KOHRING recessed the House Special Committee on Oil and Gas meeting to a call of the chair [for the purpose of waiting for a committee substitute to be delivered to the committee].

[8:44:40 AM](#)

CHAIR KOHRING reconvened the House Special Committee on Oil and Gas. Present at the reconvening were Representatives Dahlstrom, Samuels, Doogan, Kawasaki, and Kohring. Representative Olson arrived as the meeting was in progress.

[8:46:13 AM](#)

REPRESENTATIVE DAHLSTROM moved to adopt the committee substitute (CS) for HB 177, Version 25-GH1060\E, Bullock, 3/30/07, Version E as a work draft.

[8:46:19 AM](#)

CHAIR KOHRING objected.

REPRESENTATIVE DOOGAN objected and explained that he does not know the content of Version E well enough to adopt it as a work draft.

[There was discussion regarding the correct procedure and it was determined that a vote did not have to be taken; instead the motion with the two objections was left pending.]

8:48:07 AM

PATRICK GALVIN, Commissioner, Department of Revenue (DOR), explained the changes made to HB 177 in Version E. He directed the committee's attention to page 2, lines 22-24, which reads in part:

... however, the state's contribution may not exceed 50 percent of the qualified expenditures incurred before the end of the first binding open season ...

COMMISSIONER GALVIN said that the changes are to capture the concept that the license applicant can suggest a state contribution amount within the limits stated. On page 2, line 30 there is a language change to "is incurred" from the previous language of "cost occurs." The section on abandonment is now Section 240 of the bill, and the numbering has changed from the original version. On page 3, lines 18 to 19, there is an added clause allowing the commissioners to use "technical advisors" as independent contractors to assist in application development and evaluation.

8:52:39 AM

COMMISSIONER GALVIN continued to page 3, lines 22-24, and explained that DOR had suggested inserting some restrictions on appellate rights of the participants by incorporating limitations already in the state's procurement code. However, legal counsel explained that language in the state's procurement codes does not exactly match that in HB 177. Therefore, the provision provides the commissioners the authority to adopt regulations regarding appeal rights substantially similar to those in the procurement codes. He explained that changes on page 4, lines 5-6, concern the requirement that an applicant provide for the receipt and delivery point of gas before an open season has occurred. He said the applicant is not expected to provide information as to in-state delivery points in the

license application. In reference to page 4, lines 18 to 22, he explained that in the original bill there was language detailing what the applicants must provide in terms of the tariff rates and transportation services. He said there was language in that section concerning a liquefied natural gas (LNG) project that was intended to apply to a project in Canada or an LNG project. He offered that the language has been modified on page 5, line 1 to clarify some of the requests made of an LNG applicant. In response to a question, he said that the changes take the concept of proposed transportation services and expand on it to provide additional clarity and application to both Canadian and LNG projects.

[8:56:43 AM](#)

COMMISSIONER GALVIN went on to explain the changes on page 5, lines 14 and 28. He said that the original bill had a 36 month deadline in which to have an open season, the suggested amendment shortens that time to 24 months. He noted a change on 4, lines 1-2, which references a statute that prohibits an "over the top route" as described in AS 38.35.017(b).

[8:58:42 AM](#)

COMMISSIONER GALVIN said that there are changes made to page 6, line 9, to clarify that section with respect to required technical information. Page 6, line 16, incorporates a stylistic change that recognizes the normal sequence of events with regard to gas pipeline compression and pipe additions. Moving on to page 7, line 18, he explained that the changes require the applicant to describe how they propose to address a North Slope gas treatment plant, and reminded the committee that there is an inherent option for an applicant to propose a gas treatment plant as part of their transportation system. If an applicant is to include a gas treatment plant in its system, it would have to use the same debt to equity ratio required by the state. On page 7, line 26 a reference is added to require an applicant to propose not only a percentage, but a "total dollar amount" of the state's contribution under AS 43.90.110(1). This allows the state to examine what the applicant intends to spend to arrive at an open season. He responded to a question by explaining that DOR desires the applicants to at a minimum provide an estimate of costs to be spent in preparation for open season so that the state can have some basis from which to gauge the potential net present value of the project. He stated the state would like to gauge whether the applicant would have a

"breaking off point" depending upon the success of the open season, and how much the state may have to spend, he explained. He responded to a further comment by indicating that DOR is willing to discuss the need to place parameters on the applicant's ability to exceed their stated spending limit for that phase of the project.

[9:03:59 AM](#)

COMMISSIONER GALVIN explained that there is a possible error on page 7, lines 27 and 28 which refers to AS 43.90.110(1) and (2) and opined the reference should be to AS 43.90.110(1)(a) and (b). He stated that the intent of this change was to reference the 50 percent contribution up to open season and the post-open season sections of the bill.

[9:05:31 AM](#)

COMMISSIONER GALVIN referred to three new subsections on page 8, which read [original punctuation modified slightly for clarity]:

...(16) waive the right to appeal the award to another applicant or the determination under AS 43.90.180(b) that no application merits the issuance of a license;

(17) commit to negotiate, prior to construction, a project labor agreement, to assure expedited construction and labor stability for the project by qualified residents of the state;

(18) commit that the state contribution received by the licensee may not be included in the applicant's rate base and shall be used as a credit against the licensee's cost of service; ...

COMMISSIONER GALVIN explained that the intent of section 16 is to require an applicant to waive their right to appeal an adverse decision. Section 17 was suggested by DOR and is intended to require applicants to set forth that they will commit to negotiate project labor agreements.

CHAIR KOHRING suggested that proposed section 17 might be a point of contention by some members of the committee, but noted its addition allows the committee to consider it.

[9:07:31 AM](#)

REPRESENTATIVE DOOGAN asked if the term "project labor agreement" has a generally accepted meaning, or whether the phrase can have a range of meanings.

COMMISSIONER GALVIN said he was unaware of whether there was a specified meaning to the aforementioned term. He went on to explain that section 18, line 23 is a technical change to confirm that any state contribution to the project would be deducted from the rate base.

COMMISSIONER GALVIN explained that Version E contains changes suggested by DOR, by the chair and by legislative legal counsel. He directed the committee's attention to page 9, section 150 which read [original punctuation provided]:

Sec. 43.90.150. Proprietary information and trade secrets. (a) At the request of the applicant, information submitted under this chapter that the applicant identifies and demonstrates is proprietary or is a trade secret is confidential and not subject to public disclosure under AS 40.25 unless the applicant is granted a license under this chapter; after a license is awarded, all information submitted by the licensee under this chapter shall be made public.

(b) If the commissioners determine that the information submitted by the applicant is not proprietary or is a trade secret, the commissioners shall notify the applicant and return the information at the request of the applicant.

(c) An applicant that protests or appeals the award of a license or the process by which the award of a license is made shall be considered to have consented to the disclosure of all of the information submitted under this chapter by the applicant making the protest or appeal, including information that is confidential under (a) of this section.

(d) In this section, "proprietary" means that the information is treated by the applicant as confidential and the public disclosure of that information would adversely affect the competitive position of the applicant, or materially diminish the commercial value of the information to the applicant.

COMMISSIONER GALVIN explained that this section covers the treatment of an applicant's confidential information. The

section is designed to capture the concept that once a license has been issued, all information is public.

REPRESENTATIVE SAMUELS asked if whether the legislature would be aware that there was information that it did not have access to when reviewing the commissioners' license issuance recommendation.

COMMISSIONER GALVIN answered yes, and noted that the applicant must provide a public summary of the information it desires be considered confidential. He explained in response to a question that the sort of information that may be confidential could include the potential methods that pipeline companies may propose with others to share risks between themselves and the shippers.

REPRESENTATIVE DOOGAN expressed concern that keeping some information confidential will make it difficult for the public at large to evaluate the adequacy of the selection process.

COMMISSIONER GALVIN stated that there would likely not be much confidential information relevant to the actual value of the gas pipeline project to the state. He opined that most of the information likely to be in the confidential arena is information that weighs more on the likelihood of project success.

REPRESENTATIVE DOOGAN said that throughout these hearings people have been using "risk" as a code word for how much money they are going to have to pay. He asked whether the amount a shipper would have to pay would be part of evaluation process.

COMMISSIONER GALVIN opined that the issue of risk is a combination of how much an applicant is going to have to pay, and the level of uncertainty the applicant must bear. He suggested that the level of information that will be available to the public will provide a "clear band" around the range of criteria. He set forth that DOR is attempting to craft a procedure that is as transparent as possible and has very few confidential aspects. He relayed that the confidential information would not be the driving factor in the license award decision.

[9:22:04 AM](#)

REPRESENTATIVE SAMUELS asked about the situation where confidential information sets forth a proposal that the

applicant eventually does not enact and questioned whether that information would ever become public knowledge.

COMMISSIONER GALVIN responded that under the current proposal, any information that was confidential would be made public as soon as the legislature approved of the license issuance.

REPRESENTATIVE DOOGAN expressed his concern that under the current proposal, only the successful applicant's information is made public while the information in the unsuccessful applications remains confidential.

COMMISSIONER GALVIN replied that the intent is not to draw distinctions between public and non-public information. He offered that the bid parameters of an unsuccessful applicant are not normally made public. He stated that the bill attempts to be sensitive to normal business dynamics, and noted that a challenger to the license award would also have its information made public.

COMMISSIONER GALVIN explained that the intent behind the application evaluation and ranking criteria, AS 43.90.170, is to provide more structure to the determination of which application provides the most net present value to the state and the greatest likelihood of success.

[9:30:43 AM](#)

REPRESENTATIVE SAMUELS asked about the meaning of the section on page 11, line 16 which reads [original punctuation provided]:

(d) In this section, "net present value" means the discounted value of a future stream of cash flow ...

COMMISSIONER GALVIN suggested this section be addressed by the DOR's economists.

[9:32:53 AM](#)

COMMISSIONER GALVIN reviewed proposed AS 43.90.180 which read [original punctuation provided]:

Sec. 43.90.180. Notice to the legislature of intent to issue license; denial of license. (a) If, after evaluation of complete applications under AS 43.90.170 and consideration of public comments received under AS 43.90.160, the commissioners and the coordinator

determine that an application proposes a project that will sufficiently maximize the benefits to the people of this state and merits issuance of a license, the commissioners shall

(1) issue a determination, with written findings addressing the basis for the determination; the determination becomes a final agency action in accordance with AS 43.90.190;

(2) publish a notice of intent to issue a license that includes findings addressing the basis for the determination; and

(3) submit the determination along with the findings, supporting documentation, and a copy of the notice published under (2) of this subsection to the chairs of the legislative standing committees having jurisdiction over natural resources for action as provided in AS 43.90.190.

(b) If the commissioners determine that no application proposes a project that sufficiently maximizes the benefits to the people of this state and merits issuance of a license, the commissioners shall issue a written notice of that determination and the findings on which the determination is based.

(c) The commissioners' determination under this (b) of this section is a final agency action for purposes of appeal to the superior court.

(d) Within 90 days after a determination under (b) of this section, the commissioners may issue a new request for applications for a license under AS 43.90.120.

COMMISSIONER GALVIN noted there is a reference within the evaluation criteria which references the section on public comment. He went on to say that the next area with a substantive change is on page 12, line 11 which reads [original punctuation provided]:

Sec. 43.90.190. Legislative approval; issuance of license. (a) After receiving a determination from the commissioners under AS 43.90.180, the House standing committee and the Senate standing committee having jurisdiction over natural resources shall introduce a bill in their respective chambers that provides for the approval of the license proposed to be issued by the commissioners.

(b) If a bill approving the issuance of the license becomes law, the commissioners shall issue the license as soon as practicable after the effective

date of the Act approving the issuance of the license. The issuance of the license approved by the legislature is a final administrative action on the date the license is issued for purposes of appeal to the superior court.

(c) If the legislature fails to approve the issuance of the license, the commissioners may request new applications for a license under AS 43.90.120.

9:35:10 AM

COMMISSIONER GALVIN explained that this provision was at the request of the committee chair and requires approval of the issuance of the licenses in the form of a bill. .

CHAIR KOHRING set forth that nothing in the aforementioned section is "rock solid," but just something for consideration.

9:36:36 AM

COMMISSIONER GALVIN referred to page 11, line 21, which proposes that the Alaska Gasline Inducement Act (AGIA) coordinator be added to the review process. In response to a question, he noted that the timing of the hiring of the AGIA coordinator still needs to be evaluated.

CHAIR KOHRING set forth there needs to be a procedure if the two commissioners cannot agree.

COMMISSIONER GALVIN expressed confidence that the governor will make decision should the commissioners be unable to come to a unified decision.

9:38:21 AM

COMMISSIONER GALVIN noted that language on page 12, lines 25-26, is intended to clarify that the obligation to take certification either from Federal Energy Regulatory Commission (FERC) or the Regulatory Commission of Alaska (RCA) does not become an obligation until after all the administrative appeal rights have been exhausted by the applicant.

COMMISSIONER GALVIN explained that changes on page 13, lines 19-20 clarify when the time starts to run for purposes of appeal. Changes on page 13, lines 27-28 set forth that [original punctuation provided]:

... An amendment or modification approved under this section must be consistent with the requirements in AS 43.90.130 and may not diminish the value to the state of the project or the like likelihood of success for the project.

COMMISSIONER GALVIN summarized that the aforementioned section is to ensure that the project value or likelihood of success is not diminished if the project terms are modified.

[9:41:29 AM](#)

REPRESENTATIVE SAMUELS asked about the situation where a modification decreases the value to the state, but increases the likelihood of project success.

COMMISSIONER GALVIN opined that such a modification should not be allowed.

REPRESENTATIVE SAMUELS asked about the criteria which determine when the value to the state is diminished.

COMMISSIONER GALVIN responded that decisions on modifications are intended to be referenced back to the initial evaluation criteria, therefore would use the same criteria as in the initial evaluation process.

[9:42:54 AM](#)

COMMISSIONER GALVIN said that technical changes made to AS 43.90.210 are designed to clarify that the scope of the commissioners' ability to require the production of information is related only to the license procedures of AGIA. He explained that modifications on page 15, line 23, concern remedies available to the commissioners if a licensee has violated the license terms. One remedy is to allow the state to acquire the work product from the licensee. In other similar sections of the bill, language has been clarified to make clear that only the work product developed during the license period is available to the state. He explained that AS 43.90.240 covers the procedure for abandonment of the project and contains some modifications suggested by DOR regarding the process of arbitration. He said the DOR is continuing to craft language defining the term "uneconomic." If the project is determined to

be uneconomic, the state could acquire the work product at the applicant's net cost, he explained.

[9:48:06 AM](#)

COMMISSIONER GALVIN said that AS 43.90.250 covers the position of AGIA coordinator and has been modified at the request of the chair to place the position in the governor's office, to clarify the appointment process, and to further delineate the responsibilities of the position. The AGIA coordinator is subject to legislative confirmation and to reconfirmation after a gubernatorial election.

[9:50:29 AM](#)

COMMISSIONER GALVIN set forth that AS 43.90.260 has been moved from Article 3, but has not been changed. He said that all the upstream inducements in Article 3 of HB 177 have been modified to make it clear that they are all contractual in nature. The language on page 18, lines 12 and 13 which states the "inducement[s] in AS 43.90.310 and 43.90.320 are contractual" provides a clear statement of that intent, he indicated. AS 43.90.310 covers the royalty inducement provisions of AGIA. He said that 43.90.310(c) consists mostly of new language that is intended to create a contractual relationship. He offered that the intent of this section is to have a regulatory method to establish valuation for purposes of upstream determinations. The applicant will have the option to have that alternate methodology put into their contract, he explained. Although the regulations may change to update the method used, each time the lessee will have the option as to whether to change its lease terms.

[9:54:18 AM](#)

COMMISSIONER GALVIN explained that language was added on page 20, line 27 authorizing the commissioner of DOR to sign a certificate regarding the proposed production tax exemption. He disclosed that legislative legal counsel does not support this approach because of concerns regarding its constitutionality.

The committee took an at-ease from [9:55:57 AM](#) to [9:56:01 AM](#).

CHAIR KOHRING recessed the House Special Committee on Oil and Gas meeting at a call of the chair at [9:56:49 AM](#).

[The motion to adopt Version E as a work draft was left pending with objections by Chair Kohring and Representative Doogan.]

12:36:07 PM

CHAIR KOHRING reconvened the House Special Committee on Oil and Gas meeting. Present at the reconvening were Representatives Samuels, Doogan, Kawasaki, Olson, and Kohring. Representative Dahlstrom arrived as the meeting was in progress. Representative Coghill was also in attendance.

12:36:34 PM

COMMISSIONER GALVIN reviewed Article 4, page 21, lines 16 to 18 which reads [original punctuation provided]:

... Money appropriated to the fund may be spent for the purposes of the fund without further appropriation. Appropriations to the fund do not lapse under AS 37.25.010, but remain in the fund for future disbursements. Nothing in this subsection creates a dedicated fund ...

and explained the modifications were suggested by legislative legal counsel. Furthermore, changes were made to proposed AS 43.90.410 because the existing administrative code is not designed to allow two commissioners to jointly adopt regulations. The proposal allows the commissioner of revenue to adopt the regulations for decisions made jointly by the commissioners of Department of Natural Resources (DNR) and DOR, he explained. The clause "before the commencement of commercial operations" clarifies the cut-off for when the assurance that the state will not provide benefits to a competing project expires, and is added on page 22, line 16. The intent is to add a "stay faithful" clause to the deal which ends once the gas pipeline begins operations, he explained. A definition of competing project is added on page 22, line 30, and states [original punctuation provided]:

(b) In this section, "competing natural gas project" means a project designed to accommodate throughput of more than 500,000,000 cubic feet of North Slope gas a day.

COMMISSIONER GALVIN explained that this provision is to allow for in-state gas volumes to proceed without violating the nature of the "faithful" clause. He went on to explain that on page

23, line 7, the phrase "diminish the likelihood of success" was added as a factor to consider when determining whether a licensee can assign its license. There is also a change on page 23, line 21 to make clear that any job training program need not be limited to jobs on the gas pipeline project, but can include related vocational training. A definition of "North Slope" was added on page 24, line 30 and 31. Further changes in definitions include the addition of the word "financial" before commitments on page 25, lines 13 and 14. A conforming amendment was made on page 25, line 3. Further language on page 27, line 22, concerns language added by counsel regarding confidentiality and reads [original punctuation provided]:

(12) records that are
(A) proprietary or a trade secret in
accordance with AS 43.90.150;
(B) applications that are received under
AS 43.90.120 - 43.90.140 until notice is published
under AS 43.90.160.

[12:44:53 PM](#)

COMMISSIONER GALVIN further noted that Section 5, page 27 sets forth the legislative intent that the first request for license applications be issued within 90 days after the effective date of AGIA, a requirement that was previously set forth as a mandatory requirement. He explained that a severability clause regarding the upstream tax inducement provisions was inserted to insure that even if the production tax exemption was found to be unconstitutional, the remainder of AGIA would still be valid.

The committee took at ease from 12:48 to 12:52.

[12:53:21 PM](#)

DON BULLOCK, Attorney, Legislative Legal Counsel, Legislative Legal and Research Services, Legislative Affairs Agency, said the structure of AGIA remains basically the same.

REPRESENTATIVE SAMUELS asked about the change regarding the amount of money the state would match up to open season, noting it went from 80 percent to 50 percent. [Version E, page 2, lines 22 to 24.]

MR. BULLOCK explained that prior language provided that the state would match contributions made by the licensee equally up

until the end of the first binding open season, but it was not clear whether there would be any funds left at the end of open season. Under the revision, the applicant will put forth the amount of matching funds they propose to receive in the first period, with the limitation it not exceed 50 percent of the qualified expenditures incurred before the end of the first binding open season.

[12:55:59 PM](#)

MR. BULLOCK explained that in AGIA, "North Slope" is defined as North of 68 degrees North latitude, whereas federal law relating to the natural gas act uses a marker of North of 64 degrees North latitude. He noted that there are constitutional issues regarding the separation of executive and legislative powers relating to contract approval and regarding the confirmation of the AGIA coordinator. He relayed that the courts have narrowly construed provisions regarding the ability of the legislature to appoint commissioners. He noted that the AGIA coordinator position "does not fit easily" into the constitutional provisions that provide for legislative confirmations. He reminded the committee of his earlier testimony that the 10 year tax exemption was likely to be constitutional because it was a matter of general law, subject to future legislative change.

[12:58:37 PM](#)

REPRESENTATIVE DOOGAN asked if the problem with the constitutionality of the confirmation of the AGIA coordinator would be lessened if confirmation was only for the initial appointment.

MR. BULLOCK replied that was not the issue, rather the issue is whether the confirmation is required at all. The AGIA coordinator position is to be in the governor's office.

[12:59:42 PM](#)

REPRESENTATIVE DOOGAN asked if the constitutional issue changes if the tax exemption is based on the volume of gas rather than period of time.

MR. BULLOCK replied that it could be. He noted that the Alaska State Constitution, Article IX, Section 1, and Article IX, Section 4 appear to allow the legislature to enact some tax exemptions by general law.

1:01:46 PM

REPRESENTATIVE DOOGAN reiterated his question as to whether an exemption based on volume is more likely to withstand constitutional scrutiny than one based on time.

MR. BULLOCK replied that a period of time would deal with how long the legislature wanted to allow the exemption. He offered that an exemption is different than credit because an exemption states the taxpayer is not subject to tax, while a credit states that a calculated tax will be reduced.

1:02:40 PM

REPRESENTATIVE SAMUELS asked about drafting the contracts to provide flexible royalty rates which would increase or decrease in conjunction with other tax issues.

MR. BULLOCK noted that a royalty is not a tax, but a share of ownership and that share is negotiated at the time of the lease. He noted that while there may be some changes to the royalty provisions in the state leases, which the lessee may seek to add to the lease. Change would be considered a revision of the lease and be a new contract, he explained.

1:05:17 PM

REPRESENTATIVE SAMUELS asked about the ability to incorporate a flexible royalty rate to balance a possible rise in taxes and the possibility that such an approach would be less likely to be unconstitutional.

MR. BULLOCK replied that royalty terms are contractual terms that are negotiated between the parties. He indicated the lease could have a reference to any measure that would adjust for the lease amounts. He noted that the royalty provisions tax the activity of producing oil and gas, measured by the value. He reminded the committee that the state only gets a portion of royalties from federal land as it is not an owner on those lands.

1:07:40 PM

REPRESENTATIVE DOOGAN asked whether there is a benefit to including inducements as contractual royalty terms within the lease instead of structuring inducements as a production tax exemption that may face a constitutional challenge.

1:08:38 PM

MR. BULLOCK agreed with the aforementioned point. He went on to say that since the state is constitutionally required to be a good steward of its natural resources, there is a perception that royalty incentives could be inconsistent with the stewardship responsibilities. He opined that "royalties would definitely be safer." He reminded the committee that there are constitutional provisions which restrict the impairment of contractual terms.

1:09:08 PM

REPRESENTATIVE DOOGAN asked if lowering the state's royalty share in current contracts would be considered an impairment of contractual terms.

MR. BULLOCK stated he was not sure, noting that in the aforementioned example, the state's interests would be impaired.

MR. BULLOCK explained that the lease abandonment provisions have been moved to be within a more appropriate place within the structure of the bill. He referred to AS 43.90.110 on inducements as "where that 50 percent cap comes in." He went on to note that in Version E the state takes the position as coordinator of vocational training, noting that there is also a new section regarding the development of a training program. He explained that a change in AS 43.90.110 requires the commissioner of DOR to consult with the commissioner of DNR to adopt regulations to enhance the definition of qualified expenditures for purposes of the state's matching contribution. Other changes include some re-numbering because the abandonment provisions of the bill were moved to another section of the bill. He opined that there were legal problems with the prior requirement that the commissioners issue a request for application for the license within 90 days of the effective date of the act. To remedy this, this section was changed to indicate that the commissioners must do it "as soon as practical." He said there is an un-codified section at the end of the bill setting forth that legislative intent is that the commissioners act within 90 days of the effective date of the act.

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MR. BULLOCK explained that there was some desire to use the existing state procurement code provisions to award the license and govern appeals. However, he explained that there are a number of terms in the procurement codes that would be difficult to apply to the gas pipeline project. Therefore, he suggested that the commissioners are required to adopt regulations substantially similar to those in the existing state procurement codes. AS 43.90.130 has been modified to be more affirmative in that the applicant is making the commitments listed in the application, he explained. The "over the top route" through the Beaufort Sea and down through the McKenzie, has specifically been excluded, he said. He said this exclusion still leaves room for highway routes and an in-state route to tidewater. He explained that the time period for arriving at the end of open season is shortened from 36 months to 24 months. He indicated this a target date, which requires the licensee to move a bit faster.

CHAIR KOHRING noted that he had suggested this change with the intent to move things up a bit.

MR. BULLOCK stated that there is flexibility to change the law if it becomes apparent that the suggested time periods are problematic. He noted that changes had been made to recognize that expansion would likely first involve compression, and then pipeline looping later.

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REPRESENTATIVE SAMUELS asked if the time period would be in the contract, which the legislature could not change.

MR. BULLOCK opined that the applicant has the option to complete the work under the time period set as well as the flexibility to request more time.

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REPRESENTATIVE DOOGAN asked if the statute and the contract would have to be changed if the licensee needs a longer time period than 24 months.

MR. BULLOCK agreed that the terms of the law would have to be changed to grant the licensee additional time. He put forth that there is a requirement that the applicant commit not to protest the award of the license to another applicant, or a

determination by the commissioners not to issue a license to any applicant.

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REPRESENTATIVE DOOGAN asked if the term "project labor agreement" in AS 43.90.130(17) has legally defined meaning.

MR. BULLOCK said that the term is not defined in Alaska statutes, but that there is a case where a project labor agreement was upheld. He recalled that in a footnote, the court set forth a definition for the term. He stated it is a contractual provision whereby laborers are identified and agree not to strike in return for the benefits of the contract. He said that project labor agreements raise some "right to work" constitutional issues, but that an Alaska Supreme Court case affirmed the use of a project labor agreement in a case from Fairbanks. In response to a question, he explained that the Fairbanks case has some differences as it involved public monies for a public contract. The gas pipeline situation involves public money going to develop a project, and he has not researched the possible effect of these differences on the court's holding as applied to the project labor agreement section of AGIA.

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MR. BULLOCK reviewed section 43.90.140 regarding the appointment of an AGIA coordinator and stated the intent was to add a third person to the decision making process.

REPRESENTATIVE DOOGAN set forth that his expectation is that the governor will be the ultimate decision maker, and asked whether it is possible to structure AGIA so the commissioners make a recommendation, but the governor makes the actual decision of who to award the license to.

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MR. BULLOCK indicated there is no legal reason not to proceed as stated in the aforementioned method, but noted that there is some separation of powers issues, although the commissioners do work for the governor.

REPRESENTATIVE DOOGAN opined that since the governor is elected and will likely be the one actually making the final

determination, it may be preferable to state explicitly that the governor makes the final decision.

MR. BULLOCK stated Version E makes sets forth that the commissioners are entitled to seek additional information from applicants related only to the application itself. AS 43.90.150 concerns information the applicant wishes to keep confidential and includes a definition of "proprietary." The commissioners make the determination and can require a summary of the information. Upon appeal, an applicant's information is no longer confidential, he explained. AS 43.90.160 covers notice, review, and comment by the public and relates to all the applications the commissioners have reviewed and found acceptable. He stated the work of Representative Dahlstrom's committee is reflected in AS 43.90.170 so as to make the criteria for review more directed as to what the state can expect from the project. He opined that this approach brings back the focus that the greatest benefit will be at the well-head value. He opined that the criteria have been crafted to determine how capable the applicant is and how likely it is the applicant will be able to build the pipeline. He offered his belief that this section is one of the most important pieces of the bill as it gives the commissioners the basis on which to review applications to make a recommendation.

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REPRESENTATIVE SAMUELS asked about the definition of "net present value" as the "discounted value of a future stream of cash flow" on page 11, line 16-17. He opined that his inclination is to set specific numbers as the current definition may be somewhat subjective.

MR. BULLOCK replied that he thinks it is reasonable, noting there are presumptions made to the net present value calculation and perhaps this is the appropriate place to do it. He suggested that the commissioners could approach this through regulation, which can be more responsive to change than parameters set in statute.

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MR. BULLOCK reviewed AS 43.90.180 which sets forth the procedure for legislative approval of the commissioners' recommendation. The process for legislative approval set forth in AS 43.90.190 is that the chairs of the committees that received the bills will introduce a bill to approve the issuance of the license.

This is a change from the original bill which was set up so that if the legislature did nothing, the license would be issued. Version E requires the legislature to consider and a pass a bill for the license to be issued. He suggested this resolves some of the timing issues in the original bill, because as a bill, it would carry over into the next legislative session.

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REPRESENTATIVE DOOGAN asked about the procedure if the bill did not pass in regular session, but there was a special session. He queried whether the bill would be taken up from the last committee of referral, or whether it would have to "go back to square one."

MR. BULLOCK replied that new bills are introduced in special session. He opined that there is flexibility in the rules, but in general new bills are introduced in special session.

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REPRESENTATIVE SAMUELS asked why the request for a bill approving the license would not just be given to the House and Senate standing rules committees, referring to page 12, line 13.

MR. BULLOCK answered that it could be set up that way, noting that other committees can request bills introduced to the rules committees.

REPRESENTATIVE SAMUELS asked if it was possible to increase the time limits, or set forth a calendar day limit to accommodate possible scenarios.

MR. BULLOCK replied that a calendar day approach was possible, but opined that there is flexibility in the legislative organization now to manage the bill. He opined that the "day requirement" raises problems as to when the legislature receives the bill relative to the end of the session.

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REPRESENTATIVE SAMUELS expressed concern that the political dynamic could slow down approval of the bill. He indicated there should be some sort of deadline for a vote.

REPRESENTATIVE DOOGAN set forth that his understanding that once the bill for approval is introduced, it would not be until after

the next election and a new legislative session that one could definitively say the legislature failed to adopt the bill.

MR. BULLOCK agreed with the aforementioned statement, noting that the bill "would be dead" if not passed by the end of the second legislative session after introduction. The bill could also not pass by being voted down, he noted. He indicated that this provision contemplates that the legislature reviews the commissioners' determination that the recommended project is the one that maximizes benefit to the state. AS 43.90.200 covers certification by regulatory agencies and requires the licensee accept the certificate issued by the regulatory agency only after all rights relating to appeal are expired.

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MR. BULLOCK went on to say that a financial commitment is required, opining that the intent is to make sure the licensee is making a firm commitment to go forward with the project. AS 43.90.210 concerns amendments or modifications to the project plan and adds that any changes may not "diminish the value to the state of the project or the likelihood of success for the project."

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REPRESENTATIVE SAMUELS referred to a past failed refinery project in 1980 which resulted in a state debt of around \$70 to \$80 million. He expressed concern that the modification terms as set forth in the statute are subjective terms which will require negotiation and indicated his desire for assurances that a modification will not result in project failure.

MR. BULLOCK indicated he could not offer that assurance through a specific provision, but said that the section of the bill on ranking and criteria offers a system to really test the projects viability. Furthermore, the commissioners have the ability to request further information. He noted that if something occurred to put the project's economic viability in jeopardy, there are provisions in the modification section of the bill to allow the state to consider ways to salvage the project.

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REPRESENTATIVE SAMUELS noted modification would occur after the license was issued, and without legislative review.

MR. BULLOCK suggested that a provision could be added to require legislative review of substantial modifications to the contract terms.

REPRESENTATIVE DOOGAN opined that language in AS 43.90.210 regarding likelihood of success does not necessarily mean a "net present value" calculation as contemplated under AS 43.90.170. He opined that as written, Section 210 would include consideration of non-monetary value. He suggested that modifying this provision to mean "net present value" may tighten it up somewhat.

MR. BULLOCK agreed that a "best interest" concept can include many factors, noting the legislature may structure such provisions to emphasize factors it considers most important.

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REPRESENTATIVE DOOGAN suggested that the criteria to determine whether a modification should be allowed be the same criteria used to make the initial license award.

MR. BULLOCK suggested the modification section could refer to the initial criteria section. He explained that AS 43.90.220 provides the state the ability to account for funds spent. The language recognizes that parties besides the licensee may be making the expenditures. He said that it is still unclear as to how the state's contribution of \$500 million is to be paid as a matching contribution, or as reimbursement to the licensee for funds spent. AS 43.90.230 provides that the commissioners determine, through administrative hearing, whether there has been a license violation and a cure thereof. Project abandonment is covered by AS 43.90.240 and is based on a finding that the project is uneconomic. Version E incorporates use of an arbitrator from the American Arbitration Association to determine whether the project is indeed uneconomic. That determination is then filed in the court, he explained.

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CHAIR KOHRING asked whether "uneconomic" is defined in the bill.

MR. BULLOCK replied that this determination comes back to the value and expected rate of return for the project. He noted that the tariff will have a rate of return built in to it, but opined it will not mean much if there is an insufficient volume of gas.

REPRESENTATIVE SAMUELS noted that economic evaluations may differ between companies based on differing business focuses.

REPRESENTATIVE DOOGAN asked if this determination was limited to the economics of project itself.

MR. BULLOCK replied that the project itself and its benefits to the state intertwine because of policy decisions made in the determination of the license award. He said there is nothing in HB 177 that precludes development of another project should the first licensee abandon its project.

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MR. BULLOCK reviewed the inducement sections of the bill, noting that they are intended to be contractual. He explained that DNR will determine how the royalty provisions will work.

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REPRESENTATIVE DOOGAN asked about the possible constitutional problems with AS 43.90.320, the gas production tax exemption section.

MR. BULLOCK opined that the tax exemption approach in Section 320 definitely raises a constitutional issue under Section IX of the Alaska State Constitution. He offered that putting a taxation provision in the contract could bring up the constitutional provision against impairment of contracts. He said it is a matter of opinion as to how a court will rule, but opined that the court would not look favorably upon contracting away the power to tax. He noted that the Alaska Constitution is crafted to allow the legislature to have considerable financial flexibility. He noted that there is a desire to give fiscal certainty to business interests, and that the ultimate decision-maker may be the courts.

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MR. BULLOCK explained that Article 4 of AGIA concerns miscellaneous provisions. He explained that under AS 43.90.400, once the matching contribution amounts are appropriated, they will not lapse, but will be available to the commissioners in a non-dedicated fund. Under Article 4, the state assures the licensee it will not extend favorable treatment to another party. License transfers are allowed in certain conditions as

set forth in AS 43.90.450. He emphasized that a transfer of the production tax exemption must also include whatever committed capacity that transferor has in the pipeline, referring to page 17, lines 13-17. He explained that Section 5 on page 27 expresses the statutory intent that the commissioners issue a request for applications within 90 days after passage of AGIA. He said that a severability clause is included, although courts recognize the concept of severability even without a specific provision in the statute.

CHAIR KOHRING said that HB 177 would be held in committee. [Representative Dahlstrom's motion to adopt Version E as a work draft was carried over for consideration at the next meeting.]

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 2:15 p.m.