

**ALASKA STATE LEGISLATURE
LEGISLATIVE BUDGET AND AUDIT COMMITTEE**

February 17, 2009

5:11 p.m.

MEMBERS PRESENT

Senator Kevin Meyer, Chair
Representative Nancy Dahlstrom, Vice Chair
Senator Lyman Hoffman
Senator Charlie Huggins
Senator Linda Menard
Senator Bert Stedman
Senator Donald Olson (Alternate)
Representative Mark Neuman
Representative Bill Thomas
Representative Mike Doogan
Representative Bill Stoltze (Alternate)
Representative Chris Tuck (Alternate)

MEMBERS ABSENT

Representative Mike Hawker

COMMITTEE CALENDAR

APPROVAL OF MINUTES
REVISED PROGRAM - LEGISLATIVE (RPLs)
OTHER COMMITTEE BUSINESS

PREVIOUS COMMITTEE ACTION

No previous action to record

WITNESS REGISTER

PAT DAVIDSON, Legislative Auditor
Legislative Audit Division
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Provided an explanation for the analysis of the Alaska Energy Authority (AEA) process for the grant allocation for the Alaska Renewable Energy Fund.

STEVE HAAGENSON, Executive Director
Alaska Energy Authority (AEA)
Anchorage, Alaska

POSITION STATEMENT: Answered questions regarding the proposed grant allocation for the Alaska Renewable Energy Fund.

RICHARD GAZAWAY, Hearing Examiner
Regulatory Commission of Alaska (RCA)
Anchorage, Alaska

POSITION STATEMENT: Testified about the RCA certification process.

ACTION NARRATIVE

[5:11:07 PM](#)

CHAIR KEVIN MEYER called the Legislative Budget and Audit Committee meeting to order at 5:11 p.m. Senators Meyer, Stedman, Hoffman, Huggins, and Menard and Representatives Thomas, Neuman, Doogan, Dahlstrom, and Stoltze (alternate) were present at the call to order. Representative Tuck (alternate) and Senator Olson (alternate) arrived as the meeting was in progress.

APPROVAL OF MINUTES

CHAIR MEYER announced that the first order of business would be to approve the minutes of the February 4, 2009 meeting.

REPRESENTATIVE DAHLSTROM made a motion to approve the minutes of February 4, 2009. There being no objection, the minutes from the meeting of February 4, 2009 were approved.

REVISED PROGRAM - LEGISLATIVE (RPLs)

RPL 08-09-0137

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CHAIR MEYER announced that the next order of business would be consideration of RPL 08-09-0137. He noted that at the February 4, 2009 committee meeting, the Legislative Audit Division was asked to review the Alaska Energy Authority (AEA) process for the Alaska Renewable Energy Fund grant allocations; to determine, for five projects, if it met the requirements of House Bill 152 and to confirm that AEA followed the evaluation process as outlined at the Legislative Budget and Audit Committee on February 4, 2009; and to analyze whether the information gained during the AEA evaluation process was

sufficiently comprehensive and complete. He reiterated that this was a review of the process, and not an audit.

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PAT DAVIDSON, Legislative Auditor, Legislative Audit Division, Alaska State Legislature, said that she appreciated the cooperation of AEA. She provided a summary of the memorandum dated February 17, 2009. [Included in members' packets] She reported that the analysis did not reveal any of the issues addressed in the memorandum to be "fatal flaws in the process." She identified that these issues were a cumulative risk to the successful completion of the project. She defined project success as a project completed on time, on budget, and able to produce the expected energy at the projected cost. She reviewed the scope of the project as outlined earlier by Chair Meyer. She summarized that the AEA process did conform to House Bill 152, with the one exception that AEA had not completed the regulation adoption process. She reported that the Legislative Audit Division had analyzed five projects, and that one project had not received the external economic review. She noted that this review was assigned to an economics firm, but it was not completed.

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MS. DAVIDSON explained that the AEA process established goals for the regions and imposed funding caps to distribute money among the projects. She noted that one project was funded higher than the allowable cap. She testified that the AEA methodology allowed its professional judgment to override other considerations.

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REPRESENTATIVE DAHLSTROM asked if the AEA process was in keeping with the guidelines of House Bill 152.

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MS. DAVIDSON replied that these issues were not addressed in House Bill 152, so that there was no compliance problem.

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MS. DAVIDSON reported that although a considerable amount of effort was expended on the economic and technical feasibility

phase, there were no thresholds set for either economic or technical feasibility. She pointed out that project feasibility was reflected in the final score. She observed that \$16.6 million was designated for projects with a cost benefit of less than one. She noted that AEA planned on using the Regulatory Commission of Alaska (RCA) certificate of public convenience and necessity as a method to ensure, for an Independent Power Producer (IPP) applicant, that the benefits of the state's capital investment would actually go to the community residents. She indicated that it was unclear if RCA had the regulatory structure to deal with these IPPs. She offered her belief that the RCA cost and time was not considered in the application review process. She noted that RCA billed its cost to the utilities, and that these review costs were unknown. She pointed out that the memorandum outlined the differences between the AEA process for renewable energy projects and those of other states and federal agencies. She summarized that the AEA process did create a higher than necessary risk for project success, but that the risk could be mitigated with an aggressive grant management process. She explained that this aggressive process would include the creation and enforcement for points of grant termination if the expected progress or outcome was not being obtained.

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MS. DAVIDSON disclosed that the memorandum did not include a discussion with the Legislative Legal and Research Services. She determined that for AEA to transfer money between grant projects, it would need to receive permission from the Legislative Budget and Audit Committee. She noted that this would somewhat limit AEA's flexibility.

CHAIR MEYER asked about the RCA oversight for the IPP applicants.

MS. DAVIDSON responded that it was not clear whether this framework was in place, or what the RCA cost would be.

The committee took an at-ease from 5:27 p.m. to 5:30 p.m.

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CHAIR KEVIN MEYER brought the committee back to order at 5:30 p.m.

REPRESENTATIVE STOLTZE questioned why the project criteria ranking only allocated 5 percent for sustainability.

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MS. DAVIDSON said that sustainability was a factor without a stated criterion or methodology for evaluation. She noted that AEA used professional judgment as its criteria.

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REPRESENTATIVE STOLTZE expressed his concern for the lack of a definition for sustainability, even though the chairman of the Alaska Renewable Energy Fund Advisory Committee was also a member of the Denali Commission. He noted that the Denali Commission had a well defined statement on sustainability and used sustainability as a hallmark for its awards.

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MS. DAVIDSON explained that capital replacement costs were not included in either the economic benefit analysis or the sustainability criteria.

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REPRESENTATIVE STOLTZE reiterated his bafflement for the lack of a definition to sustainability.

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CHAIR MEYER said that the question could also be raised to members of the advisory committee.

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REPRESENTATIVE THOMAS asked for the cost of the [analysis].

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MS. DAVIDSON listed the participants and the time involved, but indicated that she was not aware of the actual cost.

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REPRESENTATIVE THOMAS, in response to Representative Stoltze, expressed his confidence for the projects in his district and he

noted that the majority of the grant recipients were governments and utilities that had been in business "for a while." He expressed his caution toward IPPs and [Limited Liability Company (LLCs)].

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CHAIR MEYER stated that 75 percent of the projects were with utilities and government entities.

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REPRESENTATIVE NEUMAN asked Ms. Davidson to expand on her research into other grant evaluation processes.

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MS. DAVIDSON replied that other evaluation processes for technical feasibility included plans for disposal of project components, independent qualified review for recommendations to technical details, and an additional scoring matrix based on the amount of energy replacement. She relayed that other processes for economic feasibility included requirements that the applicant provide preliminary economic assessment and plans for any additional financing. She allowed that AEA did request the plan for additional financing; however the cap structure "unbalanced that applicant's proposal with regard to the totality of financing." She observed that other processes for sustainability included plans for financial continuance after the funding and replacement plans for capital equipment.

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REPRESENTATIVE NEUMAN expressed his concern with the financial sustainability of the projects.

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STEVE HAAGENSON, Executive Director, Alaska Energy Authority (AEA), explained that House Bill 152 was the guidance for the importance of criteria, and he listed the criteria.

[5:43:01 PM](#)

REPRESENTATIVE NEUMAN asked how to measure the project success for technical feasibility.

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MR. HAAGENSON replied that grant conditions would be included to require monitoring reports for operating and maintenance costs in order to measure the true costs and savings.

REPRESENTATIVE NEUMAN referred to a Department of Natural Resources (DNR) comment that the permitting process for an additional 77 projects "would swamp us" and he asked Mr. Haagenson if there was a plan for this.

MR. HAAGENSON reported that DNR had been a participant during the process, and he offered his belief that not all 77 projects would apply for immediate permitting.

SENATOR HUGGINS reminded Mr. Haagenson of his statement that an acceptable failure rate for the projects was zero. He asked if that standard had changed.

MR. HAAGENSON responded that this had not changed. He clarified his definition of failure to be: "spent all the money and didn't get any results that would be a failure." He pointed out that money would not be distributed until "they have certain things in place." He emphasized that risk could be minimized but not eliminated.

SENATOR HUGGINS referred to the process analysis which stated that "many of these risks could be mitigated with a very aggressive grant management process." He asked if this standard could be fulfilled.

MR. HAAGENSON continued, and said:

We also have been looking at putting on clauses, you know, we found a situation where we were trying to be fair with state money to make sure we weren't discriminating with state money, so for example, we went through on some hydro projects in Southeast and we looked at if they were being interconnected, we thought, how can each of those communities hold on to their resource and make sure that that's really how that they can keep that control. And the concern was that they would lose control of the resource. So my example would be Ketchikan and Wrangell and Petersburg. Wrangell and Petersburg wanted to make sure that they didn't get all the energy from the Tye Project sucked into Ketchikan. When you add on Kake,

you know, how do you bring those people on and off. So, we actually talked through a system called economic dispatch, so if they run out of power, Kake would be the first one that would have to do some claritive action. And then, what would happen is maybe the next cheapest source of power would come on. It may be in Ketchikan. Kake would have to pay for that and get it delivered to them, but you wouldn't just cut them off and say you are on your own now. So, there's ways you can actually work together and we are proposed to do that and what we are recommending now is that they probably need, I think they understand where we are coming from, and I think they need a little time to shake out the details of hydro coordination in the system that's now interconnected in a much bigger system with the Tye line, the Swan-Tye line. And now that's in there, and so we are going to actually take that one off of the grant conditions, because I think they've got the picture. And instead of us trying to force something on them, I think they need to understand how the benefits of hydro coordination will benefit all the entire system, not just one utility. So, it's not a win-lose, it's gonna be a win-win.

SENATOR STEDMAN welcomed the dialogue toward an integrated energy plan for Southeast Alaska. He asked that a system of checks and balances with the Legislative Budget and Audit Committee include six month updates from AEA. He pointed out the need to re-direct funding between projects.

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MR. HAAGENSON agreed that updates should be six months or sooner.

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CHAIR MEYER expressed his concern with small IPPs, and asked if there was intent for RCA approval prior to grant awards.

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MR. HAAGENSON replied that it was how these would be handled. He discussed the options for an IPP waiver application, and raised the question of full regulation or a "lighter version."

He noted that a grant condition for an IPP would be for a RCA certificate of public necessity and convenience.

RICHARD GAZAWAY, Hearing Examiner, Regulatory Commission of Alaska (RCA), relayed that his understanding for an earlier proposed certification process and rate review was not covered by the standard RCA "fitness, willing, and ability" review process. He expressed the need to forward the waiver request to an RCA commissioner.

CHAIR MEYER asked for a definition of "public necessity and convenience."

MR. GAZAWAY responded that RCA was required to find that a service was in the public (indisc.) or that providing a certificate to a public utility meets certain thresholds. He noted that there were exemptions for certain utilities and one such exemption was based on revenue. He explained that this was just the terminology to pronounce the fitness of an applicant to provide the service.

REPRESENTATIVE STOLTZE expressed concern for the ambiguity of Mr. Haagenson's language, and he expressed his desire to hear an absolute commitment from the RCA Commissioner that would protect his constituents who were "down the line customers." He noted that his constituents "want affordable energy" and were not "equally warmed by the green feeling." He voiced his concern for "experimental or trendy projects being integrated in the system that my people will have the privilege of being paid for."

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CHAIR MEYER agreed that the IPP projects should be approved by RCA prior to the grant award.

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REPRESENTATIVE NEUMAN commented on the overabundance of regulations and reflected that many were based on emotion, instead of sound scientific evidence.

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REPRESENTATIVE DOOGAN asked for clarification to the \$16.6 million for projects with a benefit to cost ratio of less than one.

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MR. HAAGENSON explained that AEA was the reviewer for the Denali Commission energy projects, and that the Denali Commission eliminated any projects with a benefit to cost ratio of less than one. He reported that the advisory committee recommended not to have this strict benefit to cost ratio because the guiding principle of House Bill 152 "was to look at the high cost areas first."

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REPRESENTATIVE DOOGAN noted that the cost of oil had decreased which would lower the benefit to cost ratio even more. He asked if this concerned AEA.

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MR. HAAGENSON reminded Representative Doogan of the direction from the legislature to look first at the high cost areas.

REPRESENTATIVE DOOGAN referred to a funding strategy note in the report which declared to "spread the money around." He offered an example from one of the projects that reflected a lack of matching funds, and he asked what would happen if the project could not secure the necessary matching funds.

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MR. HAAGENSON listed a variety of bonds and loans to finance the project. He appreciated the concern for the incursion of a large debt service and allowed that it would be a decision for that project's board.

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REPRESENTATIVE DOOGAN asked what would happen to the grant award if the project could not obtain the remaining necessary funds.

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MR. HAAGENSON said that the money would return to the fund, and Legislative Budget and Audit Committee would be petitioned to reallocate the money to other projects.

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CHAIR MEYER noted that the analysis revealed that an outside auditor had not performed an evaluation for one project. He expressed his concern for any other discrepancies in the process.

MR. HAAGENSON explained that this was an oversight in the assignment of projects. He revealed that AEA had done an internal benefit to cost ratio upon realization that the review had not been assigned. He reported that there were two such incidents.

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MR. HAAGENSON clarified a mathematical error on the cap. He noted that the Delta Junction Wood Chip Heating Feasibility Study, Project 112, had exceeded the cap by \$704,684. He allocated \$190,000 to the McKinley Village Solar Thermal Construction, Project 108. He noted that Takatz Lake Hydroelectric Feasibility, Project 1, would get \$514,684.

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SENATOR HOFFMAN moved to amend RPL 08-09-0137, as follows:

The Fund Allocations for the Alaska Renewable Energy Fund will be adjusted as follows: Project 112 will be reduced by \$704, 684. Project 108 will be increased by \$190,000. Project 1 will be increased by \$514, 684.

There being no objection, the motion passed.

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REPRESENTATIVE DAHLSTROM moved that "any excess funding from projects pulled off the list by either AEA or Legislative Budget and Audit Committee go to those projects next on the master list that were approved for funding but total funds were not available."

CHAIR MEYER objected for the purpose of discussion.

CHAIR MEYER clarified that this motion would transfer any unused funding for a project to the next numerically listed project.

MR. HAAGENSON agreed, but specified that House Bill 152 did not empower AEA to make that transfer without express approval from Legislative Budget and Audit Committee.

REPRESENTATIVE NEUMAN asked for clarification for the reason behind transfer to the next numerically listed project.

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REPRESENTATIVE DOOGAN asked how many more projects would have been approved if there had been enough money.

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MR. HAAGENSON replied that two more projects would have been approved.

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SENATOR STEDMAN expressed his confidence that AEA would be able to fund the two projects not yet approved.

CHAIR MEYER, in response to Representative Neuman, noted that AEA was required to seek approval from Legislative Budget and Audit Committee before any changes in project funding.

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CHAIR MEYER withdrew his objection, and there being no other objections, the motion passed.

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REPRESENTATIVE DAHLSTROM moved for the approval of RPL 08-09-0137, as amended, "with the six month or sooner review by Legislative Budget and Audit Committee on the status of the projects, and that all IPP applicants receive a certificate of public convenience and necessity from the RCA as a grant condition."

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REPRESENTATIVE DOOGAN objected.

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CHAIR MEYER, in response to Senator Hoffman, agreed that this was for RPL 08-09-0137, as amended. He pointed out that this motion included Mr. Haagenon's agreement to return for review of the projects every six months and that any IPP projects would be required to receive the necessary certification from RCA before receiving any state grants.

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REPRESENTATIVE THOMAS asked if the intent of the motion was also to include the recommendation from the Legislative Audit Division that "the risk could be mitigated with an aggressive grant management process."

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CHAIR MEYER acknowledged that this was the intent with the six month review.

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REPRESENTATIVE DOOGAN maintained his objection and asked for a vote.

CHAIR MEYER, in response to Senator Stedman, clarified that this was a motion to move all 77 projects with a review in six months or sooner and the IPP projects would require approval from RCA before the grant is awarded.

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REPRESENTATIVE DOOGAN expressed that his objection was not with the AEA performance but that this was placing "the cart so far before the horse on this that we're gonna get run over by it." He expressed his deepest hope that he was wrong.

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REPRESENTATIVE STOLTZE said that he shared the same concerns as Representative Doogan.

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REPRESENTATIVE NEUMAN expressed his concern for the measurement of the projects.

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SENATOR HOFFMAN offered his support of the project and pointed out that many rural communities were still suffering from high oil prices.

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CHAIR MEYER noted that the projects would be watched very closely.

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A roll call vote was taken. Senators Meyer, Stedman, Hoffman, Huggins and Menard and Representatives Thomas, Neuman, and Dahlstrom voted in favor of RPL 08-09-0137, as amended. Representatives Doogan and Stoltze voted against it. Therefore, RPL 08-09-0137, as amended, was approved by the Legislative Budget and Audit Committee by a vote of 8-2.

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SENATOR HUGGINS noted that the state did not have an energy policy, but that two energy committees and a renewable energy task force were working on it.

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REPRESENTATIVE THOMAS said that he was very confident for the projects in Southeast Alaska.

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ADJOURNMENT

There being no further business before the committee, the Legislative Budget and Audit Committee meeting was adjourned at 6:28 p.m.