ALASKA STATE LEGISLATURE
SENATE RESOURCES STANDING COMMITTEE
February 10, 2010
3:37 p.m.

MEMBERS PRESENT

Senator Lesil McGuire, Co-Chair
Senator Bill Wielechowski, Co-Chair
Senator Charlie Huggins, Vice Chair
Senator Hollis French
Senator Bert Stedman
Senator Gary Stevens
Senator Thomas Wagoner

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

SENATE BILL NO. 242
"An Act providing income tax credits for geothermal resource exploration and development."

- HEARD AND HELD

SENATE BILL NO. 243
"An Act removing the royalty obligation for geothermal resources."

- HEARD AND HELD

PRESENTATION: POINT MACKENZIE RAIL EXTENSION PRESENTATION

- HEARD

PREVIOUS COMMITTEE ACTION

BILL: SB 242
SHORT TITLE: GEOTHERMAL RESOURCE TAX CREDITS
SPONSOR(s): SENATOR(s) MCGUIRE

01/27/10	(S)	READ THE FIRST TIME - REFERRALS
01/27/10	(S)	RES, FIN
02/10/10	(S)	RES AT 3:30 PM BUTROVICH 205

BILL: SB 243
SHORT TITLE: NO ROYALTY ON GEOTHERMAL RESOURCE
SPONSOR(s): SENATOR(s) MCGUIRE

01/27/10	(S)	READ THE FIRST TIME - REFERRALS
01/27/10	(S)	RES, FIN
02/10/10	(S)	RES AT 3:30 PM BUTROVICH 205

WITNESS REGISTER

MIKE PAWLOWSKI
Aide for Senator McGuire
Alaska State Legislature
Juneau, AK
POSITION STATEMENT: Commented on SB 242 and SB 243 for the sponsor.

JOHANNA BALES, Deputy Director
Tax Division
Department of Revenue (DOR)
POSITION STATEMENT: Answered questions on SB 242.

PAUL THOMSEN, Director
Policy and Business Development
Ormat Technologies
POSITION STATEMENT: Supported SB 242.

SUZANNE LAMSON, Projects Manager
Naknek Electric Association
POSITION STATEMENT: Supported SB 242 and SB 243.

MARILYN LELAND, Executive Director
Alaska Power Association
POSITION STATEMENT: Strongly supported SB 242 and SB 243.

PAUL THOMSEN
Ormat Technologies
POSITION STATEMENT: Supported SB 242 and SB 243.

JOHN DUFFY, Manager
Matanuska Susitna Borough
POSITION STATEMENT: Commented on the Port MacKenzie Rail Extension project.

RICK MYSTROM

Matanuska Susitna Borough
POSITION STATEMENT: Presented update on the Port MacKenzie Rail Extension project.

PAT GAMBLE, Executive Director
Alaska Railroad Corporation (ARRC)
POSITION STATEMENT: Answered questions about the Alaska Railroad and the extension project.

ACTION NARRATIVE

3:37:24 PM
CO-CHAIR LESIL MCGUIRE called the Senate Resources Standing Committee meeting to order at 3:37 p.m. Present at the call to order were Senators Wagoner, French, Stedman, Huggins, Wielechowski, and McGuire.

SB 242-GEOTHERMAL RESOURCE TAX CREDITS

CO-CHAIR MCGUIRE announced SB 242 to be up for consideration.

3:38:13 PM
MIKE PAWLOWSKI, aide for Senator McGuire, sponsor of SB 242, explained that this measure is an income tax credit for geothermal exploration and development. He said that geothermal is a clean renewable source of power and can provide an important base load supply of power. It has been used in other countries and states successfully.

Section 1, he said, has the geothermal resource tax credit that is located within the corporate income tax statutes under AS 43.20. This section has two tax credits: the first, on page 1, lines 9-14, subsection (b), provides a resource exploration credit in the amount of up to 50 percent of the qualified exploration expenditures for exploration conducted on state land and 25 percent for those not conducted on state land. According to the Department of Revenue (DOR), the resource owned by the state and not owned by the state should actually be adjusted to reflect the land ownership when the bill moves forward. The important limit on that credit starts on page 2, line 1 - that it cannot exceed $20 million.

3:39:51 PM
MR. PAWLOWSKI said the second credit is on page 2, lines 8-12, and is the resource development credit, which is 10 percent of the qualified development expenditures. Both of the tax credits

are limited further by subsection (d) that says the tax credit taken in either (b) or (c) can never amount to more than 50 percent of a person's tax liability. As a company develops and brings the resource on line and is accruing revenue, these tax credits can offset their tax liability - the key point being that revenue would be coming into the state at that time. A carry-forward of seven years is on page 2, lines 10-11, but it should be more like 20 years.

3:41:24 PM
CO-CHAIR WIELECHOWSKI said he thought encouraging this sort of development was a step in the right direction. He asked how "a person" is defined in sections (a) and (b) and all throughout the statute.

MR. PAWLOWSKI deferred that answer to Johanna Bales, Department of Revenue (DOR).

3:41:40 PM
SENATOR STEVENS joined the committee.

3:42:03 PM
CO-CHAIR WIELECHOWSKI asked if this tax credit is available per site or per company, per well or per unit.

MR. PAWLOWSKI again deferred to the DOR, but his understanding was that the tax credit is based on actual expenditures rather than the project multiple times.

CO-CHAIR WIELECHOWSKI asked if the credit is available when the resource goes on line or as incurred even though it may not be on line for several years.

MR. PAWLOWSKI replied that the tax credit accrues as the expenditures are made, but without production there is no income to claim the credit against. The credits are in the income tax statutes, and that is why the carry-forward provisions are necessary.

CO-CHAIR WIELECHOWSKI asked if the credit is transferable.

MR. PAWLOWSKI answered that the credit in the current version of the bill is not transferable beyond a successive interest only. So, you could sell the credit if you sell the facility along with it. That language is on page 2, lines 16-19.

3:44:27 PM

CO-CHAIR WIELECHOWSKI asked why the credit is retroactive to June 30, 2008 if the goal is to encourage future development.

MR. PAWLOWSKI explained that some companies are working on geothermal projects in Alaska to the degree that actual conducted expenditures would be creditable. The credit is to apply to projects that are currently under development.

CO-CHAIR WIELECHOWSKI asked if these credits would be passed through to consumers when the rates are set.

MR. PAWLOWSKI deferred that answer to the project sponsors in terms of their understanding of whether or not they would be rate regulated and to the Regulatory Commission of Alaska (RCA). He added that the project sponsors would also talk about the transferability issue and whether credits should be rebated or transferred similar to oil and gas credits. It was not drafted that way.

3:46:19 PM
CO-CHAIR MCGUIRE asked Ms. Bales how "person" is defined in Title 43.

JOHANNA BALES, Deputy Director, Tax Division, Department of Revenue (DOR), answered that under the Alaska income tax title a "person" is defined as an individual, a trust, an estate, a partnership, or a corporation.

CO-CHAIR WIELECHOWSKI said he is trying to understand the parameters with the $20 million cap. Could this credit be applied to multiple persons or multiple sites, so an entity could get multiple $20-million tax credits? Maybe that language needs to be tightened up.

MS. BALES answered that the way the language is written, the $20-million cap is per project. If an individual taxpayer had several different projects, he could get a $20-million tax credit for each project.

CO-CHAIR WIELECHOWSKI asked if someone is doing a well at Mt. Spurr and they do multiple wells or wells that are several miles apart, is "project" defined anywhere.

MS. BALES answered no; existing language doesn't have a definition and neither do existing corporate income tax statutes.

3:48:14 PM
SENATOR FRENCH asked how expenditures on state lands and expenditures on other lands are treated differently philosophically.

MR. PAWLOWSKI said he was unclear on the different taxing relationship between state-owned land and non-state owned land, and that these provisions are part of an entire fiscal picture.

CO-CHAIR MCGUIRE said the bill is to incentivize development on state lands.

SENATOR FRENCH said he didn't know what revenue the state gets from geothermal energy when it comes out of the ground other than cheap electricity, which he hoped the state would get lots of. The state wouldn't grab a royalty on that electricity. He was trying to understand how the consumer would be able to differential between geothermal from the state versus from the federal government. Maybe it should all be 50 percent.

MR. PAWLOWSKI responded that Ms. Chin who is developing the Naknek geothermal project that is not on state land might be able to answer that question later in the hearing. He said the definition is on pages 2-3, the qualified development expenditures, but the project language still needs work.

SENATOR STEDMAN said he had a similar concern to Senator Wielechowski's about retroactive application and thought they should tighten up "qualified exploration expenditure" language on page 3, line 9, and that they should do some background work to find out how many geothermal businesses Alaska has.

CO-CHAIR MCGUIRE replied that currently no geothermal companies are operating in Alaska although Ormat has the lease on Mt. Spurr. When they came to town they started looking at statutes on the books that deal with geothermal and what kinds of things would make a difference in incentivizing geothermal energy in Alaska. These two bills came out of those discussions. She said the next one deals with royalty.

3:52:57 PM
SENATOR WAGONER asked how this would affect the Chena Hot Springs business.

CO-CHAIR MCGUIRE responded that the Hot Springs doesn't operate in a commercial environment.

SENATOR WAGONER said the owner is developing it to supply power and lay a line over the mountain to the base, and that is a commercial application.

CO-CHAIR MCGUIRE said if he was creating a commercial entity, he would qualify for this credit. The retroactivity would be a policy decision.

CO-CHAIR WIELECHOWSKI asked if a geothermal company joins in a joint venture with another company that has money, could they take the credit if no energy is produced.

MS. BALES answered yes.

3:56:13 PM
CO-CHAIR MCGUIRE said these bills were not put in for any one entity, but rather the inspiration came from her trip to Iceland to see how geothermal energy had transformed that nation that now has a rate of 6 cents/kWh.

3:56:42 PM
PAUL THOMSEN, Director, Policy and Business Development, Ormat Technologies, supported SB 242. He introduced Raum Orenstein who is the project developer for the Mt. Spurr project and director of business development with Ormat Technologies. He thanked Senator McGuire and legislative staff for drafting these bills that remove significant barriers to geothermal development. He said he would focus on SB 242 at this time and give them a little bit of background on Ormat Technologies. He elaborated that Ormat is publicly traded on the New York Stock Exchange. It started as a company in 1965 designing and manufacturing equipment.

What sets them apart from other developers is that they are vertically integrated. They design and manufacture equipment and delineate the resource and operate the geothermal power plants. Ormat did its first contract installing remote power units in 1975 with the TransAlaska Pipeline. In that time, he said, Ormat has been responsible for over 1000 mgW of geothermal development in over 71 countries around the world. They are interested in coming back to Alaska and developing this resource to supply energy to the Railbelt; they are particularly interested in Mt. Spurr and Mt. Makushin.

He said that Ormat was honored in the recent AGA grant process when the Division of Geological and Geophysical Survey (DGGS) sited it as one of the most highly experienced companies in the

world and that the proposed approach is the best to move forward toward potential development at Mt. Spurr.

MR. THOMSEN said that they strongly support SB 242, which recognizes that geothermal exploration is similar to oil and gas exploration in that they both involve high cost/risk drilling. He added that many Alaskan resources are green fields that require blind drilling which increases the cost and the risk.

3:59:28 PM
Alaska has introduced tax credits for oil and gas exploration and this bill similarly incentivizes geothermal exploration in the same way, he explained. If passed, their financial analysis indicates that this credit, if the carry forward is increased to 20 years or made refundable, will lower the total cost of geothermal development by more than 10 percent and, therefore, lower the total cost of power to the ratepayer by 5 to 10 percent.

CO-CHAIR WIELECHOWSKI said this is a really exciting project. A particularly good thing about geothermal is that it is a solid base line of energy 24/7; it doesn't matter if the sun is out or if the wind is blowing. He asked if they have timelines for this project coming online, how they envision this credit passing through to the consumer, and if he could talk publicly about what he expects those rates to be.

MR. THOMSEN answered that typically developing a green field geothermal project from defining the resource to bringing the power on line takes 4 - 5 years, but in Alaska they are looking to extend that a little bit by having it online by 2016.

On the question of impact to the ratepayers, their financial model indicates that this credit reduces Ormat's CAPEX. With geothermal projects there are two issues - the cost to develop the project and the price they can get for selling the electricity. So within this local market they are looking at a fixed price and as an independent power producer, they look for a contract with an investor-owned utility that is competitive enough that they can get the price approved through the RCA. Prices in 2009 dollars are about 12-14 cents/kWh. That gets negotiated with an off-taker of that electricity- like GRETC or a utility. Allowing them to lower the price translates into ratepayers getting the benefit from that through lower utility bills.

CO-CHAIR WIELECHOWSKI asked if that price includes the cost of transmission lines into the main grid.

MR. THOMSEN replied no.

CO-CHAIR WIELECHOWSKI asked how the energy from this project would get tied into the main grid.

MR. THOMSEN said they were looking for solutions to that. If they had to bear building the additional transmission to reach this project and the road, that would increase the price they would need to get for their electricity to make this project viable.

CO-CHAIR WIELECHOWSKI asked how many mgW they would produce.

MR. THOMSEN answered that they believe the resource could achieve 100 mgW, but they have learned to develop these projects pragmatically. So, the initial phase would be 50 mgW, and then making sure the heat and water can sustain a full 100 mgW development before making that capital expenditure.

CO-CHAIR WIELECHOWSKI asked if they plan to add more water to create more steam.

MR. THOMSEN answered no. He explained that Ormat has a unique closed loop system. There are two types of geothermal development today: one is called "flash" and one is called "binary." The first power plant using flash technology was built in 1905 in Italy. This is basically where a well is drilled, the water comes up out of pressure, and turns to steam that turns a steam turbine. That process needs Mother Nature to work in your favor because that steam needs to be recondensed into rain so it can recharge the ground water table.

The Ormat system is closed loop: it brings up the hot water under pressure in a closed environment and heats a secondary working fluid. That working fluid vaporizes and when it expands it builds pressure and turns a turbo expander. The hot brine is then 100 percent reinjected back into the reservoir to be reheated and reused. He said this is what makes their geothermal development so unique - that it has a symbiotic relationship with the reservoir. That reservoir needs to be maintained and if they start to see a cooling effect, they know the power plant will produce less electricity and become less economic; and they will start losing money.

CO-CHAIR MCGUIRE asked him to describe their two projects in Hawaii and Reno.

MR. THOMSEN responded that their facility in Reno, Nevada, produces approximately 100 mgW of electricity; it is inside the city limits and produces enough geothermal power to supply the entire residential load of the city of Reno. The project was built over a 20-year period with incremental projects coming on line utilizing one reservoir. He said the prices have varied greatly over that 20-year period. The initial power purchase contracts were in the 6-8 cent range and today they are closer to 10 cents.

He emphasized that as they look to bring the amounts per project on rapidly, and added that the value in doing so becomes exponentially more important in looking at a fixed-price 20-year contract. They typically enter into fixed price contracts; so the earlier the project gets on the line, the lower the rate they have to negotiate, but that is what they have to live with for the life of the project. So, these projects that came on line at 6 cents in Reno in 1985 really show their value 20 years later. They hope the same effect happens at Mt. Spurr. The Reno resource is a unique geological resource that they have drilled very deep and found very moderate-temperature water; so more water and volume has to be used to sustain the reservoir.

4:07:22 PM
Contrary to that, their 30 mgW project on the Big Island of Hawaii is from a volcanic resource, and it supplies approximately 35 percent of the Big Island's energy needs. They have implemented safety protocols and standards for dealing with live molten lava and are able to produce a product there that is very reasonably priced. Mt. Spurr would be a similar project, however the price would be more in Alaska because geothermal energy would be offsetting imported bunker fuel. On the Big Island of Hawaii it would be closer to $.10 to $.12.

SENATOR HUGGINS asked for a "quick thumbnail sketch" of the two states that have federal incentives.

MR. THOMSEN replied that today the federal government offers a production tax credit, a $.02-tax rebate on the project once it starts producing energy. But since that credit needs to be reauthorized every few years, it is also unreliable. So, it is very hard to count on that credit for their project that will take five years before it will produce electricity. That tax credit currently exists and today under the Stimulus Act they

can actually forego that production tax credit and receive a 30-percent investment tax credit for projects coming on-line before 2013. So, their concern is not knowing what federal incentives will be when this project is ready to be brought online in 2016.

He said Ormat operates projects in the states of Nevada, California, Hawaii, and have built projects in Idaho and Wyoming. Many of those states have also tried to incentivize geothermal development either through property or sales tax abatements or other such incentives. While they don't like the impact to local governments that some of those incentives create, they still think that looking at the corporate income tax as a way to jump start these projects is "a great solution to that."

SENATOR HUGGINS said this is exciting because it is the future. He wanted to hear about some of their international experiences.

4:10:34 PM
MR. THOMSEN answered that they are equally as excited to trail-blaze a project in Alaska and hope what they learn in developing this project will lower the cost for future geothermal projects in Alaska. Ormat recently developed a geothermal facility at Lake Naivasha in Kenya, Africa, where they weren't able to receive financing because people were concerned about developing a project in a third world country. Ormat financed this 48 mgW project on its own balance sheet; they then refinanced it afterwards. They also improved upon the local community by teaching local people how to operate and conduct maintenance to the facility and by creating a school center for the children of those employees. Today it is a model for developing geothermal projects in third-world countries and has been cited in multiple projects moving forward.

4:12:32 PM
MR. THOMSEN, referring to Co-chair Wielechowski's previous question, said that Ormat's original concern was that their leases for Mt. Spurr date back to 2008 and they would lose their original $3.5 million investment by taking placed in service today. They won't start getting the tax credit until this project generates revenue and the majority of that exploration cost is yet to come; so, they are open to modifying that date to current.

4:13:28 PM
CO-CHAIR MCGUIRE asked him the value of the incentives to their decision to continue moving forward.

MR. THOMSEN replied that these incentives are "absolutely imperative" to moving this project forward. If they can't get the price in line with what the local utilities are willing to pay, it's a non-starter. Reducing these barriers would allow them to release the funds quicker, thus allowing this project to be actualized by 2016.

CO-CHAIR WIELECHOWSKI said, "I love clean energy, green energy; I also like affordable, low-cost energy." He asked for assurances that these tax credits will pass through to consumers in the form of lower rates. He asked if he envisioned the RCA regulating his end of the project or if he planned on going to Chugach first and having them go to the RCA - and having no RCA oversight over their project.

MR. THOMSEN replied that they envision the second getting a contract with a utility and that contract is then approved or not by the RCA. They want that contract to be transparent and to be a good thing for Alaskans. He said the exciting thing about working for a geothermal company is that it offers a base load supply of electricity 24/7 and they think that their price, while it might seem a little high compared to natural gas or coal in the Lower 48, offers something that none of those can - a fixed price over 20 years. That kind of a price hedge over 20 years will pay dividends in the future for the ratepayers of Alaska - especially talking about current debates on cap and trade, renewable portfolio standards, and so forth.

CO-CHAIR WIELECHOWSKI said the concern he has seen is that they have a similar process in place for natural gas in Cook Inlet and they have no idea how much it costs for producers to extract it and sell it to Chugach Electric, ML&P or another organization. It's something the RCA complains about a lot and he wonders what direction they are headed in.

CO-CHAIR MCGUIRE thanked them for their presentation and for believing in Alaska.

4:17:14 PM

SUZANNE LAMSON, Projects Manager, Naknek Electric Association, said she was speaking for Donna Vukich, its general manager. She thanked the committee for all of its work on energy-related issues, especially regarding geothermal. She said they are working on a green field development in Southwest Alaska and they supported SB 242 and SB 243. Removing the barriers to

geothermal development through this kind of incentive is "imperative" to develop geothermal energy in Alaska.

4:18:55 PM
MARILYN LELAND, Executive Director, Alaska Power Association, strongly supported SB 242 and SB 243. She said Alaska has the misfortune of having some of the most expensive energy costs and the biggest problem supplying energy to its citizens. But, at the same time it also has the fortune of having the best resources in the country for generating electricity with hydropower, wind and geothermal. Currently, one member, Naknek Electric Association, is drilling for geothermal; several other members including Inside Passage Electric Coop, Nome Joint Utilities, and TDX Power are considering the possibilities. However, the front-end costs are enormous and the systems of pursuing of them are generally small; and without incentives some geothermal projects just won't get done because the companies won't be able to take the risk involved with that cost, which would be a huge loss for Alaska.

MS. LELAND emphasized that geothermal is not a theoretical idea; it is a real possibility and the time is here to carry it forward.

CO-CHAIR MCGUIRE thanked everyone for their testimony and work; and closed public testimony setting SB 242 aside.

SB 243-GEOTHERMAL RESOURCE:ROYALTY/PERMIT/FEE

4:21:25 PM
CO-CHAIR MCGUIRE announced SB 243 to be up for discussion and that it is the companion bill to SB 242 that deals with the royalty relating to geothermal energy.

MIKE PAWLOWSKI, aide to Senator McGuire, sponsor of SB 243, explained that currently under AS 38.05.181(g), the State of Alaska charges a 10-15 percent royalty on gross revenues on geothermal projects. This has a significant impact on the economics of this geothermal project that has a fixed cost of $.12 to $.14. Other states don't have royalties anywhere near what Alaska has; these royalties are very similar to what the state has for oil and gas development, not for geothermal development. That is where the bill started off in concept; procedurally SB 243 removes royalty from geothermal projects in Alaska.

CO-CHAIR MCGUIRE explained that last Interim geothermal was looked at and an old reference to a 10-15 percent geothermal royalty credit was discovered. They think it was put in as a place holder back when the oil and gas provisions were being developed, but without any reflection on what an appropriate geothermal regime would look like. This resource is hot water, a renewable energy that is not extracted permanently in the way that hydrocarbons are.

She explained that the thinking behind this bill is to incentivize these projects, but also realizing that they really don't see a rationale for the state to exact a royalty on a resource that is not being removed permanently from the ground - the whole point of royalty and severance. If Alaska has a royalty, it would be the highest rate in the nation and would make any geothermal development in this state impractical.

Further, Senator McGuire said, some states with federal lands aligning them have a 1.7 percent royalty. The federal government has said 3 percent is their threshold. Clearly the 10-15 percent would be "outrageous," and she supported no royalty for the reasons she just articulated. But, she said she wanted to hear testimony from the companies about other royalty regimes.

4:25:55 PM
PAUL THOMSEN, Ormat Technologies, echoed earlier comments about how geothermal power capital costs in other states are around $4000/kW and how in Alaska the costs are 25-50 percent higher than that. They think SB 243 recognizes that in other western states geothermal power projects rarely are required to pay state royalties.

4:27:05 PM
He clarified that when they were looking at this provision, they found that a predominance of western states actually do have a very high state royalty rate in statute; they just don't have any geothermal power projects paying it. That is when they started to question it. The state of California has somewhere in the range of a 10-11 cent royalty for state lands; it is the largest producer of geothermal power in the US. A fraction of their projects sit on state lands. The geysers in Northern California that produce 1000 mgW take up a couple acres of state land and pay the 10 percent; but when you look at total projects, it's less than 1 percent. Another example is in Southern California.

MR. THOMSEN said they compared that to a state like Nevada that is the largest geothermal producer per capita, but does not have a state royalty rate at all. The state is 90 percent federally owned, so Ormat pays a federal rate. He said the Geothermal Energy Association, the National Association which Ormat is also a board member of, explained that geothermal royalties vary depending on land ownership, type and tend to range from .5 percent to 5.5 percent of revenues. The 10 percent is sometimes applied to gross revenues versus net. The majority of geothermal projects currently under development in the US are on federal lands where BLM regulations call for revenue royalties of 1.75 percent for the first 10 years and 3.5 percent thereafter.

MR. THOMSEN said that despite the fact that geothermal development faces greater financial challenges in Alaska, they think that the current statute's royalty rate of 10-15 percent is simply "cost prohibitive." Ormat's financial analysis shows that removing the royalty obligation would reduce the kWh cost by about 10 percent; and they think that removing the royalty obligations from geothermal power plants in Alaska will serve to acknowledge the unusually high costs of geothermal development and address even the AEA's concerns that the direct economic benefits of geothermal production are highly sensitive to O&M costs. Unlike the previous bill, this one really looks at reducing those costs once the project is up and operating - combating the high prices of remoteness of projects, the severity of weather and other difficult factors about developing in Alaska. This would ultimately lower the cost of clean reliable power to ratepayers.

4:29:29 PM
CO-CHAIR WIELECHOWSKI asked if he would support an amendment that said any reduction in royalty is required to be passed on to the customers.

MR. THOMSEN replied that he would examine that language, but in principle they absolutely support that concept.

4:30:03 PM
At Ease

4:34:25 PM
CO-CHAIR MCGUIRE called the meeting back to order at 4:34 p.m. SB 343 was set aside.

Presentation: Point Mackenzie Rail Extension

4:34:34 PM
CO-CHAIR MCGUIRE announced an overview of the proposed Point Mackenzie Rail Extension project.

4:34:44 PM
JOHN DUFFY, Manager, Matanuska Susitna Borough, said this project offers tremendous opportunities for the State of Alaska in terms of job creation and economic opportunities, especially in the South central region. Studies done by the University of Alaska and Northern Economics indicate the project will create thousands of jobs and pay off hundreds of millions of dollars to the state treasury over a hundred years. It begins the diversification of Alaska's economy and provides the opportunity to create major manufacturing opportunities; for instance, Alaska could supply 5 percent of the nation's cement needs with this project.

RICK MYSTROM, consultant, Matanuska Susitna Borough, said the Valley has become their new second home, and he sees how the economy of Anchorage and the Valley are very closely tied. His other business is buying and operating apartments - mostly in Anchorage and Eagle River, but his job is to understand and predict the Alaskan economy. In the last 35 years the Alaskan economy has slid three different times. One time was after conclusion of the TAPS in 1979, but at that time Governor Hammond who had just been reelected in 1978 and the legislature focused on getting jobs out into the economy. They created a capital budget that allowed for $1000/yr. for every person in Alaska for three years to get jobs into the economy. Every community got a chance to put forth its suggestions for capital projects. Since he was on the Anchorage Assembly at that time, he knows they built the $32-million Sullivan Arena, the $32-million Egan Center, a $16-million museum expansion, $44-million library, and what was going to be a $27-million performing arts center, but turned out to be $72 million (because of the dyslexic accountant).

More related to what they are now doing, Mr. Mystrom said, they also built the extension of Minnesota that went south out to O'Malley that allowed for development out there. That on a small scale is what he wanted to talk to them about today.

He related that the second time the economy slid was in 1986 when the price of oil dropped from $30/barrel down to $8. At that time Governor Cowper and the legislature decided to save the state's money and allowed for very little capital expenditure during the next two or three years - and the Alaskan

economy fell off the biggest cliff that it had ever seen. Anchorage lost 13 percent of its population and 25 percent of its assessed valuation. The same thing happened in the rest of the state.

4:42:30 PM
The third slide to the economy is happening right now Mr. Mystrom said, and he felt the next 3-5 years were going to be tough. So, he encouraged the legislature to use capital spending now because it's cheaper now and more workforce is available.

4:43:06 PM
MR. MYSTROM said to understand the impact of Port MacKenzie and the Rail Extension they need to begin thinking of the Fairbanks North Star Borough, the Denali Borough, the Mat-Su Borough and Anchorage as a regional economy. He elaborated on his slides:

Slide 1: Uncertainty about energy availability and costs, uncertainty about the gas line construction, uncertainty about the future of the TransAlaska pipeline, uncertainty about small business administration rules for contracting programs for Native businesses, and ongoing Congressional discussions of scenarios that would not be good for Alaska.

He said it's just a matter of how bad they will be for Alaska. There is also uncertainty about the exploration permits for Chukchi and Beaufort Sea. Uncertainty is very bothersome to investors; two things are certain: one is lack of transportation infrastructure and the other is lack of diversification of Alaska's economy. One of the solutions is the project he would talk about now and the effects could happen as soon as next summer.

4:46:09 PM
He said the Port MacKenzie/Rail Extension has three route options for getting the mainline of the Alaska Railroad (slide 3). One of the three will be recommended by the Surface Transportation Board that is part of the ongoing EPA study. It should come out in March and then there would be 60 days of hearings before a final recommendation. He said the extension would reduce the number of miles to tidewater by 147 miles and it would have huge positive impacts on all four areas.

4:46:46 PM
CO-CHAIR WIELECHOWSKI asked what would happen to Anchorage if things were shipped to Wasilla.

MR. MYSTROM answered "very positive" things, because the ports are very different. He said he would elaborate on that more later in his presentation.

4:47:33 PM
SENATOR WAGONER asked from where to where for the 147 miles.

4:47:37 PM
MR. MYSTROM answered "from anyplace north of Willow to tidewater" or 147 miles closer than it would be to go to Seward.

He went on to slide 4 on what the rail extension means to the regional economy:

- It opens up the Interior to resource development.
- It facilitates the development of a world-class limestone deposit in Livengood just north of Fairbanks.
- It facilitates the development of a cement production facility in or around Fairbanks.
- It opens up a 60-mile corridor along the Railbelt to exploration and extraction of strategic minerals (lead, zinc, copper, molybdenum and silver).
- It improves the transportation of lower cost and low sulphur fuel to the Interior and Southwest Alaska.
- It dramatically improves the world competitiveness of Alaska coal by about $3/ton. This savings can be applied to any aggregate coming out of the Denali and North Star Boroughs.
- It reduces transportation and staging costs for the gas pipeline construction. The Denali Project believes it will save about $100 million in transportation and staging costs of pipe for the gas pipeline. Right now the pipe for the Liberty field comes up from Japan to Houston, goes by rail to Seattle, by barge to Whittier and by rail from Whittier north.
- It increases employment in the four regions.

4:49:58 PM
SENATOR WAGONER asked why it goes that route instead of through Seward and up the railroad from there.

MR. MYSTROM said he would have to ask the Liberty people who are doing it. He continued his presentation saying that Port MacKenzie is a bulk commodities port for minerals, cement, coal, fuel and bulk fuel - very different from the Port of Anchorage that is for consumer goods and containers.

4:50:43 PM
He said the Port of Anchorage will always be the most important port in Anchorage because it focuses just on consumer goods and containers. Port MacKenzie has 14 square miles of industrially zoned area with nothing to prevent industrial development of that area - like homes. Anchorage just doesn't have that.

4:52:20 PM
CO-CHAIR MCGUIRE said Cook Inlet Region Incorporation (CIRI) did a presentation on its underground coal gasification project and they mentioned multiple times that they were trying to stay this side of the Mat-Su Borough line because of local tax issues. She wanted to know if those issues had been addressed.

SENATOR HUGGINS added that it's really about power generation and a delay factor with the permitting process. Some people, including MEA, think it's not a friendly environment for building power plants.

MR. MYSTROM remarked that CIRI, the Mat-Su Borough, and the University of Alaska Trust own the land at Port MacKenzie and are supportive of this legislation. It does not compete with Anchorage; it has a 60 ft. mean low tide. The Port of Anchorage has 35 ft. The kinds of ships that haul aggregate and minerals can't come into the Port of Anchorage. He envisioned that ultimately the two would become sister ports with a common port commission supervising both - with the Railroad included. The Railroad is very supportive of this concept.

To help understand the differences in the ports, he explained, Port MacKenzie can handle Panamax vessels, the maximum size vessel that can get through the Panama Canal, and Cape vessels that are too big to go through the Panama Canal and must go around Cape Horn or the Cape of Good Hope. Port MacKenzie can handle the largest ships in the world; it also handles barges carrying bulk commodities minerals, coals and aggregate.

4:58:25 PM
He described and explained the pictures on slides 13-18. Slide 18 showed plenty of storage and staging capacity for all the pipe needed for both gas lines. Again he said Denali estimated the rail extension would save $100 million in the cost of the pipeline.

Port MacKenzie is a two-and-a-half hour drive from Anchorage, but soon a new ferry, the MV Susitna, will start running between the MatSu Borough, Anchorage, Kenai and Tyonek. It holds 20 cars and will be christened in March in Ketchikan. The revolutionary thing about the ferry is that the cars will be drive on at the lower level and then the cars will be hydraulically lifted so the middle part of the ship never touches the water. The pontoons become the ice-breaker, making it the first high speed ice breaking ferry that has ever been built - built by the Navy and turned over to the MatSu Borough for years of testing and record-keeping. Incidentally, he said the MatSu Borough, in its negotiations with the Navy, required that it be built in Alaska.

SENATOR WAGONER asked where the ferry would dock in Kenai.

MR. DUFFY answered Nikiski.

5:02:06 PM
MR. MYSTROM said the ferry terminal is already built on the Port MacKenzie side. He said a number of studies had been done by Paul Metz, HDR, and Northern Economics that talk about how this transportation is necessary to allow the development of limestone deposits, zinc, molybdenum, copper, and silver in the Interior. It will make a significant difference in the economy of that area. The rail extension is estimated to create 3000 related construction jobs from 2010 to 2013. The Port MacKenzie portion would create 500 jobs, Anchorage 720, and the balance from the MatSu Borough for a total of 3500 jobs. Incidentally, he had found out that half the employees at the Red Dog and Pogo mines live in Anchorage and work a week on and a week off. In addition to that, this project would facilitate private development of jobs along the rail line that will become part of Anchorage's northern industrial segment.

MR. MYSTROM said the EIS will be done in March for a cost of $10 million and the construction of the road and the rail bimodal loop is under construction for a cost of $17 million, which they have in hand. The permitting, design and beginning of construction for the selected alternative is the next step, and keeping that going with $57 million is what they are looking for this year from the Legislature. The cost of constructing the railroad bed and the final project, will depend on which of the routes are selected. The laying of tracks could be completed by 2013.

CO-CHAIR MCGUIRE thanked him for his presentation.

CO-CHAIR WIELECHOWSKI asked if the Railroad is thinking about bonding for this project.

5:07:34 PM
PAT GAMBLE, Executive Director, Alaska Railroad Corporation (ARRC), responded that the legislature gave ARRC preapproval to bond for this project in a previous piece of legislation, but they haven't reached that financial decision point. Having the preapproval "in our hip pocket" makes it a lot easier to find out which vehicle will be the best one for the state to use.

SENATOR HUGGINS asked for a quick burst on ARRC's mission.

MR. GAMBLE responded that was a great question, because they are "in the business of economic development." The Corporate Act has four state policies that define the Railroad; three of them are in the development area of resources, transportation infrastructure, and economic long-term growth.

5:09:30 PM
MR. MYSTROM said he understands that the Railroad has authority for revenue bonds that aren't practical or realistic for this project.

MR. GAMBLE responded that at the time they were trying to do two things at once, one was to pre-approve the Agrium project and the other was to pre-approve bonding for this project. He didn't remember the exact bonding language, but it was clearly intended that the tool be used as appropriate - he remembered it being "some sort of a conduit bonding."

SENATOR WAGONER asked the average cost of constructing each mile of railroad right now.

MR. GAMBLE answered about $5-8 million/mile depending on the geography, interest rates, and the cost of commodities.

SENATOR WAGONER asked how much more traffic the existing line between Fairbanks and Anchorage can take before it will need modifications.

MR. GAMBLE answered that the good news is that the modifications are just about done on that line. It includes the bridges, the sidings, upgrading signalization and technology. They began building it in earnest about eight years ago in anticipation of the pipeline and actually sped the whole project up by 10 years. The legislature gave them permission to issue $165-million worth

of bonds to pay the debt service. They have three more years to complete the whole line from Anchorage to Fairbanks. Traffic now is at a fraction of what it will be able to move when and if the time comes.

5:13:27 PM
CO-CHAIR MCGUIRE thanked him again and adjourned the meeting at 5:13 p.m.