

HOUSE FINANCE COMMITTEE
April 15, 2014
8:35 a.m.

8:35:38 AM

CALL TO ORDER

Co-Chair Stoltze called the House Finance Committee meeting to order at 8:35 a.m.

MEMBERS PRESENT

Representative Alan Austerman, Co-Chair
Representative Bill Stoltze, Co-Chair
Representative Mark Neuman, Vice-Chair
Representative Mia Costello
Representative Bryce Edgmon
Representative Les Gara
Representative David Guttenberg
Representative Lindsey Holmes
Representative Cathy Munoz
Representative Steve Thompson
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Anna Latham, Staff, Representative Kurt Olson; Joe Balash, Commissioner, Department of Natural Resources; Michael Pawlowski, Deputy Commissioner, Strategic Finance, Department of Revenue; Angela Rodell, Commissioner, Department of Revenue.

SUMMARY

HB 316 WORKERS' COMPENSATION MEDICAL FEES

CSHB 316(FIN) was REPORTED out of committee with "no recommendation" and with one new fiscal impact note from the Department of Labor and Workforce Development and one new indeterminate note from the Department of Administration.

CSSB 138(FIN) am

GAS PIPELINE; AGDC; OIL & GAS PROD. TAX

CSSB 138(FIN) am was HEARD and HELD in committee
for further consideration.

#hb316

HOUSE BILL NO. 136

"An Act requiring the governor's fiscal plan to
include certain information."

8:36:18 AM

Co-Chair Stoltze referred to two amendments.

Representative Thompson MOVED to ADOPT Amendment 2, 28-
LS1362\P.1, Wallace, 4/8/14 (copy on file):

Page 1, line 11:

Delete "board and adopted by reference"

Insert "medical services review committee [BOARD] and
adopted by the board [REFERENCE]"

Page 2, line 21:

Delete "(1)"

Delete "board"

Insert "medical services review committee"

Page 2, line 22:

Delete "board"

Insert "medical services review committee"

Page 2, line 23, following "adopted":

Insert "by the board"

Page 2, line 23:

Delete ";"

Insert "."

Page 2, lines 24 - 29:

Delete all material.

Page 3, following line 23:

Insert a new subsection to read:

"(p) The medical services review committee shall
formulate a conversion factor and submit the

conversion factor to the commissioner of labor and workforce development. If the commissioner does not approve the conversion factor, the medical services review committee shall revise the conversion factor and submit the revised conversion factor to the commissioner for approval."

Page 4, following line 15:

Insert a new bill section to read:

"* Sec. 4. AS 23.30.395 is amended by adding a new paragraph to read:

(42) "medical services review committee" means the committee established under AS 23.30.0950)."

Renumber the following bill sections accordingly.

Page 4, line 16:

Delete "AS 23.30.097(j) - (o)"

Insert "AS 23.30.097(j) - (p)"

Page 4, line 18:

Delete "sec. 4"

Insert "sec. 5"

Co-Chair Stoltze OBJECTED for discussion.

Representative Thompson explained that Amendment 2 would allow the medical services review committee to directly set the conversion rates for the new fee schedule. Subsequently, the schedule would be submitted to the Department of Labor and Workforce Development commissioner for approval. In the current bill version the conversion factors were set by the 18 member workers' compensation board. The medical services review committee was made up of 9 people including members of the state medical association, chiropractic society, nursing home association, a healthcare provider, four non-healthcare providers, and the commissioner's designee. He communicated that the amendment streamlined the process and had come at the bill sponsor's request.

Co-Chair Stoltze reiterated that the amendment language had been brought to the committee by the sponsor.

ANNA LATHAM, STAFF, REPRESENTATIVE KURT OLSON, confirmed the sponsor's support of Amendment 2.

Co-Chair Stoltze asked for verification that the amendment language had originated from the sponsor. Ms. Latham replied in the affirmative.

Co-Chair Stoltze WITHDREW his OBJECTION. There being NO further OBJECTION, Amendment 2 was ADOPTED.

Representative Gara MOVED to ADOPT replacement Amendment 1:

Page 2, line 19:

Insert "(4) The fee schedules of (A) - (C) of this subsection shall not be used for any procedure or service unless they satisfy the service charge of providers in an area so that patient access to quality medical care is not compromised."

Co-Chair Stoltze OBJECTED for discussion.

Representative Gara pointed to a concern that the workers' compensation rate would be the Medicare or Medicaid rate. He understood that it was not the sponsor's intention; therefore, replacement Amendment 1 clarified that the workers' compensation rate would not be the Medicare or Medicaid rates unless they were adequate to ensure patient access to quality medical care. He stated that the sponsor intended that there would be a multiplier at some point in time.

Ms. Latham believed the amendment had good intention; however, she believed it was unnecessary for two reasons. First, it created confusion in the interpretation that Medicare or Medicaid rates would be used. Second, currently 32 states used the methodology with a conversion factor set by the state. The bill had been referred to the House Finance Committee because of its \$62,000 fiscal note associated with the medical services review committee setting the conversion factors.

Representative Gara asked for verification that the Medicare and Medicaid language in the bill did not mean that the state would adopt those rates if they were inadequate to provide quality medical services and access. Ms. Latham replied in the affirmative and pointed out that the conversion factor was a large component of the legislation for that reason.

Representative Gara was satisfied with the information put on record by the sponsor's staff. He WITHDREW Amendment 1.

8:42:16 AM

Vice-Chair Neuman referred to the unique nature of widespread costs in Alaska due to availability of medical services statewide. He imagined that cost differentials in rural Alaska could be quite varied. He wondered about alignment with Medicaid values. He asked if comparisons had been done statewide to determine how costs would average out.

Ms. Latham replied that the geographical differential had been included specifically for rural areas. She added that the bill included an exemption for rural (critical access) hospitals.

Representative Wilson asked if there was a place on the board for physical therapists. Ms. Latham replied that there was one open seat for a healthcare provider on the medical services review committee. She relayed that based on testimony, physical therapists did not account for the application of a conversion factor. The testifiers had discussed their experiences using Medicare rates, which was not the intent of the legislation. She believed some confusion existed related to the testimony.

Representative Wilson pointed out that there was an opportunity for physical therapists to apply for a medical services review committee seat if they were interested.

Representative Costello discussed the fiscal notes including one fiscal impact note from the Department of Labor and Workforce Development totaling \$62,000 in FY 15 and \$54,000 in FY 16 through FY 20; and one indeterminate note from the Department of Administration.

Vice-Chair Neuman MOVED to REPORT CSHB 316(FIN) out of committee with individual recommendations and the accompanying fiscal notes.

CSHB 316(FIN) was REPORTED out of committee with "no recommendation" and with one new fiscal impact note from the Department of Labor and Workforce Development and one new indeterminate note from the Department of Administration.

8:45:42 AM

AT EASE

8:47:53 AM

RECONVENED

#sb138

CS FOR SENATE BILL NO. 138(FIN) am

"An Act relating to the purposes, powers, and duties of the Alaska Gasline Development Corporation; relating to an in-state natural gas pipeline, an Alaska liquefied natural gas project, and associated funds; requiring state agencies and other entities to expedite reviews and actions related to natural gas pipelines and projects; relating to the authorities and duties of the commissioner of natural resources relating to a North Slope natural gas project, oil and gas and gas only leases, and royalty gas and other gas received by the state including gas received as payment for the production tax on gas; relating to the tax on oil and gas production, on oil production, and on gas production; relating to the duties of the commissioner of revenue relating to a North Slope natural gas project and gas received as payment for tax; relating to confidential information and public record status of information provided to or in the custody of the Department of Natural Resources and the Department of Revenue; relating to apportionment factors of the Alaska Net Income Tax Act; amending the definition of gross value at the 'point of production' for gas for purposes of the oil and gas production tax; clarifying that the exploration incentive credit, the oil or gas producer education credit, and the film production tax credit may not be taken against the gas production tax paid in gas; relating to the oil or gas producer education credit; requesting the governor to establish an interim advisory board to advise the governor on municipal involvement in a North Slope natural gas project; relating to the development of a plan by the Alaska Energy Authority for developing infrastructure to deliver affordable energy to areas of the state that will not have direct access to a North Slope natural gas pipeline and a recommendation of a funding source for energy infrastructure development; establishing the Alaska affordable energy fund; requiring the commissioner of revenue to develop

a plan and suggest legislation for municipalities, regional corporations, and residents of the state to acquire ownership interests in a North Slope natural gas pipeline project; making conforming amendments; and providing for an effective date."

8:47:58 AM

Co-Chair Austerman requested an explanation as to why the Department of Transportation (DOT) had not been involved in conversations about the infrastructure needs. He pointed out to the committee that the HOA states that the state was going to be responsible for the infrastructure liability.

JOE BALASH, COMMISSIONER, DEPARTMENT OF NATURAL RESOURCES, answered that the understanding was that the gasline was going to work like any other commercial entity or project approaching DOT for transportation and infrastructure services. He relayed that the HOA contemplated that the state would take actions to facilitate and support, but whenever a commercial party approached DOT looking for infrastructure, funds were provided by the party but there would still be an underlying appropriation required. He said that the actions that had been committed to in Article 10 were ministerial. He thought that it was important to highlight language in Article 9, which would give assurances that the state would not be "on the hook" for all of the costs. He referred to Article 9.3.1, part b:

The Parties would establish a series of impact payments to be paid by the Alaska LNG Parties to help offset increased service and other costs borne by the State and local governments during construction of the Alaska LNG Project.

Commissioner Balash said that he had every expectation the project would pay for the things that were solely attributable to the project. He expected that DOT would be making the decisions as to what things were 100 percent of the project and what things were partially attributable to the project.

MICHAEL PAWLOWSKI, DEPUTY COMMISSIONER, STRATEGIC FINANCE, DEPARTMENT OF REVENUE, pointed to the Page 15 of the HOA. He said that the provision recognized the principle of impact payments to the state to offset some of the impacts at the state and community level. He said that the

development of an impact payment schedule was part of the negotiations to be determined. He relayed that the decision in the announcement that Nikiski was the terminus for the project, and the preferred direction, had come in October 2013. He stated that part of the point of the state participating early was to get the state in at the ground floor of the project as it was being developed, and that the state would be fully aware of the needs of the project, and that the state would be influential of the decisions made on the project; for example, the size of pipe. He said that the size of the pipe had a material impact on the compressor stations and the amount of work that would need to be done on infrastructure.

Representative Thompson spoke of Stranded Gas Act discussions. He warned of the large impact on the City of Fairbanks once construction began on the pipeline. He mentioned the impact on police departments, emergency services, and residents quitting their current jobs to work on the pipeline for increased pay. He believed that there should be preconstruction dollars in order to address preconstruction concerns, and that those concerns should be addressed at least a year before construction began.

[8:56:44 AM](#)

ANGELA RODELL, COMMISSIONER, DEPARTMENT OF REVENUE, answered that the concern that had been discussed but not in great detail. She said that in working on the Administrative Order it had been recognized that social impacts would need to be considered. She thought that much could be learned from the TAPS construction.

Vice-Chair Neuman referred to Page 15 of the HOA. He requested a list of the impacts of the infrastructure within the state.

Commissioner Balash answered that he would provide a description of all the required reports for the Federal Energy Regulatory Commission (FERC) process. He informed that committee that there was one report in particular that spoke to the socioeconomic impacts of the project construction.

Vice-Chair Neuman declared that he was interested in the infrastructure impact.

Commissioner Balash understood. He believed there was a specific component that spoke to transportation infrastructure.

Vice-Chair Neuman queried the differentiation between tax deductions for the gas pipeline and those used against the oil taxes on the upstream side of point of production, pre flow.

[9:01:18 AM](#)

Mr. Pawlowski answered that the expenditures would be deducted against the production tax value for oil. He stated that there was no need to differentiate whether a certain piece of equipment would be used for oil and another for gas, the deductions occurred against the production tax value of oil. He said that the upstream investments that had been modeled included a revenue impact primarily from the build out at Point Thomson and some at Prudhoe Bay. He relayed that Point Thomson carried additional oil production when more gas was being produced and that those revenue were included in the models. He shared that the way that the bill was structured there would be no separation of the deductions.

Vice-Chair Neuman expressed concern with the issue. He felt that the oil company should be putting as much infrastructure as was necessary to handle the gas, and the upstream costs, in order to deduct if off of the taxes that would be paid on the oil. He wondered what protected the state from being charged hundreds of millions in deductions.

Mr. Pawlowski directed committee attention to Page 57 of the bill. He spoke to the deleted language on the page:

(C) FOR GAS RUN THROUGH AN INTEGRATED GAS PROCESSING PLANT AND GAS TREATMENT FACILITY THAT DOES NOT ACCURATELY METER THE GAS AFTER THE GAS PROCESSING AND BEFORE THE GAS TREATMENT, THE FIRST POINT WHERE GAS PROCESSING IS COMPLETED OR WHERE GAS TREATMENT BEGINS, WHICHEVER IS FURTHER UPSTREAM];

Mr. Pawlowski explained that the language had been deleted for clarity; the point of production was of the utmost importance. He said that the point of production was moved to the inlet of the pipeline leaving the fields in order to

move it up and away from the gas related process and treatment facility. He recognized that there were impacts upstream, particularly in the Point Thomson field. He stated that the Point Thomson settlement provided two opportunities for the development of the Point Thomson unit: a major gas sale and a cycling project. He said that if the cycling project were to occur under existing law, only producing liquids and re-injecting the gas, all of the expenditures would be deductible. He stressed that the natures of the fields were interconnected and that the point of production had been pushed as far upstream as possible in the legislation.

[9:07:19 AM](#)

Vice-Chair Neuman argued that Point Thomson was a different unit. He wanted to discuss standard, typical processing units for gas. He wondered where the point of production changed other than the Point Thomson field.

Mr. Pawlowski answered that the gas treatment plant would be within the Prudhoe Bay unit. He said that was excluded from the point production; it was downstream of the pipeline, leaving the central gas facility to the gas treatment plant, and the costs were not included in upstream costs for the purposes of lease expenditures.

Vice-Chair Neuman said he understood. He asked where the point of production was. He asked where the point of production would be 100 miles west of Prudhoe Bay.

Mr. Pawlowski replied that the point of production would be the point where the gas was after mechanical separation leaving the field to go to the inlet of a pipeline to transport the gas to market. He stated that the point was to take out the point of production the pipelines that were moving the gas from the fields to the treatment plant and make them downstream expenditures.

Mr. Pawlowski pointed to Page 57 of the bill:

(i) not subjected to or recovered by mechanical separation or run through a gas processing plant, the farthest upstream of the first point where the gas is accurately metered, the inlet of any pipeline transporting the gas to a gas treatment plant, or the

inlet of any gas pipeline system transporting the gas to a market;

(ii) subjected to or recovered by mechanical separation but not run through a gas processing plant, the farthest upstream of the first point where the gas is accurately metered after completion of mechanical separation, the inlet of any pipeline transporting the gas after completion of mechanical separation to a gas treatment plant, or the inlet of any gas pipeline system transporting the gas after mechanical separation to a market;

(iii) run through a gas processing plant, the farthest upstream of the first point where the gas is accurately metered downstream of the gas processing plant, the inlet of any pipeline downstream of the gas processing plant transporting the gas to a gas treatment plant, or the inlet of any gas pipeline system downstream of the gas processing plant transporting the gas to a market

];

Vice-Chair Neuman asked if all of the equipment used prior would be the same that would be used in oil production.

Commissioner Balash replied in the affirmative. The equipment was needed to initially separate gas from oil; the equipment was associated with oil production. The recognition was that the facility was needed onsite in order to get the oil; therefore, it was appropriate to deduct the expense.

Vice-Chair Neuman replied that that was his point. He asked how the state would differentiate deductions taken under SB 21 for work done primarily for SB 138. He reiterated that the state could lose millions of dollars.

[9:11:12 AM](#)

Commissioner Balash asserted that the installation of new oil facilities would be a good thing for the state. He pointed out to the committee that when it came to gas the state would receive 13 percent of the gross profit, which was an excellent position for the state even if the upstream costs were allowed to be deducted as lease expenditures.

Vice-Chair Neuman asked where the point of production would change in the differentials of Point Thomson when gas was moving as opposed to solely moving oil.

Mr. Pawlowski replied that for Point Thomson the point of production would be similar because there would be a new pipeline built to move the gas from Point Thomson to the treatment plant at Prudhoe Bay; the liquids line that was being built would move 70,000 barrels per day to allow for the additional oil production that would come from the expanded build-out of the Point Thomson unit. He relayed that the point of production would be where the gas was leaving the field and going into the new pipeline to move it from Point Thomson to the gas treatment plant.

Vice-Chair Neuman asked whether the point of production would be at the inlet or outlet well.

[9:13:40 AM](#)

Vice-Chair Neuman asked if they would be upstream.

Mr. Pawlowski answered in the affirmative. He relayed that the point of production would be where the liquids separated from the gas and went into a meter or the line to move the gas from Point Thomson to the treatment plant. He said that the gas that would come out of Point Thomson would contain impurities and would need to be cleaned.

Vice-Chair Neuman asked if there was anything in the HOA that specifically stated where the point of production was and which equipment would be covered as upstream cost and which would not.

Mr. Pawlowski replied that there were specific definitions of the Alaska LNG project, which was where the point of production was defined. He said that there was a side issue concerning the agreement in the Point Thomson settlement about the treatment of upstream costs and the implications that had for royalty or other parts of the fiscal system.

Vice-Chair Neuman wondered if the upstream wells would be allowable deductions.

Mr. Pawlowski replied yes because they would be producing both oil and gas.

Vice-Chair Neuman understood that deductions under SB21 would be allowed.

Mr. Pawlowski said that was correct.

[9:16:04 AM](#)

Representative Guttenberg pointed to Page 11 of the bill which defined the Natural Gas Act using flanges, which was something that could move. He expressed concern for possible shenanigans.

Mr. Pawlowski answered that the difference was where and why the definitions were found in the legislation. He said that the reference Representative Guttenberg referred to appeared in Section 16, page 11, line 25 through page 12, line 27, and was a specific definition of the Alaska LNG project only for the purposes of authorizing and specifying AGDC's participation in the project. He furthered that the definition had been taken from the MOU and had no relationship to state tax or royalty law, but was in the authorizing statute for AGDC to participate in a project. He stated that the AGDC's power to participate in liquefaction was limited to its participation in the Alaska LNG project, therefore the specific and available definition of the Alaska LNG project had been used. He said that the other sections were consistent with state language used to build on all of the regulatory body of support that had been developed.

Representative Guttenberg asked about the point of production for oil. He pointed to Pages 56 and 57 of the bill, which related to oil. He believed that the definitions in the bill for oil and gas point of production were ambiguous.

[9:20:52 AM](#)

Mr. Pawlowski replied that the department implemented the regulations that provided the specificity. He said he would research whether there was an upgrade that would support clarity on the point of production.

Representative Guttenberg asked about infrastructure and highway maintenance. He requested the proposed cost to maintain highways during construction and operation.

Commissioner Balash replied that DOT planned carefully to distinguish how money would be spend and where. He said with regard to the condition of the Dalton Highway, and the need to add to the material in the road base, the department would work with DOT on the issue. He relayed that the list of projects on the highway identified in 2005 had led to substantial improvements on the Dalton Highway. He stated that he would attempt to get additional information from DOT on the definition and specificity of deferred maintenance versus heavy maintenance versus possible road height and clearance issues.

Representative Guttenberg asked about settlement surrounding the Yukon River Bridge.

[9:26:07 AM](#)

Commissioner Balash was familiar with a slide that had occurred and was a concern for settlement and stability. He believed that the Division of Geologic and Geophysical Survey was doing work to understand the geo-hazards in the region. He admitted that what exactly needed to be done with the bridge was a big question.

Co-Chair Austerman asked for clarification on the project titles: Alaska LNG Project and the North Slope Natural Gas Pipeline Project. He felt that the two titles indicated two different projects.

Mr. Pawlowski shared that the legislation was enabling legislation for the Alaska LNG Project as described in the HOA, and was also general law, applicable and important to advance any natural gas project. He said that the state was currently looking at two natural gas projects and that the reference to the North Slope Natural Gas pipeline was necessitated by building off of the architecture of HB 4. He explained that the terms and powers, the need for the Department of Natural Resources to facilitate gas moving through a project, would be needed for any project with which the state went forward. He asserted that the law in SB 138 would support all forms of gas development on the North Slope.

[9:29:15 AM](#)

Representative Wilson understood that the under the legislation the state would take all earning in gas.

Commissioner Balash replied that there would be much taken in gas but that there would be fairly significant streams taken in cash; specifically, the corporate income tax and property tax.

Representative Wilson asked how the state could guarantee that credit given would be seen as revenue.

Mr. Pawlowski replied that the arrangements would be long-term contracts and would have a moving price mechanism. One of the reasons why the state could want to be hesitant about only using the producers to sell the gas would be because the producers would have had a different risk tolerance than the state. He said that sometimes LNG projects were designed with an "s" curve, one of many terms that were negotiated in the contracts and each contract would be different. The contract would specify how money changed hands for the gas.

[9:32:19 AM](#)

Representative Wilson understood that Mr. Pawlowski spoke of the terms to sell the gas and not the gas that the state would take in lieu of taxes. She expressed concern for fluctuating gas prices and the state not receiving full payment.

Mr. Pawlowski believed it was important to remember that under the in-value circumstance, the producer would take the gas and sell it for a price with was in constant flux; the difference in in-kind was that the state was taking and selling the gas. He said that the price change would occur with both an in-value of an in-kind scenario. He stated that unless the state was directly holding the gas it risked losing control over the appropriate deductions being in place at the LNG plant. He stressed that the state had more control in an in-kind situation for the project.

Representative Wilson maintained her disconnect.

Commissioner Balash pointed out to the committee that with a project with such a large price tag, property tax would be a significant cash flow element.

[9:36:31 AM](#)

Representative Wilson asserted that the state needed affordable natural gas. She probed the definition of "direct access."

Commissioner Balash admitted that there were many unknowns. He referred to page 60, Section 67 of the legislation, which required DNR to identify the various scenarios and methods of getting gas from the North Slope to market and within the state. He said that the issue of who was responsible to satisfy in-state demand would be discussed. He believed that part of the answer would be driven by market factors and part would be driven by which players were engaged. He shared that one of the reasons the administration liked that each party would be responsible of its share of the gas, infrastructure and capacity was because then everything would be even along the way. He said if the state alone was responsible for satisfying in-state demand then the state's share of the project at the liquefaction plant would be altered. He noted that MOU with TransCanada contained provisions for backhaul service, which would allow the same low prices for gas to be allowed throughout the state.

[9:40:10 AM](#)

Representative Wilson remarked that the Interior had access to heating oil but that it was not affordable.

Representative Munoz noted that the bill allowed AGDC to be involved in 2 projects. She wondered at what point the efforts would come together to focus on one project.

Commissioner Balash answered that the work that would be done during the pre-FEED phase would include and assessment and efforts to initiate marketing of the LNG by each of the parties. He said that the key question was: would any of the parties be able to sell the LNG from this project at a price that warranted the required investment. He said that the cost of continuing into the FEED phase would rise to approximately \$2 billion, which was a large amount of money even when spread across the parties involved. He said that if the decision to go forward was a positive one, the project would go forward. He stated that AGDC and the Alaska Stand Alone Project (ASAP) project would assure that if Alaska LNG did not go forward there was an alternative project in place. He could not speak to which project would move forward more quickly and believed it should be left to

the AGDC board of directors. He said that the changes made to the AGDC statues in the legislation would give them the flexibility to decide how and when to advance the ASAP project. He believed that the decision as to which project would move forward would be made in 2015.

[9:46:37 AM](#)

Co-Chair Austerman asked for further explanation of ASAP.

Commissioner Balash replied that with the passage of HB 4 the legislature gave AGDC a mission to develop the in-state natural gas pipeline project. He relayed that ASAP referred to The Alaska Stand Alone Project.

Commissioner Balash said that the ASAP project remained available to pursue in the years to come if the Alaska LNG project failed to move forward.

Co-Chair Stoltze spoke to the potential for a special session.

Representative Holmes referred to talk about the financial risk the state would bear during the early years. She asked about sideboards and protections for the state's interest.

Commissioner Balash replied that the state was seeking allies. He said that the alliances shifted from topic to topic. He thought that the balance of interest and the tension between the parties would ultimately work in the state's favor. He explained that the state was aligned with producers in terms of wanting to keep overall project costs down while seeking the highest value for the resource itself. He opined that where alignment broke down was in the development of gas that did not belong to the producers. He said that the state had a financial interest through either royalty, production tax, or both, in hundreds of trillions of cubic feet below ground in the North Slope region. He stated that he was encouraged in the alignment of interest with TransCanada to optimize expansions in the future. He furthered that having a company that was looking out for its own financial interests was something that the administration saw as valuable. He spoke to provisions that were built into the MOU requiring TransCanada to check with the state on work plan and budget. He said that if a matter arose that the state was dissatisfied with and opposed to, TransCanada was

required to vote against it per the governance structure of the joint venture. He asserted that the state would be aware of the goings on of the project, while relying on TransCanada's specific expertise day-to-day for the ultimate execution of the project. He reported that there was a provision in the HOA that was intended to support the conveyance of information by TransCanada and AGDC during the development phase, which gave them the ability to share information with state agencies.

[9:54:02 AM](#)

Representative Holmes wondered whether the obligation for TransCanada to vote down elements that were unattractive to the state was legally binding.

Mr. Pawlowski replied that the provision could be found on Page 6, exhibit C, the term sheet to the MOU. He said that the MOU had a different threshold of whether it was legally binding and the terms would be incorporated into the agreement. He said that the language would be binding in the interim agreement executed by the Commissioner of Natural Resources. He concluded that it would ultimately have to come before the legislature for approval.

Representative Holmes asked for the administration's position on the 20 versus 25 percent, and when and how the number would get locked in.

Mr. Pawlowski replied that the 25 percent was the combination of the state's royalty share plus the production tax; the production tax was levied after royalty, so the 13 percent production tax, when combined with the royalty share equated to approximately 25 percent. He furthered that the administration's decision surrounding the appropriate tax rate was part of the work that DOR and DNR had undertaken during the royalty study. The question of when terms would be locked in remained open.

[9:59:02 AM](#)

Representative Holmes assumed that the state's ownership share of the infrastructure would come before the legislature, she queried whether the administration had any recommendations.

Commissioner Balash replied that in reviewing the project the administration had estimated that being an equity participant in the project made sense as long as the state's share of the project was 20 percent or greater. He said that if the number were to fall below 20, the administration would likely recommend a different course of action. He shared that the agreements that would be developed over the next 18 months would deal with the long-term equity shares in the infrastructure and the offtake and balancing agreements. He said that the agreements needed to "sync up." He stated that time would be spent to identify the details around net profit share leases and sliding scale royalties. He asserted that SB 138 would assure that the state's production tax interest was "x", and would allow the state to go forward and develop the remainder of the agreements to bring back to the legislature.

[10:02:08 AM](#)

Co-Chair Stoltze contested that TransCanada had not been the state's first choice for a partner in the venture. He suggested that the state had been coerced into the partnership.

Representative Costello asked whether the state should be attempting to pay down its debt over the next decade.

Commissioner Rodell answered that the state currently had commitments and liabilities to consider before entering into the FEED stage of the project in 2016. She thought that the state should be set up in the position where current liabilities were managed and within the legislature's control and the state's rating was maintained in order to receive credit from investors and partners.

[10:07:08 AM](#)

Representative Costello understood that because of the involvement with TransCanada, when the gas started flowing the state would see \$300 million less coming into the state annually. She wondered whether the administration had conducted a risk reward analysis. She felt that the number was significant.

Commissioner Rodell replied that the department had looked at issue as a cost/benefit analysis, rather than a

risk/reward analysis. She felt that the forgone revenue was a cost of participation that would yield greater benefits to the state. She estimated that going forward alone was not an option because of the burden and cost it would place on the state was too significant.

[10:09:49 AM](#)

Co-Chair Austerman believed the committee needed to spend more time on the issue. He requested that the department research the issue and bring more information at the next bill hearing.

Representative Costello queried the issue of rolled-in rates.

Commissioner Balash responded that terms were driven by the tariff design. He said that the capital structure, the debt to equity ratio for the tariff, was huge. He stated that the state would get further by having a larger debt component than squeezing down on the return on equity component. He divulged that lowest tariffs possible were the goal. He stated that the partners in the venture did not have the same desire for low tariffs because they were involved in the entirety of the value chain. He said that access to the pipeline and pipeline facilities as well as the liquefaction plant had been taken into consideration. He relayed that FERC would have exclusive jurisdiction on the regulation of the liquefaction plant, which was centered on health, safety and the environment. He furthered that FERC did not regulate for access or rates, so the state had nothing to rely on from a regulatory perspective to assure that those things happen. He asserted that the solution to the problem was for the state to step into the participation role where each party would be responsible for their share of the project. He said that there would be four pipes in the pipeline and not one tariff; in the suggested proprietary arrangement each party would be responsible for the financing of its share of the project and therefore able to set its own commercial arrangements for use of the capacity built with the capital expenditure, extending all the way down to the liquefaction plant. He said that the question about rates became obsolete because there would not be a rate that all of the parties would pay and contribute to, each would be responsible for their own share. He pointed to Appendix A in the HOA, which listed the ability for any of the parties

to expand any component to the project as long as the other parties were held harmless, others could participate but did not have to. He thought that this would result in a situation where third parties would be confident in their ability to access capacity on the share of the pipe for which the state and TransCanada were responsible.

10:16:58 AM

Commissioner Balash furthered that an agreement had been secured in the MOU on the capital structure for any expansions, even though it was unknown what the cost of debt or equity would be in the future. He stated that the amount of spare capacity present in the line would depend on the specific size of the pipe. He shared that the initial plan was for the pipeline to be 42 inches, the initial throughput was expected to be in the 2.8 billion cubic feet per day range. He understood that there was to be upwards of a billion cubic feet per day of capacity available through compression until looping was necessary. He relayed that looping increased costs and heightened the need for a rolled-in rate approach. He said that the department would confirm during the pre-FEED phase what the capacity of the project ultimately was and what the increments looked like. He remarked that the pipe would have flexibility in size, but that the liquefaction plant was not as flexible. He said that an expansion to support another liquefaction train would need to be very large and would require a large discovery of gas. He believed that the department had been successful in achieving access and a capital structure resulting on low tariffs. He did not believe that rolled-in rates would be necessary, it would depend on the size and capacity of the project from day one to what it was expandable to without looping.

Representative Costello understood that the nature of the project being unregulated would be a hinge-point for other decisions.

Co-Chair Austerman discussed the direction he hoped to take during the upcoming 1:30 pm meeting. He hoped to focus on the state shifting from a tax based to a profit based structure. He discussed further housekeeping.

Representative Gara asked if the administration would address a provision in the contract concerning who paid the full cost of future expansion.

Co-Chair Austerman reiterated his desire to concentrate on the tax portion of the issue.

CSSB 138(FIN)am was HEARD and HELD in committee for further consideration.

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ADJOURNMENT

10:24:33 AM

The meeting was adjourned at 10:24 a.m.