

**ALASKA STATE LEGISLATURE  
HOUSE RESOURCES STANDING COMMITTEE**

February 26, 2014

1:08 p.m.

**MEMBERS PRESENT**

Representative Eric Feige, Co-Chair  
Representative Dan Saddler, Co-Chair  
Representative Peggy Wilson, Vice Chair  
Representative Craig Johnson  
Representative Kurt Olson  
Representative Paul Seaton  
Representative Scott Kawasaki  
Representative Geran Tarr

**MEMBERS ABSENT**

Representative Mike Hawker

**OTHER LEGISLATORS PRESENT**

Representative Andrew Josephson

**COMMITTEE CALENDAR**

OVERVIEW(S): GAS PIPELINE ISSUES - FISCAL PERSPECTIVE

- HEARD

**PREVIOUS COMMITTEE ACTION**

No previous action to record

**WITNESS REGISTER**

ANGELA RODELL, Commissioner  
Department of Revenue (DOR)  
Anchorage, Alaska

**POSITION STATEMENT:** Presented a PowerPoint titled "AK LNG: Long and Short Term Fiscal Impacts."

DEEPA PODUVAL, Principal  
Management Consulting Division  
Black & Veatch Corporation;  
Consultant, Department of Natural Resources (DNR)  
Houston, Texas

**POSITION STATEMENT:** Answered questions during Commissioner Rodell's presentation.

**ACTION NARRATIVE**

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**CO-CHAIR ERIC FEIGE** called the House Resources Standing Committee meeting to order at 1:08 p.m. Representatives Feige, Seaton, P. Wilson, Tarr, Kawasaki, and Saddler were present at the call to order. Representatives Johnson and Olson arrived as the meeting was in progress. Representative Josephson was also present.

**OVERVIEW(S): Gas Pipeline Issues - Fiscal Perspective**

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CO-CHAIR FEIGE announced that the only order of business was a presentation by Commissioner Rodell, Department of Revenue, regarding the long and short term fiscal impacts of the proposed Alaska Liquefied Natural Gas (LNG) Project.

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ANGELA RODELL, Commissioner, Department of Revenue (DNR), said that she would talk about the long and short term fiscal impact of participation by the state in the Alaska LNG project. She relayed that there were three aspects to review before the state could determine its capacity for participation in the project. The first aspect, debt capacity, entailed outstanding state debt for commitments and what the state could afford to add to this. The second aspect, the gas line analysis, would be presented by Black and Veatch. The third aspect would entail the revenue forecast.

COMMISSIONER RODELL directed attention to her presentation titled "AK LNG: Long and Short Term Fiscal Impacts." She addressed slide 3, "A note on uncertainty...." which detailed that the goal was for determination of the project impact on the short term, mid-term, and very long term. She reported that currently the state was reviewing whether it could manage its way through the short and mid-term impacts in order to benefit in the long term. She said that this analysis would include a range of possible outcomes based on the adjustment of these

assumptions, which would be continually refined as the project moved forward.

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REPRESENTATIVE KAWASAKI, referencing slide 3, asked why the state was introducing the proposed LNG bill without doing refinements to the analysis.

COMMISSIONER RODELL explained that the state had prepared the proposed bill with an analysis to determine the best way to move forward, which had led to agreement for the Heads of Agreement (HOA), the Memorandum of Understanding (MOU), and the currently proposed bill. She pointed out that this analysis was being shared with the legislature for clarification to the direction the state should take.

REPRESENTATIVE KAWASAKI said that he would have expected a refined analysis prior to the actual decision for an HOA or an MOU.

COMMISSIONER RODELL replied that not all the decisions had been made, and a bill had not yet been passed that would determine the gas tax. She declared that the current analysis was based on what the administration had included in the proposed bill, and the analysis would continue to be revised.

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The committee took an at-ease from 1:14 p.m. to 1:19 p.m. due to technical difficulties.

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REPRESENTATIVE P. WILSON asked whether DOR had taken into account PERS [Public Employee Retirement System] and TRS [Teacher Retirement System], and the effect of each aspect on the state's fiscal status.

COMMISSIONER RODELL confirmed that all the state obligations had been reviewed, although not all were discussed in this presentation.

REPRESENTATIVE P. WILSON asked if the payments for these obligations were also considered.

COMMISSIONER RODELL expressed her agreement.

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COMMISSIONER RODELL, in response to Representative Tarr, explained that the assumptions were being made using today's market conditions, although it was unknown what interest rates would be in eight years. She noted that there was a federal proposal to remove tax exemptions for some debt, which would include this type of debt. She explained that this projection assumed that the debt was taxable and that interest rates would remain unchanged from today. She relayed that all of this could change, hence the periodic adjustments to project outcomes.

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REPRESENTATIVE KAWASAKI inquired whether the models take into account the long-term, major maintenance needs 20 years from the present. He offered examples of roads and other current construction projects that would need future maintenance.

COMMISSIONER RODELL acknowledged that the model did not yet include this, as there was not enough information for the necessary reserves for operations and maintenance for this project. She offered her belief that this early analysis would need refinement, and due diligence for these future requirements for infrastructure surrounding the project. She noted that the roads, bridges, schools, and support networks had not been included in this projection of demands to be placed on the state. She allowed that the state did not yet have a sense of this impact, which was why this was being conducted "as a stage gated approach." This would allow reassessment for state participation.

REPRESENTATIVE KAWASAKI noted that the license for the Alaska Gasline Inducement Act (AGIA) had a lot of this data, especially for labor and work force development, and the demands on communities. He opined that the total cost of the project was being understated if this was not included in the model.

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COMMISSIONER RODELL directed attention to slide 5, "Debt capacity: current debt outstanding," and she reviewed the state's outstanding debt for the years 1999 to 2014. She pointed to the significant increase in the general obligation and the state-supported debt during that time period. This debt was on the books for the state to support. She directed

attention to the general obligation debt which included a \$450 million general obligation bond authorization for transportation and ports in 2012. She explained that, as \$303 million was still authorized but not yet issued, it was not yet outstanding debt. She noted that there was an additional authorization for \$695 million under the State Guaranteed, which had not yet been issued by the Alaska Housing Finance Corporation, although it was still guaranteed by the state.

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REPRESENTATIVE SEATON referenced the Knik Arm Bridge project (KABATA), which required a \$125 million bond in addition to the capital from the state, and the possibility for Alaska Industrial Development and Export Authority (AIDEA) to issue a few hundred million in bonds for oil and gas processing facilities. He asked whether these increases of debt categories would significantly impact this analysis for bonding ability, or should they be reviewed individually.

COMMISSIONER RODELL replied that these projects would be added to the debt and would impact the amount of additional debt which the state could incur. She noted that a question that must be reconciled was whether a portion of the debt capacity should be reserved for other state government business, or should it all be used for an Alaska LNG project. She declared that this was a tension for the project although she opined that there was a way to preserve the debt capacity for state government operations, such as road infrastructure and marine facilities, while utilizing other financing mechanisms for the Alaska LNG project, which made the Trans Canada MOU very attractive.

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COMMISSIONER RODELL moved on to slide 6, "Debt capacity: Historically, debt service has been low relative to revenue," and stated that the state had an historical practice for pay as you go, while limiting the amount of overall debt issued. She pointed to the debt service in Fiscal Year 2013, which was 1.7 percent of revenue.

COMMISSIONER RODELL, responding to Representative Tarr regarding slide 5, said NTSC was the Northern Tobacco Securitization Corporation, which was the tobacco settlement money.

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CO-CHAIR SADDLER asked if the percentage of revenue was undesignated general fund.

COMMISSIONER RODELL confirmed this was unrestricted general fund.

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COMMISSIONER RODELL referenced slide 7, "Debt capacity: Projected debt service," which included projected debt service along with the school debt reimbursement program. She reminded the committee that the state would support a majority of debt issued by municipalities and school districts for school capital construction. She pointed out that the highest supported debt was 9.3 percent in 1987, and when the school debt was included this became 15.8 percent. She said that the state debt levels had been significantly higher in past years than currently contemplated without the Alaska LNG project. She stated that it was important to note that the state had an A rating in 1987, which was significantly lower than the current rating.

REPRESENTATIVE SEATON asked for clarification that this depicted a percentage of unrestricted revenue, and not dollars, as the current outstanding debt was currently much higher, although the current revenue was also much higher.

COMMISSIONER RODELL acknowledged that unrestricted revenues were currently higher than 1987, and she explained that a volatile revenue source created a challenge for forecasting forward using certain assumptions as the percentage for level of debt could shift significantly.

COMMISSIONER RODELL, in response to Representative Tarr, said the top line on slide 7 included the school debt.

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COMMISSIONER RODELL addressed slide 8, "Financial Management and Debt Metrics," and said that, as general obligation (G.O.) bonds carried a pledge of the full faith, credit, and resources of the state, any taxes necessary would be raised to repay this debt. She stated that state policy, approved by the State Bond Committee, limited debt service to less than 8 percent of general fund unrestricted revenue; debt service had remained low for 15 years, with a 10 year average of 1.5 percent and 3.3 percent when the school debt reimbursement was included. She relayed that the historical preference had been for pay as you

go funding versus debt, which accounted for the low debt relative to most other states.

CO-CHAIR SADDLER asked about the genesis for the aforementioned state policy.

COMMISSIONER RODELL replied that this was an administration policy, explaining that the long-standing State Bond Committee was comprised of the commissioners of Department of Revenue, Department of Administration, and Department of Commerce, Community & Economic Development. She declared that this was a good practice policy, and noted that the State Bond Committee also fulfilled the obligations directed to it by the legislature and the executive branch.

COMMISSIONER RODELL, in response to Representative Tarr, acknowledged that a debt service in excess of 8 percent was merely a violation of a self-imposed policy.

COMMISSIONER RODELL turned to slide 8, saying the state planned to issue a Bond Anticipation Note in March, 2014, to replace the existing note and to add additional proceeds. The original note sold for a 0.09 percent interest rate. There was anticipation for this note to be \$230 million, with an additional sale for \$35 million of a Certificate of Participation to benefit the residential facility for the Alaska Native Tribal Health Consortium, approved by the legislature in 2013.

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COMMISSIONER RODELL, responding to Co-Chair Saddler, explained that a Bond Anticipation Note was in anticipation for the issuance of a long term bond. This allowed the management of costs as the issuance of long term tax exempt bonds was a commitment to spend the money within three years. She reported that the money was not always spent in the time frame anticipated, and, as it was necessary to keep the money liquid, it could cost the state a significant amount, negative arbitrage. This was the difference between the payment and the amount of investment income. The Bond Anticipation Note allowed for more prudent money management with no long term high debt cost if the money was not spent in a timely fashion.

COMMISSIONER RODELL returned to slide 8, and shared that there had been discussions about state financial support for a number of strategic capital initiatives.

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COMMISSIONER RODELL moved on to slide 10, "Options Identified by State for Equity Participation - 20%," the Black & Veatch analysis. There were three options identified by the state for equity participation at the 20 percent level: the State of Alaska goes it alone for all three components of the project; the State of Alaska works with Trans Canada on the GTP and the Pipeline, does not exercise any option to participate further, and the cash participation is solely for the LNG facility; or, the State of Alaska exercises its option within the MOU with Trans Canada to buyback 6 percent of the GTP and the Pipeline, and still invest 20 percent for the LNG facility.

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COMMISSIONER RODELL directed attention to slide 11, "Implications of Options and Potential Off Ramps - 20%." She reported that the State of Alaska would go it alone during pre-FEED, although it would require support of \$87 million for 20 percent participation. She said that participation in the liquefaction would cost the State of Alaska \$35 million, which would be the same at that time with the 30 percent buyback option with TransCanada, as the state would not exercise its option until the end of pre-FEED. She described the FEED stage, which would require approximately \$360 million for the state to go it alone, and would require \$144 million for the liquefaction facility with TransCanada. If the state exercised its 30 percent equity option with TransCanada, it would be necessary for the state to generate \$226 million.

COMMISSIONER RODELL offered her belief that the State of Alaska was in a comfortable position to exercise an option in any of the scenarios. She said that the issue would arise at the FID gate, and she reported that for the State of Alaska to go it alone would cost more than \$10.6 billion while the liquefaction with TransCanada would require more than \$5 billion. If the state exercised its option with TransCanada, this would be closer to \$7 billion. These decisions would require careful thinking to manage 2019 through 2023 for ways to generate participation at any of these levels.

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COMMISSIONER RODELL discussed slide 12, "Can the State Go It Alone? State's Debt Capacity." In terms of financing the state's share and debt service, she described the scenarios as

outlined by Black & Veatch: the first scenario to not affect the state rating, the projection of all debt on the books including debt authorized but not issued would be 5 percent of general fund revenue. This would allow about 3 percent of general fund unrestricted revenue to work with in order to maintain the state policy of debt service less than 8 percent, and it would generate the lowest cost of interest for participation, about 4.6 percent on a taxable basis. The second scenario, to allow the State to exceed the 8 percent ceiling for debt service and structure the debt to an A rating, would have a higher cost for credit, and the debt cost would be about 4.9 percent. The final scenario to move the ceiling of debt service to 11 percent of unrestricted revenue would offer a BBB+ rating, with a 5.6 percent debt cost.

REPRESENTATIVE SEATON asked for clarification that the bond rating agencies reviewed the self-imposed 8 percent debt ceiling to give the state a AAA rating, whereas a 10 percent debt ceiling service would give the state an A+ rating. He asked if this was speculation for these ratings and cost of debt service.

COMMISSIONER RODELL explained that it was an assumption based on criteria of the state's position today, knowing that the revenue source was volatile and there were other commitments, and reviewing the revenue during that time period of 2019 - 22. She acknowledged that revenues would be lower, but that the state would manage its way through the expenses, as there were benefits at the end. She reported that the state needed to manage its expenses to keep them low, as that would make more unrestricted general fund revenue available for debt service, which would change the metric. She said that as the state knew what the criteria were for the various ratings this was an estimation of the costs and how to affect them.

REPRESENTATIVE SEATON inquired whether permanent fund earnings were calculated as revenue in these forecasts, or did this just include the oil, fish, and mining taxes as revenue sources.

COMMISSIONER RODELL replied that it excluded the other revenue to the state because that revenue had not been counted on in the same way as the unrestricted revenue. She relayed that the desire was to keep this as "a pure unrestricted revenue tax obligation of the state."

REPRESENTATIVE SEATON declared that there was a huge amount of unrestricted general fund revenue that came from investments, and although it was not necessary to spend it, it could be used

to calculate a bond rating. He questioned why this revenue would be hidden, allowing the bond rating to decrease and the price of the project to increase. He expressed his concern, and suggested that this be reviewed and all available revenues be included in the calculations.

COMMISSIONER RODELL expressed her agreement to include that analysis. She offered her belief that the feedback received from the rating agencies, which she deemed to be fair, was that the state was unwilling to tap those resources for debt, and was more willing to cut expenses, instead. She declared that the corpus of the permanent fund did not give the state its AAA rating, and it was not counted by the rating agencies.

REPRESENTATIVE SEATON clarified that he was referring to the earnings as 50 percent of those were appropriated each year to pay the permanent dividends, and the balance was available as an asset. He stated that, as the project was significant and valuable to the state, the legislature should determine whether these earnings could be available for this calculation. He requested an estimate using these earnings.

COMMISSIONER RODELL said that the constitutional budget reserve was taken into account for the credit ratings, and the permanent fund earnings reserve was also used.

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CO-CHAIR SADDLER directed attention to slide 12, and asked about the various levels of debt. He asked about the debt service in scenario 1, and if this was limited to the proposed pipeline or in addition to the other 5 percent obligated for debt.

COMMISSIONER RODELL replied that this was the amount for the Alaska LNG project, which was in addition.

CO-CHAIR SADDLER mused that each scenario became more expensive.

CO-CHAIR SADDLER referenced slide 11, and asked if the red boxes were the off-ramps should the state decide not to proceed.

COMMISSIONER RODELL stated that this was the cost to the state to exercise those off-ramps.

CO-CHAIR SADDLER asked how the costs could be so precise.

COMMISSIONER RODELL deferred to Ms. Poduval.

DEEPA PODUVAL, Principal, Management Consulting Division, Black & Veatch Corporation; Consultant, Department of Natural Resources, said that these costs were attained from the cost estimates for the project. Although there were better understandings for the project costs in the Pre-FEED stage, it was less precise in the FEED stage, and the construction stage should be estimated to the nearest hundred million dollars.

CO-CHAIR SADDLER asked if the \$5.4 billion was the cost for the liquefaction construction.

COMMISSIONER RODELL acknowledged this.

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COMMISSIONER RODELL directed attention to slide 13, "Can the State Go It Alone? State's Debt Capacity," which reviewed the portion of debt to equity and the range that the state could adjust. The range between debt and equity was the factor for determining the credit rating and the interest cost. She stated that the higher the rating, the lower the interest cost, and the lesser amount of debt. She pointed to the graph as a reflection of the effect of market conditions on February 20, 2014. She expressed her interest in the comparison of the TransCanada options with the state to "go it alone." She noted that a tremendous amount of cash would be necessary in any scenario; however, inclusion of TransCanada in each scenario created relief to the state for generating so much cash for participation.

REPRESENTATIVE SEATON asked for clarification to the cost scenarios for TransCanada with no buyback and with 30 percent buyback. He asked whether this was just the portion of the state investment, and if the total investment would be the same in each scenario.

COMMISSIONER RODELL expressed her agreement that this graph just showed the investment from the State of Alaska, and its requirement for participation in each of these three scenarios. Addressing Scenario 1, Go it Alone, she declared that the state would have an investment of \$11 billion, with more than \$8 billion in equity. If the state did not exercise its buyback option with TransCanada, the state would still have to raise money for its participation in the liquefaction, about \$5.6 billion, with half being equity. This graph explained the cost

of state participation and the amount of debt necessary to raise the cash.

CO-CHAIR FEIGE asked for an explanation to the debt/equity range boxes for each bar of the graph on slide 13.

COMMISSIONER RODELL deferred to Ms. Poduval.

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MS. PODUVAL explained that slide 13 showed the debt equity range, and how much debt the state could accept in each of the three scenarios. She pointed to scenario 1, the lowest interest costs with the highest quality debt through scenario 3, with the lowest quality debt and the highest interest costs. She said that associated with this was the percentage of general funds that needed to be dedicated to service the debt. The lower the percentage of dedicated general funds to service the debt, the more comforts to the lender and the lower the interest cost.

MS. PODUVAL explained that the general fund over the 25 year loan period was reviewed to obtain the debt equity range. She noted that, as this would change annually dependent on the revenue forecast for the Alaska LNG project and the other state revenues, they chose the lowest unrestricted general fund revenue over this 25 year period with the assumption to not exceed 3 percent of this for debt service. That makes the loan amount part of the debt equity range. The higher part of the debt equity range was an average of the unrestricted general fund revenue over this 25 year period with the assumption for the debt service to not exceed 3 percent. She opined that this offered a mid-range and a conservative estimate for debt service.

REPRESENTATIVE TARR asked if the 0.5 figure in the bar graph on page 13 represented \$500,000.

MS. PODUVAL replied that this was \$500 million.

CO-CHAIR SADDLER asked for clarification that the high point of the range was calculated on the highest percentage of the unrestricted general fund revenue, while the lowest point of the range was the lowest percentage. He asked if there was a hard number limit.

MS. PODUVAL replied that the low part of that range was using the lowest unrestricted general fund revenue over the 25 year

period, while the high part of the range was using the average unrestricted general fund revenue over the same period.

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COMMISSIONER RODELL addressed slide 15, " AKLNG - Long Term Potential: Assumptions." She first outlined the assumptions used in order to manage through the amount of cash necessary, which were a review of the revenue forecast and the value to the state for participation in the project. She reported that the long term revenue forecast assumed a 2 percent annual decline for oil revenues and brought the gas revenues on line beginning in 2024. She shared the export volume assumption of 2.5 Bcf per day and an in-state volume of 0.25 Bcf per day for these modeling purposes. They also assumed that the price of oil would be \$90 per barrel in 2014, with a 2.5 percent increase annually. The calculated LNG price was estimated from the oil price at 13.5 percent the price of oil plus \$1. The general fund unrestricted revenue was assumed to include royalties, property tax, and state corporate income tax, production tax, and return on equity on the Alaska LNG project investment. She declared that the same three aforementioned scenarios were used, Go it alone, TransCanada with no buy back, and TransCanada with buy back. These all assumed that the state participation would continue at 20 percent, in order to maintain consistency throughout the modeling.

REPRESENTATIVE TARR, referencing the bullet point on slide 15 which assumed the general fund unrestricted revenue to include 75 percent of royalties, asked if this was projected for 2024 and beyond, when the Alaska LNG project came on-line.

COMMISSIONER RODELL expressed her agreement and noted that the revenue forecast was used during the construction period. She reminded the committee that 25 percent of the royalty revenue would go to the permanent fund.

CO-CHAIR FEIGE stated, "We don't want to touch that."

REPRESENTATIVE OLSON reflected on the Amerada Hess fund, noting that although the interest could be spent, the principal could not be used "because it would taint any future jury pools on the permanent fund which is why we have it sitting off in space." He asked how much was currently in the fund.

COMMISSIONER RODELL replied that she would have to research this.

REPRESENTATIVE OLSON asked if this could be used as security, or to pay down, on the proposed pipeline.

COMMISSIONER RODELL replied that Department of Revenue would review this and get back to the committee.

REPRESENTATIVE OLSON opined that this was only discussed every four or five years.

REPRESENTATIVE SEATON compared the first bullet point on slide 15, which listed an annual 2 percent decline of oil revenues between the years 2020-2024, with another bullet point that stated the oil price was increasing annually at 2.5 percent. He asked whether the decline in oil production was overpowering the value of the oil.

COMMISSIONER RODELL, in response, said that this was not a straight line projection; although there was a projected decline in production which would affect the top oil revenue decline. Within the revenue forecast, there was an assumption for this increase in oil prices, which was consistent with the forecasted revenue projections.

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REPRESENTATIVE SEATON asked about the annual decline of 2 percent in revenue, although the revenue projections included an annual increase of 2.5 percent. He asked about the projection for 2020 - 2024, as it appeared that this loss of production should also be reflected in the revenue projection.

COMMISSIONER RODELL replied that price and production impact differently and therefore the numbers could not be added to create an adjustment factor. She relayed that production had one effect on the revenue forecast. She reported that the Office of Management & Budget (OMB) assumed a slightly higher level of production for its trend. The price for oil was consistent with the forecast of a 2.5 percent growth rate, although making a determination of LNG prices required a different index than oil.

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COMMISSIONER RODELL moved on to slide 16, "North Slope Production Forecast," the oil production forecast for 2014 - 2023. She said that the assumption by the Department of Revenue

forecast was the band labeled GVR Eligible (New Oil). She directed attention to the OMB Upside Potential, 50 percent of which had been incorporated into the revenue assumption model, as well.

CO-CHAIR SADDLER asked for clarification to the definition of upside potential.

COMMISSIONER RODELL replied that upside potential was defined as the barrels which Department of Revenue would have included in past forecasts as under development or under exploration. She explained that the methodology had been changed two years prior to account for all the risk under that method, as it could be an overly optimistic projection. She stated that the further out the expectation for those barrels to come on-line, the more it was assumed that it would not happen. She said that those projected barrels were added back into the projection when it was more apparent the barrels would come on-line and produce revenue to the state. The upside potential was available in the previous forecasting methodology as work that was being done and the expectation for those barrels to come on-line.

CO-CHAIR SADDLER reflected that this was an artifact of the truing up of the forecast model, as in the past it would have been counted, whereas it was now being hoped for.

COMMISSIONER RODELL agreed.

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COMMISSIONER RODELL directed attention to slide 17, "Revenue Forecast-Official, and Mid/High Case." She pointed to the official fall forecast, 2013, in comparison to the mid/high case forecast if 50 percent of the upside potential materialized, with the major differences coming in the Fiscal Years 2020 to 2024 as discussed previously.

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COMMISSIONER RODELL presented slide 18, "Revenue Forecast vs AKLNG Obligations," which compared the obligations for the proposed gas pipeline project to the prior slide. She reported that the general unrestricted forecast, as well as the official forecast, was near \$5 billion annually, compared to the obligations for all three scenarios, which depicted that amount available for the other state government funding necessities.

REPRESENTATIVE SEATON asked for clarification that the lower bars on the graph were the costs from the project, compared to the upper bars depicting the projected revenue.

COMMISSIONER RODELL acknowledged this, and added that it also showed the value of a partnership for lowering the obligation costs.

CO-CHAIR SADDLER referred to slide 18, and asked for clarification to the lower lines, whether they were debt service or total equity cost.

COMMISSIONER RODELL explained that the blue line was the required cash obligation to TransCanada as a 100 percent partner through either debt service or equity. She pointed out the percentage relationship of the lower lines for debt service to the upper lines depicting the general fund unrestricted revenue, and noted that this had to be financed through either debt or equity. She reminded the committee that, as the state did not have the capacity for 100 percent debt, it would be necessary to finance the equity portion. She declared that this was what slide 18 was designed to show.

REPRESENTATIVE TARR asked if the data points on the graph line reflected a fiscal year.

COMMISSIONER RODELL replied that this was correct.

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COMMISSIONER RODELL offered slide 19, "AKLNG Obligations vs. GFUR Forecast," and explained that this represented a conversion of the obligation dollar amounts from the previous slide to a percentage of unrestricted general fund revenue.

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COMMISSIONER RODELL turned to slide 20, "AKLNG - Long term potential," and opined that the reason for taking on this obligation was for its long term potential and its long term fiscal impact on the state. She pointed out that there was tremendous revenue to the state once gas was flowing, although this would require careful management until that point. She said that, although there was more upside if the state goes it alone, the risk was lower with partnerships, even though it meant lower revenue. She pointed out the cost difference to the

state for a "go it alone" versus a "TC No Buyback" was \$300 million annually.

REPRESENTATIVE TARR, referencing slide 20, pointed out that the label on the vertical axis was labeled millions of dollars, and she asked if it should actually reflect billions of dollars.

COMMISSIONER RODELL concurred.

REPRESENTATIVE SEATON offered his belief that the graphs on slide 19 and slide 20 showed that the amount of unrestricted general revenue for investment between 2020 and 2023 shifted between 30 and 60 percent, if all the costs remained as anticipated. He mused that this would be even more if there were higher costs, especially if the state was a 20 percent equity owner without any investment from TransCanada.

COMMISSIONER RODELL confirmed that Representative Seaton was reading this correctly, and pointed to the negative revenue on slide 20 between 2014 through 2024 as a reflection of the percentages on slide 19.

REPRESENTATIVE SEATON pointed out that it was questionable whether the state could sustain the level of expenditure in the intervening years prior to 2024 without finding another source of revenue.

COMMISSIONER RODELL confirmed his analysis, and expressed her confidence that the state could manage through this and would be able to find partnerships and negotiate contracts. She opined that this would be more definitive in the upcoming year, especially after the FEED stage. She stated that, as all the other partners were interested in limiting the cost overruns, there was encouragement for participation with the large oil producers. She opined that discussion for equity participation greater than the illustrated 20 percent would be very difficult for the state to absorb. She reported that this range of participation had been deemed beneficial for royalties while allowing for management of cash flow. She allowed that potentially there would still be some hard decisions.

REPRESENTATIVE SEATON requested that slides 18, 19, and 20 be offered showing equity of 25 percent to compare with the 20 percent equity currently portrayed.

COMMISSIONER RODELL said that would be done.

CO-CHAIR SADDLER directed attention to slide 20, and noted that it was obvious that the state made more money if we "go it alone." He asked if this calculation was net for all the opportunity cost.

COMMISSIONER RODELL replied that this slide assumed there was an opportunity cost and the state was foregoing any investment income on that money.

CO-CHAIR SADDLER asked to see the opportunity cost factored in.

COMMISSIONER RODELL agreed to do so.

CO-CHAIR SADDLER asked if it was possible to quantify the risks, or if it was simply a judgment call for this policy decision.

COMMISSIONER RODELL offered her belief that the department had attempted to do this with the analysis, as it portrayed the percentage it would demand on unrestricted general fund revenue. She pointed out that the legislature understood the demands on the state for having to meet education, university, Medicare, Medicaid, and transportation costs. She opined that this was a policy call on the legislature for how to address these other demands and constitutional requirements, while accepting the constitutional requirement to maximize the resources for the benefit of all Alaskans.

CO-CHAIR SADDLER asked about any calculation for the price risk of commodity costs and overruns associated with ownership of the project.

COMMISSIONER RODELL replied that those costs had a very generic number attached to them as there was not enough information to fine tune it. She offered to provide insight into the various contingencies, 10 - 15 percent, in the project costs, and for any greater detail to provide to the committee.

CO-CHAIR SADDLER expressed his appreciation that this had been considered, as more information leveraged against bad outcomes.

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REPRESENTATIVE P. WILSON surmised that it would be necessary for legislators to review the budget, that it would be necessary to cut back between 20-25 percent in order to manage this project.

COMMISSIONER RODELL, in response, expressed her agreement, stating "that's all things being equal with what we know today." She opined that the revenue forecast could change and she expressed her belief that there would be more revenue during the years when the budget would become much tighter.

REPRESENTATIVE P. WILSON declared that, as it was already tough to make cuts, it would be even more difficult to make an additional 20 percent cut. She said "this is very, very, very serious."

COMMISSIONER RODELL offered her belief that this also emphasized the value for partnerships, and that the state still had the opportunity for further decision making at the ends of the pre-FEED and FEED. She acknowledged that although both of these decisions had financial impacts, the \$10 billion investment was not going to be made until there was a lot more information and the long term sales contracts were in place allowing for an expectation for the revenue. She reassured that there were ways out of this and opportunities to adjust if it looked like it could not be done.

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CO-CHAIR FEIGE asked what debt instruments would be available to the state, especially during the construction period, while waiting for revenue. He further asked about short term bridge loans and if these would be manageable for a short term.

COMMISSIONER RODELL replied that there were a number of different avenues which the state could explore. Assuming the state invested at 20 percent and wanted to "go it alone," at the construction phase there would need to be \$6-8 billion generated. She directed attention to the credit rating, and questioned whether the state was willingly to take more in debt proceeds and pay a higher interest rate, so not as much capital need be generated. She noted that other debt options, such as bonds, could be reviewed. As debt was fairly straightforward, the cash equity portion offered a variety of options, including the opportunities for additional investors or sale of a portion of the liquefaction project. She suggested that additional financing mechanisms, such as private equity or master and limited partnerships, could be other investment options for outside capital so that the state did not have to generate as much cash. She said that a cost for this would be to forego a portion of the revenue, similar to the projection of the TransCanada partnership.

REPRESENTATIVE SEATON asked to follow up regarding risk, investment decisions, and partnerships. He offered his belief that the state was not comfortable with a role as an oil company, or manufacturer, and asked about a partnership with a production revenue sharing agreement from the royalty and taxes that released the liability for project costs. This would release the legislature from the demands for fiscal investment beyond the state budget. He asked if this type of partnership was being investigated.

COMMISSIONER RODELL replied that these options would be explored if they were successful with enabling legislation, as this would be part of the due diligence during the pre-FEED stage. The enabling legislation would also allow for a marketing effort over the next 15 to 18 months to better understand which partners were willing to take on part of the infrastructure.

REPRESENTATIVE SEATON asked if there was discussion for a large gas purchaser interested in owning aspects of the entire revenue stream.

COMMISSIONER RODELL relayed that it was important to recognize that no one was going to make that commitment while this was still in the concept phase, and probably not until the pre-FEED stage. She noted that this was the reason to remain a party to this through the pre-FEED.

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CO-CHAIR SADDLER asked for clarification regarding the obligation to reduce the annual budget expenses by 25 percent in order to accommodate this project. He offered his understanding that the state would have options to finance its obligations once it arrived at the Final Investment Decision (FID). Referring to slide 18, he asked if the billions of dollars forecast for the AKLNG project was cash out of pocket or financing cost, and whether these obligations could be significantly lowered if they were financed.

COMMISSIONER RODELL replied that this did not make any assumptions about the financing cost; it only reflected the state's obligation to the project. How that money was going to be generated would be discussed at the FID stage. She explained that the obligation to the project was compared to the unrestricted general fund revenue, in case it had to be cash funded. A large portion of the project funding was equity, not

debt. She expressed her agreement that partnerships would reduce the costs.

CO-CHAIR SADDLER suggested that a 25 percent reduction in the unrestricted general fund was a possible solution, though not necessarily the preferred alternative.

COMMISSIONER RODELL expressed her agreement.

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REPRESENTATIVE TARR commented that it would be helpful to have more detail for the possibility of deficit spending and the impact on financing. She asked about the relationships for additional investment in the liquefaction facility.

COMMISSIONER RODELL replied that the AGDC subsidiary had no cash and had no capital, and in order to participate in the liquefaction, the subsidiary would require appropriations for every decision. She reported that the state would be discussing its progress with the liquefaction program. Given the size of this program within the total project, she opined that there would be discussions for partnerships at the end of the pre-FEED. She declared that there was not enough information to make these decisions at this time; however, as the value of the potential revenue could not be ignored, there was a commitment to keep the project moving forward. She expressed her relief that there was time to make these decisions.

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REPRESENTATIVE TARR referenced an article regarding "optimism bias" and asked if the discussion had included all the considerations for the worst possible case scenario.

COMMISSIONER RODELL allowed there probably was some "optimism bias" and that it is important to be continually reminding oneself of the reality of the project. She said that a lot of this optimism arose from the willingness of the three major producers to work with the state in a way unlike any past negotiation. She opined that this willingness came from recognition of the potential and a need for their companies to commercialize the resource. She suggested that the state had been motivated for the last 30 to 40 years to recognize this resource. She stated that it was necessary to take advantage of this optimism bias, and that it was owed to Alaskans to go on to the next stage.

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REPRESENTATIVE SEATON referenced the graph on slide 18, and the three cost bars at the bottom. He noted that the obligation existed regardless of debt or equity, and referenced slide 13, which projected the amount of equity versus debt that was possible. He opined that suggested partnerships included a partnership for the liquefaction project, which would also change the projected revenue to the same degree.

COMMISSIONER RODELL directed attention to the grey bar on slide 18 which depicted the state obligation without a partner. She referenced the blue bar which reflected the substantial reduction in cash outlay and obligation for having TransCanada as a partner. She directed attention to slide 20, which reflected the reduction in revenue between the blue line for "go it alone" and the light green line for the partnership with TransCanada. She pointed to the chart which quantified the revenue loss of \$300 million annually with a partner to pay the cash outlay on the gas treatment facilities and pipeline during construction.

REPRESENTATIVE SEATON asked about a project partnership, beyond that of TransCanada in the treatment plant and pipeline. He asked if there was a way to review a 50 percent partnership, and its effect on the revenues and the costs.

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REPRESENTATIVE JOHNSON reflected on the alignment of the producers and the state, noting that the state also "had skin in the game." He asked if there had been any discussion with the producers for the level of state involvement in the project that would keep the roles from becoming adversarial.

COMMISSIONER RODELL, acknowledging that this was a good point, explained that this was an attempt to find partners for the infrastructure while retaining ownership of the resource. She declared that the partners were paid with the value of that resource in exchange for a share of the infrastructure cost. She offered her belief that all partnerships would evaporate at some point, and, as long as the state was the taxing power and royalty owner and retained the right to administer the resource, the state could pledge to repay the partners in return for their activities and development of infrastructure. She opined that, as long as the state retained 20 to 25 percent control of the

project, it could bring in as many partners as desired as it was the state revenue, not the producers revenue, which was being paid out.

REPRESENTATIVE JOHNSON explained his point that, although the state was giving up that revenue, it could recoup that loss through taxes. He opined that there would not be any alignment with the producers if the state released too much of its ownership and simply relied on the revenue from taxes and royalties.

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CO-CHAIR FEIGE referenced the initial contract term (ICT) for a 25-year term, which offered several options for the state at the end of this term.

COMMISSIONER RODELL responded that the primary option at the end of the initial contract term was for a renewal of the partnership for the operation of the pipeline and gas treatment facility, as well as re-negotiation for the transportation agreements. She pointed out that the state could also terminate the partnership with TransCanada, although there would be a cost associated with this decision. She opined that, as TransCanada would be depreciating the project value over the contract, this would not be an excessive cost. The state could then operate its portion of the project without a partner. She declared that this mechanism for re-calculating the tariff contracts or taking control of the project had been an important aspect of the MOU.

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COMMISSIONER RODELL, in response to Representative Seaton, explained that the royalty rate was tied to the leases, which were very long term contracts. Regarding the tax rate, the state retained the right for any future legislature to adjust this and this would be addressed in the contract.

REPRESENTATIVE SEATON asked for clarification that the royalties, property taxes, or production tax rate could not be revised during the term of the contract.

COMMISSIONER RODELL replied that the state would have a 25-year agreement "that will contemplate a certain tax rate." She reported that the contract would have consequences for any tax rate changes so as not to preclude any future legislature from allowing a change during the term of the contract.

REPRESENTATIVE SEATON asked whether these consequences would be terminated at the end of the contract period.

COMMISSIONER RODELL agreed.

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**ADJOURNMENT**

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 3:05 p.m.