

**ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE**

April 8, 2014

4:34 p.m.

MEMBERS PRESENT

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

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

COMMITTEE SUBSTITUTE 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."

- HEARD & HELD

PREVIOUS COMMITTEE ACTION

BILL: SB 138

SHORT TITLE: GAS PIPELINE; AGDC; OIL & GAS PROD. TAX

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

01/24/14	(S)	READ THE FIRST TIME - REFERRALS
01/24/14	(S)	RES, FIN
02/07/14	(S)	RES AT 3:30 PM BUTROVICH 205
02/07/14	(S)	Heard & Held
02/07/14	(S)	MINUTE(RES)
02/10/14	(S)	RES AT 3:30 PM BUTROVICH 205
02/10/14	(S)	Heard & Held
02/10/14	(S)	MINUTE(RES)
02/12/14	(S)	RES WAIVED PUBLIC HEARING NOTICE, RULE 23
02/12/14	(S)	RES AT 3:30 PM BUTROVICH 205
02/12/14	(S)	Heard & Held
02/12/14	(S)	MINUTE(RES)
02/13/14	(S)	RES AT 8:00 AM BUTROVICH 205
02/13/14	(S)	Heard & Held
02/13/14	(S)	MINUTE(RES)
02/14/14	(S)	RES AT 3:30 PM BUTROVICH 205
02/14/14	(S)	Heard & Held
02/14/14	(S)	MINUTE(RES)
02/19/14	(S)	RES AT 3:30 PM BUTROVICH 205
02/19/14	(S)	Heard & Held
02/19/14	(S)	MINUTE(RES)
02/20/14	(S)	RES AT 8:00 AM BUTROVICH 205
02/20/14	(S)	Heard & Held

02/20/14 (S) MINUTE(RES)
02/21/14 (S) RES AT 8:00 AM BUTROVICH 205
02/21/14 (S) Heard & Held
02/21/14 (S) MINUTE(RES)
02/21/14 (S) RES AT 3:30 PM BUTROVICH 205
02/21/14 (S) Heard & Held
02/21/14 (S) MINUTE(RES)
02/24/14 (S) RES RPT CS 2DP 4NR 1AM NEW TITLE
02/24/14 (S) DP: GIESSEL, MCGUIRE
02/24/14 (S) NR: FRENCH, MICCICHE, BISHOP,
FAIRCLOUGH
02/24/14 (S) AM: DYSON
02/24/14 (S) RES AT 8:00 AM BUTROVICH 205
02/24/14 (S) -- MEETING CANCELED --
02/24/14 (S) RES AT 3:30 PM BUTROVICH 205
02/24/14 (S) Moved CSSB 138(RES) Out of Committee
02/24/14 (S) MINUTE(RES)
02/25/14 (S) FIN AT 9:00 AM SENATE FINANCE 532
02/25/14 (S) Heard & Held
02/25/14 (S) MINUTE(FIN)
02/25/14 (S) FIN AT 5:00 PM SENATE FINANCE 532
02/25/14 (S) Heard & Held
02/25/14 (S) MINUTE(FIN)
02/26/14 (S) FIN AT 9:00 AM SENATE FINANCE 532
02/26/14 (S) Heard & Held
02/26/14 (S) MINUTE(FIN)
02/27/14 (S) FIN AT 9:00 AM SENATE FINANCE 532
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02/28/14 (S) FIN AT 9:00 AM SENATE FINANCE 532
02/28/14 (S) Heard & Held
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03/03/14 (S) FIN AT 9:00 AM SENATE FINANCE 532
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03/05/14 (S) Heard & Held
03/05/14 (S) MINUTE(FIN)
03/05/14 (S) FIN AT 5:00 PM SENATE FINANCE 532
03/05/14 (S) Scheduled But Not Heard
03/06/14 (S) FIN AT 9:00 AM SENATE FINANCE 532
03/06/14 (S) Heard & Held
03/06/14 (S) MINUTE(FIN)
03/07/14 (S) FIN AT 9:00 AM SENATE FINANCE 532

03/07/14 (S) -- MEETING CANCELED --
03/10/14 (S) FIN AT 9:00 AM SENATE FINANCE 532
03/10/14 (S) Heard & Held
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03/10/14 (S) MINUTE(FIN)
03/11/14 (S) FIN AT 5:00 PM SENATE FINANCE 532
03/11/14 (S) Heard & Held
03/11/14 (S) MINUTE(FIN)
03/12/14 (H) RES AT 1:00 PM BARNES 124
03/12/14 (H) -- MEETING CANCELED --
03/14/14 (S) FIN RPT CS 6DP 1AM NEW TITLE
03/14/14 (S) LETTER OF INTENT WITH FINANCE REPORT
03/14/14 (S) DP: KELLY, MEYER, DUNLEAVY, FAIRCLOUGH,
BISHOP, HOFFMAN
03/14/14 (S) AM: OLSON
03/14/14 (S) FIN AT 9:00 AM SENATE FINANCE 532
03/14/14 (S) Moved CSSB 138(FIN) Out of Committee
03/14/14 (S) MINUTE(FIN)
03/14/14 (H) RES AT 1:00 PM BARNES 124
03/14/14 (H) <Pending Referral>
03/17/14 (H) RES AT 1:00 PM BARNES 124
03/17/14 (H) <Pending Referral>
03/18/14 (S) TRANSMITTED TO (H)
03/18/14 (S) VERSION: CSSB 138(FIN) AM
03/19/14 (H) READ THE FIRST TIME - REFERRALS
03/19/14 (H) RES, L&C, FIN
03/19/14 (H) RES AT 1:00 PM BARNES 124
03/19/14 (H) Heard & Held
03/19/14 (H) MINUTE(RES)
03/21/14 (H) RES AT 1:00 PM BARNES 124
03/21/14 (H) Heard & Held
03/21/14 (H) MINUTE(RES)
03/24/14 (H) RES AT 1:00 PM BARNES 124
03/24/14 (H) Heard & Held
03/24/14 (H) MINUTE(RES)
03/25/14 (H) RES AT 4:30 PM BARNES 124
03/25/14 (H) Heard & Held
03/25/14 (H) MINUTE(RES)
03/26/14 (H) RES AT 1:00 PM BARNES 124
03/26/14 (H) Heard & Held
03/26/14 (H) MINUTE(RES)
03/27/14 (H) RES AT 4:30 PM BARNES 124
03/27/14 (H) Heard & Held
03/27/14 (H) MINUTE(RES)
03/28/14 (H) RES AT 1:00 PM BARNES 124

03/28/14	(H)	Heard & Held
03/28/14	(H)	MINUTE(RES)
03/31/14	(H)	RES AT 1:00 PM BARNES 124
03/31/14	(H)	Heard & Held
03/31/14	(H)	MINUTE(RES)
04/01/14	(H)	RES AT 4:30 PM BARNES 124
04/01/14	(H)	Heard & Held
04/01/14	(H)	MINUTE(RES)
04/02/14	(H)	RES AT 1:00 PM BARNES 124
04/02/14	(H)	Heard & Held
04/02/14	(H)	MINUTE(RES)
04/03/14	(H)	RES AT 4:30 PM BARNES 124
04/03/14	(H)	Heard & Held
04/03/14	(H)	MINUTE(RES)
04/04/14	(H)	RES AT 1:00 PM BARNES 124
04/04/14	(H)	Heard & Held
04/04/14	(H)	MINUTE(RES)
04/05/14	(H)	RES AT 10:00 AM BARNES 124
04/05/14	(H)	Heard & Held
04/05/14	(H)	MINUTE(RES)
04/06/14	(H)	RES AT 1:00 PM BARNES 124
04/06/14	(H)	Heard & Held
04/06/14	(H)	MINUTE(RES)
04/07/14	(H)	RES AT 1:00 PM BARNES 124
04/07/14	(H)	Heard & Held
04/07/14	(H)	MINUTE(RES)
04/08/14	(H)	RES AT 8:00 AM BARNES 124
04/08/14	(H)	FIN AT 8:30 AM HOUSE FINANCE 519
04/08/14	(H)	RES AT 4:30 PM BARNES 124

WITNESS REGISTER

MICHAEL PAWLOWSKI, Deputy Commissioner
Office of the Commissioner
Department of Revenue (DOR)
Anchorage, Alaska

POSITION STATEMENT: Answered questions during the hearing on
CSSB 138(Fin) am.

JOE GRIFFITH, President
Alaska Railbelt Cooperative Transmission & Energy Co. (ARCTEC)
General Manager
Matanuska Electric Association (MEA)
Palmer, Alaska

POSITION STATEMENT: Answered questions during the hearing on
CSSB 138(Fin) am.

JOE BALASH, Commissioner
Department of Natural Resources (DNR)
Anchorage, Alaska

POSITION STATEMENT: Answered questions during the hearing on
CSSB 138(Fin) am.

CHRISTOPHER POAG, Assistant Attorney General
Labor and State Affairs Section
Civil Division (Juneau)
Department of Law (DOL)
Juneau, Alaska

POSITION STATEMENT: Answered questions during the hearing on
CSSB 138(Fin) am.

JANAK MAYER, Partner, Energy Consultant
analytica
Washington, DC

POSITION STATEMENT: As consultant to the Alaska State
Legislature, answered questions during the hearing on CSSB
138(Fin) am.

NIKOS TSAFOS, Partner, Energy Consultant
analytica
Washington, DC

POSITION STATEMENT: As consultant to the Alaska State
Legislature, answered questions during the hearing on CSSB
138(Fin) am.

ACTION NARRATIVE

[4:34:15 PM](#)

CO-CHAIR ERIC FEIGE called the House Resources Standing
Committee meeting to order at 4:34 p.m. Representatives Seaton,
Olson, P. Wilson, Tarr, Kawasaki, Hawker, Johnson, Saddler, and
Feige were present at the call to order.

SB 138-GAS PIPELINE; AGDC; OIL & GAS PROD. TAX

[4:34:28 PM](#)

CO-CHAIR FEIGE announced that the only order of business is 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."

[4:34:43 PM](#)

CO-CHAIR SADDLER moved to adopt Amendment 32, labeled 28-GS2806\I.A.31, Bullock, 4/2/14, which read:

Page 2, line 11, following "**fund;**":

Insert "**establishing the Railbelt electrical generation and transmission upgrade fund;**"

Page 11, line 20:

Delete "a new section"

Insert "new sections"

Page 12, following line 8:

Insert a new section to read:

"Sec. 37.05.620. Railbelt electrical generation and transmission upgrade fund. (a) The Railbelt electrical generation and transmission upgrade fund is created as a special account in the general fund. The fund consists of the amount determined and deposited in the fund under (b) of this section and interest earned on the fund balance. The purpose of the fund is to provide a source from which the legislature may appropriate money to replace and upgrade electrical generation and transmission infrastructure in the Railbelt that is approaching the end of its useful and economic life.

(b) The amount to be deposited in (a) of this section is 10 percent of the revenue received from the state's royalty gas transported in an Alaska liquefied natural gas project that remains after the payment to the Alaska permanent fund under AS 37.13.010.

(c) The legislature may make appropriations from the Railbelt electrical generation and transmission upgrade fund for the purposes described in (a) of this section or for any other public purpose.

(d) Nothing in this section creates a dedicated fund.

(e) In this section,

(1) "Alaska liquefied natural gas project" has the meaning given in AS 31.25.390;

(2) "Railbelt" means the area of the state between Fairbanks and Homer that is connected by road or railroad."

CO-CHAIR FEIGE objected.

[4:35:51 PM](#)

CO-CHAIR SADDLER explained Amendment 32 would create the Railbelt electrical generation and transmission upgrade fund. Most of the state's goods and services are either consumed in or passed through the Railbelt, which includes communities from Homer to Fairbanks and communities in between. Reliable energy and reasonable energy prices percolate through the entire state's economy. However, the electrical transmission infrastructure along the Railbelt is at risk. A recent Alaska Energy Authority study showed that Railbelt energy transmission faces about \$900 million in unmet needs over the next decade. Additionally, if the Railbelt doesn't have some major capital improvements the grid could be losing more than \$100 million

worth of efficiency per year. These represent significant statewide infrastructure needs that lead to outages that must be addressed before the Alaska LNG Project, which will bring more gas to the state. It is unlikely the state can address these needs over the next ten years, but it's very likely more projects will be added to the list.

REPRESENTATIVE SADDLER said innovative funding paradigms exist in utilities, including the Bradley Lake model built by splitting the cost between the state and ratepayers; however, the large backlog of needs in the Railbelt means the burden is too great for the ratepayers to bear without state assistance. The Railbelt electrical generation and transmission upgrade fund created by Amendment 32 would be capitalized by 10 percent of the post-permanent fund deposit royalty revenues, a similar mechanism to Section 13 of SB 138, with respect to the Alaska affordable energy fund. He indicated he'd like confirmation from the Department of Revenue (DOR) about this, but he estimated the fiscal note would generate about \$90 million per year [based on] 10 percent [of the post-permanent fund deposit royalty revenues].

REPRESENTATIVE SADDLER stated that Amendment 32 would give an alternative to straight general fund appropriations for Railbelt electrical improvements. It would help utilities leverage state assistance and utility financing and ratepayer contributions to meet the nearly \$1 billion need. He anticipated that some might object since it could be argued that this project already does benefit the Railbelt; however, Southcentral Alaska has had access to affordable gas since Swanson River and Cook Inlet fields were discovered in the 1950s. Despite these discoveries, there remain massive unmet transmission needs in the Railbelt. He offered his belief that Amendment 32 is a fair, equitable balance to the affordable energy fund model and he encouraged members to discuss this and support the amendment.

[4:39:10 PM](#)

REPRESENTATIVE P. WILSON noted there is already an energy section in the bill. Regarding the \$90 million, she inquired whether it is before or after the state's 25 percent royalty share.

MICHAEL PAWLOWSKI, Deputy Commissioner, Office of the Commissioner, Department of Revenue (DOR), responded that DOR's interpretation for the previous section [Section 13] is in the fiscal note based on preliminary modeling using assumptions.

Each 10 percent would be estimated to generate approximately \$90 million based on today's information, which could change with market condition and project cost.

REPRESENTATIVE P. WILSON remarked she would contemplate this.

[4:40:48 PM](#)

REPRESENTATIVE KAWASAKI asked whether some other fund, such as the power project loan fund, could be used instead of creating a new fund.

CO-CHAIR SADDLER answered that Alaska Industrial Development and Export Authority (AIDEA) has a [Sustainable Energy Transmission Development & Supply Development Fund] (SETS) fund, but it doesn't work for the Railbelt transmission. For instance, AIDEA has limits, requires collateral, and the Railbelt's borrowing capacity was "maxed out" for generation capacity by buying high efficiency generators. He acknowledged there could be some long-term savings if [AIDEA] could obtain funding for a long enough duration but it can't make an investment in new lines on savings not yet achieved since "cash up front" is necessary. He indicated this was reviewed which concluded there is a need outside the SETS fund.

[4:41:55 PM](#)

REPRESENTATIVE HAWKER commented he always has concerns about appropriating money the state does not yet have; in particular, "skirting" Alaska's Constitution with an attempt to designate funds even if the funds are not dedicated funds. He expressed concern about the Alaska affordable energy fund that's in the bill. He said \$90 million represents 10 percent of roughly \$900 million, just under \$1 billion, which is supposed to be the revenue received from the state's royalty gas transported in the Alaska LNG Project. He asked whether he could reconcile that \$1 billion with the anticipated annually projected \$3.5-\$4.5 billion in state profits for this project.

MR. PAWLOWSKI responded the revenues calculated are after deposits to the [Alaska] permanent fund. He referred to previous testimony to a schedule of royalty revenues, indicating the royalty would run approximately \$1 billion to \$1.4 billion. He explained that when calculating the fiscal note, he considered inflation in the initial years, noting the royalty could exceed \$90 million. Thus the 10 percent would be

calculated after the 25 percent of the \$1.0-\$1.4 billion in permanent fund deposits.

REPRESENTATIVE HAWKER asked how royalty is being defined. He asked whether it would be the value in which the state is accepting tax as gas (TAG).

MR. PAWLOWSKI answered that this is limited to the sale of the molecules associated with the state's royalty share and not the TAG. The models for the state's royalty gas run between 13-13.5 percent depending on which field the gas is derived from.

REPRESENTATIVE HAWKER asked whether DOR is valuing the royalty at the amount the state receives at the sales end.

MR. PAWLOWSKI clarified that DOR is taking the LNG sales price minus the liquefaction and transportation costs.

[4:44:49 PM](#)

REPRESENTATIVE SEATON asked about the nexus between this fund and the Alaska Railbelt Cooperative Transmission and Energy Company (ARCTEC) consortium that the legislature has been funding through capital appropriations.

CO-CHAIR SADDLER answered the nexus is they are both set up to address a need. He deferred to Mr. Joe Griffith, Alaska Railbelt Cooperative Transmission and Energy Company (ARCTEC).

JOE GRIFFITH, President, Alaska Railbelt Cooperative Transmission and Energy Company (ARCTEC); General Manager, Matanuska Electric Association (MEA), stated that ARCTEC is a facilitator of the transmission system. Thus, ARCTEC wouldn't have any role whatsoever in how the funds would be put together. He allowed that if ARCTEC were to receive grants for particular projects - currently there is a set of grants in "CAPSYS" - that would address this very issue. The ARCTEC, as a consortium, would then undertake the projects as funded. He characterized ARCTEC's role as being the managers and noted ARCTEC is currently working on an independent system operator concept, "ANATRANSCO," which should be in place soon.

CO-CHAIR SADDLER stated Amendment 32 would not dedicate funds but would designate funds that the legislature would set aside to fund construction via ARCTEC or perhaps other means. He pointed out it indicates transmission needs along the Railbelt

are a priority and deserve to have funding streams set aside to address the needs.

4:46:58 PM

REPRESENTATIVE P. WILSON asked whether private utilities would receive 10 percent of the royalties.

CO-CHAIR SADDLER clarified that it would go to the people represented by the utilities. Many are cooperatives that are owned by the ratepayers and the expectation is that state money would be matched by funding derived from ratepayers over many years. So, it is ratepayers and it is utilities.

REPRESENTATIVE P. WILSON understood utilities are supposed to set aside funds to maintain lines.

CO-CHAIR SADDLER deferred to Mr. Griffith.

MR GRIFFITH answered that to a degree the utilities can, of course, but the utilities are regulated entities, limited to a certain rate of return above costs, which translates to probably less than five percent today. He assured members that any nickel placed in maintenance or in a sinking fund to build future requirements comes out of the ratepayers' pockets. The result would be to raise ratepayers' rates. The Regulatory Commission of Alaska (RCA) is less than enthralled with allowing those types of funds.

REPRESENTATIVE P. WILSON acknowledged this is something that should be addressed, although she suggested it should not be addressed under this bill. She expressed concern since Southeast Alaska wouldn't be too excited about using [the 10 percent of royalty] for a specific area [along the Railbelt] when the proposed project will benefit the Railbelt. She recalled a proposal to combine all the utilities into one giant utility. She suggested perhaps that should be considered.

4:50:05 PM

CO-CHAIR FEIGE inquired whether the amendment would be used to maintain existing transmission or if the sponsor envisions that the fund would be used to build new transmission to better connect grids across the state.

CO-CHAIR SADDLER said that is difficult to answer. The goal is to have a reliable, robust system that serves the ratepayers and

the state. He envisioned some repairs and also new construction. He thought perhaps it could go to new communities, although not many new communities are being constructed along the Railbelt. He offered his belief that it would be used largely for maintenance with some new construction to improve overall reliability of the system.

[4:50:53 PM](#)

REPRESENTATIVE KAWASAKI related his understanding that the purpose of the Railbelt electrical generation and transmission upgrade fund would not be due to the anticipated Alaska LNG Project.

CO-CHAIR SADDLER answered no, saying there is an opportunity for a large unmet state need to be funded by potential future revenue streams. He stated Amendment 32 posits that the need is significant and if the revenue becomes available that this would be an appropriate place to designate it so the legislature has an opportunity to appropriate funds to the proposed fund.

[4:51:36 PM](#)

REPRESENTATIVE JOHNSON stated the legislature always has the ability to appropriate funds to a project. He expressed reluctance to set aside funds for a specific project. He said, "When I saw this amendment I kind of broke out into a sweat remembering the Railbelt Energy Fund (REF) and the fights that went on between the utilities over that." He recalled that the subsequent costs of lawsuits exceeded any funds the utilities received from the REF and expressed reluctance to set a designated fund so that utilities can sue each other over it, given "they don't always play well together." Unification of utilities is happening all over the U.S. and Alaska's utilities are small compared to the Lower 48 utilities. Until the aforementioned dynamic is solved by a unified transmission group, similar to a Susitna group, he said he is not prepared to fuel utility wars and "sweeten the pot" and pay attorneys. He recalled that the REF issue was solved by dumping the funds into another project. He preferred to have the utilities come to the legislature for each individual project and that the legislature designate funding on a per project basis.

[4:53:54 PM](#)

CO-CHAIR SADDLER understood the concern, but said that Amendment 32 would place the proposed Railbelt [electrical generation and

transmission upgrade] fund in the same section, Chapter 37, public finance, which includes the marine highway vessel replacement fund, the Alaska capital income fund, the schools maintenance construction funds, the Alaska public building fund, the tobacco education cessation fund, and the Veteran's cemetery funds. Thus, designated funds already exist; and second, unless the organizations have the means to accomplish work it won't help anyone. He offered his belief that the utilities have learned some lessons from their fractious history and that ARCTEC represents evidence of lessons learned, since the utilities have come together in a cooperative arrangement. However, they cannot do anything unless they have funds.

REPRESENTATIVE JOHNSON said, "Mr. Chairman, I don't want to get into personalities or individuals utilities, but ask Chugach [Electric] how it is working out to get their transmission line through the Homer Electric utilities." Regarding the designated funds, he remarked that the state has never had a designated fund with seven groups fighting over it. He argued that each fund mentioned represents a single entity fighting for a common cause. Unless all the utilities are fighting for the common cause of better serving Alaskans, he is unsure of the need to set up a designated fund to allow them to continue to fight.

[4:55:40 PM](#)

REPRESENTATIVE TARR acknowledged the committee has been considering several amendments that are similar in nature. She asked for an assessment of the state's overall cash position with the proposed designation and how it would affect revenue available for other things. She asked whether the legislature can spend out of the designated fund.

MR. PAWLOWSKI answered DOR has a zero fiscal note on the cost of DOR managing the designated funds mentioned here since the funds are co-invested with the [general fund and other non-segregated investments]. The funds are invested as a group on a short-term basis. The revenue going into the designated funds is revenue that would normally go into the general fund so it's just being placed in an account within the general fund. Referring to [page 1, line 23 through] page 2, line 2, of Amendment 32, he said the language indicates the legislature has the authority to appropriate for any other public purpose. However, the funds would not show up as general fund revenue or within the general fund in the same way since it would be categorized under the fund that it's in.

[4:57:15 PM](#)

REPRESENTATIVE TARR asked whether it would effectively decrease the amount that is in the general fund for calculation of the state's financial position. For example, if the state was going to bond for other projects, the designated funds would come out of the funds available for debt service. She contemplated the ratios shown in earlier slides with respect to the state's built-in limit for taking on debt.

MR. PAWLOWSKI replied he is unsure he knows the specific impact it may have and would have to get back to the committee with an answer. For example, at what point is the designation happening, whether the revenue is being diverted, and how it shows up on the balance sheet. He said he'd want to discuss this further with the treasury staff and determine how they would interpret this.

REPRESENTATIVE TARR commented she is considering the cumulative impact if all the amendments were to be adopted.

[4:58:39 PM](#)

REPRESENTATIVE SEATON recalled another fund was set up under the bill, which made sense since the property tax would be assessed and the municipal property tax would be shared through the Railbelt. He expressed concern about designating additional funds to the Railbelt for a specific energy project when the Railbelt is obtaining the benefits from the proposed pipeline project. He fully agreed with Representative Johnson on the decisions on transmission projects, which means the good projects will likely be successful. He said he cannot support Amendment 32 at this time.

[4:59:54 PM](#)

The committee took an at-ease to a call of the chair.

[5:29:30 PM](#)

CO-CHAIR SADDLER addressed earlier concerns, recalling that Representative Johnson did not wish to designate funds until a unified project moved forward. He responded that Amendment 32 would not cost anyone any money until the proposed natural gas line is built, approximately in ten years. As the AEA report indicated, significant Railbelt needs exists. He related a scenario in which a young couple wants to buy a house someday,

but that shouldn't stop them from saving towards their goal. He said he takes gentle exception to the statement that the Alaska LNG Project would provide benefit only to Railbelt communities. He did not see anything that would guarantee a price of gas for anyone and suggested it might mean the consumer's prices will be the same as under the Cook Inlet supply of natural gas. The vast majority of the gas produced from the North Slope is going to be aimed towards the export market in Asia, and while he hopes some will come to Alaska, too, that the target market is overseas. Certainly, approximately \$3 billion in revenue to the general fund benefits the entire state. Other language in the bill sends 10 percent of royalty revenue to a rural energy infrastructure fund. Absent this amendment, the bill doesn't contain any provision for Railbelt energy infrastructure. He recalled comments that the property tax revenue would benefit Railbelt communities. He asked Mr. Griffith whether property taxes are an appropriate source of funding to address Railbelt transmission needs.

CO-CHAIR FEIGE said Mr. Griffith is no longer on line.

CO-CHAIR SADDLER questioned whether property tax revenue applied to a natural gas pipeline infrastructure would be conceived as a source of funding for Railbelt transmission needs.

[5:32:05 PM](#)

REPRESENTATIVE JOHNSON urged Amendment 32 be taken off the table until the [utilities are unified] and it "is the same choir on the same tune going in the same direction."

REPRESENTATIVE OLSON indicated that he supported the transportation fund since the state originally had the fund, but he did not wish to support any more. He envisioned other dedicated funds would materialize, such as a dedicated Public Employees' Retirement (PERS) Fund, Teachers' Retirement (TRS) Fund, Education Fund, and perhaps others. He offered his belief that the legislature needs to have some control over spending.

[5:33:23 PM](#)

CO-CHAIR SADDLER said it is important to raise the discussion about the significant energy needs along the Railbelt communities that serve a lot of the state. The needs will not go away and his intention was to seek a potential future source of revenue to plan for future needs. He appreciated the discussion.

CO-CHAIR SADDLER withdrew Amendment 32.

[5:34:23 PM](#)

REPRESENTATIVE KAWASAKI moved to adopt Amendment 33, labeled 28-GS2806\I.A.40, Nauman/Bullock, 4/3/14, which read:

Page 55, following line 30:

Insert a new bill section to read:

"* **Sec. 61.** The uncodified law of the State of Alaska is amended by adding a new section to read:

STATE ADVISORY ROLE. The state may not become an equity partner or hold an ownership interest in an Alaska liquefied natural gas project, as defined in AS 31.25.390, unless the state is given a significant and meaningful advisory role regarding the assets of and management of the project, that includes reasonable access to information about the project and input into the management of the project."

Re-number the following bill sections accordingly.

Page 56, line 6:

Delete "61"

Insert "62"

Page 56, line 9:

Delete "secs. 62 and 63"

Insert "secs. 63 and 64"

REPRESENTATIVE HAWKER objected.

REPRESENTATIVE KAWASAKI paused to find his amendment notes.

The committee took a brief at-ease.

REPRESENTATIVE KAWASAKI withdrew Amendment 33.

[5:36:57 PM](#)

REPRESENTATIVE HAWKER moved to adopt Amendment 34, labeled 28-GS2806\I.A.96, Bullock, 4/6/14, which read:

Page 1, line 4, following "**projects;**":

Insert "making certain contracts by the Department of Natural Resources and the Department of Law not subject to the State Procurement Code;"

Page 11, following line 19:

Insert a new bill section to read:

"* **Sec. 13.** AS 36.30.850(b) is amended by adding new paragraphs to read:

(47) contracts for professional and technical services by the Department of Natural Resources to support the development of agreements and contracts under AS 38.05.020(b)(10) and (11);

(48) contracts of the Department of Law developed with client participation for legal services related to an Alaska liquefied natural gas project as that project is defined in AS 31.25.390, except that, to the extent practicable, the Department of Law shall use the procurement process under AS 36.30.320 with the participation of the client."

Renumber the following bill sections accordingly.

Page 14, line 3:

Delete "sec. 14"

Insert "sec. 15"

Page 17, line 24:

Delete "sec. 17"

Insert "sec. 18"

Page 21, line 16:

Delete "sec. 27"

Insert "sec. 28"

Page 25, line 9:

Delete "sec. 30"

Insert "sec. 31"

Page 31, line 18:

Delete "sec. 37"

Insert "sec. 38"

Page 53, lines 24 - 25:

Delete "sec. 23"

Insert "sec. 24"

Page 54, line 25:

Delete "sec. 14"
Insert "sec. 15"

Page 56, line 6:

Delete "Sections 1 - 14, 16, 17, 23 - 27, 29, 30,
37, 39, and 55 - 61"

Insert "Sections 1 - 15, 17, 18, 24 - 28, 30, 31,
38, 40, and 56 - 62"

Page 56, line 8:

Delete "Section 38"
Insert "Section 39"

Page 56, line 9:

Delete "secs. 62 and 63"
Insert "secs. 63 and 64"

REPRESENTATIVE SEATON objected for discussion purposes.

[5:37:19 PM](#)

REPRESENTATIVE HAWKER explained the committee has already held considerable discussion on Amendment 34 because it replaces the previously discussed amendment, labeled [28-GS2806\I.A.69, Bullock, 4/4/14], that had an exemption for the Department of Natural Resources (DNR) from procurement code provisions for contracts for professional technical services by DNR to support the development of agreements and contracts related to Alaska LNG. The language of Amendment 34 has the same intent to similar exemptions crafted for the Alaska Gasline Development Corporation (AGDC) in the previous legislative session to allow DNR to move forward with industry. Industry can be very proactive, reactive, and nimble to react to changing circumstances at any given time, and the state should be equally nimble, reactive, and proactive in managing the Alaska LNG Project. He recalled that during dialogue [on Amendment 8] that brought the Department of Law and the attorney general into a legal role with respect to AGDC, the question arose on whether the DOL and attorney general needed an expedited procurement process for legal services. Circumstances could arise on an extraordinary short timeframe requiring technical or precise legal counsel to resolve issues. He related that he worked with DOL and said the language on lines 11-15, [paragraph] (48), of Amendment 34 work well for DOL and would exempt DOL from the procurement process, except DOL shall use the procurement process under AS 36.30.320, which is the small procurement regulation typically used for quick procurement. However,

Amendment 34 would give DOL the latitude to move even more quickly than that if necessary to accommodate something that arose with the development of the Alaska LNG Project. He noted that the procurement of legal services involves the participation of the client, in this instance, AGDC.

[5:40:27 PM](#)

CO-CHAIR FEIGE inquired whether the administration has a position on Amendment 34.

JOE BALASH, Commissioner, Department of Natural Resources (DNR), offered the administration's support for Amendment 34, saying there is value in having this tool in the toolbox. He thanked Representative Hawker for his work in refining the additions for the Department of Law. The Department of Natural Resources does not intend to have all of its contracts exempt from the procurement code but he anticipated circumstances as DOL seeks specialized expertise as DNR considers upstream balancing and offtake agreements in which this will be necessary.

CHRISTOPHER POAG, Assistant Attorney General, Labor and State Affairs Section, Civil Division (Juneau), Department of Law (DOL), said he did not directly speak to the attorney general, but related his understanding that DOL's attorney general has reviewed the language in Amendment 34, is aware of it, and approves it.

[5:42:01 PM](#)

REPRESENTATIVE P. WILSON requested further clarification on AS 36.30.032.

MR. POAG answered that generally speaking this refers to the small procurement process. He explained that the language "to the extent practicable" is important because generally that is limited to contracts of \$100,000 for professional services, which was amended last year from \$50,000 by the legislature, and this is why the amount is in the supplement and not in the original statute. He has been involved in this process in a few instances. Additionally, regulations were adopted to describe the process. Under the process, a minimum of three law firms are identified that can provide the unique services that the department isn't situated to provide. First, the department sends a letter to them asking that they submit a proposal to provide representation. Second, the department and the client agency needing the services would review the proposals and

determine which is most appropriate. Third, the department would send a notice of intent to award, and begin the contract negotiation process. The only real dissimilarity from the typical procurement process is that DOL does not formally draft a request for proposal (RFP), formally using a period of time in which it is considered and scored. Nonetheless, the steps are largely based on the basis of the procurement code which is to seek competition to ensure that public dollars are well spent. Both DOL staff and the client agency are involved in determining the firms that would best serve the department's skills.

5:44:04 PM

REPRESENTATIVE KAWASAKI understood Mr. Poag to have said DOL would still go out to three firms. He asked whether this process always requires that competitive nature or could the department sole source under this new section.

MR. POAG recalled only one instance - a bankruptcy proceeding in which the Alaska Retirement Management (ARM) Board and the Alaska permanent fund were involved through a leveraged buyout that went bad. Bankruptcy trustee litigation tried to draw back the funds against the merger. Only two law firms represented public pension funds in that proceeding. In this instance, he sent letters to both firms asking them to provide terms and DOL selected the one in the best interest of the state. Typically a regulation encourages three or more proposals, but sometimes a sufficient number of firms cannot handle the specific services. Under Amendment 34, DOL would endeavor to provide competition by asking a number of firms to submit proposals to provide leverage on rates and the types of services the firms will provide. This language envisions a legal issue will arise in which DOL may need a very quick answer to a legal question. He suggested that DOL would intend to use the small procurement process as a guideline. He offered his belief that most of the legal work would fall under the \$100,000 limit, but if it exceeded this DOL would use this language as a guideline. It doesn't impose a limit because DOL could seek proposals from more than three firms, but generally that is the starting point.

5:46:58 PM

REPRESENTATIVE KAWASAKI asked whether DNR would issue competitive contracts in the same way as DOL or whether DNR would sole source contracts.

COMMISSIONER BALASH responded the principle of competition is one DNR will continue to abide by, but the rigors of the procurement process, including drawing up the scope, the notice, the opportunity for offerings, and the appeal process could drag out the assessment or evaluation. Upstream issues will "be a big darn deal" that will require specialized expertise. As DNR thinks about marketing aspects, it is likely going to need to hire people with specific relationships in different countries and with respect to trade practices DNR wants to be legal in both the U.S. and in other countries. The department sees the opportunities for this tool to be effective for DNR, although it won't represent the norm.

REPRESENTATIVE KAWASAKI asked whether it is more an issue of timing as it was with DOL in finding specific attorneys or specialization. He further asked why the current procurement code cannot be used.

COMMISSIONER BALASH answered that this particular issue is one DNR runs into when evaluating the geo-license application, as well as a similar exemption provided to the agencies factoring the Alaska Stranded Gas Development Act (ASGDA) process. He explained that contractors are not eager to put their names forward unless they are fairly confident they will be selected. The procurement process takes time, specifically outlined in statute in terms of the award, and the department believes it needs a little more flexibility to weigh more towards the technical expertise than the procurement code provides today. He said when it comes to a project worth billions to the state he does not want to be tied to the lowest bidder.

[5:50:39 PM](#)

REPRESENTATIVE HAWKER reiterated his office has worked closely with DOL and in this instance DOL shall use the procurement process under AS 36.30.320. He said this is about the process and is an exemption from procurement since the detailed rules may not be applicable; however, the process itself is applicable.

MR. POAG agreed, saying this language would exempt DOL from the procurement code, but defines the process that DOL will use in obtaining legal services. It will not be the strict requirements of each provision of statute, but rather to define the firms best suited to provide the legal services, asking them to submit proposals, evaluating them with the assistance of AGDC, selecting them, and engaging in the negotiation process.

That's why the language "to the extent practicable" is there. It is not uncommon for agencies to replace it with some form of a procurement process. The bill today provides a guideline and isn't meant to be a strict adherence.

[5:52:27 PM](#)

REPRESENTATIVE KAWASAKI observed the language clearly says under the Department of Law. He asked whether this process is the same small procurement process that DNR will also follow since the language is different.

COMMISSIONER BALASH answered that if the committee wishes it could include the same language that is on lines 13-14: "project is defined in AS 31.25.390, except that, to the extent practicable, the Department of Law shall use the procurement process under AS 36.30.320 with the participation of the client." He said he would be fine with including this language on lines 8-10 if the committee so desired.

REPRESENTATIVE KAWASAKI declined to make an amendment to Amendment 34.

[5:53:25 PM](#)

REPRESENTATIVE SEATON observed that lines 11-12 of Amendment 34 include the language "client participation" and specify the Alaska liquefied natural gas project. He inquired what potential scope of clients this language would encompass.

MR. POAG responded this language allows DOL to procure legal services for the project.

REPRESENTATIVE SEATON requested clarification that this wouldn't include TransCanada as a client for the Department of Law.

MR. POAG said that TransCanada is not a client.

[5:54:21 PM](#)

REPRESENTATIVE TARR asked whether the language in paragraph (47), which refers to AS 38.05.020(b)(10) and (11), represents a problem since it is the negotiating powers given to the commissioners. She said that this language refers generally to the North Slope natural gas project; however paragraph (48) refers specifically to the Alaska liquefied natural gas project.

She asked whether the language used matters since the projects are referred to differently.

MR. PAWLOWSKI answered that, while the focus has been largely on the Alaska LNG Project, the powers contemplated in AS 38.05.020(b)(10) and (11) are general applications for any North Slope natural gas project. The needs of the department for any gas project, be it AGDC advancing a small line with rapidity, will require similar agreements for throughput, contractual commitments, and balancing, which are all necessary to move any gas project forward. Those specific contracts of any duration will come back to the legislature for approval. It is important to obtain the best counsel to support the state no matter which project occurs.

[5:56:02 PM](#)

REPRESENTATIVE TARR said she wanted to point out the aforementioned since one is the general application of North Slope natural gas project and the other is more specific to the Alaska LNG Project. Thus, authorizing Amendment 34 would also authorize the procurement exception for any North Slope natural gas project that happens.

MR. PAWLOWSKI pointed out that the important exemption for the Department of Law, in particular, relates to the unconventional step that has been taken with previous amendments to bring the Department of Law into the AGDC, which already enjoys an exemption from procurement to ensure consistency of legal voice. In doing that, paragraph (48) became very important to ensure AGDC has the ability to function on behalf of the state in the way the legislature empowered the corporation last year. He acknowledged that the language in paragraph (47) is broader since those agreements will apply to any of the large natural gas projects to commercialize North Slope gas.

[5:57:20 PM](#)

REPRESENTATIVE SEATON observed line 13, [paragraph] (48), specifies only the project included in AS 31.25.390 of Amendment 34. He requested clarification of what that project is.

MR. PAWLOWSKI said the reference to AS 31.25.390 is the definition found on page 10 of [CSSB 138 (FIN) am] of proposed Sec. 12, which provides the most specific statutory definition of the Alaska LNG Project.

[5:58:38 PM](#)

REPRESENTATIVE SEATON removed his objection. There being no further objection, Amendment 34 was adopted.

[5:59:29 PM](#)

REPRESENTATIVE TARR moved to adopt Amendment 35, labeled 28-GS2806\I.A.41, Bullock, 4/3/14, which read:

Page 53, following line 14:

Insert a new bill section to read:

*** Sec. 58.** The uncodified law of the State of Alaska is amended by adding a new section to read:

RESERVATION RATE IN AN AGREEMENT FOR THE TRANSPORTATION OF NATURAL GAS. A firm transportation services agreement or other agreement or contract for the transportation of natural gas received by the state as royalty in kind or as payment of tax may not include a provision that requires the state to pay, during periods when no natural gas is being transported, an amount greater than the amount necessary to capture depreciation recovery, return on equity, cost of debt, income taxes, fixed operation and maintenance costs, and other taxes that are not related to income."

Renumber the following bill sections accordingly.

Page 56, line 6:

Delete "61"

Insert "62"

Page 56, line 9:

Delete "secs. 62 and 63"

Insert "secs. 63 and 64"

REPRESENTATIVE HAWKER objected.

[6:00:01 PM](#)

REPRESENTATIVE TARR explained Amendment 35 would provide protection if a service interruption occurred. She referred to page 4 of Exhibit C of the Memorandum of Understanding (MOU) [with TransCanada], commercial term 12, which says that the state will be responsible for full payment during service interruption. The term "full payment" is not defined but it

does use two other terms, the "usage rate" and the "reserve rate." The "reserve rate" reflects the owners cost of capital, debt, depreciation taxes, and other fixed costs. It doesn't include the "usage rate" which is the actual cost of operation. Thus, if Amendment 35 was adopted and in the event the pipeline is not operating, the state wouldn't have to pay that portion of the tariff - the operating costs - but would pay the fixed cost, thereby providing a little protection to the state.

[6:01:08 PM](#)

REPRESENTATIVE HAWKER, speaking to his objection, said this is "the project amendment." Natural gas transportation projects, which are a constant value chain from the wellhead to market, are predicated on those firm transportation [services] agreements (FTSAs). The "take or pay contracts" stem from the FTSAs and mean the party commits to pay for shipping a certain volume of gas, whether or not the party actually has that gas to ship. Those FTSAs represent the collateral value that is taken to the financing institutions who give the parties credit to build the pipeline. Financial institutions don't care if any service interruptions occur or if the parties don't have enough gas to ship. Financial institutions, to minimize their risk and recover the money loaned to the project, must be assured that the party will pay regardless of shipping. He appreciated the sponsor's desire to protect the state, but said Amendment 35 has the potential of violating the whole premise under which a project would be financed and operated in the real world.

COMMISSIONER BALASH said that during its review of Amendment 35, [the administration] was struck with the question of whom or what would be protected. The amendment addresses a period in which no natural gas is being transported so there is a service interruption. Having a reservation rate and usage rate as described by the sponsor represents a small difference in terms of operating costs and fuel gas that might be used to operate the system. As long as the state can make the payment it seems as though Amendment 35 directs the state to do what it is already doing. He requested further clarification on what the goal or the protection is supposed to be.

[6:04:20 PM](#)

REPRESENTATIVE TARR said she would not disagree with Representative Hawker if the process was farther along; however, Amendment 35 attempts to put some "sidebars" on the negotiations that take place to come up with a firm transportation [services]

agreement (FTSA). She related her understanding that the agreements would not be in place, but the enabling legislation attempts to provide the department the flexibility to come up with those agreements. She pointed out the Heads of Agreement (HOA) and MOU have some of the "sidebars" in place, but Amendment 35 would provide an additional one. Certainly, service interruptions could occur that have nothing to do with the state and she expressed concern about the effect the interruptions would have on the state's financial position. Amendment 35 could help avoid some operational costs since the state is "on the hook" for the FTSA's, which represent financial losses. She acknowledged that the parties have all come into the project together, which is why fixed costs are shared; however, if the state isn't responsible for the service interruption it would not be required to pay for the operation absent any gas.

[6:06:27 PM](#)

MR. PAWLOWSKI remarked he is caught between Representative Hawker's concerns about unintended consequences of Amendment 35, and the impact that language has on the administration going into a negotiation with the state required to achieve something that may be commercially unreasonable. For example, the service interruption may not be anyone's fault, but the cost would be shared, given alignment. The "daisy chain" of contracts has underpinned the proposed Alaska LNG Project and to an extent it is difficult to determine what Amendment 35 covers and what it does not cover since the agreements are technical agreements that will be started in the term sheet and brought back. Introducing something in the middle of the "daisy chain" creates uncertainty and makes the department uncomfortable. For example, as Representative Hawker described, it could upset the state's ability to actually obtain the commitments to deliver the financing for the project. The "gas not flowing" will affect all of the parties equally, which is an important point to remember. It is in everyone's interest to have the capacity utilized to the maximum extent possible on a regular basis. He understood the concern, saying it needs to be discussed with the legislature and represents healthy dialogue with this committee, but said he does not think the department can support Amendment 35 at this time due to the potential unintended consequences.

[6:08:35 PM](#)

REPRESENTATIVE P. WILSON related her understanding of Amendment 35, such that it puts the state in the middle of some of the

negotiations by stipulating "interrupted service" as one of the negotiation points. She said she doesn't think the state should engage in this.

REPRESENTATIVE TARR argued that this is the only time for the state to do so. This needs to be addressed now or it will be negotiated and come back to the legislature for approval and will be beyond the time when the state can influence the terms. Thus, keeping that interest in mind, the state would have the conversation about what it hopes will be accomplished during the negotiation.

REPRESENTATIVE P. WILSON disagreed, saying it doesn't seem reasonable to expect the other parties to pick up the "service interruption" costs since the state is one of four parties and therefore it should share the costs.

REPRESENTATIVE TARR replied that is not what Amendment 35 does. She explained that this references the MOU, which is the state's relationship with TransCanada but not with the other project sponsors. Thus, it represents the state's negotiations with TransCanada. The administration would have the authority to negotiate these contracts, one of which will be the FTSA's. She reiterated that once negotiations are completed, the legislature will be approving the agreements or contract and at that point it would be too late to introduce new terms. Thus, this is one item that should be part of the list of items the state should cover during the negotiations. She reiterated that Amendment 35 doesn't pertain to other project sponsors, but is limited to TransCanada through the MOU. The state would agree to the fixed costs; however, during any "service interruption" this language would pertain only to the state and TransCanada.

[6:11:34 PM](#)

CO-CHAIR FEIGE assumed the sponsor is referring to page 4, item 12, of the MOU, Exhibit C. He said that item covers the terms when an interruption of firm service happens including force majeure. He further said that the shipper continues to make full payment during periods of service interruption. He related his understanding under Amendment 35 that the amount the state pays would be an amount not greater than the amount "... necessary to capture depreciation recovery, return on equity, cost of debt, income taxes, fixed operation and maintenance costs, and other taxes that are not related to income." He asked for clarification on any other costs other than the variable operation and maintenance costs.

REPRESENTATIVE TARR answered the amendment refers to the general operating costs as defined by the usage rate versus the reserve rate. The reserve rate would include all the costs just described, but the usage rate would represent additional costs. She maintained this is the only opportunity for the state to negotiate.

CO-CHAIR FEIGE asked whether the sponsor knows what the relative costs are.

REPRESENTATIVE TARR replied she did not "run the numbers" on this.

COMMISSIONER BALASH commented the state will be engaging the legislature through committees during the negotiation process so the state will have an opportunity for feedback and guidance to ensure nothing "lands with a thud." Second, although he doesn't specifically have an issue with Amendment 35, he has previously objected to anything that may interfere with negotiations, so he's inclined not to support this.

[6:14:58 PM](#)

REPRESENTATIVE HAWKER, from an investment banker's perspective, asked for clarification on what Amendment 35 means and what the difference is between all the costs being incurred. Even if this language doesn't really do anything, it could impact negotiations. Even though financial companies are accustomed to FTSA's, this language is unusual and could create an increased risk and increased interest costs that could pass through to the entire project. He expressed further concern that if the state is not absolutely clear on [the language] it can become an unknown in the underwriting process that could result in either a failed process or increased risk and costs to the state. He characterized Amendment 35 as a "poison pill" at the underwriting table.

REPRESENTATIVE SEATON said he has never seen a firm transportation services agreement (FTSA). He suggested that if a usage cost rate is a normal term then it makes sense that the state isn't paying costs that the investors don't care about. The project is supported by the return on equity cost and depreciation. Acknowledging this is beyond his expertise, he said he's inclined not to put in Amendment 35, but noted the departments have a heightened awareness of the concerns raised.

[6:19:56 PM](#)

REPRESENTATIVE KAWASAKI asked whether the language in Amendment 35 represents something similar to language in other contracts.

JANAK MAYER, Partner, Energy Consultant, enalytica, concurred with Commissioner Balash, stating it is not clear to him that this isn't already in the MOU or part of a firm transportation services agreement (FTSA). He noted variable costs go up and down with transport of gas in the pipeline. However, he cannot see any direct protection that would be provided to the state but any it would provide would be minimal. He offered his belief that to the extent Amendment 35 adds ambiguity, it seems the cost is greater than the benefit, as was pointed out by Representative Hawker.

NIKOS TSAFOS, Partner, Energy Consultant, enalytica, agreed with Mr. Mayer, stating that especially thinking about a pipeline, the chief variable cost is the cost of gas used to power the pipeline so if there isn't any gas flowing, the number would be multiplied by zero or would be a small amount.

[6:23:33 PM](#)

REPRESENTATIVE TARR withdrew Amendment 35, stating that this conversation has been helpful. She referred to the MOU with respect to full payment, noting that without it being defined it led her to be concerned. She offered her belief that the conversation is sufficient to highlight the concern and to give the commissioners direction as they go through the negotiation process. She indicated that Alaska's situation is different since the state is not a multi-national corporation conducting oil and gas development projects throughout the world, such that if one project doesn't perform well, other projects provide revenue sources.

[6:25:24 PM](#)

REPRESENTATIVE TARR moved to adopt Amendment 36, labeled 28-GS3806\I.A.27, Bullock, 4/1/14, which read:

Page 53, following line 14:

Insert a new bill section to read:

"* **Sec. 58.** The uncodified law of the State of Alaska is amended by adding a new section to read:

SUBMISSION OF AGREEMENTS AND CONTRACTS FOR LEGISLATIVE APPROVAL AND THE AUTHORITY TO EXECUTE. (a)

The commissioner of natural resources may not submit an agreement or contract associated with a North Slope natural gas project for legislative approval and the authority to execute before the license issued under AS 43.90 (Alaska Gasline Inducement Act) has been revoked or abandoned.

(b) At the time an agreement or contract associated with a North Slope natural gas project is submitted for legislative approval and the authority to execute under AS 38.05.020(b)(11), enacted by sec. 14 of this Act, the commissioner of natural resources shall certify in writing that the license issued under AS 43.90 (Alaska Gasline Inducement Act) has been revoked or abandoned."

Renumber the following bill sections accordingly.

Page 56, line 6:

Delete "61"

Insert "62"

Page 56, line 9:

Delete "secs. 62 and 63"

Insert "secs. 63 and 64"

REPRESENTATIVE OLSON objected.

REPRESENTATIVE TARR withdrew Amendment 36, stating that a lot of discussion surrounds the timeline. She indicated a number of issues have been resolved as the committee substitute further outlines the transition timeframe, which is the reason that she is comfortable withdrawing Amendment 36.

[6:26:49 PM](#)

REPRESENTATIVE KAWASAKI moved to adopt Amendment 37, labeled 28-GS2806\I.A.39, Bullock, 4/3/14, which read:

Page 53, following line 14:

Insert a new bill section to read:

"* **Sec. 58.** The uncodified law of the State of Alaska is amended by adding a new section to read:

REOPENER PROVISION IN A FIRM TRANSPORTATION SERVICES AGREEMENT. If the commissioner of natural resources or another person acting on behalf of the state enters into a firm transportation services agreement for the transportation of natural gas

received by the state as royalty in kind or as payment of tax, the firm transportation services agreement must include a provision providing that the agreement may be reopened for modification if a sales contract for the natural gas that is transported provides that the sales contract may be reopened for renegotiation."

Renumber the following bill sections accordingly.

Page 56, line 6:

Delete "61"

Insert "62"

Page 56, line 9:

Delete "secs. 62 and 63"

Insert "secs. 63 and 64"

CO-CHAIR SADDLER objected.

REPRESENTATIVE KAWASAKI explained that Amendment 37 would place a reopener provision in a firm transportation services agreement (FTSA) in the uncodified law. The amendment seeks to ensure that there's a provision reopener in the shipping contracts with TransCanada, or the company holding the state's midstream interests. So, if gas sales and marketing contracts are revisited due to change in the marketing fundamentals that destabilizes gas, such as gas changes price or locations change price, that the contracts can be adjusted. He said he does not believe the current MOU addresses this aspect.

[6:28:14 PM](#)

COMMISSIONER BALASH said this provision is not in the term sheet or MOU so it would represent a material change. It would not be well received by the counter-party and it is not reasonable in terms of the pipeline transportation services agreement. He said there may be other agreements that the state negotiates in the course of this commercial transaction that may be appropriate for reopeners, but not this one.

REPRESENTATIVE HAWKER recalled a previous discussion which highlighted that what happens downstream in the market is a risk the state takes moving into this entire project. The entire pipeline project is underpinned by firm transportation services agreements (FTSAs), which are "take or pay agreements" in the value chain. He expressed concern that if the state goes to the debt market indicating it will reopen FTSAs and the "take or pay

contracts" due to downstream market changes, it will introduce risk, ambiguity, and much higher cost for capital. He said he has a difficult time with renegotiating firm transportation shipping commitments if something happens in the market, which is counter to the foundation of the pipeline project.

[6:30:21 PM](#)

REPRESENTATIVE TARR suggested the consultants could weigh in since she recalled that oftentimes this does happen but if one contract is reopened it may allow for another contract to be revisited.

MR. TSAFOS responded enalytica has discussed that the LNG contracts are likely going to include the conditions under which a price review may occur. That price review could be both periodic, such as every three or four years, as well as conditions that allow for an extraordinary review of price if the market fundamentals have changed completely. Additionally, enalytica has said the state can specify in the contracts both the conditions under which the price review may happen as well as limit the extent to which the price may change. He recalled some contracts allow the price to be changed, but it may be limited to 5, 10, or 15 percent above or below the initial price. If the seller of the gas is buying that gas from some other party, it's quite possible that a provision will link the buying and selling of gas. He related a scenario in which [Dimosia Epichirisi Paroxis Aeriou] (DEPA) is buying gas from BOTAS Petroleum Pipeline Corporation (BOTAS), and BOTAS is buying gas from Azerbaijan. He explained that Azerbaijan increased the price to BOTAS, who subsequently tried to increase the price to DEPA, which ended up in arbitration. One of the arguments was if one of the two contracts had the exact same provisions whether the contract could get renegotiated. They further held discussions on retroactivity of the renegotiations. Thus, it certainly would be possible to have this happen, he said.

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MR. TSAFOS, speaking specifically to Amendment 37, pointed out two things. First, in terms of unintended consequences, it is possible it could result in a price increase the state would need to hand over to TransCanada. He understood the intention is to protect the state against the state's margin "getting squeezed," but depending on how the language is written, it might be possible to obligate the state to share with

TransCanada as part of a reopener. Second, he speculated this type of risk is one that TransCanada would be uncomfortable taking on since it is basically a market risk. TransCanada's model allows it to take on construction risk, operation risk with compensation via a tariff; however, TransCanada does not take on market risk in the sense that its price is subject to volatility in the end-user price. He imagined that this provision would expose TransCanada to a type of risk that it is not accustomed to taking nor is TransCanada experienced in mitigating that type of risk.

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REPRESENTATIVE TARR stated that through these discussions she realizes there are opportunities in which the state could benefit, but in crafting the amendment, she had been considering that the market might worsen and the state could share the risk or reduced revenue. She asked whether it would be worthwhile to consider this for the aforementioned scenario.

MR. TSAFOS replied his reaction to what was just described by Representative Tarr is that there is a certain amount of sales risk that is taken on. However, other counter parties would be better suited to help the state manage its risk, whether it is the counter parties that the state sells its gas to or if it is the three producers if the producers are marketing the gas on the state's behalf. He fully understood the exposure Representative Tarr hopes to mitigate, but his reaction is that TransCanada would not be the vehicle to reduce that exposure. He instead suggested that the sales contracts are the more appropriate vehicles to accomplish mitigation.

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MR. JANEK, with respect to Mr. Tsafos's comments on allocation of risk and reward, said that it comes back to fixed claims and the impact on project risk. One benefit of royalty-in-kind participation is there isn't a fixed tariff that implicitly applies to the entire midstream. For example, one of the dangers that could come from reintroducing fixed claims would be TransCanada doing some form of it. It is important to be inherently aware of the risk that comes with fixed claims on the project cash flow; however, with this type of participation, there are costs and benefits. It is a hard risk to avoid since the nature of TransCanada's participation in this project is that the pipeline company has a fixed claim on the project's cash flow. As Mr. Tsafos said earlier, TransCanada provides

financing and technical expertise with a limited degree of cost and project risk, but it is not exposed to market risk. So, to ask TransCanada to do something else would be to expect the company to completely transform its role.

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REPRESENTATIVE KAWASAKI withdrew Amendment 37, stating that he appreciated the conversation and the committee discussion of Alaska and its risk profile as compared to other partners. He highlighted his goal is to find ways so Alaska doesn't "shoulder" more risk, given that its partners have many other projects [to spread risk.] He acknowledged that the reopener provisions and tying it to the service agreements probably doesn't make quite as much sense. He wondered if dealing with the reopener provisions in the sales and marketing contracts or some other option would be a more appropriate way to transfer some of the risk.

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REPRESENTATIVE P. WILSON moved to adopt Amendment 38, labeled 28-GS2806\I.A.21, Bullock, 4/1/14, which read:

Page 11, line 28:
Delete "10"
Insert "[20]"

[Note to reader: The amendment labeled 28.GS2806\I.A.21, Bullock, 4/1/14, and provided by Legislative Legal and Research Services, Legislative Affairs Agency, is not the version of Amendment 38 offered in committee.]

CO-CHAIR SADDLER objected.

REPRESENTATIVE P. WILSON explained Amendment 38, noting that changes were made to the [affordable] energy fund in the bill in the other body to insert 30 percent of [the revenue received from the state's royalty], which was later reduced to 10 percent. She expressed concern that once everything is taken out of the state's royalty it leaves about 7.5 percent for the [affordable] energy fund. Amendment 38 would increase the percentage to 20 percent, which would ultimately result in 15 percent to the [affordable] energy fund.

CO-CHAIR FEIGE asked whether the effective rate would be 15 percent of the total.

REPRESENTATIVE P. WILSON answered yes.

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REPRESENTATIVE KAWASAKI understood the affordable energy fund is intended to help develop infrastructure in areas of the state that are not expected to have direct access. He requested a definition of the term "direct access" since Fairbanks would not have direct access, but the project will be in its "backyard."

CO-CHAIR FEIGE offered his belief that Fairbanks would be directly connected.

REPRESENTATIVE P. WILSON recalled maps were previously provided that showed which areas of the state were directly affected; Amendment 38 would apply to those areas not on the map. She clarified that the effective rate would be changed from 7.5 percent to 15 percent.

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CO-CHAIR SADDLER said that regardless of how the percentages are changed, the proposal would change the reservation from about \$90 million per year, according to the fiscal note, to \$180 million per year. Given he has heard some fairly compelling arguments against dedication of funds, he said he would have a hard time supporting doubling the rate regardless of how the percentage is calculated.

REPRESENTATIVE SEATON explained that the purpose of the [affordable energy] fund is to assist areas not receiving direct benefit from the pipeline or property taxes, which is the economic development impetus. He could envision it in this case, but he could not support dedicating funds to the Kenai Peninsula, Anchorage, or Fairbanks since those areas will have access to gas. He did not find the amendment to be an unreasonable apportionment throughout the state. Additionally, he thought some type of distribution would be necessary for development of mining and other development that will generate economically for the whole state.

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REPRESENTATIVE P. WILSON felt it was important to put something like this in place for rural areas not on the road system without access although she wasn't including her area. She said

in terms of fairness it is important to assist rural areas in particular, since the Power Cost Equalization funding is being removed.

REPRESENTATIVE HAWKER sympathized with the argument being made, but pointed to the overall fiscal picture of the state. He maintained Amendment 38 would be taking "money off the table" in future years instead of requiring all of the needs to compete on equal footing. He cautioned that the legislature can't be certain of what needs may arise in 10 years. Although he is personally uncomfortable with the [affordable] energy fund in the bill, he found Representative Seaton's argument compelling. He understood some communities will have a direct impact from the operation of a pipeline but there are those that won't. Thus he could accept the current 10 percent in the bill, but maintained he will be uncomfortable increasing the amount.

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REPRESENTATIVE TARR pointed out another bill, SB 183, would extend the emerging energy technology and grant program. She asked how that fund is different than this one.

MR. PAWLOWSKI asked whether Representative Tarr is referring to the emerging energy technology fund or the sustainable energy transmission supply fund.

REPRESENTATIVE TARR replied she is referring to the emerging energy technology fund.

MR. PAWLOWSKI answered that the emerging technology fund is a grant program within the Alaska Energy Authority to fund start-up technologies. Those may or may not work, he said. They go through an advisory panel that uses some of the national renewable energy laboratory standards in terms of identifying a start-up technology. The amendments to SB 138 proposed by the other body were for the more proven infrastructure for areas without direct access to the pipeline. He said one of the things the department has described are re-gas facilities in coastal communities to ensure that they can benefit from the LNG that is coming out of this project or a continuation of the LNG plant on the Kenai Peninsula. He said that nexus of the discussion was important in the evaluation; however, they are completely different funds.

REPRESENTATIVE TARR asked whether Mr. Pawlowski has any concerns that the Alaska affordable energy fund is not defined. She

offered her belief that it would be up to the legislature's discretion as to what the legislature would want to appropriate. She envisioned the process would include application and regulations being developed by the department.

MR. PAWLOWSKI responded that while the fund is a repository, it is up to the legislature to appropriate that fund to a program. The legislature could appropriate the funds to the emerging energy technology fund or the renewable energy grant fund since the legislature has wide discretion on the use of the funds.

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REPRESENTATIVE TARR said her concern is the affordable energy fund and who makes the decision and how that is defined.

MR. PAWLOWSKI answered that the fund and the appropriate projects would be defined by the legislature.

CO-CHAIR SADDLER noted that nothing in the language says "affordable" other than the title. He inquired whether any criteria would be available to judge whether access to the energy would be affordable. Additionally he said did not see any definition of "direct access" except in the title.

REPRESENTATIVE TARR referred to page 11, proposed AS 37.05.610 (a) which read, "The Alaska affordable energy fund"

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CO-CHAIR SADDLER maintained his objection to Amendment 38.

A roll call vote was taken. Representatives Seaton, P. Wilson, Tarr and Feige voted in favor of Amendment 38. Representatives Johnson, Olson, Kawasaki, Hawker, Saddler voted against it. Therefore, Amendment 38 failed by a vote of 4-5.

The committee took a brief at-ease.

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ADJOURNMENT

The House Resources Standing Committee recessed at 6:56 p.m. to 8:07 a.m. on 4/9/14.