

SENATE FINANCE COMMITTEE

April 1, 2013

9:07 a.m.

[9:07:58 AM](#)

CALL TO ORDER

Co-Chair Meyer called the Senate Finance Committee meeting to order at 9:07 a.m.

MEMBERS PRESENT

Senator Kevin Meyer, Co-Chair
Senator Pete Kelly, Co-Chair
Senator Click Bishop
Senator Mike Dunleavy
Senator Lyman Hoffman
Senator Donny Olson

MEMBERS ABSENT

Senator Anna Fairclough, Vice-Chair

ALSO PRESENT

Senator John Coghill; Rynnieva Moss, Staff, Senator John Coghill; Michael Hanley, Commissioner, Department of Education and Early Development; Elizabeth Sweeney Nudelman, Director, School Finances and Facilities, Department of Education and Early Development; Joe Balash, Deputy Commissioner, Department of Natural Resources; Jeff Cook, Regional Director, External Affairs, Koch Industries Public Sector, Flint Hills Resources

PRESENT VIA TELECONFERENCE

Steve Noonkesser, Director of Instruction, Southwest Region School District, Dillingham; David Piazza, Southwest Region School District, Dillingham; Jerry Covey, Education Consultant, Cook Inlet Tribal Council, Citizens for the Educational Advancement of Alaska's Children, Barrow; Chris Ritan, Superintendent, Galena City School District, Galena; Eric Gebhart, Superintendent, Nenana School District, Nenana; Dr. Norman Eck, Superintendent, North West Arctic

Borough School District, Kotzebue; Lisa Rieger, General Council, Cook Inlet Tribal Council, Anchorage;

SUMMARY

SB 47 STIPEND FOR STATEWIDE BOARDING SCHOOL

SB 47 was HEARD and HELD in committee for further consideration.

SB 49 MEDICAID PAYMENT FOR ABORTIONS; TERMS

SB 49 was REPORTED out of committee with a "do pass" recommendation and with a previously published indeterminate fiscal note: FN1(DHS).

SB 59 OIL & GAS EXPLORATION/DEVELOPMENT AREAS

SB 59 was SCHEDULED but not HEARD.

SB 86 APPROVE FLINT HILLS ROYALTY OIL SALE

SB 86 was HEARD and HELD in committee for further consideration.

#sb49

SENATE BILL NO. 49

"An Act defining 'medically necessary abortion' for purposes of making payments under the state Medicaid program."

9:10:30 AM

SENATOR JOHN COGHILL, regretted that he had been unable to sit in on the previous public testimony. He offered that he had instructed his staff to write up the six main points generated from public testimony in the Senate Judiciary Committee. He said that SB 49 would attempt to define the term "medically necessary" for the purpose of Medicaid payments for abortions. He cited his six main points:

Rebuttal to Planned Parenthood and Testimony from Saturday, March 30, 2013

1. The testimony was broad and, at times, emotional. That is generally a common trait when debating issues involving abortion.

2. Sen. Coghill wants to correct some misunderstandings about the bill including some misunderstandings that come from its opponents.

POINT 1 - PLANNED PARENTHOOD STILL COULD NOT CLEARLY DEFINE WHAT AN ELECTIVE ABORTION WAS OR THAT ELECTIVE ABORTIONS EVEN EXIST.

a. Of course, a reasonable person could argue that Planned Parenthood cannot openly clearly admit that elective abortions exist because that would make them elective procedures.

i. As we are all aware elective procedures are not covered under Medicaid.

ii. Paying for elective procedures would therefore be an open abuse of Medicaid.

POINT 2 - SB 49 DOES SATISFY EQUAL PROTECTION.

1. The 2001 Supreme Court Opinion stated that the State has to provide medically necessary care for women seeking to give birth to a child.

2. The court also stated that the State has to provide medically necessary care for women seeking an abortion.

a. What some opponents, even to this day, fail to recognize is the Supreme Court directed that a definition for a medically necessary abortion can be crafted as long as we base it on neutral criteria directly related to the health care program. See tab 4c, Page 16 highlighted portion. That is what SB 49 does. It was based on the very language of the 2001 Planned Parenthood decision and includes direct language found in the federal Hyde Amendment. The conditions are neutral and taken specifically from doctors in the field.

i. One doctor disagreed with the conditions on Saturday. What she may or may not know is that the conditions were overwhelmingly directly taken from the 2001 Planned Parenthood decision.

POINT 3 - SB 49 UNFAIRLY TARGETS POOR WOMEN?

1. The US Supreme Court, long ago ruled that the Federal Constitution does not require a State to pay for the costs of elective abortions just because it pays for the costs of childbirth related medical care. See Maher v. Roe, 432 US 464, 474 (1977)

2. Additionally, the United States Supreme Court, in 1980, ruled that the Hyde Amendment (which is the foundation for SB 49) does not violate women with lower incomes right to obtain a medically necessary abortion. The case was Harris v. McRae, 448 US 297 (1980). The State has no obligation to remove obstacles that it did not create (namely the woman's status of being of little means).

POINT 4 - OTHER ATTEMPTS TO LIMIT ABORTIONS SINCE 2001 MAY OR MAY NOT HAVE BEEN SUCCESSFUL.

1. SB-49 has nothing to do with those attempts. We cannot comment on the reasons they may or may not have been successful. This is a total different focus. SB-49 is a "lean muscle" bill. We have high confidence in how thorough and specific the bill is drafted.

POINT 5 - SURVIVAL OF FETUS IS NOT CONSIDERED?

1. That is simply incorrect. We've heard testimony as to the "floating tomb" and the child being "brainless." We considered that option and incorporated Paragraph 4, B, 22 (See Tab 1). "Another physical disorder...arising from the pregnancy...that would be a major bodily impairment."

POINT 6 - AN OPPONENT OF THE BILL STATED THAT YOU CANNOT SEPARATE "PHYSICAL HEALTH" AND "MENTAL HEALTH."

1. With all due respect, President Obama via Executive Order 13535, case law, and the very existence of the Hyde Amendment prove otherwise. Sen. Coghill invites you to look at tab 7 in your binders. The language is clear to emphasize

"physical disorder", "physical injury", or "physical illness." It specifically does not include mental or psychological disorders.

2. In addition, SB 49 supporters, including 3 national doctors and 7 Alaskan doctors fundamentally disagree with that presumption. There is a genuine disagreement in the medical community that mental and psychological conditions should be included under the definition of "medically necessary abortion."

[9:15:28 AM](#)

Co-Chair Meyer recalled that there had been testimony suggesting that the legislation could result in a savings for the state.

Senator Coghill replied that possible savings to the state were indeterminate.

[9:15:50 AM](#)

Co-Chair Meyer wondered about possible cost to the state for litigating the legislation.

Senator Coghill replied that possible litigation was out of his control.

[9:16:14 AM](#)

Co-Chair Kelly MOVED to REPORT SB 49 out of committee with individual recommendations and the accompanying fiscal note. There being NO OBJECTION, it was so ordered.

[9:16:29 AM](#)

SB 49 was REPORTED out of committee with a "do pass" recommendation and with a previously published indeterminate fiscal note: FN1(DHS).

#sb47

SENATE BILL NO. 47

"An Act increasing the monthly stipend available for students attending a statewide boarding school operated by a school district; and providing for an effective date."

[9:16:58 AM](#)

Senator Coghill testified that the bill would remove the sunset provision for providing stipends to boarding schools. He said that there were many burgeoning small boarding and trade schools that had been helping young people in rural Alaska to receive an education that they might not otherwise experience. He asserted that boarding schools not only raised the bar for educational standards but also created work and college ready members of society.

[9:19:31 AM](#)

RYNNIEVA MOSS, STAFF, SENATOR JOHN COGHILL, discussed the sectional analysis:

*Sec. 1. This section removes narrow applicability to schools operating before June 1, 2005. Currently three school districts are receiving the stipend: Nenana, Bethel and Galena. The Department of Education is currently soliciting applications for three additional boarding schools statewide.

Sec. 1 also adds magnet schools that have variable-length terms but have a 180-day school year.

*Sec. 2. Section 2 increases the monthly stipend rate based on the region of the state the boarding school is located.

*Sec. 3. Section 4 allows school districts to contract room and board.

*Sec. 4. This section repeals AS 14.17.200(c) which limited DOE to approving three additional boarding school applications.

Sec. 4 also repeals AS 14.16.200(d)(2), the definition for "district-operated statewide residential program" as Section 1 now included both statewide and district-wide residential schools.

*Sec. 5. This Act has an immediate effective date.

Co-Chair Meyer observed that part of the fiscal note for the bill needed to be included in the 2013 Supplemental Budget.

Ms. Moss replied that the administration could speak to the fiscal note.

[9:22:55 AM](#)

Co-Chair Meyer asked about the Jesse Lee Home in Seward. He wondered about the qualifications needed to be labeled a boarding school.

Ms. Moss replied that boarding school qualifications were determined by the public school system. She thought that a public school could contract with the Jesse Lee Home for room and board.

[9:23:25 AM](#)

Co-Chair Meyer noted that it sounded like a charter school.

Ms. Moss informed the committee that charter schools are public schools.

[9:23:36 AM](#)

Senator Bishop pointed to Section 3. He requested an example of the kind of school intended in the section.

Ms. Moss replied that the example would be a non-profit organization that was providing room and board for students attending a public school.

[9:24:17 AM](#)

Senator Dunleavy stated that all charter schools in the state were public schools under the district of their location.

[9:24:48 AM](#)

Co-Chair Meyer inquired whether the administration supported the bill.

MICHAEL HANLEY, COMMISSIONER, DEPARTMENT OF EDUCATION AND EARLY DEVELOPMENT, stated that the department appreciated the cost of housing and monitoring students 24 hours a day, 7 days per week. He believed that the increase in the funding represented true costs. He supported shifting from a statewide to a district-wide component, which would allow

programs to bring in students from outlying schools and provide them the intensives for qualification in the Alaska Native Science and Engineering Program (ANSEP). He explained that the variable term component meant that although the school would run for the full school year, students participating in the ANSEP intensive could cycle through and return to their home schools within the school year.

[9:27:33 AM](#)

Co-Chair Meyer understood that boarding schools boasted high test scores and academic achievement.

Commissioner Hanley replied that comparisons in graduation and achievement rates between the boarding schools and the student's home schools in the state had revealed positive results on the boarding school side.

[9:28:00 AM](#)

Co-Chair Meyer asked how many boarding schools in the state would apply and receive the stipend.

Commissioner Hanley responded four. He noted that Mount Edgecumbe was unique as it was a state-run private school.

[9:28:31 AM](#)

Co-Chair Meyer pointed out to the committee that passage of the legislation would result in an additional \$1.6 million in the supplemental budget.

[9:28:46 AM](#)

ELIZABETH SWEENEY NUDELMAN, DIRECTOR, SCHOOL FINANCES AND FACILITIES, DEPARTMENT OF EDUCATION AND EARLY DEVELOPMENT, agreed that additional funding would need to be added to the supplemental budget to support the legislation.

[9:29:08 AM](#)

Commissioner Hanley interjected that the stipend increase that was awarded two years ago would sunset this year. He said that the lack of the additional funds would make future funding of the state's private schools, except for Mount Edgecumbe, challenging.

[9:29:35 AM](#)

Co-Chair Meyer relayed that the state paid for students to fly several times per year to Mount Edgecumbe in Sitka. He wondered if boarding schools saved the state money.

Commissioner Hanley replied that boarding school students still received the BSA, but that the added boarding component allowed each student one, round-trip ticket to and from school. He believed that boarding schools were more expensive than traditional neighborhood schools, but that tickets would be based on the number of beds the school housed, rather than the number of students who came and went.

[9:31:56 AM](#)

Co-Chair Kelly queried whether a boarding school had been planned for Kotzebue.

Commissioner Hanley replied that the department had recently begun an open application period to allow districts to apply for schools. He stated that the Star of the Northwest boarding school was considering allowing high school students to register.

[9:32:58 AM](#)

Co-Chair Kelly inquired what communities the department would target for boarding schools.

Commissioner Hanley replied that he would do regional research. He said he would consider Barrow, Kotzebue, Bethel and Southeast Alaska.

Co-Chair Kelly asked about Dillingham and McGrath.

Commissioner Hanley said that the Bristol Bay area, Dillingham, King Salmon and Naknek had all been considered. He stressed the importance of building schools in the region of need so that students still felt connected to home.

Co-Chair Kelly queried the lack of roads as a barrier to the success of a boarding school in Kotzebue.

Commissioner Hanley responded that road access was a barrier. He said that currently there were no roads to any of Alaska's boarding schools. He believed that greater access would be beneficial.

[9:35:48 AM](#)

Senator Olson stated that Nenana had a road.

Commissioner Hanley said that the road was relatively far removed from other communities; most of the student still had to fly to the school.

[9:36:17 AM](#)

Senator Olson asked whether there had been requests from certain school districts for a boarding school.

Commissioner Hanley replied that requests had been made. He said that local communities should make their need known to the department. He stated that four areas had applied: Kotzebue, Nome, Chugach, and Anchorage.

[9:37:27 AM](#)

Senator Olson referred to earlier testimony that some students became homesick during Christmastime visits which resulted in students dropping out of boarding school. He wondered if it would be best to not allow them to return home at Christmastime.

Commissioner Hanley said that experience had shown that when students were away from home for too long it became a problem. He recognized that being away from home could be a challenge for teenagers.

[9:38:25 AM](#)

Senator Olson commented that he came from a long line of people that had attended boarding school. He wondered what the options would be for these students if the boarding schools did not exist.

Commissioner Hanley responded that the option would be the neighborhood school; a school with 10-20 students and two teachers. He noted that it was difficult to offer a broad ranged curriculum at a very small school.

[9:39:22 AM](#)

Co-Chair Kelly queried what the cost would be to make the boarding school model work for the state across the board.

Commissioner Hanley responded that the answer was to provide more opportunities for students throughout the state.

Co-Chair Kelly asserted that he was seeking a dollar number.

Commissioner Hanley replied that if you looked at the four schools that had applied and several that had not applied, the department would have to add the cost of access to the schools. He stressed that an exact number was difficult to pencil in. He hypothesized that if you added 1000 rural Alaskan student to full or part-time variable term programs, the total cost would be approximately \$10 million.

Co-Chair Kelly queried what the capital costs would be, once there was an additional \$10 million added to the operating budget.

Commissioner Hanky relayed that the state did not currently build residential facilities; if the state were to do so, the capital cost could be as high as \$50 million per school.

[9:42:53 AM](#)

Senator Bishop noted that there were assets that could be utilized for room and board components. He cited the work in Galena where the Air Force facility was being used for culinary classes. He stressed that there were existing hard assets that could be utilized to stretch state funding.

[9:44:04 AM](#)

Senator Dunleavy asked what kind of school the if the commissioner would send his children to given the choice of a small, two teacher, school or a comprehensive, boarding home, high school.

Commissioner Hanley replied that he would be tempted by the greater options of a boarding school but would ultimately choose the school that was best for the individual child.

[9:44:52 AM](#)

Senator Dunleavy restated the question. Commissioner Hanley asserted that his first inclination as a parent would be to keep his children close to home.

[9:45:09 AM](#)

Senator Dunleavy asked what if the schools were both two blocks away from the commissioner home.

Commissioner Hanley replied that he would send them to the school with the greater opportunity.

[9:45:34 AM](#)

Senator Hoffman noted that Akiak, Akiachak and Tuluksak had been contemplating a sub-regional high school for over a decade. He said that sub-regional schools should be considered before taking half of the student population of a small town and relocating them to boarding schools. He expressed concern that the children left behind could suffer reduced educational opportunities.

Commissioner Hanley agreed that the problem should be considered. He stressed that with the variable term program the funding would stay with the home schools.

[9:48:07 AM](#)

Co-Chair Kelly believed that information should be gathered concerning the cost of building boarding schools and that the Commissioner of Transportations and Public Facilities should be probed for the costs of road they may need to be built to ensure access. He thought that information about the impact of more boarding schools on home schools should be examined.

Commissioner Handley responded that he would gather the information.

[9:50:24 AM](#)

Senator Dunleavy asked if there was a current waiting list for Mount Edgecumbe.

Commissioner Handley said yes.

[9:50:37 AM](#)

STEVE NOONKESSER, DIRECTOR OF INSTRUCTION, SOUTHWEST REGION SCHOOL DISTRICT, DILLINGHAM (via teleconference), spoke in support of SB 47. He stated that declining enrollment had caused the district to close two schools in seven years. He added that the economy of the region did not afford parents the ability to move their family for schooling, which had resulted in elementary school student moving in with other families of other schools in the district. He discussed a proposed amendment that removed the word "secondary" from statute which would provide an avenue to financially assist the house-parents that took in boarding students for communities that no longer had a school. He did not believe that the amendment would increase the fiscal note to an unreasonable level.

[9:53:17 AM](#)

DAVID PIAZZA, SOUTHWEST REGION SCHOOL DISTRICT, DILLINGHAM (via teleconference), testified in support of SB 47 and echoed the comments of the previous testifier.

[9:53:37 AM](#)

JERRY COVEY, EDUCATION CONSULTANT, COOK INLET TRIBAL COUNCIL, CITIZENS FOR THE EDUCATIONAL ADVANCEMENT OF ALASKA'S CHILDREN, BARROW (via teleconference), expressed support for SB 47. He testified that short-term variable and district residential programs worked and were cost effective. He stated that they had minimal negative impact on the student's home schools because they were gone for a short period of time. He believed that the increase of the stipend amount was warranted based on the cost of delivery. He believed that the benefit of the proposed programs would greatly outweigh the costs. He urged support of the bill.

[9:57:15 AM](#)

Senator Olson asked about the ultimate cost of students dropping out of school in underserved areas.

Mr. Covey responded with a history of Bureau of Indian Affairs (BIA) Schools in the state. He pointed out that the capital costs would need to be addressed in terms of the construction of a residential facility, and that the state would also need to determine that existing facilities were being used to their maximum extent. He said that there was space in Kotzebue High School that could accommodate an additional 150 students. He believed existing facilities should be maximized in the effort to keep costs at a minimum. He estimated that a new, 50 student dorm in Kotzebue would be approximately \$12 million. He stated that as the population shifted, the rural schools were getting smaller and smaller and were among the lowest achieving schools in the state. He stressed that one of the best things for students in small schools was to provide them with access to a comprehensive high school located in a rural community.

[10:02:01 AM](#)

CHRIS RITAN, SUPERINTENDENT, GALENA CITY SCHOOL DISTRICT, GALENA (via teleconference), spoke in favor of SB 47 and discussed some of the history of Galena school district. He stated that the district started a boarding in 1997 after gaining access to old Air Force buildings. He explained that the district had grown each year thereafter. He shared that there were 213 students currently enrolled. He said that the main focus of the school was vocational programs. He shared that a 2005 bill had provided funding to offset room and board costs, which up until that time had been paid for through the BSA and federal funding. He said that the extra money saved through the room and board stipend would give the school the ability to expand its already high quality programs for students in the state.

[10:05:04 AM](#)

ERIC GEBHART, SUPERINTENDENT, NENANA SCHOOL DISTRICT, NENANA (via teleconference), testified in support of SB 47.

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DR. NORMAN ECK, SUPERINTENDENT, NORTH WEST ARCTIC BOROUGH SCHOOL DISTRICT, KOTZEBUE (via teleconference), spoke in support of SB 47. He stressed the importance of finishing high school with specific job skills and the ability to enter into post-secondary schooling. He said that smaller

regional schools were necessary as a part of school choice in rural Alaska. He stated 9th and 10th graders in the 9 high schools in his district had a 27 percent proficiency rate on state standardized tests. He said that the percentage was higher in Kotzebue, 51 percent, because it had a comprehensive high school in a regional hub. He said Northwest Arctic had a 53 percent graduation rate for native students; however, each student that took 2 classes in career technical education had an 83 percent graduation rate. He stressed that innovative and instructional programs of practical application to students brought success. He said that the dormitory should be considered an integral part of the school in terms of major maintenance and school construction.

[10:09:05 AM](#)

Senator Olson inquired the testifier thoughts regarding homesickness among students.

Mr. Eck responded that the hope was to have wireless internet in the dorm. He shared that in the ten outlying villages in Northwest Arctic over 65 percent of the homes had internet access and could use SKYPE. He stressed the importance that students have a strong cultural base.

[10:11:21 AM](#)

Senator Olson acknowledged that the state was dealing with a budget shortfall. He asked whether Dr. Eck believed that the limited funds should be dedicated to boarding schools or early childhood education.

Dr. Eck replied that both were needed, and that his district believed so strongly in early childhood education that it had a program for 4 year-olds. He asserted that the program was so important that it was conducted without any dedicated funding. He stressed the importance that all children learn to read at grade level by the 3rd grade. He thought early childhood was the key to future academic success. He added that students who graduated from school had to be career and job ready. He opined that too many students that graduated from the district could be found unemployed six months later. He concluded that it was the districts obligation to provide the programs necessary in order for students to be successful.

[10:14:19 AM](#)

Senator Bishop wondered if elder mentors in the magnet schools could help ease homesickness among displaced students.

Dr. Eck replied in the affirmative. He noted that the district planned to use elders as part of its advisory group in the dormitory.

[10:15:49 AM](#)

LISA RIEGER, GENERAL COUNCIL, COOK INLET TRIBAL COUNCIL, ANCHORAGE (via teleconference), spoke in support SB 47 and echoed earlier testimony.

[10:19:10 AM](#)

Co-Chair Meyer CLOSED public testimony.

[10:19:28 AM](#)

SB 47 was HEARD and HELD in committee for further consideration.

#sb86

SENATE BILL NO. 86

"An Act approving and ratifying the sale of royalty oil by the State of Alaska to Flint Hills Resources Alaska, LLC; and providing for an effective date."

[10:20:20 AM](#)

JOE BALASH, DEPUTY COMMISSIONER, DEPARTMENT OF NATURAL RESOURCES, stated that the bill would grant legislative approval for the sale of royalty oil to Flint Hills Resources by the Department of Natural Resources (DNR). He began with Slide 2 of the presentation, "Royalty In-Kind Sale to Flint Hills Resources" (copy on file):

The state has a choice to take its royalty in-value (RIV) or in-kind (RIK).

- When the State takes its royalty as RIV, the lessees who produce the oil also market the State's share along with their own production and pay the State the value of its royalty share.

- When the State takes its royalty share as RIK, the State assumes ownership of the oil, and the commissioner disposes of it through the sale procedures prescribed by AS 38.05.183.

[10:22:13 AM](#)

Mr. Balash spoke to Slide 3, "Non-Competitive RIK Sale Process":

- Statute presumes State's Best Interest is met by
 - Taking royalty in-kind-AS 38.05.182(a)
 - With sale to in-state buyer-AS 38.05.183(d)
 - Accomplished through a competitive process-AS 30.05.183(a)
- August 13, 2012 Informal Solicitation of Interest sent to:
 - North Slope Producers
 - In-state Refiners
 - Industry specific & general media

[10:24:04 AM](#)

Mr. Balash addressed Slide 4, "RIK Contract Terms":

- Proposed 2013 contract is similar to 2004 contract
- Proposed 2013 contract, like 2004 contract, does not directly reference RIV valuation in RIK price calculations
- Key Contract provisions
 - Price
 - Quantity
 - Term
 - Special Commitments
 - In-State Processing and Local Hire

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Mr. Balash discussed Slide 5, "RIK Contract Price":

ANS Spot Price - \$2.15 - Tariff Allowance ± Quality Bank Adjustment - Line Loss

- ANS Spot Price = Average US West Coast Price for Alaska North Slope oil.

-Reported by industry trade publications: Platts, Telerate, Reuters

- \$2.15 = RIK Differential
 - Destination Value - Marine Costs so $RIK \geq RIV$.
 - Subject to a one-time adjustment of no more than $\pm \$0.15$ per barrel.
 - This amount = \$1.65 per barrel in the current 2004 contract.
- Tariff Allowance = TAPS and Pipelines Upstream of PS-1.
- Quality Bank Adjustment = as reported by the TAPS Quality Bank Administrator
- Line Loss = 0.0009 times the netback price

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Mr. Balash pointed to Slide 6, "RIK Contract Quality":

- Initial Quantity Range
 - 18,000 - 30,000 barrels per day
 - May be adjusted after 12 months, with Commissioner approval
- Termination of Contract
 - No or zero nomination for 3 months terminates contract
 - Contract terms comparable to the private market
- Refinery Turnaround
 - Contract allows FHR the flexibility to cease royalty oil purchases during maintenance
- Guarantees, reserves and proration clauses included
 - 24,000 barrels per day with 15 percent reserves for other RIV or RIK interests

[10:27:31 AM](#)

Mr. Balash addressed Slide 7, "2013 RIK Contract Term":

- FHR initially sought a ten-year contract
 - Creates supply and price risk
 - Increases counterparty risk

- Limits the State's ability to supply other RIK buyers
- DNR negotiated a five year term
 - April 1, 2014 to March 31, 2019
 - Possible extension condition for:
 - Large capital improvement at the North Pole Refinery
 - Binding support for a North Slope natural gas transportation system

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Mr. Balash discussed Slide 8, "2013 RIK Contract Quantity", which was a bar graph that illustrated the total expected royalty oil and liquid natural gas volume and the expected share committed to Flint Hills Resources.

[10:30:54 AM](#)

Mr. Balash spoke to Slide 9, "Commissioner's Decision Criteria":

AS 38.05.183(e) states that the commissioner must sell the State's royalty oil to the buyer who offers "maximum benefits to the citizens of the state." In making this determination the commissioner must consider:

- 1)The cash value offered
- 2)The projected effects of the sale on the economy of the state
- 3)The projected benefits of refining or processing the oil in state
- 4)The ability of the prospective buyer to provide refined products for distribution and sale in the state with price or supply benefits to the citizens of the state
- 5)The eight criteria listed in AS38.06.070(a), as reviewed by the Royalty Board

Mr. Balash addressed Slide 10, "Royalty Board's Decision Criteria":

AS 38.06.070(a) states that the Alaska Royalty Oil and Gas Development Advisory Board must consider:

- 1)The revenue needs and projected fiscal condition of the state

- 2)The existence and extent of present and projected local and regional needs for oil and gas products
- 3)The desirability of localized capital investment, increased payroll, secondary development and other possible effect of the sale
- 4)The projected social impacts of the transaction
- 5)The projected additional costs and responsibilities which could be imposed upon the state and affected political subdivisions by development related to the transactions

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Mr. Balash continued with Slide 11, "Royalty Board's Decision Criteria":

AS 38.06.070(a) states that the Alaska Royalty Oil and Gas Development Advisory Board must consider:

- 6)The existence of specific local or regional labor or consumption markets or both which should be met by the transaction
- 7)The projected positive or negative environmental effects related to the transactions
- 8)The projected effects of the proposed transaction upon existing private commercial enterprise and patterns of investment

[10:32:32 AM](#)

Mr. Balash addressed Slide 12, "Royalty In-Kind Sales." He noted that it was difficult to read. He relayed that over the course of the last 30 years the state had been engaged in the continuous sale of royalty oil. He noted that there were a variety of sales in the early 1980s and that there had been a lot more oil during that time. He said that the price crash of 1986 had caused the department to reconsider how royalty oil was sold and to limit the number and variety of sales.

[10:33:58 AM](#)

Mr. Balash spoke to Slide 13, "Best Interest of the State Served by the RIK Contract with Flint Hills Resources (FHR)":

- Cash Value Offered with Contract

- Cash value of \$3.5-5.9 Billion over 5 years
 - Analyzed for Consistent value between RIK and RIV
 - Volume weighted average of current reported netback price (11 AAC 03.026(b))
- Anticipated increases in marine transportation allowance will favor RIK contract

- Positive effect on the State
 - Maintain stability in in-state refining and distribution of refined products.
 - Support jobs and economy of Fairbanks North Star Borough

[10:35:00 AM](#)

Mr. Balash addressed Slide 14, "FHR's North Pole Refinery":

- Strategically located on TAPS

- Current throughput of 82,000-84,000 barrels per day of ANS crude

- Producing approximately 22,000-25,000 barrels of refined product

- All crude and constituents that are not transformed into refined product are injected back into TAPS (with a penalty paid)

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Mr. Balash continued to Slide 15, "FHR's North Pole Refinery":

- FHR produces approximately
 - 672,000 gallons of jet fuel per day
 - 143,000 gallons of gasoline per day
 - 41,000 gallons of home heating fuel per day
 - 68,000 to 194,000 gallons per day of product consisting of HAGO, LAGO, naphtha, asphalt, refining fuel, and a small volume of high-sulfur diesel

- 680,000 gallons per day shipped to Anchorage via the Alaska Railroad

- 230,000 gallons of ultra-low sulfur diesel and gasoline on the backhaul to Fairbanks
- FHR owns 50 million gallons of storage facilities
 - 30.7 million in Anchorage and 19.3 million in Fairbanks

[10:36:42 AM](#)

Mr. Balash addressed Slide 16, "Proposed Contract Benefits":

- Proposed contract is expected to:
 - Maintain status quo of in-state refining behavior
 - Produce 330 million gallons of refined product or 18% of gasoline and 26% of jet fuel consumed in Alaska
 - Provide approximately \$140 million per year in gross regional product sales for the Fairbanks North Star Borough (FNSB)
 - Support 1,300 direct and indirect jobs in the FNSB
 - Sustain \$100 million in annual earnings in FNSB
 - Provide socio-economic stability against energy costs

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Mr. Balash discussed Slide 17, "Projected Impacts if not Approved":

- If FHR stops refining, anticipated effects include:
 - Loss of approximately 1,300 direct and indirect jobs in the Fairbanks North Star Borough
 - State could experience increased utilization of the social safety net
 - Possibility of population redistribution
 - Increased and decreased infrastructure utilization and maintenance with population shift
 - Impact to the fuel supply for the Fairbanks and Anchorage airports, affecting trade and tourism and the Alaska Railroad
 - Loss of heat source for warming low flow in TAPS

[10:39:14 AM](#)

Senator Hoffman pointed to Slide 9. He requested further explanation of bullet four:

4)The ability of the prospective buyer to provide refined products for distribution and sale in the state with price or supply benefits to the citizens of the state

Mr. Balash responded that the criteria had been examined during the evaluation. He said that FHR distribution patterns had been examined. He said that FHR had been able to sell locally, in the interior at the refinery, as well as the Port of Anchorage area. He stated that there was a special contract commitment provision relative to the pricing of gasoline in the Fairbanks market that help to provide price discipline for the transportation segment of the business line in the interior.

[10:41:23 AM](#)

Senator Hoffman wondered how that equated to "the citizens of the state" versus "the citizens of Fairbanks."

Mr. Balash responded that that question encompassed the tension that was embedded throughout the body of the statute and regulations. He said it would be one thing if DNR were to sell royalty oil at a steep discount to any refinery in that region of the state that resulted in a lower price for consumers of the region. He said that DNR worked to ensure that one community was not benefitting at the expense of others by getting at least royalty and value equivalent for the price offered in the sale of the royalty oil itself. He said that the price available in Fairbanks was a wholesale price that was being offered to the retail outlets in the area.

[10:43:12 AM](#)

Senator Olson asked what were the possibly penalties to the state for not honoring the guarantees provided to FHR.

Mr. Balash turned to Slide 6. He said that the steepest penalty could be grounds for termination of the contract itself. He said that the refinery was required to maintain a letter of credit in good standing. He said that the credit quality of the parent company would be scrutinized as well.

[10:44:34 AM](#)

Senator Olson restated the question.

Mr. Balash responded that he did not think there were any specific penalties to the state. He said that the contract itself would obligate the state to no more than 85 percent of the total royalty volume. He assured the committee that the state was protected to a certain degree.

[10:45:24 AM](#)

Senator Olson queried the future of the refinery in the North Pole area that had been in decline.

Mr. Balash responded that both the refineries in North Pole served distinct markets. He said that FHR was in the business of making jet fuel for sale at Ted Stevens International Airport; however, some products were sold in the interior. He shared that the other refinery largely supplied fuel to military installations and home heating fuel in the residential market. He thought that if the refineries could fire their plants with a cheaper fuel product than was currently being used, overall business would improve.

[10:47:57 AM](#)

JEFF COOK, REGIONAL DIRECTOR, EXTERNAL AFFAIRS, KOCH INDUSTRIES PUBLIC SECTOR, FLINT HILLS RESOURCES, spoke in support of SB 86.

[10:53:46 AM](#)

Senator Bishop inquired whether the bill could bring about growth opportunities in jet fuel.

Mr. Cook responded in the affirmative.

[10:54:52 AM](#)

Senator Dunleavy requested a hard copy of the public testimony.

[10:55:07 AM](#)

Co-Chair Meyer CLOSED public testimony.

SB 86 was HEARD and HELD in committee for further consideration.

SB 59 was SCHEDULED but not HEARD.

10:55:27 AM

#

ADJOURNMENT

The meeting was adjourned at 10:55 a.m.