

SENATE FINANCE COMMITTEE  
March 6, 2014  
9:08 a.m.

[9:08:06 AM](#)

CALL TO ORDER

Co-Chair Meyer called the Senate Finance Committee meeting to order at 9:08 a.m.

MEMBERS PRESENT

Senator Pete Kelly, Co-Chair  
Senator Kevin Meyer, Co-Chair  
Senator Anna Fairclough, Vice-Chair  
Senator Click Bishop  
Senator Mike Dunleavy  
Senator Donny Olson

MEMBERS ABSENT

Senator Lyman Hoffman

ALSO PRESENT

Mike Navarre, Mayor, Kenai Peninsula Borough; Luke Hopkins, Mayor, Fairbanks Northstar Borough;

PRESENT VIA TELECONFERENCE

Clay Walker, Mayor, Healy-Denali Borough; Charlotte Brower, Mayor, North Slope Borough.

SUMMARY

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

SB 138 was HEARD and HELD in committee for further consideration.

#sb138

SENATE BILL NO. 138

"An Act relating to the purposes of the Alaska Gasline Development Corporation to advance to develop a large-diameter natural gas pipeline project, including

treatment and liquefaction facilities; establishing the large-diameter natural gas pipeline project fund; creating a subsidiary related to a large-diameter natural gas pipeline project, including treatment and liquefaction facilities; relating to the authority of the commissioner of natural resources to negotiate contracts related to North Slope natural gas projects, to enter into confidentiality agreements in support of contract negotiations and implementation, and to take custody of gas delivered to the state under an election to pay the oil and gas production tax in kind; relating to the sale, exchange, or disposal of gas delivered to the state under an election to pay the oil and gas production tax in kind; relating to the duties of the commissioner of revenue to direct the disposition of revenues received from gas delivered to the state in kind and to consult with the commissioner of natural resources on the custody and disposition of gas delivered to the state in kind; relating to the authority of the commissioner of natural resources to propose modifications to existing state oil and gas leases; making certain information provided to the Department of Natural Resources and the Department of Revenue exempt from inspection as a public record; making certain tax information related to an election to pay the oil and gas production tax in kind exempt from tax confidentiality provisions; relating to establishing under the oil and gas production tax a gross tax rate for gas after 2021; making the alternate minimum tax on oil and gas produced north of 68 degrees North latitude after 2021 apply only to oil; relating to apportionment factors of the Alaska Net Income Tax Act; authorizing a producer's election to pay the oil and gas production tax in kind for certain gas and relating to the authorization; relating to monthly installment payments of the oil and gas production tax; relating to interest payments on monthly installment payments of the oil and gas production tax; relating to settlements between producers and royalty owners for oil and gas production tax; relating to annual statements by producers and explorers; relating to annual production tax values; relating to lease expenditures; amending the definition of gross value at the 'point of production' for gas for purposes of the oil and gas production tax; adding definitions related to natural gas terms; clarifying that credit

may not be taken against the in-kind levy of the oil and gas production tax for gas for purposes of the exploration incentive credit, the oil or gas producer education credit, and the film production tax credit; making conforming amendments; and providing for an effective date."

9:08:30 AM

Co-Chair Kelly discussed the meeting's agenda. He related that Vice-Chair Fairclough had a bill hearing before another committee, but would join the meeting in progress.

MIKE NAVARRE, MAYOR, KENAI PENINSULA BOROUGH, appreciated the opportunity to discuss the impacts of SB 138 on local governments. He related that the Kenai Peninsula Borough was in agreement that a liquefied natural gas (LNG) project could and should be in the best interest of the state and could provide long-term revenues for both the state and the municipalities. He stated that there were a number of issues that he wanted to discuss that were relevant to local government, as well as concerns regarding some of the things that the borough had reviewed, including the legislation and the heads of agreement (HOA). He related that a group consisting of the Kenai Peninsula Borough, the North Slope Borough, the Fairbanks North Star Borough, and Valdez had got together as a group to discuss the issue of an Alaska LNG project; the group had also invited the Denali Borough, the Mat-Su Borough, and Anchorage, which may be along the route, to participate in some of the discussions regarding what the impacts of such a project might be to municipalities, as well as what issues of concern the municipalities might raise. He reported that the biggest concern to municipalities was the language in the HOA that referenced legislation that would be brought forward, presumably next year, which would allow for the construction of a pipeline and facilities necessary to monetize the natural gas resources. He stated that the concern involved a reference made to a payment in lieu of taxes (PILT) and other items that might be needed in order to have a successful project. He stated that the group of municipalities recognized that there might be concessions for a project of this size and would probably support them; however, they did not know what those concessions and impacts would be. He noted that the language in the HOA said that the state would consult with the municipalities, but observed that consult was not a very strong word; the

group would rather have agreement in the process or it would rather negotiate a deal on its own behalf.

Mr. Navarre continued to speak to language in the bill and related that past negotiations between the state and the major companies had resulted in a discussion of other fiscal certainty terms such as existing oil properties. He explained that there was a concern that because tax bases for existing oil infrastructure were a big part of local government tax revenue, they should not be changed and included in the concession with respect to a natural-gas facility and pipeline. He noted that the group of mayors recognized that companies would be taking a significant risk, but that the State of Alaska was also taking a large risk. He expected that companies that came to the table would do the best they could and would bring everything to the negotiations that would benefit them; likewise, he knew that members of the legislature would look out for Alaska's interests. He noted that the group was before the committee to make sure that in the course of discussion, they were able to raise the issues that were important to local governments that would impact them. He stated that the contractual provisions regarding what the legislative role over the project would be over time had changed significantly and that it was a way to lock in fiscal certainty. He concluded that the group's goal was to identify their concerns during the process and ask that they be addressed.

[9:15:35 AM](#)

LUKE HOPKINS, MAYOR, FAIRBANKS NORTHSTAR BOROUGH, indicated that the group of mayors had been tracking SB 138 and the conditions that it allowed the administration to go forward with and negotiate. He noted that he had experience with PILT agreements and that both sides agreed to a value that went forward to the legislative bodies for approval. He and the other mayors in the group were concerned that if they sat down and negotiated, they might not be able to come to conclusion, which would be unfortunate. He stated that the group wanted amendments to the legislation that stated specifically that there needed to be consent by municipalities, the commissioner of the Department of Natural Resources, and others negotiating with the producers. He mentioned fiscal certainty and noted that Section 10 of the HOA spoke to a healthy long-term oil business, reducing valuation, and other potential disputes

between the producer parties and the state; he stated that the group of mayors wanted language added to the bill that specified that this did not affect those items in Title 29 and AS 43.56 on existing oil and gas properties. He stated that there were methodologies and sideboards regarding how impact aid was computed and that the group could speak to that as well; however, so far, the group's in-depth review of the bill brought forward the existing oil and gas infrastructure concerns, as well as how a PILT agreement was arrived at.

Co-Chair Kelly inquired what the group of mayors' level of discussion had been with the administration about the bill and their concerns. Mr. Navarre thought that both he and Mr. Hopkins had spoken with the administration and recalled speaking to Mr. Pawlowski the prior day. He thought that Mr. Pawlowski had a better understanding of what the group's concerns were and that he had stated that the Department of Revenue was able to negotiate away existing oil properties in a contract; however, what concerned the mayors was that the HOA stated that once the parties agree, they brought forward and supported legislation before the legislature. He explained that the agreeing parties could bring forward any legislation and while they may not have statutory authority currently to do some things, they would ask for it. He expounded that the concern was that if the group of mayors did not at least raise their issues now, the next year the legislature would say that they should have been before them earlier in the process or that the dynamic of the discussion and debate over the issue next year would be that it was too late to change any of the terms that had been agreed on going forward.

[9:19:59 AM](#)

Mr. Hopkins related that the group of mayors had submitted letters asking to meet with the governor, Commissioner Rodell, and Commissioner Balash. He related that he had met with Commissioner Balash and Commissioner Rodell the day before yesterday and had very good conversations with them. He noted that he spoken with the administration about the concerns in depth and that Commissioner Balash had understood their points, as well as the need to discuss them as sideboards in the legislation.

Co-Chair Kelly noted that the Memorandum of Understanding (MOU) and the HOA would be signed and would exist

regardless of the legislation and that the legislature would trigger the next step. He related that the challenge with SB 138 was that people tended to talk about so many things that were not in the bill and that huge gas-line issues were being discussed when the project was still trying to get to the pre-FEED stage. He wanted to be sure that there was a mechanism to address the concerns of the group of mayors.

Mr. Navarre stated that he had met with the governor a few weeks prior and that the governor had related that the state did want to talk to communities but that it was too early in the process for a lot of the discussion. He opined that particularly with contractual arrangements, municipalities knew that they were unlikely to be in the negotiating room and that they would not see anything until legislation was brought forward; while it may be premature for municipalities to have specific discussions, it was not premature to raise issues of concern. He thought that during the negotiations, sideboards in the legislation for the administration would be important and would be given attention. He related that the sideboards could recommend against certain types of things being written into the agreements; he thought that instructions like this would change the dynamics of the negotiations and what would come back from it. He offered that all Alaskans had a vested interest in the project and that all of the communities would be impacted because they were part of state and received a lot of support from the state.

[9:24:42 AM](#)

Co-Chair Kelly noted that Mr. Navarre had previously been co-chair of the House Finance Committee and that his opinion carried a lot of weight. He inquired if intent language would suffice to meet the goal of the group of mayors. Mr. Navarre replied that the group had proposed some amendments to the legislation that would basically state that contracts "may not change these specific items." He noted that even with the amendments, the administration could go forward with negotiations and bring anything to legislature that the HOA allowed; however it would be stated by the legislature that extra scrutiny would be put on certain issues that were brought back from negotiations.

Mr. Hopkins stated that as you looked at the bill, there were a lot of specifics regarding what would move forward;

the group's amendments represented another piece to add more specificity to the two areas of concern. He expressed concern with using intent language instead of an amendment to affect the change.

[9:26:07 AM](#)

CLAY WALKER, MAYOR, HEALY-DENALI BOROUGH (via teleconference), related that the Healy-Denali Borough supported the methodology of a PILT payment with impact funds. He looked forward to being part of the discussion and that Mr. Hopkins had brought up an important point about the meaning of negotiation relative to consultation.

Co-Chair Kelly noted that Vice-Chair Fairclough had joined the committee in progress.

Senator Olson noted that there had been amendments drafted to protect the municipalities and inquired if Mr. Walker had seen those and agreed with them. Mr. Walker responded that he had not seen the proposed amendments.

[9:27:59 AM](#)

Co-Chair Kelly inquired if the municipalities were working as a group. Mr. Navarre replied in the affirmative.

Co-Chair Kelly stated that he had asked Senator Micciche to work with the group of mayors regarding some of the language and how to proceed forward. He noted that the committee wanted to get a new CS out the following Monday and that any language that could be provided would be appreciated. He stated that from memory, he saw about four things that needed to be addressed in the bill. He thought that the concerns of the group of mayors were worthy of consideration and should to be addressed before the bill left the committee.

Vice-Chair Fairclough apologized for being late and noted that she had had a bill before the Senate State Affairs Committee. She thought that the state absolutely wanted to protect its municipalities, but also wanted to keep enough leverage for a project to actually happen. She noted that at least for her, any language for consideration would need to leave flexibility in the state's position in negotiating with the parties involved. She explained that the project involved a commercial agreement that was much different

than telling people what to do inside of a contractual obligation. She offered that the state could negotiate certain arrangements and could also not get a project depending on what was placed inside of the legislation. She was cautiously optimistic at arriving at a process that met both expectations.

Mr. Navarre thought that everyone was in agreement that a project was desired and that the HOA specifically referenced the alignment of interests between the state and the other parties to that agreement. He thought that there should really be an alignment between the state and local governments on the issues strictly because it was a significant change from the status quo. He noted that the group did not want to stop the project, but was also concerned about what was negotiated into it. He thought that everyone should be concerned if the bill was discussing rolling existing taxable oil properties into an agreement because there was already a significance reliance on those taxes at the local-government level. He noted that things could change over time and recalled the passage of SB 21 the prior year; however, drafting things into an arrangement or compromising them at the front end of a project was something that was significant. He opined that no one was in disagreement with monetizing the gas, but that it was a matter of figuring out who got what share; furthermore, the group of mayors recognized that total government take was a key component of that and that the state was impacted as much as anyone by a project like this.

[9:31:42 AM](#)

Senator Dunleavy imagined that in the process of figuring things up front, the municipalities would have come in as a group. He inquired if the group of mayors foresaw municipalities having veto power down the road and if the concerns needed to be addressed up front before the state moved on with the project. He wondered how the group envisioned language or a mechanism by which municipalities acted as one to provide alignment and certainty as opposed to having veto power down the road. Mr. Navarre did not think that municipalities should have veto power. He stated that a PILT was different than the status quo and that determining what that looked like and how things were allocated was a key part of the agreement. He noted that he had served in the legislature and that there was always

competition for any available money. He opined that if there was a PILT paid to the state, how that was allocated could change over time. He stated that all of the mayors and municipalities that had participated in the group had a little bit different interest and take on the issue. He noted that currently, the lead site for the terminus of the LNG facilities was Nikiski. He explained that if Nikiski was the terminus, his borough's communities would be significantly impacted; as a result, he wanted some relationship between where the assets were sited, where the long-term impacts were, and what a PILT would look like. He stated that impact aid during the construction of the pipeline would look significantly different; the Kenai Peninsula would be impacted, but so would Fairbanks, Anchorage, and any other community along the corridor. He noted that the project would also impact port cities that brought materials in.

Co-Chair Kelly stated that he would not support language that resulted in a veto power for municipalities and that Mr. Navarre had stated that he also did not support that. He thought that the committee needed to put something in place for the next step that guided negotiations through that "gate" and inquired if that was an accurate. Mr. Navarre replied in the affirmative.

Mr. Hopkins noted that he and Commissioner Balash had discussed whether something similar to a MAG group that in the Stranded Gas Act would be sufficient. He stated that something similar to a MAG group was possible, but that different boroughs might have different values that they would start at with the state in the negotiation of a PILT; furthermore, these pieces should be rolled in somehow to ensure a fair process.

[9:35:24 AM](#)

Co-Chair Kelly did not want to make any commitments or statements about how the bill should look, but agreed that there needed to be some consideration for the municipalities before the next step was taken. He noted for the record that his previous statements about the new CS had not been intended to mean that the group of mayors' problems would be fixed, but that he wanted to discuss and decide what to do regarding the municipalities before the CS came out.

9:35:58 AM

AT EASE

9:40:00 AM

RECONVENED

9:40:17 AM

AT EASE

9:41:18 AM

RECONVENED

9:41:28 AM

CHARLOTTE BROWER, MAYOR, NORTH SLOPE BOROUGH (via teleconference), spoke from prepared written testimony (copy on file).

Good morning Co-chairman Kelly, Co-chairman Meyer, and Senators.

My name is Charlotte Brower. I am honored to be the Mayor of the North Slope Borough, the wife of a whaling captain, and am blessed with six children and twenty-five grandchildren.

Thank you for the opportunity to speak on SB138, a bill that authorizes the State of Alaska to move forward on developing a natural gas pipeline from the North Slope to tidewater.

Today I would like to talk about some of the concerns and interests of the North Slope Borough regarding SB 138 and the Heads of Agreement, which is a separate document that outlines the guiding principles of the Alaska LNG Project. I'm also here to offer some suggestions on how those concerns could be addressed by this committee, the Legislature, the Governor, and his Administration.

Before we talk about concerns, it's important that say 'Thank You' to our Good Lord for the opportunity to be having this discussion on how to build a 40 to 50 billion-dollar project to develop our natural gas. How many other legislators or mayors would love to trade places with us right now?

The Alaska LNG Project envisions a 20 to 25 percent ownership by the State of Alaska. This requires the Legislature to evaluate complicated policy decisions and risks and costs on a level equal with decisions made by Fortune 500 companies. Please let me take a moment to acknowledge our appreciation for your efforts on behalf of our residents. You are truly deciding the future of our state, and on behalf of the North Slope Borough, I commend you. Quyanaqpak.

As Alaskans, we've learned from the past that large projects like this can set a positive course for our future. But we also know that in order to provide the maximum possible benefits, we have to be prepared for the impacts. For example, the Trans Alaska Oil Pipeline has provided billions of dollars of revenue and jobs, but we also learned lessons about demands for public services to deal with social services, job training, infrastructure, public safety, and education.

That brings me to the points that should be addressed in Senate Bill 138 and the Heads of Agreement document before this committee.

The Heads of Agreement has language in Article 9.3 that states the "Parties" intend for the project's fiscal terms to be included in project-enabling contracts. Subject to "consultation" with local governments, the Administration will establish payments in lieu of property tax (PILT), which are to be based on a unit rate per throughput basis. In other words, the payment is calculated as cents per thousand cubic feet of natural gas.

The reason for concern is that the process for "consultation" is not defined. We see that the process for enabling contracts is an "up or down" ratification vote by the Legislature after the Administration submits them to you for approval. If the local taxing authority of municipal governments is going to be modified to provide fiscal certainty, we must be part of the process.

Let me turn now to the language in Senate Bill 138.

The current language in SB138 addresses the taxing authority of local municipal governments in three different sections.

First, the Senate Resources Committee added Legislative Intent language in Section 1 that the interests of local governmental entities "must be considered in contract negotiations to protect the financial and other interests" of the local governmental entities. The addition of this language is recognized and appreciated, but it does not have the force of law, and does not go far enough.

Second, in Section 8 of the bill, the state-created subsidiary is given the legal provisions created in current law for the Alaska Gasline Development Corporation, known as "AGDC". This includes the language in Alaska Statute 31.25.260, which exempts AGDC from municipal taxes for any property owned by AGDC. In addition, this section of law further exempts taxable property for any joint venture or partnership with AGDC during construction of the pipeline.

This creates confusion because the new subsidiary for the large-diameter project is given the all the benefits provided to AGDC, but they are two completely separate and distinct projects. In the case of the Alaska LNG Project in SB138, there is a very large project that proposes to have significant state ownership. This was not the model that was envisioned when the Legislature discussed the formation of AGDC last year during the hearings on House Bill 4.

Third, the Commissioners of the Departments of Natural Resources and Revenue are provided authority to negotiate enabling contracts that must be ratified by the Legislature. Based on the language in the HOA, these enabling contracts will be used to establish a PILT system and also establish a series of impact payments during project construction.

I am here today to request your consideration for making amendments to SB138 and other changes that will protect the interests of local governments. Before discussing those amendments, I would like to provide some background.

Less than three weeks ago I was fortunate enough to offer testimony to the House Resources Committee in Juneau to support of HJR26. HJR26 is a resolution calling upon the United States Congress to pass legislation that establish a revenue sharing program from the proceeds of oil and gas development on the outer continental shelf off our shores. Earlier this week, HJR26 passed the Senate on a vote of 17 - 0. Thank you for your vote. By working together as Alaskans, we are sending a message for receiving a fair and equitable distribution of revenues that come from energy development off our shores.

It was our combined message as state and local governments that we will need resources to keep up with infrastructure requirements, expand emergency response and search and rescue capabilities, and work to maintain healthy communities and a healthy ecosystem.

When it comes to dealing with the impacts of oil and gas development, the basic discussion between offshore and onshore is not really that much different. As the local government responsible for providing basic essential services, the North Slope Borough is there to help provide for cost of schools, emergency response, health and social services, and public safety.

Like most other municipal governments, the North Slope Borough relies upon our authority to levy a property tax in order to generate the revenue to provide these public services. That is why any discussion to exempt property taxes from a project of this magnitude gives me cause for concern.

This is not the first time we've discussed the development of a natural gas pipeline and the issue of fiscal stability for the project. And I continue to believe that municipal taxes are not the issue that makes or breaks the margin on a project that could exceed \$50 billion.

On behalf of the North Slope Borough, I would like to request your consideration for the following amendments to Senate Bill 138:

The newly created subsidiary should not be provided the tax exemptions provided to AGDC for the small in-state project. In particular, the tax exemptions under AS 31.25.260 should not apply to the large-diameter project in SB138.

Let's explore ways for municipalities to participate in the project. For all the reasons that the project benefits from participation by the State of Alaska, perhaps many of the concerns of municipalities could be addressed in the same manner. For example, perhaps municipal governments could access revenues and get access to natural gas by having an ownership stake in a portion of the project.

The Governor has authority to issue Administrative Orders that could establish an advisory working group of municipal officials, Administration officials, industry participants, and others. Perhaps this approach could be explored to get conversations started to resolve some of these concerns.

No one wants to see a natural gas pipeline more than myself. I see the opportunity for my grandchildren to have good jobs, and I also want to see access to affordable energy for my grandchildren's children.

In order to get jobs and access to affordable energy, our villages will need good schools, housing, and other basic services in order to take advantage of the opportunities. And for that reason, I am here today to speak up for the ability of our municipal government to have the authority to meet those needs.

Quyanaqpak

[9:54:00 AM](#)

Mr. Hopkins stated that as the group of mayors looked at questions regarding legislation, the MOU, and the HOA, it looked at how impact aid to municipalities was determined. Additionally it had looked at where the five take-off points were, how that was decided, and if municipalities had a role in that. He noted that his community was concerned with a possible take-off point close by. He reiterated that the group's main concerns were the existing

taxation on oil properties and being able to negotiate/consent with the PILT agreements. He was clear that PILT agreements would be part of the project.

Senator Olson requested a comment on the three suggested amendments that Ms. Brower had recommended. He inquired if Mr. Hopkins was in favor of those amendments or if there were other things that he felt should be included that were not. Mr. Hopkins replied that had not yet had a chance to discuss all of the specifics of the amendments with Ms. Brower. He noted that the representatives from the Kenai Peninsula Borough, the North Slope Borough, the Fairbanks North Star Borough, and Valdez had discussed suggested amendments, but that it was a moving target. He acknowledged the concern with AS 31 and noted that Ms. Brower had spoken to specific impact pieces that did not currently have any sideboards for discussion; he looked forward to speaking Ms. Brower as soon as possible and see if other concerns could be submitted as a as a group.

[9:57:08 AM](#)

Mr. Navarre realized that municipalities would not be part of the negotiations in the HOA. He noted that often times, someone else had to negotiate on your behalf. He stated that, in general, people who were doing the negotiation know more about how the terms were arrived at and also looked out for their own interests first before they looked at the interests of people who were not in a room; this reflected the groups concern and why they were raising the issue of impacts to local governments. He thought that 90-day sessions were sometimes inadequate for complex issues and acknowledged that the legislature spent a lot of time discussing and researching the issues. He thought that when a bill was introduced the following year, the legislature would do its due-diligence and would look out for state and municipal interests. He offered that it was the mayors' responsibility to pay attention to what was going and to express their concerns going forward because the dynamic of the debate changed when there was a bill before the legislature that could result in a \$65 billion investment; at this point, the focus would be turned on pushing the project forward. He noted that most people would be in favor of moving the project forward, but that the details of what that meant long-term would only be known by a few.

Mr. Navarre noted that the people who would know about the specifics of the agreements would be legislators because it was their job and responsibility. He reported that he had delved into some of the materials that had been presented on the HOA and the legislation, but that he could not do it full time. He added that the legislature would know more about the issue, would participate in the negotiations, and would be part of discussions with the administration. He stated that while it may not be allowed in current law, a line could be added to the legislation that stated that "notwithstanding the provisions of whatever, this is what we agreed to." He observed that the group was not trying to stop the negotiations, but was trying to put sideboards on it that protected what it viewed as municipal concerns, as well as what the long-term impacts to the state were. He noted that the group was concerned about the impacts to the state long-term because municipalities also shared in revenues that went to the state as a result of the state's resources base.

Senator Bishop thanked the mayors for their testimony and thought none of the raised concerns were over the top; he thought that the mayors' concerns represented common-sense, good-question approaches to the process. He noted that the legislature had heard time and time again how big the project was and referenced Ms. Brower's comments regarding how many other legislators would like to be negotiating a \$50 billion to \$65 billion deal. He noted that the project was huge and that expert testimony had stated that it needed to be on time and on budget in order to meet the window of opportunity. He noted that the state needed to be competitive to have a deal and that part of that was in making sure that the state's municipalities were on board with the deal. He concurred with the comments of the mayors and hoped that an agreement could be reached that got everyone in sync in order to meet the on-time, on-schedule process of the project.

[10:02:47 AM](#)

Co-Chair Meyer discussed the following meeting's agenda.

SB 138 was HEARD and HELD in committee for further consideration.

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ADJOURNMENT

10:03:06 AM

The meeting was adjourned at 10:03 a.m.