

**ALASKA STATE LEGISLATURE**  
**SENATE RESOURCES STANDING COMMITTEE**

February 21, 2014  
8:02 a.m.

**MEMBERS PRESENT**

Senator Cathy Giessel, Chair  
Senator Fred Dyson, Vice Chair  
Senator Peter Micciche  
Senator Click Bishop  
Senator Lesil McGuire  
Senator Anna Fairclough  
Senator Hollis French

**MEMBERS ABSENT**

All members present

**COMMITTEE CALENDAR**

SENATE BILL NO. 138

"An Act relating to the purposes of the Alaska Gasline Development Corporation to commissioner of natural resources on the custody and disposition of gas delivered to the advance to develop a large-diameter natural gas pipeline project, including treatment state in kind; relating to the authority of the commissioner of natural resources to and liquefaction facilities; establishing the large-diameter natural gas pipeline project propose modifications to existing state oil and gas leases; making certain information fund; creating a subsidiary related to a large-diameter natural gas pipeline project, provided to the Department of Natural Resources and the Department of Revenue including treatment and liquefaction facilities; relating to the authority of the exempt from inspection as a public record; making certain tax information related to an commissioner of natural resources to negotiate contracts related to North Slope natural election to pay the oil and gas production tax in kind exempt from tax confidentiality gas projects, to enter into confidentiality agreements in support of contract negotiations provisions; relating to establishing under the oil and gas production tax a gross tax rate and implementation, and to take custody of gas delivered to the state under an election for gas after 2021; making the alternate minimum tax on oil and gas produced north of to pay the oil and gas production tax in kind; relating to the sale, exchange, or disposal 68 degrees North latitude after 2021 apply

only to oil; relating to apportionment factors of gas delivered to the state under an election to pay the oil and gas production tax in of the Alaska Net Income Tax Act; authorizing a producer's election to pay the oil and kind; relating to the duties of the commissioner of revenue to direct the disposition of gas production tax in kind for certain gas and relating to the authorization; relating to revenues received from gas delivered to the state in kind and to consult with the 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."

- 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

**WITNESS REGISTER**

LINDSAY WILLIAMS

Staff to Senator Giessel  
Alaska State Legislature  
Juneau, Alaska

**POSITION STATEMENT:** Explained the changes in the CSSB 138(), version \N.

MIKE PAWLOWSKI, Deputy Commissioner  
Department of Revenue (DOR)

**POSITION STATEMENT:** Answered questions on CSSB 138().

JOE BALASH, Commissioner-designee  
Department of Natural Resources (DNR)

**POSITION STATEMENT:** Answered questions on CSSB 138().

**ACTION NARRATIVE**

8:02:37 AM

**CHAIR CATHY GIESSEL** called the Senate Resources Standing Committee meeting to order at 8:02 a.m. Present at the call to order were Senators French, Fairclough, Dyson, Bishop, and Chair Giessel.

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

8:03:00 AM

CHAIR GIESSEL announced SB 138 to be up for consideration. She said she had a blank committee substitute (CS) that incorporates concepts that have been brought forward by individual committee members during their hearings.

8:03:38 AM

SENATOR DYSON moved to adopt CSSB 138( ), labeled 28-GS2806\N, as the working document.

CHAIR GIESSEL objected for discussion purposes.

[8:04:07 AM](#)

SENATOR MICCICHE joined the committee.

LINDSAY WILLIAMS, staff to Senator Giessel, explained the changes in the CS. The first change was in the title to be conforming and was recommended by legal drafters.

A new section 1 was added on page 3 that involves intent language that broadly captures what is in the Heads Of Agreement (HOA). Briefly, oil and gas development and commercialization of gas is of vital public interest to the State of the Alaska. It recognizes that much of the infrastructure will be within the bounds of local governments. There will be many benefits to the state including employment opportunities, tax and royalty payments, and natural gas to communities.

Item number (4) (Article 9 of the HOA) talks about negotiations and that those must be in the interests of the state and local governments. Subsection (b)(Article 7 of the HOA) speaks to the DNR commissioner and that it's necessary he be able to negotiate contracts and enter into agreements that will be subject to legislative approval.

Item number (b)(2) (Article 6 of the HOA and Article 9.3.1) talks about access and pro-expansion principles, delivery of gas to Alaskans, and payment in lieu of taxes.

[8:06:13 AM](#)

Item number (3) (Article 8.3.1 of the HOA) talks about negotiating separately with the producers for the sale or disposition of the state's natural gas and number (4) (Article 11 of the HOA) speaks of employment for Alaska residents.

[8:06:32 AM](#)

SENATOR FAIRCLOUGH pointed out a drafting error on page 3, line 19, that should be 4 and line 23 should be 5.

SENATOR DYSON wanted some discussion about the project labor agreements mentioned in (b)(4).

MS. WILLIAMS said this legislative intent language almost exactly matches the language in the HOA under Article 11.

SENATOR FAIRCLOUGH asked if that was consistent with language in AGIA.

MS. WILLIAMS said no.

[8:08:00 AM](#)

SENATOR FRENCH said while on the subject of contracts on page 3, (b) references short term commercial agreements, negotiated contracts, and proposed contracts and asked if every single one of those instruments will come before the legislature for approval. It seems that there will be many agreements in working towards a big project.

[8:09:46 AM](#)

MIKE PAWLOWSKI, Deputy Commissioner, Department of Revenue (DOR), answered that section 11 of the bill (on page 13) has a healthy balance between unnecessarily binding the flexibility that needs to occur in the negotiation of commercial agreements. At the same time there is a complete recognition that for contracts, the binding documents that will move this project forward do need to be subject to legislative review. Page 13, line 13-14, says the DNR Commissioner can enter into a commercial agreement without coming back to the legislature. However, number (11) (on page 13, lines 15-19) when it is a contract that is going to be binding, that contract is not effective unless the legislature authorizes the governor to execute it.

SENATOR DYSON asked if the language on page 4, lines 13-14, (project labor language) has the effect that no contractor, subcontractor, or supplier can be involved in this job unless they are union.

MR. PAWLOWSKI referenced language in the HOA on page 16 that says "prior to construction, the AKLNG parties (the companies that are directly engaged in the AKLNG project) commit to negotiate in good faith project labor agreements for AKLNG project." This recognizes that there is a process going forward to work on those projects and that in principal the parties are all agreed that the process and good faith will continue during the development prior to construction of the project.

[8:12:38 AM](#)

SENATOR DYSON said he still wanted to know if the effect was that no non-union contractors will be involved as suppliers.

MR. PAWLOWSKI said he didn't think that was the intent, but it was impossible to predict the outcome until in good faith the parties get into those negotiations.

SENATOR DYSON asked if that means that non-union contractors and suppliers can enter into the negotiation process.

MR. PAWLOWSKI answered that the key contemplated here is multiple agreements. This project is so large that all Alaska businesses will be involved; anything this large will demand that.

[8:14:02 AM](#)

SENATOR DYSON asked him to answer yes or no: will non-union contractors and suppliers be able to work on this project.

MR. PAWLOWSKI answered yes.

[8:14:20 AM](#)

CHAIR GIESSEL directed Senator Dyson to the totality of the words in item 4 that has broad statements like "contracts with Alaska businesses, employment of Alaska resident."

SENATOR DYSON said respectfully that is great language, but it doesn't address the point. He was not against project labor agreements; on projects like this, labor, rest, and continuity are huge factors that can easily overwhelm any savings or whatever else can happen by having a non-union contractor on the job. But on the record they have said that non-union contractors can participate and nothing precludes them.

MR. PAWLOWSKI said his perception was that nothing here precludes them, but he was not a labor lawyer.

SENATOR DYSON said if the administration had any different view, he would enjoy knowing about it.

[8:15:48 AM](#)

SENATOR MICCICHE said in a project like this many of the trades happen to be union, but in a job of this scale there is no way you could satisfy the labor requirements with in-state union folks, period. And many of the trades simply aren't union. If anyone was going to try to drive that line, they would be giving out-of-state workers priority ahead of in-state Alaskan workers.

[8:16:59 AM](#)

MS. WILLIAMS went to section 11 on page 13 that dealt with sharing confidential information with the legislature. Version A previously read: confidential information obtained under this paragraph "may" be shared with the legislature only in committees held in executive session or under a confidentiality agreement. This change removes "may" and inserts "shall".

SENATOR FRENCH asked where that language was in the A version.

MS. WILLIAMS said the original language was on page 12, line 12, and the change is on page 13, line 29.

She said section 14 on page 16 deletes the errant "and". The DNR commissioner may propose three modifications relating to switching between a royalty in kind (RIK) and royalty in value (RIV) establishing a fair market value for royalty gas and establishing a fixed royalty rate. On line 29, following "market" there used to be an "and" and that has been removed because in reality the DNR commissioner may only do two of these items, not all three. Keeping with this same change, page 17, line 18, following "market" the word "and" was also removed.

[8:19:20 AM](#)

SENATOR MCGUIRE joined the committee.

MS. WILLIAMS said another change was offered by two members that establishes that the royalty rate may not go below 12.5 percent.

CHAIR GIESSEL said Senator Micciche and Senator French authored it.

SENATOR MICCICHE explained that 12.5 percent is what guarantees our Permanent Fund Dividend contributions, an item that was missed in the first version.

SENATOR FRENCH asked to explain, now that the state is taking RIK, how a quarter of that gets deposited into the Permanent Fund.

[8:21:02 AM](#)

JOE BALASH, Commissioner-designee, Department of Natural Resources (DNR), explained that they will still have to keep track of the state's royalty interest. Even though it will be taken in kind there will be transportation and liquefaction charges that get deducted from those royalty interests. The net of that value gets evaluated for the 25 percent Constitutional deposit into the Permanent Fund. What accounting procedures will

be employed is going to be a function of the agreements that come forward next year.

SENATOR FAIRCLOUGH stated that it is not a foregone conclusion that we are taking our gas in kind; it's an option.

COMMISSIONER BALASH said that was an excellent point. The HOA contemplates that the other parties will be able to work with the DOR to satisfy their concerns on risks associated with going in kind and will help the DOR with mitigation measures to deal with those risks. Supposing that happens, the statutes direct them to start with in kind. So, whether they are talking about an in kind sale or in value accounting they will still have to keep track of what portion of the revenue stream is royalty and 25 percent of that stream will be deposited into the Permanent Fund annually.

SENATOR FRENCH said while everyone is comfortable with the 12.5 percent royalty from Prudhoe Bay, the Pt. Thomson royalties are quite a bit higher. He asked him how much wiggle room there is still left with 12.5 percent bottom line with respect to the negotiations on the Pt. Thomson leases that have much higher royalty rates.

COMMISSIONER BALASH answered that in no way shape or form are they talking about reducing those base royalty rates; they are talking about those instances where the state has a sliding scale royalty or a net profit share lease (NPSL) that has something in addition to a base royalty rate. Often those types of leases have a base royalty rate of 12.5 percent. What they will be seeking here is a way to come up with a fixed number that is fair to the state as well as the landowner for that particular provision, be it an NPSL or a sliding scale. An example would be a lease that starts at 12.5 percent and depending upon the triggers in the lease slides up to as high as 20 percent. In that particular situation, they would be seeking a number between 12.5 and 20 percent and he would argue for a number closer to 20.

With regard to the leases that are in place at Pt. Thomson that don't have an NPSL or a sliding scale, they will be unaffected. So, it will retain that higher royalty interest relative to Prudhoe Bay.

[8:26:44 AM](#)

COMMISSIONER BALASH said that would create an issue, because with royalty rates of a different percentage between those two

fields, which field comes on first and in what volume is going to affect the state's overall share of the gas. It might be in the beginning days/years of production and operation of the project that the state might be a little long or short depending on which field is coming on first. In the long run, he expected a 75/25 mix of those two fields' production, and that's where they get to a blended number something like 13 percent.

In order to make sure the state doesn't get stuck with too much or too little gas, a balancing agreement will be needed that makes sure that in the event one field or the other is producing more than that 75/25 ratio that there is an accounting for the gas and a makeup right and an opportunity, which will be important for all parties to this agreement. No one wants to be stuck with either too much capacity or too little in the pipe.

[8:27:21 AM](#)

MS. WILLIAMS moved on to section 30 on page 28, line 4 where the title previously read: "Payment in kind of tax for gas;" the title now reads: "Payment in gas of tax for gas." So, in keeping with consistency the HOA uses the term "tax as gas" or TAG. In the HOA TAG is defined in Article 1 under definitions and in Article 8.2. There were several instances under (a) and (b) in section 30 where "in kind" was removed and replaced with "gas".

[8:29:13 AM](#)

CHAIR GIESSEL summarized that they removed the expression "tax in kind."

[8:29:27 AM](#)

MS. WILLIAMS said on line 14, the last sentence previously read: "The producer shall pay the tax in kind by delivering that 10 percent of the gas to the state at the entrance of the transportation facility specified by the state." "Entrance of the transportation facility specified by the state" was removed and replaced with "point of production" (POP), which is defined in section 46 on pages 49 and 50 of the bill. This change would provide clarity to the producers as well as the state. She said the last change was on page 50 where a new section was added under section 49 amending uncodified law.

CHAIR GIESSEL said that Senator McGuire requested this.

SENATOR MCGUIRE said that this is the best opportunity that Alaskans have had for a gasline because of the alignment that exists and the point behind this provision is that she thought an element was missing. And that is the instinctive alignment

life-long Alaskans have had with the industry, because "we" were here before the TAPS, and got to see the Alaska without the benefit of that industry and then to see it with. Over 60 percent of the Alaskan public has lived here seven years or less and it struck her in going through the oil tax debates and getting gas to Alaskans that perhaps the element of alignment was missing. Alaskans need to know they are getting something out of this partnership that they have with the oil and gas industry and to start feeling it in a tangible way. Upon discussion with the DOR about Securities and Exchange Commission laws, she thought it better to ask them to come up with a plan for a way that people could buy a share of the pipeline through their Permanent Fund Dividend similar to the "Pick, Click, Give Program."

[8:34:16 AM](#)

CHAIR GIESSEL said she appreciated the broad language she put in, since buying a share of the pipeline is a complex process.

[8:34:41 AM](#)

MS. WILLIAMS said that summed up the rest of the changes in the CS.

[8:35:01 AM](#)

SENATOR DYSON said one of the major construction unions in the state is one he had been a member of and their by-laws said they cannot take any new members in from Alaska including ones that are licensed in the state as long as there is anybody on the books in Seattle or Portland. Is there any way to solve that problem?

MR. PAWLOWSKI said in all honesty that issue was outside of his comfort zone.

CHAIR GIESSEL said it's a burning question for the whole committee and she would get the Department of Law to join them this afternoon to talk about it.

SENATOR DYSON said the other union has to do with Teamsters, and Alaska has a mix of company-owned trucks and privately owned trucks; virtually all the private owners have been members of the Teamsters for a long time, but there are places in the state where that privately owned truck cannot go on the real estate and they have to spot their load and someone else comes and picks it up. It's an issue that keeps the most efficient way of delivering the freight, sometimes, from happening. He hoped that this was so much work for so many people, that those kinds of

small and arbitrary issues can go away; removing the barriers to Alaskans working.

MR. PAWLOWSKI said it may be way too early to deal with that, but in general the administration has tried to come to high level principle agreements with companies to say this is the plan of how we're going to move forward.

CHAIR GIESSEL, finding no further questions, removed her objection and said version N CS for SB 138 was now before the committee. She held the bill in committee.

8:40:21 AM

CHAIR GIESSEL adjourned the morning Senate Resources Standing Committee meeting at 8:40 a.m.