

HOUSE FINANCE COMMITTEE  
FOURTH SPECIAL SESSION  
June 3, 2016  
3:07 p.m.

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CALL TO ORDER

Co-Chair Thompson called the House Finance Committee meeting to order at 3:07 p.m.

MEMBERS PRESENT

Representative Mark Neuman, Co-Chair  
Representative Steve Thompson, Co-Chair  
Representative Dan Saddler, Vice-Chair  
Representative Bryce Edgmon  
Representative Les Gara  
Representative Lynn Gattis  
Representative David Guttenberg  
Representative Scott Kawasaki  
Representative Cathy Munoz  
Representative Lance Pruitt  
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Fred Parady, Deputy Commissioner, Department of Commerce, Community, and Economic Development; Gene Therriault, Deputy Director, Statewide Energy Policy Development, Alaska Energy Authority, Department of Commerce, Community and Economic Development; Representative Liz Vasquez; Representative Sam Kito III; Representative Lora Reinbold; Representative Mike Chenault.

PRESENT VIA TELECONFERENCE

John Springsteen, Executive Director, Alaska Industrial Development and Export Authority (AIDEA).

SUMMARY

HB 246 AIDEA: FUNDS; LOANS; PROGRAMS; DIVIDEND

HB 246 was HEARD and HELD in committee for further consideration.

Co-Chair Thompson reviewed the agenda for the meeting. He introduced the presenters. He asked members to hold questions until the end of the meeting.

Representative Guttenberg asked the presenters to point out places in which the committee substitute for the bill differed from the original version.

#hb246

HOUSE BILL NO. 246

"An Act creating the oil and gas infrastructure development program and the oil and gas infrastructure development fund in the Alaska Industrial Development and Export Authority; relating to the interest rates of the Alaska Industrial Development and Export Authority; relating to the sustainable energy transmission and supply development and Arctic infrastructure development programs of the Alaska Industrial Development and Export Authority; relating to dividends from the Alaska Industrial Development and Export Authority; and adding definitions for 'oil and gas development infrastructure' and 'proven reserves.' "

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FRED PARADY, DEPUTY COMMISSIONER, DEPARTMENT OF COMMERCE, COMMUNITY, AND ECONOMIC DEVELOPMENT, introduced himself. He relayed he would be briefly reviewing the slides in his presentation. He stated that the bill was brought forward on behalf of the 735,000 shareholders of the Alaska Industrial Development and Export Authority (AIDEA).

GENE THERRIAULT, DEPUTY DIRECTOR, STATEWIDE ENERGY POLICY DEVELOPMENT, ALASKA ENERGY AUTHORITY, DEPARTMENT OF COMMERCE, COMMUNITY AND ECONOMIC DEVELOPMENT, introduced himself.

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RECONVENED

Mr. Parady introduced the PowerPoint presentation: "AIDEA Oil and Gas Infrastructure Development Fund HB 246" (copy on file). He turned to slide 2: "Current AIDEA Financing Tools." He pointed out the AIDEA board members listed at the top of the slide, which included himself as the designee of the Department of Commerce, Community and Economic Development. He continued that Deputy Commissioner Jerry Burnett sat on the board as the designee of the commissioner of Department of Revenue (DOR). He specified that AIDEA staff reported to the board. He listed the funds on the slide: The Revolving Fund, the Sustainable Energy Transmission Supply (SETS) Fund (for energy infrastructure), and the Arctic Infrastructure Fund. He also listed two special appropriations projects to include the Interior Energy Project and the Ambler Mining District.

Mr. Parady moved to slide 3: "Geographic Project Diversity." The slide was part of the "dashboard" for monthly and quarterly review that showed where AIDEA's money was deployed. The slide showed a geographic representation via a pie chart and state map that was divided into regions. He commented that AIDEA's mission was to serve the entire state.

Mr. Parady moved to slide 4, "Industry Diversification," which showed a pie chart entitled 'Total Existing and Approved Capacity Projects and Loans as of 10/31/15.' He indicated that the slide presented the problem that AIDEA was trying to solve. He specifically pointed out the portions of the pie chart that were 'Oil and Gas' and 'Oil and Gas Support,' which represented 14 percent of AIDEA's loan portfolio. He highlighted that mining was another large component of the portfolio, and comprised 20 percent of the pie chart. The Red Dog Mine project was a stable 20 to 30 year loan. He shared AIDEA's concern that with the oil and gas sector at 14 percent, the state was in danger of over-weighting AIDEA's portfolio in the capital-intensive industry and was therefore seeking to build a new tool. He specified that the tool was represented in the next slide.

Mr. Parady advanced slide 5, "Financing Tools after HB 246." He conveyed that the new tool he had referred to was represented by the orange bar on the slide, which was a

proposal to add a fourth fund dedicated to oil and gas infrastructure.

Mr. Parady moved to slide 6: "Intent of HB 246":

Continue infrastructure financing to:

- Support small and medium sized oil and gas developers statewide
- Increase production and bring new fields online
- Attract new investment
- Increase future State oil and gas revenues
- Support investment for energy security

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Mr. Parady discussed slide 7: "Eligible Oil and Gas Infrastructure Projects":

- Oil & Gas Development Infrastructure defined as:
  - Investment: acquisition, construction or installation (including engineering)
  - Projects: road, pad, camp, processing facility, gathering system or other-site improvement or equipment
- Projects must support fields with proven reserves
- Proven Reserves defined as:
  - Analysis of geological and engineering data
  - Commercially recoverable under current economic conditions, operating methods, and government regulations
  - Can be categorized as developed or undeveloped

Mr. Parady emphasized that the fund was precluded from investing downhole.

Mr. Parady turned to slide 8: "Financing and Tax Credits":

- After opting to use AIDEA financing, projects may no longer use:
  - Exploration & Development tax credit (AS 43.20.043)
  - Production tax credit (AS 43.55.023)
  - Production tax credit for exploration expenditures (AS 43.55.025)
- Projects with past tax credits still eligible for AIDEA financing

Mr. Parady reviewed slide 9: "Market Based Interest Rates":

- AIDEA will base interest rates on:
  - Project risk
  - Borrower creditworthiness
  - Owner and financing partner commitments
  - Benefit to the State
- Interest rates may be higher for oil and gas infrastructure projects due to the inherent industry risk

Mr. Parady turned to slide 10: "Other Bill Components":

- Modifies financing limits of SETS and Arctic Infrastructure development funds
- Proposes that all 3 funds be allowed to loan up to 50 percent of an eligible project or offer a loan guarantee up to \$25,000,000
  - Amounts in excess of these limits would require prior legislative approval

Mr. Parady added that current statute dictated that the two other AIDEA funds could loan up to 33 percent of a project up to \$20 million. He expressed that the change was due to the scale oil and gas infrastructure projects and the need for consistency. He relayed that Mr. Therriault would address additional sideboards that were added to the bill in the House Resources Committee.

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Co-Chair Thompson acknowledged that Representative Reinbold was in the audience.

Mr. Therriault turned to slide 11: "Sectional Analysis." He indicated that there were two documents in the member packets, including an explanation of changes. The explanation of changes document would highlight that Sections 1 through 11 of the committee substitute either had no change or merely had stylistic drafting changes. He indicated that he would highlight different amendments that were adopted in the House Resources Committee bill version, which all applied to Section 12 of the bill. He reviewed the sectional analysis for version W:

Sections 1 through 3: Sections 1 through 3 amend the language of AS 44.88.088, to include payment of a

dividend from the proposed new oil and gas infrastructure development fund.

Sections 4 through 9: Sections 4 through 9 amend subparts of AS 44.88.159, which governs the interest rates AIDEA charges under its loan participation program and its SETS and Arctic infrastructure Development programs. These sections of the bill use many of the same interest rate provisions applicable to any loans provided through the SETS and the Arctic infrastructure program and fund. In essence, the interest rate provisions require a minimum interest rate that ensures AIDEA does not lose money on its loans, and the interest rates AIDEA uses in these programs are more or less in line with the rates commercial lenders offer. Sec. 9 adds a new section (h) to AS 44.888.159, so that the authority may by regulation establish differing interest rates, as well as for methods for setting interest rates, based on the risk of the financing and the security provided.

Section 10: Section 10 amends AS 44.88.690(a) to increase the loan limit from one-third to 50% of the capital cost of a qualified energy development and increases the limit of a loan guarantee to \$25 million under the sustainable energy transmission and supply (SETS) fund.

Section 11: Section 11 amends AS 44.88.840(a) to increase the loan limit to 50% of the capital cost of an Arctic infrastructure development and increases the limit of a loan guarantee to \$25 million under the Arctic infrastructure development fund.

Section 12: Section 12 is the heart of the bill, and it adds a new chapter to AIDEA's statutes to create the oil and gas infrastructure development program and separate fund. The new statutory provisions the bill adds do the following:

AS 44.88.850 creates the oil and gas infrastructure development program within AIDEA.

AS 44.88.860 creates the oil and gas infrastructure development fund within AIDEA separated from Authority's existing Revolving Fund. The new fund will consist of money the

legislature appropriates to it and investment returns obtained from financing activity provided by the fund. AIDEA is authorized to pledge the fund to the payment of bonds issued to finance oil and gas infrastructure development.

AS 44.88.870 authorizes AIDEA to use the money in the oil and gas infrastructure development fund to finance oil and gas infrastructure development.

AS 44.88.880 specifies AIDEA's powers and duties with respect to the oil and gas infrastructure development program and fund, and requires AIDEA to adopt regulations to implement the new program. These regulations must contain a process sufficient to confirm the existence of proven reserves sufficient to justify proposed project financing. AIDEA is also authorized to contract for legal, bond counsel, engineering, or other expertise necessary to fulfill the purpose of the program and protect the authority.

AS 44.88.890 establishes limitations on the financing AIDEA can provide through the oil and gas infrastructure development program and fund. Without getting legislative approval, AIDEA cannot make a loan through the oil and gas infrastructure development fund for more than the lesser or one-half of the capital cost of an oil and gas infrastructure project or \$100,000,000. Without prior legislative approval AIDEA may not issue a loan guarantee through the new program for more than \$25 million.

AIDEA may not utilize this new oil and gas financing program unless all participants in the proposed development agree they will not take, apply for, or accept any exploration and development tax credit under AS 43.20.043; production tax credit under AS 43.55.023 or production tax credit for exploration expenditures under AS 43.55.025.

Individual project financing under the proposed Oil and Gas Infrastructure Development Program must not exceed a loan to value ration of

seventy-five percent. Resource reserves that may be offered as part of the collateralization for a project loan must be valued conservatively.

AIDEA must be properly shielded from any potential dismantlement, removal and restoration obligations that may stem from the infrastructure development project before financing from the proposed Oil and Gas Infrastructure Development Program can be provided.

Finally, any financing under the new program must be for the expected life of the project, but not for more than 30 years.

Section 13: This section sets out the definition of the terms "oil and gas infrastructure development" and "proven reserves".

It amends AS 44.88.900 by adding a new Paragraph (20) that defines the term "oil and gas infrastructure development" to mean "the acquisition, construction, or installation of and engineering for the construction or installation of a road, pad, camp, processing facility, gathering system, or other on-site improvement or equipment for an oil or gas field, or an oil and gas field, located in the state that has been explored and for which proven reserves have been established;

In addition it amends AS 44.88.900 by adding a new Paragraph (21) that the defines "proven reserves" to mean "those quantities of petroleum which, by analysis of geological and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under current economic conditions, operating methods, and government regulations; "proven reserves" can be categorized as developed or undeveloped."

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Representative Gattis asked about what other funds would be included.

Mr. Therriault replied that there could be a variety of actions taken with the new mechanism in Section 12. He continued that it would allow for AIDEA to engage in revenue bonding to go into the fund and then loan to a project. He qualified that even if the fund was not initially capitalized, its existence was valuable.

Mr. Therriault continued to discuss Section 12. He recounted that when the legislature created the SETS Fund and the Arctic Infrastructure Fund, which were both initiatives that came from the legislature; there was a viewpoint that funds created for AIDEA had to have certain components. As AIDEA moved forward to create the new Oil and Gas Infrastructure Fund, it copied the blueprint that had been established. He referred to page 7, lines 21 through 23 of the bill, which contained the second amendment adopted by the House Resources Committee. The lines clarified that AIDEA had the same authority for the new fund that it did under the SETS Fund and the Arctic Infrastructure Fund to hire outside expertise such as legal counsel, bond counsel to ensure appropriate use of the fund. He stated that previously there had been a separate line in the bill that required approval of the attorney general in order to get bond counsel and outside legal counsel.

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Mr. Therriault directed attention to page 8 of the bill, which addressed more of Section 12 and pertained to limitations on financing. He discussed line 8, and the boundaries on financing below the need for legislative approval; and pointed out that line 10 set an upper hard dollar amount at \$100 million for AIDEA participation. If the authority wanted to go beyond the \$100 million amount, even if it was under the 50 percent participation limit; it would have to gain specific legislative approval. He confirmed that the change was a result of Amendment 3 adopted by the House Resources Committee.

Mr. Therriault moved on to page 8, line 13 of the bill. He read from the document "Explanation of Changes," (copy on file):

Sec 12: H/Res amendment #1 modified the language of Sec. 44.88.860 to restrict the ability of the AIDEA Board to move funds to the proposed Oil and Gas

Infrastructure Development fund from other AIDEA sources.

H/Res amendment #2 modified the language in Sec. 44.88.880 to clarify that AIDEA is authorized to hire outside legal, bond counsel, engineer, or other technical expertise necessary to fulfill the purpose of the program and protect the interest of the authority.

H/Res amendment #3 modified the language of Sec. 44.88.890 to include a limit of \$100,000,000 on AIDEA participation in individual oil and gas infrastructure development financing without first receiving legislative approval.

H/Res amendment #4 added specific language to Sec. 44.88.890 requiring that AIDEA be protected from any potential future dismantlement, removal and restoration obligations associated with the proposed development project before financing from the proposed oil and gas infrastructure development fund is allowed.

H/Res amendment #5 also added language to Sec. 44.88.890 requiring that financing from the proposed oil and gas infrastructure development program must not exceed a loan to value ratio of seventy-five percent. This language will require loans from the program to be over-collateralized to protect the authority against a default. The amendment also requires the calculation of value for resource reserves that may be pledged as part of the loan collateral to be computed conservatively

Sec 13: Drafting style changes only

Mr. Therriault relayed that Representative Seaton had wanted specific language added to the limitations to iterate that until AIDEA was indemnified for future responsibility, loans could not be issued.

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Mr. Therriault discussed line 24 on page 8 of the bill. He discussed specific language regarding the loan-to-value ratio that could not be exceeded in the lending. He

directed attention to line 25 on page 8, which indicated the loan-to-value ratio at no time could exceed 75 percent. The language signified that in doing the lending, there could be no security pledged for the amount being lent. If the project loan was \$75 million, AIDEA would have to exceed the amount in collateral - a conservative amount to ensure protection in the case of default.

Mr. Therriault addressed lines 27 through 29 on page 8, which discussed oil and gas reserves being used as collateral, and required the calculation of such collateral to be computed conservatively. He used the example of looking at the previous 12 months of the resource price and comparing with an estimation of the price for the next 12 months to take the lesser of the two. He commented on the specific nature of the language, which corresponded to Amendment 5 adopted by the House Resources Committee.

Mr. Therriault discussed Section 13 of the bill, where there was style changes and slight changes in the intent of the bill. He continued that the section was the definition section for oil and gas infrastructure development, which included definition of the types of projects AIDEA could use the fund to lend for. Additionally, there was a definition of 'proven reserves.'

Mr. Parady went back to the slide presentation and turned to slide 12: "AIDEA Due Diligence":

Established analysis and decision making process

- Technical due diligence
  - AIDEA sets procedure for verifying proven reserves
- Financial due diligence
  - Review developer creditworthiness and financing partner commitments
  - Analysis of economics, including oil price stress tests
- Analysis of benefit to State
  - Jobs created and petroleum revenues created
- Managed by AIDEA staff with hired consultants/specialists
- AIDEA Board makes final investment decision

Mr. Parady turned to the graph on slide 13: "Analysis & Decision-Making." The slide showed a flow chart titled 'Established analysis and decision making process.' He

highlighted the four headings on the table: Phase 1 - Suitability Assessment, Phase 2 - Feasibility Analysis, Phase 3 - Deal Structuring and Due Diligence, and Phase 4 - Finalization and Close. He continued that there was substantial detail listed below each phase for the committee's review.

Mr. Parady advanced to slide 14: "Financing Repayment":

- AIDEA financing at market-based rates to reflect individual project risk
- Loans repaid with interest
- AIDEA will earn revenue
  - Some earnings to the State as a dividend
  - Some earnings to fund future projects

Mr. Parady explained that there was a graphic at the bottom of slide 13 that showed that once the legislature established the Oil and Gas Infrastructure Development Fund, AIDEA would look to finance appropriate oil and gas projects. Further, project revenues would return revenues to repay AIDEA, and in turn AIDEA would pay a dividend to the state. He characterized the process as "a virtuous circle."

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Mr. Parady turned to slide 15: "AIDEA Entry Point & Criteria." He conveyed that the slide was a key slide to illustrate the cost of capital, correlated to the level of risk (from low to high); with the x-axis of the graph showing the range of project stages. He qualified that AIDEA tried to center its activities in the "sweet spot" in the center of the graph; where there was operating experience on behalf of the project proposers, a capital contribution from other entities that contributed to the project, a final design with plans and specifications, permitting processes were complete, and signed purchase agreements and signed sales agreements.

Mr. Parady continued discussing the graph on slide 15, noting that AIDEA's preferred role was not in venture capital, seed capital, or private equity; but rather right in the middle of getting things done. He asked the committee to consider the project experience of the state, and noted that no entity in AIDEA's line of business would

have an unblemished record, but AIDEA's overall portfolio had provided consistently strong returns to the state.

Mr. Parady furthered that AIDEA had repaid the capital that was invested by the state originally; and its loan portfolio included projects known to all the members, including the Red Dog Road, the larger ship plant in Ketchikan, the oil transfer site in Skagway, the FedEx Hangar at the Anchorage airport, and a host of smaller-scale retail businesses. He referred back to slide 4; and the pie chart which illustrated industry diversification through projects in restaurants, recreation, tourism, vessels, warehouses, offices, wastewater plants, healthcare, fuel distribution, and car washes. He asserted that AIDEA was supporting a niche in the Alaska economy in helping to provide liquidity and enable people to generate jobs and economic activity across the state.

Mr. Parady scrolled to slide 16: "Summary":

- Provides AIDEA a specific program to finance oil and gas infrastructure
- Eligible oil and gas infrastructure must have proven reserves and undergo established due diligence review
- Finance terms will be market based

Mr. Parady reviewed slide 17: "Implementation Cost":

- Implementing the program will involve minor modification of regulations, which will be carried out in-house
- Program implement cost will be absorbed
- Program management cost will be absorbed
- Modified fiscal note submitted to acknowledge potential fund capitalization

Mr. Parady believed that there was a zero fiscal note because the appropriations bill had already moved past the point where it might have been possible to add capital to the project. He recognized that it was always unlikely for the project to receive capital due to the current challenging fiscal climate. He continued that AIDEA still believed that the financing structure of the proposed program would add another element to AIDEA's toolkit and enable it to better support small and medium-sized operators across the state.

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Co-Chair Thompson referred to Amendment 4, which pertained to reclamation and dismantling that AIDEA would not be responsible for. He wondered about any eventualities in which AIDEA would have to take on responsibilities of dismantling and reclamation.

Mr. Therriault believed the bill language would require that AIDEA would be indemnified from any of the responsibility, even in the case of a default.

Co-Chair Thompson asked if there was a possibility of state liability in the event of loan default.

Mr. Parady believed that the indemnification to protect the state would still be in place and was separate from the project title and default.

Co-Chair Thompson asked who would dismantle and reclaim if the company in question was in default.

Mr. Parady understood that responsibility would fall to either the insurance carrier or the indemnification mechanism that was created to secure AIDEA from the liability.

Co-Chair Thompson asked if the AIDEA process would require insurance to cover the possibility of default.

Mr. Parady responded in the affirmative, and deferred further comment to the executive director of AIDEA.

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JOHN SPRINGSTEEN, EXECUTIVE DIRECTOR, ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY (AIDEA), responded that the mechanisms were as previously stated, to include insurance or some form of bonding mechanism to make sure than any dismantlement or remediation was taken care of at the time contracts were drawn.

Co-Chair Thompson felt reassured by the information.

Vice-Chair Saddler asked if any other states offered the oil and gas industry the same kind of public loan opportunity that AIDEA was proposing.

Mr. Springsteen was unsure if other states offered a similar type of loan program. He knew there were tax credits offered in other states, as well as a continual effort to find other financing mechanisms to work alongside with industry. He furthered that there were other jurisdictions around the world that made direct investments in oil and gas development, and went further towards equity and ownership positions with state-owned oil companies. He qualified that in contrast, the bill had a narrow focus on top-side infrastructure to support oil and gas development.

Vice-Chair Saddler asked if Mr. Springsteen had indicated that other states did not engage in such loans, but did take equity positions in oil and gas projects.

Mr. Springsteen responded that the model he was referring to was regarding foreign-owned oil companies, rather than an individual state model. He continued that Alaska was unique in its ownership of below-ground assets. He compared the state to being more like a foreign nation that worked with oil companies rather than a state with federal land managed through mechanisms of the federal government.

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Vice-Chair Saddler asked if Mr. Springsteen knew of other states that offered such loans, or took equity positions in oil and gas projects.

Mr. Springsteen answered in the negative, and offered to contact Vice-Chair Saddler at a later time to confirm his answer.

Vice-Chair Saddler referred to page 7, Line 10 of the bill; and asked if the other loan programs administered by AIDEA also had separate authority to hire separate bond counsel. He thought it might be something that could be operated as centralized function within AIDEA.

Mr. Springsteen replied that AIDEA utilized the Assistant Attorney General Jerry Juday, who was key to ongoing operations. He continued that AIDEA worked in coordination with other parties.

Vice-Chair Saddler reiterated his question to ask if all AIDEA lending programs had the same authority for bond counsel.

Mr. Springsteen responded affirmatively.

Vice-Chair Saddler asked why there was separate authority for each program rather than a centralized function.

Mr. Springsteen explained that AIDEA had worked with the administration on provisions in the bill.

Vice-Chair Saddler reiterated his question as to why AIDEA had separate authority for each program.

Mr. Springsteen stated that the bill moving forward was in coordination with the administration.

Mr. Therriault responded that the separate authority was due to how the statutes were constructed; and each time a new tool was given to AIDEA, rather than have the legislature put together a centralized authority for hiring outside counsel, it was mentioned specifically in each one of the tools.

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Vice-Chair Saddler referred to the first two items in Section 12 of the bill, and the discussion of changing the loan limit from 30 percent to 50 percent. He wondered about the original justification for a 30 percent cap on AIDEA's loan participation, as well as the reason for raising the cap to 50 percent.

Mr. Therriault referred to Sections 10 and 11 of the bill, which made reference to the SETS Fund and the Arctic Infrastructure Fund. He relayed that the legislature had chosen to set the limits at one-third participation as well as a \$20 million loan guarantee. In creation of the new fund being proposed in the bill, AIDEA recognized the cost of infrastructure, and asked for a higher limit of up to 50 percent or a \$25 million loan guarantee. He noted that funding beyond the amounts stipulated in the bill would require specific legislative approval.

Mr. Therriault continued, and relayed that AIDEA thought that rather than having different limits for the three

different programs, it would be beneficial; however it was a separate policy call as to whether to include Section 10 and Section 11, which adjust the other funds up to the same level that was being proposed for the new fund.

Vice-Chair Saddler asked if the proposed higher limit would lead to an increase in the number of loans AIDEA was able to offer.

Mr. Therriault responded that the increased participation level was beneficial for AIDEA's clientele if the loan programs had consistency. Additionally, the possibility of a higher loan amount gave the opportunity of considering more projects. He acknowledged that if a project was above a certain amount, AIDEA was able to request legislative approval, however there was a certain amount of uncertainty inherent in such a request. He added that a prospective borrower might find pursuing a legislative request to be onerous.

Co-Chair Thompson noted that Representative Kito was in attendance.

Representative Guttenberg asked how interest rates for AIDEA projects were established in the competitive market.

Mr. Parady deferred to Mr. Springsteen.

Mr. Springsteen relayed that AIDEA looked at market rates, and rates were available to the borrower based on third-party funding. When AIDEA made adjustments to the rate, it considered the benefit provided to Alaskans; which could include the provision of jobs, incremental taxes and royalty revenue, or other potential social benefits provided to Alaska shareholders. The basis was a market rate, with consideration given for the developer and the things it did for the state.

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Representative Gattis thanked Mr. Therriault for coming to her office to answer some of her questions. She recounted her question pertaining to how to avoid a boondoggle. She had heard Mr. Parady suggest that the final decision on projects rested with the board, and wondered if there was a statute in place in order to prevent such an occurrence. She mentioned a "fish church" as an example.

Co-Chair Thompson understood that the only projects that had failed had been projects forced upon AIDEA by the legislature.

Mr. Therriault expressed appreciation for the frank conversation with Representative Gattis the previous day. He recounted that AIDEA had been initially capitalized with about \$330 million; and had since paid all the money back, plus another \$50 million. He acknowledged that AIDEA had a couple of stumbles over its life, but by in large the authority was very solid. He continued that the state reported data on lending institutions, including AIDEA. The data from one year previously had reported that AIDEA had a default rate of .47 percent. Since that time, based on a 12-month rolling average, AIDEA's delinquency rate had gone down to .34 percent. He added that the all-Alaska banking delinquency rate at the time was almost twice that of AIDEA at .78 percent.

Mr. Therriault referred to slide 13, which reflected a due diligence process discussed earlier by Mr. Parady. He informed that the previous executive director had helped to strengthen the due diligence process of AIDEA by learning from mistakes as well as how to ensure that any lending was to an entity with a solid business plan that was financially able to pay back a loan. Additionally there were sideboards added by the House Resources Committee; which informed the authority that they had to over-collateralize loans if they were going to use reserves as part of collateral. He thought using conservative calculations would help to protect AIDEA and make sure that its overall track record remained positive.

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Representative Gattis thanked Mr. Therriault for his remarks and commented on the work of the AIDEA board.

Representative Kawasaki asked for clarification about the AIDEA projects initiated by the legislature. He mentioned a municipal project in Valdez that was often attributed to AIDEA.

Mr. Therriault confirmed that there had been no AIDEA participation in the grain terminals project in Valdez. He

added that he had been in office when there was quite a bit of legislative involvement in a project.

Representative Kawasaki referred to slide 4, with a pie chart showing that the largest amount of AIDEA projects were in the mining sector. He referred to a comment about the mining industry having risk, and wondered if the project area was mainly comprised of the Red Dog Mine.

Mr. Parady confirmed that AIDEA had invested in the Red Dog Mine, which was providing a stable source of income.

Representative Kawasaki asked if the concept of bringing out an oil and gas fund separately was based on the oil and gas industry being considered to be volatile. He wondered if the industry was always volatile, or if the state of oil and gas prices had become especially changeable.

Mr. Therriault recognized that there had been volatility in the oil and gas industry, and asserted that the type of lending involved in oil and gas projects had a different risk-reward profile. He shared that AIDEA expected to charge a higher interest rate; and as the project category grew in scope, it would start to impact the overall blended rate of AIDEA's overall portfolio. He relayed that AIDEA's financial advisors had shared the concern with the board, and if it continued to be approached by that type of lending, it would start to impact what could be done out of the whole blended portfolio.

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Representative Kawasaki referred to the part of the bill pertaining to the powers and duties of the new fund on page 7, Section 44.88.880. He referenced language stating that the authority shall adopt some regulations dealing with the confirmation of proven reserves; and on page 8, language referring to fiscal controls and accounting procedures for the infrastructure. He asked Mr. Therriault to explain exactly what AIDEA would be prescribed to do as a result of the bill language.

Mr. Parady deferred to Mr. Springsteen.

Mr. Springsteen asked Representative Kawasaki to repeat his question.

Representative Kawasaki reiterated his question referring to the new part of the bill pertaining to oil and gas infrastructure development, including the fund itself and the powers and duties. The section in question mentioned confirmation of the existence of proven reserves, and sufficient proposed project financing. He thought it looked as though (under the bill) the authority would have to confirm the proven reserves and prove that project was viable.

Mr. Springsteen stated that in addition to internal due diligence processes, regulation that further defined the approach used as AIDEA examined project developers was up for discussion. He stated that with the current recommended sideboards, there was a maximum of 50 percent participation or \$100 million (the lesser of the two), so it was necessary to ensure that a project partner could provide a capital contribution that was equal to or greater than what AIDEA put forth. He addressed the discussion pertaining to proven reserves, which was in aid of over-collateralizing AIDEA's loan to a project developer. He furthered that that there was some definition that existed in statute, but it would be further addressed in regulation and in AIDEA's due-diligence process.

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Representative Wilson referred to slide 8, which stated that after opting to use AIDEA financing, projects may no longer use tax credits for exploration and development or production tax credits. She wanted to better understand the reasoning behind the language, considering that the tax credits were earned.

Mr. Parady answered that given the existence of the tax credits, and the ongoing discussion regarding the topic, AIDEA was trying to create a new loan tool and not further extend the state's exposure in the construction of the tax credits. He relayed that DOR Deputy Commissioner Jerry Burnett was present and available to provide additional information.

Representative Wilson maintained that she understood the liability aspect of the matter. She asked what kind of companies might participate in the proposed loan program if AIDEA was considering higher interest rates and not allowing tax credits. She thought a regular bank might be

more attractive to businesses, which could utilize the tax credits as collateral.

Mr. Parady referred to ongoing debate pertaining to oil and gas tax credits in the state.

Co-Chair Thompson referred to prior testimony on another bill, and reported that some companies had borrowed money to do project work, expecting tax credits to pay for what had been borrowed. He asserted that if AIDEA used market interest rates, the amount would be much lower than businesses would receive in the marketplace, considering the uncertainty of tax credit payments.

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Representative Wilson understood that companies were able to take tax credit certificates to the bank, and the interest rate would be dropped and the company could borrow less money. She was trying to figure out why the state was considering tying itself to a loan program to help small and medium sized oil companies, and tying tax credits to the program. She understood the state had a liability, but did not understand why the new program would be advantageous for companies.

Mr. Parady restated that no one was making anyone do anything. He asked Mr. Springsteen to further amplify his comment.

Mr. Springsteen confirmed that it would be the choice of the applicant to utilize the proposed loan program. He stated that AIDEA used "market-based rates" versus market rates; whereby the authority started with an "arm's length" rate that a developer could get by going out for financing in the market. Additionally, AIDEA would perform another layer of analysis and to identify potential benefits to Alaskans such as job creation, royalty, and tax revenue. He confirmed that AIDEA could make adjustments to the interest rate after starting with a market rate and considering the additional benefits provided to Alaskans.

Mr. Therriault referred to page 8, lines 19 to 21 of the bill, which clarified that an oil and gas company was able to apply for tax credits in order to look for or delineate a resource. A company could go to AIDEA for financing for surface infrastructure to produce a resource, but would not

be able to utilize tax credits after engaging in financing with AIDEA.

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Representative Wilson thought it seemed that the proposed program was tied to the tax credit program. She asked if it was the belief of AIDEA that smaller and medium size companies would have more difficulty going to the private sector for financing because tax credits were not being paid as quickly.

Mr. Parady responded that the origination of the bill idea was born in the overweighting of the oil and gas sector in AIDEA's revolving loan portfolio. He expressed that to the degree it was possible, he wanted to stay disentangled from the subject of oil and gas tax credits. He emphasized that AIDEA was focused on creating a tool that would support small and medium size companies. He stated that AIDEA had a strong balance sheet and a very positive and strong credit rating; and had access to liquidity that was useful in a range of applications, including the oil and gas sector.

Co-Chair Thompson acknowledged Speaker Chenault in the audience.

Representative Wilson pointed out that oil and gas tax credits were mentioned in the bill. She referred to concerns outlined in a letter from the Alaska Oil and Gas Association (AOGA), as well as a concern outlined in a letter from the governor. She did not understand the portion of the letter referring to AIDEA being given the authority to take a lien or security interest in real or personal property, with respect to an oil or gas infrastructure development. She wanted to ensure that in no way the bill would be a way to get out of the state's tax credit liability, and now owning oil fields.

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Co-Chair Neuman asked if the state would be competing against banks that would otherwise be making loans to the same companies.

Mr. Therriault believed that AIDEA had a good relationship with banking institutions, particularly with in-state banks. He explained that with the type of infrastructure

being considered, the dollar amounts were high; and quite often AIDEA would partner with a bank or offer a loan guarantee for lending by an in-state bank. He continued that the banking institutions in the state (and the bankers association) watched AIDEA and were vocal if it considered that AIDEA had "stepped across the line" by being beyond partnering with the banks or picking up in a niche area where the banks were not able to operate.

Co-Chair Neuman relayed that he would have his office check with the banking association on the matter. He wanted to ensure AIDEA was not competing with private industry. He stated that many times AIDEA was able to assist projects in instances where banks would not.

Vice-Chair Saddler referred to lines 5 and 7 on page 6 of the bill; and noted that the bill raised the loan participation rate from one-third to 50 percent. He noted that line 7 discussed a loan guarantee on a hard dollar amount, which would be raised from \$20 million to \$25 million. He wondered if there was a hard dollar limit on the amount of a loan that could be made under sub-paragraph 1, line 5.

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Mr. Springsteen asked if Vice-Chair Saddler was referring to the SETS and Arctic Infrastructure programs, or to the Oil and Gas Infrastructure loan program.

Vice-Chair Saddler clarified that he was referring to the SETS Fund.

Mr. Springsteen stated that currently the limit on loan participation would be a percentage-based limit or guarantee cap of \$25 million.

Vice-Chair Saddler stated that there was one reference in the bill to 50 percent of a loan, and \$25 million of a loan guarantee. He asked for an explanation of the difference between a loan and a loan guarantee.

Mr. Springsteen explained that an AIDEA loan signified when AIDEA was making a direct investment in a venture; versus an AIDEA loan guarantee, where another lender provided funds to a project, and the loan guarantee was provided as

a backstop to the loan. He continued that AIDEA's role in the loan guarantee scenario would be a last resort.

Vice-Chair Saddler asked if there was a reason why there was not a hard dollar limitation in the loan amount, nor a percentage limitation on a loan guarantee amount.

Mr. Therriault responded that the amounts were set in statute by the legislature.

Representative Gara mused about why AIDEA was not also funding exploration for oil and gas, and surmised that exploration was not a lucrative venture.

Mr. Therriault stipulated that AIDEA felt comfortable loaning for only the infrastructure for prudent reserves rather than "wild catting."

Representative Gara understood why AIDEA would want there to be prudent reserves before assisting with development of said reserves. He was trying to find portions of the bill pertaining to loan and financing being limited to proven reserves. He asked if page 7, line 29 of the bill had language about the limitation.

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Mr. Therriault observed that there was language stipulating AIDEA had to show proven reserves to justify financing, but could not find the specific reference that Representative Gara was asking for.

Representative Gara wanted to ensure the bill contained the limitation if it was intended to do so.

Mr. Therriault specified that the information was in the definition section of the bill on page 9, line 6. He continued that the language included a list of things the financing tool could be used for; including roads, pads, processing facilities, "for which reserves have been proven."

Representative Gara asked if the language limited the development fund, and meant the development fund applied to places where proven reserves had been established.

Mr. Therriault answered in the affirmative, and continued that the authority was supposed to put together a process to guarantee that the information was correct and the reserves did exist.

Representative Gara recalled that the state used to have an agency that helped to finance start-up businesses. The agency had been eliminated, and he wondered if it had been the entity that had financed the aforementioned "fish church."

Mr. Therriault did not recall.

Representative Gara recalled that the fish church had not been an AIDEA project.

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Vice-Chair Saddler observed that the same percentage limitations existed on loan guarantees and the same dollar amount limits existed on AIDEA loans for both the SETS Fund and the Arctic Infrastructure Fund as well as for the proposed Oil and Gas Infrastructure Fund. He wondered if it would help or hinder AIDEA if there were hard dollar limits to direct AIDEA loans, and percentage-based limits on AIDEA loan guarantees.

Mr. Therriault responded that the authority of AIDEA was comfortable with the existing structure in the SETS Fund and Arctic Infrastructure Fund, and the authority had interacted with the legislature at the time the limits were being set. He stated that adjustments were being proposed that would bring the two fund limits to match the fund limits for the proposed fund. In addition, the House Resource Committee was concerned enough about oil and gas lending that it had put in a hard dollar amount limit of \$100 million. He iterated that there was a 50 percent or \$100 million limitation on the proposed fund.

Vice-Chair Saddler asked if the same hard dollar limit should be imposed on the participation in loan guarantees for the SETS Fund and the Arctic Infrastructure Fund.

Mr. Therriault responded that AIDEA was more comfortable without the limits being added.

Vice-Chair Saddler asked if he was correct interpreting that there were no limits on loan guarantees (by dollar or percentage of participation).

Mr. Therriault stated that more flexibility for the AIDEA board was preferred, and confirmed that there were no hard dollar amount limits for loan participation; but in the SETS Fund and the Arctic Infrastructure Fund, the existing statutory limit for loan guarantees was \$20 million, and AIDEA was suggesting the limit be adjusted up to \$25 million.

Vice-Chair Saddler asked if there was a risk for the limit to increase without the legislature being able to constrain the percentage of a hard dollar limit, depending up on if it were a guarantee or a loan.

Mr. Therriault relayed that in the two existing funds, the limit was set by percentage, and AIDEA was suggesting the limits be raised to 50 percent. If the authority wanted to go beyond 50 percent, it would have to come back for specific legislative approval.

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Co-Chair Neuman remarked that AIDEA was involved in Cook Inlet Gas and gas in the Interior. He wondered if a company could take part in the proposed program in order to build a gas pipeline from Cook Inlet to Fairbanks.

Mr. Therriault referred to page 9 of the bill which defined the kind of construction:

(20) "oil and gas infrastructure development" means the acquisition, construction, or installation of and engineering for the construction or installation of a road, pad, camp, processing facility, gathering system, or other on-site improvement or equipment for an oil or gas field located in the state that has been explored and for which proven reserves have been established;

Mr. Therriault clarified that "on-site" meant where the resource was being produced. If a company were to come with

the desire to build a gas pipeline to transmit gas from the Cook Inlet to Fairbanks, he did not think the activity would fit the statutory definition. He continued that the project might fit the SETS Fund definition, however, the existing SETS definition had a preclusion that it was not possible to build a pipeline from the North Slope or Cook Inlet to deliver gas to market. He added that in the House Resources Committee there had been a suggestion about a similar limitation being put in the bill. Although it was not anticipated that the Darwin Mine project would look to AIDEA for financing, if it did so with the intention to build a pipeline to deliver gas from Cook Inlet, the SETS Fund would be a better fit yet had a preclusion.

Co-Chair Neuman asked if a company could take part in the proposed program in order to build the infrastructure for a gas pipeline from Cook Inlet to Fairbanks, while a business partner built the pipeline itself. He wanted to ensure that the state was not involved in competing pipelines, and asked about possible sideboards.

Mr. Parady stated that the AIDEA board had a clear understanding of the sideboards as established. He noted that the SETS Fund stipulated no pipeline, and the proposed Oil and Gas Infrastructure Fund had confining language within the definition section. He viewed the language as too narrow to be able to get to a pipeline. He stated that if there was a wish to strengthen the language, it was in the purview of the committee.

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Co-Chair Neuman suggested that maybe the legislature should look to try and make sure there were more opportunities to make such a project happen. He didn't see anything wrong with the state doing components of a project such as he had suggested.

Mr. Therriault stated that in the Houses Resources Committee there had been 6 proposed amendments, the sixth of which contained language proposed by the Speaker of the House. The amendment had been withdrawn, but proposed a similar limitation or exclusion so AIDEA did not somehow have an entity that was building a pipeline across the state. He relayed that there was enough concern that the Speaker withdrew the amendment with the intent of mulling the subject over further.

Mr. Therriault continued, and stated that with reference to Cook Inlet, because of the existing ENSTAR system there could be a scenario in which a company could develop proven reserves of an oil and gas field on some acreage, and it could be a mile to the ENSTAR system. Reaching out under the AIDEA funding to get to the ENSTAR system would be considered taking the resource to market. He did not think that the state wanted to preclude production on-site, with a very short distance to get to the pipeline system. He reiterated that just a proposal to get gas from point A to point B would fit within the statutory description. He added that the hypothetical proposal may have fit under the SETS Fund, but there was a specific exclusion. He suggested that the committee might want to revisit the topic.

Co-Chair Neuman asked about Mr. Therriault's comments about getting gas to market. He wondered if Mr. Therriault had been referring to markets within Alaska, markets within America, or global markets.

Mr. Therriault responded that the existing statute just said "to market."

Co-Chair Neuman wondered if Mr. Therriault took the words to mean global markets.

Mr. Therriault thought that perhaps at the time the language was added, the legislature was considering it to be global markets. He noted that there had been a lot of debate about a pipeline at the time, to get Alaska's gas to an overseas market. He thought it would be necessary to examine the legislative record to determine exactly what was intended by the phrase "to market."

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Representative Edgmon pointed to page 8 of the bill. He thought the definitions for 'oil and gas infrastructure,' and 'proven reserves' were straightforward. He addressed the 'loan-to-value' description beginning on line 24 on page 8:

(d) The authority may not provide financing under AS 44.88.880 if the loan-to-value ratio at the time of financing exceeds 75 percent; the value of proven

reserves that are included in the value must be calculated using the lesser of

Representative Edgmon wondered if further sideboards were necessary given the fluctuation and volatility in current economic conditions and government relations. He mused that at the time of financing, the loan-to-value ratio might be under 75 percent; but at a future time, the loan-to-value ratio could become skewed and become higher than 75 percent.

Mr. Parady noted that the bill dictated that 'the value of proven reserves that were included in the value must be calculated.' As the AIDEA board assessed the loan-to-value ratio, it would examine the nature of the overall package of what was being valued in the loan-to-value ratio. The assessment would include what the collateralization was, and proven reserves were but one part. He thought that if the board was looking at a loan that relied entirely on the value of proven reserves, it would be greeted with a great deal of skepticism.

Mr. Springsteen echoed Mr. Parady's comments, and stated that the oil and gas reserves were but one part of the collateral package in addition to all of the other parts of the top-side infrastructure that was put in place and that would hopefully also enable further development of resources in the state. He furthered that the board looked to be over-collateralized in the interest 735,000 Alaskan shareholders.

Representative Edgmon referred to slide 2 of the presentation, and commented on the risk profile of the other four funds. He thought it was intuitive that AIDEA was proposing to add an additional fund with a higher risk profile. He referred back to his question regarding additional sideboards for the loan-to-value ratio, and asked for a confirmation of the board's position on the matter.

Mr. Parady stated that the board had reviewed the issue, and thought the most conservative element of the bill was the loan-to-value ratio of 75 percent. After such a conservative assumption was made, further conservative assumptions about reserves were in the chain of collateralization. When considering reserves, the amount would be reduced by 10 percent from what was proven; and

then the lower of two pricing time frames was considered. He commented on the imperfection of assessing risk. He believed that the board was confident that the sideboards were sufficiently conservative. He commented that AIDEA had 14 percent of its revolving loans invested in the oil and gas sector, and the loans were performing well. He commented on the well-established staff structure for assessing risk.

Co-Chair Neuman referred to Representative Edgmon's previous question, and asked if mines were evaluated by the same measure of 75 percent of known reserves.

Mr. Parady stated that mining reserves were typically evaluated differently, and were tied to the Toronto stock exchange and the standard that Canada had established for how reserves were quantified and evaluated.

Co-Chair Neuman had wondered if there were similar mechanisms for evaluating mines.

Representative Edgmon referred to line 8 on page 8 of the bill:

(A) 50 percent of the capital cost of an oil and gas infrastructure development; or

Representative Edgmon asked if the language was referring to the entire capital cost or a portion.

Mr. Therriault believed the language was referring to the portion of the capital cost the project was bringing for financing. If a project was self-financing or had separate financing for another component of the development, the language applied to the component that AIDEA was being asked to participate in.

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Representative Edgmon asked if capital costs were defined in AIDEA regulations or in statute.

Mr. Springsteen stated that it was addressed in regulation.

Vice-Chair Saddler was concerned with some of the definitions. He asked if the limit would be 50 percent of the capital cost that was being financed, rather than the

total cost with what a project was self-financing. He asked if capital costs were defined sufficiently in regulations.

Mr. Springsteen responded in the affirmative.

Representative Wilson asked if AIDEA still be coming forward with the bill if the state was able to pay all of its tax credits as soon as they were turned in.

Mr. Therriault answered in the affirmative, because the portion of AIDEA's existing loan portfolio had grown too large. If AIDEA wanted to continue to loan on oil and gas infrastructure activity, it needed a separate tool that could accommodate the risk profile and the interest charged for the specific type of lending.

Representative Wilson asked how important it was to leave the tax credit language in the bill.

Mr. Therriault responded that the language was a policy call on the part of the legislature.

Vice-Chair Saddler emphasized that oil and gas exploration credits were not intrinsically bad, but might create a temporary cash flow problem for the state. He stated that the record showed that the tax credits were very productive. He thought the idea that the loan would supplant the need for tax credits was a policy call, but suggested that the bill was presented to the committee with the limitation that deprived the legislature of a policy call. If an entity took a loan for oil and gas development under the program, it would deprive itself of the opportunity to take advantage of the credits. He did not know if the tax credit language was necessary, and thought it might be counter-productive.

Mr. Parady referred to Page 8, starting on line 19:

(2) after the date of the authority's financing commitment, the participants will not take, apply for, or accept a tax credit for expenditures on the oil and gas field under AS 43.20.043, AS 43.55.023, or 43.55.025.

Mr. Parady noted that tax credits were available to companies prior to the date specified in the bill, and it

was the company's choice as to whether to move forward with AIDEA financing or not.

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Representative Edgmon read page 7, line 13 to 15:

(1) use the oil and gas infrastructure development fund (AS 44.88.860) to finance oil and gas infrastructure development, guarantee loans or bonds for oil and gas infrastructure development, and establish reserves;

Representative Edgmon asked about the definition of 'and established reserves' in the bill section.

Mr. Therriault stated that the bill section pertained to the operation of the loan mechanism itself, and referred to financial reserves. He reported that the Legislative Legal Department had advised that the language was similar to that which appeared in the language for the SETS Fund and the Arctic Fund.

Co-Chair Thompson thanked the presenters.

HB 246 was HEARD and HELD in committee for further consideration.

Co-Chair Thompson reviewed the agenda for the meeting on Saturday, June 4, 2016 at 3:00 p.m., at which time public testimony would be heard.

Co-Chair Thompson recessed the meeting to a call of the chair [Note: the meeting never reconvened].

#

ADJOURNMENT

[4:38:12 PM](#)

The meeting was adjourned at 4:38 p.m.