

HOUSE FINANCE COMMITTEE
May 11, 2019
9:00 a.m.

9:00:21 AM

CALL TO ORDER

Co-Chair Wilson called the House Finance Committee meeting to order at 9:00 a.m.

MEMBERS PRESENT

Representative Neal Foster, Co-Chair
Representative Tammie Wilson, Co-Chair
Representative Jennifer Johnston, Vice-Chair
Representative Dan Ortiz, Vice-Chair
Representative Ben Carpenter
Representative Andy Josephson
Representative Gary Knopp
Representative Bart LeBon
Representative Colleen Sullivan-Leonard
Representative Cathy Tilton

MEMBERS ABSENT

Representative Kelly Merrick

ALSO PRESENT

Representative Jennifer Johnston, Sponsor; Angela Rodell, Executive Director, Alaska Permanent Fund Corporation; Lynn Gattis, Staff, Representative Tammie Wilson; Maridon Boario, Staff, Senator Lyman Hoffman; Heidi Teshner, Administrative Services Director, Department of Education and Early Development, Office of Management and Budget; Christine O'Conner, Executive Director, Alaska Telecom Association; Patience Frederickson, Director, Alaska Division of Libraries, Archives, and Museums, Department of Education and Early Development.

PRESENT VIA TELECONFERENCE

Mike Coons, Association of Mature American Citizens (AMAC), Palmer; Herman Morgan, Self, Aniak; Dan Britton, Interior Gas Utility, Fairbanks.

SUMMARY

HB 87 LIQUEFIED NATURAL GAS STORAGE TAX CREDIT

CASHB 87(FIN) was REPORTED out of committee with four "do pass" recommendations and six "no recommendation" recommendations and with one new indeterminate fiscal note from the Department of Revenue.

HB 139 AK PERM. FUND CORP. PROCUREMENT EXEMPTION

HB 139 was HEARD and HELD in committee for further consideration.

CSSB 74 (FIN)

INTERNET FOR SCHOOLS

CSSB 74 (FIN) was HEARD and HELD in committee for further consideration.

#hb139

HOUSE BILL NO. 139

"An Act providing an exemption from the state procurement code for the acquisition of investment-related services for assets managed by the Board of Trustees of the Alaska Permanent Fund Corporation."

9:00:52 AM

REPRESENTATIVE JENNIFER JOHNSTON, SPONSOR, read from a prepared statement to introduce the bill:

Thank you for your willingness to consider House Bill 139 this morning. House Bill 139 grants an additional exemption to the state's procurement code to the Alaska Permanent Fund Corporation (APFC) for the purposes of evaluating and managing investments. The types of investments this exemption would apply to are often very profitable for our state. Under existing law, the corporation exempt from the states procurement code when it requires income producing assets or delegates its investment authority. However, they must comply with the state's procurement code when evaluating and managing the assets in which they invest. The change proposed in this bill would allow a

timeline that better aligns with the pace of the market in which APFC works and would result in a more streamlined process.

9:02:15 AM

Representative Sullivan-Leonard asked for an example of why changing statute would be important for the Alaska Permanent Fund Corporation (APFC). Vice-Chair Johnston answered that the corporation was involved in private equity investments. She indicated that without the exemption, the cost of evaluating private equity was paid to an investment manager that may charge more than the state would thorough contracts with internal expertise.

ANGELA RODELL, EXECUTIVE DIRECTOR, ALASKA PERMANENT FUND CORPORATION, agreed that there were numerous private investments made by APFC that required subject matter expertise or going through the procurement process to directly invest. Currently, the corporation hired outside managers to swiftly move the transaction forward. The bill would streamline the process and reduce the costs that was necessary to act on the types of investments. Representative Sullivan-Leonard asked for verification that there was a time element involved and by sidestepping the procurement process the investments were quickly secured. Ms. Rodell affirmed the statement.

Vice-Chair Ortiz asked how long APFC had been without the exemption. He wondered if there was any downside to making the adjustment. Ms. Rodell answered that they had begun private equity investments in the 2008 to 2009 timeframe and was a more recent development. Vice-Chair Ortiz asked if there was any downside to allowing the change. Ms. Rodell answered in the negative.

9:05:29 AM

Representative Knopp considered how the procurement code applied to the work done by APFC. He deduced that the exemption would allow the corporation to enter into short term contracts with external fund managers. He asked how the state's procurement code exemption related to sole source contracts. Ms. Rodell responded that presently the corporation was fully subject to state's procurement code, apart from purchasing investments. She exemplified that the corporation could expend \$250 million to buy an office

building but it could not directly hire an engineer to inspect the building without going through the state procurement code. She detailed that the code had a timeline for an open bid process that tended to be 14 to 21 days. In addition, a committee to evaluate and score the bids along with a 10-day notice of intent to award was required. The notice time allowed for grievances by the bidding parties. She explained that if a building was for sale that had a 30-day open period to complete the inspection the current procurement process would miss the purchasing window. She added that that the code included a limited process for contracts that were less than \$100,000, but in many cases the subject matter requirements were in excess of that amount, which did not make the limited process feasible for APFC. Representative Knopp asked whether the APFC was limited to investments up to \$250 million. Ms. Rodell answered the corporation was permitted to purchase any investment of any size. Representative Knopp verified that the exemption was for subject matter analysis with costs exceeding \$100,000. Ms. Rodell answered that the \$100,000 limit had just been one example. She furthered that any type of expertise; i.e. doctors or medical researchers for a biotech investment - any expertise that was not the acting fiduciary fund managers were the third-party outsourcing referred to by Vice-Chair Johnston. She stated that the exemption was an effort to allow direct investments while eliminating fund manager fees and having the expertise at the table to act within a timely manner. Many investment purchases operated on a short timeframe of up to 3 months. Representative Knopp asked whether the investments operated under earnest agreements.

[9:09:30 AM](#)

Ms. Rodell replied that earnest agreement features were not part of private investment transactions.

Co-Chair Wilson asked how much business the APFC had lost because it lacked the exemption. Ms. Rodell replied that the answer was difficult to quantify. She shared that APFC looked at 6 to 10 investment opportunities each year that required the process and had passed on roughly five to ten investments each year. Co-Chair Wilson asked whether APFC had passed on the investments because they did not have the exemption or if other reasons applied. Ms. Rodell responded that the reasons varied and when the corporation identified the process as a problem, they hired a fund manager to

handle the process. Co-Chair Wilson understood that the APFC could bypass the state's process, but it was more costly without the exemption. Ms. Rodell replied in the affirmative and confirmed that it was much more expensive. Co-Chair Wilson asked for documentation showing the costs. Ms. Rodell answered that the documentation was difficult to provide but would comply. She explained that when APFC sought investments through a fund manager, the manager was entitled to a share of excess profit and a threshold of performance was added to the contract. In the case of excess profit over and above the expected return, the excess was referred to as "carried interest." The fund was entitled to a percentage; the industry standard was 20 percent of the excess profit went to the manager and 80 percent to APFC. The exemption would mean APFC captured all the excess profit through direct investing. She accentuated that the process made it difficult to quantify to costs. The corporation had been attempting to make more direct investments through internal managers. The bill did not ask for a full procurement code exemption. The bill would provide expanded authority when considering direct investments allowing APFC to bring in expertise and return more excess profit to the state. Co-Chair Wilson asked for information on the process they used in the past five years. She wanted to determine how often APFC had to use the outside process Ms. Rodell just described. Ms. Rodell agreed to follow up.

[9:13:02 AM](#)

Representative Carpenter deduced that the corporation could do what it wanted to do; it just took longer. Ms. Rodell affirmed. Representative Carpenter asked whether there was a higher risk involved in doing things in a shorter time period. Ms. Rodell answered that when APFC conducted due diligence on an investment the window was open for a specific time period - typically 30 to 45 days. The state procurement code did not enable APFC to act within the timeframe. She detailed that in terms of risk, the ability to hire subject matter experts within 10 days and work closely with them for 30 days versus relying on outside investors created a different risk profile. There were risks to both processes, but the effort was to provide more comfort in the due diligence process, not increase risk.

Representative Josephson construed that APFC paid a fee for an expert through an investment manager and subsequently

paid them a share of the profits from a successful investment. He asked for verification. Ms. Rodell responded affirmatively. She recapped the process she had explained earlier. Representative Josephson restated his question whether the manager profited from Alaska's investments. Ms. Rodell responded in the affirmative. She furthered that the investment manager acted as the fiduciary and needed to evaluate the investment and assess risk for their investors. The investor was at risk and did not serve their interests to "rubber stamp" an investment.

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Representative Josephson gave an example of APFC wanting to purchase a building in Manhattan. He asked whether what the corporation paid for the investment was a matter of public record. Ms. Rodell answered in the affirmative and added that all the expenses associated with investments were reported quarterly. Representative Josephson asked whether the process could be taken advantage of. He hypothesized a situation where the state had always hired the same architect in Denver. Ms. Rodell thought it was a fair question. She believed that it was necessary for the corporation to continue to maintain an internal process that scrutinized and distributed contracts. The corporation used a number of outside consultants to weigh in and ensure a procedure "passed the smell test." She elaborated that the performance of the fund's portfolio was an indicator of the quality of the due diligence undertaken by APFC. She expected that the investments would perform well.

Representative LeBon thought the discussion was "mixing apples and oranges." He elaborated that the issue was about the global market for venture capital investments and working with a fund manager to invest in a business. Ms. Rodell answered that all the issues encompassed in the entire discussion were relevant and included his example as well as an engineer evaluation of a building and a market assessment to sell "widgets in Europe." Representative LeBon asked for verification that APFC would still have the fiduciary responsibility to perform diligence and was not trying to shortcut the process. Ms. Rodell replied in the affirmative. Representative LeBon surmised that the corporation was attempting to build a base of expertise in order to make many types of investments and was seeking the flexibility to call on the experts quickly in a timeline that fit the opportunity to make the investment and respond

to market opportunities. He asked whether his statement was "fair." Ms. Rodell agreed with his summation.

Co-Chair Wilson asked whether it mattered if there was an in-house versus external manager. Ms. Rodell replied that if APFC undertook the process they had to operate through the procurement process versus when the corporation hired an external manager and invested in a fund the transaction was exempt from the procurement process. Co-Chair Wilson asked whether the arrangement was exclusive to buildings. Ms. Rodell reiterated that the process was for any type of investment.

[9:22:44 AM](#)

Co-Chair Foster believed a similar bill had been before the legislature in the past. He asked if there were any negatives that they should be aware of. Ms. Rodell answered that the prior bill provided a full procurement exemption like the full exemptions allowed the ARM Board, Alaska Housing Finance Corporation (AHFC), AIDA, and all other quasi-agencies like APFC. She elaborated that the current bill was a compromise and had been developed by the corporation at the request of the trustees. The change was a priority of the board. She did not see any negative aspects to the bill and ideally would prefer a full exemption. Co-Chair Foster surmised that the answer to the concern was a more targeted procurement exemption. Ms. Rodell affirmed.

Representative Carpenter did not want to defend a procurement process that exceeded 50 days, but he did not know the process. He asked what parts of the process would be omitted by the exemption.

Co-Chair Wilson interjected that she was trying to understand if the overall procurement system was broken. She felt that it was not the problem of APFC if the whole system was broken.

[9:25:41 AM](#)

Ms. Rodell answered that the state procurement code was in place to purchase everything state government needed to operate - from pencils to furniture and all other items. She observed that the code was written more for commodity acquisitions than services. The code was designed to give

comfort to the public that a competitive process was in place. In APFC's case, the code caused the corporation to pay more for services because they were forced to use an alternative method for necessary investment related services. She believed the balance point had to be weighed. She could not speak to the procurement code and how it worked for other departments like the Department of Transportation and Public Facilities (DOT). The board wanted the corporation in charge of the decision making process to more align with the fund's investment goals. The exemption offered an opportunity for APFC to create more value for the state. She offered that 4 years ago the fund totaled \$52 billion and was currently \$66 billion after a \$2.7 billion transfer in FY 19 to the state's Treasury. The corporation took its stewardship seriously and looked for ways to save costs. She believed that the exemption provided the tools for APFC to tap into expertise that was not needed daily and reduced the investment costs thereby, increasing returns.

[9:28:55 AM](#)

Representative Carpenter needed more clarity on what parts of the process would be eliminated by the exemption. He thought the person in charge of the procurement process was better suited to answer the question. He was concerned there was an "unwieldy" procurement process but did not favor providing exemptions when the process was challenging. He felt that the procurement code served a purpose. He determined that the process needed to be fixed or improved but was not a justification to make exemptions from the process. He concluded that without understanding the process that was being exempted he was unable to support the legislation.

Co-Chair Wilson noted that the committee could hear from the Department of Administration (DOA) at a future hearing.

Co-Chair Foster referenced Representative Carpenter's concern. He suggested a chart illustrating how the procurement process works.

Ms. Rodell referenced a document provided in members' packets [titled "APFC Legislative Initiative: Procurement Streamlining"] (copy on file). She communicated that the timeframe information was included in a chart format. She

pointed to the timeline information with and without the procurement code process.

Co-Chair Wilson interjected to reference the document. She asked Ms. Rodell to speak to what was eliminated via the exemption. Ms. Rodell responded that the 21 day notice, and the 10 day protest period would be eliminated. Co-Chair Wilson asked what would happen if the protest period was removed. She deemed that the ability to protest a contract award would be eliminated.

[9:33:03 AM](#)

Ms. Rodell confirmed her conclusion. She maintained that the idea of the exemption was to enable the corporation to hire a subject matter expert without much bidding. She delineated that the contracts would not be sole source contracts but were considered limited source contracts. Very few individuals had the expertise for much of the subject matter. Co-Chair Wilson reiterated her concern that if someone disagreed with the process there would be no period for protest. She suggested shortening the protest period.

Vice-Chair Johnston noted that the bill requested a degree of flexibility. She referenced private equity investment and the speed at which the market was operating at present. She pointed to Silicon Valley and the biomedical field as examples. She observed that in order for APFC to get in on the "ground floor" of some of the investments without a fund manager "it was necessary to be good and somewhat flexible." She provided a historical example of a biomedical fund investment that had done well for the Permanent Fund (PF) and the investment manager. The corporation invested directly before the company went public on the stock market and garnered large profits for the state but also the fund manager. The APFC was starting to get sophisticated enough to do some of the work itself that would involve hiring a small group of market analysts. The question to the committee was whether they wanted to stay with the status quo and be dependent on fund managers and make less on the investment by following the procurement code. Alternatively, did they want a process for APFC to hire someone with strong expertise and bring the corporation to the private equity table. She asked Ms. Rodell how often the option would be used annually.

[9:37:30 AM](#)

Ms. Rodell answered the fund would use the option approximately 10 to 12 times per year. She reported that APFC was spending \$1.2 billion or so on private equity investments per year and guessed the answer based on the calculation.

Co-Chair Wilson believed that the committee's due diligence required determining whether the timeframe in the bill was accurate. She thought everyone wanted the fund to have the ability to purchase investments but maintained her concern over relinquishing "checks and balances" that were in place.

Representative Knopp shared that prior exemptions from the procurement code with the Department of Corrections (DOC) and the recent sole source contract issues with the new administration created concerns over procurement code exemptions. He wanted to understand the implications. He remarked that managing assets and acquiring them were two separate processes. He wondered whether external fund managers had the discretion to acquire assets or if the decision was made initially through the APFC board. He asked who performed the due diligence. Ms. Rodell answered that external fund managers conducted their own due diligence. Representative Knopp deduced that the exemption would apply to investments by APFC and their internal management. Ms. Rodell replied affirmatively.

Representative LeBon surmised that a venture capital firm would already have performed its own due diligence before offering an opportunity to a potential client. Ms. Rodell agreed with the statement.

[9:41:37 AM](#)

Representative LeBon communicated that a venture capital firm valued its offering and divided the amount into shares that were purchased by a group of investors. He asked whether his statement was correct. Ms. Rodell answered in the affirmative. Representative LeBon stated that when the opportunities were offered time was of the essence. He stated that if a ninety day window of opportunity was offered the bill would be unnecessary. Ms. Rodell affirmed his conclusion. Representative LeBon stated that the investor set the clock. Ms. Rodell agreed with the

statement. Representative LeBon was attempting to "frame the discussion" and pointed out the need for the legislation.

Representative Josephson noted that there were 50 existing exemptions to the procurement code. The bill would create the fifty-first exemption. He asked how to avoid any sort of long-term "coziness" between the contractor and APFC. Ms. Rodell answered that if the corporation was fortunate to get the exemption the process would be imbedded in the investment policy process that was reviewed frequently by the APFC board. There was a regular review trustees conducted on performance and existing investment manager relationships. The board's reporting requirements extended to the public. She reassured the committee there would be a process in place with the intent to avoid "coziness."

9:45:08 AM

Representative Josephson emphasized that along with APFC's ability to be nimble and act quickly the corporation would retain more of the profit that currently went to fund managers. He deduced that the exemption was about increasing profit for the state. He asked for more information regarding the increased profitability under the exemption. Ms. Rodell replied that APFC would report the size of the investment manager fees in total at its upcoming board meeting. She detailed that currently, the carried interest profit sharing piece was in excess of \$100 million. The asset class was approximately \$9 billion at present and had returns of almost 33 percent in FY 18. The entirety of the fund was not invested in the asset class because it was too high risk and illiquid. She furthered that the goal was a balanced asset portfolio and the current discussion included roughly 12 percent of the fund. When the fees were paid, APFC received 80 percent, but the corporation would like to capture more of the lucrative returns. She explained that the method to capture more of the lucrative returns was to "reduce the levels" - either directly or through a fund. The corporation had used a fund called a "fund to funds." The fund to funds encompassed hiring a fund to choose the funds for APFC that chose the underlying investments or portfolio companies. The corporation initially employed the fund to fund method, but over time APFC had gotten rid of most of the fund to fund categories to reduce expenses and was additionally considering how to reduce reliance on fund managers and

allow the corporation to examine portfolio opportunities and invest more directly. The bill would provide a resource to engage in the process more directly.

Co-Chair Wilson wondered how the legislature would know whether the exemption was "the wrong way to go." She trusted Ms. Rodell but inquired how the legislature could judge whether reinstating the "extra parameters" embedded in the procurement code was necessary if the exemption was unsuccessful.

[9:49:39 AM](#)

Ms. Rodell answered that she would judge success in the return metric. She explained that APFC determined its returns by measuring itself against a passive benchmark; as if a computer was choosing the investments, and a performance benchmark that indicated how the active managers were performing. The two benchmarks indicated how well the internal staff was performing over and above the external managers. She added that market influences created poor performance and the benchmarks eliminated the "market noise" from the performance to understand where investment selection was driving value to the fund. She noted that each asset class had its own performance benchmark that assessed whether the fund was consistently underperforming. If the corporation was awarding too much to one contract that lead to bad investments it would be reflected in the numbers on a quarterly basis.

Representative Sullivan-Leonard stated her support of the bill.

[9:51:40 AM](#)

Representative Carpenter asked about the value of the investment decision procurement example on the left side of the table on page 2 of the APFC document that illustrated the review process. He noted the inclusion of a Proposal Evaluation Committee (PEC) under the existing procurement process and felt that it was indicative a "good review process." He observed that good management of public funds was not adversarial to flexibility for the corporation. He wondered whether a partial exemption "may be at odds with good management." He suggested the committee examine why the procurement process was necessary and answer the question of "what exactly was going to be exempt."

Co-Chair Wilson noted that an employee from the procurement office at DOA would address the committee at a future meeting. She thought it would be interesting to find out why the procurement steps were initially implemented.

Representative Josephson asked what value came from the RFP (Request for Proposals) process. He wondered how the corporation was guided to "names that were predictable" to the corporation. Ms. Rodell replied that the corporation had a network of people it interacted with that held a variety of expertise for the different types of investments. For example, if APFC was looking to invest in an Australian infrastructure project it would probably call for recommendations on expertise from the managers of the two Australian sovereign wealth funds that APFC invested in and had experience with. The RFP process would "make it difficult" to proceed in the manner she just described.

[9:55:11 AM](#)

Representative LeBon indicated that the opportunity costs that were lost if the corporation never had the chance to follow up on an investment were difficult to measure. Ms. Rodell agreed with the statement. Representative LeBon suspected the procurement process had been written before the inception of APFC. He asked how many other agencies had asked for the same modification from the procurement process. He suspected the answer was very few or none. Ms. Rodell replied that the Alaska Retirement Management Board (ARMB) was completely exempt from the state procurement code.

Co-Chair Wilson OPENED public testimony.

[9:56:25 AM](#)

MIKE COONS, ASSOCIATION OF MATURE AMERICAN CITIZENS (AMAC), PALMER (via teleconference), opposed the legislation. He recounted Ms. Rodell's testimony that previous requests for the exemption was not granted. He stated that his faith in the Permanent Fund process was extremely low. He thought once the current Permanent Fund issues were taken care of and the trust of the public had been regained perhaps, he could support the bill.

Co-Chair Wilson asked if Mr. Coons would be sending a letter in from AMAC. Mr. Coons replied that he would try.

Co-Chair Wilson asked what AMAC stood for. Mr. Coons answered that it stood for the Association of Mature American Citizens. Co-Chair Wilson asked if he was speaking on his own behalf or the organization. Mr. Coons indicated that he was speaking on behalf of the chapter and agreed to send a letter.

[10:00:50 AM](#)

HERMAN MORGAN, SELF, ANIAK (via teleconference), did not support the bill. He did not trust the legislature. He did not support using money from the Permanent Fund for a gasline. He thought the legislature needed to listen to the people of Alaska.

Co-Chair Wilson clarified that the bill was about procurement and not the dividend.

Co-Chair Wilson CLOSED public testimony.

Ms. Rodell reviewed the zero fiscal note from the Department of Revenue, APFC. She believed the legislation would not increase costs.

Co-Chair Wilson asked if the Department of Administration would have to write any regulations related to the proposal. Ms. Rodell answered in the negative.

Co-Chair Wilson noted the bill would be heard again.

HB 139 was HEARD and HELD in committee for further consideration.

#hb87

HOUSE BILL NO. 87

"An Act extending the liquefied natural gas storage facility tax credit; and providing for an effective date."

[10:04:21 AM](#)

Co-Chair Wilson referenced the document she distributed earlier in the member's packets titled "Interior Alaska Natural Gas Utility Schedule of Sustainable Energy Transmission and Supply (SETS) Loan Funds as of May 9, 2019" (copy on file). She emphasized that the SETS funds

were a loan fund. She questioned where the funding to move the tanks from Fairbanks to the North Pole would come from and if the project would only supply Fairbanks if funding was insufficient.

DAN BRITTON, INTERIOR GAS UTILITY, FAIRBANKS (via teleconference), reviewed the formerly cited document. He pointed to the SETS fund totaling \$125 million. He read the following from the document:

Uses

Projects:

North Pole Distribution System	\$29,346,778
Fairbanks Distribution System	\$14,806,184
Fairbanks 5.25M Gallon Storage Facility	\$37,026,281
North Pole Storage Facility	\$678,542
Pentex Acquisition	<u>\$21,208,913</u>
Total Proceeds Used	\$103,066,697
Remaining Loan Proceeds	\$21,933,303

Remaining Committed Project Uses

Fairbanks 5.25M Gallon Storage	\$18,147,587
Fairbanks and North Pole Customer Service Connections	\$1,992,250
North Pole Storage Facility	\$993,466
Titan 2 & 3 FEED	<u>\$800,000</u>
Total Remaining Committed Project Uses	\$21,933,303
Remaining Loan Proceeds	\$0

Mr. Britton indicated that the Interior Energy Project (IEP) had the ability to issue Conduit Revenue Bonds through Alaska Industrial Development and Export Authority (AIDEA) that was backed by the moral obligation of the state of up to \$150 million. The project hired a financial advisor and began the process of preparing the bond package. The initial bond issuance would total \$75 million to cover the cost to construct the liquefaction plant and Fairbanks Gas Storage Facility. The IEP secured a commitment of \$14 million in funding from a local bank and requested access to a \$7.5 million line of credit from the Fairbanks North Star Borough who assessed whether to allow

the line of credit to proceed. He concluded that the short term funds and the bond funding he described were the funds IEP would employ to fund the projects.

10:09:23 AM

Co-Chair Wilson asked for verification that the project was over \$200 million in debt. Mr. Britton answered in the negative. He clarified that the total indebtedness was the \$125 million in SETS funding. The bond issuance would subsequently create a total indebtedness of \$200 million. The SETS loans had a 15-year deferral accruing no principal payments or interest along with an additional 5 year further deferral if the conversion process was slower than anticipated. The \$125 million was flexible debt put in place by the legislature to remove some of the risk associated with the conversion.

Representative Knopp asked about the construction timeframe and total cost associated with the liquefaction plant. Mr. Britton answered that the liquefaction expansion cost \$50 million. He explained that construction was on a two-year timeframe beginning in the fall of 2019 and an RFP was issued for liquefaction and pretreatment equipment that was part of the front end engineering and design process.

10:11:28 AM

Vice-Chair Johnston MOVED to ADOPT the proposed committee substitute (CS) for HB 87, Work Draft 31-LS0619\U (Nauman, 5/9/19). There being NO OBJECTION, it was so ordered.

Co-Chair Wilson asked for her staff to review the changes in the CS.

LYNN GATTIS, STAFF, REPRESENTATIVE TAMMIE WILSON, reviewed the changes in the CS. She relayed that on page 1, line 7 the date was changed from January 30, 2021 to January 1, 2021 and on page 2, line 9 (a) \$7.5 million was changed to \$5 million. She added that on page 2, lines 10 (b) through 11 were deleted.

Representative LeBon discussed that the North Pole facility tanks were currently located in South Fairbanks and were previously owned by Fairbanks Natural Gas. He asked whether he was correct. Mr. Britton affirmed the statement. He furthered that the North Pole facility would allow the

tanks to be moved to that location. The relocation required the installation of vaporization equipment to vaporize liquid natural gas (LNG). Representative LeBon ascertained that the IEP had two parts: The Fairbanks component that included the 5.25 million tank that was currently under construction and the North Pole component that was not connected to the Fairbanks market. He wondered whether his statement was accurate. Mr. Britton responded in the affirmative. He elaborated that the two systems were not connected at present but would eventually be connected and the same rates would be charged. They would be managed as one service area but were currently independent. The only way to provide gas service in North Pole was to add the storage facility that would provide LNG to pipes that were currently under nitrogen pressure. Representative LeBon asked how large the North Pole piece was in comparison to the Fairbanks component. Mr. Britton answered that the IEP had installed 72 miles of the distribution system in North Pole and Fairbanks had over 140 miles of the distribution system with plans to expand the North Pole system. He elucidated that the demand primarily came from the Fairbanks area. North Pole would account for around 35 percent of the total demand versus the core area of Fairbanks at 65 percent.

[10:16:47 AM](#)

Representative LeBon asked if the LNG supply lines were almost completed. Mr. Britton answered that the Interior Gas Utility (IGU) had completed most of the Phase 1 planned distribution system and the next phases of expansion for North Pole would come in future years when expansion estimates were confirmed, and the demand increased.

Co-Chair Wilson asked why the two systems were separate. Mr. Britton answered that until June 2018 the two systems had been under separate ownership. They were currently under common ownership through the purchase of Pentex by IGU, which provided the opportunity to connect the two systems. The original system was not designed for expansion into the North Pole. Providing service to the North Pole required proper pressure that necessitated the storage facility in North Pole.

[10:18:39 AM](#)

Vice-Chair Ortiz asked whether HB 87 extended the tax credit program for up to \$15 million. He asked for clarification.

Co-Chair Wilson replied in the negative. She detailed that the project was extended for one year and the cost could not exceed more than \$5 million; any additional amount was not covered under the tax credit program and the project had to be completed to the point of commercialization to qualify for the credit. She clarified that that the "old program" that included the \$15 million tax credit program expired on the date as planned. The bill provided a one-year extension and lowered the credit to \$5 million. She added that if the IGU could commercialize its storage plants by December 31, 2019 they would still be eligible for the \$15 million tax credit, failing that they would fall under the \$5 million plan. Vice-Chair Ortiz appreciated the clarification.

Co-Chair Wilson offered that the Fairbanks area's energy costs were not equalized with of the cost of energy in Anchorage, but she desired an eventual end of the tax credit program. She learned that areas of the Mat-Su and bush still heavily relied on diesel fuel.

Representative Carpenter wondered about the length of time it would take to repay the tax credit. Co-Chair Wilson answered that the project would not generate revenue to the state. The project was a benefit to the Interior for paying a high cost for energy for many years.

Vice-Chair Ortiz asked if the \$5 million would be a part of the bonding option. Co-Chair Wilson answered in the negative and added that bonding would come first in order to complete the Fairbanks project. The IEP had to be ready for commercialization by the deadlines to be eligible for the tax credit. She noted that there was a chance IEU would not complete the program in time; therefore, the tax credits would be void.

[10:23:47 AM](#)

Vice-Chair Johnston asked about the fiscal note.

Co-Chair Wilson answered that the bill reduced the maximum amount of the credit to \$5 million of the costs incurred to establish or expand the facility if the facility commences

commercial operation on or after January 1, 2020 and before January 1, 2021. She explained that the tax credit depended on the timing of the project's completion and whether the Department of Revenue (DOR) bond issuance for the tax credits was sufficient to include the credits for IEP. The project would have to wait in line behind other tax credits or may never receive it, since it ultimately depended on appropriation by the legislature.

[10:25:04 AM](#)

Vice-Chair Johnston MOVED to REPORT CSHB 87(FIN) out of committee with individual recommendations and the accompanying fiscal note.

CSHB 87(FIN) was REPORTED out of committee with four "do pass" recommendations and six "no recommendation" recommendations and with one new indeterminate fiscal note from the Department of Revenue.

[10:25:52 AM](#)

AT EASE

[10:27:25 AM](#)

RECONVENED

#sb74

CS FOR SENATE BILL NO. 74(FIN)

"An Act relating to funding for Internet services for school districts; and providing for an effective date."

[10:27:28 AM](#)

Co-Chair Wilson reported the companion bill HB 75 had been heard previously and public testimony had been taken.

MARIDON BOARIO, STAFF, SENATOR LYMAN HOFFMAN, , discussed the sponsor statement for SB 74 (copy on file):

SB 74 increases the broadband requirement for schools from 10 megabits per second (Mbps) to 25 Mbps of download speed and provides funding to help schools reach the 25 Mbps through the School Broadband Assistance Grant (BAG).

Districts that qualify for discounted rate for internet services under the Federal Universal Services Program are eligible.

The Universal Service Administrative Company, Schools and Libraries Program, commonly known as "E-rate," provides discounts of up to 90 percent to help eligible schools and libraries in the United States obtain affordable telecommunications and internet access.

The School BAG was established in 2014 and created to assist schools to reach internet download speeds of 10 Mbps. Currently the grant funds may be used to cover eligible costs incurred by the school districts for schools that have less than 10 Mbps each fiscal year. Since 2014 new and improved technologies and increases to internet services have allowed for more and faster delivery of internet services. Because the cost of internet in some rural districts has decreased, the annual internet costs have fallen below the 2014 benchmark established by state law. To allow school districts to utilize these advances, SB 74 will increase the minimum requirement of Mbps from 10 to 25 which will increase the amount of Broadband Assistance Grants (BAG) that the state can pay to school districts.

In 2019, 80 schools in 20 school districts will benefit from the school BAG awards.

The funding leverages federal E-rate funds at approximately 8:1. The program allows for leverage for up to 9:1 based on a formula for free and reduced lunch calculation by district.

Thank you for your consideration of SB 74 to help bring improved broadband services to rural Alaska and improve service for schools across the state.

I urge your support of this legislation to provide Alaskan students, classrooms and teachers and all educators better access to the digital world.

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Ms. Boario indicated that the state BAG (Broadband Access Grant) program was designed to help schools cover their share of the E-rate costs of approximately 20 percent. The legislature implemented the program to increase internet speeds by helping school districts cover their broadband expenses after the federal E-rate subsidy was applied. She added that the program was voluntary, and the grants were awarded in August each year. She noted that the grant could serve up to 170 schools in 30 school districts totaling over 20 thousand students.

Co-Chair Wilson asked for an explanation of the changes in the Senate Finance Committee Substitute version. Ms. Boario explained that a question arose about whether the increased funding for the grant program would impact the disparity test for the federal impact aid. In addition, the funding was not distributed equally across the districts which could affect the disparity test. Co-Chair Wilson asked what districts were included in the disparity test. Ms. Boario replied that because the funding was different due to the higher broadband costs in some districts; districts paying more received higher federal subsidy and BAG grant awards, which could affect the disparity test. The districts did not receive equal funding. Co-Chair Wilson asked Ms. Boario to cite where in the bill the changes were made. Ms. Boario answered that on page 1, line 10, Section 2 and page 2, line 6, Section 3 additional conditional effect language was inserted as follows:

Sec. 2. The uncodified law of the State of Alaska is amended by adding a new section to read:

CONDITIONAL EFFECT; NOTIFICATION. (a) Section 1 of this Act takes effect 13 only if, on or before January 1, 2020, the Department of Education and Early Development has received certification from the United States Department of Education that E-rate funding under the federal universal services program may be excluded from the federal 1 disparity test 2 under 34 C.F.R. 222.160-169, as amended.

Sec. 3. If, under sec. 2 of this Act, sec. 1 of this Act takes effect, it takes effect the day after the date the commissioner of education and early development receives certification from the United States Department of Education.

Co-Chair Wilson asked how long it took to get the certification and whether it was requested in the past. Ms. Boario answered that it had never been request for the E-rate program. However, she was aware that the Department of Transportation and Public Facilities (DOT) funds were exempted from the disparity test.

HEIDI TESHNER, ADMINISTRATIVE SERVICES DIRECTOR, DEPARTMENT OF EDUCATION AND EARLY DEVELOPMENT, OFFICE OF MANAGEMENT AND BUDGET, answered that the certification waiver requested from the United States (US) Department of Education asked if the E-rate funding that districts received could be moved to a special revenue fund or removed completely from the calculation for the disparity test.

Co-Chair Wilson asked how long the waiver process would take. Ms. Teshner hoped that the certification would be issued in several weeks. Co-Chair Wilson spoke to the BAG awards for 2019. She observed that the grants were mostly awarded to rural schools. She asked whether most urban schools paid for their own internet.

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Ms. Boario answered yes "conditionally." Primarily rural schools were affected due to the high cost of internet and urban schools were able to obtain high speed internet much cheaper than in rural areas and the grants applied to schools only receiving 10 Mbps. Technically the grants applied to all schools, but some schools were ineligible due to better connectivity. Co-Chair Wilson had never known her school district to "not want money." She knew Fairbanks had problems with its internet service at times and could not perform testing in all schools on the same day. She asked for clarification regarding eligibility for the grant. Ms. Boario replied that the e-rate funding federal subsidy was utilized by all schools in Alaska. The BAG grant only provided additional funding to schools that qualified to help increase their speeds to 25 Mbps. Co-Chair Wilson wondered why the fiscal note was \$7 million. She determined that the \$7 million would be added to the \$1 million and cover a number of years. Ms. Boario affirmed her statement.

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Co-Chair Wilson stated that she misspoke. She reported that the BAG grant covered 172 schools which increased the megabit threshold for each School from 10 megabits to 25 megabits per second and continue paying the \$7 million amount for years to come. Ms. Boario affirmed her statement. She acknowledged that it was a grant program, but costs were expected to decline over the years as the coverage increased. Co-Chair Wilson had heard from prior testimony that most of the areas had more than one provider. She did not believe the information was accurate. She wanted to know what private company would be receiving \$7 million of state funds. Co-Chair Wilson wanted the committee to understand that the state was paying an additional \$7 million each year with passage of the bill. She was interested in information regarding the competition that existed among internet providers for the \$7 million.

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CHRISTINE O'CONNOR, EXECUTIVE DIRECTOR, ALASKA TELECOM ASSOCIATION, answered that there was a minimum of two providers in every area according to a survey of the association's members. There was a satellite provider that covered the entire state and was very active in bidding on e-rate contracts. In addition, all locations had existing landline providers that bid on fixed broadband services. She stressed that the e-rate rules required that all landline providers bid on E-rate RFPs. In many areas there were three or four providers. She offered the example of vigorous competition among 4 providers in Nome for bidding to provide E-rate service, which drove down the rates. She noted a 37 percent decrease in broadband rates for schools. The competition created new partnerships amongst the providers and e-rate rules encouraged schools to bid together as consortiums. She reported that the factors happened within the last few years and were driving rates down. However, gaps in service still existed due to the need for and more infrastructure. Co-Chair Wilson asked for more information. She had not seen a drop in internet costs for schools. She wanted to better understand the competition.

Representative Carpenter asked how the FY 19 10 mbps program numbers predicted the FY 21 25 mbps numbers. Ms. Teshner answered that the note used the average FY 19 BAG grant in order to determine a cost if all 172 schools applied for the grant. She mentioned that the average was

the best data the department had to approximate the cost to raise speeds from 10 mbps to 25 mbps. Representative Carpenter referred to the following language in the fiscal note analysis:

This \$1,487.5 will need to be funded in all of the out years, in order to pay for 0-10mbps internet coverage in tandem with current fiscal note that covers 10-25mbps. The entire program will continue as one application for up to 25mbps.

Representative Carpenter wondered whether the actual total was \$8.6 million versus \$7.1 million, which was not reflected in the fiscal note. Ms. Teshner replied in the affirmative.

Co-Chair Wilson asked why FY 20 did not show the over \$1 million currently awarded to grants. Ms. Teshner answered that when the department was told to only report the costs necessary for the speed increase from 10mbps to 25mbps and the \$1.4 million figure was included in the analysis to show that amount was needed to continue the 0 mbps to 10 mbps program as well. Co-Chair Wilson thought the entire amount should be reflected in the FY 20 cost. She reported that before the change from 10 mbps to 25 mbps the school districts were asked to show how they were able to fund the 25 mbps increase. She asked why the grant was increased if the school districts demonstrated they were able to fund the increase. Ms. Teshner answered that the fiscal note was an estimate. Co-Chair Wilson restated her question. She clarified her question and asked why the grants would be necessary. Ms. Teshner answered that the program was voluntary and based on a baseline number and if costs went below the baseline level the school district would no longer qualify because the overall cost would decrease. She deferred to Patience Frederickson, from the Division of Library, Archives, and Museums who ran the program for further clarification.

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Co-Chair Wilson was not blaming any school district for getting funds. She pondered why the grants amounted to up to \$8 million when many districts could pay for internet service.

PATIENCE FREDERICKSON, DIRECTOR, ALASKA DIVISION OF LIBRARIES, ARCHIVES, AND MUSEUMS, DEPARTMENT OF EDUCATION AND EARLY DEVELOPMENT, responded that the E-rate application asks the school to certify that they can repay the remaining portion of the bill. Therefore, school districts only applied for the E-rate if they know the BAG grant was available. The districts could not apply for 25 mbps in the current year because the bill did not exist during the application period. Districts would be able to apply for 25 mbps during the next application period knowing that the BAG grant was available to pay for the remainder of the E-rate. She reiterated that the certification was not on the state application, it was on the federal application. Co-Chair Wilson surmised that all the bill was essentially doing was securing E-rate BAG grant funding in the outyears. Ms. Frederickson answered in the affirmative. She furthered that the program had been designed to increase levels of internet speeds. Co-Chair Wilson wondered why the legislature would not just increase the Base Student Allocation (BSA).

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Ms. Frederickson replied that she was not conversant on the BSA program. She suspected the reason was because it included the federal E-rate funding. She detailed that the genesis of the BAG program came out of the OWL (Online With Libraries) program, which helped libraries achieve a certain speed of internet to enable them to participate in a video conference network. The idea behind the OWL program was to combine E-rate, library, and grant funding to increase the internet speeds. The BAG program was based on OWL.

Co-Chair Wilson remarked that the OWL funding was appropriated in all school districts. She asked whether she was correct. Ms. Frederickson answered in the negative. The OWL program video conference network was available in every public library, but the subsidy went to approximately 20 public libraries. Co-Chair Wilson requested the list of libraries involved in OWL.

Vice-Chair Johnston remembered that the Nome bidding war happened because it was cheaper to provide the higher speed 25 mbps than the lower speed internet. She asked for confirmation.

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Ms. O'Conner answered that she was unfamiliar with the details but thought Ms. Frederickson's recounting made sense. She acknowledged that Nome had relatively good connectivity and multiple providers. Relatively large bandwidth was purchased "in bulk" and 10 mbps was a very small amount. Vice-Chair Johnston considered the fiscal note and improved technology. She thought the scenario could be repeated in the rest of the state with improved satellite technology and as competition increased. She deduced that the fiscal note was currently high, but it could decrease with improved technology in the future. Ms. O'Conner agreed with her conclusion. She indicated that multiple projects were coming online in the near future in Alaska. Every company was taking advantage of newly stabilized federal funding for increased connectivity. She noted that the lower orbit satellite technology was untested and was not imminent.

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Ms. Frederickson concurred with Ms. O'Conner's assessment and noted she had experienced lower costs with the BAG program. She pointed out that in the program's early years the average BAG grant was \$30 thousand and fell to \$17,000 within 5 years. She determined that as the cost of internet decreased to get to 10 mbps the mathematical formula to qualify remained at the 2014 benchmark and districts fell out of the program due to decreased costs; in FY 19 awards declined from 119 to 80.

Co-Chair Wilson pondered whether the funds belonged in the BSA as an ongoing cost.

Representative Carpenter noted that the federal government's standard was 100 mbps. He deemed that 100 mbps was currently cost prohibitive in Alaska. He imagined that once districts obtained 25 mbps there would be later discussions about increasing the speed to 50 mbps and higher. He asked if currently low earth orbit satellites were over Alaska. Ms. O'Conner answered in the negative.

Representative Carpenter recounted that in previous testimony a school district testifier had been unaware of what the cost had been to increase from 10 mbps to 25 mbps. He inquired how it was known that the program would cost

\$7.1 million. Ms. Frederickson answered that the fiscal note was estimated from current costs. She observed that the problem was the competitive bid process for the e-rate application.

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Representative Carpenter understood the process of how it was purchased but "we don't put a bid in to find out if we can afford it." Ms. Frederickson replied that the process was confidential, and she did not have access to the information.

Co-Chair Wilson asked whether the information was confidential to the school districts. She commented that the school districts were queried about the costs and one response was received. She hoped the districts knew how much their portion of the E-rate costs would be when applying for the BAG grant program since it was a separate process from the federal E-rate program. Ms. Frederickson responded that with passage of SB 74 she would establish new benchmarks based on what the school districts were paying in January 2020. Subsequently, the school BAG program schools "would never pay more than what they were paying in January 2020." The costs would be frozen the districts would rely on the BAG program for the remainder of costs. She acknowledged that she was not answering the question correctly.

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Representative Carpenter interposed an analogy to illustrate the question. He exemplified a business that wanted to increase its bandwidth from 10 mbps to 25 mbps. The business would go to a provider for a quote to know if it had the money available to pay for the increase. He declared that the state had the opposite process and paid over \$8 million without knowing the actual costs. He characterized the process as "backwards." He contended that a district should know what the increased service would cost. He wanted to know what the actual cost was but discerned that the costs were unknown. Ms. Frederickson agreed that the costs were unknown. She restated that the cost was based on the current program "and some cocktail napkin figures" and noted that "it was the best they could come up with."

Ms. Boario understood the statements and questions by Representative Carpenter. She explained that the confusion sprang from receiving federal funding first. She thought that knowing how the E-rate contracts went to bid might provide more clarity.

Co-Chair Wilson stated that her issue was why the BSA did not cover the costs. Additionally, the federal e-rate program required to know whether the districts could cover the remaining costs. It was her understanding the school districts had the money for the increased bandwidth and they relied on the BAG program to cover the remaining costs. Ms. Boario clarified that it was rural school districts that could not cover the costs on their own. Co-Chair Wilson cited prior districts' testimony that they could cover the costs. In addition, she was unaware that the costs were ongoing each year.

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Representative Josephson asked for clarity regarding the proprietary information. Ms. Frederickson answered that when the school districts utilize the E-rate computer they enter each school and the amount of broadband service desired for each school. The internet service providers submitted the bids for each school, which was the proprietary information the state did not have. They could not tease out the information that answered what the actual costs were. She added that in the first year of the program they had received \$5 million from the legislature and only \$3.5 million had been used.

Co-Chair Wilson requested that the sponsor provide further information regarding the committee's questions.

Representative Josephson asked whether Regional Educational Attendance Area (REAA) schools absorbed internet costs through the BSA or if they dropped out of the BAG program. Ms. Frederickson replied in the affirmative, but asked members to bear in mind that if a district chose not to apply it was because the competition had driven cost down.

Co-Chair Wilson recognized the many questions and concerns about the bill. She asked members to keep an eye on the schedule for future hearings.

CSSB 74(FIN) was HEARD and HELD in committee for further consideration.

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ADJOURNMENT

11:08:34 AM

The meeting was adjourned at 11:08 a.m.