

SB

100

<TARGET><BILL>SB 100</BILL><SUBJECT>SB
100</SUBJECT><COMM>SCRA29</COMM></TARGET>

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Governor Bill Walker
STATE OF ALASKA

April 6, 2015

The Honorable Kevin Meyer
President of the Senate
Alaska State Legislature
State Capitol, Room 111
Juneau, AK 99801-1182

Dear President Meyer:

Under the authority of Article III, Section 18, of the Alaska Constitution, I am transmitting a bill relating to the assessment of property for the property tax for a North Slope natural gas project.

Due to the achievements by the Municipal Advisory Gas Project Review Board and the Alaska Liquefied Natural Gas project, it is time to move forward with legislation to address the property tax on a North Slope natural gas project. Revenues from the property tax on a North Slope natural gas project are anticipated to provide vital support for the State and local governments to establish sustainable fiscal platforms.

The bill would provide a framework for the assessment of property tax on a North Slope natural gas project once the project begins to transport gas. The assessment for property exclusively used for a North Slope natural gas project would be based on the full and true value of the property determined by adjusted original cost and annualized throughput. The bill would define a North Slope natural gas project for the purposes of the property tax to include a gas treatment plant, a gas pipeline, a liquefaction plant, and a marine terminal. Consistent with the concerns expressed by local governments and legislative direction last year, the property tax on existing North Slope oil and gas and pipeline properties would be unchanged by this bill.

There is still much work to be done before this all-important project can be built. This bill demonstrates my Administration's continued commitment to building a gasline to provide gas to Alaskans and liquefied natural gas to world markets. I urge your prompt and favorable action on this measure.

Sincerely,

A handwritten signature in blue ink that reads "Bill Walker".

Bill Walker
Governor

Enclosure

SENATE BILL NO. 100

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-NINTH LEGISLATURE - FIRST SESSION

BY THE SENATE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

Introduced: 4/7/15

Referred: Community and Regional Affairs, Resources, Finance

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to the assessment of property for oil and gas exploration, production,
2 and pipeline transportation property tax on a North Slope natural gas project;
3 amending the definition of "taxable property"; adding a definition for "North Slope
4 natural gas project"; and making conforming amendments."

5 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

6 * **Section 1.** AS 43.56.060(a) is amended to read:

7 (a) The department shall assess property for the tax levied under
8 AS 43.56.010(b) and AS 29.45.080 on property exclusively used for a North Slope
9 natural gas project and on property used or committed by contract or other
10 agreement for use for the pipeline transportation of gas or unrefined oil or for the
11 production of gas or unrefined oil at its full and true value as of January 1 of the
12 assessment year.

13 * **Sec. 2.** AS 43.56.060(e) is amended to read:

14 (e) Except as provided in (h), the [The] full and true value of taxable

1 property used or committed by contract or other agreement for pipeline transportation
 2 of gas or unrefined oil or in the operation or maintenance of facilities for the pipeline
 3 transportation of gas or unrefined oil is:

4 (1) on the construction commencement date and until January 1
 5 following the date the pipeline begins to transport gas or unrefined oil, the actual cost
 6 incurred or accrued with respect to the property as of the date of assessment;

7 (2) determined on each January 1 thereafter with due regard to the
 8 economic value of the property based on the estimated life of the proven reserves of
 9 gas or unrefined oil then technically, economically, and legally deliverable into the
 10 transportation facility; however, if the proven reserves of gas or unrefined oil then
 11 technically, economically, and legally deliverable indicate an economic life materially
 12 shorter than the estimated physical life of the transportation facility, the full and true
 13 value is the actual cost reduced by an annual allowance for depreciation on a straight
 14 line basis over an economic life based on the actual elapsed life from the
 15 commencement of full operation to the date of assessment plus the estimated
 16 remaining life of the proven reserves of gas and unrefined oil then technically,
 17 economically, and legally deliverable into the transportation facility as of the date of
 18 the assessment;

19 (3) on the assessment date next following inability to use or construct
 20 all or a substantial part of the facility for a period of 90 or more consecutive days
 21 because of natural disaster or legal prohibition, or other events beyond the control of a
 22 person having ownership or control of the property, adjusted to take into account any
 23 diminution in value.

24 * **Sec. 3.** AS 43.56.060 is amended by adding a new subsection to read:

25 (h) Starting on the construction commencement date, the full and true value of
 26 taxable property exclusively used for a North Slope natural gas project is determined
 27 on each January 1. On January 1 following the date a North Slope natural gas project
 28 begins to transport gas, the full and true value is the original cost adjusted for inflation,
 29 the product of which is reduced by an annual allowance for depreciation, and the
 30 remainder of which is subject to a throughput factor. The throughput factor includes
 31 the estimated annual throughput as measured in thousands of cubic feet of gas

1 transported divided by the original annual throughput design basis as measured in
 2 thousands of cubic feet of gas.

3 * Sec. 4. AS 43.56.210(5) is amended to read:

4 (5) "taxable property"

5 (A) means real and tangible personal property exclusively used
 6 for a North Slope natural gas project or real and tangible personal
 7 property used or committed by contract or other agreement for use within this
 8 state primarily in the exploration for, production of, or pipeline transportation
 9 of gas or unrefined oil (except for property used solely for the retail
 10 distribution or liquefaction of natural gas unless the property is exclusively
 11 used for a North Slope natural gas project), or in the operation or
 12 maintenance of facilities used in the exploration for, production of, or pipeline
 13 transportation of gas or unrefined oil; "taxable property" includes

14 (i) machinery, appliances, supplies, and equipment;

15 (ii) drilling rigs, wells (whether producing or not),
 16 gathering lines and transmission lines, pumping stations, compressor
 17 stations, power plants, topping plants, and processing units;

18 (iii) roads, tank farms, tanker terminals, docks and other
 19 port facilities, and air strips;

20 (iv) aircraft and motor vehicles owned by a person
 21 whose principal business in the state is the exploration for, production
 22 of, or pipeline transportation of gas or unrefined oil and whose
 23 operation of the aircraft or motor vehicle directly relates to the conduct
 24 of that business;

25 (v) maintenance equipment and facilities, and
 26 maintenance camps and other related facilities; and

27 (vi) communications facilities owned by a person
 28 whose principal business in the state is the exploration for, production
 29 of, or pipeline transportation of gas or unrefined oil and whose
 30 operation of the communications facilities directly relates to the
 31 conduct of that business;

- 1 (B) does not include
- 2 (i) permanent residences;
- 3 (ii) office buildings requiring substantial local
- 4 government services;
- 5 (iii) oil and gas pipeline systems owned and operated by
- 6 a public utility that is certificated under AS 42.05.221 and is regulated
- 7 by the Regulatory Commission of Alaska;
- 8 (iv) aircraft and motor vehicles, except aircraft and
- 9 motor vehicles taxable under (A)(iv) of this paragraph; and
- 10 (v) communications facilities, except communications
- 11 facilities taxable under (A)(vi) of this paragraph;

12 * **Sec. 5.** AS 43.56.210 is amended by adding a new paragraph to read:

13 (7) "North Slope natural gas project" means a project to transport gas

14 produced north of 68 degrees North latitude through a gas treatment plant, a gas

15 pipeline, a liquefaction plant, and a marine terminal; in this paragraph,

16 (A) "gas pipeline" means a pipeline transporting gas beginning

17 at the outlet flange of a gas treatment plant terminating at the inlet flange of a

18 liquefaction plant, including all pipe, compressor stations, station equipment,

19 and all other facilities necessary for an integral line of pipe to effectuate the

20 transportation of gas from point to point, excluding any pipelines downstream

21 of an offtake point between a gas treatment plant and a liquefaction plant;

22 (B) "gas treatment plant" means a facility located north of 68

23 degrees North latitude to treat natural gas to pipeline specifications and deliver

24 treated natural gas to the inlet flange of a gas pipeline, excluding any

25 transmission lines that deliver gas to the inlet flange of the facility;

26 (C) "liquefaction plant" means a facility that receives from the

27 outlet flange of a gas pipeline gas for liquefaction in the facility, including

28 storage and facilities for off-loading liquefied natural gas;

29 (D) "marine terminal" means a terminal and those facilities

30 required to receive liquefied natural gas from the boundary of a liquefaction

31 plant for marine transportation, including storage and facilities for off-loading

1 liquefied natural gas.

2 * **Sec. 6.** The uncodified law of the State of Alaska is amended by adding a new section to
3 read:

4 **APPLICABILITY.** Sections 1 - 5 of this Act apply to tax years beginning after
5 December 31, 2015.

An Act relating to the assessment of property for oil and gas exploration, production, and pipeline transportation property tax on a North Slope natural gas project; amending the definition of "taxable property"; adding a definition for "North Slope natural gas project"; and making conforming amendments.

SECTIONAL ANALYSIS

Senate Community & Regional Affairs Committee

Section 1 amends AS 43.56.060(a), related to assessment of property, to add a conforming reference to property exclusively used for a North Slope natural gas project.

Section 2 amends AS 43.56.060(e), related to the full and true value of pipeline transportation property, to add a conforming reference to except property exclusively used for a North Slope natural gas project in new subsection (h).

Section 3 amends AS 43.56.060 to add a new subsection (h), related to the full and true value of taxable property exclusively used for a North Slope natural gas project. This section provides that the full and true value of taxable property exclusively used for a North Slope natural gas project will be determined on each January 1 starting on the construction commencement date. This section provides that on January 1 following the date a North Slope natural gas project begins to transport gas, the full and true value of taxable property exclusively used for a North Slope natural gas project is determined by original cost with adjustments for inflation and depreciation and subject to a throughput factor. The throughput factor is measured in thousands of cubic feet of gas.

Section 4 amends AS 43.56.210(5), defining "taxable property", to add conforming references to property exclusively used for a North Slope natural gas project. The liquefaction plant and marine terminal of a North Slope natural gas project would be taxable property subject to the 20 mill levy in AS 43.56.010(a).

Section 5 amends AS 43.56.210 by adding a new paragraph (7) defining "North Slope natural gas project." This section includes subparagraphs (A)-(D) defining "gas pipeline", "gas treatment plant", "liquefaction plant", and "marine terminal" for the purposes of the definition of North Slope natural gas project in this section.

Section 6 provides that secs. 1-5 of the bill apply to tax years beginning after December 31, 2015. This applicability section would go into uncodified law.

The bill does not have a special effective date.

FISCAL NOTE

STATE OF ALASKA
2015 LEGISLATIVE SESSION

Bill Version LL 0832-2
 Fiscal Note Number _____
 () Publish Date _____

Identifier (file name) 0832-DOR-TAX-4-1-15 Dept. Affected Revenue
 Title Property Tax North Slope natural gas project. Appropriation Tax and Treasury
 Allocation Tax Division
 Sponsor Rules Committee
 Requester Governor OMB Component Number 2476

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

	FY16 Appropriation Requested	Included in Governor's FY16 Request	Out-Year Cost Estimates				
			FY17	FY18	FY19	FY20	FY21
OPERATING EXPENDITURES	FY16	FY16	FY17	FY18	FY19	FY20	FY21
Personal Services							
Travel							
Services							
Commodities							
Capital Outlay							
Grants, Benefits							
Miscellaneous							
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0	0.0

FUND SOURCE		(Thousands of Dollars)					
1002	Federal Receipts						
1003	GF Match						
1004	GF						
1005	GF/Prgm (DGF)						
1007	I/A Rcpts (Other)						
1156	Rcpt Svcs (DGF)						
		0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS							
Full-time							
Part-time							
Temporary							

CHANGE IN REVENUES							

Estimated **SUPPLEMENTAL (FY15) operating costs** _____ (separate supplemental appropriation required)
 (discuss reasons and fund source(s) in analysis section)

Estimated **CAPITAL (FY16) costs** _____ (separate capital appropriation required)
 (discuss reasons and fund source(s) in analysis section)

ASSOCIATED REGULATIONS

Does the bill direct, or will the bill result in, regulation changes adopted by your agency? no
 If yes, by what date are the regulations to be adopted, amended, or repealed? n/a Discuss details in analysis section.

Why this fiscal note differs from previous version (if initial version, please note as such)

Prepared by Jerry Burnett, Deputy Commissioner
 Division Commissioner's Office
 Approved by Randall Hoffbeck, Commissioner
 Agency Commissioner's Office

Phone 465-3669
 Date/Time 4/1/15 12:00 AM
 Date 4/1/2015

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2015 LEGISLATIVE SESSION

BILL NO. LL 0832-2

Analysis

Bill provides a framework for determining the taxable value of a North Slope natural gas project measured against the three criteria of clarity, robustness/durability, and lack of ambiguity. The following parameters were considered to meet these criteria, in the context of an LNG export project:

Original cost
Inflation
Design throughput
Actual throughput
Depreciation
Tax (Mill) rate

By combining these features, an output similar to what would have been derived under AS 43.56 is achieved without the incumbent uncertainties in interpretation, especially around Replacement Cost New (RCN), Obsolescence, and/or measuring sales or revenue.

The proposed basic construct of the formula is as follows:

Original cost x Inflation x Depreciation x (Actual throughput/Design throughput) x Mill rate

The fiscal impact of this bill is zero during the period covered by the fiscal note.

Upon completion of a North Slope natural gas project, the property tax revenues will be dependent on the inputs to the formula above. At this point the revenues are indeterminate.

Fiscal Note

State of Alaska
2016 Legislative Session

Bill Version: SB 100
Fiscal Note Number: _____
() Publish Date: _____

Identifier: SB100-DOR-TAX-01-24-16
Title: NORTH SLOPE GAS PROJ PROP
TAX;ASSESSMENT
Sponsor: RLS BY REQUEST OF THE GOVERNOR
Requester: Senate Community and Regional Affairs

Department: Department of Revenue
Appropriation: Taxation and Treasury
Allocation: Tax Division
OMB Component Number: 2476

Expenditures/Revenues

Note: Amounts do not include inflation unless otherwise noted below. (Thousands of Dollars)

	FY2017 Appropriation Requested	Included in Governor's FY2017 Request	Out-Year Cost Estimates					
			FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
OPERATING EXPENDITURES								
Personal Services								
Travel								
Services								
Commodities								
Capital Outlay								
Grants & Benefits								
Miscellaneous								
Total Operating	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Fund Source (Operating Only)

None								
Total	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Positions

Full-time								
Part-time								
Temporary								

Change in Revenues								
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Estimated SUPPLEMENTAL (FY2016) cost: 0.0 *(separate supplemental appropriation required)*
(discuss reasons and fund source(s) in analysis section)

Estimated CAPITAL (FY2017) cost: 0.0 *(separate capital appropriation required)*
(discuss reasons and fund source(s) in analysis section)

ASSOCIATED REGULATIONS

Does the bill direct, or will the bill result in, regulation changes adopted by your agency? no
If yes, by what date are the regulations to be adopted, amended or repealed? n/a

Why this fiscal note differs from previous version:

updated to 2016 form

Prepared By: Jerry Burnett, Deputy Commissioner
Division: Department of Revenue
Approved By: Randall Hoffbeck, Commissioner
Agency: Department of Revenue

Phone: (907)465-4785
Date: 01/24/2016 12:00 AM
Date: 01/24/16

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2016 LEGISLATIVE SESSION

BILL NO. SB100

Analysis

Bill Analysis

Bill provides a framework for determining the taxable value of the AKLNG project or other North Slope natural gas project measured against the three criteria of clarity, robustness/durability, and lack of ambiguity. The following parameters were considered to meet these criteria, in the context of an LNG export project:

- Original cost
- Inflation
- Design throughput
- Actual throughput
- Depreciation
- Tax (Mill) rate

By combining these features, an output similar to what would have been derived under AS 43.56 is achieved without the incumbent uncertainties in interpretation, especially around Replacement Cost New (RCN), Obsolescence, and/or measuring sales or revenue.

The proposed basic construct of the formula is as follows:

Original cost x Inflation x Depreciation x (Actual throughput/Design throughput) x Mill rate

The fiscal impact of this bill is zero during the period covered by the fiscal note.

Upon completion of the AKLNG project, the property tax revenues will be dependent on the inputs to the formula above. At this point the revenues are indeterminate.



THE STATE
of **ALASKA**
GOVERNOR BILL WALKER

Department of Revenue

COMMISSIONER'S OFFICE

State Office Building
333 Willoughby Avenue, 11th Floor
PO Box 110400
Juneau, Alaska 99811-0400
Main: 907.465.2300
Fax: 907.465.2389

April 7, 2015

The Honorable Click Bishop, Chair
Senate Community & Regional Affairs Committee
State Capitol Building
Juneau, AK 99801

Dear Senator Bishop:

The Department of Revenue (DOR) respectfully requests that SB 100, "An Act relating to the assessment of property for oil and gas exploration, production, and pipeline transportation property tax on a North Slope natural gas project; amending the definition of "taxable property"; adding a definition for "North Slope natural gas project"; and making conforming amendments," be scheduled in the Senate Community & Regional Affairs Committee at your earliest convenience.

Your favorable consideration of this request is appreciated. If you need any additional information, please contact Jerry Burnett, Deputy Commissioner for the Department of Revenue at 907-465-3669.

Sincerely,

A handwritten signature in blue ink, appearing to read "Randall J. Hoffbeck".

Randall J. Hoffbeck
Commissioner

Cc: Darwin Peterson, Legislative Director, Office of the Governor
Jerry Burnett, Deputy Commissioner, Department of Revenue
Ken Alper, Director, Tax Division, Department of Revenue

Status Review on Proposed Payments in Lieu of Property Tax

Senate Community & Regional Affairs

January 28, 2015

Randall J. Hoffbeck, Commissioner

Department of Revenue



Current Status of PILT Discussions

Tentative alignment reached with Producer Parties on:

1. Amount of Construction-related Payment in Lieu of Tax (CPILT) and
2. Structure and target amount for Operations-related Payment in Lieu of Tax (OPILT)

Overview

- Conceptual overview of CPILT
- Conceptual overview of OPILT
- OPILT calculation
- CPILT proposal

CPILT

- Total amount = \$800 million
 - 4:4ths
 - Expected pay out over 5-year construction period
- Annual payment amount, schedule, and allocation among State and impacted local jurisdictions yet to be determined

OPILT

- Target amount total = \$15.7 billion
 - Actual payment amount will vary as actual flow rate with five year averaging varies from project design flow
 - Calculated using MAGPRB recommended formula
 - Paid out over 25-year period
 - 4:4ths
 - Payment schedule incorporates 1% increase in payments each year, which is included in target amount
 - Allocation among State and local jurisdictions yet to be determined
-

OPILT Methodology – Initial Formula

MAGP Board Recommendation (March 13, 2015)

$$\left(\text{Capital Cost} \times (1 + e)^m \times \text{Depreciation Factor} \times \left(\frac{\text{Actual Throughput}^n}{\text{Design Throughput}} \right) \times \text{Mill Rate} \right)$$

MAGP Board Recommendation
(Formula Values)

n = exponent to dampen effect of actual flow
e = annual escalation rate
m = years of operation (startup = 0)

Capital Cost = FID estimate x 1.1
e = 4% per annum
Depreciation Factor based on 50 year floating life
Actual Throughput = 5 year floating average
n = 1
Mill Rate based on current statutes **for all Project assets including LNG Plant**

OPILT Methodology – Modified Formula

SB 100 Recommendation

$$\left(\text{Original Cost} \times \text{Inflation Factor} \times \text{Depreciation Factor} \times \left(\frac{\text{Actual Throughput}}{\text{Design Throughput}} \right) \times 20 \text{ Mills} \right)$$

Original Cost = Fixed by **pre-FID** project specific data/fiscal agreement

Inflation Factor = Fixed by fiscal agreement

Depreciation Factor = Fixed by fiscal agreement

Actual Throughput = Operational measurable

Design Throughput = Fixed by **pre-FID** project specific data

Mill Rate = Fixed by statute, **with total take adjusted by fiscal agreement**

OPILT Methodology – Current Formula

Tentative Alignment

$$\left(\text{Original Cost} \times \text{Escalation Factor} \times \text{Depreciation Factor} \times \left(\frac{\text{Actual Throughput}}{\text{Design Throughput}} \right) \times \text{Blended Mill Rate} \right)$$

Original Cost = \$55 billion

Escalation Factor = 2.5% (3.25% inflation - .75% obsolescence)

Depreciation Factor = 30 year modified floating/fixed life

Actual Throughput = Operational measurable (5 year rolling average)

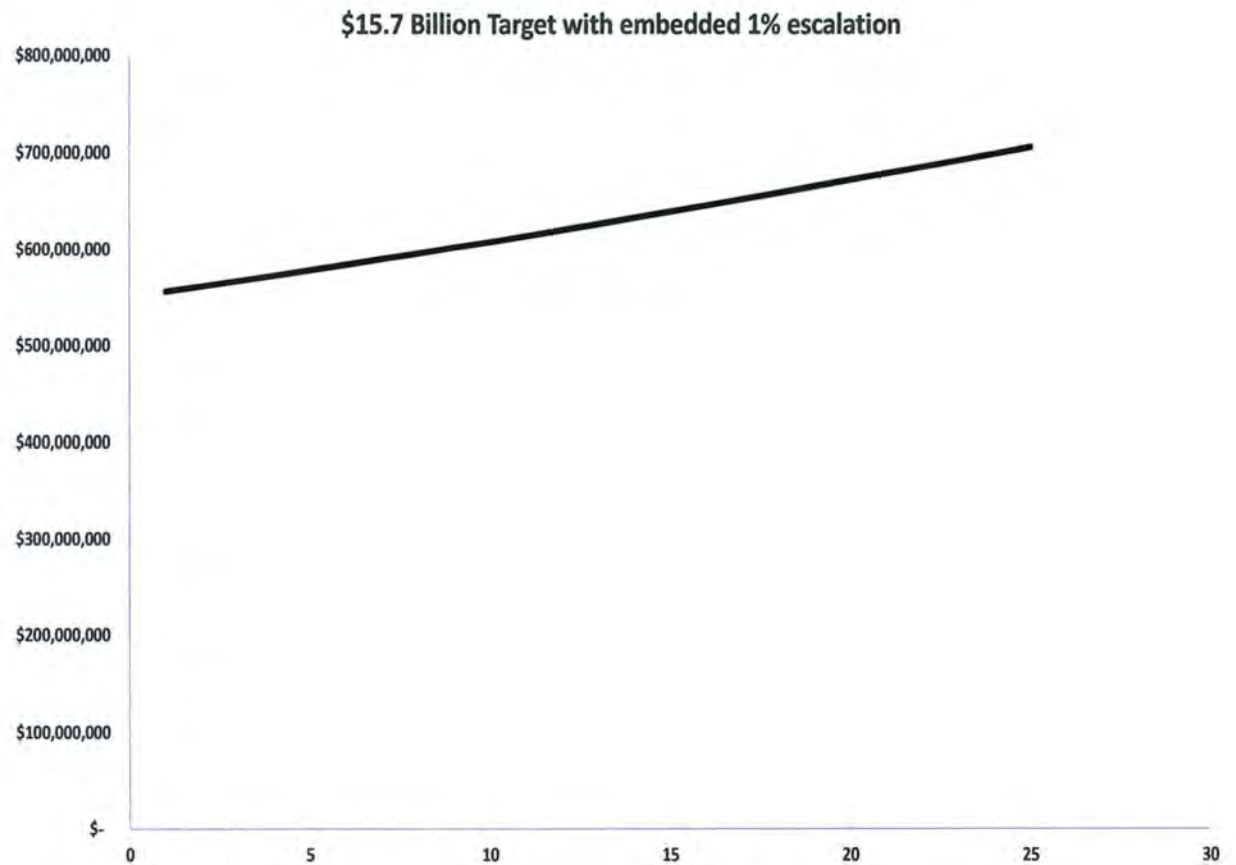
Design Throughput = To Be Determined

Mill Rate = 13.75 Mills (20 mills GTP, 20 mills pipeline, 7.5 mills LNG*)

\$15.7 billion

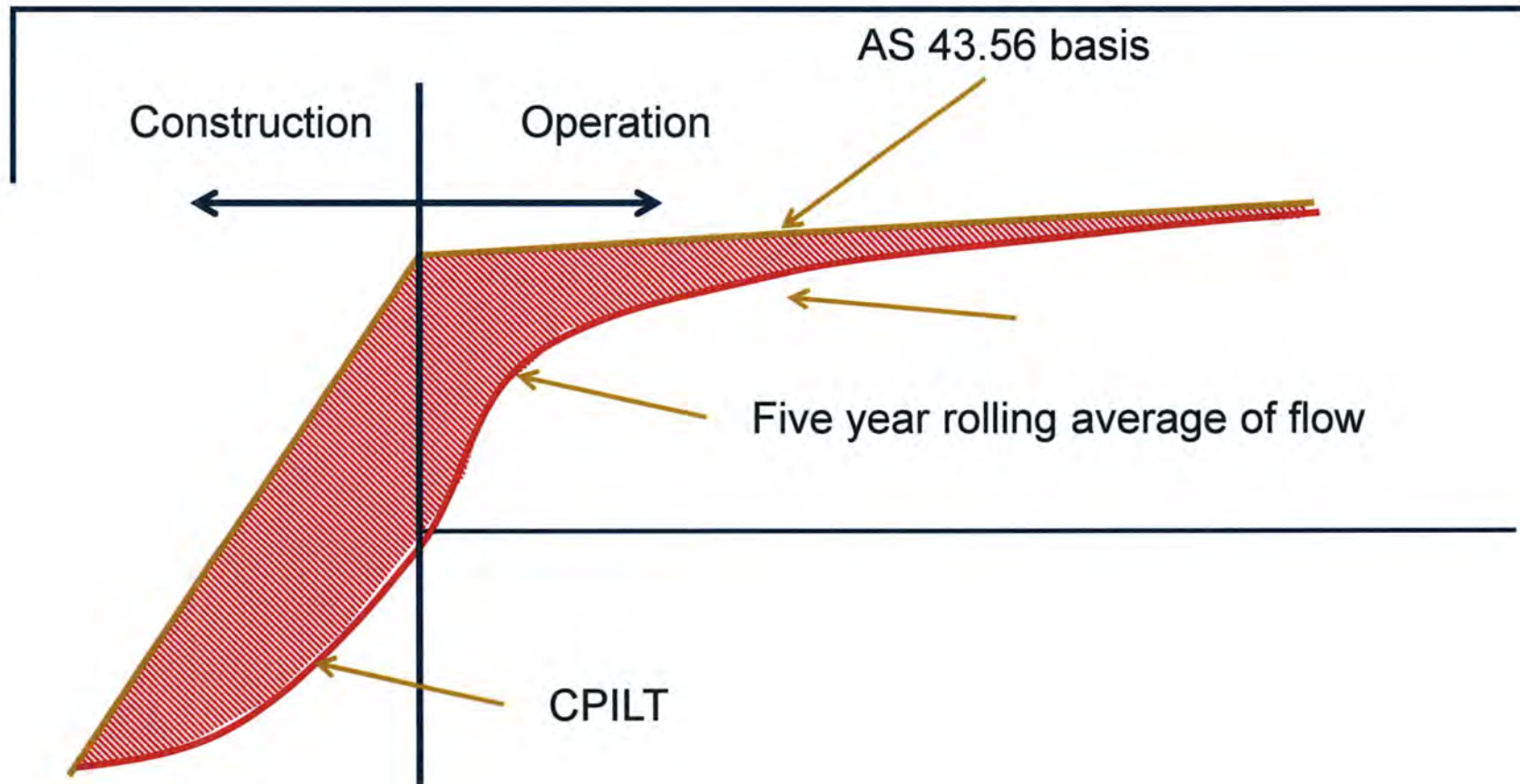
OPILT Target Payments (millions)*

Year 1	\$	556
Year 2	\$	562
Year 3	\$	567
Year 4	\$	573
Year 5	\$	578
Year 6	\$	584
Year 7	\$	590
Year 8	\$	596
Year 9	\$	602
Year 10	\$	608
Year 11	\$	614
Year 12	\$	620
Year 13	\$	626
Year 14	\$	633
Year 15	\$	639
Year 16	\$	645
Year 17	\$	652
Year 18	\$	658
Year 19	\$	665
Year 20	\$	672
Year 21	\$	678
Year 22	\$	685
Year 23	\$	692
Year 24	\$	699
Year 25	\$	706
Target	\$	15,700



*Actual payment amount will vary as actual flow rate with 5 year averaging varies from project design flow

Conceptual Project Benefits from PILT Target Payments



Schematic, not to scale

OPILT Target Payment Components yet to be Determined

- Volume and timing for setting design rate
- Flow rate measurement based on Mcf (thousands of cubic feet) or mmbtu (millions of British Thermal Units)
- Measurement location taken at each component (GTP, Pipeline, LNG) individually or one location for entire project
- Measurement taken at the inlet or the outlet of project components

Next Steps for MAGPRB

- Provide recommendations on proposed structure and target amounts
 - CPILT
 - OPLT
 - Provide recommendations on allocation and disbursement of payments among State and local jurisdictions
 - Drafting 2015 MAGPRB Annual Report
 - Recommendations on legislation
-



SB100

Presentation to Senate Community & Regional Affairs

April 14, 2015

Randall J. Hoffbeck, Commissioner
Alaska Department of Revenue



Components of Property Tax that need to be Considered

- Impact Payments during the construction period
- **Durable and predictable property tax payments during operational period**
- Distribution of revenues between Government entities

Initial Feedback from the Municipal Advisory Gas Project Review Board (MAGP Board)

- **Fair**
 - Must be fair and equitable to all stakeholders
- **Clear**
 - Must be easily understood
- **Robust/Durable**
 - Should be able to cope with future changes
- **Unambiguous**
 - Should not be subject to judgment and interpretation
- **Commercially Sound**
 - Must enable the AK LNG project to compete in global markets

Initial Feedback from AK LNG Producers

- **Simpler is better**
 - Fewer variables is preferred
- **Prefer a general property tax formula**
 - Enacted as a law of general application
 - Meets AK LNG Project economic expectations
 - Acceptable to the municipalities
- **Prefer a flow related property tax payment**
 - Unit rate per throughput basis (e.g., ¢/mcf or ¢/mmbtu)
 - Adjusts by known non-variable factors

Formulaic Interpretation of Initial Feedback

$$\left(\text{Actual Cost} \times \left(\frac{\text{Actual Gas Flow}}{\text{Design Throughput}} \right)^n \times \frac{\text{Year (n) Index} - y}{\text{Year (0) Index}} \times 20 \text{ mills} \right) \times \text{Adjustment Factor}$$

Additional Feedback from AK LNG Producers

1. Mill Rate

- The proposed LNG plant and terminal (possibly the GTP also) are excluded from the definition of “taxable property” subject to the 20 mill rate under AS 43.56. Mill rates under AS 29.45 are sometimes lower and prevailing rates in the relevant jurisdictions should inform final Mill rate in the LNG (and possibly the GTP) FRPT formulation.

2. Capital Cost

- The Project cost estimated at FEED or FID (Final Investment Decision) in lieu of actual Project cost determined after completion could be adopted for additional simplicity and to remove uncertainty for an FID decision.

3. Depreciation/Obsolescence

- Depreciation/obsolescence are acknowledged features of the current methodology, and a factor should be included in the formula to address them.

4. Flow Adjustment

- The HOA between the parties contemplates payments in lieu of property taxes (PILT) for each property based on a simple unit rate per throughput basis.
- Use of an exponent may detract from the ability to use a single, durable formula for debottlenecking and expansion.
- Flow variations could be dealt with through monthly averaging.

5. Inflation

- Inflation is an acknowledged feature of the current methodology (e.g., replacement cost), but represents a future variability risk. A fixed escalation would remove that risk.

6. Adjustment Factor

- This factor could be viewed as arbitrary. A formula that is sufficiently robust would avoid use of an adjustment factor.

MAGP Board Recommendation (March 13, 2015)

MAGP Board Recommendation (Formula)

$$\left(\text{Capital Cost} \times (1 + e)^m \times \text{Depreciation Factor} \times \left(\frac{\text{Actual Throughput}}{\text{Design Throughput}} \right)^n \times \text{Mill Rate} \right)$$

n = exponent to dampen effect of actual flow
e = annual escalation rate
m = years of operation (startup = 0)

MAGP Board Recommendation (Formula Values)

Capital Cost = FID estimate x 1.1
e = 4% per annum
Depreciation Factor based on 50 year floating life
Actual Throughput = 5 year floating average
n = 1
Mill Rate based on current statutes

Subsequent Feedback from AK LNG Producers

1. Mill Rate

- Mill Rate can be accommodated through other adjustments in the formula

2. Capital Cost

- A cost overrun would damage project economics, so consider a mechanism that doesn't exacerbate consequences of overrun.

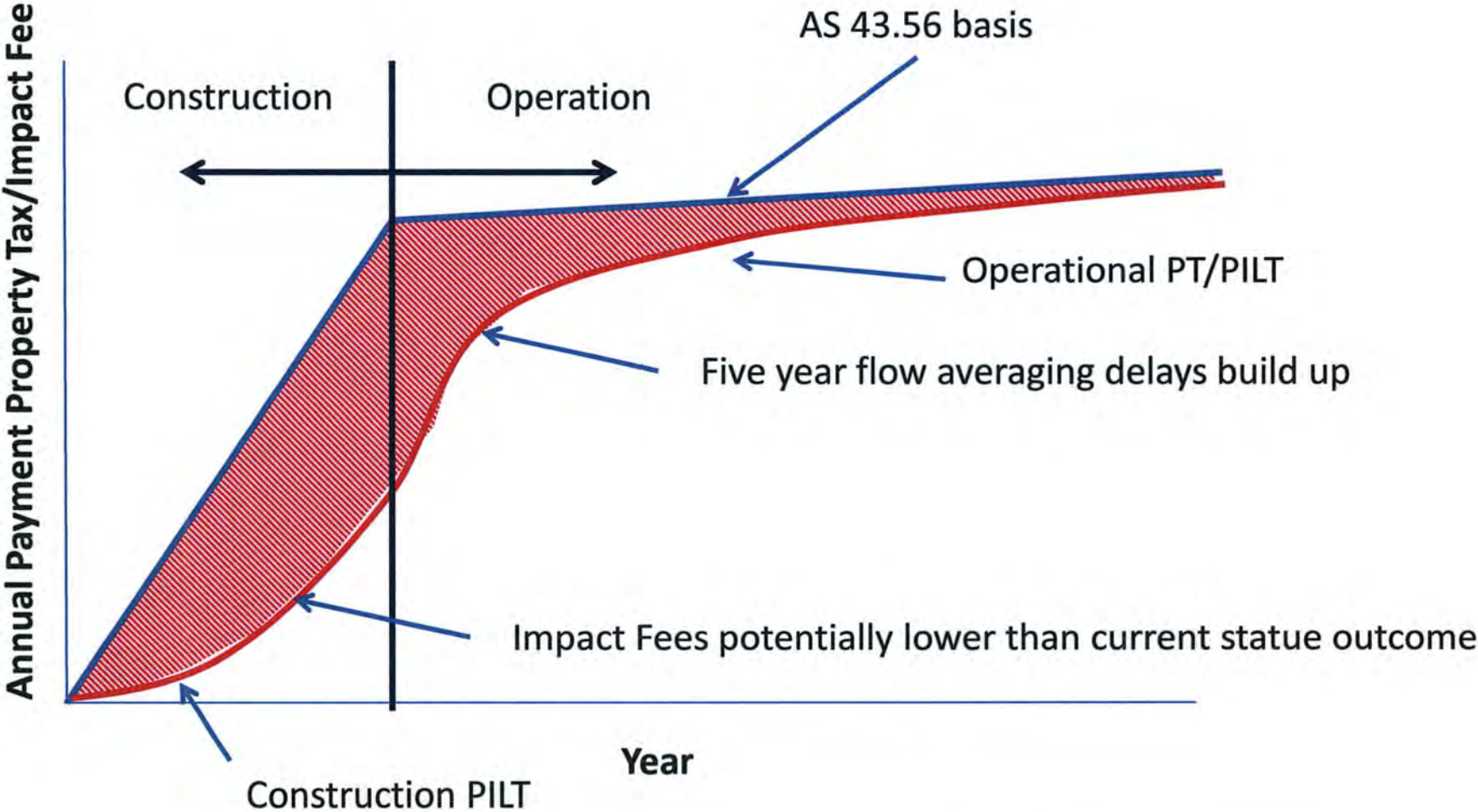
3. Depreciation/Obsolescence

- Instead of using depreciation formula, consider averaging asset value over time (depreciating to a fixed minimum), and applying a single averaged factor.

4. Inflation/Escalation

- Consider slope (i.e., lower initial PT, with discount factor applied)

Potential Project Benefits



**Schematic, not to scale, representative of one of a number of potential outcomes*

SB 100 Recommendation

$$\left(\text{Original Cost} \times \text{Inflation Factor} \times \text{Depreciation Factor} \times \left(\frac{\text{Actual Throughput}}{\text{Design Throughput}} \right) \times 20 \text{ Mills} \right)$$

Original Cost = Fixed by project specific data/fiscal agreement

Inflation Factor = Fixed by fiscal agreement

Depreciation Factor = Fixed by fiscal agreement

Actual Throughput = Operational measurable

Design Throughput = Fixed by project specific data

Mill Rate = Fixed by Statute

THANK YOU

Please find our contact information below:

Randall Hoffbeck

Commissioner

Alaska Department of Revenue

Randall.Hoffbeck@alaska.gov

(907) 465-2300



dor.alaska.gov

Hypothetical PILT distribution between municipalities and state

				27%	73%		
				Municipalities	State of Alaska		
\$ 596,000,000							
	PILT Payment				\$ (149,000,000)		
	Statewide PILT Allocation			\$ 75,000,000	\$ (75,000,000)		
		Pipeline Miles	Compressor Stations	Percentage of Totals			
\$ 140,000,000	Pipeline Allocation						
		North Slope Borough	183	2	23.02%	\$ 8,701,560	\$ 23,526,440
		Fairbanks North Star Borough	2	0	0.20%	\$ 75,600	\$ 204,400
		Denali Borough	86	1	11.03%	\$ 4,169,340	\$ 11,272,660
		Matanuska-Susitna Borough	179	2	22.80%	\$ 8,618,400	\$ 23,301,600
		Kenai Peninsula Borough	50	0	5.00%	\$ 1,890,000	\$ 5,110,000
		State of Alaska	304	3	37.95%		\$ 53,130,000
\$ 171,000,000	GTP and Feeder Pipeline Allocation						
		North Slope Borough			100.00%	\$ 46,170,000	\$ 124,830,000
\$ 285,000,000	LNG Plant Allocation						
		Kenai Peninsula Borough			100.00%	\$ 76,950,000	\$ 208,050,000
						\$ 221,574,900	\$ 225,425,100

ASSUMPTIONS - Pipeline mileage, compressor station locations, % cost estimates subject to change

Original construction cost for total project, \$55 billion:

LNG plant and marine facility, \$25 billion

North Slope gas treatment plant and Point Thomson pipeline, \$15 billion

Main pipeline and compressor stations, \$15 billion

Compressor stations (eight initial stations) represent 20% of the construction cost of the pipeline component of the Alaska LNG project (42-inch line)

PILT calculations as per state/producers negotiated formula presented to the municipal advisory group Sept. 23, 2015

(Original cost + inflation factor - depreciation x throughput x blended mill levy)

PILT calculations and municipal shares based on assumed blended levy of 13.75 mills

Allocations of PILT revenues:

50:50 split of revenues after accounting for State PILT payment and Statewide allocation

Projected PILT revenues are for eighth year of operations

(Due to the five-year rolling average for actual throughput in the PILT calculation, the eighth year could be the first year under the formula to reflect full operations – assuming three years for phased start-up of the three liquefaction trains and three gas treatment plant trains.)

(SOA/DOR) 12-14-15



THE STATE
of ALASKA
GOVERNOR BILL WALKER

Department of Revenue

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February 17, 2016

The Honorable Click Bishop
Chair, Senate Community and Regional Affairs Committee
State Capitol Room 115
Juneau AK 99801

Senator Bishop:

Thank you for the opportunity to present to the Senate Community and Regional Affairs Committee. Several questions were asked of the Department of Revenue in the hearing on SB 100 held Thursday, January 28, 2016. These questions are reprinted here in italics and the responses from the Department of Revenue follow.

1. *Is the State's interest in the AKLNG project exempt from federal income taxation? (MacKinnon)*

Currently the States interest ownership through AGDC is exempt. However as the project progresses with the State being a 25% owner and the remainder owned by private taxable entities the future tax exempt status is an open question. DOR, in coordination with AGDC, is currently formulating a formal request for a ruling by the IRS on whether the Alaska Gasline Development Corporation (AGDC) will be subject to federal income tax on its Project related revenues. That request cannot be submitted until the commercial agreements for the Project are finalized as the Project commercial structure will be a required element for IRS review.

2. *How much of the AKLNG project is on State land? (MacKinnon)*

Since the premise of the hearing was property tax and PILT, I am assuming that the question primarily referred to State taxability rather than the ownership of the land. The Alaska LNG Gas Treatment Plant (GTP) and two feeder pipelines from Point Thomson and Prudhoe Bay, estimated to cost approximately \$15 billion or about 27.3 percent of total project capital expense, will be located 100 percent within the North Slope Borough.

The Alaska LNG main gas pipeline will have an estimated 304 miles (37.8 percent) of its total length outside of organized boroughs and municipalities (State-only property tax). Of the eight compressor stations planned for the main gas pipeline, three of the eight (37.5 percent) will be located outside of organized boroughs and municipalities (State-only property tax). The main gas pipeline and compressor stations component of the Alaska LNG project 42-inch line are estimated to cost about \$15 billion (27.3 percent) of total project capital expense. Of the estimated \$15 billion, the eight initial compressor

stations represent 20 percent of that cost, or about \$3 billion.

The project's LNG liquefaction plant, storage and loading facilities, estimated to cost approximately \$25 billion or about 45.5 percent of the total project capital expense, will be located 100 percent within the Kenai Peninsula Borough.

3. *What is the gas price per Mcf in the model? What gas price does the Project have to realize to break even after payment of the Payment in Lieu of Tax (PILT)? (MacKinnon)*

Breakeven price for the Alaska LNG Project includes several cost streams in addition to the PILT. Many of the estimates for these cost components are in development or are unknown at this point in time (i.e. for Project financing the stakeholders will need to survey the financial markets closer to final investment decision). Breakeven price is most sensitive to project capital costs and cost of capital; breakeven prices will ultimately differ for each of the stakeholders as each stakeholder may finance their portion of the project differently. While the PILT payments make up a portion of the breakeven price, it is not expected to be a driving factor in a go or no go decision.

4. *How much of the 25 percent State share is the property tax? (Stedman)*

Property tax makes up no part of the calculation of the State's ownership interest in the Alaska LNG Project. The State's ownership share is expected to be approximately 25 percent, consistent with the sum of Royalty in Kind (RIK) and Production Tax as Gas (TAG) as a percentage of the total gas supply for the Project.

5. *How do other jurisdictions do property tax payments for this type of project, such as British Columbia? Do they use impact payments, PILTs, traditional property tax, or something else? (Stedman)*

It is difficult to benchmark property tax systems and community impact payments around the world. Different jurisdictions emphasize different responses to impacts. Some governments focus on quantitative measurements of mitigation measures and others are satisfied with more qualitative benefits as compensation. Some governments ask for fixed-fee payments others ask for per-unit payments. In general, the guiding principle for community impact mitigation is to compensate local governments for the impact of resource development on local land and livelihoods and to enable local governments to share in the benefits flowing from the development of their land.

In British Columbia property tax is payable on an annual basis by owners of real property. Property tax is based on the assessed value of the property, as determined by the BC Assessment Authority, and the property tax rate. Property tax rates are determined by the municipality in which the property is located based on the classification of the property (i.e., the asset class).¹

The 2013 municipal tax rates for Prince Rupert and Kitimat were set at approximately \$33.26 and \$63.74, respectively, per \$1,000 of assessed value for "major industry" property (class 4B in Prince Rupert / class 4 in Kitimat). Based on these rates, the annual

¹ KPMG LLP, 2014, Insights and Update on Proposed BC LNG Tax Regime.

municipal tax cost in Prince Rupert and Kitimat would total approximately \$33.3 million and 63.7 million, respectively, for each \$1 billion of assessed value.

The proposed Kitimat LNG Terminal Project is a co-venture between Shell Canada, PetroChina, Korea Gas, and Mitsubishi. The project could cost up to \$40 billion and would initially consist of two processing units called trains, each able to produce 6.5 MTA of LNG.²

It is expected that the introduction of LNG activities to these municipalities will cause a significant reduction in municipal tax rates for all taxpayers as the total annual tax collection at current rates would far exceed municipal budget requirements. Nonetheless, agreements must be reached between the communities and the LNG proponents to ensure the LNG industry's share of the municipal tax burden is fair and reasonable.

WCC LNG is a proposed project to develop and operate a liquefied natural gas (LNG) export facility at Tuck Inlet in Prince Rupert, British Columbia. Exxon Mobil Corp. and their partners plan to spend up to \$25 billion on the project terminal facility, similar in cost to the LNG and terminal facilities for the ALKLNG project. WCC LNG project partners will pay the City of Prince Rupert \$18 million over two-years. WCC LNG has already paid a \$1 million non-refundable deposit and will pay another \$7 million within 30 days of zoning of the site and an additional \$10 million at a later date.³

Woodfibre LNG is a smaller, \$1.7 billion capital cost, natural gas liquefaction and export facility located at a former pulp mill site, Squamish, B.C. Woodfibre LNG is proposing to pay \$2 million a year in property tax to the District of Squamish when the facility begins operations, and increase that amount 2.5 percent a year, up to \$3 million a year, in property tax. More work needs to be done on property tax, but we felt it was important to make a proposal given the level of community interest in potential property tax revenue from Woodfibre LNG. In addition, as part of its export approval Woodfibre LNG committed to developing a local hiring strategy, local training strategy, and regional procurement strategy.³

6. *Could DOR provide committee with any examples of other jurisdiction tax systems that the Producers provided to the project/Commissioner, if not confidential? (Bishop)*

After discussions with the producers they have indicated that the contracts they have with other jurisdictions are confidential business sensitive documents which are not available for public release.

7. *Please provide more detail on project economics, State revenue value stream, etc. and how AKLNG property tax fits in with it, how large a portion of the value stream is property tax? (Stedman)*

State revenues from the AKLNG project include royalties, production tax, property taxes, and State corporate income taxes. Property taxes are proposed to be based on the

² Kane, Laura, 2016, LNG Canada gets permit for export facility in Kitimat, B.C.; The Globe and Mail.

³ Gaffney Cline & Associates, 2015, LNG Community Impact Mitigation, Global Overview, presentation to the Municipal Advisory Gas Project Review Board on July 1, 2015.

throughput in the AKLNG project, and are a more certain revenue stream for the State than the other three (royalties, production tax, and State corporate income tax). The other three revenue streams for the State from AKLNG - royalties, production tax, and State corporate income tax – are dependent on LNG prices, volumes and project costs including capital cost, operating costs and financing costs. Of these variables, LNG prices are the largest driver of State revenues. Assuming LNG prices that are indexed to crude oil, and a long-term oil price range of \$40-80/bbl (2015\$), property taxes as a percentage of the total expected State revenues can range from 15 percent to over 80 percent. As oil prices fall, property taxes becomes a larger percentage of the total State revenues, conversely as oil prices rise, property tax becomes a smaller percentage of the total State revenues.

8. *Does inclusion of the agreement with the Producers on property tax in the Fiscal Agreement prevent the legislature from appropriating the PILT revenues for the 25 year term of the Fiscal Agreement? (Stedman)*

The Fiscal Agreement, as currently anticipated by the State, would only apply to the agreed upon fixed Construction-related PILT (CPILT) amount and the negotiated Operations-related PILT (OPILT) target amount and calculation process. The Legislature will retain authority to appropriate and allocate the property tax revenues received from the Project.

Please let me know if you have additional questions or need clarification on any of the answers above.

Sincerely,



Randall J. Hoffbeck
Commissioner

From: Persily, Larry
Sent: Friday, February 12, 2016 3:52 PM
To:
Cc:
Subject: LNG project impact aid in British Columbia

Senator,

I did some research after the Senate CRA hearing Jan. 28 on property taxes and impact aid for the Alaska LNG project. Sen. Stedman had implied at the hearing that British Columbia had negotiated an impact act PILT in lieu of property taxes for LNG projects. But that's not really the case. I talked Feb. 10 with tax officials in British Columbia.

There are some impact aid funding agreements between B.C. municipalities and First Nations and project sponsors. But they are **in addition to** any property taxes, not in lieu of taxes. The impact aid funds are separate side agreements between the local governments and tribes and project sponsors -- there is no provincial role whatsoever.

The one sort-of-kind-of exception to the above is Port Edwards, a small community of about 500 people near Prince Rupert, and site for one of the proposed B.C. LNG projects. Because Port Edwards is so small, and the LNG property tax would be so large, the B.C. parliament passed a special law that allowed Port Edwards to negotiate a PILT for the LNG project (construction and operations). Which the municipality did negotiate, but no funds yet -- as there is no project yet. And the law applied only to Port Edwards.

The province has negotiated, however, what it calls a Project Development Agreement with one LNG proponent (Pacific North West LNG, proposed for near Prince Rupert), and has offered to negotiate similar deals with other developers. But the PDAs, as they are called, deal only with the province's new LNG income tax, natural gas tax credits, B.C.'s carbon tax, and any LNG-directed gas-emissions regulations. The PDA does not touch property taxes.

Property taxes in British Columbia are complex, but interesting:

- There is a province-wide property tax assessment, called a "school tax," although it gets blended in with the province's "consolidated revenue fund" (much like our general fund). Everyone pays this tax.
- And the province sets and collects a "rural area" property tax for unincorporated (non-municipal) areas.
- Each municipality gets to set its own property tax.
- Regional boards set a property tax rate for regional hospital districts.
- And B.C. has something called "regional districts," which have waste management authority and local service roads and some other powers not granted to municipalities. These regional district boards also set a property tax.

As in Alaska, property taxes start the year a project begins construction and site work gets underway. The assessed value then ramps up each year.

The B.C. tax officials noted that "major industry class" property (such as an LNG plant) is allowed a 4% annual depreciation deduction, which, they said, probably is not so good, as the property eventually will produce little

revenue but the municipalities and hospitals will still need the money. They said this is a real problem looking out 20 years for the multibillion-dollar LNG projects -- one which no one has yet answered.

I just wanted to share this with you. I'd be happy to explain the B.C. property tax structure and impact aid, and the Stranded Gas Act 2006 impact aid fund, at any time you thought it would help the committee.

Larry

From: Persily, Larry
Sent: Friday, February 05, 2016 11:07 AM
To:
Cc:
Subject: LNG project impact aid

Senator,

After Sen. Stedman raised the issue at last week's Senate CRA hearing of the negotiated impact aid under Gov. Murkowski's proposed Stranded Gas Development Act contract in 2006, I did some research. Yes, the producers in 2006 agreed to \$125 million total in construction PILT, spread over several years. A far cry from the \$800 million negotiated this time around. But, that doesn't mean \$125 million was the right number -- it's just what the administration settled for in negotiations. A few points lawmakers might want to consider:

The big difference is that the \$125 million construction PILT was based on a \$7 billion project; today's \$800 million is based on a \$55 billion project. (The SGDA project was \$21 billion in total, but only \$7 billion in Alaska as most of the pipe was in Canada.)

The SGDA project was all pipe in Alaska to the Canadian border; no LNG plant or marine terminal construction impacts.

The \$125 million was 2006 dollars. The \$800 million assumes 2019-2024 dollars.

The \$125 million number does NOT include an estimated "*\$284 million in new state highway and port projects that will be required in advance of gas pipeline construction.*"

The \$125 million number came from a 2004 report by Information Insights, which some thought soft-pedaled some of the local community impacts during construction.

Just for the sake of a math exercise, if you take a \$125 million construction PILT on a \$7 billion project in 2006 and “ramp it up” (times eight) to a \$55 billion project in 2019-2024, you are at \$1 billion, not even accounting for inflation. The \$800 million impact aid fund today doesn’t look so out of whack.

Larry

MUNICIPAL ADVISORY GAS PROJECT REVIEW BOARD

ANNUAL REPORT 2014

(Final version submitted March 2015)

This report is available exclusively online and can be downloaded at the Board's website provided by the Department of Revenue:

<http://dor.alaska.gov/MunicipalAdvisoryGasProjectReviewBoard.aspx>

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PREAMBLE

The Municipal Advisory Gas Project Review Board (MAGP Board), formed as a consequence of Administrative Order No. 269 on March 25th, 2014, is charged with developing a framework to evaluate the local governmental options that could be adopted to address and mitigate the impacts of new infrastructure associated with the development of the State's North Slope natural gas resources. The MAGP has recently been reviewing information relating to a specific gas project, the Alaska LNG Project.

The MAGP Board consists of twelve members who are appointed by the Governor of the State of Alaska. Members include the Commissioners of Revenue, Natural Resources and Commerce, Community and Economic Development; Mayors of the North Slope Borough, the Fairbanks North Star Borough, the Matanuska-Susitna Borough, the Denali Borough, the Kenai Peninsula Borough, and the Municipality of Anchorage. In order to provide representation for other areas of the state the Mayor of the Northwest Arctic Borough, the Finance Director for the City and Borough of Juneau, and the Energy Coordinator for the Southeast Conference were also appointed to the board.

The first meetings of the MAGP Board were on August 5th-6th, 2014, and have been held regularly since. Board members attended presentations on selected information related to the status of the Alaska LNG Project by company representatives, consultants contracted with the State, and the Office of the Federal Pipeline Coordinator. Certain documents from the MAGP Board meetings can be found on the following link:
<http://dor.alaska.gov/MunicipalAdvisoryGasProjectReviewBoard.aspx>
The work of the MAGP Board will be relevant to a range of gas commercialization options.

This report reflects the MAGP Board's preliminary recommendations regarding structural options to establish the amount and means of providing value to the State and local communities to mitigate the costs to these governments of supplying support to the project both during construction and subsequently during the project's operational phase. Due to the change in administration and substantial turnover in board membership, this report is submitted as an interim document. A final version will be approved and submitted in early 2015.

The MAGP Board supports continued work to advance a viable gas commercialization project. Should the Alaska LNG Project not come to fruition, the MAGP Board urges that other projects be explored as alternative means of supplying communities with long term, stable supplies of lower-cost energy.

One of the major issues surrounding the construction and commercialization of North Slope natural gas is determining the form and size of total government "take" for municipalities and the State.

OVERARCHING PRINCIPLES THAT SHAPE THE GOVERNMENT TAKE METHODOLOGY

The state laws concerning the taxation of oil and gas property in Alaska are Alaska Statutes 29.45 (Municipal Property Tax) and 43.56 (State of Alaska Oil and Gas Exploration, Production and Pipeline Transportation Property Taxes). While the MAGP Board may not share a common view on certain issues, nonetheless the Board does agree that any recommendations for changes to the tax structure in AS 29.45 and/or AS 43.56 should be based on a set of principles. These principles include:

- 1) Municipal governments and the State must be able to maintain their financial capacity to address impacts throughout the life of the project.
- 2) Industry project leaders should be allowed to maintain the relative competitiveness of their project compared to other projects.
- 3) There should be opportunities for all Alaskans to benefit from the project.
- 4) Any property tax or alternative tax system should be predictable for both investors and municipalities.
- 5) Revisions to AS 29.45 or AS 43.56 should be limited only to the Alaska LNG Project under consideration. Those revisions shall not include any property that is taxable under AS 29.45 or AS 43.56 prior to construction of the Alaska LNG Project. Furthermore, no property taxed under AS 29.45 or AS 43.56 prior to construction of the Alaska LNG Project should receive a tax deferral or a tax exemption under the contract.
- 6) Revenues received by municipalities and the State through any alternative property tax methodology to the existing property tax methodology set forth in AS 29.45 or AS 43.56 must realize revenues of no less than 20 mils of the full and true value of the Alaska LNG Project.
- 7) Any revisions to AS 29.45 or AS 43.56 relevant to the Alaska LNG Project should not disadvantage the competitiveness of the Alaska LNG Project under consideration.
- 8) Reflecting the statewide nature of a large gas project, revenues from the Alaska LNG Project should be shared by all communities across Alaska, and not just communities expected to have ongoing impacts from the project.
- 9) Actual impacts on communities and the State, incurred during the construction and operation of the Alaska LNG Project, should be paid by the Alaska LNG Project. The MAGP Board recognizes that the actual impacts are not commensurate to the length of the pipeline or the value of taxable property within a community's boundaries. Instead, impact payments should be based on the actual community impacts.

OPTIONS FOR FISCAL TERMS

With the above principles in mind, the MAGP Board explored options for structuring government take methodologies, recognizing that there are several alternative fiscal structures under which municipal take may be determined. Below is a list of those options. While the MAGP Board does not endorse any one particular choice, it does have recommendations on necessary characteristics that some of the options need to have to ensure an equitable outcome for all stakeholders.

- 1) **The Alaska LNG Project could be taxed under AS 43.56**
- 2) **The Alaska LNG Project could be taxed under AS 29.45**
- 3) **PILT:** The State and municipalities could agree to a PILT contract through negotiations. A “payment in lieu of taxes” or PILT for a gas project is statutorily authorized under AS 29.45. The statutes also allow the municipalities to negotiate a PILT collectively. The State could serve as a facilitator in those proceedings should this avenue be pursued; however, if the State does facilitate the PILT negotiations, the municipalities must be allowed to participate and concur with the terms of any PILT.
- 4) **Appropriation:** If PILT payments are to be paid in lieu of property taxes during operation of the Alaska LNG Project, payments should be made directly to municipalities, and not subject to legislative appropriation.
- 5) **Throughput Based Calculation:** This method would take the full and true value (which could potentially be based on the original cost of construction adjusted upward for inflation and downward for depreciation) and divide it by the throughput of natural gas molecules through the pipeline. This potentially leads to more predictable value for every thousand cubic feet (mcf). These calculations still need to be determined for the future. Appraisal methods will be further discussed and defined by the report.
- 6) **Municipal Equity Share:** Municipalities could be provided with an equity share in the Alaska LNG Project infrastructure. This creates consistent and predictable revenues for communities.

OTHER RECOMMENDATIONS

- A. Access to Alaska LNG Project Economics:** As referenced earlier, the MAGP Board support efforts to further gas commercialization, including the Alaska LNG Project. To that end, local governments need to be informed about a gas project's economics to determine how their choices of government-take methodologies impact the competitiveness of the Alaska LNG Project under consideration. However, the MAGP Board on behalf of the communities they represent must be able to maintain adequate transparency to assure their constituents that their local government is striking a fair balance. MAGP Board members acknowledge that more work is needed to ascertain more precisely the type of information that will need to be maintained in confidence to protect the viability of a gas project.
- B. PILT/Impact Payment Team:** An alternative to property taxes is a PILT. A PILT would calculate a set of payments and could be subject to fewer adjustments than annual property tax assessments. The communities most affected by the adoption of a PILT are those local jurisdictions that would cede taxing authority, and these same communities would feel the greatest impacts from the development and operation of the Alaska LNG Project. Therefore, the MAGP Board recommends the formation of a PILT/Impact Payment Team if this option is pursued. A PILT to a municipality ceding taxing authority should not be subject to legislative appropriation.
- The team could consist of those local government members of the MAGP Board, who represent communities directly impacted by the adoption of a PILT (i.e., those jurisdictions that will be ceding taxing authority); and two (2) members appointed by the Governor. The team would meet and deliberate the terms of a proposed PILT, and agree to a determination of impact payments dealing with the Alaska LNG Project. Decisions would be reached by majority vote. The PILT/Impact Payment Team shall offer its recommendations to the MAGP Board for its consideration.
- C. Conditions on Adopting PILT:** In the event that a PILT system is acceptable to municipalities, the PILT should be adjusted for inflation. The term of the PILT should be carefully considered and perhaps limited to the initial term of the gas contracts. There should also be provisions for inclusion of qualified new communities to the PILT structure.
- D. Payment During Interruption:** In the event of an interruption during operation of the Alaska LNG Project post-construction, continued PILT payments, or another commensurate form of payment, should be made to communities during that time period.
- E. Local Control:** Nothing in these recommendations, or state contracts, should be

construed to prohibit a municipality from making its own individual decision to govern their tax bases or negotiate separate agreements on infrastructure, other than as agreed to by a municipality in a PILT agreement.

- F. Contractual Limitation of Scope:** A municipality should never be coerced into ceding its taxing authority or into agreeing to the assessment of taxable property on any basis other than on the full and true value used to tax other taxpayers. The MAGP Board strongly supports prohibiting the targeting of a municipality's tax provisions within any of the contracts for a specific gas project. Likewise, the MAGP Board agrees that a gas project designed to benefit all Alaskans and their communities, should not be subject to blockage because of one individual community.
- G. Dual Use Facilities:** Contracts for a gas project should clarify how dual use facilities will be taxed.

IMPACT STATEMENTS

Assessing Impact Payments: Alaska LNG Projects designed to move gas in interstate and international commerce will be permitted by the Federal Energy Regulatory Commission under the Natural Gas Act, Section 3. This will require an Environmental Impact Statement (EIS) that assesses, among other matters, the socio-economic impacts to communities from the project. Those documents, and the processes associated with them, will be authoritative and publically documented. Any effort at this point to assess impacts should consider how to coordinate and/or incorporate those impacts into the FERC Pre-File and EIS processes respectively.

Appropriation: If impact payments are to be paid in lieu of property taxes during construction of the Alaska LNG Project, payments should be made directly to municipalities, and not subject to legislative appropriation.

Tiers: The MAGP Board recommends that there be two tiers of impact payments: direct and indirect payments. Direct impact payments are for those communities that will be affected immediately by the construction of the Alaska LNG Project through the use of municipal services and infrastructure. Indirect impact payments are for communities where the Alaska LNG Project is not an immediate presence in their jurisdiction, but nevertheless indirectly impacts the municipal services (e.g. loss of municipal workforce to the project). Indirect impact payments could be made by the State through a separate fund.

Schedule: Impact payments should be scheduled and paid, regardless of construction schedule or activity. This is critical for communities directly impacted by work stoppages, who require a predictable revenue stream to offset impacts on services. The contract should also include provisions for the extension of construction terms, allowing for overruns.

Local Hire: Wherever possible, the State of Alaska and the Alaska LNG Project should maximize local hire to ensure the employability of the local workforce and to reduce the impacts of an imported labor pool overloading municipal services.

Access to Energy: The State should commit to providing access to energy infrastructure in order to lower the cost of delivered energy for Alaskans. This can occur at off-take points, or other facilities that provide natural gas, or other forms of energy to communities, including through use of the Alaska Affordable Energy Fund (AAEF). The Alaska LNG Project and the State of Alaska should consult with the MAGP Board on the location of off-take points and other facilities that would provide communities with access to energy.

NEXT STEPS: FERC PRE-FILE PROCESS

Interstate/International Gas Projects are subject to many different permits at the federal level. There are two federal agencies whose approval is necessary for the success of the project. One is the Department of Energy, which is responsible for issuing export licenses for countries with free trade agreements, and those without free-trade agreements.

The second federal agency relevant to the Alaska LNG Project is the Federal Energy Regulatory Commission (FERC), which regulates the construction, operation and safety environment of the project. After initiation of the pre-filing process, FERC coordinates the preparation of a single Environmental Impact Statement (EIS), to be used by all federal agencies for their respective permit and authorization services. The basis for the EIS is twelve (12) resource reports that the applicant is required to submit to FERC. The MAGP Board recommends that it stay very active in the drafting of the EIS for any gas project by submitting timely responses to any relevant resource reports and maintaining open lines of communication with FERC and any other relevant agencies. The MAGP Board also recommends that local governments participate in the EIS process on behalf of their respective communities.

Pre-filing is important because the burden is on the applicant to gather data for the EIS and review by FERC. The early identification of potential issues with regard to community concerns, environmental impacts and others during the pre-file process will generally result in a stronger application outcome.

Once the pre-filing process is complete, FERC will then issue a draft EIS. That draft will be open for public comment and review. After the public comment and review process, a final EIS draft is issued. Finally, the FERC commissioners will make a determination as to whether or not to authorize the construction and operation of the project. Without an EIS and FERC authorization, the Alaska LNG Project does not reach the critical Final Investment Decision (FID) phase, which is the stage when the majority of funds for a project are committed and construction begins.

Of the twelve resource books that collectively make up the draft EIS, resource book number five (5) is of the most interest to the MAGP Board. Resource Book No. 5 is the socioeconomic resource report. That book describes the baseline in communities regarding their socioeconomic conditions, and evaluates the socioeconomic impacts of the project as well as what can be done to reduce those impacts. The baseline encompasses everything from employment, housing, school enrollment and government services.

The MAGP Board recognizes that the fiscal impact analysis of any gas project will be crucial in terms of determining the costs associated with an influx of temporary or permanent workers, the duration of their stay, and the use of municipal services. The MAGP Board

therefore reiterates its recommendation to stay very active in the drafting of an EIS.

In the context of the EIS timeline, the Alaska LNG Project has hosted open houses in several communities; twelve (12) open houses were conducted between October and November, 2014. FERC personnel, though not participating, did observe the proceedings. The Alaska LNG Project is in the preliminary front end engineering design (pre-FEED). The estimated cost is between \$400-500 million, encompassing 2014 and 2015. If the project still holds promise after that period, then the project moves into full front end engineering design (full FEED). The estimated cost of that phase is in excess of \$2 billion, and a timeline of two to three years. During that time, the draft resource reports will be submitted, along with agency and community feedback. The final draft of the resource reports would then be made available. Scoping sessions are expected to begin sometime in February, 2015. The MAGP Board strongly recommends having a presence at these scoping sessions and contributing to the information being gathered for the Resource Books and the final EIS.

RESOURCES:

Office of the Federal Pipeline Coordinator: <http://www.arcticgas.gov/>

Municipal Advisory Gas Project Review Board Website:
<http://dor.alaska.gov/MunicipalAdvisoryGasProjectReviewBoard.aspx>

Alaska LNG Project Website: www.ak-lng.com

Alaska Department of Revenue Website: <http://www.dor.alaska.gov>

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Phone: (907) 269-0080

Fax: (907) 276-3338

APPENDICES

Appendix A-1. Municipal Advisory Gas Project Review Board members:

RANDALL HOFFBECK (Chair)

Commissioner, Alaska Department of Revenue

MARK MYERS

Commissioner, Alaska Department of Natural Resources

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CLAY WALKER

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MIKE NAVARRE

Mayor, Kenai Peninsula Borough

DAN SULLIVAN

Mayor, Municipality of Anchorage

CHARLOTTE BROWER

Mayor, North Slope Borough

LUKE HOPKINS

Mayor, Fairbanks North Star Borough

LARRY DEVILBISS

Mayor, Matanuska-Susitna Borough

REGINALD JOULE

Mayor, Northwest Artic Borough

ROBERT VENABLES

Energy Coordinator, Southeast Conference

ROBERT BARTHOLOMEW

Finance Director, City and Borough of Juneau

PILT MODELING ANALYSIS

The following information and analysis is intended to build on the PILT discussion from the February 20, 2015 Municipal Advisory Gas Project Review Board meeting with some high level financial projections and background information around a proposed PILT methodology.

**Department of Revenue
March 2, 2015**

INTRODUCTION

At the Feb 13th MAGPR Board meeting, a methodology was proposed by Commissioner Hoffbeck to set out a possible PILT alternative for the AK LNG project, in place of the current AS 43.56 approach. A review of possible parameters was presented measured against the three criteria of clarity, robustness/durability, and lack of ambiguity. The following parameters were considered to meet these criteria, in the context of an LNG export project:

- Actual cost
- Design throughput
- Actual throughput
- Inflation (against an index measured in year 0 and applied in year n)
- Tax (Mill) rate

By combining these features, an output similar to what would have been derived under AS 43.56 was envisaged, without the incumbent uncertainties in interpretation, especially around Replacement Cost New (RCN), Obsolescence, and/or measuring sales or revenue.

The proposed basic construct of the formula was as follows:

Actual cost x (Actual flow/Design flow rate) x (Inflation index year n/Inflation index year 0) x Mill rate

During the presentation of the methodology, a number of other potential features which were thought to introduce additional ways to track the “Status Quo” comparison with AS 43.56 were set out, including:

- An exponent to reflect the greater capital efficiency of expansion/de-bottlenecking
- A factor to modify the inflation measure, partly to reflect depreciation of the plant

The discussion among the MAGPR Board Members focused on the following areas:

1. Actual Cost. No comments on Actual Cost, which was considered a parameter which could be set based on Front End Engineering Design (FEED), or an audited post construction figure.
2. Actual and Design Gas Flow Rate. The following comments were offered:
 - a. Potential for a floor on actual gas flow rate, to protect against a period of zero flow interrupting Borough funding for essential programs
 - b. An alternative of emergency funding held in Escrow, was put forward
 - c. A 3-5 year rolling average for Actual Gas Flow.
 - d. Query whether the Design Flow Rate should change to reflect significant future alterations to the plant, such as a major expansion (though the formula could also accommodate this)
 - e. Query whether the Design Flow Rate should change during the commissioning phase, as each of the proposed trains is brought into operation.

- f. Exponent for Gas Flow Rate factor. An exponent of 0.45 has been used by the State previously in respect of a pipeline PILT, and 0.65 in respect to additional processing plant.
3. Inflation
 - a. It was noted that FERC use PPI for pipeline tariff escalation
 - b. Further comment from the group suggested that CPI might be a better reflection of costs borne by Boroughs
 - c. A more local index, such as Anchorage CPI was also noted as a possibility
4. Depreciation. Alternatives were considered as follows:
 - a. None
 - b. Introducing a feature which addresses some form of depreciation, or otherwise modifies that inflation aspect of the formula. Three approaches were suggested including
 - i. Included in the equation through a fixed constant reduction to the inflation factor prior to multiplying the factors
 - ii. Introduction of an additional factor into the equation, with a mathematically identical impact to (i) above
 - iii. A separate factor reflecting a rolling depreciation, for example, over a 30 to 50 year forward horizon, resulting in an exponentially decaying depreciation that reduces over time.
5. Mill Rate
 - a. It was suggested that a 20 Mill rate across the board was the most logical application, especially with the objective of avoiding uncertain or variable tax rate setting for the LNG plant, under Kenai Peninsula Borough local ordinances.
 - b. It was noted that distribution of a PILT may not be in proportion to the ratio of capital cost in each borough (partly reflecting impact on a wider set of stakeholders), but that this aspect would be discussed on a future occasion, when the formula mechanism was better defined
6. Economic test for LNG export viability
 - a. It was noted that following review in the context of project economics, an adjustment (X-factor) may be required to enable the project to compete globally, but it was noted that this was not the primary focus of the group in setting methodology.

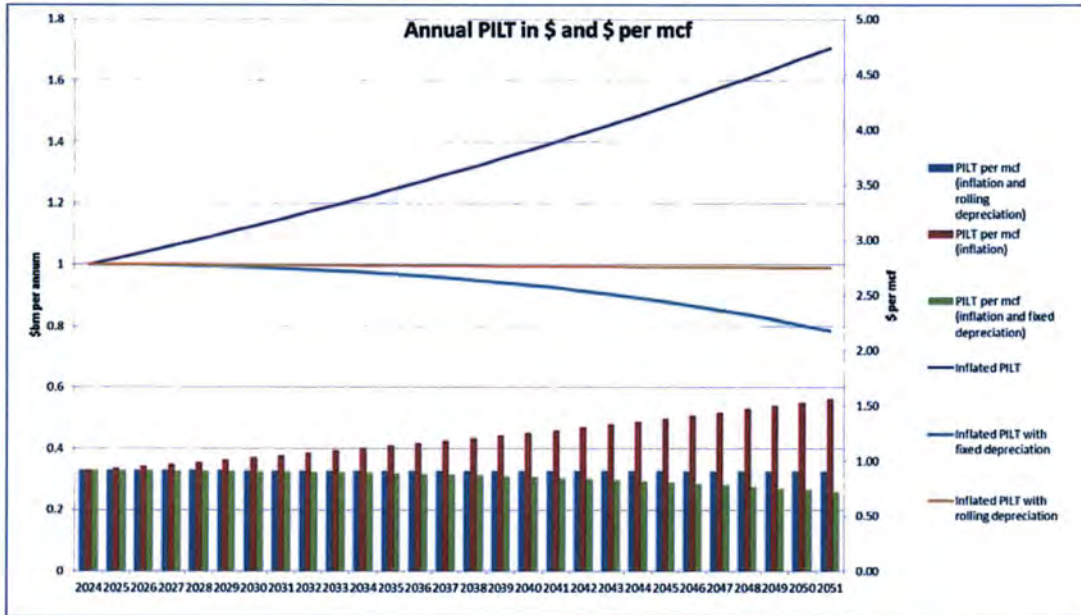
ANALYSIS OF THE FEATURES ABOVE

The illustrations below show the impact of the three approaches discussed above:

- Un-amended inflation
- Inflation combined with a fixed depreciation
- Inflation combined with rolling depreciation over a fixed horizon

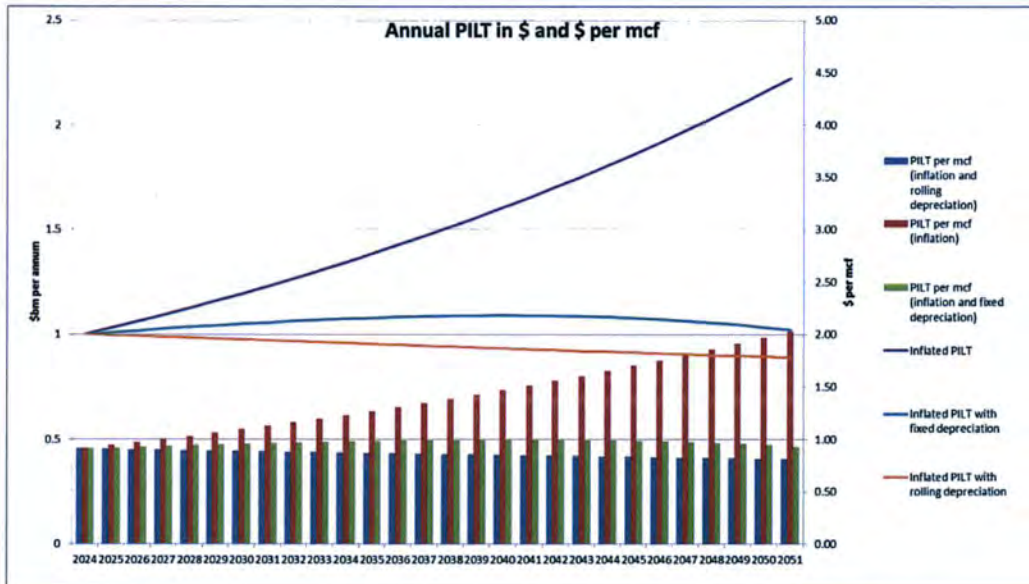
DEPRECIATION – Case 1

This case indicates the outcome with a 2% inflation rate, a fixed 2% depreciation per annum, or a 50 year rolling depreciation. As can be seen below, the rolling horizon compensates almost exactly for inflation, whereas the fixed depreciation starts to diverge downward in the later years modelled.



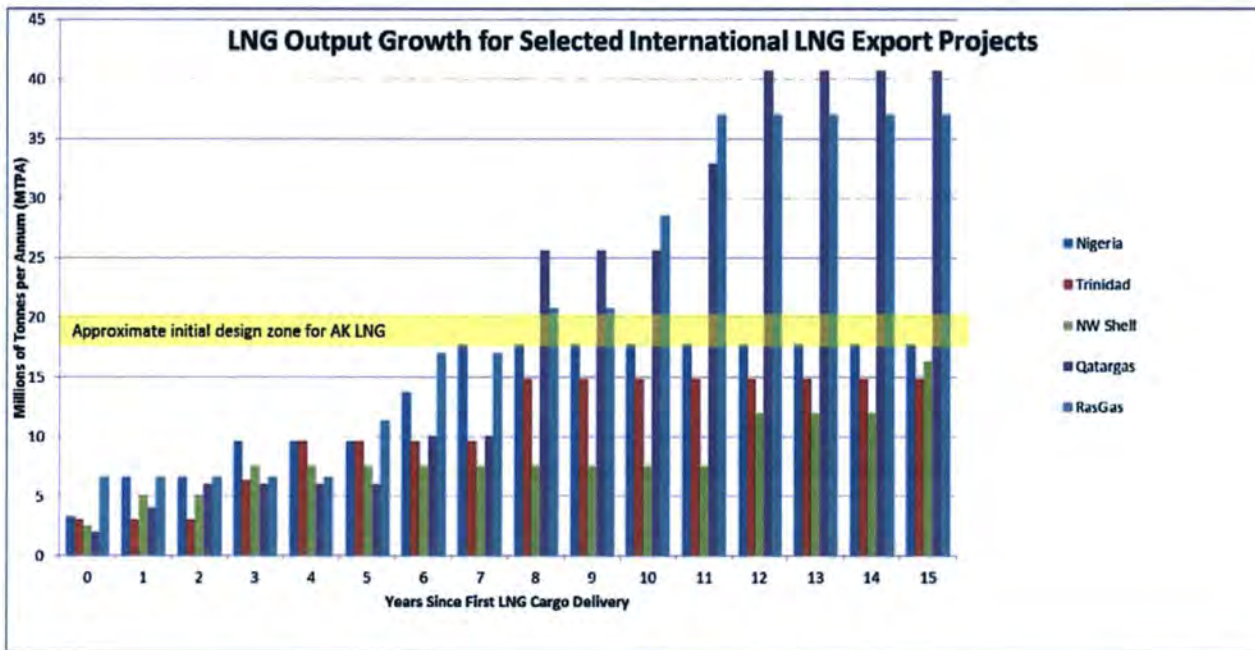
Case 2

In the event that inflation is higher (3%) and we assume a 30 year rolling depreciation, but the fixed depreciation is maintained at 2%, both approaches produced a more or less static PILT over the period modelled:



IMPACT OF GAS FLOW EXPONENT

Before considering the impact of the gas flow exponent, it is useful to look at how a typical LNG project matures over the first decade or so of its life. The chart below examines the way in which a number of LNG export projects in various locations around the world have expanded over the first 10-15 years of their existence, typically with the addition of extra LNG trains (the term for a unit of production characterized by refrigeration, heat exchangers, and sometimes storage tanks). The data below reflects historical LNG capacity growth for Nigeria LNG, Australian North West Shelf Project, Qatargas and Rasgas (both projects are in Qatar), and Trinidad.



The other way in which LNG output is typically boosted is through so-called “de-bottlenecking” which is a technique for making the liquefaction trains more efficient by amending the design of critical features in a way that optimizes the overall plant, and how its components operate together. This typically happens after an LNG train or trains have been operating for a few years, and an understanding has been gained as to which components need to be modified, redesigned, or sometimes replaced.

A particularly noteworthy de-bottlenecking was carried out on the Qatargas I, three train plant, which first delivered LNG in December 1996. The original 3 trains had a design capacity of 2 million tonnes each, but after a major debottlenecking project completed in 2005, output was raised to 10 million tonnes (combined) for the three trains.

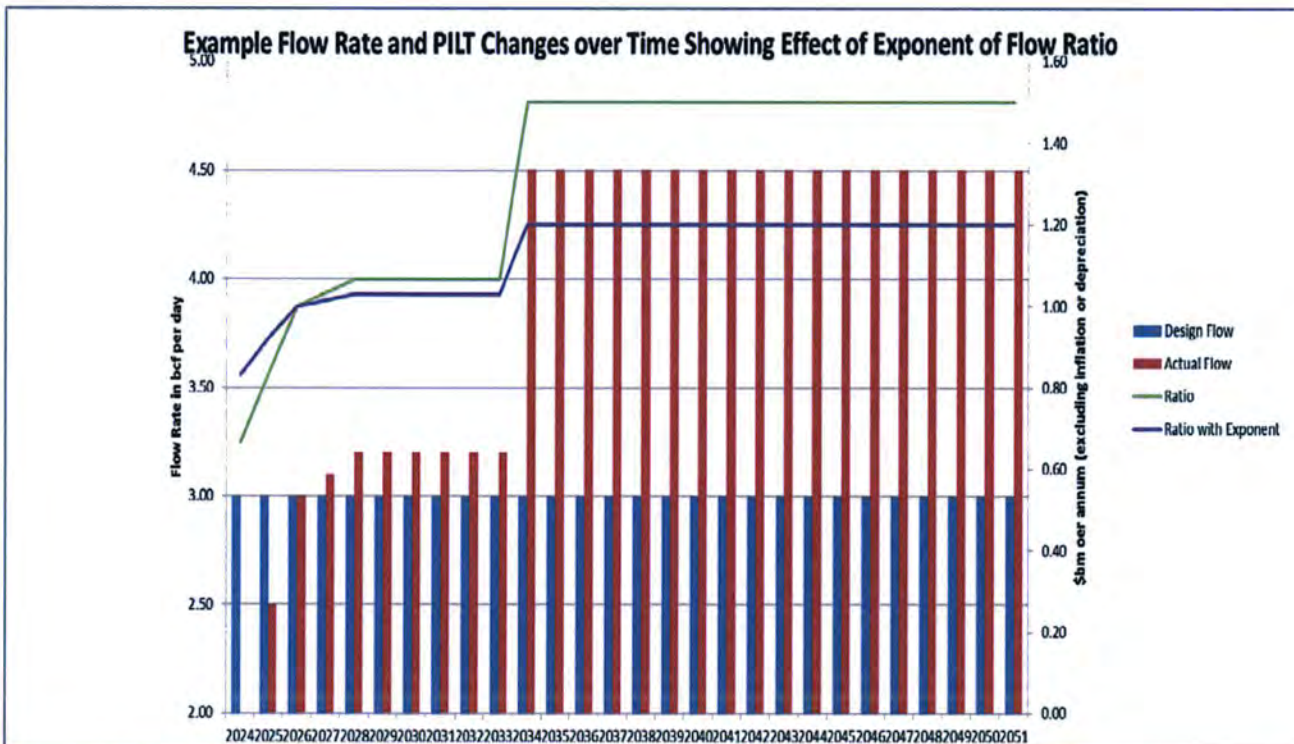
However, applying this historical data to what might be seen in Alaska has a number of major uncertainties associated with it, particularly the following:

- LNG technology has developed considerably since many of these example projects have commenced production, and train sizes are now typically two to three times bigger than those that were constructed in the projects cited above.
- The AK LNG project has a much larger initial design basis, than any of the projects noted above.
- Unlike Qatar, for example, with the very large proven reserves associated with the giant North Field (the largest conventional gas reservoir in the world), the natural gas resource in Alaska, while substantial, has not yet been proven up sufficiently to indicate whether additional gas production could be warranted.

However, with these provisos in mind, a growth trajectory has been modelled below, based on the following assumptions:

- First gas in 2024, fully commissioned in 2026 with a design flow of 3bcfd (a combination of State gas and LNG exports)
- Debottlenecking between 2026 and 2028, giving rise to a 7% increase in gas deliveries
- Addition of an additional train in 2034, with gas flow rising to 4.5 bcfd

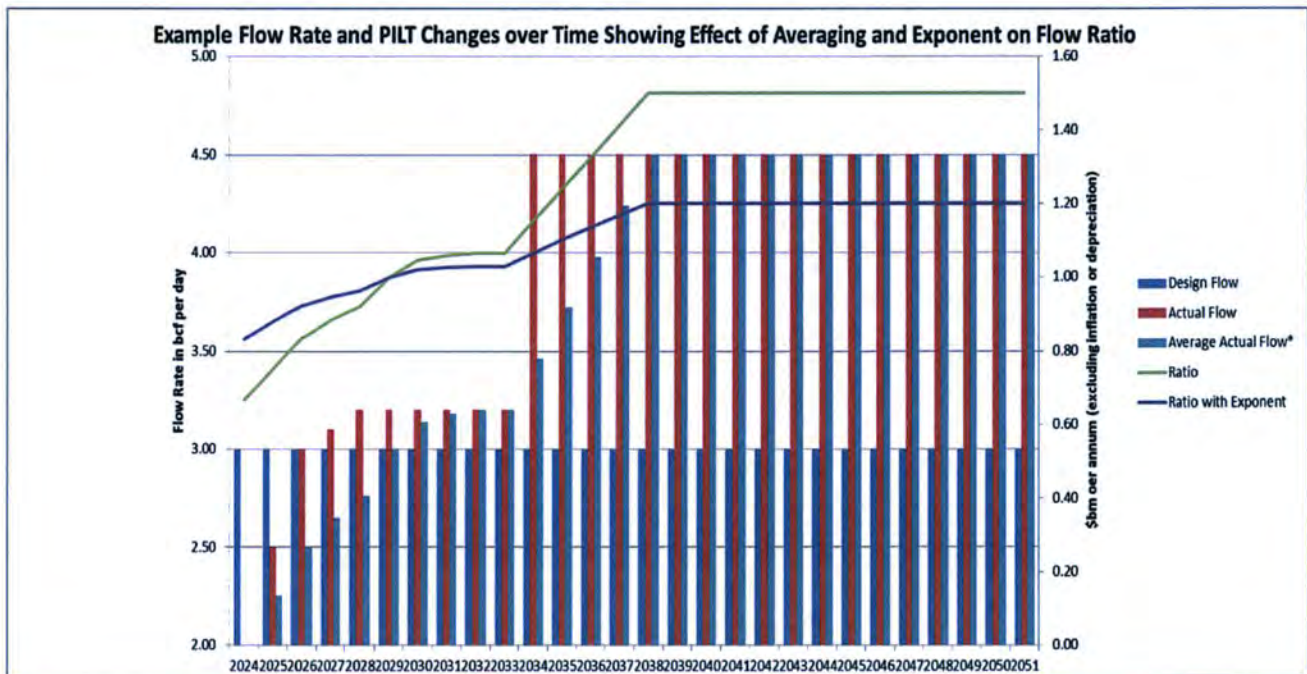
These three scenarios were looked at with no exponent and a 0.45 exponent, with the following result:



IMPACT OF EXPONENT AND FIVE YEAR MOVING AVERAGE ON FLOW INTERRUPTION

The same three scenarios were used as previously, but using a 5 year rolling average flow rate, against previous scenarios.

These three scenarios were also looked at with no exponent and a 0.45 exponent, with the following results:

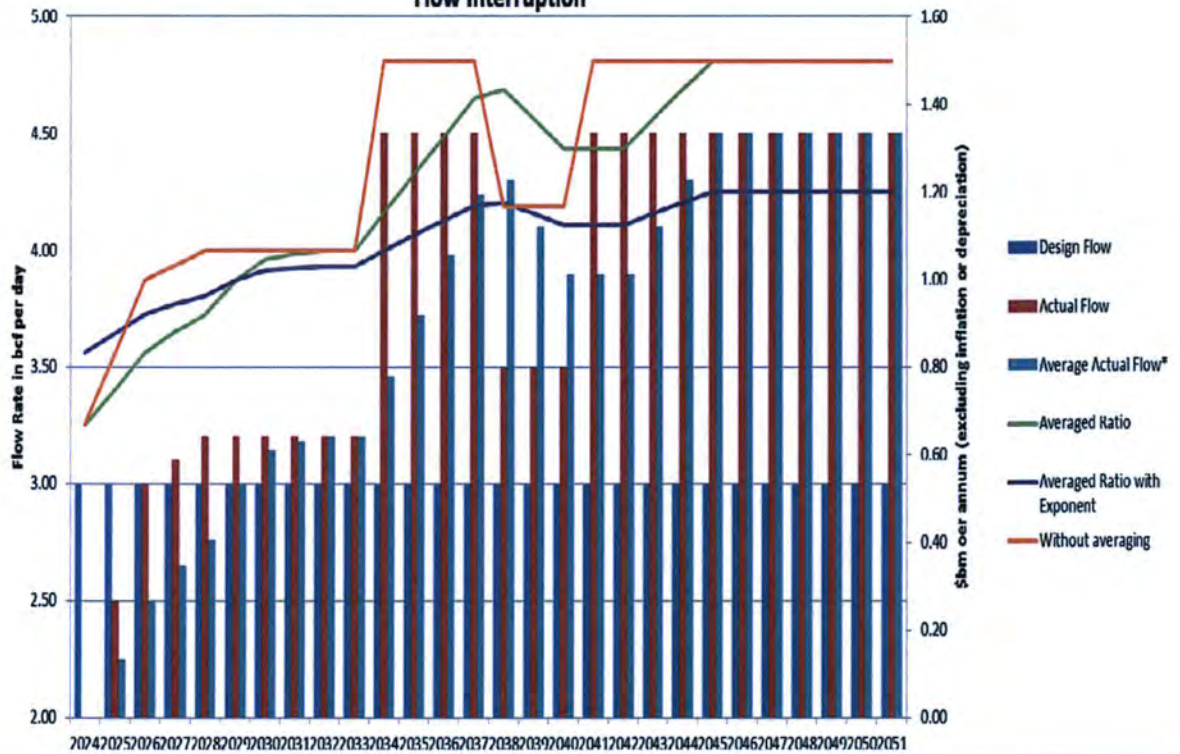


Finally, although it should be noted that *flow interruptions for any significant time are very rare for LNG projects*, the impact of a 1bcfd reduction on flow through the gas line/LNG plant was modelled between 2038 and 2040 inclusive, showing the impact with and without flow averaging and the use of a 0.45 exponent in the formula.

Examples of LNG plant which have curtailed or suspended operations would include the following:

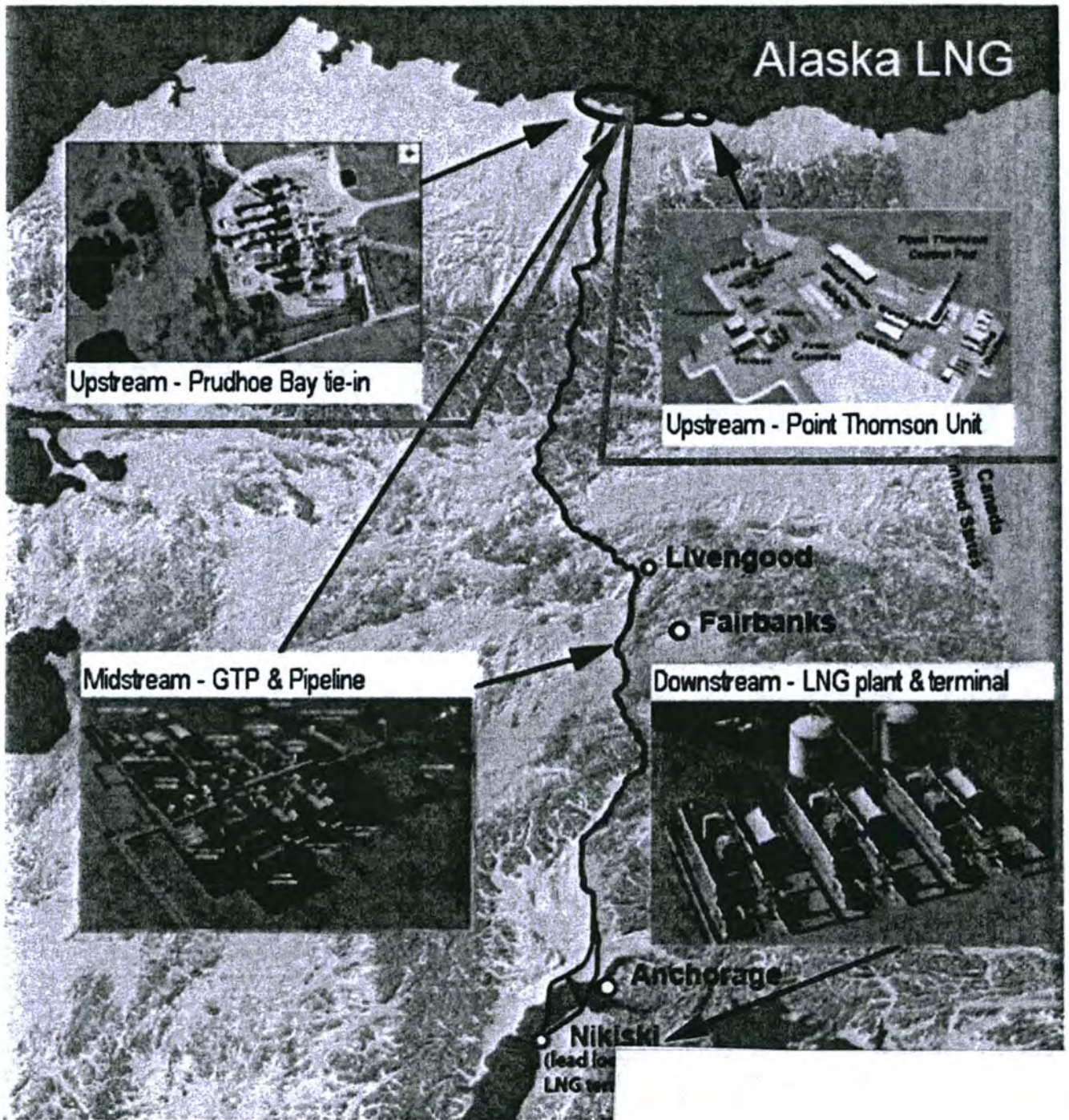
- Egypt, where two LNG export plants have had to curtail capacity since 2011, and the country is switching to LNG imports, similar to LNG export plants in Indonesia and Malaysia that are doing the same to address increasing domestic demand.
- Oman, where an LNG export plant has curtailed output due to shortage of feed gas amid rising energy consumption internally.
- Snohvit LNG in Norway, and Angola LNG which both suffered from commissioning and start-up reliability issues.

Example Flow Rate and PILT Changes over Time Showing Effect of Averaging and Exponent on Postulated Flow Interruption



CONCLUSION

The analysis in this discussion paper is intended to inform the MAGPR Board members and interested members of the public, in terms of the potential impact on a PILT of some of the features that were discussed at the meeting on February 20th. This is not definitive, and further analysis and discussion will be required as the Board moves towards any recommendation following subsequent meetings and discussions, chaired by Commission Hoffbeck.



ALASKA GAS PIPELINE PROJECT O



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Mike Navarre
Borough Mayor

April 14, 2015

Senator Click Bishop, Chair
Senate Community and Regional Affairs Committee
Alaska State Legislature
Room 115
State Capitol, Juneau

Dear Senator Bishop and Committee Members,

As you would expect, the Kenai Peninsula Borough and its almost 60,000 residents are keenly interested in Senate Bill 100, regarding the assessment of property taxes on a North Slope natural gas project, as we focus on seeing this project move forward in the best interests of all Alaskans for decades to come. The economics of financing, building and operating the facilities and marketing liquefied natural gas in today's global marketplace are challenging, with multiple LNG hopefuls worldwide all competing for the same customers. As such, the Kenai Peninsula Borough sees the need — and the wisdom — of adopting a fiscal structure that will allow an Alaska North Slope gas pipeline and LNG project to succeed in that competitive environment.

A key part of that fiscal structure is property taxes; key for the municipalities affected by the project and key for the project sponsors as they strive to determine all of their costs before committing to tens of billions of dollars in debt and equity to pay for construction. Looking at the decades of contentious litigation between the trans-Alaska oil pipeline owners and the state and municipalities, arguing over the assessed value of the oil line and related facilities, it's important that all parties avoid a repeat of a similar property tax debate over a North Slope gas project. The investment decision cannot afford that level of fiscal uncertainty, nor can the affected municipalities.

As a member of the Municipal Advisory Gas Project Review Board (more often called the Municipal Advisory Group, or MAGP), I have been involved in the search for the best way to avoid years of disputes over the property tax assessment for a natural gas pipeline and liquefaction plant, and I believe the bill before you Tuesday, April 14, Senate Bill 100, is a good step toward a solution. The bill is far from complete, but, while it currently lacks details and will require more work to meet the needs of all parties, it provides positive momentum toward a successful project. It is good to see the administration and legislature willing to address this issue, one of the many complex components necessary to advance an Alaska North Slope gas pipeline and LNG project that will benefit all Alaskans.

If we're willing to learn from our history, I'm confident there is a better way to assess the property tax liability of a North Slope gas project. The proposal in SB100 of an alternative calculation, as proposed for AS43.56.060(h), looks to be a good way to get there, certainly a more durable way than decades of fighting over the replacement value, income-producing value or depreciated value of a world-class investment for which there are no easily quantifiable comparables.

I commend the administration for working on legislation intended to protect municipalities' interests while treating the project sponsors fairly. I also commend the Senate Community and Regional Affairs Committee for making time to hear the bill in these final days of the regular legislative session.

Please call on my office for any assistance we can provide as work continues on this bill after adjournment of the regular session. Only through a concerted effort by the state, municipalities, and project partners, can we get where we need to go with this bill — a fair solution to property taxes and a successful project investment decision.

Sincerely,



Mike Navarre
Mayor

**TESTIMONY of
NORTH SLOPE BOROUGH MAYOR CHARLOTTE BROWER
SENATE COMMUNITY & REGIONAL AFFAIRS COMMITTEE
JANUARY 28, 2016**

Good afternoon Chairman Bishop and members of the Senate Community & Regional Affairs Committee.

My name is Charlotte Brower, and I am the Mayor of the North Slope Borough.

Thank you for looking at Senate Bill 100 and for taking testimony.

I would like to begin my testimony with a short walk down memory lane. Two years ago we all worked together to pass Senate Bill 138 to create the framework for the AK LNG natural gas pipeline project. Some of the members of this committee today were on the Senate Finance Committee in 2014 when we all worked together to address some of the concerns being expressed by municipal mayors.

One of the primary concerns back then was how the state would address property taxes on the project. There were many questions then, and there are still many questions today.

The North Slope Borough operates under the property tax system of Alaska Statutes 43.56 and 29.45. Taxable oil and gas properties represent 97% of the Borough's Full Value Determination. We do not have significant access to other tax base options, such as retail sales, raw fish, alcohol, tobacco, or car rentals.

Throughout our history, the North Slope Borough has developed a good working relationship with the oil companies. We have a great deal of experience with these companies on both property taxes and payments in lieu of taxes.

There are three points I would like to put forward today.

First, the North Slope Borough has worked with the oil industry and the State of Alaska on North Slope development for over 40 years.

The Borough now is looking at further development with the AK LNG project. Not only do we want to see the benefits of this project, but we want to see this project benefit our fellow Alaskans and our industry partners.

Second, the legislation before you today – Senate Bill 100 – is about coming up with a replacement system for local property taxes. Whatever system is used to replace property taxes should therefore be allocated with respect to the location and value of the respective assets.

Third, once a replacement system and allocation plan has been agreed upon by the municipalities, the State, and the oil companies, the North Slope Borough would like to see annual payments made directly from the taxpayer to the impacted municipalities. This last point is very important, and it is one that we ask you to give full consideration. Our own experience with working with industry has taught us that a direct payment system will provide better fiscal certainty to the project.

Quyanaqpak for the opportunity to testify today.