

ALASKA LEGISLATURE SPECIAL COMMITTEE/SUBJECT FILES 8672

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MR. NEFF said the ACIB is involved in a broad public information project. The ACIB puts out regular publications that have become sort of standards for the industry; the Pacific Rim Fisheries Report which has 200 subscribers, the Russian Far East News which is considered by some to be the premier source. It has only one real rival on what is going on, particularly the developments on Sakhalin Island which will be important for the Alaska oil and gas industry. The International Trade Directory the other publication is a combined effort between the ACIB and a private business.

Number 1325

MR. NEFF displayed a brochure for the North Pacific Rim Fisheries Conference and said he has never seen an activity started by a university that has become an international conference in such a short time. He said eight years ago ACIB brought together, for the first time, representatives of government, fishers and fish processing people and provided a chance for them to talk. The fourth conference was bid on heavily by Korea and Japan. He said when a planning conference was held in Seattle there were representatives from each of the six governments involved around the Pacific Rim. He said the conference will be attended by 250 people with ten different nations participating. The conference is now being sponsored by the government of Japan and the ACIB.

Number 1412

MR. NEFF said he would now talk about the American Russian Center which is funded entirely by federal monies. He said the American Russian Center received its fourth grant from the Agency for International Development. Through those grants the American Russian Center has; founded and operated four small business training centers in the Russian Far East in Khabarovsk, Magadan, Yakutsk and Yuzhno-Sakhalinsk which put them as the first people on Sakhalin Island and a valuable resource as that develops, provided small business training programs for Russians and brought some of the best graduates to Alaska for additional training, provided internships with Alaskan businesses, sent Alaskan businesses to the Russian Far East to provide training on airport management, banking, road rebuilding, single family home construction and hair dressing. He said the center has increasingly brought Russian delegations to Alaska to find out more about what Alaska has to offer the Russian Far East. He said it is important to note that the Russian contribution to those trips has gone up and up, with about \$400,000 a year being contributed now from the Russian side and growing each year.

Number 1475

MR. NEFF said about \$15 million in federal source grants have been received including two grants from the U.S. information agency which has sponsored 33 separate cultural exchange programs,

training about 10,000 Russians.

MR. NEFF said the center also had a program under the U.S. Agency for International Development called the partnership program that which linked universities together. He said this might be one of the most important contributions to Alaska. He said there have been direct linkages between Anchorage and Magadan in developing new business curricula. He said the UAA had the largest number of Russian students of any university in the United States. He said over the years the UAA will have an alumni association in the Russian Far East which will become the equivalent of those people who come through the Fullbright Program over the years.

MR. NEFF said the university in Khabarovsk asked to be a part of this exchange. He said eventually, 20 Russians a year will have two summers in Alaska, taught the first three years of their programs with their fourth year in Anchorage and will receive American business degrees with the entire cost of that program being paid for by the Russians. He said the center has enough funding to continue through the middle of 1998 and hopes, via contractual arrangements, to continue after that.

Number 1567

REPRESENTATIVE PHILLIPS asked if other states have business centers in the same communities that the Alaska Russian Center has.

Number 1573

MR. NEFF said they do not in Yakutsk, Magadan. He said there have been attempts off and on, both in Khabarovsk and Yuzhno-Sakhalinsk, particularly Portland State University. He said the University of Maryland is active in Vladivostok and in Irkutsk and the University of Washington in Krasnoyarsk. He said the American Russian Center is the strongest and, in many ways, the only real continuing presence in the Russian Far East.

Number 1599

REPRESENTATIVE PHILLIPS said people were bringing the Russian people to the Kenai Peninsula to do mine training and asked if this is done through the center.

Number 1608

MR. NEFF said he would have to check that specific program as there have been so many groups. The center acts both as a facilitator and as a sponsor. He said his guess was that it is probably associated with the center in some way and he could look into it. The center sent a number of groups to the Kenai working with people down there, particularly on oil and gas technical training. He said Alaska's main export to the Russian Far East is going to be

its expertise in oil and gas training and other areas. He said in the (indiscernible) training program which are being submitted to AIDEA, basic business training with infrastructure training focusing on oil and gas, transportation and communications to try to train Russian sectors to the point that they will be more capable of hiring Alaska businesses.

Number 1689

REPRESENTATIVE PHILLIPS said this training is all well and good if we're getting paid for doing the training, that we are not supplying the training. She said she appreciated his comment that the American Russian Center is funded totally by grants and that by 1998 the Russians will be paying most of the portion of the training.

Number 1679

MR. NEFF said that is the intent. He said infrastructure training is all based on the assumption that a high percentage of that cost will be paid for by Russian sources.

Number 1687

REPRESENTATIVE PHILLIPS asked if this was our assumption and whether or not it was their assumption as well.

Number 1689

MR. NEFF said it is their assumption because we are telling them that is the only basis on which we can operate.

Number 1693

REPRESENTATIVE PHILLIPS questioned that if we don't give them the training for free and other states do, whether we will we lose out.

Number 1699

MR. NEFF said this was not necessarily the case. He said the Russians are quite prepared to pay for the training, but want to be in on the planning of what it is. He said there are significant cultural negotiations that have to go on before you can have effective training. An example is that the Russians are still based on a full employment model. They would like to train lots and lots of workers, have five shifts instead of two. He said a compromise will have to be reached. It will not be as employment efficient as Prudhoe Bay right away, but the center will try to get them away from some of the inefficiencies that have characterized the previous system.

Number 1728

REPRESENTATIVE PHILLIPS asked if the Russians feel that they have a closer cultural connection to Alaska than they do to other states.

Number 1733

MR. NEFF said this is absolutely true. He said it is changing a bit, it is not the exclusive cache that Alaska used to have. He said when you introduce yourself as an American you get a different reaction than when you introduce yourself as an Alaskan because of the historic connections and because Alaska has had different experiences than they have had. He said he tells new Russians coming to Anchorage two things; it was founded the same year as the Russian Revolution and it was 70 percent destroyed in 1964. He said the Russians look around and see nothing comparable in the Russian Far East.

Number 1770

REPRESENTATIVE KIM ELTON requested the budget data that was referenced by Mr. Neff. He said if he has a question on freezer space in Taiwan why couldn't he call OIT, why would he call ACIB.

Number 1809

MR. NEFF said the two groups have different strengths and sometimes they will have more specific information on a few areas. He said ACIB works off what they already know, they get their information because they are asked by the industries to do a particular in-depth study. If ACIB has done it, then it is not necessary for OIT to do it. He said OIT will know of the existence of that report and it will become part of their information base. He said OIT is not set up to do the same kind of detailed analysis of market possibilities that ACIB does. He said ACIB is a research and information agency, whereas OIT is focused on developing market possibilities for particular businesses.

Number 1847

REPRESENTATIVE ELTON asked if it was the mission of ACIB to develop market possibilities for individual businesses and industries.

Number 1852

MR. NEFF said when ACIB works with a group such as a small niche market like reindeer sausage and antlers, where no one else was working with them, they become more deeply involved than they usually do. He said normally, aside from providing information about the possibilities, ACIB does not take the business and help them get into the market.

Number 1874

REPRESENTATIVE ELTON said he has always been intrigued by the idea that budgets can provide a kind of market test for policy makers because the more receipts you receive from fee programs tends to indicate the value of your program to those who are willing to pay the fees. He asked how much of the program is based upon fees that are charged to people who use the services, how much is received vis a vis the endowment and how much from the general fund.

Number 1903

MR. NEFF said he would not discuss how much is passed on to the World Trade Center, as that is separate. He said ACIB received approximately \$330,000 from the general fund, \$310,000 from the endowment and \$247,000 from grants and other sources. He said most of what ACIB calls grants are in fact contracts for particular kinds of research services. He said these contracts come from the Alaska Seafood Marketing Institute or from reindeer herders in Kugarak. Part of it is a contract with the Institute for Social and Economic Research to do the Salmon Market Survey. He said these are funds coming in from outside sources, essentially fee for service.

Number 1958

REPRESENTATIVE ELTON said he is more interested in how much Alaskan businesses and industries fund and pay for ACIB, not funded from other state or university organizations.

Number 1978

MR. NEFF said the bulk of it comes to ACIB through the medium of organizations like the Alaska Seafood Marketing Institute.

Number 1987

REPRESENTATIVE ELTON asked what groups are involved in the monthly round table discussions.

Number 2010

MR. NEFF said it is the Alaska Center for International Business, the World Trade Center, American Russian Center, Division of Trade and Development of the Department of Commerce, the representative from the U.S. Department of Commerce, and AIDEA. He said there were others, but those groups were the principal participators.

Number 2018

REPRESENTATIVE ELTON asked if there were any representative from coal and timber trade associations.

MR. NEFF said that currently no one represents those groups in the

discussions.

Number 2027

REPRESENTATIVE ELTON clarified that OIT is the Division of Trade.

Number 2033

CHAIRMAN COWDERY asked how many people work in the American Russian Center and if they are contract or state employees.

Number 2041

MR. NEFF said they are paid through the university on contracts that make it clear they don't get any money unless the grants continue. He said, currently, there are seven people in Anchorage, six Americans in the Russian Far East and approximately 16 Russians in the Russian Far East.

Number 2059

CHAIRMAN COWDERY referred to the recent contract and said, "Sakhalin that we have to represent that the Governor proposed to represent us -- what is -- our role or, or do you think that the background of this company is also representing other states maybe, would have been, in your opinion, better suited to have an Alaskan firm or company to represent us there."

MR. NEFF said there are several alternatives and a decision has been made for the short run, only a few months. He said he expressed concern, before the decision was made, that we need to look out for Alaska interests first. He said these might be well served under this arrangement, but since it is an organization that receives its funding from elsewhere and has other obligations it is important to keep a close eye on it.

Number 2107

CHAIRMAN COWDERY asked for the procedure to disperse funds to subcontract grants to the American Russian Center and others.

Number 2125

MR. NEFF said ACIB does not do much subcontracting. He said he could only think of one instance where the American Russian House subcontracted in 1993 with a bank in Oregon. He said now there are banks in Alaska that will work with them. By and large the center works through programs which are operated 80 percent by center staff. He said, otherwise, they will have the participation of Alaskan businesses or government officials in Alaska who are providing training for airport managers or in banking. He said banks, primarily the National Bank of Alaska, will participate, at

least to a certain extent, at their own expense.

Number 2181

CHAIRMAN COWDERY asked, at the height of the training and travel, how companies were selected between Russia and Alaska.

Number 2186

MR. NEFF said companies are not selected in the sense that the American Russian Center is not sponsoring a company for a business activity. He said the center will often have representatives from different companies go to a training situation. The center is almost exclusively involved with training. If the center is trying to help someone understand single family construction, companies who are involved with that type of activity are approached. He said the center typically calls different companies, tells them about the opportunity, ask them if they are interested and go with those companies interested enough to expend some money to do a training situation.

Number 2223

CHAIRMAN COWDERY asked what percentage of ACIB's total public service and market research activities were conducted by the World Trade Center Alaska.

Number 2231

MR. NEFF said the World Trade Center has had an agreement with ACIB to do some of its short term instructional activities such as; short term seminars, how to get an export license in Russia, obtaining a visa, or what opportunities for trade are available in Taiwan. He said this used to be a separate line item budget which is not the case anymore. The World Trade Center receives, from the general funds ACIB receives, approximately one-third of their money.

Number 2279

CHAIRMAN COWDERY referred to a booklet titled, "State of Alaska Private Sector International Business Needs Assessment, dated July-October 1995," and read that, "ninety percent of Alaska exporters don't need or want government assistance for their export programs." He said if this is the case, why is the state spending money on export assistance and who is ACIB actually helping in this.

Number 2290

MR. NEFF said he would have to reread that information.

CHAIRMAN COWDERY said that also in the booklet, that the exporters that would seek help; 33 percent would seek private sector help, 23 percent would use the World Trade Center, 16 percent would use U.S. Commercial Service, 10 percent would use ACIB, and 6 percent would use the University of Alaska. He asked why the OIT and UAA have such a low public reliance factor.

Number 2350

MR. NEFF said part of this might be due to confusion on the part of companies and individuals that their received information ultimate source is the university. He said a great deal of information ACIB generates is provided through the Alaska Seafood Marketing Institute. He said their data is the data that ACIB collects. He said there has not been enough of an attempt to allow the public, as a whole, to know everything that UAA has been doing. He said the World Wide Web site will do a lot to correct that. He said ACIB receives 1,600 inquiries a year which include walk-in people and telephone calls to which they provide direct assistance.

Number 2391

CHAIRMAN COWDERY said back in the 13th Legislature he was co-sponsor of the legislation that created trade offices in Seoul and Taiwan. He said he has been over there many times. When he worked for the municipality in Anchorage, he received several calls from people who were looking for small businesses in the Pacific Rim or find out about small businesses. He said he put them in touch with some. He said it appeared that a lot of people are unaware of where to ask. He asked what the states role should be in international trade.

Number 2444

MR. NEFF said the state needs a combination of interlocking services, similar to what it has now. He emphasized that he is not saying that it is the perfect mix or that the balance of support is the right one. He said the state does need some selective representation in certain markets. He said, because he has not studied it, he would not say whether what the state has now are right ones in the right proportion. He said Seoul and Taiwan, with their portions of the Alaska trade market, are places where Alaska ought to be represented. He said moving towards some type of representation in the Russian Far East makes sense because Sakhalin shows every indication of being a good market.

TAPE 97-1, SIDE B
Number 0000

MR. NEFF said it is important to help the connections between large scale sectors of Alaska business and their opportunities abroad. He said the university has a responsibility to bring people along

to be ready to participate in the international market, partly in indirect ways through information, research and directly through individuals. He said the World Trade Center is part of that. It is specifically involved in trying to bring a kind of micro training and services to its members which will help them in the final stages of getting into the markets. He said, beyond that, there is an importance for Alaska to harness its financial resources through AIDEA, a combination between AIDEA and banks to get some development capital that has an Alaskan name on it in these particular markets.

MR. NEFF said ACIB has tried, in the Russian Far East through a lending organization set at the national level by the United States government to get rather small amounts of money out on the street for those people to get into new entrepreneurial situations. He said this program is not going very well. He said there have been numerous conversations with various Alaska banks.

Number 0031

CHAIRMAN COWDERY said Alaska has very few people and lots of resources and the Pacific Rim area has just the opposite. He said it is logical that we are a natural trading partner with those countries. He said the companies involved with the bigger resources; oil and gas, hard rock minerals deal directly with companies abroad. He said there are just as many smaller businesses in the Pacific Rim and that this is an area to develop. He said businesses need and want business information.

Number 0079

MR. NEFF said he would call disseminating information a form of assistance. He said it is necessary to get the word out there about what information and resources are already available. He said when a business does come to the World Trade Center or to the Alaska Center for International Business they are helped to find that niche market which will allow them to sell those goods.

Number 0110

CHAIRMAN COWDERY asked approximately what percentage of ACIB is conducted in response to a companies request. He asked if ACIB maintained a staff specifically for these requests.

Number 0118

MR. NEFF said two and a half people are involved with research. One staff person is working almost exclusively in the fisheries area, another is a specialist in SouthEast Asia in timber and one is a kind of generalist. He said ACIB is close to 100 percent in responding to industry or government agency needs for research in these areas.

CHAIRMAN COWDERY asked if it was industry that makes these requests.

MR. NEFF said it is primarily industry.

Number 0162

REPRESENTATIVE PHILLIPS referred to Mr. Neff's testimony that ACIB does not conduct basic research and asked him about his comments that he has people involved in research.

Number 0170

MR. NEFF said the research they are doing is not academic research which identifies a broad problem.

Number 0181

CHAIRMAN COWDERY asked how many investment proposals were completed last year and what methods were used to track the success rate.

Number 0191

MR. NEFF said he would get the exact number to the committee. He said an informal system is used. Once a company gets talking with ACIB, they are asked if they have used the research and how its been helpful to them. He said ACIB uses this information in doing the next round of research.

Number 0221

JAMES McMILLAN, Deputy Director of Credit, Alaska Industrial Development and Export Authority (AIDEA), was next to testify. He said he has been with AIDEA since July of 1996. His primary responsibility is management an oversight of AIDEA's credit programs (indiscernible due to papers over the microphone) revenue bond program are tax exempt and taxable, umbrella bond program, business assistance program and export assistance program.

MR. McMILLAN said AIDEA has had an export assistance program in place since 1987. That program provides a guarantee to banks who extend both pre-export and post-export financing. To date it has not issued any guarantees under this program and to the best of his knowledge there have not been any requests to do so.

Number 0315

REPRESENTATIVE PHILLIPS clarified that he said there have been no requests or money given out since 1987.

Number 0324

MR. McMILLAN said AIDEA is well aware of the lack of success of this program and are attacking it on three different fronts in attempts to find solutions. Before he talked about these attempts, he discussed reasons why the program has not been successful. One reason is timing. While Alaska has been exporting for many years, AIDEA thinks the majority of those exports have been accomplished by large companies, sometimes national firms, who are experience exporters that either don't need financial assistance or have established relationships with outside banks that can meet that need. He said AIDEA also thinks, to some degree, that there has been a reluctance on the part of the banking community to get involved with export financing, although there is beginning to be a change in that area. The rising interest in the Russian Far East has in itself been a problem for the program. The lack of political and economic stability in Russia has led to a hesitancy to commit financial resources to that area. For example, the Export-Import Bank of the United States (Ex-Im Bank) publishes a Country Limitation Schedule indicating which countries and which sectors in those countries are open for business with Ex-Im Bank. This business of Ex-Im Bank includes export credit insurance which is a requirement of AIDEA's current export assistance program. Until November of last year, all business in the private sector was closed to the Ex-Im Bank. Businesses in the public sector was open only if the transaction had the full faith and credit of the Russian government behind it. Once again, that is beginning to change. He said AIDEA is now finding more of an interest on the part of the banking community to provide export assistance and the Ex-Im Bank is now open for business in the private sector in Russia.

MR. McMILLAN said as he mentioned earlier, AIDEA is taking steps to find solutions to their problem. First, AIDEA has met with the banking community to seek their input on what changes they think need to be made in order for the export assistance program to become more viable. Second, AIDEA has sought alternative programs which meet the financing need of exporters. Specifically, late last year AIDEA completed the necessary training to become a city/state partner of the Ex-Im Bank. As a city/state partner AIDEA provides local access to the Ex-Im Bank programs which include among others; export credit insurance and working capital guarantees. Finally, AIDEA is in the process of reviewing successful export finance programs already established in other states. By utilizing that information, along with the input AIDEA has received from the banking community, it will be prepared to recommend changes to our export assistance program in order to make it a more viable program. He said AIDEA is confident that this approach will be successful.

MR. McMILLAN said two personnel within AIDEA, including himself, dedicate a portion of their time to export assistance. The other individual, Katelyn Ohmer, is the Economic Development Specialist who dedicates a good portion of her time to the area of export

assistance. The remainder of her duties include marketing and public relations, responding to inquiries about AIDEA's mission and programs, legislative liaison and monitoring budgets for projects and assigned programs.

MR. McMILLAN said AIDEA is also pursuing other means to become a more visible player in the export arena. He said AIDEA fully realizes that visibility and education are important ingredients to their success. Along these lines, AIDEA is an active member of the International Business Round Table.

MR. McMILLAN said, through the assistance of the Department of Commerce and Economic Development (DCED) Deputy Commissioner, Debbie Sedwick, this group recently executed a "Memorandum of Understanding" which took place in October of 1996. He said this really sets the path for a cooperative and unified effort to provide export assistance and develop programs and projects which will help each member to achieve their goals. Currently, AIDEA is working on development of a series of seminars for the banking community and exporters which would outline the various financing programs available through the Ex-Im Bank. This program should get off the ground this spring.

MR. McMILLAN said he was invited to become a member of the Finance, Insurance and Taxation Subcommittee of the Alaska-Sakhalin Working Group and will be speaking at the groups next meeting on January 31, about the Ex-Im Bank programs.

MR. McMILLAN said that while AIDEA is confident that all these efforts will lead to a more successful and well rounded export assistance program, they are actively working with a couple of banks and exporters on projects to assist them in their exporting needs. One involves a business which exports goods to the Russian Far East and is in need of export credit insurance to finance their receivables. The other project involves a guarantee of a line of credit extended by a local bank to a bank in the Russian Far East. The line is used to confirm letters of credit issued by the Russian bank to their customers who would become buyers of goods and services exported from Alaska. The letter of credit has been the most used means of financing up to this point. In addition, AIDEA is working with a large company in the petroleum industry to assist them with export financing through the Ex-Im Bank.

MR. McMILLAN said in summary, AIDEA's short term goal was to emphasize the Ex-Im Bank programs for financing of Alaska's exporters. He said AIDEA believes these programs provide the means and flexibility to assist Alaskan Exporters. He said the long term goal is to review and revise AIDEA's program to better serve the needs of the banking community and Alaska's exporters. As part of this goal, AIDEA is looking to establish co-guarantee programs with the Small Business Administration and the Ex-Im Bank. A co-guarantee program would allow AIDEA to leverage their program and

reduce the risk. It would also provide better flexibility with their financing program.

Number 0661

REPRESENTATIVE PHILLIPS asked if any previous legislative body examined this program or has the management of AIDEA looked at this program. She asked why nothing had been done.

Number 0683

MR. McMILLAN said as far as the management of the authority is concerned they have examined it. They met with the banking community and with some of the organizations to try and find out why the program was not being used. He said there are some problems with the program structure.

Number 0702

REPRESENTATIVE PHILLIPS asked if any attempts were made to correct those problems so that it could be a program that people could use.

Number 0704

MR. McMILLAN said, looking back in the history of the files, it appears that this effort took place around the beginning of 1994. He said, to the best of his knowledge, other than some of the things mentioned such as forming alliances with other groups, there doesn't appear to have been any direct effort at changing the program yet.

Number 0731

REPRESENTATIVE PHILLIPS asked if a major oil industry company went to the Ex-Im Bank for financing if they were fitting under this program or were they fitting under a different authority guarantee are ...

Number 0740

MR. McMILLAN said, no, as a city/state partner AIDEA is somewhat like an agent of Ex-Im Bank and can provide local access. He said AIDEA will be working with the company to utilize the Ex-Im Bank programs. He said especially now that the Russian Far East is open for business in the private sector, he believes that Ex-Im Bank programs will serve the majority of the Alaskan exporter's needs, both small and large. He said the program, as it is currently structured, has a maximum guarantee of \$1 million.

Number 0783

REPRESENTATIVE PHILLIPS questioned whether a program that was in

place that nobody could, would, was required or is was going to utilize would it be his recommendation to just get rid of the program.

Number 0793

MR. McMILLAN said no he would not. He said AIDEA is in the process of conducting a survey to find out specifically what the financing needs are of Alaskan exporters.

REPRESENTATIVE PHILLIPS asked if this was identified in the report done last year.

MR. PIGNALBERI said it was addressed, but not comprehensively.

REPRESENTATIVE PHILLIPS asked if Mr. McMillan was involved in that report.

MR. McMILLAN said no he was not. He reiterated that he just began working for AIDEA in July of 1996. He said he has read through that report. He said it does address the area of financing, but he did not believe it provided some of the information that AIDEA was looking for in order to provide the education needed for exporters and the banking community.

MR. McMILLAN returned to the earlier question and said the bottom line should be that we give financing assistance to Alaskan exporters. He said if this can be done through utilization of the Ex-Im Bank and if it really serves all the needs of both the banking community and the exporters, then he would suggest that the state utilize that program. He said if AIDEA can create or revise their program so that it filled in some of the holes that are not being covered by the Ex-Im Bank program then he would suggest that AIDEA do that. He said a duplicate program should not be kept for the sake of having a program.

Number 0878

REPRESENTATIVE PHILLIPS asked when he anticipated having an answer to that question.

MR. McMILLAN said he hoped to come to a conclusion by the middle of this year. He said he is looking at programs in other states to try and find out what the differences are between their programs, our programs, how they are leveraging Ex-Im Bank, and what they find. He said he realized that the needs of exporters from other states are much different than those of Alaskans.

Number 0903

REPRESENTATIVE PHILLIPS recommended that sometime during the middle of the interim the committee follow-up on this issue by getting an

answer. She said if we have a state program in place that isn't workable, no one has used it in the past ten years, then let's look at getting rid of it.

Number 0921

CHAIRMAN COWDERY said that is the basic purpose of these committee meetings.

Number 0925

REPRESENTATIVE ELDON MULDER said he believed that Senator Kelly sponsored legislation changing the name of AIDEA to include the export authority. He said he would look into why the export program was needed in the first place. He said he believed Commissioner Tony Smith was advocating it. At that time Alaska was in a recessionary period and the commissioner might have been looking to stimulate exports. He said he did not feel that the export program is not such a big problem as not much time or resources have been spent on it. He said the bigger question is how can we revise it to actually make it workable.

REPRESENTATIVE PHILLIPS said if we have state employees identified in that program with their salaries being paid for by that program and the program is not doing anything.

MR. McMILLAN said he and one other staff person have a portion of their time dedicated to export assistance.

REPRESENTATIVE MULDER said the staff works in a multitude of areas, without an export specialist per se. He said a statute might need to be revised, to make it more applicable and user friendly if it is not possible to do this then at that point we should discard the program.

MR. McMILLAN said he did not want to diminish the fact that for whatever reason the program has not been successful. He said the program has not been utilized. He said, in his opinion, the program is directed towards small businesses and when the program was created there was not a lot of small businesses exporting. He said there might have been a lot of businesses that had an idea that they might want to get into business and export, but neither this program or the Ex-Im Bank program is for the total novice. He said there is a higher degree of risk when you start doing business in a foreign country as compared with doing business within the United States. He said this is part of the problem. He said timing is also an issue.

MR. McMILLAN said AIDEA has looked at the statutes, at the regulations and at this point, without making any commitment, if AIDEA feels it can create a program that will compliment Ex-Im Bank it will take some legislative change.

REPRESENTATIVE MULDER said at the time of implementation of the program, the banking industry was struggling with only two institutions on solid ground. Those two banks were not lending to anybody without 70 percent equity.

MR. McMILLAN referred to his 20 years experience in the Alaskan banking industry and said that when someone came in and said they wanted financing to export goods or services overseas you did everything you could to shift the subject. He said sometimes when banks did financing for businesses that were exporting, it was treated like it was a loan for business done in Alaska. He said some of it is just misunderstanding on the part of the banking community. He said this is why we need to educate the banking community and the exporter.

MR. McMILLAN said that when you look at the changes in the banking community, with kudos to the National Bank of Alaska because of their support for export assistance, some smaller banks were not geared up for export assistance, others have offices outside which provide assistance but refer the customer to their Seattle office.

Number 1205

REPRESENTATIVE PHILLIPS requested a copy of Mr. McMillan's comments.

Number 1208

CHAIRMAN COWDERY asked when the comparison with other state programs will be done.

Number 1218

MR. McMILLAN said he was in the process of drafting a letter that will go out to the different states that have some type of export authority or export assistance program. He said the timing involves getting the letter out and getting the responses back. He said the letter will be very specific in what AIDEA is requesting so that it could be a comparison of apples to apples. He said he would hope to complete this around the mid-year.

Number 1250

CHAIRMAN COWDERY referred to an example of when he worked for the municipality of Anchorage. He said a company asked for export assistance for some water products to Korea. He said the answer they received was to let a bank package their proposal and then AIDEA would see if they could help. He said this was a small company and would have liked to have had some assurance before they did the paperwork.

Number 1295

MR. McMILLAN said it is a fine line that the export authority walks. They try not to confuse the private sector, primarily the banking community. He said the last thing the program wants is to move in front of the banks and take away their customers. He said the authority is always receptive to questions and inquiries from perspective business people who need assistance from AIDEA. He said AIDEA always offers them the caveat that they are not in the business to do direct lending. The program can provide them assistance, help them along, make them feel like there is something there that they have got to work with and then ask them to contact their local bank.

MR. McMILLAN said as a certified city/state partner, the authority has the obligation to directly provide those services to the banking community and the exporters. He said hopefully you will not find an incident like the one mentioned in the future.

Number 1412

JOSEPH L. PERKINS, Commissioner, Department of Transportation and Public Facilities (DOT/PF), was next to testify. He said most trade matters require some type of transportation and his department provides and operates the infrastructure in the state of Alaska to make this possible. He said this is particularly true of the Alaska Marine Highway System which is delivering people to the state every day and with the international airports.

Number 1494

KURT PARKAN, Deputy Commissioner, Office of the Commissioner, Department of Transportation and Public Facilities, said he had some brief comments and provided handouts to the committee. He said part of the mission of the airports, which include both the Fairbanks and Anchorage airports, is to promote cargo, passenger air service and related activity to the economic benefit of the state of Alaska. He said the airport marketing strategy is to identify and promote air service development opportunities on both a carrier by carrier and on an industry wide basis. He said generating cargo related activity is aimed at capturing the trans-Pacific as well as the European business, a rapidly growing sector. The activity is also aimed at competing on a world wide basis.

Number 1578

MR. PARKAN said airport funding is through the International Airport Revenue Fund which is an enterprise fund of the state of Alaska, established in 1961. He said the airports are independently funded from the general funds, but the general fund does not contribute to the operations of the airport. He said all capital debt service costs are generated through the International Airport Revenue Fund in addition to what is received from the Federal Aviation Administration (FAA) in terms of capital

improvement projects.

Number 1610

MR. PARKAN said the marketing budgets, for the past several years and proposed for this year, are \$400,000 for Anchorage and \$100,000 for Fairbanks. He said approximately 50 percent of the Anchorage budget and 70 percent of the Fairbanks marketing budgets are for ongoing international projects. He said, in terms of personnel dealing with marketing, there are two positions at Anchorage under the development manager. One is currently filled and one is to be filled. Both of the efforts in Anchorage and Fairbanks are combined with the economic development corporations of those respective cities. He said, in Fairbanks, the full amount of the marketing money goes to the Fairbanks Industrial Development Corporation. In Anchorage a portion of the budget goes to the Anchorage Economic Development Corporation (AEDC) for specific projects, approximately \$100,000 to \$120,000. Projects that they are currently working on pertain to international markets.

Number 1705

MR. PARKAN said the state is seeing a growth in both international cargo and passenger trends at the airports. Anchorage is number two in the United States in terms of gross landed weight and Fairbanks is number seven. The state has received from the United States Department of Transportation (US DOT) expanded cargo transfer rights last fall for increased traffic rights for foreign carriers. He said this will generate a considerable amount of growth at the international airports. It will allow international cargo carriers to do more than just land and fuel, they will also be able to fuel, transfer cargo to other carriers, to hub, and to continue flying through to the lower 48 from the Asian markets. He said these traffic rights exclude Japan and United Kingdom carriers for now, but the state is hoping to get them included. He said those countries are currently excluded as there are bilateral negotiations going on that are much bigger and broader than what the state's specific request was for. He said these rights are for one year at a time, but the state will apply for an extension.

Number 1852

MR. PARKAN said this decision of the US DOT has created a considerable amount of interest in third party developments. He said there are people who are clamoring to come to the airport and set up warehousing operations and hubbing operations.

MR. PARKAN said DOT/PF is participating in the Governor's Pioneer Incentive Program which is attempting to get direct passenger flights from Japan to Anchorage or Fairbanks. He said this effort involves the Department of Commerce as well as AEDC, the Anchorage and Fairbanks Visitor and Convention Bureau, AIDEA is also involved

because of their financing view of the world. Hopefully they will package some type of an incentive to bring a carrier on at least a weekly basis to Alaska from Japan. He said the commissioner is chairing the committee with Debbie Sedwick from the Department of Commerce and Economic Development.

Number 1923

REPRESENTATIVE MULDER asked if any carriers have expressed interest.

Number 1937

MR. PARKAN said DOT/PF has identified a couple of carriers that have some potential. He said subcommittees are working to get that interest increased. He said hopefully within the next year there will be announcement from somebody to come here. He said right now the focus is on Nippon Airways and NorthWest. He said it is unclear which city out of Japan will be able to provide the direct flights, Tokyo is pretty tied up.

Number 2003

REPRESENTATIVE PHILLIPS repeated that the Pioneer Incentive is offering \$1 million to an airline company willing to come from the Orient and asked where that money was coming from.

Number 2033

COMMISSIONER PERKINS said the committee is looking at several sources of revenue, with at least half of the money coming from the private sector from such organizations as the Anchorage Visitors and Convention. He said another source that is being sought for the other half of the money. He said the committee might ask the state, but it has not been decided. The subcommittee will exhaust all other possibilities before doing so. He said AIDEA is on the committee and they are the financial people working to get the incentive money.

Number 2082

COMMISSIONER PERKINS said this incentive money is not cash payments. What is being discussed is a marketing effort for the airline to come to Alaska.

Number 2116

REPRESENTATIVE PHILLIPS clarified that it is not a direct cash payment and you are looking at marketing and asked if it would be price reductions on marketing efforts or what other kinds of things are they looking at.

Number 2138

COMMISSIONER PERKINS said the money would be directed to marketing that flight. Another thing being looked at is people who are beneficiaries of this service. For instance, the potential of Alyeska blocking off so many seats. He said there are several ways that these incentives can be formed.

Number 2195

MR. PARKAN said the subcommittee working on that feels that more than \$1 million could be generated, particularly in the private sector. He said \$1 million was not the magic number, it was the minimum.

Number 2229

CHAIRMAN COWDERY asked if there would be any ripple effects from other airlines that did not receive incentives to come to Alaska.

Number 2243

COMMISSIONER PERKINS said the committee has not received any comments as this is a special circumstance, it is for international flights and currently Alaska does not have any international flights.

Number 2266

REPRESENTATIVE PHILLIPS asked if there was a stipulation that the flight had to go to Anchorage, or if it could go to Fairbanks.

Number 2284

COMMISSIONER PERKINS said it could go to Fairbanks, but realistically it would probably go to Anchorage. He said Fairbanks is heavily involved with the task force because many of the passengers that come in from Japan go to Fairbanks, especially in winter to see the Northern Lights and visit the hot springs. He said there are benefits to Fairbanks even if the flight terminates in Anchorage.

Number 2372

CHAIRMAN COWDERY said the airport is proposing a 3 percent head tax on passengers to pay for a new terminal building and asked if this was correct.

MR. PARKAN said the airports had proposed to Legislative Budget and Audit (LB&A) the approval of a passenger facility charge. He said if it looks, feels and smells like a tax you can call it a tax, but Congress specifically said that it wasn't a tax but a user fee. He

said the passenger facility charge would be \$3.00 for deplaned passengers at Anchorage and Fairbanks. That money would be used to fund identified capital improvement projects.

TAPE 97-2, SIDE A
Number 0000

MR. PARKAN said there were very good discussion comments from the public with concerns expressed by people who felt that it would place a burden on them. He said the subcommittee would put out a report to the full committee with recommendations. He said they felt it would be more appropriate for this discussion to take place before the full legislature, so DOT/PF decided to withdraw the request for LB&A to do the fund source shift from FAA funds to Passenger Facility Charges (PFC) and wait for the report to come out from LB&A. At that point, take a look at what the report said and then decide at that point whether or not to go forward. He said no decision has been made to continue with PFCs. He said, when the report comes out, DOT/PF can discuss with the legislature what the mutual interest is in PFCs.

MR. PARKAN said PFCs are used throughout the country, they are charged every time you go through Seattle or through most of the major airports in the U.S. He said it is a fund source that helps diversify the revenue the airports receives to meet their capital needs. He said the capital needs, especially at the international airports when they are expanding, far exceed the ability to pay for them with revenues. He said the federal AIP program makes it difficult. He said DOT/PF has recently been notified that the Administration is proposing a \$1 billion AIP program for next year, currently it is \$1.46 billion. He said this would make a 30 percent reduction in funding for capital programs. He said right now almost all of the capital projects are funded through Airport Improvement Plan (AIP) with match and some smaller projects funded through the revenue source.

MR. PARKAN said the alternative to PFCs would be to not do the projects or finding some other revenue source such as bonds or increasing airport fees which could have a rippling effect on passengers.

Number 0251

COMMISSIONER PERKINS said any of us that fly out of state are paying this fee anyway. He said the additional charge would be for intra-state travel.

Number 0302

REPRESENTATIVE PHILLIPS said she would like to get back to the issue of airports and their role and in international business. She said she wanted to commend the Anchorage airport on the

briefing given to the legislators. She said it was good to see the growth that was occurring and the development plans.

Number 0347

REPRESENTATIVE PHILLIPS asked if there was a direct relationship with the World Trade Center, the Center for International Business, the American Russian Center or if the airports worked just with the DOT/PF. She asked how they were tying in international business expansion at the airports with what we see as international trade in Alaska.

Number 0396

MR. PARKAN thanked her for her comments.

Number 0437

MORTON PLUMB, Director, Anchorage International Airport, Department of Transportation and Public Facilities, was next to testify. He said the airport deals directly with the World Trade Center on trade information. He said, as far as the overall business picture in Anchorage is concerned, the airport works very closely with the municipality, AEDC, and AIDEA. He said the airport has formed sort of a troika with AIDEA and AEDC for their marketing effort. He said, in that regard, the airport works directly with other agencies that are promoting business.

MR. PLUMB said the Anchorage airport has what they call their personal shopper who assists perspective customers work their way through the bureaucratic process of trying to find out information in case they choose to develop there. He said, in addition, the municipality has committed themselves to a similar process and the airport tries to link up so that the airport is user friendly to the customer. He said the airport coordinates very well between the various organizations.

Number 0535

REPRESENTATIVE MULDER referred to a DOT/PF subcommittee which talked about re-evaluating the international concourse as it was not being utilized to its full capacity. He said it was felt there was growth at the national market and to adding the concourse to the domestic terminal. He asked what the future was for the international concourse.

Number 0594

MR. PLUMB said there was an effort a few years ago to convert some of the international terminal. He said once you spend capital to reduce capability you then limit what you can attract there. He said many people in Anchorage do not have the opportunity to see

how busy the international terminal is. He said at 1:00 a.m. there is no room to park any more airplanes. He said what is indicative of that is the duty free concession which provided somewhere between \$108 million and \$117 million gross which provided (indiscernible due to coughing) a year. He said this had a sharp decline bottoming out somewhere in the 1994 time frame to where the gross is \$7 million and probably less than \$1 million to the airport.

Number 0643

MR. PLUMB said last year the duty free grossed close to \$14 million, almost \$6 million greater than the initial bid came in. He said he believed the international traffic is on the upswing. He felt it would probably be a mistake to spend capital to change that. He said the airport might get a synergy as they see more cargo coming. He said 60 percent of cargo is carried in the belly of passenger airplanes. As the airport sees with EVA airlines, they are currently flying what they call 747 COMBIs with passengers in the front and the cargo in the back.

Number 0708

MR. PLUMB said this might become more lucrative as the hub concept is developed. He said as a result of the relief received from the U.S. DOT, not only was more cargo flexibility but the opportunity to do what they call change a gage and starburst. Effectively, what that will do is it has the potential to increase the yield and that is the bottom line. The airlines will be able to hub and sort internationally which is very similar to what UPS and FedEx does today on the domestic market.

MR. PLUMB said this might allow someone like Korean Airlines, to stop at Anchorage and then go over to Frankfurt on a large airplane such as a 747 which could hub smaller airplanes such as a 727 as long as they had traffic rights to go down to Seattle, Los Angeles, or San Francisco. While the larger aircraft heads over to Fairbanks with its cargo, takes the fee from the other three small airplanes that came up, loads up the 747 and goes back to Korea. As the airport sees it that area might become very attractive to other airlines such as KLM which also has COMBIs. They might start bringing cargo in and put some passengers in the front end. If passengers come, then there will need to be a place for them to disembark.

MR. PLUMB said Representative Mulder was correct but he hoped the airport would increase their traffic. He said they were up 20 percent which he said is easy to do when you have a very small number. He said the airport feels there is a better alternative then converting that space.

Number 0810

REPRESENTATIVE MULDER commented that the airport had sunk to a very low point on the international level. He asked at what point in time you pull the plug and say that the long range plans, the efficiencies and the routes are not going to produce a direct route between Japan and Alaska.

Number 0878

MR. PLUMB said the Anchorage airport has been working that effort for some time and said it appears that they are getting pretty close, it is a matter of the bottom line. He said the airport knows for a fact because they have done the studies, that the route analysis will show a positive in the black revenue. He said the issue is airframe availability. For example a company such as NorthWest with a DC 10 has a revenue flow between Los Angeles and Heathrow that is greater than it would be between Norito and Anchorage. Therefore, they have done the route analysis and that the Norito/Anchorage route would not make as much money. He said as the economy grows, as we get greater airframe availability then the airport will get them as customers. He said the airport watches to see what companies are buying large aircraft.

MR. PLUMB said he feels that NorthWest will start summer air traffic between May and September, 13 flights occurring once a week. He said the Pioneer Incentive would ask for a period of two years which would bring the amount offered \$500,000 a year and it would not be spent until someone commits to that route. He said the airport would not pull the plug on the effort because they are not paying any interest on the money and are receiving advertising as a result of it. He said the airport would continue offering the incentive for at least another three years before pulling the plug. He said this is just the airport's side of it and it would also depend on what DOT/PF and Fairbanks want to do.

Number 0997

CHAIRMAN COWDERY asked what the benefit dollars were of a jumbo jet landing.

Number 1011

DOYLE RUFF, Manager, Fairbanks International Airport, Department of Transportation and Public Facilities, was next to testify. He said a detailed analysis was done to determine economic impact. He said one 747 landing once a week for one year is just a hair under \$1 million direct spending in Fairbanks. He said the bulk of that is to the fuel supplier. The rest of it is in fees to the airports with the direct fee being \$1,400 per landing between the fuel flowage fee and the landing fee based on the gross weight of the aircraft. He said the other direct spending income is to the ground handlers, the food suppliers, hotels and the other dragon's tail of support services. He clarified that he is talking about

cargo traffic as there is no international passenger traffic that is occurring now.

Number 1084

REPRESENTATIVE PHILLIPS asked how many cargo flights on a weekly basis are landing in Fairbanks.

Number 1090

MR. RUFF said there are 23 to 25 flights on a scheduled basis.

Number 1098

REPRESENTATIVE PETE KOTT referred to the Pioneer Incentive Program and asked if any firm commitment had been given to the \$500,000 trying to be raised by the private sector.

Number 1121

COMMISSIONER PERKINS said there appeared to be a firm commitment with the Anchorage Convention and Visitors Bureau. He said others are close to being committed. He said that nothing will be committed until the deal is signed for two years.

Number 1169

MR. PARKAN said the folks that are going to be committing money will be sitting down at the table during negotiations with the carrier to decide what their commitment is going to be. He said it is hard to say how much until we sit down with the carriers.

Number 1185

REPRESENTATIVE KOTT asked if there were competing interests out there in some of the other Western states that offer the same type of incentive program.

Number 1195

MR. PLUMB said Memphis spent a considerable amount of money, as much as \$5 million to try to get KLM in there by putting up a couple of international gates. He said the Port of Seattle spent approximately \$10 million to buy some buildings from NorthWest, NorthWest in turn leased them back for around \$70,000 a year. He said eventually the port is going to need that. He said some large expenditures are spent just trying to attract carriers in there. He said, in Seattle, the deal was to start a Hong Kong twice weekly flight, going up to three times a week. He said there is a reasonable precedent to set up some sort of incentive.

Number 1253

MR. PLUMB said the airport is getting the byproduct of this as they have been in Aviation Week and other publications. He said it has just been marketed around the world and they haven't spent that much. He said this has not been the intent, but have gotten more out of this proposal then has been spent so far. He said, realistically, no one is going to make a deal for \$500,000 a year. Japan Airlines was bleeding to the tune of \$1 million a day and \$500,000 can be lost over two flights. He said no one is going to make a deal to fly here for two years for \$1 million, the economics do not work that way.

Number 1300

REPRESENTATIVE KOTT asked if the airlines were required to stop over in Alaska or if it was the final destination.

Number 1311

MR. PLUMB said if it is a domestic carrier that can come from Norito to Anchorage unload, pick up passengers and continue on to Minneapolis. He said this is the probable scenario as this is the closest deal right now. He said if Japan Airlines or ANA coming out of Norito, Osaka, Nagoya or Chitose and stopped at Anchorage and could not pick up passengers, there would not be much incentive because they would in fact be losing revenue as that seat would be vacant. He said for internationals it would have to be a turn around and for domestics it did not matter.

Number 1366

REPRESENTATIVE KOTT asked if there was an dialogue occurring with the state's federal delegation to perhaps open up the opportunity for those foreign carriers to pick up traffic here on their destination to wherever. He also asked if there was an ongoing dialogue that would offer some type of relief concerning visas. He said those passengers coming over could get off and spend four or five days benefitting the small mom and pop shops in the Anchorage or the Fairbanks area.

Number 1399

MR. PLUMB said there has been a considerable effort for the visa waiver program, especially with Korea. He said the Administration here in Alaska as well as the delegation in Washington has been supportive of this. He said there have been some strong opponents of this, people who are fearful of having people come over and stay longer than they should. He said there is not a great potential that this will happen in Alaska, but it would be a potential down in the Lower 48. He said, "with the other area, I'm not sure if the delegation's been contacted or not. I yield to Deputy Commissioner Parkan."

Number 1445

MR. PARKAN said in terms of contacts with the delegation concerning opening up rights for international carriers, he knows that there has been an expressed interest by the delegation regarding bilateral negotiations. He said a lot of this centers on the Department of State negotiating a deal with Japan. He said the state is interested in, but not at the table concerning, the negotiations of the bilaterals.

Number 1493

MR. PLUMB said this is a very technical area and right now they are seeing a lot of bilaterals. He predicted that it will go into a more multi-lateral and eventually open skies. He said if they go to open skies then they won't have to go through all of these negotiations. He said there is so much with regard to quid pro quo as we go through these bilateral negotiations. He said they start very close to those on a weekly basis. He was just talking yesterday with Ed Oppler, a chief negotiator with US DOT who just informed him that Singapore will probably have open skies in the near future.

MR. PLUMB said the airports make their intentions known to them through telephone contact and through the Airports Counsel International. He said everyone has the same objective, but the U.S. doesn't want to give away something that would reduce the negotiating position with regard to leverage with a country holding the U.S. hostage either by not permitting one of our carriers to operate freely there or by charging them what could be considered an exorbitant amount. He said this area of negotiation usually stays on the U.S. DOT and State Department side as opposed to getting tied in the legislative side.

Number 1564

REPRESENTATIVE MULDER asked how the state compares with other airports along the West Coast. He asked if the route decision was based on money or were other factors considered regarding both cargo and passenger service.

Number 1585

MR. RUFF asked if he was primarily speaking to what it costs a carrier, whether it was are passenger or cargo carrier, to operate in Alaskan airports as compared to airports on the West Coast.

Number 1604

REPRESENTATIVE MULDER asked how the state was competing, are we at an advantageous position.

Number 1612

MR. PARKAN said Alaska has an ideal location so the state competes very well, particularly in terms of cargo traffic but also international passengers to a certain extent. He said location is a considerable factor. He said the landing fees are comparable to other West Coast airports.

Number 1641

MR. PLUMB said location is important, but not everything and pointed to the fact where passenger traffic technology can change. He said it is imperative that the state take this opportunity to capitalize on the globalization of the aviation industry. He said there is an emerging market in the Pacific. As we see that grow there is going to be a great thirst to go ahead, locate, build infrastructure and do things. He said it is like water seeking a level, if the state does not exercise the opportunity at this time or take advantage then other markets will be found such as Petropavlovsk, Khabarovsk, Vancouver or Edmonton. He said while the economics might not be exactly right, the state must take advantage of it at this time. Certainly we must do this in the cargo area.

MR. PLUMB said the reason for the advantageous position is because of location. He said the cargo carriers work on very, very small margins. He said you have the next day products such as overnight mail which yield \$16 to \$17 a pound. He said when you start to get to what is considered the "bottom feeders" you might be getting down to .60 cents, .70 cents or even \$1 a pound which creates margins that are very close. He said if you can stop in Anchorage with 68,000 pounds and save 68,000 pounds of fuel, that means you can upload 68,000 pounds of cargo. He said, done on a daily basis, this adds up to millions of millions of dollars in the long run.

Number 1729

MR. PLUMB said the passenger side is different because the load is not as important. He said when we travel we like to get from Point A to Point B with very little interruptions. He said it is going to be very tough to get into the passenger market. He said if it can be tied into the cargo side, Alaska will become more attractive.

Number 1777

MR. RUFF said the rates and charges to the air carriers are very favorable, be they passenger or cargo, be they international or domestic, compared to other major airports such as Vancouver or airports on the West Coast. He said for all cargo the Anchorage airport ranks number one and Fairbanks then moves down to number 37. He said those positions tell us how we are doing in those

areas. He said during the heyday of the duty free concession the state was guaranteed an income of \$14 million. He said the international traffic went to zero, but it is now slowly building back up.

MR. RUFF said, on the domestic passenger side, Alaskans enjoy being a heavily targeted tourist destination with steadily climbing passenger traffic. He said the state must cover every base to the time that Russia might be a competitor with Alaska. He said that is why the runway extension projects at both airports are so important, to keep this international business. He said we must continue to pursue these areas to continue to do well into the future.

Number 1900

MR. RUFF said everything about servicing in Russia, from the tarmacks to the quality of the fuel, is not there and a will be a long time in coming. He said, by that time, Alaska wants to be so solidified that this is the Text-Stop hub.

Number 1926

MR. RUFF referred to the incentive program and said it is important that we know what the role of the airport is, that we don't misidentify ourselves. He said this happened in Portland when they attempted to compete with Sea-Tac. He said when they shifted gears and focused more on cargo development they did well. He said the role for both airports in Alaska is clearly defined.

Number 1982

ADJOURNMENT

There being no further business to conduct, CHAIRMAN COWDERY adjourned the meeting of the House Special Committee on International Trade and Tourism at 12:30 p.m.

APPENDIX

I

MISCELLA- NEOUS BACK-UP

Alaska

INTERNATIONAL TRADE PROFILE

Global demand for resources complements Alaska's great wealth of fish, timber, oil and gas, minerals, and coal. The rapid growth of Alaska's export sector reflects an increase in global demand. Over the last ten years, Alaska's exports have grown 137 percent reaching \$2.48 billion in 1994.

However, given the commodity make-up of Alaska's exports, the total value of Alaska's exports for 1994 was significantly affected by low world commodity prices for the seafood, oil and gas, and mineral sectors. Yet, the volume of exports remained relatively stable.

Fish and seafood is Alaska's top export commodity. In 1994, the seafood industry generated \$1.2 billion of exports from Alaska. These exports comprised 41.7 percent of total U.S. fish and seafood exports.

Timber exports amounted to \$450 million (1994). The Japanese market made up 81 percent of total timber exports. South Korea, Taiwan, China, and Canada accounted for most of the remaining exports.

Much of Alaska's crude oil is federally mandated for domestic use, yet crude petroleum and natural gas can be exported from the Cook Inlet fields. In 1994, these exports were valued at \$140 million. Petrochemical by-product exports—urea and ammonia—make up 5.9 percent of Alaska's total exports valued at \$125 million.

Red Dog Mine metallic ore and concentrates export sales totaled \$102 million for 1994. Belgium, Canada, Japan, Germany, and South Korea made up the top five markets for mineral exports.

Usibelli Coal mine at Healy is the state's only active coal mining operation. In 1994, the mine exported half of its production at a value of \$23 million to South Korea.

In 1994, Japan continued to be Alaska's top export client with sales totaling \$1.67 billion, 67 percent of total Alaska exports. The South Korean and Canadian export markets ranked second (7.6 percent of total exports) and third (4.3 percent of total exports), respectively. China, Belgium, Taiwan, Russia, Germany, Spain, and Thailand fill out the rank of Alaska's list of top ten export markets.



Foreign Trade Zones (FTZs)

There are currently four FTZs in Alaska: St. Paul, Valdez, Anchorage, and Fairbanks. Goods imported into these areas and subsequently reexported are subject to neither local inventory taxes nor U.S. import duties.

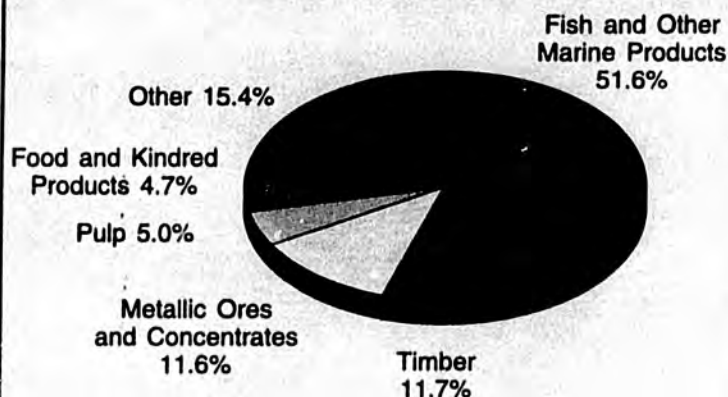
Alaska Cargo & Warehousing

Located equidistant from Northeast Asia, North America, and Europe, Alaska sits at the crossroads of the three dominant economic regions of the world. By virtue of this geographical position, Alaska has become an ideal technical stop and international distribution point for carriers flying between those markets. More all-cargo, wide-body aircraft move through Anchorage International Airport than any other airport in the United States. Approximately 75 percent of all scheduled cargo flights on Europe/Asia and North America/Asia routings come through Alaska.

Top Commodities Exported from Alaska

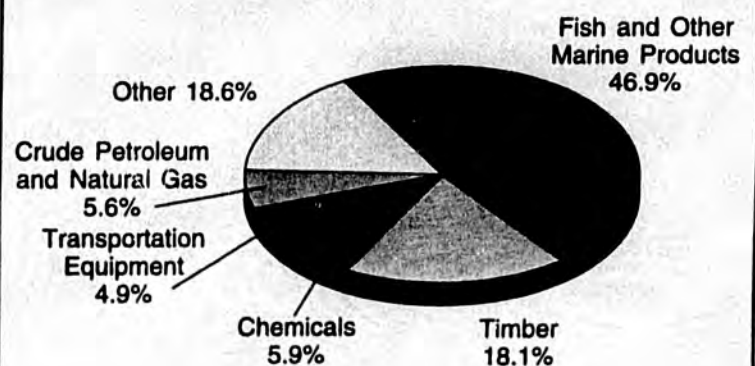
1992

Total = \$3,392,638,722



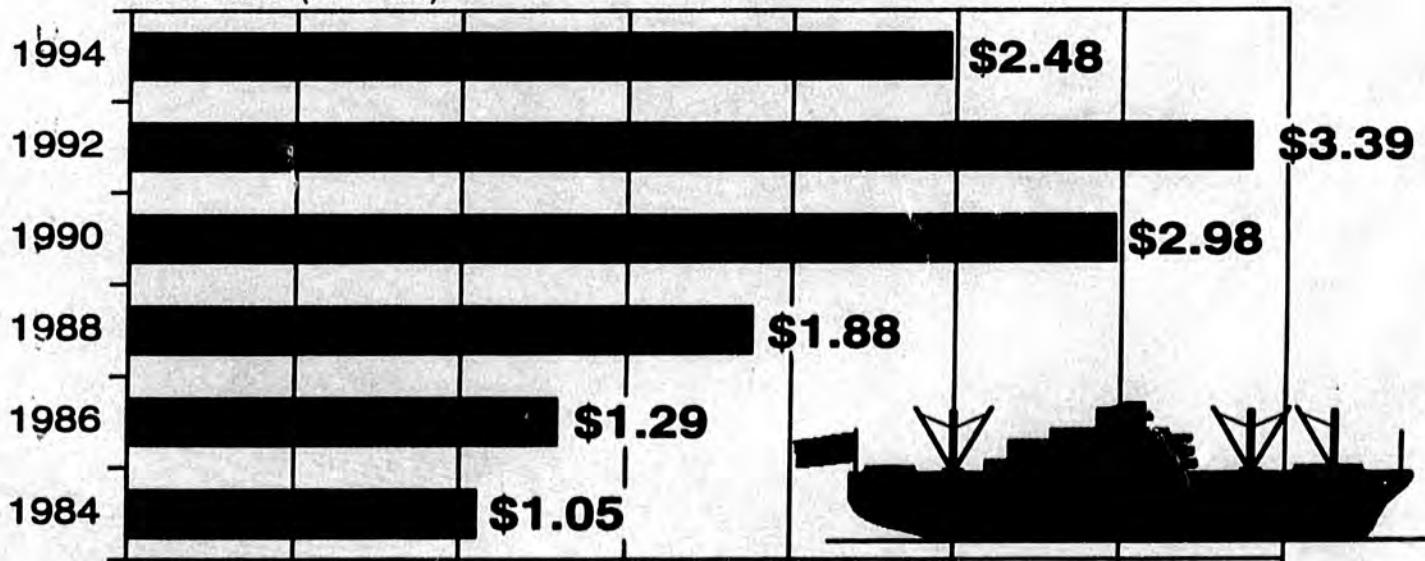
1994

Total = \$2,479,755,952



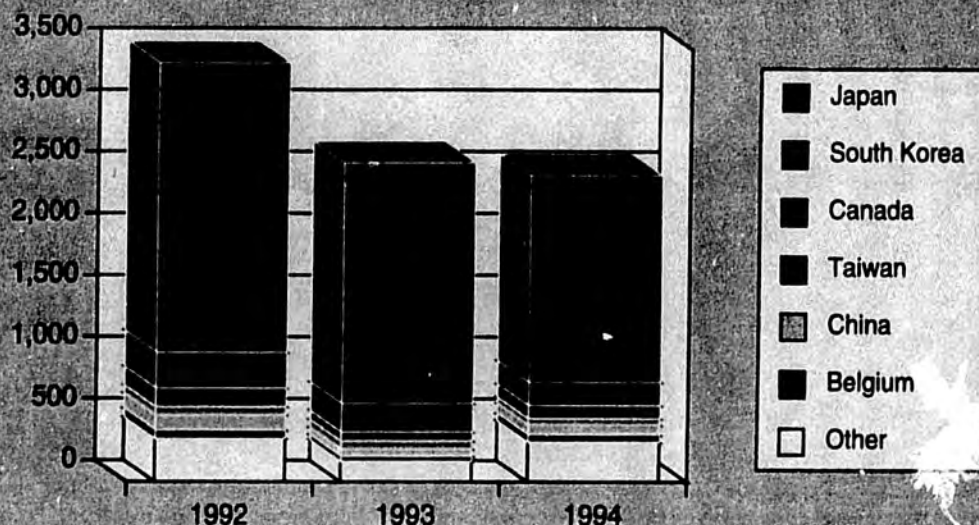
Total Value of Exports Originating in Alaska

U.S. Dollars (In billions)



Total Value of Exports by Destination

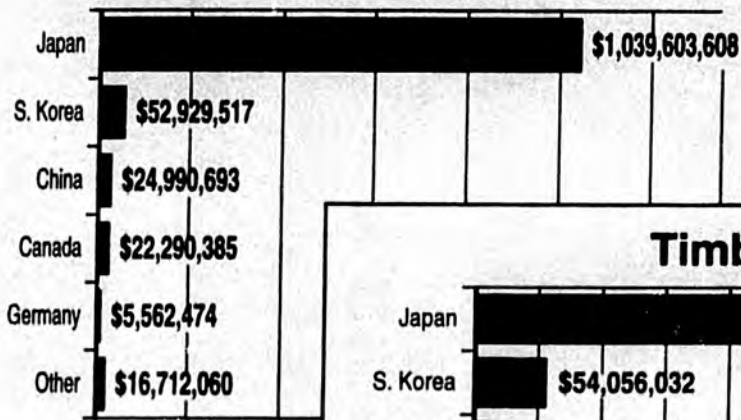
U.S. dollars in millions



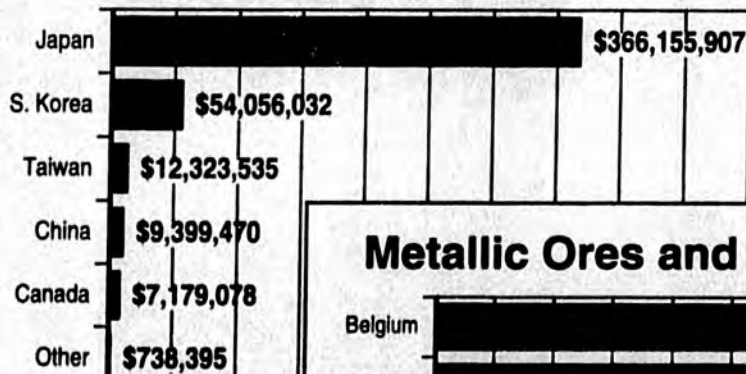
Exports Originating in Alaska by Country of Destination

Ranked by Value of Exports for 1994 • U.S. Dollars

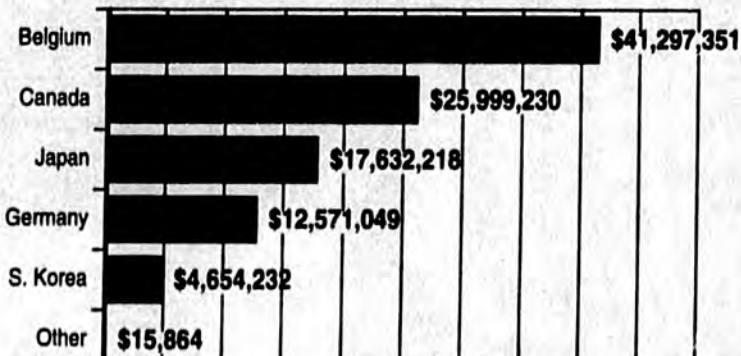
Fish and Other Marine Products



Timber



Metallic Ores and Concentrates



Alaska's Top Three Markets

Japan



The relationship between Alaska and Japan has been long-standing. In 1965, Alaska was the first U.S. state to open an office in Tokyo. In 1971, Japan established a Consulate General in Anchorage.

Japan is the largest market for Alaska seafood, accounting for 90 percent—or \$1.04 billion—of all seafood exports in 1994. Salmon and ground fish are the leading species.

In 1994, the Japanese market comprised 81 percent of Alaska's lumber export. Alaska's light-colored, tightly-grained Sitka Spruce is highly valued by the Japanese consumer.

South Korea



As the economic strength of South Korea has grown, so has its relationship with Alaska. South Korea opened its Consulate General in Anchorage in 1982. In 1985, Alaska opened a trade office in Seoul.

South Korea has become Alaska's second largest export market, accounting for \$189 million of exports in 1994. Timber, seafood, chemicals, coal, and petroleum and oil products account for over 87 percent of Alaska's exports to South Korea.

The growth of Alaska timber exports to South Korea is steady. Timber exports totaled \$54 million in 1994.

In 1994, 28 percent (\$53 million) of Alaska seafood products and 19 percent (\$35 million) of Alaska chemical exports were destined for the South Korean market. South Korea will continue to be an important market for Alaska coal.

Canada



A common border and a long history of cooperation have contributed to making Canada Alaska's third largest trading partner. In 1994, the Canadian market accounted for \$106 million of exports. The composition of Alaskan exports to Canada is quite diversified, but the majority of exports comprise metallic ores and concentrates, seafood, petroleum and oil products, food products, and lumber.

Canadian heavy investment and involvement in Alaska's mining industry accounts for a large amount of mineral exports destined for the Canadian market.

Emerging Markets

China

As China's economy continues to grow at a dramatic rate, its need for natural resources increases. In 1994, Alaska exported \$82 million to China, making it Alaska's fourth largest trading partner. Exports of seafood, pulp, chemicals, timber, and transportation equipment rounded out the top five export products.

Taiwan

Taiwan represents one of the most powerful future Asian partners for Alaska. The country ranks as Alaska's sixth largest export market (1994 exports of \$51 million). Pulp, timber, food and kindred products, and seafood comprise 97 percent of Alaska's export commodities to Taiwan.

Russian Far East

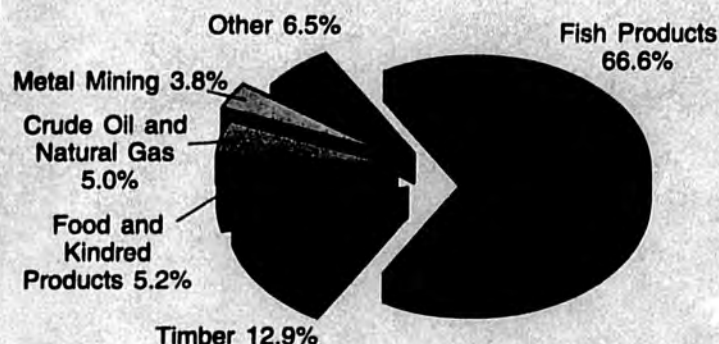
Historical links and proximity have encouraged the rapid evolution of Alaska's trade relationship with Russia. In 1994, Russia rose to Alaska's number seven trading partner accounting for \$46 million in exports. Existing trade ventures include a satellite communications system linking the Russian Far East and Alaska, mining development, wood construction, oil and gas services, heavy machinery, and horticulture.

Direct passenger and cargo air service exists between Alaska and the Russian cities of Anadyr, Providenya, Magadan, Khabarovsk, Vladivostok, Yakutsk, Petropavlosk-Kamchatsky and Moscow.

Exports from Alaska to Japan

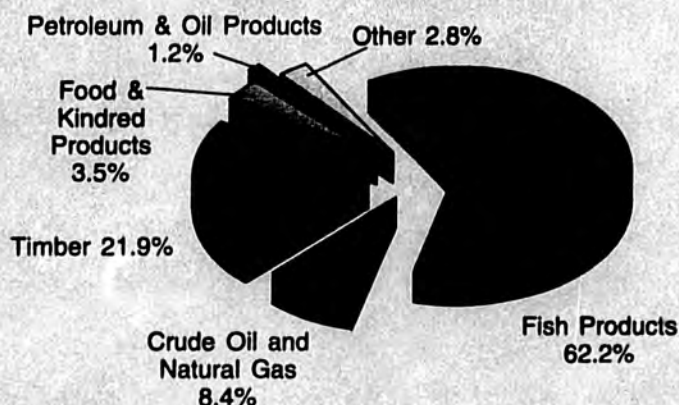
1992

Total = \$2,343,064,255



1994

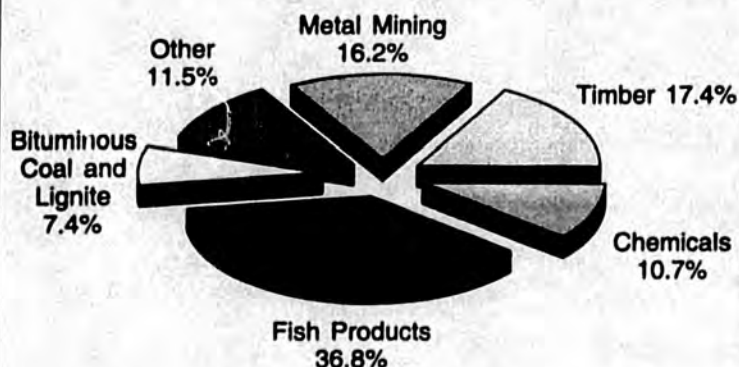
Total = \$1,672,313,637



Exports from Alaska to South Korea

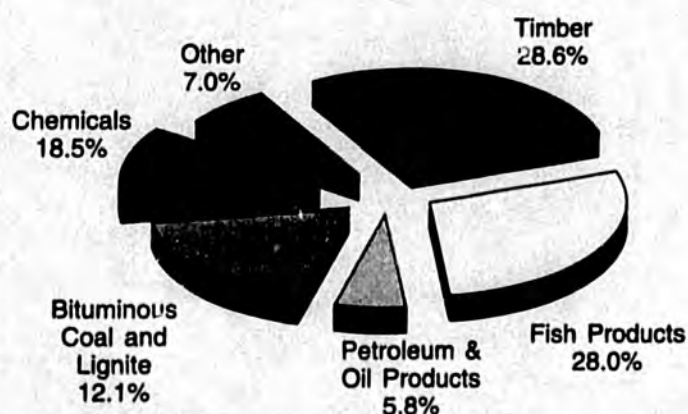
1992

Total = \$291,815,028



1994

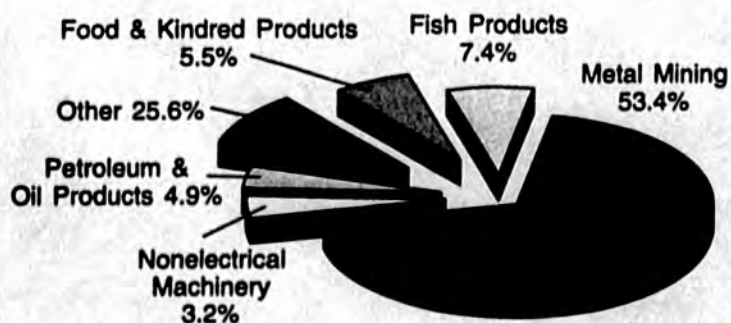
Total = \$189,131,551



Exports from Alaska to Canada

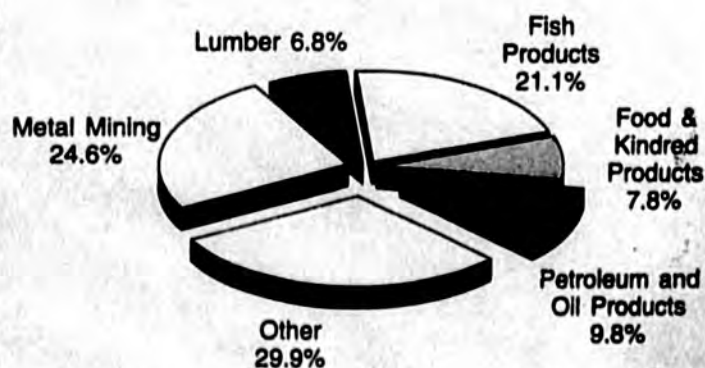
1992

Total = \$150,744,404



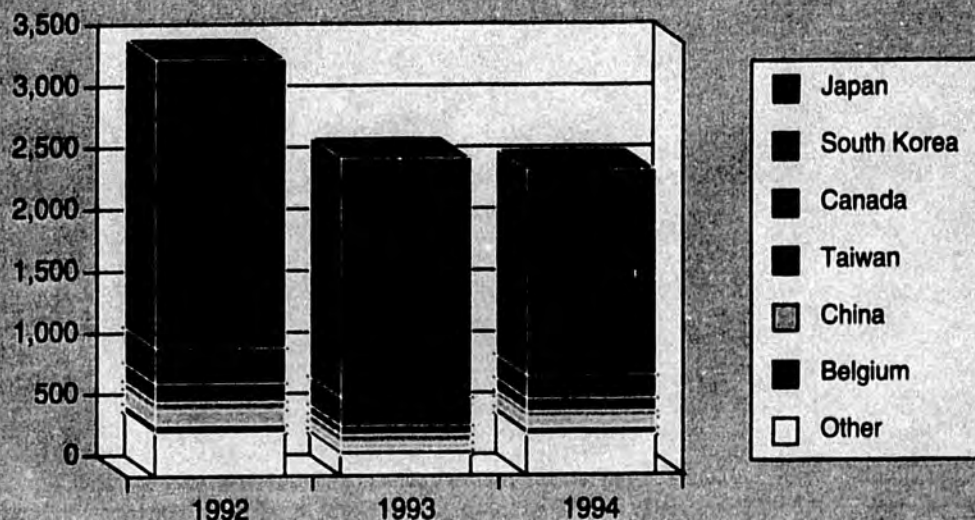
1994

Total = \$105,758,276



Total Value of Exports by Destination

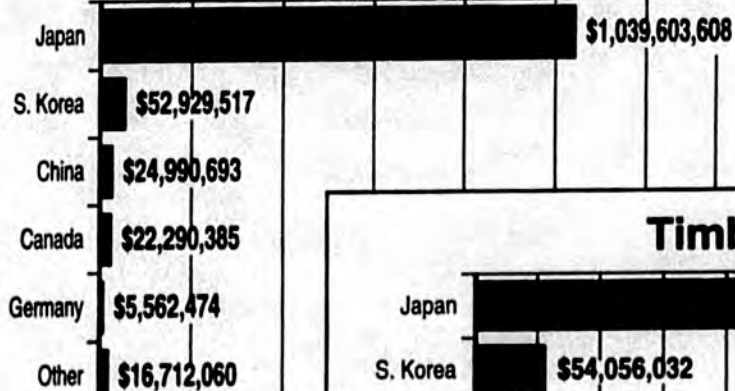
U.S. dollars in millions



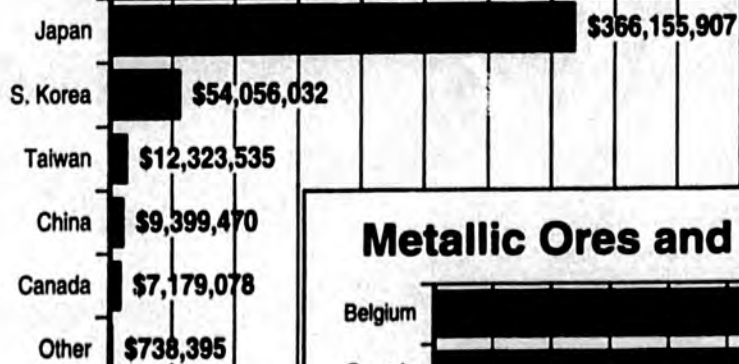
Exports Originating in Alaska by Country of Destination

Ranked by Value of Exports for 1994 • U.S. Dollars

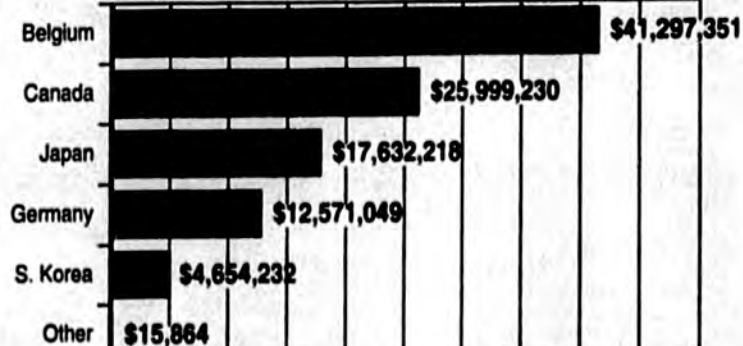
Fish and Other Marine Products



Timber



Metallic Ores and Concentrates





DEPARTMENT OF COMMERCE AND
ECONOMIC DEVELOPMENT

**Office of International Trade
(OIT) Alaska**

3601 C Street, Suite 798
Anchorage, Alaska 99503
Phone: (907) 561-5585
Fax: (907) 561-4577

*OIT also has trade offices located
in Tokyo, Japan; Seoul, South
Korea; and an Honorary Trade
Representative in Taipei, Taiwan.*

*For: Marketing and export
information in Japan, Canada,
Russia, Korea, Taiwan and other
countries.*

**UNITED STATES DEPARTMENT
OF COMMERCE**

**Commercial Service of U.S.A.
International Trade Administration
U.S. Department of Commerce
Anchorage District**

421 West First Avenue, Suite 300
Anchorage, Alaska 99501-1635
Phone: (907) 271-6237
Fax: (907) 271-6242

*For: International marketing plan
development assistance*

**UNIVERSITY OF ALASKA
ANCHORAGE**

**Alaska Center for International
Business & American Russian
Center**

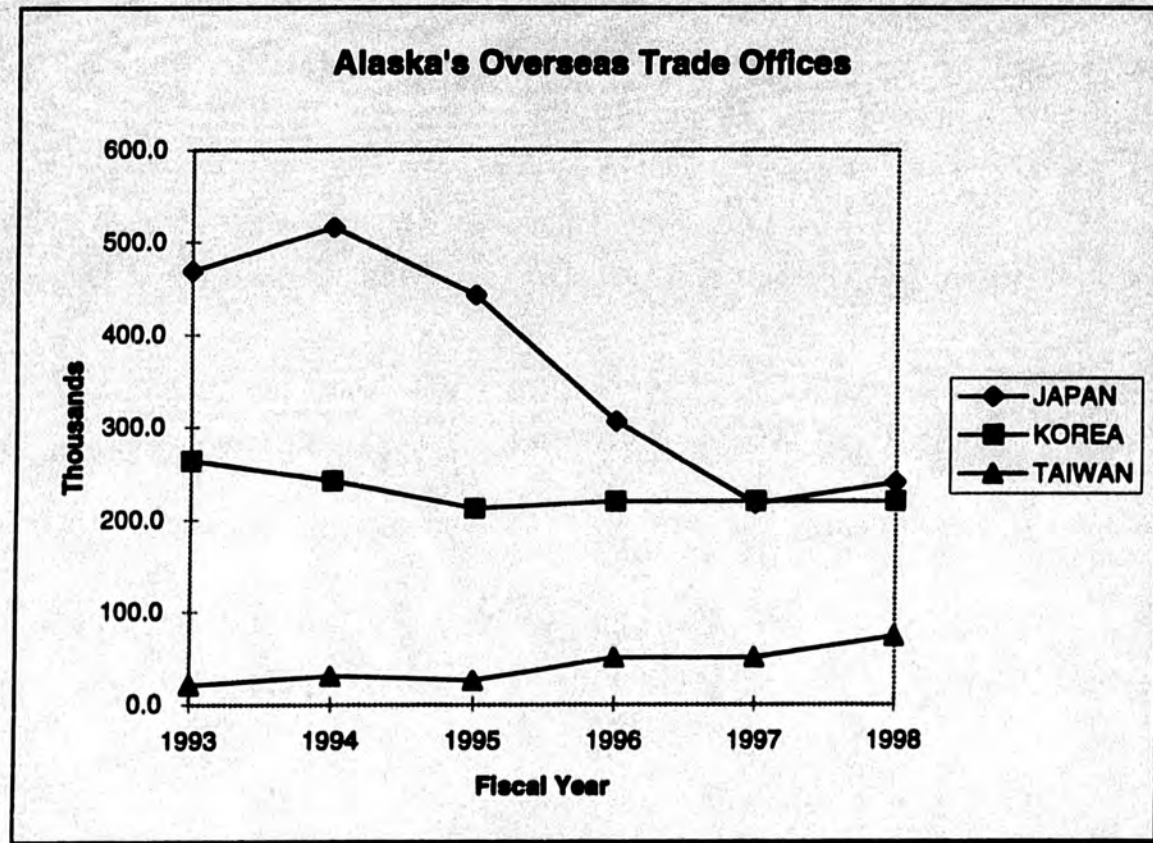
Business Education Bldg.
3211 Providence Drive, Room 203
Anchorage, Alaska 99508
Phone: (907) 786-4300
Fax: (907) 786-4319

*For: Market research, statistics,
and assistance to entrepreneurs
wanting to establish a business in
Russia*

World Trade Center Alaska
421 West First Avenue, Suite 300
Anchorage, Alaska 99501-1635
Phone: (907) 278-7233
Fax: (907) 278-2982

*For: Trade leads, World Trade
Center Network*

**ALASKA'S OVERSEAS TRADE OFFICES
HISTORICAL BUDGET INFORMATION**



Fiscal Year	JAPAN	KOREA	TAIWAN
1993	468.9	263.4	20.0
1994	516.0	242.0	30.0
1995	442.0	212.0	25.0
1996	306.0	220.0	50.0
1997	217.3	220.0	50.0
1998	240.0	220.0	73.1

authorized, all funding sources

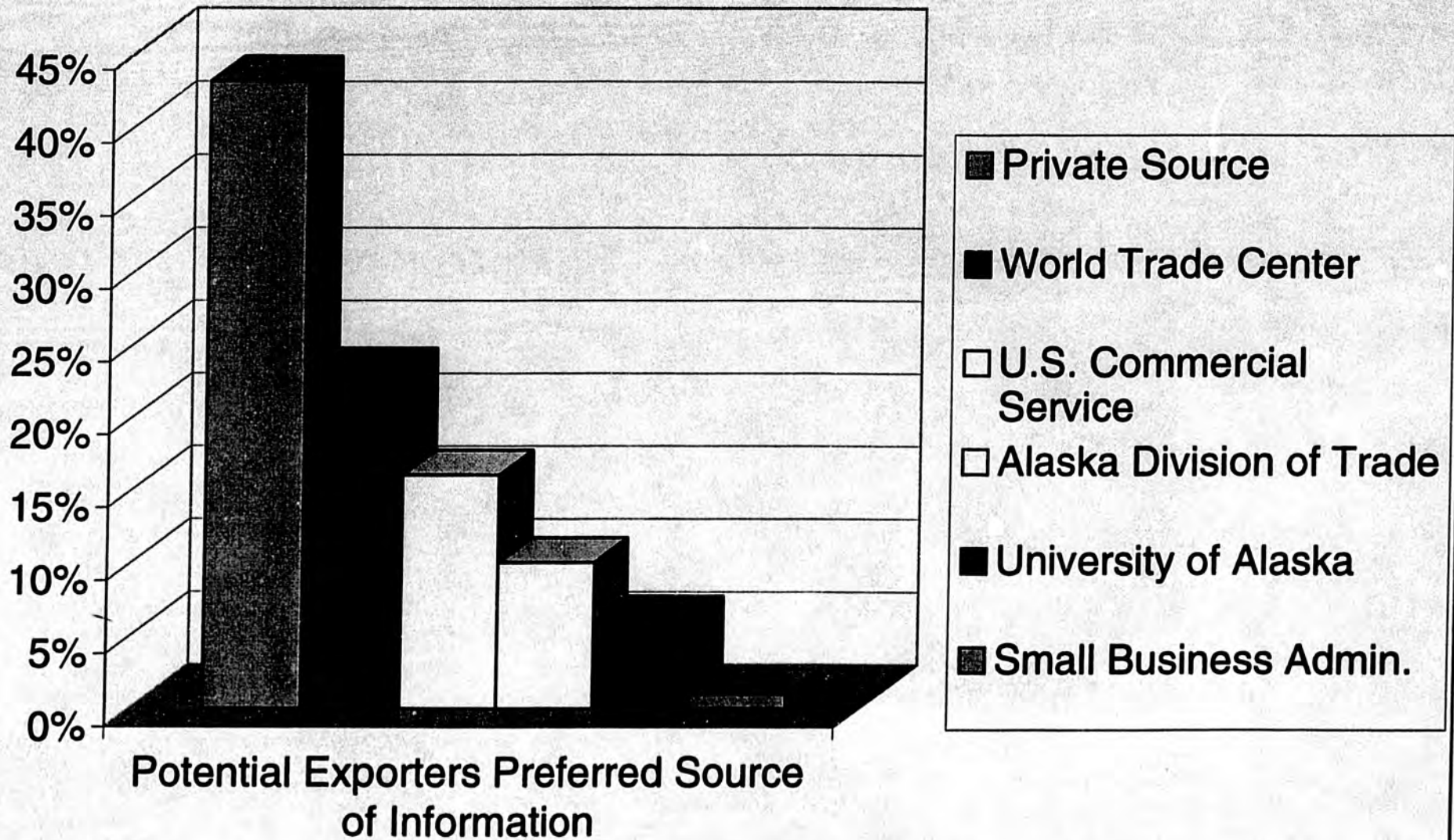
MEMORANDUM

To: Representative Mark Hanley, Co-Chair House Finance
From: Senator Drue Pearce, President of the Senate
Representative Gail Phillips, Speaker of the House
Date: April 23, 1996
Subject: Budget Reductions/Reallocations on International Trade

Pursuant to the attached resolution recently passed by the Senate/House Interim Task force on International Trade, I wish to request your assistance in following through with specific budget recommendations supported by private industry testimony at the Task Force Hearings. Specific recommendations are as follows:

- \$500,000 - transferred from UAA's Alaska Center for International Business (ACIB) to the General Fund or the Department of Revenue. Public record supports these funds can more effectively be utilized as outlined in the following manner.
- + \$128,000 - transferred from the General Fund/Dept. of Revenue to the World Trade Center Alaska to provide a more consolidated International Trade information source;
- + \$100,000 - transferred from the General Fund/Dept. of Revenue to the University of Alaska Fairbanks to further support the international business degree program.
- + \$200,000 - transferred from the General fund thru AIDEA to support the establishment of a Finance Export Assistance Specialist to be collocated in the World Trade Center Alaska and U.S. Foreign Commercial Service offices.

Potential Exporters Would Turn To:



Author: Priscilla_Wohl@commerce.state.ak.us at CC2MHS1

Date: 1/12/98 11:15 AM

Priority: Normal

TO: Peter Torkelson at LAA_TRANS

Subject: Establishing a Business in Alaska

Peter - following is the information you requested regarding number of copies of the Establishing a Business in Alaska brochure. These numbers represent number of copies distributed in 1997. The cost for these is \$11.50 via the mail and \$8.00 in person. We encourage folks to use the web

site and save money. We have a handout at the counter with the web site address on it that we give out. Most requests come from folks who have just turned in their business license application!

Let me know if you need additional information. Priscilla

Forward Header

Subject: Establishing a Business in Alaska

Author: Robin Boysen at DCED_FRONT

Date: 1/12/98 10:23 AM

153 copies over the counter

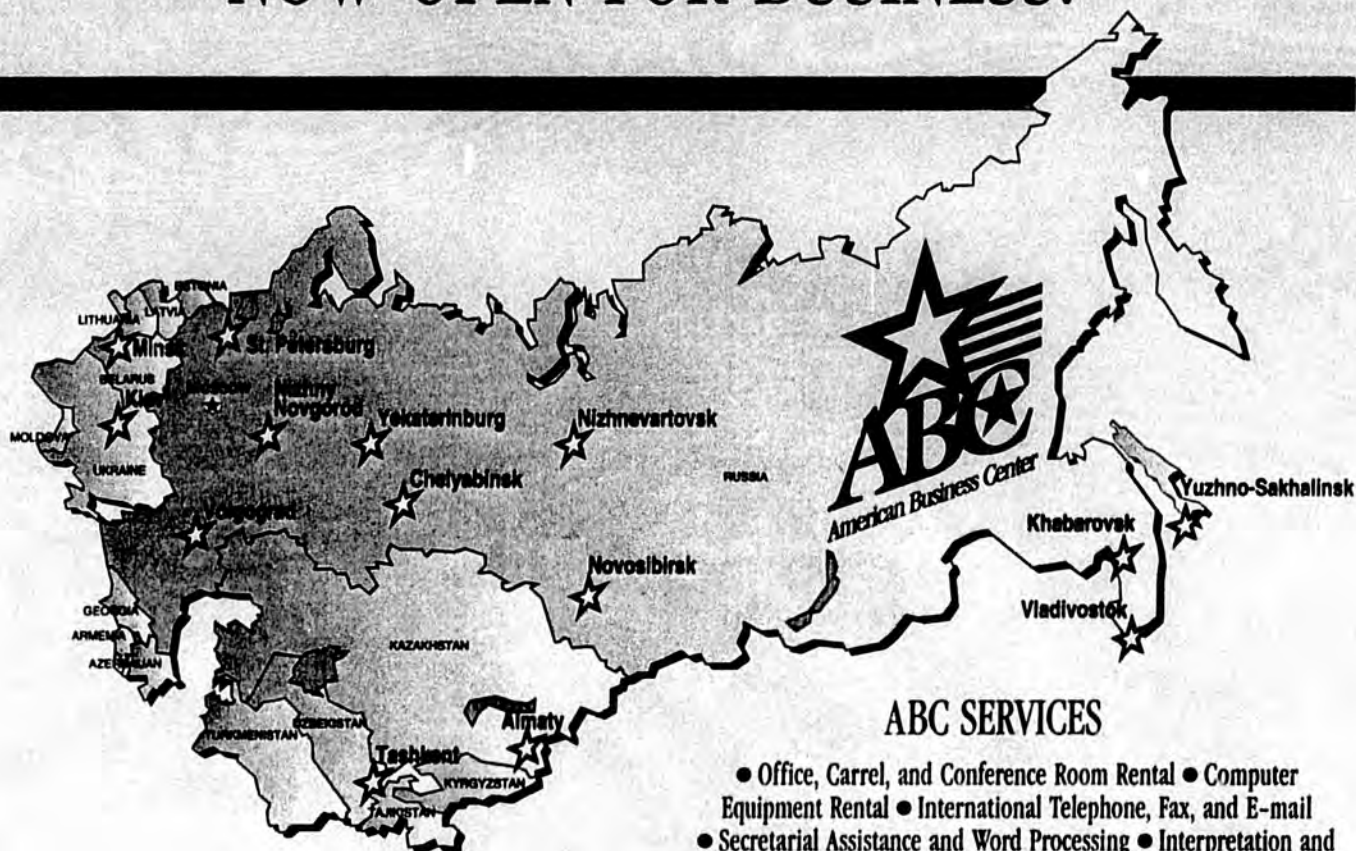
14 ordered by mail

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Voice Mail: (202) 482-4655, option #21

Flashfax: (202) 482-3145, document #7022

or

look us up on the Internet at:

<http://www.itaiep.doc.gov/bisnis/abc/abc.html>



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THANK YOU FOR YOUR BUSINESS!

Author: liz.hasbrouck@aspeninst.org (Liz Hasbrouck) at CC2MHS1
Date: 2/10/98 2:03 PM
Priority: Normal
TO: Peter Torkelson at LAA_TRANS
Subject: Re: FWD>>International Trade

Mr. Toreklson:

"The International State: Crafting a Statewide Trade Development System" was published in 1996 by the Aspen Institute's Rural Economic Policy Program (REPP). It is available for \$15.00 (postage paid) through the Institute's Publications Office, PO Box 222, Queenstown, MD 21658. Orders must be prepaid with a check or money order; faxed credit card orders are accepted, but MUST BE SIGNED by the cardholder. Be sure to include all pertinent information, such as credit card name, number and exp. date, as well as a complete mailing address. Fax to Tonya Downes at 410-827-9174.

If you wish to contact Ms. Conway, I must refer you to Meriwether Jones, the Director of REPP, at meriwether@aspeninst.org

Regards,
Liz Hasbrouck

Date: 2.10.98 12:40 PM
To: Liz Hasbrouck
From: Sylvia Pear

Date: 2/9/98 4:35 PM
From: Peter
Greetings from Alaska.

I am trying to make contact with Ms. Carol Conway about a publication she was involved in concerning International Trade Assistance (state) programs. I am informed that her report may have been released through the Institute. Are you aware of such a publication or do you know how I may contact Ms. Conway?

Peter T.

----- RFC822 Header Follows -----
Received: by aspeninst.org with ADMIN;9 Feb 1998 16:33:34 +0100
Received: from laa_linux.legis.state.ak.us (root@laa_linux.legis.state.ak.us [146.63.202.106]) by smtpmail1.legis.state.ak.us (8.8.5/8.7.3) with ESMTTP id MAA16969 for <dave.austin@aspeninst.org>; Mon, 9 Feb 1998 12:30:51 -0900
Received: from legis.state.ak.us ([146.63.193.101]) by laa_linux.legis.state.ak.us (8.8.5/8.7.3) with ESMTTP id MAA05643 for <dave.austin@aspeninst.org>; Mon, 9 Feb 1998 12:30:50 -0900
Message-ID: <34DF754B.BB16F39@legis.state.ak.us>
Date: Mon, 09 Feb 1998 12:29:47 -0900
From: Peter <Peter_Torkelson@legis.state.ak.us>
X-Mailer: Mozilla 4.03 [en] (Win95; I)
MIME-Version: 1.0
To: dave.austin@aspeninst.org
Subject: International Trade
Content-Type: text/plain; charset=us-ascii
Content-Transfer-Encoding: 7bit

*order it
put it on my
or John's card.*

Author: Priscilla_Wohl@commerce.state.ak.us (Priscilla Wohl) at CC2MHS1
Date: 4/8/98 11:27 AM
Priority: Normal
TO: Peter Torkelson at LAA_TRANS
Subject: Re[2]: "Trade Mission"

Peter - A trade mission can either be "in-coming" or "out-going". I will use Japan as an example to describe these.

In-coming trade missions originate from Alaska and are made up of Alaska business and, sometimes, Trade staff or Government representatives. The Japan Office will do the initial planning for activities, meetings etc in Japan; meet the mission and brief them on their itinerary, and most often accompany the mission to the meetings.

An Out-going mission is Japanese businesses and government leaders visiting Alaska. The Japan Office would assist in determining their objectives for the trip, work with the Alaska Trade Program in establishing their itinerary, and conduct a post-mission interview/survey to determine the effectiveness of the mission and gather information for follow up for Alaska companies.

The numbers of missions reported vary by country, but generally there is considerably more trade mission activity through the Japan and Korea Offices than with Taiwan, although we hope to see this change. Also, Ida Yao, our Taiwan Representative, may not be counting all of the delegations which are counted as a mission - essentially any incoming/outgoing group that is provided assistance by the office.

Hope this helps. Let me know if there is any further information that you need. Priscilla

Reply Separator

Subject: RE: "Trade Mission"
Author: Peter_Torkelson@legis.state.ak.us (Peter Torkelson) at CC2MHS1
Date: 4/7/98 2:40 PM

Hello,

I was reviewing
with a question
dozens of "tr

What is the d

Thanks,

Peter

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had just 5.

file or trash

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>RCPT TO:<Priscill
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>Received: from ccbridge.legis.state.ak.us (ccbridge.legis.state.ak.us [146.63.2
02.114]) by smtpmail1.legis.state.ak.us (8.8.5/8.7.3) with SMTP id OAA14037 for

<Priscilla_Wohl@commerce.state.ak.us>; Tue, 7 Apr 1998 14:43:54 -0800
>Message-Id:<199804072243.OAA14037@smtpmail1.legis.state.ak.us>
>Date: Tue, 07 Apr 1998 14:40 -0900
>From: "Peter Torkelson" <Peter_Torkelson@legis.state.ak.us>
>To: "Priscilla_Wohl@commerce.state.ak.us" <Priscilla_Wohl@commerce.state.ak.us>

>Subject: RE: "Trade Mission"

SCOMM

103:3

MEMORANDUM

Representative John Cowdery

TO: SEN. MIKE MILLER, SENATE PRESIDENT
REP. GAIL PHILLIPS, SPEAKER OF THE HOUSE
FROM: REP. JOHN COWDERY *JC*
DATE: MARCH 10, 1997
RE: ALASKA'S ROLE IN SAKHALIN
CC:

NOTE: Hearing on March 20th at 3:30 pm,
Butrovich Room

BR

The purpose of the hearing is to bring the legislature and public up to date about events and opportunities for Alaska in Sakhalin.

Briefings will be given by Steve Smirnoff- Russian Consulate, Division of Trade & Development, Marathon Oil, Lynden Air Freight, Exxon, World Trade Center, Alaska Center for International Business, The Alliance, Chuck Becker, Reeve Airlines, Alaska Airlines, C.L. Wareham, Arctic Camp and Equipment, and others yet to confirm.

The briefers will impart their knowledge about Sakhalin's development and what they see as the State of Alaska's role.

Ultimately, the legislature must make a decision whether the State of Alaska will commit any portion of the budget to facilitate our business community's opportunities in Sakhalin.

Alaskans have an inside track because of our proximity and similarity to Sakhalin. However, competition is stiff. Alaska Airlines indicates that they are carrying many more passengers from Seattle to Sakhalin than from Anchorage to Sakhalin.

International corporations like Marathon, Exxon, other oil companies, and their support service companies, operate in both Alaska and Sakhalin. However, this does not mean that they will put Alaskan

MEMORANDUM
Senator Mike Miller
Rep. Gail Phillips
Page 2

interests first. They are international players whose geopolitics are much broader than Alaska.

What I have learned from many conversations with a variety of Sakhalin-watchers is that Alaska will only play a significant role if some kind of government to government accommodation is made.

The legislature and the governor will have to decide in what form the accommodation will be, and how much we are willing to spend.

The approach being taken by the governor is to set up an office in Sakhalin and hire a local consultant there. Many others are doing the same thing.

I asked Smirnoff what would happen if we reversed the approach and invited Sakhalin to set up an office in Alaska. In this way, our private sector could contribute office space, telecommunications, etc. The government to government accommodation could be that Sakhalin makes their Alaskan office their clearing house for investment and contracts with the U.S. We could also offer to pay some of their costs. They could give us weekly intelligence reports, to be defined by contract, that would be useful to Alaskan businesses.

Smirnoff (Honorary Russian Consul) likes the idea. But, it would take some state funding and initiative from the legislature. You, Mr. President and Madam Speaker, may want to make this an initiative on behalf of the legislature. Please let me know how I can assist you.

By: D. Stary, OAA

Testimony to House Oversight Committee

20 March 1997

Representative Cowdery, Chair

On behalf of the University of Alaska Anchorage and our Joint Venture Partners, Bill Stamps of Peak Oilfield Services Company, and Mikhail Krasny of the Russian Academy of Science, I would like to thank Chairman Cowdery and the members of the committee for your kind invitation to testify this afternoon.

I have spent the past 27 years with the University training workers for the resource development industries of Alaska, primarily in oil and gas, but more recently in mining as well. My entire career has been tied up in vocational training in Alaska.

We have a joint venture to establish and operate the "Sakhalin Alaska Technical College" based on the expertise of our JV partners, the Kenai Peninsula College and the Mining and Petroleum Training Service. This College will be developed jointly by the joint venture and the operators of the Sakhalin oil and gas projects. We will attempt to do on Sakhalin what we have been doing in Alaska for the past 27 years. This College will ultimately address training in other resource industries including forest products, fisheries and environmental technology.

Our involvement with Sakhalin Island began over two years ago, first with the sister city relations on the Peninsula, Kenai with Okha and Soldotna with Nogliki. Borough Mayor Don Gilman, Kenai Mayor John Williams and Soldotna Mayor Ken Lancaster introduced us to the many Sakhalin delegations to Alaska which demonstrated their intense desire to share in oilfield technology training. This interest and desire was included high on the first Alaska Sakhalin protocols signed by Governor Hickle, later reaffirmed by Governor Knowles.

We learned that one of our Alaskan friends, Tom Brooks with Marathon Oil Company was leading the Sakhalin Energy group in Yuzhno-Sakhalinsk. Mr. Brooks was kind enough to introduce us to the rest of the operators on Sakhalin and suggested the approach we should take with respect to training the Russian workforce. His advice was accurate, useful and saved a great deal of time.

Testimony/3/20/97/12:20 PM

We began by a thorough needs assessment including polling the operators, and conducting certification training for Russian workers to determine as to their needs their competence. From this process came the ultimate training strategy. This strategy has just been reinforced by Sakhalin Energy training personnel who have just returned from Sakhalin. At this time we are working closely with both Sakhalin Energy and Exxoneftgaz regarding the direction the project will take.

Our purpose is twofold. First to fulfill the intent of the Alaska Sakhalin protocol and second to provide a means of showcasing Alaskan technology and expertise. Our hope is that Alaskan business will be able to market their expertise through the medium of participating in classes involving potential clients for their goods and services.

After Prudhoe, this may be the greatest opportunity for our businesses to sell their services that we will ever see. The advantages of our special expertise in offshore and onshore drilling, development, transportation, logistics and environmental protection in the arctic and sub arctic may never see this kind of opportunity again.

The Sakhalin is intimidating to many Alaskan enterprises. It is complicated beyond any American understanding with taxes and regulations from many levels. The Petrosak refinery on Sakhalin is subject to 68 separate taxes before the product even ships from the facility, and many more before it reaches the consumer. Customs, living standards, medical and dental services, transportation and sanitary facilities may not meet modern Alaskan expectations. Beside the language barrier, there is a cultural gulf which can and must be bridged in order for effective commerce to take place. Those who are active on Sakhalin right now are the leaders. They are the ones who are willing to assume the risks and pave the way for those to come.

The situation has many parallels to the Alaskan gold rush era. The people people in that era who had the fortitude to come to Alaska essentially made it possible, or at least much easier for everyone who followed. Those pioneers did not have an easy time of it, but I suspect every real Alaskan considers them real heroes of our state.

In the Global Economy, individuals cannot participate or even survive without secure, fundamental support from their government. In my opinion, and I do not claim to be an old Russian hand, without the full support of both the Legislature and the state Administration, Alaskans will be shut out of the Sakhalin Island development. This is fundamental.

There are several organizations which have contributed to our progress. First, the Department of Commerce and Economic Development has probably be the greatest resource. They have provided introductions and windows that we would never had access to in any other way. The Department parallels Russian governmental expectations and mirrors the way they expect to do business. I send Commissioner Hensley and his people our most sincere thanks.

Testimony/3/20/97/12:20 PM

The American Business Center is gratifyingly prompt and effective. An e-mail sent at 0800 Alaskan time usually has a complete and accurate response by 1400 hours. (Sakhalin time is Alaska -4 hours) Several times they have enabled us to meet critical deadlines, and in the process have saved us many thousands of dollars.

Alaska has a number of organizations which provide essential services to business on Sakhalin and the Russian Far East. My personal concern is that there is considerable overlap and duplication of effort with resulting loss of focus. We recommend that a task force of persons already involved in business on the island be formed to evaluate the various service groups and recommend effective roles for each which will make the greatest use of their individual expertise. The task force should be charged with developing an accurate description of who is responsible for what and communicating that information to the interested business community.

I would encourage you to consider making Alaskan Sakhalin Joint Ventures which meet strict guidelines eligible for business loans and even grants in some instances where the interests of the state are involved.

Finally, the actions of the legislature and administration toward Sakhalin and the entire Russian Far East should be models of democratic efficiency. Swift decisions, and equally swift implementation of our policy would I believe send an effective message to the Sakhalin administration and the Russian Duma that economic development is dependent upon reasonable governmental policy, promptly developed and promptly implemented.

I and myJV partners, as well as our parent organizations are excited about our role in bringing Alaska and Sakhalin closer together. We have received the finest kind of encouragement and participation from the operators, government and industry on Sakhalin. We believe this is because we did our homework and confined ourselves to areas where we had the greatest expertise.

I am extremely pleased that the legislature and Chairman Cowdrey have held this hearing. It indicates a high level of awareness on the part of the legislature of the potential rewards the state and our people might achieve by becoming real partners with our neighbors on Sakhalin.

I hope your interest will continue, and we will do our best to keep you informed about our progress and our success. We hope our project meets with your approval, and we hope we can count on your support.

RECEIVED

MAR 20 1997

Ans'd.....

DATE: March 11, 1997

COMMENTS: Charles Becker, Director
USDOC, Alaska Export Assistance Center

REFERENCE: Alaska - Sakhalin Island Legislative Overview

CHAIR: Representative Cowdery

Thank you for inviting us to participate in your overview hearing on development activities on Sakhalin Island. The Committee's timing is most fortuitous since we have with us a key member of the U.S. diplomatic corps, Timothy (Tim) Smith, Principal Commercial Officer, at the American Consulate General in Vladivostok, Russia. Mr. Smith is prepared to respond to any questions you or members of the Committee may have.

I will address your questions directly. I am the Director of the Alaska Export Assistance Center here in Anchorage. The Center is a unit of the U.S. Commercial Service of the United States Department of Commerce. Domestically, the Commercial Service operates 75 Export Assistance Centers nationwide. Abroad, we are located in 135 cities in 65 key foreign markets. Our mission is to help U.S. companies successfully penetrate these markets with sales of their products and services.

For Sakhalin specifically, the Commerce Department has funded one of a network of 14 American Business Centers operating in key locations throughout Russia and other countries of the former Soviet Union. The ABCs, as we call them, provide American companies with western business services such as office space and equipment, rental, international telephone, fax and e-mail capacity, scheduling, meeting arrangements, travel assistance, counseling and market research. As you know, Governor Knowles has established a state presence on Sakhalin through the (ABC) in Yuzhno-Sakhalinsk. I'm sure you know that for many companies in Alaska, the potential \$30 billion development scenario on Sakhalin could prove to be their next "Prudhoe Bay." The oilfield service and supply industry in Alaska has the expertise to handle the exceptional challenges of offshore oil and gas development on the island. The government and private industry leaders on Sakhalin I have spoken with personally, are fully cognizant of that fact. Representation through the ABC on Sakhalin should prove to be a cost-effective

strategy for maximizing Alaskan company participation in the developments.

The ABC network has proven to be invaluable to representatives of U.S. companies in the challenging markets of the Newly Independent States. We now operate three ABCs in the Russian Far East - Vladivostok, Khabarovsk and Yuzhno-Sakhalinsk. The U.S. Commercial Service operates the ABC in Vladivostok while the Foundation for Russian American Economic Cooperation administers the others. The three have developed an excellent working relationship, often collaborating on optimizing business missions by individual company representatives, trade missions, and logistical services.

Dinty Miller, Executive Director of the American Business Center in Yuzhno-Sakhalinsk, is formerly from Alaska's "oilpatch" and has gained the confidence of the Alaska business community. To date, over 70 Alaska companies have used his services for everything from telecommunications facilities and business meetings services to corporate registrations. Miller's personal familiarity with Alaskan companies and the hurdles they have mastered in the Cook Inlet and the North Slope, is a remarkable asset in a representative office. The ABC has developed a close working relationship with the Sakhalin Regional Administration as evidenced by formal protocols executed with the shelf department and other key departments in the Administration. Moreover, the ABC has recently executed a protocol with the Administration of the Khabarovsk Krai, tying in that very important and proximate area to the Sakhalin development initiative.

In addition to the ABC in Yuzhno-Sakhalinsk, the Commerce Department has also funded a joint proposal of the Municipality of Anchorage, the World Trade Center Alaska and the State Division of Trade & Development through our CABNIS program. As you may know, the World Trade Center Alaska, the administrator of the program, opened an office on Sakhalin called the Troika Alaska Center, in addition to their original office in Khabarovsk. Initially funded by our Department, the office has carved out a niche among the service providers offering individual representation to companies in Alaska. Moreover, the office has begun to publish a newsletter focused on developments in the petroleum industry on Sakhalin.

Supplementing these operations, the American Russian Center of the University of Alaska Anchorage, funded through the U.S. Agency for International Development, has an operation in Yuzhno-Sakhalinsk that works toward the goal of developing a cadre of individuals trained in the principles of a market economy.

These three offices constitute a remarkable network of intelligence gathering sources and talented assistance providers for American corporate representatives as they begin to explore business opportunities on Sakhalin and to obtain work in the exploration and development phases of the oil and gas operations there. This network may prove to be the competitive edge needed by our firms. As you can imagine, they will be facing stiff competition from foreign oilfield service and supply companies, especially those currently operating in the North Sea. Japanese firms are also likely to prove challenging competitors. Not only are major Japanese companies involved in joint ventures with the producers, the Government of Japan has also opened an office in Yuzhno founded on service principles comparable to the ABC.

We are pleased your Committee is taking the leadership in reviewing developments on Sakhalin and welcome the Legislature's assistance in developing a comprehensive strategy for tapping into this remarkable developing opportunity for Alaska companies. Your interest will help us focus the attention of corporate executives on the importance of immediate attention to developing an effective market penetration strategy. With a commitment to a 70% local content target by the producers, Alaska companies will find it essential to be partnered up with a Russian enterprise in order to bid successfully on projects on the island. Finding that partner and developing a solid relationship, on which all lasting business is conducted in Russia, takes time and effort. The Legislature's efforts can help to again call this imperative to the attention of our oilfield service and supply companies.

You may be interested in knowing that we are working on several initiatives that will also serve to underscore that imperative. Tomorrow we will feature Tim Smith, Commercial Officer in charge of our operations in the Russian Far East, at three public presentations. Additionally, Ambassador Dick Morningstar, U.S. coordinator for all policy and assistance in the Newly Independent States and Bruce Shewmaker, newly appointed president of The U.S. Russia Investment Fund, and Jack Brougher, Director of the Russia division of the U.S. Department of Commerce, will also be here to brief Alaska companies on opportunities in Russia. Later this Spring, we will be featuring Jane Miller Floyd, U.S. Consul General in Vladivostok in a number of appearances around the state. Briefings by these VIPs, coupled with the Governor's trade mission to Sakhalin, should help to alert Alaska companies to the importance of initiating their partner search.

For your information, we are also working with the suppliers Committee of the

Alliance and the Anchorage Economic Development Corporation, in the founding of an international marketing consortium focused immediately on the Sakhalin play. It appears as if we may be able to bring close to 40 companies operating in Alaska into this consortium. As we proceed, we are working to ensure that these companies will be protected from prosecution under the federal anti-trust statutes through another program of the Commerce Department.

We applaud the leadership of the State in its essential government-to-government initiatives and in founding the Sakhalin-Alaska Working Group. We applaud the World Trade Center Alaska for its foresight in opening up what I would call a "Man in Sakhalin" operation. We applaud the Anchorage Economic Development Corporation for its leadership role in spearheading development of the marketing consortium. We applaud the American Russia Center for its unique efforts in free market development. If we can all work together, corporate Alaska is bound to win in this exceptionally challenging and potentially exceptionally rewarding development.

Once again, we appreciate the Committee's interest in this important initiative.

Copy: Members of the ITT Committee:

Rep. Ramona Barnes
Rep. Pete Kott
Rep. Eldon Mulder

Rep. Gail Phillips
Rep. Kim Elton
Rep. Reggie Joulie

Members of the World Trade & State/Federal Relations Committee

Rep. Alan Austerman
Rep. Gene Kubina

Rep. Irene Nicholia

**SPECIAL COMMITTEE
on
INTERNATIONAL TRADE
and TOURISM**



**LEGISLATIVE OVERVIEW
of the
ALASKA - SAKHALIN ISLAND
WORKING RELATIONSHIP**

MARCH 20, 1997

**Representative John J. Cowdery, Chair
Representative Gail Phillips, Representative Ramona Barnes,
Representative Eldon Mulder, Representative Pete Kott,
Representative Kim Elton, Representative Reggie Joule**

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**SPECIAL HOUSE COMMITTEE on
INTERNATIONAL TRADE and TOURISM**

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Original Correspondence

The House Special Committee on International Trade and Tourism will hold an overview hearing on development activities on Sakhalin Island, Russian Federation. The meeting will take place March 20, 1997. The meeting time will be from 3:30 p.m. to 5:30 p.m. in committee room 120 of the Capitol Building. Teleconference will be available at the Anchorage Legislative Information Offices, located at 716 W. 4th Ave.

«title» «last name», we would appreciate it if you would provide part of the initial overview, focusing on the basic tenets of the Alaska - Sakhalin working relationship; past, present and future. Furthermore, addressing basic questions such as:

- A brief historical and geographical perspective of Sakhalin
- How does Sakhalin affect Alaska
- Who else in our state, and out of state is involved and why
- In your view, What is the role of the State.
- What do we need to do to ensure Alaska is a primary player in Sakhalin
- A brief description of your company's mission and strategies regarding Sakhalin

Please limit your presentations to fifteen minutes, plus question and answer time from the committee members. Please send in advance as much of the material as possible for review and organization by the committee. Please confirm name of testifiers with contact phone number and fax by March 14. You may fax it to 465-2069. The committee will issue a summary report of the hearings.

Thank you for your cooperation

Yours truly,

John J. Cowdery
Representative

Contact: Casey Sullivan 1.888.269.3879 or 907.465.4967

SAKHALIN PROJECTS-ALASKA'S ROLE

Overview

If Alaska is to play an active role in the monumental Sakhalin Island projects, it is imperative that we, as a state, project a unified effort and form a coalition - an alliance - between the private and public sectors and begin to actively seek out business opportunities. The opportunities are there, but they will not be handed over on a silver platter. The competition is fierce both from international sources as well as from other states. If we want opportunities, we have to actively pursue them.

It is equally important to demonstrate to the Russian Federal government and to the Government of Sakhalin, that Alaska is interested in playing an active role and is ready, and certainly able, to assist the project managers in virtually every stage of development. We have done this before on the North Slope, we have the knowledge and the technology. What we need now is to actively market those skills in Russia.

To this point we have not done very much. Certain Alaskan companies have taken some preliminary steps. Some trade missions have taken place, and these are to be commended. But, frankly, most efforts up to this point have not proceeded past the discussion stage. Unfortunately, the image we have projected to the Sakhalin Administration is not one of a state ready to become an integral partner. This perception needs to be changed immediately.

We must proceed to change our image through a well managed program that sells Alaskan expertise to both Russian and American decision makers on Sakhalin. Such a program will need leadership, funding and long term commitment by all participating interest groups.

Organizational structure and Strategy

The organizations which will support such an effort and be key players may elect to form a consortium. A suggested name is SakhAlaska Partnership. The word 'group' has been deliberately omitted so that there will not be any confusion - especially by the Russian side - with another effort undertaken locally.

The nucleus of the organization will be the existing Troika Alaska operation in Sakhalin. The group is on site, well connected, but understaffed and under budgeted.

The main purpose of Sakhalin Partnership is to operate, for a want of a better name, **ALASKA SUPPORT ALLIANCE**. The concept of a one-stop-shop providing instant information on all Alaskan resources, on site, will be a great equalizer with existing American efforts which promote primarily Washington state interests.

It is absolutely vital that this proposal be viewed as a *long-term investment* and not a short term expense. The suggested initial start up and first-year budget is \$400,000 which would be used to hire staff, purchase office equipment, pay for leased office space, fund an in-depth marketing and sales program, and provide operating funds. The specific details, to include structure and suggested incorporation of existing Troika Alaska office into the expanded presence will be discussed later.

Sakhalin Island

Sakhalin Island, in the Russian Far East, has been producing oil since the turn of the century, when pools of standing oil were found by Czarist geologists. It was not until the breakup of the USSR that foreign companies were invited by the Sakhalin government to explore for additional reserves of oil and natural gas, and to enter into joint production agreements.

Today, a number of large American and foreign petroleum companies are in Sakhalin gearing up for the inevitable boom. These include Mobil, Exxon, Standard Oil, & Marathon Oil. Other substantial players include Shell, Mitsui, Mitsubishi and McDermott.

Projects - Current and Future

The Government of Sakhalin had designated four distinct projects for the exploration and extraction of natural gas and oil. Currently, Sakhalin 1 and 2 are in the early stages of operation. The first flow of oil is expected 1999.

Sakhalin 1

A consortium of Exxon Neftegaz (JV with Russian partner), Sakhalin Oil and Gas Development Co. (SEDECO) Japanese, Rosneft-Sakhalin (Russian) and Skhalinmorneftegas (Shell Oil and Russian JV).

Estimated cost of project - \$15 billion US.

Total investment to date by US side - \$300 million US.

Estimated reserves - 2.5 - 5 billion barrels of oil & 15 trillion cubic feet of gas.

Sakhalin 2

A consortium of Sakhalin Energy Investment Company, LTD made up of Marathon Sakhalin (JV), McDermott Sakhalin (JV), Mitsui Sakhalin Development Co. (JV), Shell Development Sakhalin B.V. (JV), Diamond Gas Sakhalin, B.V. (JV) (a subsidiary of Mitsubishi).

Estimated cost of project -- \$10 billion US.

Total investment by US side to date -- \$80 million.

Estimated reserves -- 1 billion barrels of oil & 13 trillion cubic feet of gas.

Sakhalin 3

On horizon - Major players are Texaco and Mobil. Current investment by US companies -- \$300 million plus.

Sakhalin 4

On drawing boards - 2020.

Opportunities

Opportunities exist on Sakhalin for numerous enterprises. In addition to the obvious oil patch support areas they include, but are not limited to, the following:

- Housing construction - apartments, schools, hospitals
- Road building
- Security
- Food services
- Transportation
- Telecommunications
- Supplies - everything from window glass to shoes
- Services - environmental & social.
- Government relations
- Education - job related schools and training facilities

Anchorage's role

A number of Anchorage-based companies have sent representatives to personally investigate opportunities on Sakhalin. Most have reported positive first impressions. Some have already entered into contracts for products and services.

Among the more promising organization to seek opportunities on Sakhalin is the Support Industry Alliance. A 350-member statewide organization whose members

constitute a petroleum support group, the Alliance would like its members to participate in Sakhalin's development and is encouraging its member companies to investigate opportunities through personal contact, whenever possible. The Alliance - in their words - wants Alaska to be a part of the project.

In July of this year, a delegation of 26 Alaskan business and government leaders traveled to Yuzhno-Sakhalinsk - the capitol city - to evaluate possible business ventures in the Island's rapidly growing oil patch. The fact-finding mission was organized by the World Trade Center Alaska and Troika Alaska - a support organization funded by municipal, state and federal funds to assist American companies interested in exporting American products and business know-how to Russia generally and specifically to the Russian Far East.

The feedback received from delegation participants has also been positive. There is widespread support for Anchorage to become an active player in the Sakhalin project.

The most obvious avenue is for Anchorage to become a staging area for movement of personnel and equipment, in much the same fashion that the city was the gateway to Alaska's North Slope. Equipment, especially high tech, low weight items which can be delivered by air would ideally be warehoused in Anchorage for delivery to Sakhalin in a matter of 4 -5 hours.

The benefits which would accrue to Anchorage as a result of becoming a gateway to and from Sakhalin are numerous. Perhaps the best way to describe them is to state that they would reflect similar benefits the State of Alaska, and Anchorage in particular, experienced during the TAPS project and continue to enjoy to this day.

While the Municipality of Anchorage, along with the State of Alaska and the state's private sector have a very distinct opportunity to position Anchorage as the gateway to Sakhalin, there are competitors for the title.

Seattle, Tacoma and to a lesser degree, Portland have declared themselves as the 'gateways' and all are moving forward with establishing themselves as dominant players. State of Washington has an office in Yuzhno-Sakhalinsk with a combination American-Russian personnel. The office is co-located in the same building as the majority of American and foreign oil companies and is actively lobbying for Washington-based firms. This is happening now.

Troika-Alaska also has offices in the same building but is faced with continuing budgetary shortfalls. However, Troika has been in the game since the start, and would be an ideal foundation on which to build an expanded Alaskan presence on Sakhalin.

Anchorage and Alaska need to become extremely active, on-site if we are to become a serious contender. Such a step would demonstrate to the Russians that Anchorage and Alaska are committed to playing an active role in the Sakhalin projects and are able to deliver on that commitment.

Yukon Pacific

Some may perceive the proposed participation in the Sakhalin project as assisting a competitor at the expense of the Yukon Pacific project. However, it should be noted that the Alliance, which is closely tied to the Alaskan petroleum infrastructure is supportive of the Sakhalin project and sees the many opportunities for its members almost immediately.

The Alaska gas line is years away and may be brought on stream during the first decade of the next century. The gas owners have not reached agreement on the sale of the gas and the market for the gas remains tenuous at best.

The Sakhalin projects will proceed regardless of whether Anchorage or Alaska participate. It must be clearly understood that we are not promoting the Sakhalin project. It is happening and the choice to become or not to become a participant is entirely ours.

Immediate needs

Among the more immediate needs is to bring the Yuzhno-Sakhalinsk airport up to international flight standards. Local aviation officials estimate that the initial cost would be in the area of \$20 million. Construction of an international passenger terminal and freight warehousing facilities will add an additional \$30 million.

It is imperative that multi-national funding sources be located. European Bank for Reconstruction and Development, the ExIm Bank and a number of US funded program are excellent starting points.

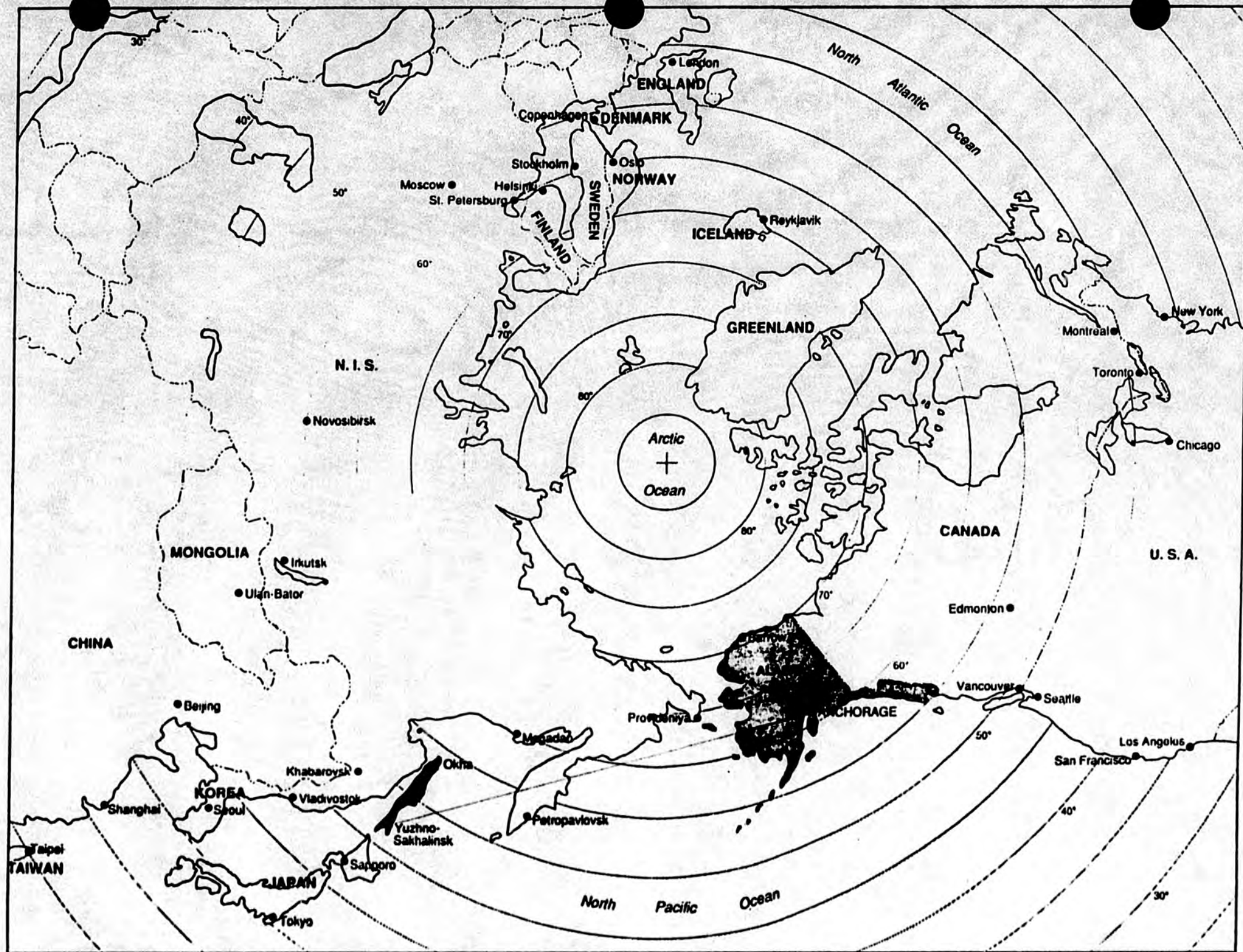
Conclusion

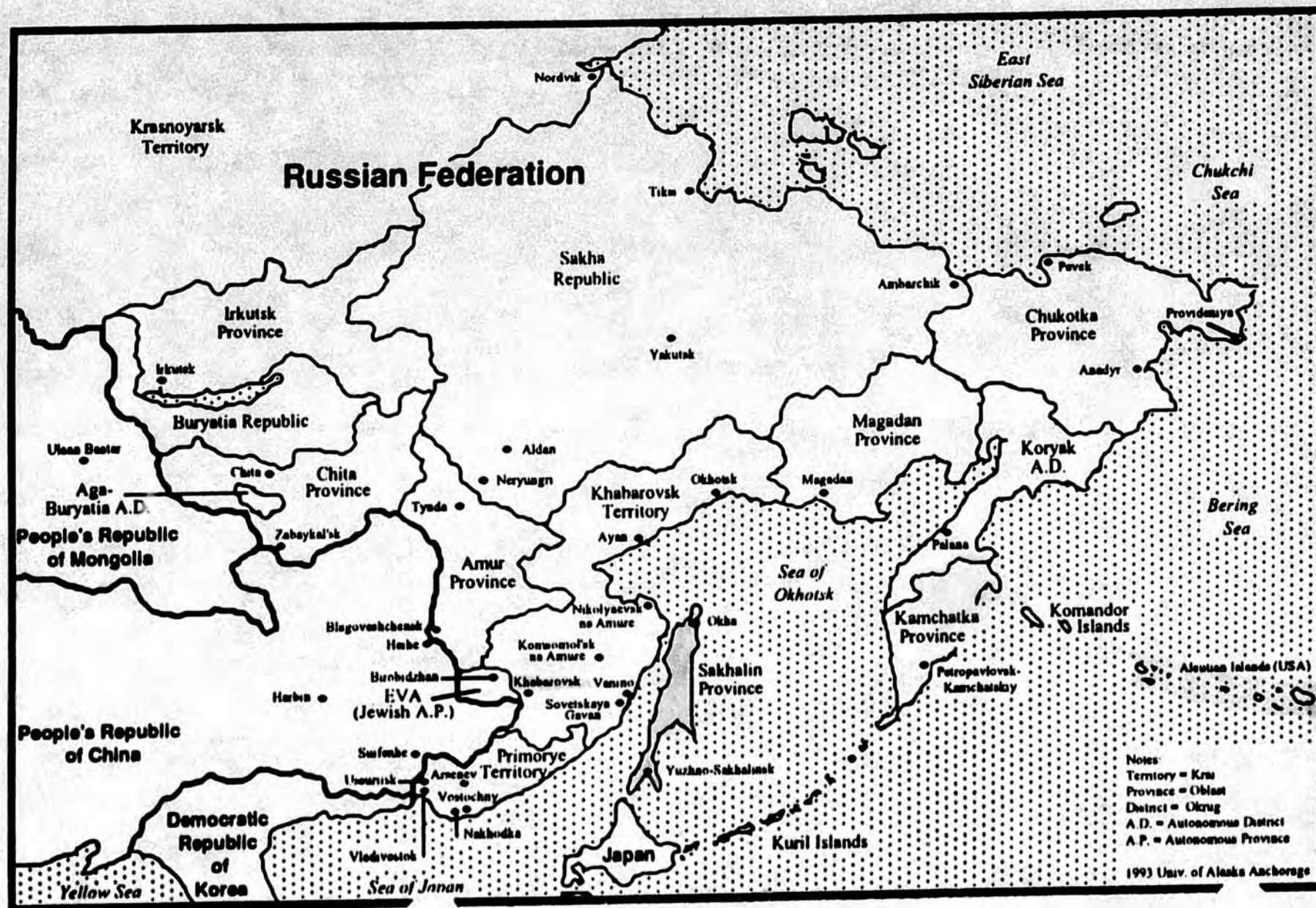
Sakhalin is happening now. The Government of Sakhalin has opened its doors to both American investment as well as expertise. Progressive American oil companies have already invested heavily into the projects. These astute companies do not invest without a full understanding of long term returns. They realize that these investments will return huge profits over the 10-20 year life of the Sakhalin mega-projects.

The Yukon Pacific gas line will likely happen, but not for many years. When it does, Anchorage will still realize the economic impact as we did during TAPS. Can we afford to let the opportunities available to us in Sakhalin today, pass us by?

**Submitted by
Steve R. Smirnoff**

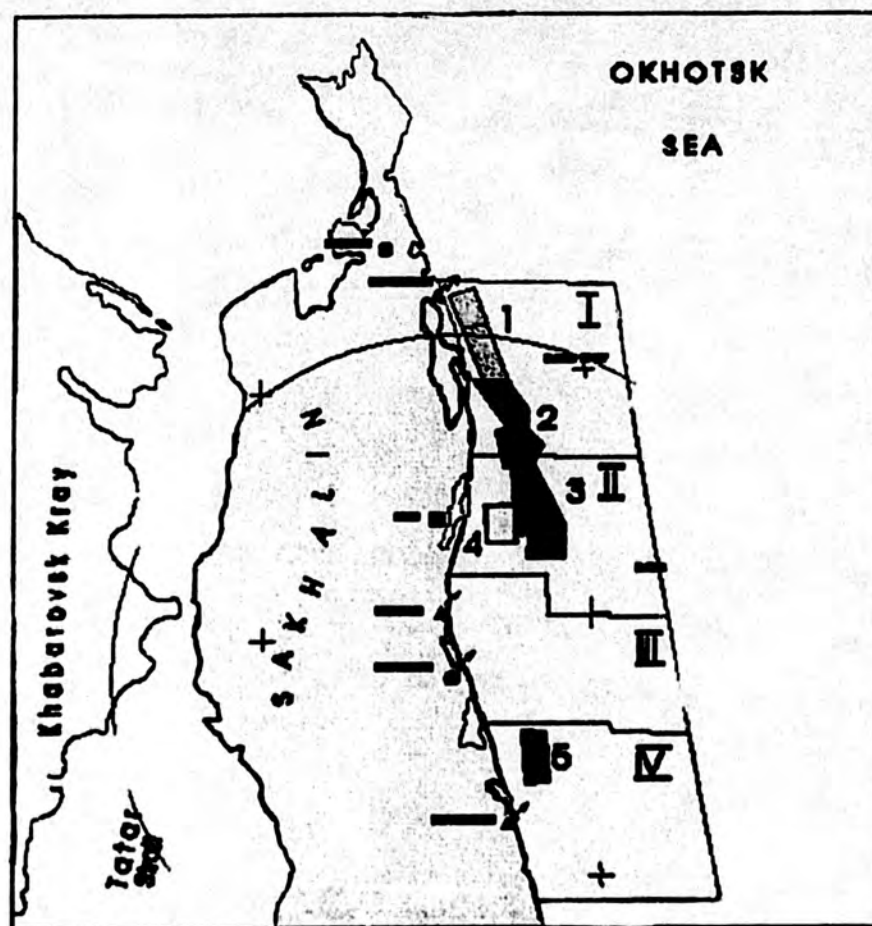
December 1, 1996





Current Sakhalin Offshore Projects:

- I, II Exxon Neftegas Limited, (Project Sakhalin - III)
- IV Mobil, Texaco, (Project Sakhalin - III)
- 1, 5 Sakhalin Energy Investment Company Ltd.,
(Project Sakhalin - II)
- 2, 3, 4, Exxon Neftegas Limited, (Project Sakhalin - I)



Sakhalin Oblast (Russia)

Area: 87,100 sq. km.

Population: 676,000 (as of January 1995)

Capital: Yuzhno-Sakhalinsk

Membership in the Northern Forum: 1993-present

Sakhalin Oblast is made up of Russia's Sakhalin Island and the Kuril Islands. With a relatively large amount of snow, average temperature in February ranges from -14 degrees to -23 degrees Celsius and from 15 degrees to 17 degrees Celsius in August. There is no permafrost in Sakhalin and the climate is more mild than the continental area of the Russian Far East. Two thirds of the area of Sakhalin is covered with forests.



Currently there are approximately 2,008 Nivkhi, 320 Ulta (or Oroki), 188 Evenk and 173 Nanai peoples living on Sakhalin island. Ainu peoples also lived on the island at one time. The language of the largest group, the Nivkhi, has been preserved and the Nivkhi publish their own newspaper, the Nivkhi Dif (Nivkhi Word). About 50 percent of the Nivkhi people on the island live in northern towns and villages and work in the industrial sector. The other 50 percent of the Nivkhi on Sakhalin live in settlements on the northwest coast where they fish and hunt.

Key industries in the Sakhalin Oblast include fishing, lumber and paper pulp, raw materials-related industries including coal and natural gas, as well as food processing. The fishing industry is Sakhalin's largest, accounting for over 30 percent of the region's gross economic output with an annual catch of over 570,000 tons.

With its rich forestry resources, the timber and paper pulp industry are developed and active industries. Sakhalin has 60 deposits of approximately 11.3 billion tons of coal, 37 percent of the Russian Far East's total reserves. There are 58 oil and gas fields on Sakhalin, most of these on the continental shelf. The total reserves of the Sakhalin shelf alone are estimated at 700 million tons of oil and more than 35 billion cubic feet of gas. Currently, several foreign investment and joint venture projects center around the development of projects on the shelf.

Sakhalin has one international and ten local airports, and a 1,100 km. railroad line. Many schools are located in Yuzhno-Sakhalinsk, including the Institute of Sea Geology and Geophysics, Far-East Branch of Russian Academy of Sciences, and many museums.

The Sakhalin Oblast has been active in projects of the Northern Forum since it joined the organization in 1993. Currently the Oblast is engaged in the Environmental Monitoring, Environmental Health and Emergency Response, and East-West and Circumpolar Air Routes projects. In October 1994, Sakhalin hosted a major conference of environmental specialists from Northern Forum regions.

Additional sources of information about Sakhalin.

Useful Information about Sakhalin Island

[Home Page](#)	[Fast Fax](#)
[Members](#)	[Become a Member](#)
[Banking](#)	[Financing Sources](#)
[American Business Center](#)	

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Production Sharing Law

Investment by foreign companies in the development of Russia's oil and gas resources has been slow to take place. Foreign investors have traditionally cited a number of factors discouraging investment in Russia, including uncertain tax structures, the lack of a clear definition of ownership and antiquated laws applied without uniformity, frequently to the detriment of foreign companies. To alleviate such concerns, oil and gas companies operating in developing markets frequently sign Production Sharing Agreements (PSA's) or Contracts (PSC's) with the government of the country they seek license to operate in. Until now, international agreements in Russia, between foreign companies and either regional or federal authorities, have had their legal basis in presidential decree, a basis too unstable and too much at odds with other Russian laws governing subsurface resources to validate the PSA process. This will change with the adoption of the so-called Law on Production Sharing Agreements (PSAL) which is currently working its way through the Russian parliament.

Legislative Process

Any proposal for a new law in Russia must receive three readings in the Lower House of the Parliament (Duma) and must pass a vote after each reading. Then the draft law must be passed by the Upper House (Federation Council) and signed by the President before it is official law. An early draft of a PSAL passed the Parliament, only to be vetoed by President Yeltsin. Another PSAL was passed after one reading in the Parliament in February 1995, but it was sent back to the Duma by the Federation Council for amendments. The law, it was felt,, was not sufficient to induce foreign investors to move ahead with large-scale projects.

On June 9th, the amended law received a second reading and failed to pass. It was necessary to have at least 225 votes for the draft to pass. The law passed the Duma on June 14th with 255 and 227 votes in its second and third readings respectively and went to the Federation Council and the President for final approval (or veto). In the third reading, Duma deputies also accepted about 100 amendments, including some from the Cabinet and the Federation Council.

Forecasting Russian legislation is difficult at best, but sources throughout the industry are optimistic that the PSAL will pass in its current form sometime this year.

What Is The Current PSA Law?

According to the new law, a PSA is a contract between the state and an investor. In return for payments, the investor receives, for a specified period of time, the exclusive rights to explore, survey, and extract minerals from an area of land indicated in the agreement, as well as the right to carry out related work. The agreement defines all the necessary conditions for using mineral resources, including the conditions and procedures for dividing the output between the parties.

Among its main provisions, the draft simplifies the tax regime for foreign investors with production-sharing agreements, allows some field-development licenses to be awarded without bidding or tender (when the interests of the Russian Federation require an agreement with a particular entrepreneur or when the competitive bidding or auction is declared null and void because there was only one bidder), states that the investors share of the output under the terms of the agreement is the investor's property and protects investors against changes in the law that could hurt project economics (for example, if in the future the Government decides to restrict oil and gas exports).

The law also includes a clause explicitly stating that its provisions are universally applicable, even if they contradict other legislation on the use of subsurface resources and on foreign investment.

Under the PSA law, state oil monopoly Rosneft, slated for eventual privatization, will be Moscow's legal agent in PSA operations. Rosneft is the only remaining Government-owned oil and gas company in Russia.

A PSA cannot be signed without the consent of the administration of a region. The portion of the output assigned to the Russian side under terms of the agreement is distributed between the government organ signing the agreement and the administrative region.

Moscow's Kommersant Daily reports pending and future oil and gas PSAs could represent foreign investment of \$7-8 billion/year.

Ongoing Concerns

Three problems which will exist, even with the adopted law, are:

- ☐ taxes
- ☐ inflation and the exchange rate of the ruble
- ☐ rights for using pipelines.

Even while incorporating some of the taxes into the in-kind portion of the agreement to be covered by the Russian government, the legislation will leave in place a large tax burden for foreign investors.

Inflation in Russia is more or less under control (6% for June 1995 compared to 18% a year ago). But this is still a large figure for western investors. The Central Bank regulation of the exchange rate creates some temporary stability.

Quotes for using pipelines in Russia for 1995 have exceeded the actual capacity of existing ones. The Russian Government should create a system of rights for using the pipelines, which should be based on three things: existing capabilities, needs of producers, and needs of refineries. Without such a system the oil and gas production will be a more risky undertaking.

In summary, the PSA law:

- ☐ sets out conditions and procedures for production sharing.
- ☐ provides a license for use of underground resources within 30 days of PSA signature.
- ☐ provides for export of production free of previous restrictions.
- ☐ grants relief from taxes, fees, and duties under current law other than the profits tax and royalties, plus a one-time signing or milestone bonus (the foreign investor will pay directly only a profit tax,, bonuses., rentals, and royalties, while other payments can be in-kind),
- ☐ ensures an investor's adequate return by modifying the PSA if other laws or regulations reduce the value of the investment.

Oil Consortium Projects

Sakhalin is the Russian Far East's leading center for oil production. Oil recovery started in 1921. The oil is mostly light and low in sulfuric content. Natural gas is high in methane. About 40 fields are in operation. The only offshore deposit tapped so far is Odoptu, but Russian drillers, lacking capital and technology, had to use directional wells drilled to the offshore sector from the onshore part of the field.

Sakhalin-1

In 1975, the Japanese Sodeco company and the Soviet Oil Ministry started the Sakhalin-1 project (for Chaivo, Arkutun-Daginskoye, and Odoptu fields off northeast sakhalin). The project has been plagued by numerous problems for many years. New life came in 1993 when Exxon joined with Sodeco on the project. Exxon and Sodeco each have 30% of the project, and Rosneft and Sakhalinmorneftegas combined for 40%.

On July 30, 1995 the members of the Sakhalin-1 consortium and Russian Minister of Fuel and Energy Yuri Shafranik signed a production-sharing agreement in Moscow. Domestic enterprises will be contracted for about 70% of the work under the project. Sakhalinmorneftegas will receive 23% of the profits, Rosneft will receive a 17% share, and Exxon and Sodeco will each receive 30%. Royalties were set at 8% of product cost and the companies will pay a 32% profit tax.

Production will peak at 10 million tons of oil and 15 billion cubic meters of gas four years after production begins. Nearly 245 million tons of oil and 286 billion cubic meters of gas will be recovered during the 33-year contract.

The fields hold 291 million tons of oil reserves and 420.8 billion cubic meters of natural gas. The Chaivo and Arkutun-Daginskoye fields will be developed in the first stage of the project, which will cost \$ 12.7 billion.

Sakhalin-2

On January 27, 1992 the Sakhalin Island Governmental Tender Commission, headed by the Russian Minister of Ecology and Natural Resources, awarded the contract for development of two off-shore oil and gas fields in the Sea of Okhotsk (Piltun-Astokhskoye and Lunskeye fields) to the "3-M" consortium of Marathon Oil Co., McDermott International, and Mitsui & Co. The Commission recommended that the consortium include Mobil Corporation and the Japanese consortium Sodeco in the development projects.

Under the terms of the award the consortium received a right to conduct a feasibility study for development of the two fields and complete it by the end of that year. The production of oil was planned to begin in the Piltun-Astokhovskoe field by 1995

(production of liquefied gas from the second field was scheduled to begin in 1999). The consortium needs to develop a suitable infrastructure for the processing and transportation of natural gas. A pipeline will transport the gas and condensate to an onshore production facility at Katangi for further processing. Neither exist as of yet. The natural gas will then be transported to the South of Sakhalin Island through the pipeline and directed for both domestic use and for export. The gas to be exported will be converted to liquefied natural gas at Prigorodnoye.

In the middle of 1992, the consortium was joined by Shell Development Sakhalin (a subsidiary of Royal Dutch/Shell), and at the end of that year the "3-M" consortium expanded into the MMSM consortium (when Mitsubishi joined). In April, 1994, the consortium created the Sakhalin Energy Investment Company Ltd. to manage the development, production, financing and marketing aspects of the Astokhskoye and Lunskeye fields. On June 24, 1994, Sakhalin Energy signed a Production Sharing Contract for Sakhalin-2, the first project in Russian history that gives foreign companies permission to develop off-shore oil/gas fields. The Russian Government agreed to a lower level of profit tax for the project of 32%, instead of the usual 35%.

According to the Production Sharing Contract,, production sharing will begin in the first year of operation. Until the project returns a profit of 16.5%, investors will receive 85% of the oil produced, and the Russian Government will receive 15%. At the second profit threshold, the split will be 50-50, and at the third level - 30-70 in Russia's favor.

The 4MS consortium spent \$80 million on a feasibility study of the fields. Two appraisal wells were drilled during the summer of 1992. The study was completed and submitted to the government on December 31, 1992. It promises results in 3-4 years.

It was determined that all platforms for oil and gas exploration will be single leg structures, or monopods. They will be designed to meet not only the extreme ice loads but also the severe geo-technical loads expected in this earthquake prone area.

The anticipated development scheme for the Piltun-Astokhskoye field will include three ice-resistant monopod type platforms for full field depletion over a 30-year period. The platforms will be about 10 miles offshore in 100 feet of water. Marine pipelines must be buried under fifteen feet of cover for protection from ice gouging.

In the Lunskeye field, a single platform will supply a six million ton Liquefied Natural Gas (LNG) plant in Prigorodnoye as well as gas for domestic consumption.

Sakhalin-3

This project works with the East Odoptu field. Block 1 of this project was sold to Mobil and Texaco. Exxon has two blocks. Amoco and Shell are also interested in the project. Sakhalinmorneftegas will drill two exploratory wells this year. The company will have a 20% share.

The Sakhalin-3 contract zone covers 15,000 square kilometers. Mobil Oil and Texaco will explore the first section and have invested \$151 million. Exxon will invest more than \$300 million to develop the

second and third blocks. The three companies could sign the Sakhalin-3 contract with Russia in September or October, 1995. Both sides have agreed on the size of the profit tax, which was set at 35% as stipulated by a production sharing agreement.

Other Projects

The next sections to be leased (further off in the future) include the Sakhalin Area and the Southern Kurils. The Southern Kurils have significant oil and gas structures. Local geologists who have conducted extensive surveys in these waters say that the potential reserves there could exceed the largest known reserves off of Sakhalin. Moreover, they are located in ice free waters at a shallow depth.

Economic Overview of Sakhalin Island

The economy of Sakhalin Island has three major sectors, each of which dominates in one of three parts of the island. The fishing industry, located predominantly in the southern part of the island comprises more than 40% of the area's commodity output and exported more than 8,000 metric tons of fish and seafood last year. The fishing fleet is represented by different types of vessels: from small fishing sailers for coastal fishing to big ocean trawlers and other fishing vessels.

The majority of the catch is processed at regional enterprises. Only a small part is sold unprocessed. The most wide-spread method of processing is freezing both prepared and unprepared fish, but there is also some salting and canning done on the island. Other kinds of seafood products produced on the island include dried and smoke-dried fish. Other types of finished product are insignificant in volume.

The center of the island is home to the timber industry (18% of the region's commodity output). Almost 68,600 tons of lumber and paper products were exported from the region last year. The Ulegorsk Pulp and Paper Plant is the major supplier of newsprint in the Russian Far East.

The energy industry (oil and gas production, coal and peat) is the third largest sector of the island's economy. It accounts for 12% of the the region's output. The island exported 93,800 metric tons of crude oil last year. Annual oil output is approximately 2 million tons, natural gas output is 2 billion cubic meters, and coal output is close to 5 million tons.

Despite being the most developed and equipped industries in Sakhalin, all of these industries suffer from material deficiencies and a lack of capital investment. The fishing industry needs advanced Western processing technologies, which would make it possible to both produce food products of high consumer demand and use resources more efficiently. Obsolete vessels with a high grade of deterioration form the main part of both the fishing and processing fleet. The technological equipment of the fleet as well as of shore enterprises do not meet modern requirements. The amount of hard manual labor in the industry is fairly high and output is low in comparison with world standards. The pulp and paper and woodworking sectors of the timber industry are represented, in general, by depreciated plants which need technological development. The forestry sector is in need of environmental restoration projects. The energy sector faces problems due to a depletion of on-shore fields. There is great potential in off-shore exploration, but the domestic industry lacks the technical expertise or capital to address the technical challenges (earthquakes, winter ice floes) facing those projects.

The major oil and gas fields are located off the northeast shore of Sakhalin Island in the Sea of Okhotsk. They have attracted much foreign involvement. There are already three big projects to explore those fields (named Sakhalin-1, Sakhalin-2 and Sakhalin-3). which have among their participants such firms as

Marathon Oil, McDermott International, Mitusi and Co., Shell, Mitsubishi, Amoco, Smith Energy, and Sodeco. The forth project, Sakhalin-4, located to the northwest of the island, is in the early stages of planning.

The oil and gas sector is the largest expected growth sector on the island and will have a considerable impact on the Sakhalin economy. Its growth will affect such sectors as transportation, construction, telecommunications, and power engineering.

The construction and building materials industry is of local significance. It partially supplies the building materials needed by the region. 13.1% of the working population of the region is employed in this sector. The industry can not supply enough building materials. A lack of materials, combined with the high cost of bringing in supplies from other parts of Russia, doesn't allow it to satisfy the demand for new construction. For the past five years, the amount of construction by the industry has fallen by 65% (compared to 1989). With the exploration of the oil and gas fields in the north part of the island this industry will have an opportunity to grow.

The region's transportation infrastructure is also in need of improvement. Marine transport plays the most important role in the region's life. It provides practically all freight turnover between the region and other parts of Russia. The most important ports on Sakhalin are Korsakov (the main fishery and international shipping port) and Kholmsk (site of a rail-barge to mainland Russia). Due to a shortage of orders from consumers, the Sakhalin Steamship Company (which operates the rail-barge to the mainland) and river transport enterprises have been experiencing some difficulties. The exploration of oil and gas will give them the necessary value of work and allow them to modify their fleet.

Rail lines connect the northern and southern districts of the island. There is rail- barge service from Vanino (Khabarovsk krai) to Kholmsk, but because the railway system was originally built by the Japanese in the first half of the century, the Sakhalin network of railway lines has a narrow gauge, which necessitates that each rail car's chassis be switched at port in Kholmsk. There are several proposals to connect Sakhalin Island and mainland Russia by rail and automobile bridge. One of these has been submitted by the Japanese company "Dzuro" and proposes to connect Japan and the Russian Far East by the start of the next century via two unique bridges for rail, road, and pipe (first bridge from Cape Soya (Japan) to Cape Crillon (42km) and the second one - from Pogibi (Sakhalin) to Lazarev (7km)). The cost of the project is 7 trillion yen. There is also a proposal (sponsored by the Sakhalin Regional Administration) to build a tunnel or bridge from Pogibi to Lazarev (without changing the current railway system).

The exploration will bring more human resources to the northern part of Sakhalin. This will necessitate changes in social infrastructure in order to meet the needs of the increasing population. Currently, the northern part of the island (which includes Ohinsky and Nogliksky administrative districts) is the largest (33% of territory) portion of the island, but it is under-developed and is the most sparsely populated part of the island (61,060 people in 1992, which is less than 10% of Sakhalin's population).

Transportation on and around Sakhalin

There are three ways to deliver cargo to Sakhalin Island: railway, air, or sea transport.

The only railway is from the Russian mainland via train ferry from Vanino to Kholmsk (12 hours). Sakhalin railways use Japanese diesel trains which carry less cargo than a usual train on the Russian mainland. The Oblast Administration is considering resuming construction of a rail tunnel under the Tatar

Strait (to Khabarovsk territory) that was begun in the 1940's and 1950's. They believe that construction of the tunnel will be more cost-effective than replacing the ten obsolete ships which now comprise the ferry fleet.

There are several airlines which work on Sakhalin Island. Aeroflot has everyday flights to and from Khabarovsk, Vladivostok, Petropavlovsk-Kamchatskii, Moscow, and several other cities and towns in the Russian Far East. It is planning to commence regular flights between Yuzhno-Sakhalinsk and Seoul and between Yuzhno-Sakhalinsk and Pusan. Unfortunately, the Yuzhno-Sakhalinsk airport can not receive wide-body airplanes because of its short runway. Sakhalin International Airport (SIA) and Skidmore Owings and Merrill (San Francisco) led a consulting group working to develop a comprehensive plan for airport development. The plan was ready by April, 1994. The estimated cost of construction was \$30 million. Aeroflot also can organize cargo transport to Sakhalin. Other airports on Sakhalin include Kholmsk, Okha, Zonalnoe and Shahtyorsk. None of these, however, are approved for international flights.

Sakhalinskije Aviatrassi (SAT Airlines - former Sakhalin agency of Aeroflot) has its own planes and can transport cargo from Sakhalin to the Russian mainland and back. It has regular service to Khabarovsk, Vladivostok, Hokodate, Hokkaido (Boeing 737-200 several times a week), and Seoul (once a week) and is planning charter flights to Atlanta, Korea, and China.

Volga-Dnepr Russian Cargo Airline plans to offer all-cargo scheduled air service from Alaska to Sakhalin Island.

There are several companies, which ship cargo to Sakhalin by sea: FESCO Agencies shipping one or two times a month from Tacoma, Sunmar Shipping Inc. with the same frequency from Seattle, Sakhalin Shipping Company from the Russian mainland, Hyundai Merchant Marine Corporation shipping cargo from Korea, Primorsk from Vladivostok and Vostochny, and Kamchatka from Petropavlovsk-Kamchatski. Kholmsk and Korsakov are the island's main ports. The majority of cargo goes via Korsakov, with Kholmsk serving as fishing industry port.

There is ferry service between Korsakov/Kholmsk and Wakkanai/Otaru (Hokkaido).

There are also several express carriers which can deliver mail and cargo to and from Sakhalin. Northern Hemisphere Express ships priority packages and cargo between Sakhalin and the U. S., Mexico, and Canada. DHL has an office in Yuzhno-Sakhalinsk and ships documents and packages to and from there. U.S. Postal Service Express Mail is also an effective option for documents and small parcels.

Why You Should Do Business on Sakhalin Island

- ☐ Sakhalin Island is located strategically on the Pacific Rim, within close proximity of major air and shipping routes, positioning Yuzhno-Sakhalinsk, the region's capital, as a major center for international trade and investment activity. Sakhalin Island has a population of 710,000, with Yuzhno-Sakhalinsk boasting 180,000 inhabitants.
- ☐ The region offers tremendous opportunities in the energy industry. Some of the greatest potential oil and gas fields in the former Soviet Union are located on and offshore Sakhalin Island.

The potential impact of offshore oil and gas drilling on the region's economy is immense. Correspondingly, the potential market for U.S. secondary and tertiary support services and

technology is extremely large. Several major U.S. oil and gas companies, including McDermott, Marathon, Mobil, Texaco and Exxon, are heavily invested in multi-billion dollar drilling projects on and around the island. Local Russian firms are anxious to partner with U.S. companies to capitalize on this specialized market.

Even for companies outside the oil and gas industry, markets on Sakhalin Island will expand with the increasing oil and gas activity. Officials on the island predict broad economic impact from development projects, and this will in turn cause an increase in demand for everything from electronics and office equipment to household consumer goods. '

- ☐ There is excellent potential for U.S. investment in the fisheries industry, currently the dominant industry on Sakhalin Island, accounting for over 40 percent of the region's economic output. Sakhalin's timber industry, including logging, pulp and paper, and woodworking, also holds significant potential for U.S. companies. Modern machinery, technological development and environmental restoration in both sectors are in great demand.
- ☐ Despite being located off the mainland of Russia, Sakhalin Island has excellent access to transportation. There are five major ports on Sakhalin, including the Port of Korsakov, which serves as the island's main port for international cargo shipping. The Port of Kholmsk connects the island to the mainland by rail barge and ferry. An extensive network of railroads provides access to all areas of Sakhalin. The island has one international airport, located in Yuzhno-Sakhalinsk, with flights to mainland Russia, South Korea and Japan.

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American Business Center

Yuzhno-Sakhalinsk, Sakhalin Island

Useful Information about Sakhalin Island

Sakhalin Island offers tremendous potential for U.S. trade and investment activity. As some of the most active foreign investment projects in the entire Russian Far East proceed with the development of the island's natural resources, the demand for U.S. goods and services constantly increases.

This rich frontier offers a vast natural resource base, a progressive international outlook and an emphasis on private sector development. Sakhalin Island is positioned to become one of the most important centers in the Russian Far East for two-way trade with the United States.

Opportunities exist for U.S. companies to supply goods and services in a number of industry sectors, including:

- ☐ Oil, mineral and energy-related
- ☐ Forest products and construction
- ☐ Light-industry
- ☐ Agribusiness
- ☐ Fisheries
- ☐ Telecommunications
- ☐ Financial services
- ☐ Environmental services
- ☐ Consumer goods

Services

The ABC Yuzhno-Sakhalinsk has been established to take advantage of the high demand for U.S. goods and services in the region. The ABC increases U.S. business opportunities by providing the information and services critical for successfully establishing operations and conducting business in the Sakhalin region.

- ☐ Matchmaking of business partners
- ☐ Market analysis and research services
- ☐ Export counseling
- ☐ Trade fairs and missions
- ☐ Product display / demonstration
- ☐ Business appointments
- ☐ Interpretation / translation services
- ☐ Secretarial services
- ☐ Short-term office space rental
- ☐ Reliable phone, fax and e-mail service
- ☐ Conference room rental
- ☐ Computer rental
- ☐ Photocopier service
- ☐ Hotel and travel-related arrangements

Additional ABC Locations

There are fourteen American Business Centers located strategically throughout the Newly Independent States.

Russia

- ☐ *Chelyabinsk*
- ☐ *Khabarovsk*
- ☐ *Nizhnevartovsk*
- ☐ *Nizhny Novgorod*
- ☐ *Novosibirsk*
- ☐ *St. Petersburg **
- ☐ *Vladivostok **
- ☐ *Volgograd*
- ☐ *Yekaterinburg*

Belarus

- ☐ *Minsk*

Ukraine

- ☐ *Kiev **

Uzbekistan

- ☐ *Tashkent **

Kazakhstan

- ☐ *Almaty **

** These ABCs are under the management of the U.S. Department of Commerce's U.S. and Foreign Commercial Service.*

For a general information packet on the American Business Centers, contact the Business Information Service for the Newly Independent States at:

Phone: (202) 482-4655, option 21

Flashfax: (202) 482-3145, document #7022

Sakhalin Island



Sakhalin Island is located off the Pacific Coast of Russia, slightly north of Japan. The island has a population of approximately 700,000 people. A single administrative region (Sakhalinskaya Oblast) encompasses the entire island. Owing to its geographic location and status as the capital of the region, Yuzhno-Sakhalinsk is well situated to serve as a center for economic development. Approximate flight times from major Asia Pacific cities are:

Khabarovsk: 1 hour
Vladivostok: 1 hour
Seoul, Korea: 2.5 hours
Niigata, Japan: 5 hours

Other major cities on Sakhalin Island include:

- ☐ Kholmsk, a port city which channels shipping to and from mainland Russia;
- ☐ Poronaisk, a center for coal mining and paper production;
- ☐ Korsakov, an international shipping port and major center of the fishing industry;
- ☐ Okha, the working capital of the oil and gas industry.

Contact Information

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Russian Language Resources
Vadim Zima

Law

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LeBoeuf, Lamb, Leiby & MacRae
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C-Lee Manufacturing

Marketing

Marketing Data Research
TRADEC

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Goodwill Physicians Exchange
NCA MED International/NCA Pharma-Plus
Segol Distributing
Virginia Mason Medical Center

Petroleum

Norsk Petroleum

Port