

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 86 / 2

439 SCOMM12: OIL & GAS TAXATION & PIPELINE 1972-77

entering in under those circumstances and ^{up}shipping the oil. For example, I can, let's take for example Arco who has a refinery down Seattle way. Let's say that that refinery burned up, or blew up, for some reason or another, and a hundred thousand barrels a day of Arco's oil ^{up there} would not have its normal place to flow, and it might be given away at unit rates, I am not quite sure how they can stop their percentage of the unit from flowing downstream to the market anyway. But, on the assumption that there was some way that they could, we would then have them reobligate it to offer that one hundred thousand barrels first to another member of the consortium, which I think they probably do under any circumstances as it is, but if, for some reason or another, another member of the consortium didn't want the oil either, then we would expect the State to step in and move the oil to market for the bond holders' welfare.

Rettig: Your further condition being to secure an agreement that the oil companies, failing to ship the minimum, would agree then to sell to the State, presumably as a back-up to the guarantee this minimum. Is that correct?

Guilderhouse: If it was first offered to another oil company.

Rettig: Failing in that, the State would have the option to purchase?

Guilderhouse: Yes sir.

Rettig: What would the State do with this?

Guilderhouse: Well, I said that the premise is that there exists, and will exist, continue to exist, a demand in the "lower 48" for Alaskan crude and that the assumption is that Alaska^N crude will be competitive with other sources of domestic crude ~~crude~~ oil over the long run. On that assumption, I assume that the State could find a buyer for the oil. Now, ^I understand that there ^{are} ~~are~~ ^{known} great amounts of complexity involving oil companies make their plans ^{known} ~~least~~ time six months. They know where their oil is coming from ^{from} any particular refinery. So it is entirely possible to suggest that the State could not market or sell the oil. That nobody would buy it, I think it's highly unlikely and I think ^{you} can get testimony more expert than I, to suggest that Alaska^N oil will be marketable somewhere in the United States over the long run. I would suggest that is the

reason the oil companies are willing to spend six billion dollars in the long run to bring that oil to market. They believe that over the next 25 years, they'll have a place to sell it.

Rettig: Wouldn't it be reasonable to assume that if the minimum under the contract fails its probably because of failure of the market. Those who are in the business of marketing if their market fails, would you suggest a place ^{there} that the state might find a market for this oil.

Guilderhouse: I would say that if the market for Alaskan crude oil is non-existent, the State will not be able to sell oil. I also say that *I* don't think the market for Alaskan crude will be nonexistent. I do not think ^{that} the State will probably ever have to sell a barrel of oil because I think ^{that} the oil companies will sell the oil over the next 25 years and the circumstance for which we are providing in this case is highly unlikely ever to occur. And I would also say that if there was no market for Alaskan oil, the State could not sell it and ^{THAT IS THE RISK THAT} ~~that would be a risk~~ that we'd be asking the bondholder to take is that the market for Alaskan oil evaporates because we're providing to move the oil to a market that is assumed to exist. If the market is not there --

Rettig: Just one additional point--I believe you referred to this minimum guarantee requirement as in effect a mere pledge of the oil in the ground. Is that?

Guilderhouse: Yes sir.

Rettig: I don't think that term is quite clear to me. In relating it to your initial statement that we're not asking the oil companies to guarantee any credit, now this is their oil, is it not? At least seven-eighths of it is.

Guilderhouse: I think the oil belongs to the people of the State of Alaska

Guilderhouse: Well, I'm not--it was my understanding that a lease--the oil companies have leased the land under which the oil exists--they haven't bought the oil.

Guilderhouse : Yes sir.

Guilderhouse: I'm not a lawyer, and I'm not going to ---~~Ixfriixexxexxxnawxne~~
~~xnxxxegaxdxehaxxiixanxxonxxxwherxxxxxxxxxxxx~~

Guilderhouse: Well, I

Guilderhouse: I'm going to have to deal with Paul Harper, the lawyer addressing the Attorney of the lease, in terms of what it means.

Senator
We touched on this before and I think ownership as we have discovered, such items as the Native Land Claims, is a divisible interest and certainly we recognize that there are private rights of ownership in this oil that are the property of the bidder that bid on the oil; there are also interests the State of Alaska has which might also be described as being ownership rights in general, diversionary rights, belonging to an ownership

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....right of ownership. Title is an intangible subject.

_____: I don't think this is really the thrust of my question, in any event, but the fact that we are pledging, asking the oil companies to pledge this minimal amount of oil to secure this bond service - something ^{THAT they were} ~~xxxxxx~~ not otherwise planning to do.

_____: Well, if you ^{figure it out} ~~figure~~ the pieces.....we are asking them as part of a mutually beneficial arrangement, and not forcing them because I have stated that there is a hostile atmosphere and we can't work this out, ^{if} this does not make sense with all the parties concerned, nothing will ever happen in terms of public financing. If this doesn't make any sense, ^{so} ~~and~~ there is no way that anybody is going to make them do it, now I would suggest.... ^{now I'm} talking about encumbering their credit, or encumbering the ability of the oil company, let's say to go to a commercial banker, and the commercial banker will say "you have such a large ^{liability} ~~with that pipeline~~ arrangement you have with the State of Alaska, ^{I won't} I won't lend you any more money because I am concerned about that liability." Or to the ^{extend} that a bond rating agency ^{would} reduce the bond rating of a particular oil company because he entered into an arrangement of this sort. I am suggesting, and I think it is substantiated, that such ^{an agreement} ~~would not~~ encumber the credit of ^{oil} oil companies in this attitude. With respect to their being a footnote perhaps in their balance sheet, because this is a material commitment on their part, ^{a significant} a significant commitment that needs to be brought to the attention of the share holders and other people that certainly would be missing, but when I say encumber their credit, ^{its not like you take} ~~xxxxxx~~ a play where they say "if you don't ship you have to pay money", or in this case we say "if you don't ship we'll come in and ship the oil for you and pay you". ^{for that oil}

_____: Thank you.

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_____ : I have a couple of questions . Going to your point that any agreements should be ^{MADE BETWEEN THE TWO}...must be between the two partners, and must benefit both partners, it would seem to me and I this is pretty basic but I am having a little trouble, it would seem to me that as cheap as we can build the line is the most desirable thing both for the State and for the oil companies. Now if the State would build, ^{IT}perhaps they would sell the bonds at ...if they were revenue or tax free bonds...would sell them at an interest rate less than what normal bonds could be sold for. Is that right?

_____ : Yes, sir.

_____ : We would figure the point spread from ., I think anywhere from 1.5 to 2 points. Is that correct?

_____ : PLEASE PLESE

_____ : So this is very general. So that would result in substantial savings, ^{WOULD BE A LOT}as far as debt service is concerned.

_____ : It depends on how much of the pipeline is/financed by going to be equity on the part of the oil companies, and how much of the pipeline is oil companies. going to be openly financed by debt on the part of the pipeline. Because (or, million?) if the State would go out and lets say borrow ^{ONE} 3.5 billion dollars, then the State would be paying, ^{FOR THE DEBT SERVICE}lets say 7% interest on that, ^{OR, 7%}it is possible that the oil companies will not be able to borrow 3.5 million dollars, they will only be able to borrow say half of that, and for the rest they will have to sell shares of stock to the public and also use their own cash flow of retained earnings, to finance this. Well there is a cost associated with that capital which I think with the oil companies is higher than 7%, and there is also a cost associated with the debt which I think the oil companies, ^{FOR}in this magnitude, will be higher than 7%. So in a long-winded way, yes, it would be cheaper for the State to finance it in terms of tax exempt bonds.

_____: And we're talking about maybe 1 or 1.5 per cent?

_____: Now, in the other area, as far as the Federal government is concerned, if the State owned the pipeline, then the State would be entitled as a private company to make the suggested 7% ... the ICC allowance, then a 7% profit would be taxable if the line were/in private ownership held profit by the Federal government. The 7% would not be taxable by the Federal government if held under State ownership. Now, in millions of dollars, can we estimate what that saving would be. It seems to me that there would be a substantial piece of money and that that would eventually inure to the benefit of the shipper - the oil companies - as well as the State.

_____: Yes sir, I think you are right on it.

_____: Can you estimate what that figure.....

_____: Should have a run..... more specifically

_____: lets do it, it can be done/xxxxxx somewhere, but lets say that it costs three billion dollars, and the State lets say in the first year will pay ...well in the first year the whole debt issue, ...in the State, would pay 7% interest on that, so you are talking 210 million dollars/, and if the oil companies lets say had 100% financing, you said that they had a cost associated with it, of lets just say for argument's sake 9% lower than the oil companies would like it, they earn on their assets, you've got 2% difference there, thats essentially 60 million right there, I guess. And of the income tax, thats a year, ...

_____: Let me continue with Federal and State taxes that we calculated, that would be paid by private ownership, in our private ownership base case.

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They are, the first year, 33.73 million dollars in State income taxes; but 158.8 million dollars Federal income taxes.

In the second year, a similar amount 33 plus million dollars, ^{IN STATE TAXES} and again 150 and a quarter million dollars in Federal income tax.

Moving on to the third year of operation, the Federal income tax and State income tax ^{5,142} remain roughly the same - 34 million in State, 158 million dollars in Federal.

_____: That's third year? ^{is it?}

_____: Third year. Yes sir.

_____: Well, I can have all these figures.....

_____: No, that's not necessary....as my rough figures show that's about 200 million dollars a year in tax savings if the State would own it. Am I right?

_____: You are right.

_____: Now, that 200 million dollars, ^{how is that} which is a substantial piece of money going to be distributed? Wouldn't the oil companies benefit in part because, ^{75¢} say for example if it takes ~~5¢~~ to ship a barrel of oil from Prudhoe to Valdez, but you don't have to pay tax on it, you could say, then ^{which is} in rough figures, say then it only cost them 50¢ a barrel.....is that right?

_____: ^{is it?} Correct, I am not sure of your numbers.....actual tax savings are definitely a part of the tariff calculation, the lower the taxes the lower the tariff.

_____: All right, now let me ask you another question: would the tax savings anywhere compare to the 7% profits they would make if they held the title under private? You see what I mean?

_____: Yes.

_____: In other words they would save a quarter a barrel if its ~~1/4~~

in State ownership, but are they going to make profit at a quarter a barrel if they hold it in their own hands? Is there any way to equate that?

_____ situation: The ~~xxx~~ you just described, yes, you ^{CERTAINLY CAN} just ~~can't~~ equate it

.....it looks like a ^{PROFIT} ~~loss~~. The profit that theoretically the profit ^{ON A} ~~that~~ of 7% - if we're going to use the 7% ^{NUMBER}, with a 3 billion dollar pipeline, the profit is 210 million dollars. That's how much profit they

can make. ^{Its} /that simple a calculation, 7% of 3 billion dollars. Now the

profit - if you're going to use the 7%, is 210 million dollars. Equate... ^{AND}

use these numbers and we come up to around 200 million dollars. ^{SE} Well, in

terms of the cash position of the oil companies, its a ^{PROFIT} ~~foot~~. ^{BUT IF} I could say

something....I'll make it quite clear that this is a 7.5% (7)

sort of an opinion and nobody else really has anything to do with it, its

strictly ours. That ^{there} might be a way to make this concept more feasible

and engender the environment in which cooperation might take place, ^{by} Suggesting

to the oil companies that under state ownership it might not chose to build its

tariff structure around a 7% return. Say perhaps the State not only would

provide this type of savings but ^{COULD} ~~could~~ conceivably develop its tariff

structure on a basis ^{SOMETHING} /less than the maximum. Again I want to emphasize that

this is TEMPLE, BAKER & Sloan speaking. As a suggestion for consideration,

if you ever reach the point where you are driving ^{TRY TO SAGGESS} ~~this~~ ^{in terms} ~~is~~ favorable

climate TO TRY TO COME TOGETHER ON THE UNIFORM ISSUES

_____ : Right, that was sort of what I was thinking, ^{in terms} /of each having

a benefit, not one at the expense of the other.

_____ : I heartily recommend that.

_____ : Only one other thing that bothers me - the oil companies of

course would have the right to depreciate the pipeline as ~~xxx~~ an asset, I

assume.

_____: Yes sir.

_____: And that would be a tax of paper transaction ^{BECAUSE} we assume the pipeline is going to be there and carry all the oil out and I suppose

_____: zero, ^{THE} State wouldn't have that, ... the State ^{WOULDN'T} since it doesn't get doesn't pay taxes, it ~~XXXXXXXXXXXX~~ the depreciation quite obviously.

Now, how does that gear into that?

_____: Well, the ^{THE} ~~structure~~ of oil company financing and accounting, ^{EXACTLY} is an art unto itself. And I'm not really qualified to say/how much the depreciation ^{OF} the pipeline is worth to a particular oil company, or in ^{CONSIDER} the undivided interest structure what value ~~xxx~~ a particular member of the consortium would place ^{TO} that depreciation. With respect....lets say that it was a separate entity, ^{A SEPARATE ENTITY} and not an undivided interest structure, the depreciation would really not make a whole lot of difference to the private ownership on the basis of ^{THE} 7% consent decree limitation. Because that's a cash dividend ^{LIMITATION} figure, and what they're working ^{ON} on on that basis, they can just take 7% cash out of the dividends and that ...and then the depreciation within the structure would not be a significant item at all.

_____: ~~XXXXXXXXXXXXXXXXXXXX~~ Okey.

_____: But thats not in the same place with the undivided interest, ^{BECAUSE} that ~~is~~ ^{THE} all folded back within the parent corporation, ^{THE} the depreciation may well have some values beyond the.....

_____: All right, now in just ^{THE} the painting with the broad brush, we've got 200 million dollars here that can be saved in taxes

_____: Yes, sir.

_____: Isn't that...and if the oil companies are going to share in some of the savings, ^{THE} now isn't that going to....not withstanding the

arrangement between the State and the oil companies, isn't that going to result in the oil companies being more competitive in their own area of marketing? I would think that would follow.

_____: You mean to the extent that their costs are lower, that they are more competitive in the market? Yes sir.

_____: So they'd get a substantial advance, I would think.

~~Under~~ ^{I THINK SO, YES, SIR, UNDER} the right circumstances I think there are tremendous advantages to the oil companies, both in reduced costs and in reduced financing burdens. (?)

_____: Mr. Rettig is a banker... ^{YES, I'LL LET HIM} ~~I'm going to~~ continue, as I'm getting a cold in my head.

PLEASE NOTE: THE FOLLOWING PAGES WERE TREATED
AS A UNIT IN THE ORIGINAL DOCUMENT.

Guilderhouse: _____ referred to establishing the tariffs, and I would suggest it should be a factor in establishing the tariffs. In order to recover the costs.

Rettig: Yes sir, I'm sorry, I just wanted to clarify a point. When I performed an analysis on the income statements of an owner of the pipeline, be it the state or a private secrete, I did in fact include straight line depreciation over a 30 year line for 15% _____ VALUE, in either case.

Guilderhouse: Thank you, I had thought it ^{was} important to make it clearer ~~that~~ we all understood ~~XXXXXXXX~~ the treatment of depreciation in either case.

Eppenback: If I may add _____ Mr. Chairman, the cases showing estimated income to state public ownership which Chairman McVay was eluding ^{by 404. And shown on chart} ~~page 3~~ and reduce dividen levels 7, 5.5, and 4, so that the committee has this information before us and again to perhaps being a little oversensative to refute any imputation of the state had shown only the worse case or that the governor has ^{made it} ~~only the~~ worse case, these charts are before the committee and we'll be ready to respond to them at your pleasure.

Rettig: thank you.

Wohlforth: Senator Raider has a question,

Raider: I have a question for Mr. Guilderhouse, under the various proposals here how would the issues of 3 1/2 million ^{involue} or would it effect our abilities to issue bonds for normal governmental purposes? That question was asked this morning, but I'd like to have your opinion.

Guilderhouse: Well, mines just an opinion, I happen to believe that ownership of the pipeline will enhance the states ability to issue general revenue bonds. I think that ownership of the pipeline increases the security of the states total income package. I think, first of all, I think the pipeline is a good business, and because its a good business, or a sound business, and lets say it would be operated in a sound fashion. The ability to protect the states well head and protect the states royalties and severences, generate lets say a moderate st surplus or even a large surplus, however

if we're at doubt from pipeline operations to develop other activities in the state, would enhance the states abilitating the state would be in a stronger financial ~~XXXXXXXXXX~~ position rather than a weaker, financial position.

Holm: Mr. Guilderhouse, haven't you assumed that the price per barral for transportation to the line is the same ^{whether} ~~weather~~ its state ownership or private ownership?

Guilderhouse: No sir, I would say in line with the discussions we have there, that there would be some costs savings, ah, in state ownership because of the reduced cost of financing the reduced cost of taxation. That the actual cost of moving under state ownership would be less than the actual costs of moving under private ownership, given equal efficiency in operations.

Holm: Than what relationship doXX these charges have, or these charts upon the wall have to a diferential between the rate charged and thus the competitive position of the state operating the pipeline, the oil that passes through that, on the world market as compared with that under private ownership?

Guilderhouse: Could you rephrase it sir, I'm sorry.

Holm: Well, under private ownership they will have a certain value on the world market, because it will be certain costs, ah, is state ownership going to put the oil on the market at a better competitive price to compete with Venezuelan Oil, East Indian Oil, any other oil? Or have we built in basically the same end price in Bellingham?

Guilderhouse: I'm not really qualified to testify on the world market prices, I had some discussion with a Mr. Whelley, several long discussions, and he states that ^{Alaskan} ~~any~~ oil, I hope I'm not misphrasing him, as I understood him, stated that ^{Alaskan} ~~any~~ oil will probable be a price taker and not a price maker for a long time. So, I can't talk about Indonesian Oil, or Venezuelan Oil, but I am saying the cost associated with the transportation move of the oil to the market is probable given equally efficient operation of the pipeline to be some magnatude less on the public ownership, than private. The actual cost _____ the cost of plans.

Holm: Now these figures predicated upon a specific figure, now I thought they were the same, I thought you were using the same figures, weather under private ownership or the other. If you want to let someone else answer that I can ask that later. May I ask you one other question? You stated earlier major risks of the bond holder was maybe lack of market, ah, isn't it a major risk of the bond holder, to contemplate strike, to contemplate injunctions because of a, a maybe the ^{Sighen man} ~~bitterman~~ getting all worked up over some oil spills and so forth, how will this relate to the cost of our bond?

Guilderhouse: To the cost of the bonds? ah,

Holm: What happens, for example if these things occur and the state is in an impossible position of delivering?

Guilderhouse: Well, that is the reason you would establish a general reserve fund. If you remember one of the things I talked about, was that, it would have to be established under conditions of state ownership, A substantial reserve fund that was equal to, lets for discussion sakes, say one year or 18 months of the total operation costs of an interest in amunization costs associated with the pipeline, to provide sufficient income to meet the authorities obligations in the event of a situation such as you described.

Holm: You don't think that will have a depressing effect on the cost of our bond?

Guilderhouse: Well, it depends on how vague, in terms of the interest costs, it depends on how vague you ultimately decide to make the general reserve, I you made it for a 10 year period or a 5 year period which is _____ of course, but it, it depends on how big a general reserve fund you make, and how the market proceeds and risks, you have described occur. I would say that, yea, there are, this is not going to be the cheep^{est} bond that was ever issued. I would say that, given one the size, you have to attract a lot of people,

Farrow: In answer to Representative McVay, You, on one question indicated that this was a darn good business to be in, ah, with that in mind, do you think its necessary for the

state legislature to put the full faith and credit of the of the state on the line to guarantee anything?

Guilderhouse: No sir, I don't think its necessary to put the full faith and credit of the state on the line.

Farrow: Thank you

Guilderhouse. Mr. Farrow,

Farrow: The point you brought up in response to this

1. What representation can you make with respect to the duration the _____ duration Such a Fund would have to be established for, how would you establish it in terms of the senate of revenue? and secondly, how would this enhance the states ability to _____ obligation box? Or would it decrease the states ability to establish a _____ ah, 20% ah, revenue,

Guilderhouse: May I restate the question to make sure I understood? You're asking essentially 3 questions, How would you go about establishing the size of the general reserve fund? and how much it should be, and then how it would effect the ability to sell the bond.

1) How you go about establishing, it is first, ah, you figure out what the cost, for lets say 1 year cause thats a convenient term, what the interest costs are, what the amortization costs are, and what the operating costs to the pipeline are. Fortunately pipeline is you can get a pretty good fix to what costs are because its not labor intensive, you know, you can really figure out after awhile pretty close to what it cost to operate a pipeline. You know your interest in your amortization, so you say that if, for some reason or another we have a force ~~XXXXXX~~ or the injunction to the strike that the senator mentioned, ah, how long is this liable to last, what is the biggest exposure and how long do we have to pledge to the investment bankers who are representing the investment community _____, How much do they say that you've got to give us before we can sell you bonds? And its negotiated and is sometimes an excruciatingly agonizing process

to come to drifts with how long this is, with the state or the seller of the bonds saying, "well it only needs to be 18 months," and the investment banker saying, "well gee, I can't sell it unless its 3 years," and then you say, "well I'll give you 20 months," for if he can say, I can sell in 2 and 1.5 years. Its this process of evaluation of risks, ah, and the likelihood and the probability of risks as well as what the actual costs are that ultimately come in to whats necessary to sell the bond, and its generally some multiple of what the costs are to operate the line in case its shut down. Or operate the facilities in case its shut down, and with respect to its impact on the states ability to sell other bonds, I don't see how it would have an adverse effect on it. The ensistance of the general reserve fund will send the context of the pipeline. I don't believe it would have an adverse effect.

McVay: Excuse me, Mr Farrow, are you through? Just one more point, it would seem to me that if ~~and~~^{also} the state pays off this bond, it aquires an etquity position in terms of a very expensive asset. That would seem to me, to help the general obligation situation. directly or indirectly, would it not? In a concrete way, at the end of five years if you've got 100 million dollar equity that you didn't have five years before, or an asset, or equity unit asset, then that would be helpful for the general balance sheet, would it not?

Guilderhouse: Yes sir, in my opinion it would.

McVay: Would that be an _____? as to how this would improve the G.O. picture.

Guilderhouse: I don't see how the existance of the general reserve funds would _____ contract to the overall financeing of the pipeling. It would be damaging to the G.O.

Havelock: Ah, I'm going to have a ten minute break.

McVay: ~~Just before we start~~ Like to call Robert Macy, ~~of the~~ _____ Company of N.Y.

who will discuss the marketing of public pipeline issues. Mr. Macy. Mr. Macy, would you

XXXXX please, before you start, XXXXXXXXXXXXXXXX just for the record, give us just a brief background of your experience.

Macy: I am Vice Pres. _____ of N.Y., i have been a student over the past 3 years. I have had 4 years of economic investment consulting, for National Company in Washington Prior to that time _____ for approximately the previous 4 years I was with _____ Company, which I was responsible for analysing various investment projects.

McVay: Thank you. Macy Mr. Chairman, member of the committee: As a representative of _____ I wish to note that we are pleased to be here to express our views as members of the investment banking group, which is consisting to state in evaluating the feasibility of state financing of the oil pipeline project. A project of this unprecedented magnitude obviously poses many unusual considerations, in analyzing various approached to the financial market. The first and most important group of consideration is the identification of the major risk factors involved. In this category we would include the following major investors concern, 1st) Are there sufficient oil reserves on the north slope to establish an economic justification for long term finance 2nd) Are there adequate assurances that the pipeline can be constructed within reasonable time and cost estimates. 3rd) Once built, can the pipeling be operated and maintained on a satisfactorily economic basis. 4th) are there adequate assurances that once built, sufficient revenue will be generated, to cover operating maintenance in debt servicing requirements _____ that issue. 5th) assuming the financing would have to be accomplished in stages, what ~~xx~~ assurance do the investors in the earlier stages have that market conditions will continue to sustain the timely injection of funds needed to complete the project. 6th) Are there back-up alternatives that the state finds that it cannot finance, build, or operate the pipeline on an economic basis. 7th) Does the status of domestic and world oil markets as projected, give satisfactory promise oil for ~~from~~ this source over the life of the issue and at what maximum price? 8th) What additional finance over reserves are there incorporated in the financing plans, to cover unforeseen problems in the future? Few if any of the above

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risks can be satisfied by absolute guarantees to the investor. Each, however must be addressed to some degree in the financing plan, and the relative degree to which these risks are secured. We'll determine not only the feasibility of the financing, but also the cost. We understand that extensive economic and engineering studies are available as background data and _____ some investors concern. The sizeable investment already made by the oil companies is undoubtedly a plus. In addition the state could, in theory, take certain steps to provide additional financial reserve to cushion the impact on the servicing of temporary unforeseen problems related to the afore major risks. However, these assurances alone, we believe, are insufficient to facilitate the market, the successful marketing of an issue of this magnitude. Furthermore, from all the suggestions which our group has considered, we know of no feasible plan which does not involve to some degree the cooperation of the oil ^{companies} ~~companies~~ with the state, in arriving at a feasible financing plan. The question is what form of co-operation is necessary and desirable? The first and most obvious to an investor, is to have both the full faith and guarantee of the state and the oil ^{companies} ~~companies~~ behind the issue, however we understand while the oil companies in particular may not wish to pledge their credit in this fashion. An alternative, and one we must recognize as a significant ~~leap~~ jump, in terms of the risk, as viewed by the investor. Is to restrict the liability or financial exposure of the oil companies in any financing, to the state which they have in the AKN oil venture. We have heard several possibilities suggested along each line, including those expressed earlier in these proceedings. Upon consideration, we believe that subject to the conclusion of satisfactory, contractual agreements with the oil company and others pertaining to the construction and utilization of the pipeline, that it is possible that these agreements coupled with satisfactory guarantees by the state, could make such an issue feasible. In conclusion, we ~~XXXXXX~~ believe that if as there appears to be in earlier testimony, there are sound, economic, and social reasons for the state

and the oil companies to cooperate in the financing of this project. ^{Now} ~~the~~ establishment of a legislative and organizational framework as presently under consideration by the legislature, should facilitate discussions between the state and the oil companies. The output of such discussions could greatly assist us as well, in providing a more definitive judgement as to whether we believe a state finance oil pipeling is feasible at this time. Thank you

XXXXX

McVay: We'll take, ah, questions in the usual order.

Groth: Mr. Macy, you say that subject to the conclusion of satisfactory contracts it is ~~XXXXX~~ possible, couples with satisfactory guarantees by the state that it might ~~XXXXX~~ work., ah, what kind of state guarantees are we talking about?

Macy: Senator Groth, One of the difficulties I think we all encounter in answering questions like this and one of the reasons ~~XXX~~ why I really outlined what we considered the major risk to the investors in such an issue, is that to satisfy any one of these risks ~~XX~~ theres a whole varity of different guarantees, different methods, that ^{are used} ~~are used~~ to satisfy the risk element to the investor. I think that perhaps it would be, I think it is pre-mature, if I may say so, to try to dissect one risk, or one method. And say well if we provided this then this would make is feasible, because frankly, I think until the legislation has been passed to set frame. And some feasible plan, or some mode of cooperation has been established with the oil ^{company} ~~company~~. That you cannot come up with sufficient pieces of a plan to satisfy, ^{to really make any meaningful judgement,} to really make any meaningful judgement.

Groth: Mr. Chairman, Thats one of the things that troubles me, and has troubled me since this discussion first arose.. Because, ~~XX~~ ah, seems to me, wether we have a bill or don't have a bill, somebody should go to oil companies and make an ^{enquiry} ~~enquiry~~, gentlemen, are you prepared to sell what you already have, and are you prepared to enter into meaningful negotiations with us presumming we have the power to do so. And it becomes a ^{discussion and} ~~discussion and~~ arrangement that troubles me very greatly. The first inquiry seems to me

I mean we all talk about establishing, buying meaningful negotiations, and opportunities for cooperation, but I'm troubled by the fact that maybe the first inquiry hasn't been made.

McVay: May I recognise that your not the ~~XXXXX~~ person for me to ask that question.

I haven't had any other questions. Thank you

Barber: Mr. Macy, I would like to ^{ask} ~~ask~~ you if you _____ that the passage of this house bill 569, The Trans ^{Alaska} ~~Alaska~~ Authority, is a matter which should be determined prior to negotiations with the oil industry, as to their reseption, of state~~own~~ ownership of the pipeline.

Macy: I believe it is.

Barber: The prime factor in initial negotiation.

Macy: Well I think that it, if I can try to expand a little ^{matter} ~~last~~ _____. I think that, _____ ~~there~~ perhaps a healthy indication in our system for private companies to exhibit considerable reserve in entering openly in cooperative agreements with public organizations. I think it's possibly, partly due to communication, it's partly due to some misgivings concerning motivations, objectives, goals _____ of interest and what have you. I think the variety of such motivation, on the part of public organizations, is certainly, probably greater than the variety on the corporate side. I think to the extent the state can exhibit through legislation their willingness to cut down and to focus what their motivations and interests are. It's really not only the legislation it's even the hearings and the testimony that we have here that exhibit what the goals and objectives of the state are and this is crystallized, I believe, in this legislation. I think this is very helpful to the corporations in better focusing on in what is involved in this, ~~this~~ this very broad term of cooperation of the State in such a project of this magnitude.

Barber: The saving in corporate tax determination would also very possibly, would it not, be a prime consideration to the oil industry.

Macy: In other words, you're saying if, if we

Barber: Won before I.R.S., and got a favorable decision, ^{what} ~~it~~ would enhance this Trans-Alaska Authority.

Macy: I believe this is the case. I think there is perhaps one additional factor that has to be brought to bear. Let us assume that you have ^{basic} ~~a~~ security. All things being equal, what might be the difference in interest costs between a tax. if it were taxable, or if it were non-taxable? The question here also involves one other factor. An issue of this size is going to ^{have} ~~be~~ have to be marketed very broadly. Some of the institutions which would have to be included in the market, such as life insurance companies, do not have the same tax structures as other institutions to which tax exempt securities might you might say, might normally be, to which they might normally be marketed. Therefore, I think you would probably because of the sheer size of this issue and the marketing problem, have to give up a portion of that differential between a, the normal differential, between a taxable and a non-taxable issue.

Barber: Senator Rettig

Rettig: Mr. Macy, in your studies of this situation, this proposition so far, are you and you as representing your associates and the companies that perhaps you're associated with in this study together this proposal, are you in a position to suggest that we should pass this, in other words, do you feel the chances are favorable that once it is passed that these bonds and various contracts could be worked out? Would you, in other words, recommend that we act favorable on this?

Macy: I would recommend that you act favorable on this. There is an urge to be ^{somewhat} flip in saying that you will never know, or you may never know, if such a financing were feasible until you provide a framework which would allow, I think, for what I consider a more cooperative exchange between the State and the oil companies.

Rettig: You're saying we can't do this unless we do have the vehicle.

Macy: Well, I say I find it highly doubtful that you could do that without the vehicle.

Rettig: Thank you.

Macy: I'm not guaranteeing that you'll be successful.

Rettig: I understand.

McVay: Any other questions - Mr. Farrow

Farrow: Thank you, Mr. Chairman. Assuming that the State goes ahead Mr. Macy, and starts to build the pipeline, despite an outstanding agreement with the oil companies, will this _____, or not?

It seems to me that we'd be able to save the time _____ at this time, There must be some area that you can say how the State has to guarantee its own _____. What areas are we talking about?

Macy: I'm afraid I have to come back to the same answer that I gave to Senator Groh earlier, that frankly, mind you, one of the

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such as satisfactory, reasonable, sufficient ~~and~~ if ~~you~~ ^{undoubtedly} Aside from the risks which I have listed here, there are ^{undoubtedly} others I could list, throw in another dozen; anyone of these risks can be met in a number of ways. To get focused on one ^{of this risk} way to attenuate part of the problem/by looking to the State for certain guarantees, is, really misleading.

I think that if you want a broad-- broader statement, which is highly generalized, the State and the oil companies, if such a plan, vaguely along these lines, were developed, have a stake in the development, exploitation, shipment, of oil to--(??) North Slope. When you put together a prospectus to market this issue, and assuming that you're not counting on external guarantees by the oil companies, I give full credit to the oil companies, you're going to have to ^{focus} on the economics of the North Slope, its oil and its future market, and cost of getting it there. You're going to be focused on what the state has invested ^{there}. I think perhaps that to the degree the revenues and stake that the State has, and that the oil companies have, that these are areas in which you will undoubtedly be exploring for certain assurances, guarantees, ^{agreements}. I am sorry, I don't think it is meaningful to be more explicit than that.

RITTING: I believe ^{Mr. Macey} -----
Mr. Macey, / you have indicated that you feel the chances of working out a suitable arrangement with the oil companies are sufficiently good that you would recommend the passage of HB 569, and you also ^{as} would/agree that up to that we should proceed with passing the ^{or bond} authorization ~~and~~ measure at the same time? Is that a necessary part of the...at this stage of the game?

MACEY: I think this is very useful. ^{the} the acceptance of these levels of financing to which the State to some degree is going to have its name

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~~for, perhaps~~

attached, because the legislature is going to go along with this, I think this is very important.

RETTIG,

We have, ~~perhaps~~ ^{perhaps} as you are no doubt aware, ^{per capita of bond} one of the highest/indebtednesses of any state at this time, and I am aware that many of the bond underwriters ^{look at it its on the books} already to be authorized.

With the many, many ~~still~~ ^{still} unanswered questions in connection with the three and one half billion dollar issue, ^{would the very} fact that that is on the books, ^{have} has any effect upon our other general obligation bonds that we may have to market immediately or in the near future?

MACY: I don't believe so. ~~It is~~ not, as I understand from Mr. Cady's interpretation.....what is really involved in the issue here, as I understand it, before any obligation of this type could occur, it requires so many plans enabling enabling legislation...I cannot really see where this would have effect ^{it is not}.

Thank you.

MACY

Any further questions? Mrs. Fisher?

Mrs. Fisher: Mr. MACY (Melsdig???) If HB 569 is passed, if everything went right, what time would you estimate the first bonds could be sold? This could be a guessistimate.

MACY: I would say the first bonds ^{might} ~~could~~ be sold.....the time factor, point of departure, the time after this cooperative agreement is reached with

the oil companies so it becomes given that that is reached, and that with suitable inputs from the investment community, that this agreement can be brought up to.....the investment bankers judge to be a satisfactory level of investment grade, ^{if you will} I would assume that within three

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to six months after that, the bonds could ^{you could} ~~would~~ begin to sell the bonds. (925)

Now we also have conditions over which none of us have control. It is not only

as I understand it

^{NOT ONLY} it's a question of whether you can sell the bonds. ^{AS HOW MUCH YOU CAN} ~~you might be able to~~ sell the bonds, how much ^{OF THE BOND} you can sell ^{AND} ~~the bonds for~~, at what cost. ^{AND} ~~these~~ are subject to market conditions, which we have relatively little control over.

MCVARE:

Other questions? Mr. ~~Stevens~~ ^{Grohst}

GROH: One quick one - in the broadest general terms, Mr. Macy, counsel fees, what are potential underwriting fees, in connection with the three and a half billion dollar issue? ^{HA HA} No, just as.....I think the people of Alaska ^{ought} ~~would like to~~ know. I'd like to know.

MACY: ^{I THINK THAT} This again is something that ^{I WOULD ALWAYS STOP AND} ~~would~~ say is existing subject to market conditions ^{probably graded it is} ~~and so forth~~ I would say that you have to accept ^{THE} ~~that~~ initial issues are going to have a larger underwriting spread, which is investment banking fee I think you are referring to, than the later issues because it is ^{A SHEER} educational effort that is going to have to go into the market. I think that various comments that we have discussed ^{AMONG THE} ~~with~~ members of the group, I think ^{THAT THE INITIATIVE} ~~the~~ that the underwriting discount here...somewhere between 1-1/2 and 2-1/2 %. Now admittedly I have heard of rumors in the ^{ended} slightly higher than that for newspapers that somebody is willing to ~~hire~~ the underwriters service, but ^{I THINK THAT} this is perhaps a realistic REALITY in today's market.

GROH:

You deal in these figures all the time - would you translate that for me?

MACY: Yes, that is the principal ~~(32M)~~ amount of THE ISSUE.

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CLARIFICATION
MCVANE: I would like ~~verification~~ ^{to 2%} on that...are are you....
are you saying 1-1/2 [^] of the entire issue, or would that 1-1/2 to 2% say of the
first hundred million?

MACY: No, each series, as it comes. Theoretically, at the end of
total
the total issue, the/underwriting spreads.....total ^{should} 1-1/2 to 2-1/2 % of the
total principal amount of the bonds - in this case 3-1/2 billion dollars.

MCVANE: you say seventy million.....2% ^{would be} ~~70~~ million?.....

(much hilarity)

HOLM:

MACY, I just want to follow that up - would this be the same, whether it was sold by
private industry or not?

MACY: Now in general, the underwriting spread for ^A private issue
here, on this particular case - I think the alternative you are referring to
would be the oil companies (yes) financing - would be less.

HOLM: Approximately how much less?

MACY: This gets very subjective: I'd say that it might run a
half percent lower.

HOLM: So we pay a half per cent premium? Why do we pay a
half per cent premium?

MACY: I think it is because ^{OF THE WAY IN WHICH} the difference in which corporate
municipal or
issues are marketed, and the way ~~in which~~ public issues are marketed,
the relationship between the sale ^{being} --- IF YOU WILL, THE SELLERS
the underwriters and the institution.

HOLM: Well, ^{THEN IT WOULD BE --} ~~anyway~~, doesn't that narrow that 1-1/2 % spread that
^{A LITTLE BIT} was talked about, earlier - I suppose you were here - ^{DOESN'T} this narrow that down
^{THAT WERE RAISED} to one, and some of the other questions [^] took another half per cent ~~out~~ OFF,

MACY : Well, ^{you} we have to understand....you have two things here....
in an underwriting discount, our spread, ^{IF you will} if you will, ^{which} is a one time cost at
the front end... ^{THIS} ~~it~~ comes out and is deducted from the net proceeds ^{OF} ~~that~~
^{the} ~~are offered~~ ^{ing.}

HOLM : So it is just the first year, ^{MACY:} its not an annual thing,

HOLM : No, I UNDERSTAND, BUT ITS

 : I understand, the.....

MACY : I think the spread that you're referring to was the spread
in the interest cost, for the life of the issues. (PT)

HOLM : For the first year there would be the spread wouldn't
be nearly as great?

MACY : That is correct.

HOLM : Thank you.

RETTIG : Mr. Macy, would you be willing to pay the bond counsels
fee out of that?

RETTIG
(laughter) you don't have to answer that.

Mr. Rose?

Mr. Rose : My question, Mr. Chairman, was along the same line
that you were just asking.....the answer to Senator ^{GROH} ~~Rowe's~~ (PT) question.
I am interested in the underwriting fee, but Senator Groh asked about the
counsel fee - what kind of a spread does that represent?

MACY : I am afraid I couldn't GUESS MYSELF.

Mr. Rose : You have no idea? There is no DOOR OPEN FOR THIS KIND OF THING.

MACY : There may be - I believe Mr.

RETTIG : I believe Mr. Macy has indicated he ~~did not respond to that~~
is not prepared for that,
not being bond counselor.

RETTIG : Are there any other questions?

CHRISTENSON: Yes.....where can we get this figure?

RETTIG: Mr. Wohlforth, would you care to volunteer this information?

Wohlforth: ~~I am afraid I am not any improvement as unfortunately I was~~ ^{there}
some
in conversation at my table.

W: Can you rephrase it?

ROSE: Senator Groh ~~asked~~ ^{earlier} about what the normal liquidation bond
fee
counsel/would be ~~RETTIG:~~ what would be the bond counsel's fee for representing
the State in this issue?

WOHLFORTH: Well, again since I didn't hear the question, I imprudently
came to the table

RETTIG: Are there any other questions?

WOHLFORTH: ~~It is the largest or not~~ ^{FINANCED} would be the largest ~~PROJECT~~ ^{THINK} ~~It would certainly be the~~
~~largest project~~ in the Western Hemisphere and I....the second largest in the
world, to be perhaps "smart alecky" negotiable ^{AGAIN,} an arms length transaction
between those public officials responsible for the public purse, or those

people who are performing services. And again, I ~~think~~ ^{think} its of the magnitude
ON which unfortunately I
where I don't think the committee can begin on meaningful information.

MCVINE: Its not on a minimum fee schedule?

RETTIG: Mr. Macy, do I understand that you have to leave town tomorrow?
Tonight, there'll be a few minutes perhaps shortly, that any members who want
to consult with Mr. Macy, may do later. ^{SO}

W: Thank you very much, Mr. Macy, for appearing.

RETTIG: In this hearing we've considered only the various aspects
OF possible State ownership of the pipeline. There are other majors introduced
by the administration ..sponsored by the administration....namely SB 313, 14 and 15
concerning rights of ways, safety standards and pipeline regulations. Mr. Havelock,

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are you ready to proceed?

Mr. Havelock: Senator, the....if I may be allowed a moment of digression
^{A NON-}
to answer ~~the~~ question of Senator Groh earlier - he asked ...he made an inquiry

about he couldn't understand why we hadn't approached the oil companies

^{TO FIND OUT}
~~about~~ this preliminary question of whether they were willing to....if I may

answer this in sort of an analogy.....I suppose if possible that I could get

up from this table and go and ask the attractive girl at the end of the table

whether she's willing, and I'm sure she'd tell me to go jump in the lake. ^{IF I Did so.} On

the other hand, if I invited her out ^{TO DINNER} I might get a good deal more information ^{ABOUT}

whether she was willing.....start looking in store windows, I would ^{AT FURS & DIAMONDS}

probably get a good deal more information! An old negotiator like Senator

^{GROH}
Grothe is probably quite aware of the answer to this. (laughter) This is

Attorney General OLAF HELLIN who will discuss the bills YOU REFERRED TO

GROH: Mr. Chairman, I have a comment....my question is, have
you ever called them?

HAUFLOCK: We've talked to them hundreds of hours.

GROH: Did you ever ask them "are you willing to sell?"
^{ITS BEEN covered in the papers quite fully.}
BETTIG: According to the papers, quite willing. (???)

BETTIG: The answer was "no."

GROH: Then, what are we doing here?

BETTIG: He is still taking them out to dinner!

GROH: ^{I SEE.} Havelock: Before Mr. Helin starts

^{with his}
~~as part of the~~ testimony, Mr. Chairman, there is a bill that is not before this

committee, ^{BUT} which will relate to the subject matter generally which will be

testified before other committees, which is the so-called 20 mill property tax

^{TO}
~~law on the~~ ^{OK} ^{EQUIPMENT} pipeline transportation, which is very much related to the subject

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Testimony of Eric E. Wohlforth
Commissioner of Revenue

March 6, 1972

I am Eric Wohlforth, Commissioner of Revenue. I will summarize past projections of North Slope revenues and those presented today based on private ownership, and contrast the revenue effect of private ownership case with the case of a pipeline owned by the State.

The most recent public North Slope oil revenue projections, before those referred to the Governor last week, were made by the Division of Oil and Gas in cooperation with the Department of Revenue as part of the State's contribution to the federal pipeline Impact Statement released by Governor Egan on July 30, 1971. These projections were developed from a computer model which was based on the information then available to the State and showed numerous economic cases on differing assumptions again based on facts then assumed to be ascertainable.

The July 30 report states on page 166 that, "the originally estimated \$900 million cost of the pipeline has already increased considerably. Present cost estimates range from about \$1.0 to \$2.3¹ billion." The revenue projections used the assumption of \$1 billion as the lowest installed cost and \$2.5 billion

as the highest estimate. The footnote to this statement gives the backup for the State's cost estimates. It notes that as late as June 19, 1971 Alyeska furnished the State Department of Revenue an estimate of \$969 million as the cost of the entire contract and concludes with reference to a statement from Interior Secretary Rogers C. B. Morton in late spring of 1971 that environmental precautions are contributing to a higher price tag of around \$2.3 billion. This figure of \$2.3 billion total cost was used in the State's "most likely" estimate of North Slope revenues. The revenue estimates included in the State's Report developed from this estimate of total cost, assumed refinery values in fiscal year 1976, the then estimated start up year, of \$3.37, marine transportation costs of 44 cents, a pipeline tariff initially of 80 cents per barrel, giving a wellhead value of \$2.12. From these figures it was estimated that total royalties and taxes would amount to \$164 million a year in fiscal year 1976, the first year of pipeline operation. In the second year of operation, fiscal 1977, total revenue was estimated at \$278 million, the third year \$282 million, and the fourth year \$311 million. In the then estimated fifth year of production, fiscal 1980, the pipeline tariff was calculated at 47 cents a barrel with the marine transportation costing 52 cents leaving a wellhead value of \$2.56. In that year we showed a total of \$348 million in total royalties and severance taxes from the pipeline.

Other estimates were also run with different assumptions. For example, one set the pipeline cost at \$1 billion with again the initial production year assumed in fiscal 1976. A wellhead value of \$2.75, with lower marine transportation and tariffs produced \$212 million in revenues in the first year of production and the fifth year of production on this optimistic/projection the State was assumed to capture \$412 million in oil pipeline revenues. ^{then} A pessimistic case which assumed a pipeline cost of \$2.5 billion shows a wellhead value of \$1.76 in the initial year of 1976 and royalties and taxes of \$136 million in that year. In 1980, however, at a wellhead value of \$2.20 ^a per barrel, royalties and severance taxes reached a figure of \$297 million. Incidentally, in all of these cases, one of the main reasons wellhead value increases over the years is that transportation costs go down as the volume of oil shipped increases.

Several important events have now come to light which have required the State to revise downwards drastically its revenue estimates. The first indication of the fact that the State was incorrect in assuming as it did in the Impact Statement that a production flow starting at 600,000 barrels per day would reach 1.7 million barrels per day in the second year of production was disclosed in the summary project description of the trans-Alaska pipeline system received by the State this fall. On page 55 of that document it is stated that

the pipeline system will be brought to its full capacity in stages. In the initial phase of operation the system will have the ability to transport 600,000 barrels per day. The report goes on to state that the second phase is tentatively scheduled to be completed approximately two years after initial start up. In this phase the system will have a design capacity of 1,200,000 barrels per day. The final phase is expected to be completed approximately seven years after initial start up at which time the pipeline will reach its ultimate capacity of 2,000,000 barrels per day according to the project description. In other words, there will be at least 500,000 barrels per day less production in the second year of operation and *each* every year thereafter for the initial seven years.

The next shock to the State was disclosed by the SEC Registration Statement filed by British Petroleum Co., Ltd., on October 12, 1971. In the offering circular accompanying the registration statement the following statement is made at page 24:

... "The initial construction phase of the pipeline is expected to provide a minimum aggregate throughput capacity upon completion of 600,000 barrels per day. This capacity is designed to be expanded in two stages, the first stage resulting in a total capacity of 1,200,000 barrels per day, and the second in a total capacity of 2,000,000 barrels

per day. / It is presently estimated that the cost of the pipeline upon completion to the 600,000 barrels per day capacity would be approximately \$2.3 billion, and that increasing the capacity to 2,000,000 barrels per day would increase the cost by approximately \$400 million." (Emphasis added.)

On November 10, 1971, Atlantic Richfield / filed a Registration Statement with the SEC stating that:

... "The cost of the system upon completion to the 600,000 barrel per day capacity is presently estimated to be approximately \$2.4 billion, of which the Company will be responsible for approximately \$675 million. The additional cost to all participants of increasing the capacity to 2,000,000 barrels per day is estimated to be at least \$400 million." (Emphasis added.)

Thus, by mid November, / the total pipeline cost had escalated to \$2.8 billion or \$500 million over the average case assumed in July when the State made its revenue estimates. In fact it increased \$100 million in less than one month

between SEC filings. This dramatic increase in pipeline costs revealed in official documents at the time of Governor Egan's first announcement on State ownership made it urgently necessary that the State finally determine the likely magnitude of pipeline costs. Commissioner Campbell has already indicated the independent study which the State has made through its consulting engineers, Tibbets, Abbott, McCarthy and Stratton, and the foundation for the present estimate of \$3.5 billion. These figures have ^{been} ~~just~~ recently been developed along with an independent evaluation of operating costs so that for the first time the State can make a reasonable projection of the probable amount it can expect to capture from North Slope oil revenues.

The base case shown to you today in graphic form assumes the total pipeline cost of \$3.5 billion financed 90% by debt at an interest rate of 8%. It conforms to the Alyeska throughput assumptions of full production only in the seventh year of pipeline operation. It shows the same ICC permitted rate of return as shown in the State's projection in July. In the fourth year from the beginning of construction ^{or} and the first year of production, or 1977, we now show a negative wellhead or no State oil revenues. This was the year comparable to that in which it was earlier shown that the State would capture at least \$164 million in revenues. The fifth year, 1978, the second assumed year of operation,

we earlier estimated \$278 million in State revenues. In these two years alone the net revenue loss to the State over earlier estimates amounts to \$442 million. By the sixth year or 1979 the new projection shows \$84.6 million in oil severance and royalty revenues. Earlier we estimated \$282 million for that year. The net loss by that year over earlier estimates is \$640 million. Not until the 15th year of the pipeline operation do royalties and severance taxes amount to near the amount shown to our previously calculated second year. In the 15th year we show severance and royalty revenues of \$277 million.

The question may be asked whether this is most pessimistic of cases which can be produced. The answer is clearly no for three reasons. In the first place the revenue loss figure mentioned above gives no effect to our expectation now of first pipeline operation in the year 1977, whereas in July ^{assumed} we estimated a full year of revenues starting on July 1, 1975.

In the second place we show State taxes in each year of operation of approximately \$33 million. For the first three years of operation State income taxes are estimated to total approximately \$100 million or \$33 million a year. This assumes the full State income tax rate on pipeline profits. Experts have indicated that this may not be a realistic assumption. Even, however, with the most optimistic income tax estimate net revenue loss from earlier projections amounts to \$540 million during the critical first three years of operation.

Thirdly, calculation of the 7% permitted rate of return on valuation may err on the low side. The leading text on the subject "Petroleum Pipelines and Public Policy" by Arthur Johnson cites numerous instances of the slowness of the ICC to actually evaluate pipeline costs and its heavy reliance on industry figures. The Cook Inlet pipeline valuation itself took three years to complete.

The 7% figure is not high also when it is remembered there are seven separate proposed pipeline owners, each of which may aggregate earnings of other pipelines when the 7% rate is considered. It is entirely possible that higher return rates may be permitted until the valuation of the line is complete and even thereafter when earnings of other pipeline companies are aggregated to arrive at a total rate of return.

The next case presented shows the possible economic effect of State ownership of the pipeline. Financing is assumed in the amount of \$1 billion in each of the first two years of construction at 8%, \$900,000,000 in the third year of construction at 6-1/2%, \$250,000,000 at 8% in the first year of operation, and \$310,000,000 in the second year of operation. This case also assumes the same ICC permitted rate of dividend payout as assumed for the private case, namely, 7% which is a cash dividend payout limitation in each year of the projection. In arriving at the State's net cash flow, operating expenses, amortization, and interest on bonds are deducted from the gross income. During the

first year of operation net cash flow to the State through its tariff on the pipeline is \$230 million and royalty and severance taxes of \$15.7 million for a total of \$245 million. Obviously, in State ownership no federal or state income taxes are calculated on pipeline income. In the fifth year from beginning of construction or the second year of operation net cash flow is \$228 million which together with royalty and severance taxes of \$17 million produce a total of \$245 million. In the sixth year from the beginning of construction and the third year of operation net cash flow amounts to \$227 million through the tariff and total royalties and severance taxes amount to \$123 for a total of \$350 million. In the 15th year cash flow is reduced to \$183 million by reason of the fact that the pipeline has depreciated but total royalties and severance taxes amount to \$297 million for a total to the State treasury of \$480 million.

It is emphasized that this case makes almost identical assumptions to that for the private case described above. It should be emphasized that the net income shown to the State is computed after debt service on State bonds. To avoid a speculative argument on the possible differential between interest rates on the State's debt which may be tax exempt versus taxable interest on the private borrowing we show all but \$900,000,000 in State bonds at the same 8% rate. The main differences, of course, lie in the fact that the State is not subject to federal income tax and will receive no state income tax from pipeline operations.

since it is the owner. The timing of the bond issues for both private and public ownership is the same although the term of the public bond issue is shorter indicating heavier debt service loads and the State of course is financing the pipeline 100% on a debt basis.

Numerous additional assumptions can be made on the question of the manner of public financing, the rate of return permitted either to the State or to private pipeline owners, interest rates payable by the State and private owners, the effective tax rate in private ownership, to mention only a few. We know that estimating the effect of economic projects based on events three to seven years away must rest on assumptions which are to a degree speculative. You will hear testimony that our assumptions are incorrect. The point is that no one can say with positive certainty what our revenue picture will be with the pipeline in private ownership. We have, however, tested prior assumptions based on official information now before us. This effort has convinced the administration that it must do what it can now to remove the uncertainty of the revenue picture in the late 1970's and in the 1980's. Mr. Eppenbach will explain how our projections were made and some of the detail on the charts before you.

JOINT HEARINGS ON PROPOSED PIPELINE LEGISLATION

MARCH 6 THROUGH MARCH 9, 1972

WITNESS REGISTER

<u>NAME</u>	<u>AFFILIATION</u>	<u>REPRESENTING</u>
1. H. A. Boucher	Lt. Governor	Administration
2. Charles Herbert	Commissioner, Nat. Resources	Administration
3. John E. Havelock	Attorney General	Administration
4. Bruce Campbell	Commissioner of Highways	Administration
5. Eric E. Wohlforth	Commissioner of Revenue	Administration
6. Larry Epperbach	Department of Revenue	Administration
7. Joseph R. Henri	Commissioner of Administration	Administration
8. H. M. Temple III	Temple, Barker & Sloane	Administration
9. Charles Kates	Hawkins, Delafield & Wood	Administration
10. Tom Gildehaus	Temple, Barker & Sloane	Administration
11. L. E. Crowley	Salomon Brothers	Administration
12. Robert Macy	Kuhn, Loeb & Company	Administration
13. John E. Havelock	Attorney General	Administration
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JOINT HEARINGS ON PROPOSED PIPELINE LEGISLATION

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<u>NAME</u>	<u>AFFILIATION</u>	<u>REPRESENTING</u>
1. Charles E. Spahr	Aleyeska Pipeline	Standard Oil of Ohio (SOHIO)
2. W.J. Williamson	Aleyeska Pipeline	Law Professor U. of Houston
3. Harry R. Jones	Aleyeska Pipeline	Attorney specializing in State & Interstate commerce. Houston, Texas
4. Donald W. Markham	Aleyeska Pipeline	Washington, D.C. Attorney
5. Edward L. Patton	Aleyeska Pipeline	President of Aleyeska Pipeline
6. Joseph R. Cortese	Aleyeska Pipeline	Attorney Ohio, specialist in law re Powers of State & local govt
7. Raymond B. Gary	Aleyeska Pipeline	Investment Banking, Underwriting & distrib of securities.
8. George A. Seymour	Aleyeska Pipeline	Mobil Pipe Line Company.
9. Thomas R. Broussard	Aleyeska Pipeline	Atty. Spec in taxation, Legal Dept. ARCO
10. Edward L. Patton	Aleyeska Pipeline	Aleyeska President. See 5 above
11. Joseph R. Cortese	Aleyeska Pipeline	Same as 6 above.
12. Richard M. Donaldson	Aleyeska Pipeline	V-Pres & Gen Counsel of SOHIO
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JOINT HEARINGS ON PROPOSED PIPELINE LEGISLATION

MARCH 6 THROUGH MARCH 9, 1972

WITNESS REGISTER

<u>NAME</u>	<u>AFFILIATION</u>	<u>REPRESENTING</u>
1. S. C. SANDUSKY	DIVISIONAL MANAGER	MARATHON OIL COMPANY
2. DON DICKEY	GENERAL MANAGER	STATE CHAMBER OF COMMERCE
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BY THE RULES COMMITTEE BY
REQUEST OF THE GOVERNOR

IN THE HOUSE

HOUSE JOINT RESOLUTION NO.
IN THE LEGISLATURE OF THE STATE OF ALASKA
SEVENTH LEGISLATURE - SECOND SESSION

Proposing an amendment to the
Constitution of the State of Alaska
provisions regarding the use of state
funds for the debt of public
corporations.

BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. Sec. 7, art. IX of the Constitution of the State of Alaska
is amended to read:

SECTION 7. DEDICATED FUNDS. The proceeds of any state tax or license
shall not be dedicated to any special purpose, except when required by the
federal government for state participation in federal programs, or when
dedication is provided by law, for the purpose of securing the payment of
bonds and notes of a public enterprise or public corporation of the state
or a political subdivision of the state. This provision shall not prohibit
the continuance of any dedication for special purposes existing upon the
date of ratification of this constitution by the people of Alaska.

* Sec. 2. Sec. 8, art. IX of the Constitution of the State of Alaska
is amended to read:

SECTION 3. STATE DEBT. No state debt shall be contracted unless
authorized by law for capital improvements and ratified by a majority of
the qualified voters of the State who vote on the question except that the
State may guarantee by law bonds and notes of a public enterprise or a public
corporation of the State created or empowered to construct pipelines for the
transportation of oil or gas or both and may by law authorize such public
enterprise or public corporation to mortgage any State lands or properties

1 and royalties or rents, issues and profits therefrom as additional security
2 for its bonds or notes, whether or not guaranteed by the State. The State
3 may, as provided by law and without ratification, contract debt for the
4 purpose of repelling invasion, suppressing insurrection, defending the State
5 in war, meeting natural disasters, or redeeming indebtedness outstanding at
6 the time the constitution becomes effective.

7 * Sec. 3. The amendment proposed by this resolution shall be placed
8 before the voters of the state at the next statewide election in conformity
9 with sec. 1, art. XIII of the Constitution of the State of Alaska and the
10 state election laws.
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PROPOSED AMENDMENTS TO HOUSE BILL NO. 569

Page 2, line 26:

After the word "interest." strike the words "It is also declared to be in the public interest for the state to guarantee the principal and interest on bonds issued to finance the facility."

Page 19, line 12:

Delete all of AS 44.58.260.

Statement of Charles F. Herbert
Commissioner of Natural Resources

In 1964 the State of Alaska selected 1,593,705 acres on the North Slope, between Naval Petroleum Reserve No. 4 and the Arctic Wildlife Range. The land selected was considered to have good potential for petroleum but none suspected that it would contain the largest oil pool ever found in North America. On the map, the lands north of the heavy green line are those selected in 1964 and the orange-shaded area covers the Prudhoe Bay oil field. I want to emphasize that not all of the land within the shaded area will be productive of oil or gas--in fact, there are a number of dry holes within the area shown as the oil field.

Although millions of dollars had been spent in an unsuccessful search for oil on Federal lands southwest of State lands, the first lease sale of North Slope lands by the State was moderately successful and provided revenue at a time when it was needed badly. Greater interest was shown in subsequent lease sales even though drilling on State lands had been disappointing. Finally, on what was said to be a "last try" for oil on the North Slope, ARCO announced a major discovery in July, 1968. The State then selected an additional 2,852,880 acres south of the original North Slope selection. This later selection, for which tentative approval by the Bureau of Land Management has not been received, lies between

the green and brown lines on the map. Note that over half of the area in the later selection is covered by leases. These are Federal noncompetitive leases which had been issued prior to State selection. Some have expired recently and many are due to expire within the next few years, unless oil or gas is found in productive quantities.

With oil interest at fever pitch, the State sold much of remaining tentatively approved North Slope lands at a lease sale on September 10, 1969. The total of bonus bids received at that sale is the largest ever recorded anywhere.

Bonuses received from the sale of State leases on the North Slope:

<u>Date of Sale</u>	<u>Acres Leased</u>	<u>Bonus/Acre</u>	<u>Total Bonus</u>
Dec. 8, 1964	476,147	\$ 9.20	\$ 4,379,729.91
July 15, 1965	403,000	15.25	6,145,472.59
Jan. 24, 1967	42,397	34.87	1,478,777.23
Sept. 10, 1969	<u>412,548</u>	<u>2,181.66</u>	<u>900,041,605.34</u>
	1,334,092*	\$ 683.65	\$912,045,585.07

* This figure includes some offshore lands and some duplication caused by forfeiture of leases and subsequent re-leasing.

Bonuses on future sales of leases on the North Slope are most difficult to estimate. Certainly, there is little incentive to purchase leases in the area until such time as construction of a pipeline is assured. About all we know is that the State does own, or will own, land that can be offered for competitive oil and gas leasing.

We estimate that the following land may be offered at some future date:

Unleased land on which the State now has tentative approval	200,000 acres
Selected land, less valid Federal leases - at least	1,000,000 acres
Offshore lands between Pet. 4 and and the Arctic Wildlife Range	300,000 acres

Since Alaska now ranks second among the states in proven oil reserves, and will probably outrank the leading state, Texas, when more active drilling is resumed, Alaska can look forward for very many years to substantial income from oil and gas royalties and severance taxes.

The Prudhoe Bay field alone has a proven reserve of 9.6 billion barrels of oil and 26 trillion cubic feet of natural gas. To the west of Prudhoe Bay, the Ugnu field has oil but there has not been enough drilling to permit a reliable estimate of reserves. Wells in the Ugnu field are much less productive than those in the Prudhoe Bay field but they should add materially to North Slope production. Other potentially productive structures are known so we think that an estimate of 20 billion barrels of oil from State lands on the North Slope is justified.

In addition to production from State lands and offshore lands on the North Slope, oil and gas will be produced from lands that may be selected by Native Regional Corporations and from Federal lands that are or may be leased. We expect that someday Petroleum Reserve No. 4 will be developed, and there is some possibility that the very attractive Marsh Creek anticline in the northwesterly portion of the Arctic Wildlife

Range may be drilled. The highly regarded Canadian publication, OILWEEK, estimates that the Alaskan North Slope will produce 50 billion barrels of oil and many trillions of cubic feet of natural gas. Most certainly, oil and gas pipelines from the North Slope will be busy for many years.

In all existing leases on the North Slope, royalty is fixed at 12-1/2% of the wellhead value. However, leases issued prior to 1969 provide for a royalty of 5% of the production from a lease on which a discovery of a new field is made. Only one lease in the Prudhoe Bay field is entitled to the reduced royalty and that privilege expires in 1978, ten years after the date of discovery.

All existing North Slope leases have a term of ten years, or as long as production is maintained. Leases may also be extended if committed to an approved unit agreement. Unit agreements, which are formed by pooling of interests of all lessees on a geologic structure capable of, or believed to be capable of, producing oil or gas, carry specific drilling requirements which must be approved by the Department of Natural Resources if on State land, or by the U.S. Geological Survey if on Federal land. Prior to 1969, leases on lands to which the State had only received tentative approval were issued as conditional leases and the lease term did not begin to run until the State received patent to the land. With the exception of the leases sold in the September, 1969 sale, North Slope leases are conditional and the term of lease has

not begun to run.

The wellhead price of oil or gas, on which royalty and severance taxes are based, is stated in each lease as the highest of (1) the price actually paid by a purchaser at the well, (2) the posted price by the Lessee in the oil or gas field, or (3) the prevailing price paid to other producers. Since nearly all Alaskan oil is sold on the West Coast of the United States, the wellhead price is determined by the field price at the point of delivery on the West Coast, less transportation charges. Since these charges are variable among producing companies there has been enough confusion in the Cook Inlet Basin to cause a lawsuit between the State and one of the producers. Since this matter is now before the court I cannot comment further, other than to hope that clear guidelines for the determination of wellhead price are established either by directive from the court or by general agreement.

All oil and gas produced from State lands on the North Slope, other than offshore lands, is subject to a payment of 2% of the gross value (i.e., wellhead price) to the Alaska Native Fund, until such time as \$500 million has been paid into that fund from all sources of State income subject to such payment. Although provision for payment to the Alaska Native Fund effectively reduces State royalty on a standard oil and gas lease to 10-1/2%, the payment is treated in State accounts as an obligation against the State treasury and so does not enter into estimates of State income from minerals.

After deduction of royalty from wellhead price, the remaining value is subject to a State severance tax based on the rate of production from each producing well. The tax on oil is:

3% on the first 300 barrels per day

5% on the next 700 barrels per day

6% on the next 1,500 barrels per day

8% on all production over 2,500 barrels per day

The severance tax on natural gas is 4% of the wellhead price, regardless of the rate of production.

Derivation of State income from royalty and severance tax is:

Assumed wellhead price of oil	\$ 2.00
State royalty @12-1/2%	0.25
Taxable value of oil	<u>1.75</u>
Severance tax @ 7% (best estimate)	0.12

Total State income then would be \$0.37, or 18-1/2% of the wellhead price, a percentage that is probably applicable to oil production from the North Slope, regardless of wellhead price. For natural gas, State income is 16% of the wellhead price.

3/6/72

I HAVE BEEN ASKED BY GOVERNOR EGAN TO DELIVER HIS MESSAGE TO THE PEOPLE OF THE STATE OF ALASKA IN HIS ABSENCE.....AS LIEUTENANT GOVERNOR I HAVE HAD THE OPPORTUNITY TO WATCH OUR CHIEF EXECUTIVE DEAL WITH THE AGONIZING REALITIES THAT DELAY IN PIPELINE CONSTRUCTION AND SPIRILING COSTS HAVE RESULTED IN.... AND WHILE APPRAISALS THAT DO NOT VIEW A PORTION OF OUR FUTURE TOTALLY THROUGH ROSE COLORED GLASSES ARE DISTASTEFUL TO SOME.... I HAVE NEVER SEEN OUR CHIEF EXECUTIVE SWERVE FROM HIS DUTY TO OUR STOCKHOLDERS.....THE PEOPLE OF THE STATE OF ALASKA

THE FUTURE OF OUR STATE IS A BRILLIANT ONE....NO ONE KNOWS THIS BETTER THAN OUR GOVERNOR WHO HAS DEVOTED OVER THIRTY YEARS OF HIS LIFE IN SERVICE TO ALASKA AND HER PEOPLE....THERE HAVE BEEN ROCKY SHOALS BEFORE AND OUR SHIP OF STATE HAS NAVIGATED THEM.... THEY WERE NOT OVERCOME BY WISHFUL THINKING...WE NEED NOT BE AT ODDS WITH OUR PARTNERS IN THE FUTURE...THE OIL INDUSTRY...WE RECOGNIZE YOUR CORPORATE RESPONSIBILITIES....I AM SURE YOU WILL RECOGNIZE AS GOOD CITIZENS OUR RESPONSIBILITIES...AND IT IS IN THIS SPIRIT THAT GOVERNOE EGAN HAS ASKED THAT I READ THIS MESSAGE INTO THE RECORD.....

SCHEDULE OF JOINT HEARINGS ON PROPOSED
PIPELINE LEGISLATION

COMMITTEES:

SENATE COMMERCE COMMITTEE, RON L. RETTIG, CHAIRMAN.

HOUSE STATE AFFAIRS COMMITTEE, RICHARD L. MCVEIGH, CHAIRMAN.

LOCATION: GOLD ROOM, BARANOF HOTEL

BILLS TO BE CONSIDERED:

SB 313 - Relating to lease of rights-of-way.

SB 314 - Relating to safety standard for oil and gas transportation.

SB 315 - Creating Alaska Oil and Gas Transportation Commission.

SB 294 - Creating Alaska Leasing Board.

HB 569 - Establishing Trans-Alaska Authority.

HB 570 - G. O. bonds, \$3,500,000,000.

MEETING SCHEDULE:

Monday, March 6, 1972	2:00 p.m. to 6:00 p.m.
Tuesday, March 7, 1972	8:00 a.m. to 11:00 p.m. 2:00 p.m. to 6:00 p.m.
Wednesday, March 8, 1972	8:00 a.m. to 12:00 p.m. 1:30 p.m. to 6:00 p.m.
Thursday, March 9, 1972	8:00 a.m. to Completion

A special section will be reserved for other Members of the Legislature.

Testimony of Lawrence Eppenbach
State Investment Officer

March 6, 1972

Mr. Chairman, Committee Members. In testimony already presented you have heard a great deal about revenues, costs of pipelines, calculations of royalties and severance taxes and permitted dividends. Rather than to add more numbers, more formulas, more calculations, I think it would be prudent now to pause and develop perspective on the numbers already given to you and about the many charts. To do this, I should like to talk first about how the State brought all of its pipeline information together to calculate what is really the most important piece of information thus far and that is an estimate of total revenue from the North Slope.

^ We employed a computer model which simulated each year, economic operation of the pipeline under varying conditions regarding ownership, financing, taxes, and earnings limitations. In a sense, an income statement was prepared each year for the owner of the line. This income statement does not appear so very different, at least in terms of its expressions, from that of any other income statement. Gross revenues to the pipeline are derived from its tariff charge on barrels of oil transported through the line. That gross revenue less the cost of operating and maintaining the line, less depreciation, and less interest costs for financing

the line, will produce a net income figure. From that we deducted any federal or state income taxes paid to yield a net after taxes income.

Similarly, the cash flow to a pipeline company is much like that of any other business. The net after tax income plus any additional cash flows which may be generated because the depreciation charge that is provided for in the income statement happens to be greater than the bond retirement actually made by the company. The only place that pipeline operation appears different, economically, to that of the ordinary company, is in the dividend payout allowed each year by the pipeline company to its owners.

That dividend is not some percentage of equity or some rate of return of capital investment, it is a percentage dividend allowed on the valuation of the pipeline as determined by the ICC. The ICC valuation approach takes into account many issues: original cost of the line, depreciation, percentage increases for going concern value, and additional percentage increases for inflation. Our computer model had to also simulate this ICC valuation. In general terms, during the first year of operation ICC valuation was about \$3-1/4 billion. In the following years it increases slightly as additional phases of operation were under way providing for higher throughput and then decreased in value as the line began to depreciate.

The dividend limitation on ICC valuation is a critical variable in the

economics of pipeline ownership. Our model, given a dividend rate calculated back up the income statement to find out what kind of tariff would have to be placed upon the pipeline in any year to provide gross revenue required to generate the appropriate cash flow for the dividend. During the first year of operation of the trans-Alaska pipeline, the 7% dividend limitation provides for a dividend to the parent company of over \$230 million, a legal dividend provided only to the owner of the pipeline.

If I may turn your attention now to the large chart it is that very dividend that accounts for the vast difference between estimated income to the State of Alaska under conditions of public ownership on the top line, versus conditions of private ownership, the bottom line. You will note that both lines slope upward as the throughput of oil through the line increases, clearly shown as a step increase between operation of the line in phase one, a capacity of 600,000 barrels a day up to phase 2, a design capacity of 1,200,000 barrels per day. But the graph does not display all of the information which is in the tables alongside of it.

First, in public ownership, the major part of revenue during the early years is derived from dividends with positive and growing amounts of revenue coming from wellhead value royalty and production taxation. You will note that there are no state income taxes included here as a revenue source to the State

under conditions of public ownership.

Under conditions of private ownership, a very different case develops. Here in the initial year a total of about \$37 million should accrue to the State. Where does it come from? \$3.2 million of it only comes from the North Slope in the form of gas royalty and production tax payments. This is gas that is assumed to be shipped in a trans-Canadian gas pipeline. The remaining \$34 million comes from state income taxes. In the 7% dividend case displayed here there is no positive wellhead value for oil during the first two years of operation under private ownership. In this case, for there to begin to be some positive wellhead for oil during the first two years, the dividend payments must be no greater than $4\frac{2}{4}\%$ and even if the dividend were lowered to zero the State's income from royalty and severance tax of approximately \$53 million would be less than one third of that estimated as recently as last year.

I shall present at the close of the testimony this afternoon a series of cases for the committee to study that explore this question of taxation and dividend limitation. For the present, however, let us return to these two cases that we have displayed before you. Again, they provide a legal 7% ICC dividend. In the private case even though a negative wellhead value is indicated for the first two years it is quite possible that the oil companies would still pump oil

as their true cost of shipping their own oil through their own pipeline may be different than their calculated cost of shipping the State's oil through their own pipeline. Not only is the dividend permitted legal, but together with the costs and throughput capacity limitations as stated in the Impact Statement, this case of private ownership of the line appears quite possible. So are the revenues it generates. Speaking next to the very important question of what these revenues will mean to the State will be the Commissioner of Administration, Joseph Henri.

PLEASE NOTE: THE FOLLOWING PAGES WERE TREATED
AS A UNIT IN THE ORIGINAL DOCUMENT.

TESTIMONY OF JOSEPH R. HENRI
Commissioner of Administration, State of Alaska,
Before the Senate Commerce Committee
And the House State Affairs Committee
At Juneau, Alaska, 6 March 1972,
Regarding Income From North Slope Oil and Gas,
And How it Affects the State Budget

Mr. Chairman and Members:

I am Joseph Henri, Commissioner of Administration. This part of the State's presentation deals with budget expenditures vis-a-vis income to be derived from North Slope oil and gas extraction. The essential questions are:

1. Will we be able to maintain our current level of services, adjusted for population growth and inflation?
2. Will we be able to increase our level of service to meet compelling needs recognized by this administration, the legislature and the citizens of Alaska?
3. Will we have to reduce our level of service, and if so, what are the activities affected?

The answers to these questions rest in the amount of dollars the State can expect as its share of the Prudhoe Bay oil basin. Once upon a time, the Department of Administration felt much more certain about future State income than it does today. When will the

pipeline begin? What extraordinary man-caused interruptions will delay its completion? What will be the first year capacity of the line? The second year? The third? What is the maximum extraction rate the basin structure will prudently allow? What volumes of oil can be expected in any of the first seven years of the pipeline? What will be its final cost?

All of these variable factors, well known to each of us in this room, make budget planning extremely difficult, because the major part of Alaska's State revenue has come and will come from the North Slope resources. In the budget now pending before the legislature, we have recommended a total general fund expenditure of \$311.7 million; *those are State* of this sum, \$97 million will have to come directly from the Prudhoe Bay bonus money, the principal, and \$52 million more from interest earnings on the investment. As we dip heavily into the corpus - invade the principal - interest earnings diminish, compounding the revenue problem. Our present or anticipated recurring revenues are simply too low to fund our present and anticipated expenditures. We are depleting our savings account. As the following year's budget figure increases, more of the principal will have to be spent; the interest yield will dwindle further. Obviously, we will soon hit the bottom of the barrel. Only large and new revenues from the North Slope can allow us to continue our present budget growth rates.

What is the growth rate we have recommended for Fiscal Year 1973? For the general fund, it is 3.5%; for the total budget, 4.6%. We have had to slash so dramatically the rate of increase because pipeline delays and cost escalations have darkly influenced

our future revenue projections. With ~~such~~ a small increase in the budget, a number of programs have already felt the chill winds of dollar scarcity. The proposed Fiscal Year 1973 budget contains such unpalatable ^{things} ~~things~~ as holding school foundation funding to the current year's level, regardless of enlarged student population; keeping the University's ^{Alaska} ~~increase~~ to \$800,000 in the face of a claimed need for an addition of over \$5 million just to maintain current activities; a limitation of nursing home care and general medical relief; foregoing general obligation bonds for lengthening two more ferry boats, and for a larger program of airport construction. There are many more "pinches" in the budget, besides ^{as I mention}. Nonetheless, so far we have not jeopardized any State activity essential to health and safety. These painful adjustments herein noted were recommended in spite of the fact oil was projected on stream in July 1976; now another year's delay - or more - seems probable. The consequences are obvious.

Our budget book for Fiscal Year 1973 projects a growth rate of 6% compounded annually through 1976, and 8% thereafter through Fiscal Year 1981, covering a ten-year period. Further, it envisions capital improvement bond authorizations of \$60 million in 1974, and \$100 million in the next biennial election, and each one thereafter. I can only characterize these projected budgets as "modest." They are very little more than maintenance figures. Program dollars will still be limited. Careful budgeting and allocation will still be required. New starts and new programs will be exceedingly selective. The 6 and 8% growth rates most likely mean a shortage of funding for the school foundation plan, and for the revenue sharing program with local governments. Yet, I express ~~confidence~~ ^{hope} that the revenue receipts in the State treasury during the next ten years may be pitifully shy of the sums needed even to maintain our austerity.

Previously, in the testimony Commissioner Wohlforth and the Department of Revenue, test cases have been articulated regarding revenue to be derived under (A) private ownership and (B) State ownership of the crude oil pipeline. All of us realize that a multitude of variations in revenues and expenditures are possible under each heading. Nevertheless, for purposes of comparison we have presented two likely cases and their dollar results: Both examples entail the seven-year oil volume build up delineated in the Department of the Interior Environmental Impact Statement submission by Alyeska, a 7% dividend to the owner, a line cost of \$3.5 billion, and oil on stream in July 1977.

Exhibits A and B, attached at the conclusion of these remarks, portray the figures - and the story - for the decade 1972-1982. Under the private ownership case, Exhibit A, were Alaska to continue to increase its budget expenditures at the 6 and 8% rates, mentioned earlier, the first year of deficit would be Fiscal Year 1978, wherein we would experience a shortfall of over \$156 million. This shortage would increase so that by Fiscal Year 1982 the deficit would be \$1,135,000,000. Of course, deficits for operating expenditures are in fact impossible under our State constitution; instead of experiencing a billion dollar deficit ten years from now, we would in actuality have to reduce State expenditures radically.

Under the private ownership case the State could have in its treasury at the end of Fiscal Year 1982 the sum of \$45 million if, and only if, its operating expenditures in every year of the planning decade rose annually by only 1% (see Exhibit C). Now an increase of 1% equals a huge cut in all programs, and the elimination of many. A

The dollar crunch is graphically portrayed in the following paradigm. Under the private ownership operating budget column, increasing annually at 1%, the available dollars are recorded. Contrast these with the operating budget under public ownership, the first column on the left. The figure shows that if the State of Alaska owned the pipeline there would be sufficient dollars in each of the next ten years to meet our planned 6 and 8% annual increases. In fact, the revenue would be sufficient to raise the budget from these maintenance or austerity levels so that expansion of present services and the addition of new ones could be handily realized. Were the oil line privately owned the State would have almost billion less dollars to spend over the next ten years. We would be able to authorize 365 million fewer dollars for capital improvements.

(Graph on following page)

COMPARISON OF FUNDS AVAILABLE

PRIVATE VS PUBLIC OWNERSHIP

(ALL FIGURES IN 1000)

FISCAL YEAR	PUBLIC OWNERSHIP		PRIVATE OWNERSHIP	
	OPERATING BUDGET *	DEBT AUTHORIZED	OPERATING BUDGET *	DEBT AUTHORIZED
1972	260186.5	71000.0	260186.5	71000.0
1973	276232.7		276232.7	
1974	292910.7	60000.0	278994.8	15000.0
1975	310485.1		281784.3	
1976	329114.1	100000.0	284601.8	20000.0
1977	355443.1		287447.4	
1978	383878.5	100000.0	290321.5	20000.0
1979	414588.8		293224.3	
1980	447755.8	100000.0	296156.1	20000.0
1981	483576.2		299117.3	
1982	522262.2	100000.0	302108.1	20000.0
TOTAL	<u>4075433.7</u>	<u>531000.0</u>	<u>3150174.8</u>	<u>166000.0</u>

* All figures refer to expenditure from general fund only

Difference in Operating Expenditure is over \$925,000,000

Difference in Capital Debt Authorization = \$365,000,000

The attached graphs, Exhibits D and E, portray what I have been saying. In Exhibit D, under private ownership of the oil pipeline, the general fund would be depleted around January of 1978. On the contrary, under State ownership of the line, the precipitate drive to insolvency would stop in 1976 at a general fund balance of \$231 million, and rise to a plateau of \$450 million in the general fund by 1982. Furthermore, as Exhibit B shows, the total expenditure for that year would be approximately \$605 million, and the total revenue \$602 million; a parity between income and expenditure would have been achieved, and a surplus of almost half a billion dollars enjoyed. In actuality, no doubt, were the funds from State ownership available, the administration and the legislature would have expanded the budget faster than the 8% increase portrayed for the years 1977 and beyond so that no such surplus would likely exist at the end of Fiscal 1982.

The private ownership case I have presented to the Committees, Mr. Chairman, necessitates an abrupt and drastic reduction in State services and activities. I cannot tell you with certainty where the administration or the legislature would cut, but I can cite a few startling and likely areas of impingement in each of our program categories:

The State pays approximately 90% of local school district costs, constituting roughly 30% of annual State dollar expenditure. That State aid would be materially reduced; it would be impossible for the local areas to maintain present educational standards through increased property taxes. State Operated Schools and the University

of Alaska would have to radically abate their present service levels.

The welfare or social services activities of the State would experience vast curtailment in the number of eligible cases and the amount of benefits; many people would be compelled to leave Alaska; distress or ^{even} starvation would haunt many who decided to stay. Public health and mental health retrenchments could force the closing of the Alaska Psychiatric Institute, and a diminution or abolishment of the State's work in drug abuse, alcoholism, tuberculosis testing and venereal disease control. The necessitated nullifications of State expenditure in these areas will in turn lose large amounts of federal dollars now enjoyed. Our ability to operate and maintain an effective Pioneers' Homes program will be materially impaired.

No new fish hatcheries would be built. No hunter safety program would be initiated. Salmon yields in Southeast Alaska would remain significantly below maximum sustained yield. Land use planning and the inventorying of our natural wealth would be jeopardized, thus making management of the State's surface and subsurface resources haphazard at best. Added park and recreation sites would be forgotten, and the maintenance of existing facilities lessened. Many Alaska communities would remain without sewage treatment facilities. Programs for coastal zone management, environmental engineering, permafrost and soils engineering would likely be abolished.

In the category of Public Protection, disaster planning, the Public Utilities Commission, the Alaska Transportation Commission,

other programs would be initiated or

The State police would experience a great shrinkage in manpower, and the courts and their ancillary agencies could not cope with their workloads.

Tourist promotion would have to be seriously curtailed and our work in research, in community improvement and grant assistance, and at conventions and trade shows would most likely fall by the board. The work of the agricultural loan fund and the small grain incentive program would be enfeebled or eliminated. The Division of Planning and Research and the State Economic Opportunity Office would be crippled or possibly dropped.

Our program of revenue sharing with the local governments, around \$7 million in the current year, would no doubt go out the window. The Marine Transportation System for Southwest Alaska would likely be eliminated, and service in Southeast materially contracted. Airport maintenance in rural Alaska would be severely curtailed, likely forcing the winter closure of those ports, thus isolating a large part of Alaska for five months of the year, denying medical and other critical services. Likewise, winter maintenance of many of our highways would be only a pale reflection of the excellent job being performed today.

The various boards and commissions whereby Alaskan citizens take a direct and active part in the work of the State government would be minimally funded, or in some cases, unfunded. I am speaking of activities like the Western Interstate Conference on Higher Education, the Athletic Commission, the Status of Women Commission, the International Development Commission, the Pioneers'

Advisory Board, the Yukon Taiya Commission, the Rural Affairs Commission, the International North Pacific Fisheries Commission. Our Youth in Government program, recently instituted with such great success, would likely be abandoned.

I do not represent to you, as the view of this administration, that each of these reductions suggested above would come to pass under the private ownership case portrayed in Exhibits A and C. Nevertheless, no one can say that many of the above dire consequences would not eventuate under that case; undoubtedly some would. The economic and social dislocation would be grievous indeed.

The purport of my remarks is that this State has a vital interest in an adequate share of North Slope riches. If we do not realize that share, State expenditures over the next decade will be woefully inadequate to do the job Alaskans expect from their government. The solution we propose to sufficiently fund the budget is the ownership of the crude oil pipeline by the State of Alaska.

Exhibit A

STATE OF ALASKA DIVISION OF BUDGET AND MANAGEMENT

BUDGET PLANNING MODEL

RUN ID RUN 3

DATE MARCH 3, 1972

COMMENTS

PRIVATE OWNERSHIP
7% TARIFF
BASE CASE
DIL IN 77

ASSUMPTIONS

ANNUAL RATE OF INTEREST ON GENERAL FUND = 6.00%

ANNUAL RATE OF INTEREST ON NEW BONDS = 6.00%

MATURITY PERIOD ON NEW BONDS IN YEARS = 20.

% ABOVE G.F. UNENCUMBERED BAL. UNEXPENDED = 0.0%

GROWTH RATES FOR OPERATING EXPENDITURE FROM PRIOR YEAR

1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
6.00	6.00	6.00	6.00	8.00	8.00	8.00	8.00	8.00	8.00

NEW BOND AUTHORIZATIONS IN EACH YEAR

1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
71000.0	0.0	60000.0	0.0	100000.0	0.0	100000.0	0.0	100000.0	0.0

FISCAL YEAR	NON INVESTMENT REVENUE	INVESTMENT INTEREST	TOTAL REVENUE	OPERATING EXPENDITURE	DEBT SERVICE	MISC EXP SHD TAXES GE CAP EX	TOTAL EXPENDITURE	SURPLUS OR DEFICIT	GENERAL FUND END OF YEAR
1972									761268.2
1973	162264.1	42466.7	204730.7	276331.0	24020.8	11358.6	311710.3	-106979.6	654288.4
1974	162367.0	35772.1	218139.0	292910.7	29646.2	11756.5	334313.4	-116174.4	538114.0
1975	190047.0	28146.4	218193.4	310485.1	32973.5	12749.8	356208.4	-138015.0	400099.0
1976	136752.0	18960.8	207712.8	329114.1	33479.2	13200.6	375833.8	-168171.1	231927.7
1977	220569.0	8673.9	229242.8	355443.1	35373.3	13153.0	403969.4	-174726.6	57201.4
1978	225954.9	-2988.6	222966.3	383878.5	39390.5	13719.0	436988.0	-214021.8	-156820.4
1979	314776.0	-14823.9	299952.1	414588.8	42494.9	23358.3	480441.8	-180489.8	-337310.1
1980	329299.9	-26743.6	302556.3	447755.8	46529.0	25105.1	519389.9	-216832.6	-554143.8
1981	332012.4	-41200.4	290811.9	483576.2	47129.4	25167.5	555873.0	-265061.1	-819204.8
1982	344154.7	-58641.5	285513.1	522262.2	52863.3	26698.5	601824.0	-216310.9	-1135515.0
	2490194.0	-10378.5	2479816.0	3816342.0	383899.9	176356.8	4376599.0	-1896782.0	

AGO 530854

Exhibit B

STATE OF ALASKA DIVISION OF BUDGET AND MANAGEMENT

BUDGET PLANNING MODEL

RUN ID RUN 4
DATE MARCH 3, 1972
COMMENTS
PUBLIC OWNERSHIP
7% TARIFF
BASE CASE
OIL IN 77

ASSUMPTIONS

ANNUAL RATE OF INTEREST ON GENERAL FUND = 6.00%
ANNUAL RATE OF INTEREST ON NEW BONDS = 6.00%
MATURITY PERIOD ON NEW BONDS IN YEARS = 20.
% ABOVE G.F. UNENCUMBERED BAL. UNEXPENDED = 0.0 %

GROWTH RATES FOR OPERATING EXPENDITURE FROM PRIOR YEAR

1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
6.20	6.00	6.00	6.00	8.00	8.00	8.00	8.00	8.00	8.00

NEW BOND AUTHORIZATIONS IN EACH YEAR

1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
710000.0	0.0	60000.0	0.0	100000.0	0.0	100000.0	0.0	100000.0	0.0

FISCAL YEAR	NON INVESTMENT REVENUE	INVESTMENT INTEREST	TOTAL REVENUE	OPERATING EXPENDITURE	DEBT SERVICE	MISC EXP SHD TAXES GF CAP EX	TOTAL EXPENDITURE	SURPLUS OR DEFICIT	GENERAL FUND END OF YEAR
1972									761268.2
1973	162264.1	42466.7	204730.7	276331.0	24020.8	11358.6	311710.3	-106979.6	654288.4
1974	182367.0	39772.1	218139.0	292910.7	29646.2	11756.5	334313.4	-116174.4	538114.0
1975	190047.0	29146.4	218193.4	310485.1	32973.5	12749.8	356208.4	-138015.0	400099.0
1976	188792.0	18960.8	207752.8	329114.1	33479.2	13270.6	375883.8	-168171.1	231927.9
1977	430209.0	15116.4	445325.4	355443.1	35373.3	14482.8	405299.1	40026.3	271954.3
1978	434394.9	16695.3	451090.2	388878.5	39390.5	15217.0	438486.0	12604.2	284558.4
1979	547046.0	19533.7	566579.7	414588.8	42494.9	27485.9	484570.4	82009.3	366567.7
1980	550369.9	23532.2	573902.1	447755.8	46529.0	28343.7	522628.5	51273.6	417841.3
1981	567962.4	26121.0	594083.3	483576.2	47129.4	28359.7	559065.2	35018.1	452859.4
1982	575119.7	27093.4	602210.1	522262.2	52863.3	29787.4	604912.9	-2702.8	450156.6
	3428529.0	253434.8	4681963.0	3816342.0	383899.9	192832.9	4393075.0	-311111.4	

Exhibit C

STATE OF ALASKA DIVISION OF BUDGET AND MANAGEMENT

BUDGET PLANNING MODEL

RUN ID RUN 3

DATE MARCH 3, 1972

COMMENTS

PRIVATE OWNERSHIP
7% TARIFF
1% GROWTH
GREATLY REDUCED CAPITAL EXPENDITURES

ASSUMPTIONS

ANNUAL RATE OF INTEREST ON GENERAL FUND = 6.00%
ANNUAL RATE OF INTEREST ON NEW BONDS = 6.00%
MATURITY PERIOD ON NEW BONDS IN YEARS = 20.
% ABOVE G.F. UNENCUMBERED BAL. UNEXPENDED = 0.0 %
ANN OPER EXPEND GROWTH RATE AFTER 1ST YR = 1.00%

NEW BOND AUTHORIZATIONS IN EACH YEAR

1972	1974	1975	1976	1977	1978	1979	1980	1981	1982
71000.0	0.0	15000.0	0.0	20000.0	0.0	20000.0	0.0	20000.0	0.0

FISCAL YEAR	NON INVESTMENT REVENUE	INVESTMENT INTEREST	TOTAL REVENUE	OPERATING EXPENDITURE	DEBT SERVICE	MISC EXP SHD TAXES GF CAP EX	TOTAL EXPENDITURE	SURPLUS OR DEFICIT	GENERAL FUND END OF YEAR
1972									761268.2
1973	162269.1	42459.7	204733.8	276232.7	24020.8	11358.6	311612.0	-106878.3	654389.8
1974	182367.0	36208.7	218575.7	278994.8	29646.2	11756.5	320397.5	-101821.8	552567.9
1975	170047.0	29928.1	219975.1	281784.3	32973.5	12749.8	327507.6	-107532.5	445035.4
1976	188752.0	23147.4	211899.3	284601.8	32478.4	13290.6	330390.6	-118491.3	326544.1
1977	220569.0	16705.2	237274.2	287447.4	32921.2	13153.0	333521.5	-96247.3	230296.8
1978	225954.9	10787.1	236741.9	290321.5	33723.5	13719.0	337764.0	-101022.1	129274.8
1979	314776.0	6882.4	321658.3	293224.3	34212.3	23358.3	350794.8	-29136.4	100138.3
1980	329299.9	5394.7	334694.5	296156.1	33837.2	25105.1	355148.3	-20453.8	79684.5
1981	332012.4	4182.2	336194.5	299117.3	31872.0	25167.5	356156.8	-19962.3	59722.2
1982	344154.7	3140.6	347295.2	302108.1	33246.7	26698.5	362053.3	-14758.1	44964.1
	2490194.0	178845.6	2669040.0	2899986.0	319001.6	176356.8	3385343.0	-716303.9	

Exhibit D
ENDING GENERAL FUND BALANCE
Private vs Public Ownership
Budget Book Expenditure Plan

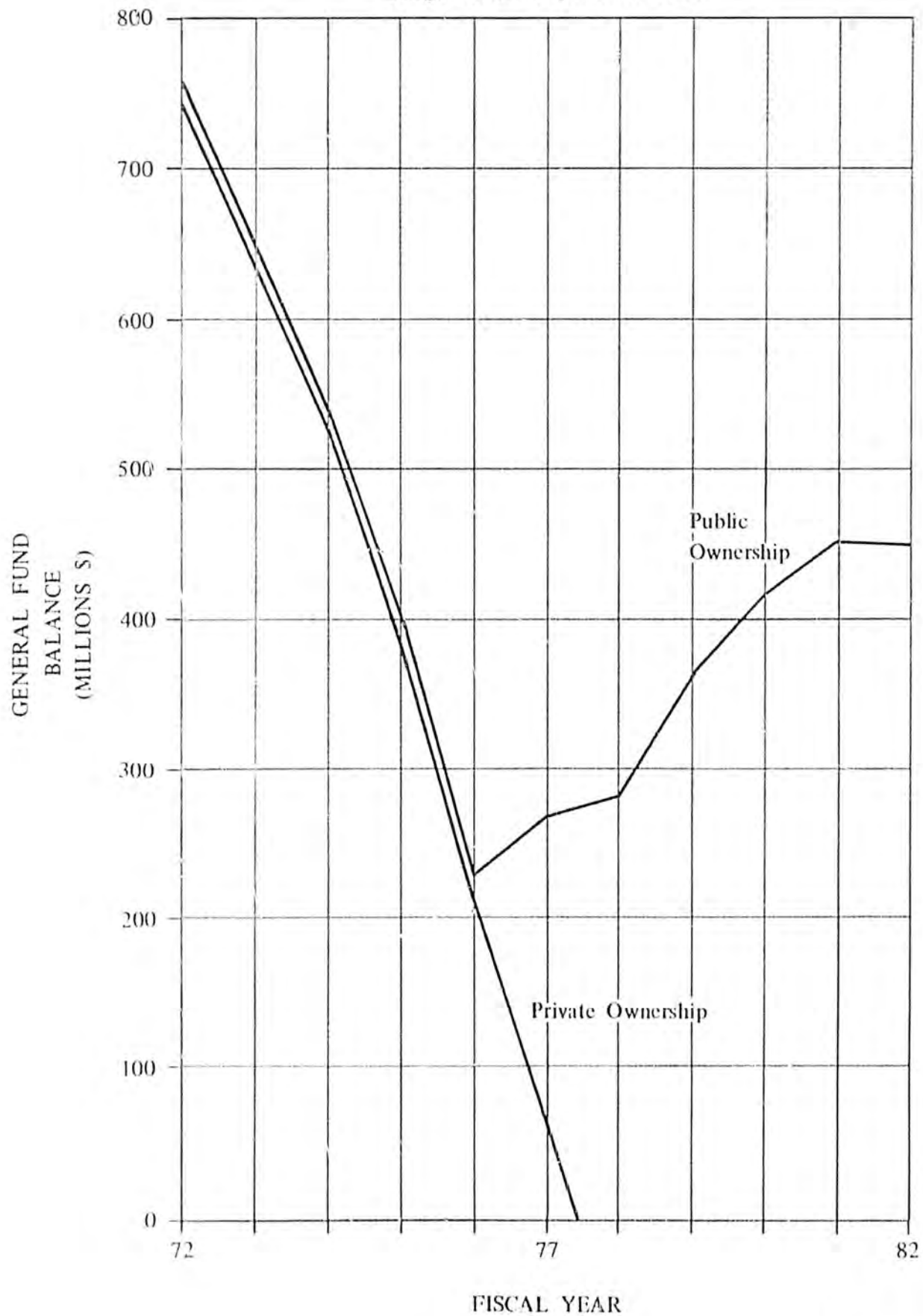


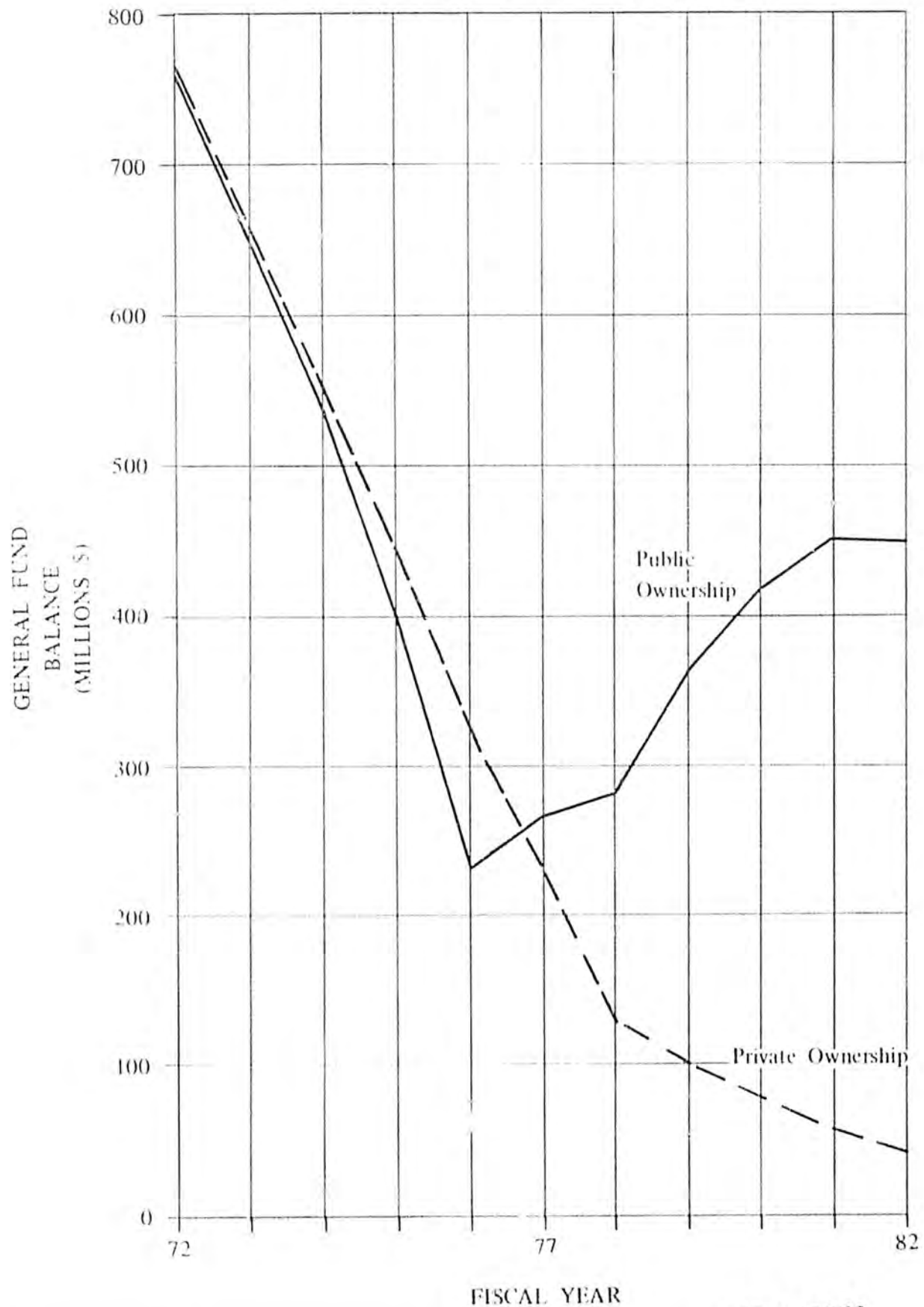
Exhibit E

ENDING GENERAL FUND BALANCE

Public Ownership Budget Book Expenditure Plan

vs

Private Ownership Subsistence Expenditure Plan



AGO 530858

PLEASE NOTE: THE FOLLOWING PAGES WERE TREATED
AS A UNIT IN THE ORIGINAL DOCUMENT.

Culetta: ⁸⁸ for State acquiring money, your testimony, or my interpretation, is that this money is the problem that we face and, if I interpret your testimony correctly, one of the alternatives was the State ownership proposal. With supplementary income from severance and royalties we were going to make up the deficit in monies that we need through the profit that is allowed on the pipeline. Have you looked into any other alternatives?

Henri: Well, Representative Culetta, when you mean alternatives do you mean other natural resource development or just what is the general thrust of this.

Culetta: Yes, either in that field or coupled to the Prudhoe Bay. Is consideration being given to, recently we read in the paper where gas research not taken out of the ground. Have we considered selling our pre-owned, you know approximately 20%?

Henri: Well, right, I think that should be the essence of it is Commissioner Herbert's. But, I would say in general that I have looked at every conceivable possibility for getting income for the State, more or less, I don't mean to tell you that we spent several hundred thousand dollars on each conceivable possibility. We certainly have tried to imagine any income source. There isn't anything, including gas, that is anywhere near like oil. That is the problem. I mean the oil is so far and above the great yield of revenue to the Treasury that there just isn't anything else remotely comparable to it.

Culetta: Mr. Chairman. Again, I was apparently misinformed but it seems that I recall from the news article that between two and five hundred million dollars in one gas sale had been negotiated.

Henri: Well, I don't doubt, Mr. Culetta, that if they sold all the oil in the Prudhoe Slope right today that they could get a figure quite a bit higher than that, obviously, but that is the total figure over many years. My concern, of course, is to funding the budget in 1978 and 1979, not that I am representing to you that I'm going to be the one who's doing it then, but at least we have

to fund the budget then and those are the years, particularly the late seventies, that are so critical to our State.

Culetta: Mr. Chairman. Commissioner, what I am driving at is until the line is on full capacity we seen to be facing the problem . It seems conceivable to me that we should sell some of the future production now to make up the deficit until the line is on stream so that we could solve our problem.

Havelock: If I may answer that for the Commissioner. I have discussed this with a number of people as a prospect, but the effect is, and it is a strategy the State may wish to use at the appropriate point, but the strategy does not change basic lines of the projection. What you can do through the advance sale, lets take sale of oil and gas futures, is to nip off the bottom of the deep part of the V when you hit bottom. You can't sell anything, or you can't sell for any kind of advantageous price until you have the assurance that the product is going to be marketed, otherwise, you are going to be selling a highly discounted comodity. Even if you do sell it, you are selling something that otherwise you would count on in the future. So, the effect is that you can round off the bottom of the V in the bottom of the dip but you don't change the basic trend of the decade by that kind of strategy. As far as other alternatives go, I do call to your attention one of the measures the Legislature may wish to consider, one of measures we had introduced does call for a twenty mill property tax on the pipeline and related oil property as a method of raising revenue and, of course, the legislature may wish to consider the utilization of the property tax as one of the various tax tools that is available to the State in meeting its fical problems.

Rettig: In several different ways the question has been posed, why can't we not increase severence taxes to make up for what, otherwise, would be pipeline profit. Perhaps Mr. Wohlforth could explain where most of this pipeline profit really comes from under State ownership. Would you care to do that Eric?

Wohlforth: Yes I would be glad to. The pipeline profit is shown under pipeline income

in the years 1977, 78, and 1979 to some extent, comes from pipeline income, that is to say, in the amount of the charge which the State is entitled to make as the owner of the pipeline.

Rettig: Perhaps I didn't make myself clear. For example,

Wohlforth: as well as the fact that we are not taxable as a pipeline owner.

Rettig: That is the point I was trying make. Out of perhaps four hundred million dollars of pipeline income, perhaps two hundred fifteen million of that ^{merely} is money that would otherwise go to Uncle Sam for taxes.

Rose: My curiosity is getting the best of me, what is a

?

Henri: It is an example of figures.

Groth: Joe this is the last question and I realize that I am probably being argumentative but I don't mean it. If you refuse to put anything in the budget on the value of the 1.5 million acres on the slope or the seventy seven million acres that the State otherwise has, would you sell it to me for a hundred million dollars? Of course you wouldn't, so you do have a figure on it someplace and it seems to me that that figure has to be put in your revenue projections someplace.

Henri: Senator, you're referring to lands that the State has?

Groth: Yes sir.

Henri: Of course, the lands, whether they are oil bearing lands is question number one. Again, I would have to ask whether Chuck Herbert thinks they are, but even Chuck has missed one or two acres in Alaska as to whether they have oil under them or not. So that in itself seems to be problematical, and then the question of when the oil companies would be interested in taking the oil is the thing that clenches us up. All we are talking about is a ten year period. I think that over the long run of time that we can get through the next ten years probably, our future is particularly bright in this State.

Adjournment until 2 p.m.

McVay: This is a continuation of the hearings on the pipeline proposals of the administration. Our schedule calls for us to go straight through until 6:00 this afternoon and we'll have breaks approximately every hour and fifteen minutes. Mr. Attorney General do you have the next witness?

Havelock: Mr. Co-Chairman and members of the committee, at this time the State would like to call Mr. Charles Kades of Barker, Stella, Field and Wood, special council of the State on public financing. He will discuss the statutory framework of State ownership. In connection with Mr. Kades testimony I have a distribution in line with the previous comments that I have made and other witnesses have made regarding a proposed introduction of the proposed amendment to the constitution of Alaska and with the Chairs permission I would like to distribute that now for your perusal and, in addition, we have to the amendment bill already committed to the committee we have two other proposed amendments to HB 569 which the committee may wish to consider.

McVay: Mr. Kades, when you are ready to begin would you give us a little bit of your background for the records.

Kades: Mr. Co-Chairman, my name is Charles L. Kades. I am a partner in the firm of Barker, Field, Stella and Wood of New York City. I have been a partner for some twenty some odd years. Prior to that I was overseas during WW II until about 1942. In an earlier period I had been Assistant General Council of the United States Treasury in Washington from 1933 or 1934 until 1940. After we were retained to advise the Attorney General and other members of the administration in connection with the ownership of the, or possible ownership of the pipeline by the State, we conferred at length and concluded that the device that was best adapted to providing the State ownership of the pipeline would be public authority. The authority device is not a new device. It is not untried and, at its best, under competent members, it has advantages of full private and public management. It must pay its way and usually it has no access to the public treasury. It has no stock; it is operated under Government and after its debt is paid it properly belongs to the State and to the people. Although there

has not been any project of which I am aware of comparable size to the pipeline under consideration here, there have been authority financings amounting to billions of dollars. For example, the Port of New York Authority now has outstanding about one and a half billion dollars worth of bonds and it has retired about an equivalent of that amount of bonds. The Los Angeles Power and Light Authority has outstanding about a billion dollars worth of bonds. The Power Authority of the State of New York has outstanding a billion and a half of bonds. The New York State Thruway has a billion in principle amount of bonds outstanding. The New Jersey Turnpike Authority has approximately three quarters of a billion; Illinois Turnpike Authority has over six hundred million; and the Nebraska Public Power Agency has a half a billion dollars in bonds outstanding. All of these projects have been financed without any recourse whatever to tax revenue. These projects have been self-liquidating, self-supporting, and are managed by the authority as an autonomous, independent, separate corporate legal entity. That is the purport of H.R. number 569 which creates the Trans-Alaska Authority as an independent corporate entity. Its membership is appointed by the Governor with the confirmation of both houses in joint session of the Legislature. It has all the general powers of a private corporation as well as a public corporation. It has specific powers to issue bonds or notes and to make agreements with the bond holders and note holders for the financing of the project and it can make rates and charges and revise them from time to time without the surveillance of any other regulatory agency sufficient to pay the interest and principal on the bonds as well as its debt service as well as the operating and maintenance expenses. It has the power to acquire the property of any other pipeline company, either by purchase of stocks or by purchase of property, or by physical property or, if necessary, by exercising the right of eminent domain upon payment, of course, of just compensation. The Act is not mandatory. The Act is purely permissive. All it does is set up the framework from which the State can then determine its next move. It is purely enabling legislation. It might never be used or it might be used in part or in whole, but it is indispensable ^{to have} some legal framework if the proposals that there may be State

ownership is to move forward. The hearings, I think, became confused at one point in regard to pledge of credit of the State. An independent public authority such as should be self-supporting. All of the authorities that I have mentioned are self-supporting. Sometimes it has been desirable, although I only know of one case, to guarantee the bonds, although no recourse has ever been had to that guarantee. That is in the case of the New York State Thruway, where some bonds were issued guaranteed by the State, after a constitutional amendment was adopted authorizing the guarantee, but the project has been completely self-liquidating and there had never been any of payment of any of the interest or principals out of the revenues. Did one of the amendments that the Attorney General introduced or offered to the committee at the opening of this session eliminates from this act the recital or from this bill, the recital in the legislative findings that it is clear to be in public interest for the State to guarantee the principal and interest on bonds issued to finance the facility. The other amendment eliminates the section which provided to the extent that the constitution permitted the bonds might be guaranteed. Now, that section was pure surplus and really doesn't belong in the bill because the constitutional amendment provides that, if it is adopted by the people, then the Legislature is authorized by an act to guarantee the bonds but, first of all, the constitutional amendment is required to pass the people and, secondly, another Legislature must act to pass a law before any of the bonds are guaranteed. So there (Its redundant) for anything of that character to be in this bill, thats why it has been eliminated. As it stands, the bill authorizes an authority to make plans and to proceed with the project but doesn't require the authority to do anything, and doesn't in any way pledge directly, or indirectly, the credit of the State or the taxing power of the State. I may say of this connection that the project, as defined in the Act, is much broader than the pipeline. There are many other things that are required to be built which would be revenue producing. For example, port facilities, airports, docks, wards, storage